National Grid Gas plc
DN Regulatory Accounting Statements 2006/2007

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About regulatory accounting statements

National Grid Gas plc is the holder of two gas transporter licences: one in respect of its gas transmission (NTS) business and one in respect of its gas distribution network (DN) businesses. Under Standard Special Condition A30 of each of these licences, National Grid Gas plc is required to prepare and publish annual regulatory accounting statements setting out the financial position and performance of each of the regulatory businesses covered by that licence.

These DN regulatory accounting statements are in respect of National Grid Gas's DN businesses, including its gas metering businesses. National Grid Gas also prepares and publishes regulatory accounting statements in respect of its NTS business, including its LNG storage business. Together, these two sets of regulatory accounting statements must comprise all the businesses and activities of National Grid Gas, except for the four gas distribution networks which National Grid Gas sold on 1 June 2005.

Reconciliations between certain financial information included in these DN regulatory accounting statements and the equivalent financial information for National Grid Gas as a whole, are provided in note 2 to these DN regulatory accounting statements.

Scope of DN regulatory accounting statements

These DN regulatory accounting statements are in respect of the following regulatory businesses of National Grid Gas plc:

- the Distribution Networks (DNs);
- the metering business;
- the meter reading business; and
- de-minimis and other activities associated with these businesses

These regulatory businesses are collectively the gas distribution and metering businesses.

Further information about these businesses can be found on page 7 of the Operating and financial review.

National Grid Gas's NTS business, LNG storage business and associated de-minimis and other activities are reported in the separate NTS regulatory accounting statements.

The regulatory businesses reported on in regulatory accounting statements are defined in accordance with the gas transporter licence under which the regulatory accounting statements are prepared and differ in some respects from the business definitions used in National Grid Gas's annual report and accounts.

Relationship of regulatory accounting statements with statutory accounts

The financial information contained in these regulatory accounting statements does not constitute statutory accounts within the meaning of Section 240 of the Companies Act 1985. Statutory accounts for National Grid Gas plc for the year ended 31 March 2007, to which the financial information relates, have been delivered to the Registrar of Companies.

The Auditors have made a report under Section 235 of the Companies Act 1985 on those statutory accounts which was unqualified and did not contain a statement under Section 237(2) or (3) of the Companies Act 1985. The auditors' opinion on the National Grid Gas plc statutory accounts is addressed to, and for the benefit of, the members of National Grid Gas plc and not for any other person or purpose. The auditors have clarified, in giving their opinion on those statutory accounts, that it 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. In giving their opinion, they do not accept or assume responsibility for any other purpose or to any other person to whom their audit report on the statutory accounts is shown or into whose hands it may come save where expressly agreed by their prior consent in writing.

The statutory accounts of National Grid Gas plc can be obtained from the Company Secretary's Office, National Grid plc, 1-3 The Strand, London WC2N 5EH.

Basis of preparation of regulatory accounting statements

These regulatory accounting statements contain arbitrary apportionments of certain revenues, costs, assets, liabilities and shareholders' equity which are not specifically attributable to the businesses and activities reported in these regulatory accounting statements, but which, nevertheless, are required by the gas transporter licence under which these regulatory accounting statements are prepared, to be reported against those businesses and activities. Further details of these items are provided in the Basis of preparation on page 38.

The bases used to allocate the revenues, costs, assets, liabilities and shareholders' equity of National Grid Gas to the businesses reported on in these regulatory accounting statements have been determined in accordance with the requirements of the gas transporter licence under which these regulatory accounting statements have been prepared. These bases may differ from those used to determine the segmental analysis provided in the annual report and accounts of National Grid Gas plc.

Operating and financial review

This Operating and Financial Review describes the main trends and factors underlying the development, performance and position of the businesses reported in these regulatory accounting statements during the year ended 31 March 2007 as well as those likely to affect their future development, performance and position. It has been prepared in line with the guidance provided in the Reporting Statement on the Operating and Financial Review issued by the UK Accounting Standards Board in January 2006, except that in accordance with the requirements of the gas transportation licence under which these regulatory accounting statements are prepared, performance during the year is only discussed for the businesses in aggregate.

Content of Operating and Financial Review

About National Grid Gas

Principal operations

National Grid Gas is a part of the National Grid group of businesses. Its principal operations are in regulated gas networks in the UK and comprise the transmission and distribution of gas and the provision of gas metering services.

History

National Grid Gas originated from the restructuring of the UK gas industry in 1986. In 2005, following the sales of four UK regional gas distribution networks, we adopted National Grid as a single name for all our principal businesses.

Key milestones

1986	British Gas incorporated as a public limited company
1997	British Gas demerged Centrica
1999	Financial and restructuring programme completed leading to creation of a new parent company, BG Group, separation of the regulated Transco business from the other businesses of BG Group and the establishment of a financial ring-fence around Transco
2000	Lattice Group, including Transco, demerged from BG Group
2002	Merger of Lattice Group and National Grid to form National Grid Transco
2005	Sales of four regional gas distribution networks
2005	National Grid adopted as the group brand name, with Transco renamed National Grid Gas

External market environment

The principal market in which National Grid Gas operates is the natural gas market in the UK.

The supply of natural gas in the UK is competitive in that consumers can contract with different suppliers to obtain the gas they need. Those suppliers are then responsible for sourcing that gas from gas extractors or importers as appropriate, as well as arranging for that gas to be delivered through physical delivery networks.

These networks, including the ones National Grid Gas operates, are monopolies in their local areas as, for the majority of consumers, there are no alternative methods of receiving natural gas.

Natural gas delivery

Natural gas is transported through the gas national transmission system to regional gas distribution networks that then deliver that gas to consumers on behalf of suppliers. Certain end customers, primarily large industrial users, receive gas direct from the national transmission system.

National Grid Gas is the owner and operator of the gas national transmission system and of four of the eight regional gas distribution networks in Great Britain.

The gas distribution networks in Scotland and southern England are owned by Scotia Gas Networks, in the north of England by Northern Gas Networks, and in Wales and the west of England by Wales & West Utilities.

Other markets in which National Grid Gas operates

National Grid Gas also operates in gas related markets in Great Britain which are directly connected to its regulated businesses described above.

National Grid Gas participates in the competitive market for the provision of LNG storage services in Great Britain.

Although there is now a competitive market for metering services in the UK, National Grid Gas does not participate in this competitive market, but is the owner of a legacy portfolio of gas meters comprising the majority of the gas meters in operation in Great Britain. As the competitive market for metering services expands, this portfolio will decline as National Grid Gas's meters are replaced.

Regulation

As a result of its position in, and importance to, the UK economy, National Grid Gas's gas transmission and distribution businesses are subject to UK and European Union laws and regulations.

National Grid Gas's businesses are regulated by the Office of Gas and Electricity Markets (Ofgem). Ofgem operates under the direction and governance of the Gas and Electricity Markets Authority and has established price control mechanisms that restrict the amount of revenue that can be earned by regulated businesses, typically covering five-year price control periods.

National Grid Gas has two price controls for its gas transmission operations, one in its role as transmission owner and the other as system operator. For gas distribution operations, it has four price controls, one for each of its four regional gas distribution networks.

These price controls are based around incentives. National Grid Gas has a financial incentive to invest, receiving a return on efficiently incurred capital expenditure through it increasing its regulatory asset base, and it can gain or lose through incentive arrangements for performance in managing system operation, internal costs and pass-through costs.

The last price control period for gas transmission operations ended on 31 March 2007. A new price control period commenced on 1 April 2007 and is planned to last until 31 March 2012. The current price control period for gas distribution operations has been extended until 31 March 2008. The next price control period is expected to last until 31 March 2013.
National Grid Gas's businesses are subject to safety legislation which is enforced by the Health and Safety Executive (HSE). Gas operations work under a permissioning regime, whereby National Grid Gas's organisation, processes and procedures are documented in safety cases that are subject to acceptance by the HSE.

National Grid Gas has securities which are listed on the London Stock Exchange and on the New York Stock Exchange. As a consequence, it is regulated by the Financial Services Authority in the UK and by the US Securities and Exchange Commission.

More information about the regulatory environment and on the nature of National Grid Gas's price controls, is provided in the section, About the businesses on pages 7 to 9.

Objectives and strategy

Strategic review

National Grid has undertaken a thorough and disciplined strategic review of its business which will set the direction of the businesses included in these regulatory accounting statements for the next 5 to 10 years. In conducting this review, National Grid considered market trends and opportunities that exist in the utility sector, National Grid Gas's market position, how value is derived from its businesses and the views of the capital markets. National Grid announced its conclusions in November 2006 and objectives have been updated accordingly.

Focus

National Grid's future is about becoming more focused – a clear business model based on the ownership and operation of large scale asset intensive businesses, focusing on its principle growth markets, including gas infrastructure in the UK.

Integration

National Grid Gas aims to run its businesses in a more integrated way – organising activities along lines of business, supported by effective and efficient shared services and information systems. This involves deploying proven processes, common systems and best practices within each business, supported by common operating principles, and safety and environmental standards. In this way, National Grid Gas will maximise the competitive advantages that come from being part of an international organisation. However, it is critical that this is balanced with the need to provide excellent service to customers and to maintain and build local relationships with other key stakeholders.

Discipline

National Grid Gas plans to be more disciplined in the application of best practice. Increasingly, it will standardise its approach, applying even greater rigour to financial discipline, ensuring that it has the capital to grow, but maintaining the investor confidence that comes from a disciplined approach to its balance sheet.

Objectives

National Grid Gas's primary objective is to grow its businesses in order to create value for National Grid's shareholders. It can only create value if it achieves operational excellence and continues to improve its financial performance, it invests for the future and is financially disciplined, and it develops, recruits and retains skilled, talented and motivated people. In each area, it aims to increase its focus, benefit from improved integration and be disciplined in its approach.

As consequence, National Grid Gas has identified specific objectives in the following areas which apply to all its businesses:

Performance	The aim is for operational excellence by operating to the highest standards of safety, reliability and efficiency. National Grid Gas aims to continue to improve its financial performance.
Investment	National Grid Gas will invest in its existing businesses to generate future growth. It will be financially disciplined in the way it invests and in the way it manages its balance sheet.
Talent	National Grid Gas aims to maximise the contribution made by its employees by motivating its people to strive for continued improvement, developing their skills and talents, and by promoting a culture that recognises and respects inclusion and diversity.

This strategy is underpinned by National Grid Gas's commitments to developing strong and valued relationships with its customers, regulators, suppliers and the communities in which it operates and to acting responsibly, including specific commitments to reducing its environmental impact and to corporate governance and business ethics.

Relationships	National Grid Gas aims to improve its relationships with customers, regulators, suppliers and the communities in which it operates by focusing on the areas that are important to them, such as the quality of service National Grid Gas provides to customers, the quality of information it provides to regulators, by investing in local communities and by the way it address the concerns of, and interact with, all its stakeholders.
Responsibility	National Grid Gas believes operating responsibly is essential to the way it conducts its operations, invests, develops its people and manages its relationships and so responsibility underpins everything it does. It is committed to taking positive action to reduce its contribution to climate change and its other impacts on the environment. National Grid Gas wants to operate to the highest standards of corporate governance and it believes in strong business ethics, based around its core values of respect, integrity and ownership.

Risk

National Grid Gas's principal risks relate to the achievement of its objectives and strategy, as it believes that by delivering on these objectives it will achieve its principal objective of delivering growth to drive shareholder value. The way in which it intends to achieve its objectives is set below and performance during the year against those objectives, by the businesses included in these regulatory accounting statements, is set out on pages 16 to 22.

In considering the opportunities there are to grow and develop the businesses included in these regulatory accounting statements, National Grid Gas has identified a number of risks and uncertainties in achieving its objectives. The most significant risk factors identified relate to:

- changes in laws or regulations;
- breaches in environmental or health and safety law or regulations;
- network failure or inability to carry out critical non-network operations;
- achievement of business performance objectives, including regulatory targets and delivering anticipated cost and efficiency savings;
- regulatory treatment of commodity costs passed through to consumers;
- reputation damage from disruptions to supply, even if outside National Grid Gas's control;
- fluctuations in exchange rates and interest rates and their impact on borrowings and derivatives;
- increases in interest rates;
- restrictions in borrowings and changes in credit ratings or in tax rates;
- future funding requirements of pension schemes; and
- changes in accounting standards.

These are described in more detail on pages 11 to 13.

Shareholder value

By achieving its objectives around performance, growth, talent, relationships and responsibility National Grid Gas aims to deliver sustainable growth to create value for National Grid's shareholders.

Following are some of the specific objectives National Grid Gas has set itself in these areas in order to support its overall goals and which are relevant to the businesses included in these regulatory accounting statements. The objectives are set in the context of its strategy of increasing its focus, seeking to benefit from improved integration and being disciplined in its approach.

Performance

National Grid Gas's aim is for operational excellence, performing to the highest standards of safety, reliability and efficiency and continuing to improve its financial performance:

Safety	Safety is paramount. National Grid Gas's most important goals are: to ensure that members of the public are not injured as a direct result of its operations; to deliver a working environment where there are zero work-related injuries or illnesses; to reduce gas leaks on its distribution networks; and to improve the health of its employees so they are fit for work every day. Measures used to monitor performance against the safety objectives include: members of the public injured as a direct result of operations; employee lost time

	injury frequency rate; standards of service for responding to gas escapes; kilometres of gas distribution mains replaced; and employee sickness absence rate.
Reliability	National Grid Gas's principal operations are critical to the functioning of the UK economy. The reliability of gas infrastructure networks and the delivery of gas to customers, are, therefore, the next highest priorities after safety. National Grid Gas's approach to maintaining and improving reliability involves: investing in infrastructure and systems to provide the operational tools and techniques necessary to manage its assets and operations to high standards and investing in the renewal of assets; investing in the skills and capabilities of its people to give them the ability to operate its networks to a high degree of service excellence; and maintaining a constant focus on reliability as one of its principal objectives, ensuring it is proactive about planning to ensure reliability and that it reacts quickly to factors that could compromise reliability. National Grid Gas uses business-specific reliability performance indicators to measure its reliability performance.
Efficiency	By improving efficiency, National Grid Gas can constrain the cost of its operations borne by customers and improve returns to shareholders. It reviews its operations continually to identify opportunities to improve the operational productivity of assets and people, and to identify areas in which it can reduce costs or restrict cost increases. Planning ahead is essential in National Grid Gas's approach to maintaining and improving efficiency. The primary method of measuring improvements in efficiency is through financial performance as described below.
Financial performance	If National Grid Gas achieves its objectives, it should be able to deliver continued improvements in financial performance. This will contribute to National Grid delivering on its commitment to growing its dividend by 7% per annum until 31 March 2008. The principal measures used to monitor financial performance are adjusted operating profit* and operating cash flows.

* Adjusted operating profit is operating profit before exceptional items and remeasurements.

Growth

Investment and financial discipline are critical to National Grid Gas's plans to grow the businesses included in these regulatory accounting statements.

Investment	National Grid Gas invests in its existing businesses in order to grow those businesses. Measures used to monitor investment include capital expenditure.
Generate value from investment	National Grid Gas aims to generate value from investment by improving the operating performance of the gas distribution and metering businesses and by selecting investments that will provide the best return. Measures used to monitor the value generated from investments include return on investment.
Financial discipline	In order to deliver sustainable growth National Grid Gas must be disciplined in the way it manages its balance sheet. This means that cash will be returned to National Grid's shareholders to the extent that it is not required for the investment objective.

Talent

National Grid Gas depends on the talents, skills and motivation of its employees. It aims to maximise the contribution made by its employees by developing their skills and talents, by motivating and driving continued improvement and by promoting a culture that recognises and respects inclusion and diversity and where all employees share National Grid Gas's core values of respect, integrity and ownership. In addition to obtaining the views of employees on an ongoing basis, employee surveys are periodically carried out to identify areas where the way National Grid Gas develops and interacts with them can be improved.

Motivation and performance	National Grid Gas plans to improve its operational performance and the service it provides to customers by motivating employees to strive for continued improvement. The aim is for a world-class performance management system, involving integrated common performance processes, a single set of performance criteria, pay linked to leadership qualities as well as operational and financial performance and greater differentiation between levels of performance.
Development of talent and skills	Critical to National Grid Gas's success is identifying, recruiting and developing talented people and helping management and employees to operate to the best of their abilities.
Inclusion and diversity	In order to develop, recruit and retain talented people, National Grid Gas aims to achieve a more inclusive and diverse culture. A number of priority action areas have been identified to help achieve the vision of developing and operating the business in a way that results in a more inclusive and diverse culture, reflecting the composition of the communities in which National Grid Gas operates, and to

be seen as an employer of choice across diverse communities.

Performance measures used to monitor this objective of promoting inclusion and diversity include the percentage of female employees and the percentage of black and minority ethnic employees.

Values

National Grid Gas's aim is for all its people to be proud to work for National Grid Gas, to share its core values of respect, integrity and ownership.

Relationships

National Grid Gas has a diverse range of external stakeholders including employees, customers, regulators, government and local communities. It strives to be open and constructive in its dealings with external audiences.

Relationships with stakeholders are critical to National Grid Gas's future success. National Grid Gas's strategy involves improving these relationships by focusing on the areas that are important to them, such as the quality of service provided to customers, the quality of information provided to regulators and the way it addresses the concerns of, and interacts with, all its stakeholders.

Customer service

National Grid Gas's objective is to impress its customers with the quality of the services provided, with its responsiveness when things go wrong and with its dedication to continued improvement.

National Grid Gas plans to improve the way it interact with customers by enhancing or replacing the systems used, through providing employees with the training, empowerment and support they need to deliver and by improving the quality of communications with customers and internally.

Business-specific service quality performance indicators are used to measure performance in this area.

Regulatory relationships

National Grid Gas's regulators' primary responsibilities are to gas consumers. Hence, the foundation of the relationship with regulators is based on the safety, reliability and efficiency of National Grid Gas's operations and the quality of its customer service. The strategic focus on operational excellence and on customer relationships plays a critical part in improving relationships with regulators.

The other critical element in regulatory relationships is in building trust. This involves being responsive to the need of regulators for high quality information, complying with rules and regulations, operating in an ethical way and, most importantly, delivering on promises.

Suppliers

National Grid Gas aims to work in partnership with its suppliers, developing constructive relationships and working together effectively. National Grid Gas's objective is to develop contractual arrangements with suppliers that align their interests with its own, as far as possible, and share financial risks appropriately.

Community involvement

National Grid Gas's role as a good corporate citizen supports its strategic ambitions, and is delivered through a sustained and consistent approach.

In all community investment, National Grid Gas aims to develop its business, support its employees, support communities and enhance its reputation. Its approach is based on two principles: 'Investment in our Communities, Investment in our People', and continues to be centred on three key themes: energy and environment; education and skills; and community development.

Sharing of best practice across the business and working collaboratively with key partners and stakeholders enables National Grid Gas to maximise how communities benefit from its activities.

Responsibility

National Grid Gas is committed to operating in a responsible way and this underpins its commitments to performance, growth, talent and relationships as discussed above.

As an asset intensive business, National Grid Gas's operations have an impact on the environment. The most significant of these for the gas distribution and metering businesses are climate change and historically contaminated land. National Grid Gas also takes actions to minimise other environmental impacts of its operations, it is committed to strong governance and ethical standards and it is committed to protecting human rights.

Climate change

Climate change is possibly one of the greatest challenges facing society in the 21st Century. National Grid's public position statement on energy delivery and climate change sets out its approach to delivering energy while playing its role in minimising any impact its operations may have on the climate.

National Grid's target is to reduce its carbon emissions by 60% compared with a verified baseline, ahead of the Government's target of 2050.

The biggest greenhouse gas emission for the businesses covered in these regulatory accounting statements is methane leakage from the gas distribution networks. A major ongoing programme of replacing old cast iron pipes with modern polyethylene pipe is reducing leakage from the distribution system year on year.

National Grid Gas plans to reduce emissions relating to its own energy use, saving at least 5% in energy consumption, and use the resultant cost savings to enable it to procure all of the electricity it uses from renewable sources by the end of 2010.

	The key performance indicator used to monitor National Grid Gas's performance in this area is the percentage reduction in greenhouse gas emissions.
Historically contaminated land	National Grid Gas has an inherited portfolio of historically contaminated land including former manufactured gas plants and former gas holder stations. Sites can have a complex mix of contamination dating back over 100 years. The main focus of its remediation programme is on managing the environmental risk and returning land to beneficial use. Its goal is to return these sites to productive public or private use.
Protecting the environment	National Grid Gas is committed to continuous improvement in its environmental performance. Its objective is to help protect the environment for future generations. In addition to aiming to actively reduce its contribution to climate change, National Grid Gas is committed to: ▪ being efficient in its use of natural resources; ▪ keeping waste to a minimum and increasing the economic value of any waste produced; ▪ acting to prevent environmental incidents; and ▪ improving, where it can, the environmental status of the land on which it operates. National Grid Gas has implemented environmental management systems certified to the international standard ISO 14001 in all its businesses to help it deliver improvements in these areas. Key performance indicators that are monitored in this area comprise the number of significant direct environmental incidents and the total value of fines from prosecutions.
Corporate governance	National Grid Gas believes strong corporate governance is essential to operating responsibly and achieving its goals. The approach to corporate governance is set out on pages 30 and 31.
Business ethics	Not only is National Grid Gas committed to ensuring that all its behaviours are lawful and that it complies with its policies and licences, it also expects all of its employees to live up to the core values of respect, integrity and ownership.
Human rights	National Grid's public position statement sets out the commitment to protect human rights within National Grid Gas's sphere of influence and ensure its own operations are a force for good, wherever it operates.

About the businesses

Businesses

These DN regulatory accounting statements include the following regulatory businesses and activities of National Grid Gas:

Regulatory business	Description of regulatory business
Distribution network (DN) businesses	Provide gas distribution services in four geographic regions: the North West of England; the West Midlands; the East of England; and North London
Metering business	Provides regulated gas metering services throughout Great Britain.
Meter reading business	Provides meter reading services for third parties and for National Grid Gas's DN and NTS businesses.
De-minimis activities	Other business activities carried out in association with the DN and metering businesses which are not subject to direct regulation by Ofgem.
Other activities	Other activities carried out in association with the DN and metering businesses with the specific consent of Ofgem.

All of these businesses and activities are undertaken within Great Britain.

Business drivers

The operation of highly complex gas networks means there are many factors that influence the financial returns National Grid Gas obtains. The Directors consider the following to be the main business drivers relevant to the businesses reported in these regulatory accounting statements:

Price controls	The prices National Grid Gas charges for use of its gas distribution networks are determined in accordance with regulator-approved price controls. The negotiation of these arrangements has a significant impact on the revenues obtained from operations. In addition, these arrangements include incentives that permit National Grid Gas to earn additional revenues based on its performance or penalise it if it does not meet agreed performance targets. The period of these arrangements is significant to National Grid Gas in that they provide stability to its operations and allow it to plan ahead and invest in the confidence that it will obtain financial returns. These price controls typically cover periods of five years.
Multi-year contractual arrangements	Revenues from metering services are determined by contractual arrangements, which are usually long-term and with 'blue chip' customers.
Safety and reliability	National Grid Gas's ability to operate safely and reliably is very important to it, its employees, contractors, customers, the public and its regulators. Its financial performance is affected by its performance in these areas.

Efficiency	National Grid Gas's objective, and that of its regulator, Ofgem, is for it to deliver services as efficiently as possible. This allows National Grid Gas to limit price increases or to reduce prices to its customers and improve its own financial performance to the benefit of National Grid's shareholders.
Capital investment	Capital investment is a significant driver for organic growth. In National Grid Gas's regulated gas networks, the prices it charges include an allowed return for capital investment determined in accordance with its price controls. This provides incentives for it to enhance the quality and reach of its networks through capital improvements.
Relationships and responsibility	National Grid Gas's reputation is vitally important to it. Delivering sustainable value depends on the trust and confidence of its stakeholders and this can only be earned by conducting its business in a responsible manner.

A number of other factors also affect National Grid Gas's financial performance, but are less significant than the principal business drivers above, or are mitigated by the way its operations are structured:

Weather and volumes	Changes in the quantities of gas delivered through National Grid Gas's distribution networks may result in an increase or decrease in its revenues. Volumes are affected by weather and consumer demand as well as other factors. The impact of changing volumes may sometimes be offset by changes in costs or may sometimes result in an under- or over-recovery against allowable revenues, with a corresponding increase or decrease in revenue in future periods.
Pass-through costs	National Grid Gas is allowed to recover certain costs through charges to customers. The timing of recovery of these costs can vary between financial periods leading to an under or over-recovery within any particular financial period.
Commodity costs	National Grid Gas is affected by movements in commodity prices to the extent that they affect its own energy requirements, the most significant of which relates to gas purchases required for the operation of the gas distribution networks.
Inflation	Without action to improve efficiency, operating costs increase each year as a result of wage increases and inflation in external costs. In general, revenues also increase each year, although not necessarily at the same rate, depending on regulatory or contractual arrangements. As a consequence, National Grid Gas's ability to control costs and improve efficiency is important to its ability to increase operating profits. National Grid Gas's price controls are linked to retail price inflation, as are a proportion of its borrowings.
Seasonality	Revenues from the gas distribution networks are weighted towards the end of the financial year, as gas demand is typically higher during the winter months. Seasonality does not have a significant impact on other revenues. With the exception of commodity costs, operating costs are generally not seasonal.
Interest rates	The costs of financing operations are affected by changes in prevailing interest rates, as some of National Grid Gas's debt is at floating rates. Some of the exposure to interest rates is hedged with fixed-rate debt and derivative financial instruments to maintain a proportion of debt at fixed interest rates.

Distribution Networks

National Grid Gas owns four of the eight regional gas distribution networks (DNs) in the UK, comprising almost half of Great Britain's gas distribution system. National Grid Gas's DNs consist of approximately 82,000 miles of distribution pipelines and transport gas on behalf of approximately 34 active gas shippers, from the gas national transmission system to around 11 million consumers.

National Grid Gas also manages the national emergency number (0800 111 999) for all of the gas distribution networks and for other gas transporters in the UK. During 2006/07 it handled approximately 2.3 million calls to the national emergency number.

Detailed arrangements for transporting gas are provided through the Uniform Network Code as approved by Ofgem, which defines the obligations, responsibilities and roles of the industry participants. National Grid Gas holds a single DN transporter licence, which authorises it to operate its four DNs. However, each DN has its own separate price control, which establishes the prices which can be charged for the services provided by that network.

The price controls that applied to the DNs up until 31 March 2007, took into account Ofgem's estimates of operating expenditure, capital expenditure, replacement expenditure and allowed rate of return (which is currently set at a real pre-tax rate of 6.25% on regulatory asset value).

Ofgem has extended the current five-year gas distribution price control for a further year, through an extension price control to cover the year ending 31 March 2008. The next full price control period will now cover the period from 1 April 2008 to 31 March 2013. As at 31 March 2007, the aggregate regulatory asset value for the DNs is estimated at approximately £6.0 billion. Each DN's separate regulatory asset value associated with its distribution assets was originally allocated to it using an estimate of the overall gas distribution business regulatory asset value as at 1 April 2002. The allocation was aimed at minimising unnecessary regional differentials in transportation charges.

Price control formulae specify a maximum allowed revenue for each DN. Each formula retains a 65% fixed, 35% variable revenue associated with transportation volume changes, a mains replacement incentive mechanism and the pass-through of prescribed rates and gas transporter licence fees. In any year, revenue can be more or less than is allowed under the price control formula, although it should be set to recover allowed revenue. Any difference is carried forward and charges are adjusted accordingly in future periods.

Replacement expenditure maintains the safety and the reliability of the network, by replacing older gas pipes with modern pipes. Ofgem treats 50% of projected replacement expenditure as recoverable during the year and 50% as recoverable over future years. Each DN is subject to its own mains replacement incentive mechanism and retains 33% of any outperformance against Ofgem's annual cost targets as additional return or, alternatively, bears 50% of any overspend if it underperforms.

Ofgem has established standards of service National Grid Gas is required to meet that apply to DN operations. These include overall standards of service, for example answering 90% of all calls to the national gas emergency number within 30 seconds of the call being connected and attending 97% of reports of a gas escape or other gas emergency within the required timescale; connections standards of service that require connections to be provided to consumers to agreed timescales after an unplanned interruption; and guaranteed standards of service for other transportation services. Compensation is paid to customers for any failure to meet guaranteed or connections standards of service.

Metering business

The metering business provides gas meters and meter installation and maintenance services to gas suppliers in the regulated gas market. It provides services to an asset base of around 19 million domestic, industrial and commercial gas meters, situated throughout Great Britain.

The metering business is regulated by Ofgem as it has a dominant market position in the provision of existing meters to UK gas suppliers.

Although the metering business operates within the parameters set out within National Grid Gas's two gas transporter licences and hence is subject to price controls with respect to its meters, the pricing for the majority of meters is specified by long-term contracts with gas suppliers. These contracts provide gas suppliers with the flexibility to replace National Grid Gas's meters whilst reducing the risk of asset stranding.

Meter reading business

The meter reading business provides meter reading services for gas suppliers and for the DNs.

The provision of meter reading services for gas suppliers is unregulated, the market being fully competitive, but the provision of services for the DNs is regulated by Ofgem.

The pricing for meter reading services for gas suppliers is determined by medium term contracts.

De-minimis activities

De-minimis activities comprise those activities undertaken by National Grid Gas which do not form part of its DN business, metering business, meter reading business, NTS business or LNG storage business, based on the definitions of those businesses in National Grid Gas's two gas transporter licences, and which have not been specifically consented to by Ofgem.

De-minimis activities mainly comprise the provision of contracting type services for other companies in the National Grid group of companies and for third parties.

While the carrying out of de-minimis activities is not directly regulated by Ofgem, the overall volume of such activities are constrained by two caps set out in National Grid Gas's gas transporter licences. The revenue cap restricts the aggregate revenue that can be earned from de-minimis activities to no more than 2.5% of the revenue from the regulatory businesses and the investment cap restricts the aggregate net investment in de-minimis activities to no more than 2.5% of National Grid Gas's net assets.

Other activities

Other activities comprise those activities undertaken by National Grid Gas which would be classed as de-minimis activities except that Ofgem has given specific consent for these activities to be undertaken. Such consents are for limited duration, but can be extended or withdrawn by Ofgem.

Other activities mainly comprise the provision of common services to other companies in the National Grid group of companies and the provision of specific services to the four gas distribution networks sold in 2005.

Current and future developments

External market developments

Market structure and ownership

There have been no significant changes in the structure of the UK gas infrastructure market since 2005, when National Grid Gas sold four of our regional gas distribution networks to other operators.

Energy market developments

The UK is in a period of changing energy supply patterns, as more reliance is placed on imported gas. The decline in UK continental shelf gas reserves means there is a continued trend toward greater use of imported gas for both consumption and power generation.

As a consequence of the decline in gas production from the UK continental shelf, National Grid Gas's latest forecast is that the UK will import around 50% of its gas requirements by the end of the decade.

Regulatory developments

During the year ended 31 March 2007, there were no significant changes in the legislative and regulatory framework in the UK.

In January 2007, the European Commission published its final report on its energy sector competition inquiry, concluding that further action is required to improve energy markets in the European Union. It focused on problems from high levels of market concentration as well as vertical integration of supply, generation and infrastructure leading to a lack of equal access to, and sufficient investment in infrastructure. The report also called for improvement in the regulatory framework to remove gaps in regulation, address concerns with market concentration and increase transparency in market operations.

Price controls

The current price controls for National Grid Gas's DNs were extended for one year until 31 March 2008. National Grid Gas is currently in discussions with Ofgem on the next five year price control for the period from 1 April 2008 to 31 March 2013.

Legal and related matters

Metering competition investigation

In June 2005, Ofgem announced that it was going to investigate certain aspects of the domestic gas metering business under the Competition Act 1998 and information requested as part of this investigation has been provided to Ofgem. No findings have been issued with respect to this investigation. However, a supplemental statement of objections was issued by Ofgem in April 2007, to which National Grid Gas responded in early July 2007, since when a representations hearing has been held.

Environmental remediation

In last year's DN regulatory accounting statements it was noted that National Grid Gas, together with the Environment Agency, had sought judicial review to clarify the legal position with regard to the remediation of a site in Bawtry, Yorkshire, a former gas site that was not part of the assets that formed part of the gas privatisation in 1986 and therefore had never been owned by National Grid Gas. On 17 May 2006, the High Court found in favour of the Environment Agency. However, the judgement concluded that the matters raised in the proceedings were of considerable general importance and permission to apply for leave to appeal directly to the House of Lords was granted.

A hearing before the House of Lords took place on 21 May 2007 and a unanimous judgement in favour of National Grid Gas was received on 27 June 2007. Therefore, National Grid Gas plc (as well as its holding and subsidiary companies) has no legal liability with respect to the site in Bawtry, nor for other UK gas sites which did not form part of the assets acquired at the time of privatisation.

Principal risks and uncertainties

Risk management

Understanding and managing risks is integral to the way National Grid Gas is run. There is a well established enterprise-wide risk management process that ensures risks are consistently assessed, recorded and reported in a visible, structured and continuous manner, the outputs of which are primarily used as a management tool. A secondary and natural output from this process is information that provides assurance to management at all levels and thus helps safeguard National Grid Gas's assets and reputation. It is designed to manage rather than eliminate material risks to the achievement of strategic and business objectives while also recognising that any such process can provide only reasonable, and not absolute, assurance against material misstatement or loss. This process complies with the Turnbull working party guidance (revised October 2005) and, in addition, contributes towards compliance with obligations under the Sarbanes-Oxley Act as well as other internal assurance activities.

Risk management in National Grid Gas has become further embedded over time and this experience has enabled the identification of a number of key success criteria linked to both the risk management framework and process that, if in place, will help ensure the process continues to remain embedded.

The risk management process continues to be based on both bottom-up and top-down assessments of operational, financial and other business or project risks. From the bottom-up, National Grid Gas's business units prepare and maintain risk registers that capture key risks and the actions being taken to manage them. These risk registers are regularly reviewed and discussed by the executive committees for those business units. The key element in the top-down assessments of the enterprise-wide risk profile is the involvement of Directors and other senior management at critical stages in the review process. Their review and debate of bottom-up assessments produces the overall evaluations of the risks that are faced by National Grid Gas. In addition, the Executive, the Risk & Responsibility and the Audit Committees of National Grid plc review National Grid's overall risk profile twice a year. The Audit Committee of National Grid plc also reviews the risk management process at least once during each year and reports on this to the Board of National Grid plc.

During the year National Grid Gas has continued to derive benefits from this process through ongoing interaction with National Grid plc's Internal Audit function and Sarbanes-Oxley teams. The external benchmarking exercise of National Grid as a whole has continued with other FTSE 100 companies and public sector organisations to measure the effectiveness of the approach and exchange ideas on best practice. With the move to a line of business operating model, the opportunity is being taken to restructure risk and compliance management services to ensure approaches are consistent across businesses and continue to provide value to business operations, including major projects.

Risk factors

National Grid Gas's risk management process has identified the following risk factors which could have a material adverse effect on its business, financial condition, results of operations and reputation, as well as the value and liquidity of its securities. Not all of these factors are within National Grid Gas's control. In addition, other factors besides those listed below may have an adverse effect on National Grid Gas. Any investment decision regarding National Grid Gas's securities and any forward-looking statements made by it should be considered in the light of these risk factors.

Changes in law or regulation could have an adverse effect on National Grid Gas's results of operations.

National Grid Gas's principal businesses are utilities or networks that are subject to regulation by the Government and other authorities. Consequently, changes in law or regulation could adversely affect it. Regulatory decisions concerning, for example, whether licences or approvals to operate are granted or are renewed, whether market developments have been satisfactorily implemented and whether there has been any breach of the terms of a licence or approval, the level of permitted revenues for National Grid Gas's businesses and proposed business development activities could have an adverse impact on its results of operations, cash flows, the financial condition of its businesses and the ability to develop those businesses in the future. For further information, see the 'External market environment' and 'Regulation' sections of this Operating and Financial Review.

Breaches of, or changes in, environmental or health and safety laws or regulations could expose National Grid Gas to claims for financial compensation and adverse regulatory consequences, as well as damaging National Grid Gas's reputation.

Aspects of National Grid Gas's activities are potentially dangerous, such as the transmission and distribution of natural gas. Gas utilities also typically use and generate in their operations hazardous and potentially hazardous products and by-products. In addition, there may be other aspects of National Grid Gas's operations which are not currently regarded or proved to have adverse effects but could become so. National Grid Gas is subject to laws and regulations relating to pollution, the protection of the environment, and how it uses and disposes of hazardous substances and waste materials. It is also subject to laws and regulations governing health and safety matters protecting the public and its employees. Any breach of these obligations, or even incidents that do not amount to a breach, could adversely affect National Grid Gas's results of operations and its reputation. For further information about environmental and health and safety matters relating to National Grid Gas's businesses, see the 'Our Responsibility' section of National Grid's website at www.nationalgrid.com.

Network failure or the inability to carry out critical non-network operations may have significant adverse impacts on both National Grid Gas's financial position and its reputation.

National Grid Gas may suffer a major network failure or may not be able to carry out critical non-network operations. Operational performance could be adversely affected by a failure to maintain the health of the system or network, inadequate forecasting of demand or inadequate record keeping. This could cause National Grid Gas to fail to meet agreed standards of service or be in breach of a licence or approval, and even incidents that do not amount to a breach could result in adverse regulatory and financial consequences, as well as harming its reputation. In addition to these risks, National Grid Gas may be affected by other potential events that are largely outside of its control such as the impact of weather or unlawful acts of third parties. Weather conditions can affect financial performance and severe weather that causes outages or damages infrastructure will adversely affect operational and potentially business performance. Terrorist attack, sabotage or other intentional acts may also physically damage National Grid Gas's businesses or otherwise significantly affect corporate activities and as a consequence adversely impact the results of operations.

National Grid Gas's results of operations depend on a number of factors relating to business performance including performance against regulatory targets and the delivery of anticipated cost and efficiency savings.

Earnings maintenance and growth from National Grid Gas's regulated gas businesses will be affected by its ability to meet or better efficiency targets set by or agreed with Ofgem and other regulators. Earnings from National Grid Gas's regulated businesses will be affected by its ability to recover incurred expenditure. Levels of earnings also depend on meeting service quality standards set by regulators. In addition, from time to time, National Grid Gas also publishes cost and efficiency savings targets for its businesses. National Grid Gas is also reorganising operations along lines of business. To meet these targets and standards, it must continue to improve operational performance, service reliability and customer service. If National Grid Gas does not meet these targets and standards, it is not able to recover incurred expenditure, or it does not implement this reorganisation as envisaged, it may not achieve the expected benefits, its business may be adversely affected and its performance, results of operations and its reputation may be harmed.

Changes to the regulatory treatment of commodity costs may have an adverse effect on the results of operations.

Changes in commodity prices could potentially impact National Grid Gas's gas distribution businesses. Current regulatory arrangements in the UK provide the ability to pass-through virtually all of the increased costs related to commodity prices to consumers. However, if Ofgem were to restrict this ability, it could have an adverse effect on National Grid Gas's operating results.

National Grid Gas's reputation may be harmed if consumers of energy suffer a disruption to their supply even if this disruption is outside its control.

National Grid Gas's gas distribution business is responsible for transporting available gas. National Grid Gas consults with and provides information to regulators, governments and industry participants about future demand and the availability of supply. However, where there is insufficient supply, National Grid Gas's role is to manage the relevant network safely, which in extreme circumstances may require National Grid Gas to disconnect consumers.

Fluctuations in exchange rates and interest rates could have a significant impact on National Grid Gas's results of operations because of the significant proportion of its borrowings, and derivative financial instruments that may potentially be affected by such fluctuations.

National Grid Gas's results of operations may be impacted because a significant proportion of its borrowings and derivative financial instruments are affected by changes in exchange rates and interest rates. For further information about this and how this risk is mitigated, see the 'Financial position and financial management' section of this Operating and Financial Review.

The nature and extent of National Grid Gas's borrowings means that an increase in interest rates could have an adverse impact on its financial position and business results.

A significant proportion of National Grid Gas's borrowings are subject to variable interest rates which may fluctuate with changes to prevailing interest rates. Increases in these interest rates could therefore increase National Grid Gas's costs and diminish its profits. For further information about this, see the 'Financial position and financial management' section of this Operating and Financial Review.

National Grid Gas's financial position may be adversely affected by a number of factors including restrictions in borrowing and debt arrangements, changes to credit ratings and effective tax rates.

National Grid Gas is subject to certain covenants and restrictions in relation to its listed debt securities and its bank lending facilities. It is also subject to restrictions on financing which have been imposed by regulators. These restrictions may hinder National Grid Gas in servicing the financial requirements of its businesses. National Grid Gas's debt is rated by credit rating agencies and changes to these ratings may affect both its borrowing capacity and the cost of those borrowings. The effective rate of tax it pays may be influenced by a number of factors including changes in law and accounting standards and National Grid Gas's overall approach to tax planning, the results of which could increase that rate.

Future funding requirements of pension schemes could adversely affect National Grid Gas's results of operations.

Substantially all of National Grid Gas's employees are members of a defined benefit scheme where the scheme assets are held independently of National Grid Gas's own financial resources. Estimates of the amount and timing of future funding for the scheme are based on various actuarial assumptions and other factors including, among other things, the actual and projected market performance of the scheme assets, future long-term bond yields, average life expectancies and relevant legal requirements. The impact of these assumptions and other factors may result in a requirement for additional contributions to the pension scheme. National Grid Gas's legal obligations to the scheme are limited to paying the employers' contribution rate set by the trustees of the scheme. However, circumstances may require that it makes additional contributions. To the extent that any increases in contributions are not recoverable under National Grid Gas's price controls, its results of operations could be adversely affected.

New or revised accounting standards, rules and interpretations by the UK, or international accounting standard setting boards and other relevant bodies could have an adverse effect on National Grid Gas's reported financial results.

The accounting treatment under International Financial Reporting Standards (IFRS), as adopted by the European Union, of replacement expenditure, pension and post retirement benefits, derivative financial instruments and commodity contracts significantly affect the way National Grid Gas's financial position and results of operations are reported. As a body of practice develops for IFRS, the application and interpretation of accounting principles to National Grid Gas's circumstances, and to those areas in particular, could result in changes in the financial results and financial position that it reports. In addition, new standards, rules or interpretations may be issued which could also have significant effects.

Key performance indicators

National Grid Gas measures the achievement of objectives through the use of qualitative assessments and through the monitoring of quantitative indicators, termed key performance indicators (KPIs).

In line with operating objectives, both financial and non-financial KPIs are used. Where relevant, KPIs are used as the primary measures of whether principal operating objectives have been achieved. However, the scale and size of National Grid Gas's operations means that many other detailed performance measures are used in addition to KPIs. KPIs are also used to measure performance against the primary objective of growing the business to create value for National Grid's shareholders. Qualitative assessments are used to judge progress against objectives in areas where numerical measures are less relevant.

The majority of KPIs are unchanged from last year, but the table below has been expanded to include business-specific reliability KPIs.

Value	KPI	Description	Target	Results
Performance – safety	Injuries to members of the public	Members of the public injured as a direct result of gas distribution and metering operations[1]	Zero	2006/07: 20 2005/06: 11
	Employee lost time injury frequency rate	Injuries resulting in employees taking time off work (per 100,000 hours worked)	Zero	2006/07: 0.17 2005/06: 0.17
	Gas safety-related service standards	Proportion of uncontrolled gas escapes attended within one hour	97%	2006/07: 98.51% 2005/06: 97.97%
	Gas distribution mains replacement	Kilometres of gas main decommissioned	2006/07: 1,824 km 2005/06: 1,724 km	2006/07: 1,850 km 2005/06: 1,724 km
	Sickness absence rate	Proportion of available work days which are lost due to sickness	Zero work-related sickness[2]	2006/07: 2.2% 2005/06: 2.2%
Performance – reliability	Gas distribution network reliability	The proportion of total customer days without unplanned customer interruptions	99.999%	2006/07: 99.999% 2005/06: 99.999%
Performance – efficiency and financial performance	Adjusted operating profit[4]	Operating profit from continuing operations excluding exceptional items and remeasurements for the gas distribution and metering businesses	To increase sufficiently to support 7% growth in National Grid's dividend through to March 2008	2006/07: £484 million 2005/06: £583 million
	Operating cash flows	Cash generated from continuing operations of the gas distribution and metering businesses		2006/07: £1,001 million 2005/06: £705 million
Growth - investment	Capital expenditure	Additions to plant and equipment and to intangible assets for the gas distribution and metering businesses	There is no numerical target for capital expenditure, as each investment is different and is considered on its merits.	2006/07: £572 million 2005/06: £509 million
Growth – value from investment	Return on investment	Adjusted regulatory profit[5] for gas distribution as a percentage of regulatory asset value	To achieve a minimum return of 5.05% from 1 April 2007 consistent with the return projected by Ofgem for the 5-year price control period commencing 1 April 2007.	2006/07: 4.4% 2005/06: 5.5%
Talent – inclusion and diversity	Percentage of female employees	Proportion of employees who are female	There are no specific targets, the aim being to ensure that the best candidates are recruited regardless of sex, race, disability, sexual orientation, age, religion or belief	2006/07: 20.0% 2005/06: 19.4%
	Percentage of ethnic minority employees	Proportion of employees who are black and minority ethnic		2006/07: 4.5% 2005/06: 4.5%
Responsibility – climate change	Reduction in greenhouse gas emissions[6]	CO_2 equivalent emissions estimated to be caused by gas distribution operations	Year on year reduction	2006/07: 0.3%

Value	KPI	Description	Target	Results
Responsibility – protect the environment	Significant direct environmental incidents	Own fault and contractor related environmental incidents	Zero	2006/07: 1, zero 2005/06: zero, zero
	Total value of fines from environmental prosecutions	Financial amount of fines imposed	Zero	2006/07: zero 2005/06: zero

1 Injuries comprise fatalities, injuries that require the person to receive hospital treatment and other injuries reported under the Reporting of Injuries, Diseases and Dangerous Occurrences Regulations (RIDDOR).

2 The sickness absence rate includes absences resulting from both work-related and non-work related illnesses. The target relates to work-related illnesses, however, National Grid Gas does not have a measure that excludes non work-related illnesses sufficiently accurately.

3 The KPI for a 30% reduction in controllable costs by 31 March 2007 in for gas distribution business is no longer included as it was achieved by 31 March 2006.

4 Operating profit from continuing operations including exceptional items and remeasurements fell from £556 million in 2005/06 to £475 million in 2006/07.

5 The calculation of adjusted regulatory profit is explained on page 19.

6 The KPI used for measuring reduction in greenhouse gas emissions has been changed from last year's measure of greenhouse gas emissions per £m revenue to a measure that aligns with National Grid's target of a 60% reduction in emissions.

Performance during the year

In accordance with the requirements of National Grid Gas's DN gas transporter licence, the performance of the businesses included within these DN regulatory accounting statements is considered in aggregate. These businesses are the four DNs, the metering business, the meter reading business and the associated de-minimis activities and other activities. The aggregate of these businesses is referred to as the gas distribution and metering businesses.

Performance information relating to National Grid Gas as a whole can be found in its Annual Report and Accounts 2006/07. The performance information provided below is that which is particularly relevant to the gas distribution and metering businesses.

Performance

Safety

Aspects of safety performance deteriorated in 2006/07 compared with 2005/06, which is disappointing after the significant improvement recorded last year. The aim in 2007/08 is to improve safety performance in line with National Grid Gas's goal of zero injuries.

Public safety

20 members of the public were injured as a result of gas distribution and metering operations compared with 11 during 2005/06.

Targets for safety-related standards set by Ofgem were again exceeded with more than 98% of 'uncontrolled' gas escapes (where the gas leak cannot be controlled by turning the gas supply off at the meter) attended within one hour and more than 99% of 'controlled' gas escapes (where the gas leak can be controlled at the meter) attended within two hours.

The DNs decommissioned approximately 1,850 km of gas pipes in 2006/07, exceeding the HSE target this year, compared with 1,724 km in 2005/06.

Employee safety

During 2006/07, 24 of gas distribution and metering employees received injuries that resulted in them taking time off work, compared with 25 in 2005/06. Employee lost time injuries per 100,000 hours worked was 0.17 in both years.

Contractor safety

There was a reduction in contractor lost time injuries from 26 in 2005/06 to 14 in 2006/07.

Employee health

Around 2.2% of available work days were lost due to sickness absence in 2006/07, the same as the previous year. This equates to 5.8 days of sickness per employee per year. The UK Confederation of British Industry's 2007 sickness absence survey reported that average annual sickness for UK company employees was 7.0 days.

Reliability

Over the year, gas distribution and metering achieved all the standards of service set by Ofgem.

Efficiency

National Grid Gas has continued to institute measures during the year to improve efficiency, with the implementation of a shared services function to support its gas transmission and gas distribution businesses.

Gas distribution performance

Actual gas consumption fell to 303 TWh in 2006/07, compared with 347 TWh in 2005/06, mainly due to very mild weather in 2006/07. Underlying levels of gas demand, excluding the effects of weather, also fell from 347 TWh in 2005/06 to 331 TWh in 2006/07, thought to be mainly due to the high levels of gas supply prices during 2006/07 affecting usage. The reduction was particularly noticeable for larger users.

Performance under the current distribution network exit incentive scheme and the mains replacement incentive scheme was broadly neutral in 2006/07.

Financial performance

Gas distribution and metering operating profit from continuing operations, before exceptional items and remeasurements, fell from £583 million in 2005/06 to £484 million in 2006/07. Operating profit from continuing operations fell from £556 million in 2005/06 to £475 million in 2006/07.

Profit for the year from continuing operations before exceptional items and remeasurements fell from £376 million in 2005/06 to £154 million in 2006/07. Profit for the year from continuing operations fell from £350 million in 2005/06 to £130 million in 2006/07.

Cash flows generated by continuing operations increased from £705 million in 2005/06 to £1,001 million in 2006/07.

More information on financial performance is contained under financial results on pages 19 to 22.

Growth

Capital investment

Capital investment for the gas distribution and metering businesses continues to increase as increasing demand for gas and the renewal of gas distribution networks require increased investment in infrastructure and £572 million was invested in the form of capital investment during 2006/07, compared with £509 million in 2005/06.

	2007 £m	2006 £m
Reinforcement and extension of gas distribution networks	**156**	149
Replacement expenditure	**333**	295
Metering	**83**	65
Capital investment	**572**	509

Reinforcement and extension expenditure increased from £149 million in 2005/06 to £156 million in 2006/07 reflecting continued investment in the reinforcement of high pressure pipelines, together with higher information technology expenditure to replace obsolete equipment in system control, operational and support activities.

Replacement expenditure increased from £295 million in 2005/06 to £333 million in 2006/07 in line with the planned increase in the long-term iron mains replacement programme agreed with the HSE. During the second year of the alliance partnerships for the DNs, approximately 1,850 kilometres of gas mains have been laid, with an increasing proportion of the workload comprising complex replacement of large diameter mains.

In addition to providing meters for new gas connections and replacing older meters, the metering business is investing in technology such as smart metering and automated meter reading systems in response to customer requirements. Metering capital expenditure in 2006/07 amounted to £83 million, an increase of £18 million compared with £65 million in 2005/06.

Generating value from investments

This year, a return on investment measure is reported for the first time, the purpose of which is to allow National Grid Gas to monitor how it is performing in generating value from its businesses and from the investments it makes. Return on investment has been calculated using the measure developed by Ofgem when setting transmission price controls for the 5 year period commencing 1 April 2007. If the DNs perform in accordance with Ofgem's projections, then they would earn an average annual return of 5.05% using Ofgem's measure. For 2006/07, the DNs return on investment using this measure is 4.4%, compared with 5.5% in 2005/06. The return in 2006/07 is lower than Ofgem's projected return of 5.05%, as due to the reduction in the DN business adjusted operating profit which is discussed on page 20.

The following table shows how return on investment has been calculated:

	Years ended 31 March 2007 £m	2006 £m
DNs adjusted operating profit[1]	**375**	480
Adjustment of operating costs onto a price control basis[2]	**17**	(2)
Investment adjustment[3]	**(117)**	(104)
Excess of regulatory value depreciation over accounting depreciation and amortisation	**(60)**	(69)
Regulatory operating profit	**215**	305
Notional current taxation on a price control basis[4]	**37**	3
Regulatory return	**252**	308
Estimated average regulatory value[5]	**5,766**	5,600
Return on investment – regulatory return as a percentage of regulatory value	**4.4%**	5.5%

1 Adjusted operating profit is operating profit before exceptional items and remeasurements.
2 Adjustments to operating costs primarily comprise movements in provisions which are recognised on an expenditure basis for price control purposes.
3 The investment adjustment is in respect of the 50% of replacement expenditure which is treated as an operating cost for price control purposes, but as capital investment for accounting purposes.
4 Notional current taxation is an allocation of the actual current tax for the year, excluding prior year items and adjusted for the effect of actual interest payments being less than would result from the gearing level assumed by Ofgem when setting the price control.
5 Regulatory values have been restated from previous estimates to reflect the outcome of the extension price control review for the year to 31 March 2008 and are average values for each year.

Talent

Development of talent

Development and recruitment of employees is undertaken on an integrated basis for all National Grid's UK businesses, including the gas distribution and metering businesses.

National Grid Gas continues to invest in the recruitment and development of skilled employees for the future and, in the past year, National Grid recruited 160 trainees onto the apprentice, foundation engineer, graduate and student programmes in which the gas distribution and metering businesses participate. National Grid's UK Foundation Engineering Programme, launched in early 2006, is designed to facilitate the entrance, training and progression of talented people into key engineering roles. In conjunction with Aston University and Energy Utility Skills, the industry sector skills council in the UK, National Grid has also designed an industry specific foundation degree.

Inclusion and diversity

Several employee interest networks have been established in National Grid, focusing on gender, ethnicity and faith and disability. The networks provide a mutually beneficial relationship for our employees by providing opportunities for employees to network with each other and senior management, to attain career building skills and to provide a better understanding of National Grid's businesses.

Working groups have been established with senior executive sponsors focusing on recruitment and employee development, employee engagement, communications and measuring the impact of inclusion and diversity policies. National Grid has also initiated a field force pilot programme in the UK to explore the development of inclusion and diversity best practices examples that can be replicated across operational sites.

At 31 March 2007, 20% of employees were female and 4.5% were from black and ethnic minority groups compared with 19.4% and 4.5% respectively at 31 March 2006.

Relationships

Customer service

The DNs achieved all the connections standards of service over the year, along with all other standards of service set by Ofgem that relate to DN gas transportation services. During the year ended 31 March 2007, around 40,000 new connections were made to the DN networks (2005/06: 50,000). The proportion of service interruptions which were planned (as against unplanned) was 98.92% in 2006/07 compared with a target of 95%, while the proportion of customer complaints responded to within five working days was 94.71% in 2006/07 compared with a target of 90%.

Regulatory relationships

The DNs continue to work very closely with Ofgem on the renewal of the gas distribution networks and in expanding those networks to meet new and changing demand. In addition, National Grid Gas seeks to maintain a professional approach with Ofgem in areas where there is disagreement, in particular with respect to Ofgem's investigation into metering services as discussed on page 10.

Suppliers

Progress continues to be made in improving the quality of relationships with suppliers. A particular focus has been on the investment programmes in gas distribution operations, where alliances have been created with a number of suppliers. Under these alliances, the suppliers and DNs work in combined teams to deliver construction projects and share in the financial risk associated with these projects.

Community investment

Community investment takes place on a company basis and further information can be found in the National Grid Gas Annual Report and Accounts 2006/07.

Responsibility

Climate change

National Grid as a whole has committed to reducing its greenhouse gas emissions by 60% against a verified baseline, in advance of the target date of 2050 set by the UK Government.

The vast majority of emissions relating to the gas distribution and metering businesses fall within Scope 1 of the World Resources Institute' greenhouse gas protocol initiative. This comprises direct emissions such as methane leaking from the gas distribution networks. Scope 2 emissions comprise indirect emissions, such as those resulting from purchased electricity.

Emissions made by National Grid Gas cannot all be attributed to specific businesses, but during 2006/07, Scope 1 emissions for methane leakage from gas distribution networks amounted to some 2,317 million tonnes CO_2 equivalent, a 0.3% reduction compared with emissions of 2,325 million tonnes in 2005/06. During the year, the DNs replaced approximately 1,850 kilometres of old cast iron pipes, the largest source of these emissions.

Information on the total Scope 1 and Scope 2 emissions made by National Grid Gas can be found in its Annual Report and Accounts 2006/07.

Historically contaminated land

Land contamination issues in respect of sites currently owned by the DNs and previously used for gas production are managed by National Grid Properties.

Protecting the environment

All employees work to certified ISO 14001 environmental management systems.

There was one significant environmental incident in 2006/07 arising directly from distribution and metering business operations, compared with none in 2005/06. There were no prosecutions by enforcing bodies resulting from this incident.

Business ethics

In March 2007, National Grid published its Standards of Ethical Business Conduct, replacing its UK Code of Business Conduct. The new Standard provides a common set of practical guidelines to ensure behaviours are lawful, policies and licences are complied with, and the values set out in National Grid's Framework for Responsible Business and its core values of respect, integrity and ownership are followed.

Financial results

Financial results and position are reported in accordance with International Financial Reporting Standards (IFRS) as adopted in the European Union.

The financial results of the gas distribution and metering businesses are presented within continuing operations.

Measurement of financial performance and use of adjusted profit measures

In considering the financial performance of regulatory businesses, each primary financial measure of operating profit, profit before tax and profit for the year is analysed into two components, comprising firstly 'business performance' which excludes exceptional items and remeasurements and secondly 'exceptional items and remeasurements'. Exceptional items and remeasurements are excluded from the measures of business performance used by management to monitor financial performance, as they are considered to distort the comparability of reported financial performance from year to year.

Measures of business performance are referred to in these regulatory accounting statements as adjusted profit measures in order to clearly distinguish them from the comparable total profit measures of which they are a component. Adjusted operating profit, adjusted profit before tax and adjusted earnings differ from total operating profit, profit before tax and profit for the year respectively by the exclusion of exceptional items and remeasurements.

Exceptional items and remeasurements are items of income and expenditure that, in the judgment of management, should be disclosed separately on the basis that they are material, either by their nature or their size, and are relevant to an understanding of our financial performance. Items of income or expense that are considered by management for designation as exceptional items include such items as significant restructurings, write-downs or impairments of non-current assets, material changes in environmental provisions and gains or losses on disposals of businesses or investments. Remeasurements comprise gains or losses recorded in the income statement arising from changes in the fair value of derivative financial instruments. These fair values increase or decrease as a consequence of changes in financial indices and prices over which National Grid Gas has no control.

Adjusted profit measures are limited in their usefulness compared with the comparable total profit measures, as they exclude important elements of underlying financial performance, namely exceptional items and remeasurements. Management believes that in separately presenting financial performance in two components it is easier to read and interpret financial performance between periods, as adjusted profit measures are more comparable by excluding the distorting effect of exceptional items and remeasurements, and exceptional items and remeasurements are more clearly understood if separately identified and analysed. The presentation of these two components of financial performance is additional to, and not a substitute for, the comparable total profit measures presented.

Management uses adjusted profit measures as the basis for monitoring financial performance and in communicating financial performance to investors in external presentations and announcements of financial results. Internal financial reports, budgets and forecasts are primarily prepared on the basis of adjusted profit measures, although planned exceptional items, such as significant restructurings, are also reflected in budgets and forecasts. Management compensates for the limitations inherent in the use of adjusted profit measures through the separate monitoring and disclosure of exceptional items and remeasurements as a component of overall financial performance.

Operating financial performance

	Years ended 31 March	
	2007	2006
	£m	£m
Revenue	**1,470**	1,497
Operating costs excluding exceptional items and remeasurements	**(986)**	(914)
Adjusted operating profit	**484**	583
Exceptional items	**(9)**	(27)
Total operating profit	**475**	556

Revenue, operating costs and operating profit

The movements in the year in revenue, operating costs and operating profit by can be summarised as follows by regulatory business:

	Revenue £m	Operating costs £m	Operating profit £m
2005/06 results	1,497	(941)	556
Add back 2005/06 exceptional items	-	27	27
2005/06 adjusted results	1,497	(914)	583
North West DN	1	(18)	(17)
East of England DN	7	(27)	(20)
West Midlands DN	(2)	(14)	(16)
North London DN	(36)	(16)	(52)
Metering	2	4	6
Meter reading	2	(4)	(2)
De-minimis activities	2	(2)	-
Other activities	(8)	10	2
Inter-business	5	(5)	-
2006/07 adjusted results	1,470	(986)	484
2006/07 exceptional items	-	(9)	(9)
2006/07 results	1,470	(995)	475

The principal factors causing the movements between 2005/06 and 2006/07 are summarised below:

	Revenue £m	Operating costs £m	Operating profit £m
2005/06 results	1,497	(941)	556
Add back 2005/06 exceptional items	-	27	27
2005/06 adjusted results	1,497	(914)	583
Transportation price changes	73	-	73
Weather and transportation volumes	(69)	-	(69)
Timing of recoveries	(32)	-	(32)
DN depreciation and amortisation	-	(12)	(12)
DN business rates	-	(23)	(23)
Transfer of employee liabilities	-	(17)	(17)
Other	1	(20)	(19)
2006/07 adjusted results	1,470	(986)	484
2006/07 exceptional items	-	(9)	(9)
2006/07 results	1,470	(995)	475

Revenue for gas distribution and metering fell by £27 million in 2006/07 compared to 2005/06.

DN formula income was up by £4 million, with the benefit of an average price increase of 8.8% implemented on 1 October 2006 giving rise to a £73 million increase in revenue. This was largely offset by delivery volumes being significantly lower than the prior year, reducing revenue by £69 million.

The weather in 2006/07 was significantly warmer than 2005/06 lowering consumption by 28 TWh, which, combined with the impact of underlying volumes being lower by 16 TWh (caused principally by the continuing effect of high wholesale gas prices), led to an under-recovery of income of £42 million in 2006/07. Together with a £10 million under-recovery in 2005/06, this resulted in a net year-on-year timing impact on the recovery of income of £32 million.

Operating costs were £72 million higher in 2006/07 compared to 2005/06. Depreciation and amortisation costs for the DNs were £12 million higher, reflecting the increased capital investment in the gas distribution networks. There was a £23 million increase in business rates following the changes in rateable values introduced from 1 April 2005. The remaining increase in operating costs of £20 million was mainly driven by workload, including significant investment in maintenance and other safety-related activities in the DNs.

Adjusted operating profit was £99 million lower in 2006/07 than 2005/06.

The exceptional charge of £9 million in 2006/07 related to the costs associated with the creation of the new shared services organisation. The exceptional charge in 2005/06 of £27 million related to DN restructuring costs under the Way Ahead programme.

Operating profit was £81 million lower in 2006/07 than 2005/06 due to the £27 million reduction in revenue, the £72 million increase in operating costs and the £18 million reduction in exceptional charges.

Profit for the year from continuing operations

Net finance costs and taxation largely comprise amounts relating to National Grid Gas as a whole which have been allocated as described in the basis of preparation of regulatory accounting statements on page 38.

Adjusted profit for the year

	Years ended 31 March	
	2007 £m	2006 £m
Adjusted operating profit	**484**	583
Net finance costs excluding exceptional items and remeasurements	**(188)**	(116)
Adjusted profit before taxation	**296**	467
Taxation excluding taxation on exceptional items and remeasurements	**(142)**	(91)
Adjusted profit from continuing operations	**154**	376

Profit for the year

	Years ended 31 March	
	2007 £m	2006 £m
Total operating profit	**475**	556
Net finance costs	**(208)**	(126)
Profit before taxation	**267**	430
Taxation	**(137)**	(80)
Profit from continuing operations	**130**	350

Net finance costs

Net interest excluding exceptional finance costs and remeasurements, as allocated to the gas distribution and metering businesses, increased by £72 million from 2005/06 to 2006/07. This was primarily explained by an increase in average debt balances.

Exceptional finance costs and remeasurements

Exceptional finance costs allocated to the gas distribution and metering businesses of £23 million in 2006/07 relate to the early repayment of debt. There were no exceptional finance costs allocated to the gas distribution and metering businesses in 2005/06.

Financial remeasurements relate to allocated net gains on derivative financial instruments of £3 million, compared with allocated net losses of £10 million in 2005/06.

Taxation

A net charge of £137 million was allocated to the gas distribution and metering businesses in 2006/07, compared with £80 million in 2005/06. This includes allocated net tax credits in respect of exceptional items and remeasurements amounting to £5 million and £11 million in 2006/07 and 2005/06 respectively. The effective tax rate was 51% for 2006/07 and 19% for 2005/06.

Excluding the effect of net tax credits on exceptional items and remeasurements, the effective tax rate for 2006/07 and 2005/06 was 48% and 19% respectively, compared with a standard UK corporation tax rate of 30% for both years. These effective tax rates reflected an allocated prior year tax charge in 2006/07 equivalent to an effective tax rate of 16% and an allocated prior year tax credit in 2005/06 equivalent to 5%. These prior year items arose from the settlement of outstanding prior year tax issues.

A reconciliation of the main components giving rise to the difference between the relevant effective tax rate and the UK standard corporation tax rate is shown in note 10 to the regulatory accounting statements.

Profit for the year

The gas distribution and metering business profit for the year fell from £350 million in 2005/06 to £130 million in 2006/07 as a consequence of the above changes.

Adjusted profit measures

The following tables reconcile the adjusted profit measure to the corresponding total profit measure in accordance with IFRS.

a) Reconciliation of adjusted operating profit to total operating profit

	Years ended 31 March	
	2007	2006
	£m	£m
Adjusted operating profit	**484**	583
Exceptional operating items	**(9)**	(27)
Total operating profit	**475**	556

Adjusted operating profit is presented on the face of then Income Statement, under the heading 'Operating profit – before exceptional items and remeasurements'.

b) Reconciliation of adjusted profit before taxation to profit before taxation

	Years ended 31 March	
	2007	2006
	£m	£m
Adjusted profit before taxation	**296**	467
Exceptional operating items	**(9)**	(27)
Exceptional finance costs	**(23)**	-
Financial remeasurements	**3**	(10)
Total profit before taxation	**267**	430

Adjusted profit before taxation is presented on the face of the Income Statement, under the heading 'Profit before taxation – before exceptional items and remeasurements'.

c) Reconciliation of adjusted profit for the year to profit for the year

	Years ended 31 March	
	2007	2006
	£m	£m
Adjusted profit for the year	**154**	376
Exceptional operating items	**(9)**	(27)
Exceptional finance costs	**(23)**	-
Financial remeasurements	**3**	(10)
Tax on exceptional items and remeasurements	**5**	11
Profit for the year	**130**	350

Adjusted profit for the year is presented on the face of the Income Statement, under the heading 'Profit for the year from continuing operations – before exceptional items and remeasurements'.

Cash flows

Cash flows from operating activities

Cash generated from operations for the gas distribution and metering businesses was £1,001 million in 2006/07 compared with £705 million in 2005/06. This included cash outflows relating to exceptional items of £25 million and £76 million respectively. After reflecting cash flows relating to tax paid, net cash inflow from operating activities was £1,011 million, compared with £635 million in 2005/06.

In 2006/07, there was a net corporate tax repayment of £10 million allocated to gas distribution and metering compared with an allocated payment of £70 million in 2005/06.

Cash inflows from investing activities

Cash outflows from investing activities for gas distribution and metering fell from £3,307 million in 2005/06 to £820 million in 2006/07. This was fall was primarily a result of an interest free loan in 2005/06 to National Grid Gas's immediate parent company, National Grid Gas Holdings plc, of which £2,771 million was allocated to the gas distribution and metering businesses. This loan represented part of the £5,750 million cash received by National Grid Gas from the sales of four of four gas networks in June 2005. Cash outflows to purchase property, plant and equipment and intangible fixed assets, net of disposal proceeds, increased to £602 million in 2006/07 from £513 million in 2005/06, as a result of the increase in capital investment. Allocated cash outflows to acquire financial investments increased from £23 million in 2005/06 to £218 million in 2006/07.

Cash flows from financing activities

Cash flows from financing activities largely comprise cash flows of National Grid Gas as a whole which have been allocated as described in the basis of preparation of regulatory accounting statements on page 38.

Net cash related to financing activities changed from an inflow of £2,827 million in 2005/06 to an outflow of £238 million in 2006/07. The position in 2006/07 reflects allocated payments to providers of finance, in the form of net interest and dividends, of £1,476 million and allocated inflows from additional net borrowings of £1,238 million. The cash inflow in 2005/06 arose from a net increase in allocated borrowings and derivatives of £3,164 million less allocated payments to providers of finance of £337 million.

Allocated net interest cash outflows, excluding exceptional debt redemption costs, increased from £134 million in 2005/06 to £207 million in 2006/07, due to higher average net debt. Allocated exceptional debt redemption costs from restructuring the debt portfolio were £23 million in 2006/07 compared with none in 2005/06.

Dividends

Dividends in respect of the financial year

The following table shows the ordinary dividends paid or payable by National Grid Gas in respect of the last two financial years and which have been allocated to the gas distribution and metering businesses as described in the basis of preparation of regulatory accounting statements on page 38. These dividends do not include any associated UK tax credit in respect of such dividends.

	2007 £m	2006 £m
Interim	**171**	203
Final	**-**	1,075
Total	**171**	1,278

In accordance with IFRS, dividends are reported in the financial statements for the year in which they are approved. As a consequence, the final dividend for 2005/06 is reported in the current year.

Financial position and financial management

Going concern

Having made enquiries, the Directors consider that National Grid Gas has adequate resources to continue in business for the foreseeable future and that it is therefore appropriate to adopt the going concern basis in preparing these regulatory accounting statements.

Capital structure

Balance sheet

The balance sheet of the gas distribution and metering businesses at 31 March 2007 can be summarised as follows:

	Assets £m	Liabilities £m	Net assets £m
Property, plant and equipment and non-current intangible assets	6,030	-	6,030
Other non-current assets and liabilities	4,025	(922)	3,103
Current assets and liabilities	220	(588)	(368)
Deferred tax	-	(1,190)	(1,190)
Total before net debt	10,275	(2,700)	7,575
Net debt	417	(3,769)	(3,352)
Total as at 31 March 2007	**10,692**	**(6,469)**	**4,223**
Total as at 31 March 2006	10,461	(5,188)	5,273

The reduction in net assets from £5,273 million at 31 March 2006 to £4,223 million at 31 March 2007 resulted from attributed dividends paid of £1,246 million partly offset by the profit for the year of £130 million, changes in allocation of funding between National Grid Gas's regulatory businesses of £49 million, net income recognised directly in equity of £8 million and other changes in equity of £9 million.

Net debt and gearing

Allocated net debt increased by £1.1 billion from £2.3 billion at 31 March 2006 to £3.4 billion at 31 March 2007, as a result of an increase in allocated borrowings of £1.1 billion.

The composition of net debt at 31 March 2007 is shown in note 27 to the regulatory accounting statements.

Gearing at 31 March 2007 and 31 March 2006, calculated as net debt at that date expressed as a percentage of net debt plus net assets shown in the balance sheet, amounted to 44% and

31% respectively. By comparison, the gearing ratio, adjusted for the inclusion of regulated businesses at their estimated regulatory asset values (adjusted gearing ratio), amounted to 38% at 31 March 2007 compared with 27% 31 March 2006. The adjusted gearing ratio at 31 March 2006 has been restated to reflect the impact of the outcomes of the gas transmission and gas distribution price control reviews on estimates of regulatory asset values.

National Grid Gas believes this adjusted ratio is a more relevant measure of gearing than one based on book values alone, because the book values do not reflect the economic value of the regulated business assets. A reconciliation of the adjustments necessary to calculate adjusted net assets is shown in the following table:

	2007 **£m**	2006* £m
Net assets per balance sheet	**4,223**	5,273
Adjustment for regulatory asset values	**1,650**	1,620
Deferred tax	**(495)**	(486)
Adjusted net assets	**5,378**	6,407

* The regulatory adjustments at 31 March 2006 have been restated as described above.

Equity shareholders' funds

Equity shareholders' funds fell from £5,273 million at 31 March 2006 to £4,223 million at 31 March 2007. The decrease was mainly explained by attributed equity dividends paid of £1,246 million being greater than the profit for the year to 31 March 2007 of £130 million.

Liquidity and treasury management

Cash flow

Cash flows from National Grid Gas's operations are largely stable over a period of years, but they do depend on the timing of customer payments. National Grid Gas's DN operations are subject to multi-year price control agreements with the regulator, Ofgem. Significant changes in volumes, for example as a consequence of weather conditions, can affect cash flows in those businesses, with abnormally mild or cold weather driving volumes down or up respectively. Subject to this, cash flows are essentially stable.

Cash flow forecasting

Both short- and long-term cash flow forecasts are produced frequently to assist in identifying the liquidity requirements of National Grid Gas.

These forecasts are supplemented by a financial headroom position, details of which are supplied to the Finance Committee of the Board of National Grid plc regularly to demonstrate funding adequacy for at least a 12 month period. National Grid Gas also maintains a minimum level of committed facilities in support of that objective.

Credit facilities and unutilised Commercial Paper and Medium Term Note Programmes

National Grid Gas has both committed and uncommitted facilities that are available for general corporate purposes. At 31 March 2007, National Grid Gas plc had a US$2.5 billion US Commercial Paper Programme (unutilised) and a US$1.25 billion Euro Commercial Paper Programme (unutilised); and National Grid Gas plc and National Grid Gas Holdings plc had a joint Euro Medium Term Note Programme of €10 billion (€5.9 billion unissued).

At 31 March 2007, the National Grid Gas plc had £840 million of long term committed facilities (undrawn) and around £840 million of uncommitted borrowing facilities (undrawn).

In addition to the above facilities, National Grid Gas plc signed a loan agreement in 2006/07 for £370m with the European Investment Bank. At 31 March 2007, £190m of this remained to be drawn and this remaining £190m was drawn in May 2007.

Regulatory restrictions

As part of National Grid Gas's regulatory arrangements, its operations are subject to a number of restrictions on the way it can operate. These include a regulatory 'ring-fence' that require it to maintain adequate financial resources and restricts its ability to transfer funds or levy charges between itself and other companies in the National Grid group of companies.

Treasury policy

The funding and treasury risk management for National Grid Gas is carried out on its behalf by a central department operating under policies and guidelines approved by the Board of National Grid plc. The Finance Committee, a committee of the Board of National Grid plc, is responsible for regular review and monitoring of treasury activity and for approval of specific transactions, the authority for which may be delegated. National Grid plc has a Treasury function that raises funding and manages interest rate and foreign exchange rate risk for National Grid Gas.

There is a separate financing programme for National Grid Gas. The Finance Committees of both National Grid plc and of National Grid Gas approve all funding programmes.

The Treasury function 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 use of derivative financial instruments is controlled by policy guidelines set by the Board of National Grid plc. Derivatives entered into in respect of gas commodities are used in support of the business' operational requirements and the policy regarding their use is explained below.

Borrowings outstanding at 31 March 2007 and allocated to the gas distribution and metering businesses amounting to £3,700 million (31 March 2006: £2,605 million). The table in note 22 shows the expected maturity of these borrowings.

Appropriate committed facilities are in place, such that management believes that the maturing amounts in respect of its contractual obligations, as shown in ‘Commitments and Contingencies’, can be met from these facilities, operating cash flows and other refinancings that can reasonably be expected to be able to secure in the future. National Grid Gas’s financial position and expected future operating cash flows are such that it can borrow on the wholesale capital and money markets and most of its borrowings are through public bonds and commercial paper.

Surplus funds are placed on the money markets, usually in the form of short-term fixed deposits that are invested with approved banks and counterparties. Details relating to cash, short-term investments and other financial assets at 31 March 2007 are shown in notes 16 and 21 to the regulatory accounting statements.

As of 31 March 2007, the long-term senior unsecured debt and short-term debt credit ratings respectively provided by Moody’s, Standard & Poor’s (S&P) and Fitch were as follows:

Moody’s	A2/P1
Standard & Poor’s (S&P)	A/A1
Fitch	A+/F1

In connection with the proposed acquisition of KeySpan Corporation by National Grid, National Grid Gas’s ratings have been moved to ‘creditwatch with negative implications’ by S&P. Moody’s have placed National Grid Gas’s ratings on ‘review for downgrade’ and Fitch have placed its ratings on ‘rating watch negative’.

It is a condition of the regulatory ring-fence around National Grid Gas plc that it uses reasonable endeavours to maintain an investment grade credit rating. At these ratings, it should have good access to the capital and money markets for future funding when necessary.

The main risks arising from National Grid Gas’s financial activities are set out below, as are the policies for managing these risks, which are agreed and reviewed by the Board of National Grid plc and the Finance Committee of that Board.

Refinancing risk management

The Board of National Grid plc controls refinancing risk mainly by limiting the amount of financing obligations (both principal and interest) arising on borrowings in any financial year. This policy is intended to prevent National Grid and its subsidiaries from having an excessively large amount of debt to refinance in a given time-frame.

Interest rate risk management

Interest rate exposure arising from borrowings and deposits is managed by the use of fixed and floating rate debt, interest rate swaps, swaptions and forward rate agreements. The interest rate risk management policy is to seek to minimise total financing costs (being interest costs and changes in the market value of debt) subject to constraints 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 National Grid Gas’s bonds in issue are index-linked, that is their cost is linked to changes in the UK Retail Prices Index (RPI). Management believe that these bonds provide a good hedge for revenues and National Grid Gas’s regulatory asset values that are also RPI-linked under its price control formulae.

The performance of the Treasury function in interest rate risk management is measured by comparing the actual total financing costs of our debt with those of a passively-managed benchmark portfolio. More information on the interest rate profile of debt is included in note 18 to the regulatory accounting statements.

Foreign exchange risk management

National Grid Gas a policy of hedging certain contractually committed foreign exchange transactions over a prescribed minimum size. This covers a minimum of 75% of such transactions expected to occur up to six months in advance and a minimum of 50% of transactions six to twelve months in advance. Cover generally takes the form of forward sale or purchase of foreign currencies and must always relate to underlying operational cash flows.

Counterparty risk management

Counterparty risk arises from the investment of surplus funds and from the use of derivative instruments. The Finance Committee of National Grid plc has agreed a policy for managing such risk, which is controlled through credit limits, approvals and monitoring procedures. Where multiple transactions are entered into with a single counterparty, a master netting arrangement can be put in place to reduce our exposure to credit risk of that counterparty. At the present time, we use standard International Swap Dealers Association (ISDA) documentation, which provides for netting in respect of all transactions governed by a specific ISDA agreement with a counterparty, when transacting interest rate and exchange rate derivatives.

Derivative financial instruments held for purposes other than trading

As part of its business operations, National Grid Gas is exposed to risks arising from fluctuations in interest rates and exchange rates. Financial instruments are used, including derivatives, to manage exposures of this type and they are a useful tool in reducing risk. National Grid Gas’s policy is not to use derivatives for trading purposes. Derivative transactions can, to varying degrees, carry both counterparty and market risk.

National Grid Gas 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, it enters into bought and written option contracts on interest rate swaps. These contracts are known as swaptions. National Grid Gas 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.

National Grid Gas 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, starting at a future specified date.

More details on derivative financial instruments are provided in note 17 to the regulatory accounting statements.

Valuation and sensitivity analysis

The fair value of debt and derivative instruments are calculated by discounting all future cash flows by the market yield curve at the balance sheet date. The market yield curve for each currency is obtained from external sources for interest and foreign exchange rates. In the case of instruments that include options, the Black's variation of the Black-Scholes model is used to calculate fair value.

The valuation techniques described above for interest rate swaps and currency swaps are a standard market methodology. These techniques do not take account of the credit quality of either party, but this is not considered to be a significant factor, unless there is a material deterioration in the credit quality of either party.

In relation to swaptions, these are only used for hedging purposes with a European style exercise. As a consequence, the Black's variation of the Black-Scholes model is considered to be sufficiently accurate for the purpose of providing fair value information in relation to these types of swaptions. More sophisticated valuation models exist but National Grid Gas does not believe it is necessary to employ these models, given the extent of its activities in this area.

For debt and derivative instruments held, National Grid Gas utilises a sensitivity analysis technique to evaluate the effect that changes in relevant rates or prices will have on the market value of such instruments.

Details of the sensitivity of the income statement and equity to changes in the UK Retail Prices Index and UK interest rates are set out in note 18(d) to the regulatory accounting statements. Under the assumptions set out in note 18(d), a 0.50% change in the UK Retail Prices Index would affect the income statement by £5 million, but would have no effect on equity, while a 0.50% change in UK interest rates would affect the income statement by £7 million and equity by £10 million.

Commodity contracts

Commodity derivatives

In the normal course of business, the DNs are party to commodity derivatives. These have included gas futures, gas options and gas forwards that are used to manage commodity prices associated with their gas delivery operations.

These financial exposures are monitored and managed as an integral part of National Grid Gas's financial risk management policy. At the core of this policy is a condition that it will engage in activities at risk only to the extent that those activities fall within commodities and financial markets to which it has a physical market exposure, in terms and volumes consistent with its core business. National Grid Gas does not issue, or intend to hold, derivative instruments for trading purposes, and holds such instruments consistent with its various licence and regulatory obligations.

Commitments and contingencies

Commitments and contingencies outstanding at 31 March in respect of the gas distribution and metering businesses are summarised in the table below:

	2007 **£m**	2006 £m
Future capital expenditure contracted but not provided for	**272**	213
Total operating lease commitments	**39**	80

In addition, National Grid Gas has other commitments at 31 March 2007 of £213 million (2006: £154 million) which relate to the company and are not attributable to the regulatory businesses.

Information regarding obligations under pension and other post-retirement benefits is given below under the heading 'Retirement arrangements'.

National Grid Gas proposes to meet all of its commitments from operating cash flows, existing credit facilities, future facilities and other financing that it reasonably expects to be able to secure in the future.

Retirement arrangements

The substantial majority of employees of the gas distribution and metering businesses are members of the National Grid UK Pension Scheme (the 'Scheme') which is operated by Lattice Group plc, an intermediate holding company of National Grid Gas.

The Scheme has both a defined benefit section, which is closed to new entrants, and a defined contribution section, which is offered to all new employees.

As there is no contractual arrangement or stated policy for charging the net defined benefit cost of the scheme to National Grid Gas, it accounts for the Scheme as if it were a defined contribution scheme and does not recognise any share of the assets and liabilities of the Scheme.

The last completed full actuarial valuation of the Scheme was as at 31 March 2006. This concluded that the pre-tax deficit was £371 million (£260 million net of tax) in the defined benefit section on the basis of the funding assumptions adopted by the actuary.

It has been agreed that no funding of the deficit identified in the March 2006 valuation will need to be provided to the Scheme until the outcome of the interim actuarial assessment at 31 March 2007 is known. At this point, National Grid will pay the gross amount of any deficit up to a maximum amount of £520 million (£364 million net of tax) into the scheme. Until the 31 March 2007 actuarial valuation has been completed, National Grid has arranged for banks to provide the trustees of the 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 Gas becoming insolvent or National Grid failing to make agreed payments into the fund. Employer cash contributions for the ongoing cost of the Scheme, including administrative expenses, are currently being made at a rate of 32.7% of pensionable payroll.

National Grid Gas does not provide post-retirement benefits other than pensions.

Related party transactions

National Grid Gas provides services to and receives services from related parties. In the year ended 31 March 2007, the gas distribution and metering businesses charged £23 million and received charges of £153 million from National Grid Gas's related parties (other than Directors and key managers), compared with £23 million and £165 million respectively in 2005/06.

Further information relating to related party transactions is contained within note 28 to the regulatory accounting statements. Details of key management compensation are included within note 6(c) to the regulatory accounting statements.

Accounting policies

Basis of accounting

The regulatory accounting statements present the results for the years ended 31 March 2007 and 2006 and the financial position as at 31 March 2007 and 2006 of the regulatory businesses therein. They have been prepared using the accounting policies shown, in accordance with International Financial Reporting Standards (IFRS), as adopted by the European Union.

Choices permitted under IFRS

Since 1 April 2005, National Grid Gas has presented its regulatory accounting statements in accordance with IFRS. It was required to make a number of choices on the adoption of IFRS and in addition it continues to choose from certain options that are available within accounting standards.

The principal choices made on the adoption of IFRS, which cannot be changed, were as follows:

Option	Choice adopted
Transition date	The opening IFRS balance sheets were established as at 1 April 2004. Certain balances in National Grid Gas's previous UK GAAP regulatory accounting statements were used as the basis for its opening IFRS balance sheets.
Business combinations	Business combinations prior to 1 April 2004 were not changed retrospectively.
Financial instruments	National Grid Gas adopted IAS 39 on 1 April 2005. As a consequence the opening balances at 1 April 2005 are presented using different accounting policies for financial instruments from those used for 2005/06 and 2006/07.
Carrying value of assets at transition	In most cases National Grid Gas used brought forward depreciated cost, as adjusted for changes in accounting policies to conform to IFRS, to be the opening carrying value under IFRS.
Share-based payments	National Grid Gas recognised all active grants retrospectively.
Cumulative translation differences	National Grid Gas chose to present cumulative translation differences arising since 1 April 2004 only.

Significant choices that National Grid Gas continues to make on an ongoing basis include the following:

Option	Choice adopted
Presentation formats	National Grid Gas uses the nature of expense method for income statements and totals its balance sheets to net assets and total equity. In the income statement, National Grid Gas presents subtotals of total operating profit, profit before tax and profit from continuing operations, together with additional subtotals excluding exceptional items and remeasurements. Exceptional items and remeasurements are presented on the face of the income statement.
Pensions	National Grid Gas recognises transactions with the defined benefits section of the National Grid UK Pension Scheme as if it were a defined contribution scheme, and does not recognise any of the scheme assets and liabilities or actuarial gains and losses.
Capitalised interest	Interest is capitalised into the cost of assets that National Grid Gas constructs.
Capital contributions	Contributions received towards capital expenditure are recorded as deferred income and amortised in line with the depreciation on the associated asset.
Financial instruments	National Grid Gas normally opts to apply hedge accounting in most circumstances where this is permitted.

Segmental reporting

As the results, assets and liabilities of the gas distribution and metering businesses are reported separately in these regulatory accounting statements for each regulatory business, no further segmental reporting is provided.

Critical accounting policies

The application of accounting principles requires National Grid Gas to make estimates, judgments and assumptions that may affect the reported amounts of assets, liabilities, revenue and expenses and the disclosure of contingent assets and liabilities in the accounts. On an ongoing basis, estimates are evaluated using historical experience, consultation with experts and other methods that are considered reasonable in the particular circumstances to ensure compliance with IFRS. Actual results may differ significantly from these estimates, the effect of which is recognised in the period in which the facts that give rise to the revision become known.

Certain accounting policies have been identified as critical accounting policies, as these policies involve particularly complex or subjective decisions or assessments. The discussion of critical accounting policies below should be read in conjunction with the description of the accounting policies set out in these regulatory accounting statements.

National Grid Gas's critical accounting policies and accounting treatments for the gas distribution and metering businesses are considered to be:

Attribution of revenues, costs, assets, liabilities and equity to regulatory businesses	Many of the amounts reported in these regulatory accounting statements include or comprise amounts which are not directly attributable to the regulatory businesses concerned and which have been apportioned between the regulatory businesses. Significant judgement is exercised in determining those bases of apportionment. Where there is no reasonable basis of apportionment, arbitrary bases have been adopted. Amounts determined by apportionment within these regulatory accounting statements comprise net costs of £514 million included in the income statements (2006: £414 million), assets of £4,784 million (2006: £4,779 million) and liabilities of £5,574 million (2006: £4,346 million).
Estimated asset economic lives	The reported amounts for amortisation of intangible fixed assets and depreciation of property, plant and equipment can be materially affected by the judgments exercised in determining their estimated economic lives. Intangible asset amortisation and depreciation of property, plant and equipment amounted to £2 million and £301 million respectively in 2006/07 and £11 million and £286 million respectively in 2005/06.
Carrying value of assets and potential for impairment	The carrying value of assets recorded in the balance sheets could be materially reduced if an impairment were to be assessed as being required. Total assets at 31 March 2007 were £10,692 million, including £6,011 million of property, plant and equipment, £19 million of other intangible assets and £4,025 million owed by National Grid Gas's immediate parent undertaking. Impairment reviews are carried out either when a change in circumstance is identified that indicates an asset might be impaired. An impairment review involves calculating either or both of the fair value or the value-in-use of an asset or group of assets and comparing with the carrying value in the balance sheet. These calculations involve the use of assumptions as to the price that could be obtained for, or the future cash flows that will be generated by, an asset or group of assets, together with an appropriate discount rate to apply to those cash flows.
Revenue accruals	Revenue includes an assessment of transportation services supplied to customers between the date of the last meter reading and the year end. Changes to the estimate of the transportation services supplied during this period would have an impact on the reported results of National Grid Gas. Estimates of unbilled revenues amounted to £88 million at 31 March 2007 compared with £92 million at 31 March 2006.

Assets and liabilities carried at fair value	Certain assets and liabilities, principally financial investments and derivative financial instruments, are carried in the balance sheet at their fair value rather than historical cost. The fair value of financial investments is based on market prices, as are those of derivative financial instruments where market prices exist. Other derivative financial instruments are valued using financial models, which include judgments on, in particular, future movements in exchange and interest rates as well as equity prices.
Hedge accounting	National Grid Gas uses derivative financial instruments to hedge certain economic exposures arising from movements in exchange and interest rates or other factors that could affect either the value of National Grid Gas's assets or liabilities or affect future cash flows. Movements in the fair values of derivative financial instruments may be accounted for using hedge accounting where National Grid Gas meet the relevant eligibility, documentation and effectiveness testing requirements. If a hedge does not meet the strict criteria for hedge accounting, or where there is ineffectiveness or partial ineffectiveness, then the movements will be recorded in the income statement immediately instead of being recognised in the Statement of Recognised Income and Expense or by being offset by adjustments to the carrying value of debt.
Pensions	Defined benefit pension obligations are accounted for as if the Scheme were a defined contribution scheme. This accounting treatment is based on there not being any contractual arrangements or a stated policy under which the National Grid Gas is charged for the costs of providing pensions. A change in these arrangements may lead to National Grid Gas recognising the cost of providing pensions on a different basis, together with a proportion of the actuarial gains and losses and of the assets and liabilities of the pension scheme.
Exceptional items and remeasurements	Exceptional items and remeasurements are items of income and expenditure that, in the judgment of management, should be disclosed separately on the basis that they are material, either by their nature or their size, to an understanding of financial performance between periods. Items of income or expense that are considered by management for designation as exceptional items include such items as significant restructurings, write-downs or impairments of non-current assets, material changes in environmental provisions, gains or losses on disposals of businesses or investments. Remeasurements comprise gains or losses recorded in the income statement arising from changes in the fair value of derivative financial instruments. These fair values increase or decrease as a consequence of changes in financial indices and prices over which National Grid Gas has no control.
Provisions	Provision is made for liabilities that are uncertain in estimates. These include provisions for the cost of environmental restoration and remediation, restructuring and employer and public liability claims. Calculations of these provisions are based on estimated cash flows relating to these costs, discounted at an appropriate rate where the impact of discounting is material. The total costs and timing of cash flows relating to environmental liabilities are based on management estimates supported by the use of external consultants. At 31 March 2007, recorded provisions totalled £77 million (2006: £74 million), including £44 million (2006: £44 million) in respect of environmental liabilities.
Tax estimates	National Grid Gas's tax charge is based on the profit for the year and tax rates in effect. The determination of appropriate provisions for taxation requires National Grid Gas to take into account anticipated decisions of tax authorities and estimate National Grid Gas's ability to utilise tax benefits through future earnings and tax planning. National Grid Gas's estimates and assumptions may differ from future events.

In order to illustrate the impact that changes in assumptions could have on reported results and financial position, the following sensitivities are presented:

Asset economic lives	An increase in the useful economic lives of assets of one year on average would reduce the annual depreciation charge on property, plant and equipment by £10 million, but would have a negligible effect on the annual amortisation charge on intangible assets.
Revenue accruals	A 10% change in the estimate of unbilled revenues at 31 March 2007 would result in an increase or decrease in recorded net assets and profit for the year of approximately £6 million net of tax.
Assets carried at fair value	A 10% change in assets and liabilities carried at fair value would result in an increase or decrease in the carrying value of derivative financial instruments of £1 million.
Hedge accounting	If the gains and losses arising on derivative financial instruments during the year ended 31 March 2007 had not achieved hedge accounting then the profit for the year would have been £28 million lower than that reported net of tax and net assets would have been £28 million higher.
Provisions	A 10% change in the estimates of future cash flows estimated in respect of provisions for liabilities would result in an increase or decrease in net assets of approximately £8 million.

Accounting developments

New IFRS accounting standards and interpretations adopted in 2006/07

In preparing these regulatory accounting statements, National Grid Gas has complied with International Financial Reporting Standards, International Accounting Standards and interpretations applicable for periods beginning on or after 1 April 2006. The following amendments to standards and interpretations were adopted during 2006/07, none of which resulted in a material change to National Grid Gas's consolidated results, assets or liabilities in 2006/07 or in those of previous periods.

Leases	International Financial Reporting Interpretations Committee (IFRIC) 4 on leases provides guidance on determining when other forms of contractual arrangements should also be accounted for as leases.
Financial instruments	Amendments to IAS 39, IFRS 4, and IAS 21 allow for financial liabilities to be designated as fair value through profit and loss in certain circumstances, for certain financial guarantees to be recorded in the balance sheet at their fair value and permitted inter-company exchange gains and losses to be taken to equity reserves on consolidation in certain circumstances.
Other interpretations	IFRIC 5, IFRIC 6 and IFRIC 7 contain guidance on accounting for decommissioning, restoration and environmental funds, for waste electrical and electronic equipment and for subsidiaries in hyperinflationary economies.

Forthcoming changes in IFRS

The following accounting standards and interpretations have not yet been adopted, but are expected to be adopted in future periods.

Segment reporting	IFRS 8 on segment reporting changes the requirements for segmental reporting. Assuming that it is adopted by European Union, it will apply with effect from 1 April 2009. If IFRS 8 had been adopted in 2006/07, there would have been no change in business segments reported.
Service concessions	IFRIC 12 on service concessions, effective from 1 April 2008, requires assets operated on behalf of a public authority as a concession, where the asset reverts back to the public authority at the conclusion of the arrangement, to be recognised as a financial or intangible asset, depending on whether income is recovered from the public authority or from users. This is not expected to affect the majority of National Grid Gas's assets and liabilities. However, a full assessment of this interpretation has not yet been completed, so it is possible that there may be an impact on assets and liabilities as a consequence of the adoption of this interpretation.
Borrowing costs	An amendment of IAS 23 on borrowing costs will require interest to be capitalised into the cost of assets National Grid Gas constructs. It already adopts this policy and so this will have no impact.
Other interpretations	IFRIC 8, IFRIC 9, IFRIC 10 and IFRIC 11 contain guidance on accounting for share-based exchange transactions, embedded derivatives, impairments in half yearly reports and share-based payments. These interpretations are not expected to have a material impact on National Grid Gas's results, assets or liabilities.

Corporate governance

As a part of the National Grid group of companies, National Grid Gas does not have a separate corporate governance process, but instead is subject to National Grid's corporate governance policies, which are described on pages 77 to 85 of the National Grid plc Annual Report and Accounts 2006/07.

National Grid's corporate governance policies comply with best practice for a company quoted on the London and New York Stock exchanges and include:

- published governance policies;
- independent Non-executive Directors for National Grid plc;
- a rigorous succession process for Executive Directors of National Grid plc;
- appropriate training for Directors;
- monitoring of the performance of the Board of National Grid plc;
- separation of the roles of Chairman and Chief Executive of National Grid plc;
- appointment of a Senior Independent Director;
- clear definition of the role and responsibilities of the Board of National Grid plc, including the establishment of an Executive Committee and a Finance Committee;
- independent Audit, Nominations, Remuneration, and Risk & Responsibility Committees comprised of Non-executive Directors; and
- a group-wide risk management process. Details of National Grid Gas's risk management process are provided on page 11.

Board of National Grid

The Board of National Grid plc has delegated responsibility for the operational management of the businesses of National Grid to executive committees, composed of members of the Board of National Grid and directors of the businesses. Responsibility for the operational management of the gas distribution businesses has been delegated to the Distribution Executive Committee.

Responsibility for treasury activities in respect of National Grid Gas is retained by the Finance Committee of National Grid and a detailed description of treasury policy is provided on page 23.

Matters reserved for the Board of National Grid include:

- corporate governance including establishment of executive committees, internal control arrangements, National Grid Code of Business Practice, delegations of authority, and public position statements and codes;
- approval of financial policy, material changes to accounting policies, the budget and business plan for National Grid and the business strategy of National Grid;
- funding and managerial arrangements for pension schemes; and
- appointment of auditors.

Board of National Grid Gas

The Board of National Grid Gas plc is responsible for ensuring that all the businesses of National Grid Gas comply with all relevant laws and regulations, including compliance with the Gas Transporter Licences and with the business separation requirements of Special Condition C20 of the NTS Gas Transporter Licence. These business separation requirements are discussed in more detail below.

The Board of National Grid Gas is responsible for appointing the members of the Distribution Executive Committee.

Distribution Executive Committee

The Distribution Executive Committee acts within National Grid's overall corporate governance framework and delegated authorities and is responsible for the operational and financial management of the distribution businesses and achieving performance targets set by the Board of National Grid.

The Distribution Executive Committee meets on a monthly basis and its membership comprises:

Mark Fairbairn (Chair)	Executive Director of National Grid
Jeremy Bending	Director, Network Strategy
Jon Butterworth	Director, Operations
Mike Calviou	Director of Distribution Support
Isobel Hoseason	Director of Communications
Alison Kay	UK General Counsel and Company Secretary
Adam Mallalieu	Director of UK Safety, Health, Environment and Security
Peter Massey	Director of Transformation
Rowan Sharples	Director of UK Construction
Paul Whittaker	UK Director of Regulation
Adam Wiltshire	Director of Finance
Nick Worrall	UK HR Director

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

Business separation

Special Condition C20 of National Grid Gas's NTS gas transporter licence requires that National Grid Gas maintains managerial and operational systems such that:

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

National Grid Gas's policy on business separation is set out in its Compliance Statement.

National Grid Gas has taken the following actions to comply with the requirements of Special Condition C20:

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

Directors' report

The information in this Directors' Report does not comprise a Directors' Report within the meaning of the Companies Act 1985. Such a report for National Grid Gas plc is included within that company's annual report and accounts.

Board of Directors

Mark Fairbairn (48)

Appointed to the Board of National Grid Gas plc in June 2003, he is also Executive Director of National Grid plc with responsibility for gas distribution. He joined National Grid in 1989 from BNFL. He was awarded an OBE in 2001 for his services to the electrical industry in respect of his leadership of the fundamental changes implemented for the introduction of the New Electricity Trading Arrangements. As Chief Operating Officer of National Grid Gas plc, he has played a key role in helping to restructure the UK gas distribution market through the gas networks sales and the creation of National Grid's new gas distribution business.

Andy Chapman (50)

Appointed to the Board of National Grid Gas plc in June 2007, he is also Finance Director for National Grid plc's transmission business. Prior to this, he was Financial Controller of the National Grid Electricity Transmission plc, following five years in overseas in joint ventures, where he spent two years as Chief Financial Officer for Intellig Communications in Brazil and three years with the Copperbelt Energy Corporation in Zambia as Finance Director and then Chief Executive Officer. He joined National Grid Electricity Transmission plc in 1992 and is a qualified accountant.

Malcolm Cooper (48)

Appointed to the Board of National Grid Gas plc in June 2007, he is also Tax and Treasury Director of National Grid plc. He joined British Gas plc in 1991, having previously worked for Andersen Consulting and was appointed Director of Corporate Finance in October 1998. He is President and a Fellow of the Association of Corporate Treasurers. He is also a Fellow of the Chartered Association of Certified Accountants.

Paul Whittaker (47)

Appointed to the Board of National Grid Gas plc in June 2007, he is also UK Director of Regulation for National Grid and is responsible for National Grid Gas's relationship with Ofgem. He was previously Head of Strategy for National Grid. He joined British Gas in 1981 and has held a number of commercial and regulatory roles since then.

Adam Wiltshire (41)

Appointed to the Board of National Grid Gas plc in July 2006 as Finance Director, he is responsible for all financial aspects and corporate governance matters within National Grid Gas. A Chartered Accountant, he joined National Grid Gas in 1999 and has held a number of posts in finance.

Nick Winser (46)

Appointed to the Board of National Grid Gas plc in July 2003, he is also Executive Director of National Grid plc responsible for transmission. He was previously Chief Operating Officer of the US transmission business of National Grid Transco plc. He joined National Grid Company plc 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.

During the period since the last regulatory accounting statements the following directors have resigned: Roger Urwin, Chairman, on 31 December 2006, and Steve Holliday, Steve Lucas and Chris Murray on 27 June 2007.

Alison Kay

Company Secretary

Alison Kay was appointed Company Secretary on 21 October 2002. She is also Company Secretary of National Grid Electricity Transmission plc.

Other information

As the gas distribution and metering businesses reported on within these regulatory accounting statements do not comprise a legal entity, the following information is provided for National Grid Gas as a whole.

Principal activities

The principal activities of National Grid Gas plc and its subsidiaries during the year were the transmission and distribution of gas and the provision of gas metering services.

Substantial shareholders

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

Directors' interests

None of the Directors (nor any person connected with them) has a beneficial interest or non-beneficial interest in the share capital of National Grid Gas plc. None of the Directors (nor any person connected with them) holds any interest in any other securities of National Grid Gas plc, including options over National Grid Gas plc's shares.

Directors' remuneration

The following information is taken from the Annual Report and Accounts of National Grid Gas plc and relates to the persons reported as Directors in those financial statements.

The aggregate amount of emoluments paid to Directors in respect of qualifying services to National Grid Gas plc for 2007 was £1,638,436 (2006: £2,490,520). The amount paid in respect of compensation for loss of office in 2007 was £nil (2006: £284,510). Directors' emoluments include amounts in respect of accrued bonus.

Two Directors exercised share options during 2007 (2006: five Directors).

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

As at 31 March 2007, retirement benefits were accruing to six Directors under a defined benefit scheme (2006: seven directors).

The aggregate emoluments for the highest paid Director were £469,743 for 2007 (2006: £572,517); and total accrued annual pension at 31 March 2007 for the highest paid Director was £64,960 (2006: £195,000). The amount of contributions paid in respect of defined contribution pension schemes was £nil (2006: £17,300).

National Grid Gas does not have a Remuneration Committee, National Grid Gas's Directors being remunerated in line with the policy developed by the National Grid plc Remuneration Committee, details of which may be found in that company's annual report and accounts.

Dividends

During the year a final dividend of £1,500 million in respect of the year to 31 March 2006 and an interim dividend of £350 million were paid by National Grid Gas plc (2005: £310 million interim dividend). The Directors have not proposed a final dividend.

Of the dividends paid by National Grid Gas plc during the year, £1,246 million (2006: £203 million) is reported in these regulatory accounting statements.

Donations

Charitable donations of £732,000 were made by National Grid Gas during the year in support of community initiatives and relationships in the UK (2006: £421,000).

No donations were made in the UK and EU for the purposes of the Political Parties, Elections and Referendums Act 2000.

Research and development

Expenditure on research and development by National Grid Gas was £1.5 million during the year (2006: £1.7 million).

Financial instruments

Details on the use of financial instruments and financial risk management are included on pages 23 to 25.

Disabled persons

National Grid Gas 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.

Employee involvement

National Grid Gas, as a part of National Grid, has well established and effective arrangements through electronic mail, intranet and in-house publications (including videos and briefing meetings), at each business location, for communication and consultation with both employees and trade union representatives and for communication of results and significant business issues.

National Grid Gas, as a part of National Grid, recognises the importance of aligning employee and shareholder interests. It is committed to employee share ownership through participation in the National Grid plc Share Incentive Plan and Sharesave scheme.

Policy and practice on payment of creditors

It is National Grid Gas's policy to include in contracts or other agreements, terms of payment with suppliers. Once agreed, it aims to abide by these terms of payment.

The average creditor payment period at 31 March 2007 was 23 days (27 days at 31 March 2006).

Auditors

PricewaterhouseCoopers LLP have indicated their willingness to be re-appointed auditors of National Grid Gas.

Audit information

Having made the requisite enquiries, so far as the Directors in office at the date of the signing of this report are aware, taking into account their periods of office, there is no relevant audit information (as defined by Section 234ZA of the Companies Act 1985) of which National Grid Gas's auditors are unaware, and the Directors have taken all the steps they ought to have taken to make themselves aware of any relevant audit information and to establish that the National Grid Gas's auditors are aware of that information.

Statement of Directors’ responsibilities for preparing regulatory accounting statements

The Directors of National Grid Gas plc are obliged by Standard Special Condition A30 of National Grid Gas’s DN Gas Transporter Licence to prepare regulatory accounting statements for each financial period, which comply with the requirements set out in Standard Special Condition A30, as amended by consents received from Ofgem.

The Directors consider that, in preparing the regulatory accounting statements, National Grid Gas plc 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 preparing the regulatory accounting statements on the going concern basis, unless it is inappropriate to presume that National Grid Gas plc will continue in business. Therefore, the regulatory accounting statements have been prepared on the going concern basis.

The Directors have responsibility for ensuring that National Grid Gas plc and its related undertakings keep accounting records in such a form that the revenues, costs, assets, liabilities, reserves and provisions of, or reasonably attributable to, each of the regulatory businesses are separately identifiable in the books of National Grid Gas and its related undertakings from those of any other business.

The Directors have responsibility for ensuring that the regulatory accounting statements fairly present the financial position, financial performance and cash flows of, or reasonably attributable to, each regulatory business.

The Directors have responsibility to ensure that, so far as is reasonably practicable, the regulatory accounting statements have the same content and format in respect of the businesses to which they relate as the equivalent statutory accounts of National Grid Gas plc and that they comply with all relevant accounting and reporting standards currently in force which have been issued or adopted by the International Accounting Standards Board.

The Directors have responsibility to ensure that the regulatory accounting statements include for each regulatory business and for the regulatory businesses in total, an income statement, a statement of changes in equity and, if appropriate, a statement of recognised income and expense, a balance sheet and a cash flow statement, including notes thereto. The Directors also have responsibility to ensure that the regulatory accounting statements include, for the regulatory businesses in total, a statement of the accounting policies adopted, a corporate governance statement, a directors’ report and an operating and financial review.

The Directors have responsibility to ensure that the regulatory accounting statements include a reconciliation between the regulatory accounting statement and the statutory accounts of National Grid Gas.

The Directors have responsibility to ensure that the regulatory accounting statements show separately and in appropriate detail the amounts of any revenues, costs, assets, liabilities, reserves or provisions that have been charged from or to any non-National Grid Gas business of National Grid, or that have been determined by apportionment, where they relate to goods or services received or supplied for the purposes of the regulatory businesses.

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

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

The Directors confirm that the Audit Committee of National Grid plc continues to review the adequacy of the system of internal financial controls adopted by National Grid Gas.

The Directors are responsible for ensuring that the regulatory accounting statements are published in accordance with the requirements of Amended Standard Condition A30 and where they are published on the Internet, for the maintenance and integrity of the website. Uncertainty regarding legal requirements is compounded, as information published on the Internet is accessible in many countries with different legal requirements relating to the preparation and dissemination of financial statements.

Independent auditors’ report to the Gas and Electricity Markets Authority and the Directors of National Grid Gas plc

We have audited the regulatory accounting statements of National Grid Gas plc (the Company) for the year ended 31 March 2007 on pages 38 to 87 which comprise the accounting policies, income statements, balance sheets, statements of recognised income and expense, cash flow statements and the related notes to the regulatory accounting statements.

This report is made, on terms that have been agreed, solely to the Company and the Gas and Electricity Markets Authority (‘the Authority’) in accordance with Standard Special Condition A30 (‘the Condition’) of the Regulatory Licence granted to the Company, being the Gas Transporter Licence in respect of the Distribution Networks dated 1 May 2005. Our audit work has been undertaken so that we might state to the Company and the Authority those matters we have agreed to state to them in our report, in order to: (a) assist the Company to meet its obligations under the Regulatory Licence to procure such a report; and (b) to facilitate the carrying out by the Authority of its regulatory functions, and for no other purpose. To the fullest extent permitted by law, we do not accept or assume any responsibility or liability in respect of our work to anyone other than those parties whom we have agreed in writing may have the benefit of our work, whom have accepted our engagement terms and to whom we have assumed a duty of care under written arrangements entered into with such parties.

Basis of preparation

The regulatory accounting statements have been prepared under the historical cost convention and in accordance with the Condition and the accounting policies set out on pages 38 to 43.

The regulatory accounting statements are separate from the statutory financial statements of the Company.

Respective responsibilities of the Gas and Electricity Markets Authority, the Directors and Auditors

The nature, form and content of regulatory accounting statements are determined by the Authority. It is not appropriate for the auditors or the directors to assess whether the nature of the information being reported upon is suitable or appropriate for the Authority’s purposes. Accordingly we make no such assessment.

The directors of the Company are responsible for preparing the regulatory accounting statements and for compliance with the Condition, as described on page 35.

Our responsibility is to audit the regulatory accounting statements in accordance with International Standards on Auditing (UK and Ireland) issued by the Auditing Practices Board, except as stated in the ‘Basis of audit opinion’, below and having regard to the guidance contained in Audit 05/03 “Reporting to Regulators of Regulated Entities”.

We report to you our opinion as to whether the regulatory accounting statements have been properly prepared in accordance with the Condition and, in respect of each of its DN businesses, the metering business, the meter reading business, the de-minimis business and the other activities, whether they fairly present the financial position, financial performance and cash flows of, or reasonably attributable to those businesses. We also report to you if the Company has not kept proper accounting records or if we have not received all the information and explanations we require for our audit.

We read the other information contained in the regulatory accounting statements, on which we do not express an audit opinion, and consider the implications for our report if we become aware of any apparent misstatements or material inconsistencies with the regulatory accounting statements. The other information comprises: the Cautionary statements; the Obligation to produce regulatory accounting statements; the Operating and financing review; the Corporate governance statement and the Directors’ report.

Basis of audit opinion

We conducted our audit in accordance with International Standards on Auditing (UK and Ireland) issued by the Auditing Practices Board except as noted below. An audit includes examination, on a test basis, of evidence relevant to the amounts and disclosures in the regulatory accounting statements. It also includes an assessment of the significant estimates and judgements made by the Directors in the preparation of the regulatory accounting statements and of whether the accounting policies are 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 regulatory accounting statements are free from material misstatement, whether caused by fraud or other irregularity or error. However, as the nature, form and content of the regulatory accounting statements are determined by the Authority, we did not evaluate the overall adequacy of the presentation of information, which would have been required if we were to express an audit opinion under International Standards on Auditing (UK and Ireland).

Our opinion on the regulatory accounting statements is separate from our opinion on the statutory financial statements of the Company on which we reported on 4 June 2007, which are prepared for a different purpose. Our audit report in relation to the statutory accounts of the Company (our "Statutory" audit) was made solely to the Company's members, as a body, in accordance with section 235 of the Companies Act 1985. Our Statutory audit work was undertaken so that we might state to the Company's members those matters we are required to state to them in a Statutory auditors' report and for no other purpose. In these circumstances, to the fullest extent permitted by law, we do not accept or assume any responsibility to anyone other than the Company and the Company's members as a body, for our Statutory audit work, for our Statutory audit report, or for the opinions we have formed in respect of that Statutory audit.

The Condition requires the regulatory accounting statements to be drawn up on the basis set out therein, including the separate disclosure of amounts charged to or from other businesses of National Grid plc or determined by apportionment. The Directors of National Grid Gas plc are responsible for determining the bases of charges and apportionments, which requires a number of judgements and assumptions to be made. We do not give an opinion on the appropriateness of the bases of charges and apportionments.

Opinion

In our opinion, on the basis set out above, the regulatory accounting statements fairly present in accordance with the Condition and the accounting policies set out on pages 38 to 43, the assets, liabilities, reserves and provisions of National Grid Gas's DN businesses, metering business, meter reading business, de-minimis activities and other activities at 31 March 2007 and the revenues and costs of its DN businesses, metering business, meter reading business, de-minimis activities and other activities for the year then ended and have been properly prepared in accordance with the Condition and the accounting policies.

PricewaterhouseCoopers LLP
Chartered Accountants and Registered Auditors
Cornwall Court
19 Cornwall Street
Birmingham
B3 2DT

27 July 2007

1. The maintenance and integrity of the Company web site is the responsibility of the Directors and the maintenance and integrity of the Regulator's web site is the responsibility of the Authority; 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 regulatory accounting statements since they were initially presented on the web sites.

2. Legislation in the United Kingdom governing the preparation and dissemination of financial statements and regulatory accounting statements may differ from legislation in other jurisdictions.

Accounting policies

(a) Basis of preparation of regulatory accounting statements

These regulatory accounting statements have been prepared in accordance with International Financial Reporting Standards (IFRS) adopted by the European Union, and Standard Special Condition A30 (the condition) of National Grid Gas plc's DN gas transporter licence issued under the Utilities Act 2000 (the licence). They are prepared on the basis of all IFRSs and Interpretations that are mandatory for periods ending 31 March 2007 and in accordance with applicable United Kingdom law and Article 4 of the IAS regulation. The 2006 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.

These regulatory accounting statements have been prepared on a historical cost basis, except for the revaluation of certain financial instruments from 1 April 2005 onwards, the date of adoption of IAS 32 'Financial Instruments: Presentation and Disclosure' and IAS 39 'Financial Instruments: Recognition and Measurement'.

These regulatory accounting statements are presented in pounds sterling.

The preparation of regulatory accounting statements 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 revenues and expenses during the reporting period. Actual results could differ from these estimates.

Attribution of revenues, costs, assets, liabilities and equity

The condition requires that all the revenues, costs, assets, liabilities and equity of National Grid Gas are attributed to the regulatory businesses reported in the regulatory accounting statements. Those revenues, costs, assets, liabilities and equity which are not directly attributable to specific regulatory businesses have been apportioned between one or more regulatory businesses according to whether they are related items or unrelated items.

Related items

Related items comprise all those revenues, costs, assets and liabilities of National Grid Gas which are not directly attributable to a specific regulatory business, but where there is a reasonable basis for apportioning those revenues, costs, assets or liabilities between the regulatory businesses. These items comprise activities in respect of the DNs carried out on a centralised basis and shared services.

These revenues, costs, assets and liabilities are apportioned between regulatory businesses in accordance with the activities giving rise to the income, costs, assets or liabilities.

Unrelated items

Unrelated items comprise all those revenues, costs, assets, liabilities and equity of National Grid Gas which are not directly attributable to a specific regulatory business, and where there is no reasonable basis for apportioning those revenues, costs, assets, liabilities and equity between the regulatory businesses. These items mainly comprise corporate activities, financial items, taxation, dividends, share capital and reserves.

These revenues, costs, assets, liabilities and equity are apportioned between regulatory businesses using the following arbitrary bases:

- Corporate costs charged to National Grid Gas by National Grid are apportioned between the regulatory businesses using the same metrics as National Grid uses to determine the allocated charge to National Grid Gas. These metrics take into account relative revenue, operating profit, employees and net assets of the regulatory businesses.
- The non-current amount owed by National Grid Gas Holdings plc is apportioned between the regulatory businesses in the ratio of their estimated regulatory values.
- Net debt at 1 April 2005, which comprises borrowings and bank overdrafts, less cash, cash equivalents and financial investments at that date, was apportioned between regulatory businesses in the ratio of estimated regulatory values at that date. No amounts were apportioned to the de-minimis business or to other activities. The amounts at subsequent period ends are determined by separately adjusting these initially apportioned amounts by the cash generated or used by each regulatory business, movements in fair value of net debt allocated to each business and other funding movements. Other funding movements in the year ended 31 March 2006 substantially comprise the movements arising from the sale of four DNs on 1 June 2005, which were apportioned between the regulatory businesses relative to net debt at 1 April 2005. The adjustments to net debt at 1 April 2005 as a consequence of adopting IAS 39 were apportioned between the regulatory businesses relative to net debt at 1 April 2005.
- Interest is apportioned between the regulatory businesses according to the relative level of net debt determined according to the principles set out above.
- Current and deferred taxation are apportioned between the regulatory businesses relative to the results of undertaking notional current and deferred tax computations for each regulatory business. Prior year tax adjustments substantially relating to transactions which occurred prior to 1 April 2005 are apportioned in the ratio of estimated regulatory values at that date. The estimated capital allowances pools at 1 April 2005 were apportioned between the regulatory businesses in the ratio of estimated regulatory values at that date. Current tax liabilities have been apportioned relative to current tax charges and tax paid or recovered is determined by balance.
- Equity dividends primarily funded from profits for the year have been apportioned on the basis of profits for the year. Equity dividends primarily funded from retained earnings have been apportioned on the basis of relative regulatory values.

- The total equity of National Grid Gas at 1 April 2005, comprising called up share capital, share premium account, retained profits and other reserves, was determined as a balancing item at that date. The amounts at subsequent period ends are determined by separately adjusting these initially allocated amounts by the equity movements derived for each regulatory business as a consequence of all other allocations, including transfer to the regulatory businesses of funds received by National Grid Gas from the sale of four DNs on 1 June 2005.

Outer Met Area

A geographical area on the boundary of the East of England DN and the London DN, the Outer Met Area, forms part of the London DN for managerial, operational and cost accounting purposes. For regulatory and income accounting purposes, the Outer Met Area is treated as part of the East of England DN. Accordingly, the relevant operating costs, assets and liabilities are reported in these regulatory accounting statements as part of the East of England DN.

Additions to the gas distribution network for the Outer Met Area are assessed by management based upon project information. Other amounts for the Outer Met Area, comprising transportation business operating costs, the overall balance of property, plant and equipment, other assets and related liabilities are deemed to be 9% of those amounts of London DN.

(b) Basis of consolidation

These regulatory accounting statements consolidate the financial information of the Company and its subsidiaries in respect of the regulatory businesses specified in the condition.

A subsidiary is defined as an entity controlled by the Company. Control is achieved where the Company has the power to govern the financial and operating policies of an entity so as to obtain benefits from its activities.

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

The results of subsidiaries acquired during the year and covered by the accounting requirements of the condition are included in the regulatory accounting statements from the effective date of acquisition. The results of subsidiaries disposed of during the year, or which otherwise cease to be covered by the accounting requirements of the condition, are included in the regulatory accounting statements up to the effective date of disposal, or the date when those accounting requirements cease to apply.

(c) Foreign currencies

Transactions in currencies other than the functional currency of National Grid Gas plc or the subsidiary 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. Other non-monetary assets are not retranslated unless they are carried at fair value.

As set out in note (n) below, as permitted by IFRS 1, prior to 1 April 2005 National Grid Gas plc adopted the prevailing UK GAAP for hedge accounting in its regulatory accounting statements and, consequently, monetary assets and liabilities denominated in foreign currencies were translated at hedged rates instead of closing exchange rates.

Gains and losses arising on retranslation of monetary assets and liabilities are included in the income statement.

On consolidation, the assets and liabilities of overseas financing operations are translated at exchange rates prevailing at the balance sheet date. Income and expense items are translated at the weighted average exchange rates for the period. Exchange differences arising are classified as equity and transferred to the consolidation translation reserve.

(d) Intangible assets other than goodwill

Identifiable intangible assets other than goodwill 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, other than goodwill are amortised on a straight-line basis over their estimated economic useful lives. The principal amortisation periods for categories of intangible assets are:

Amortisation periods	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.

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

Property, plant and equipment include assets in which National Grid Gas'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, or 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 profit and loss account over the estimated economic life of the assets to which they relate.

Depreciation is not provided on freehold land or assets in the course of construction.

Other property, plant and equipment, apart from certain meters, which are depreciated on a sum-of-the-digits basis, 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	Years
Freehold and leasehold buildings	up to 50
Plant and machinery:	
mains, services and regulating equipment	30 to 100
meters and metering equipments	5 to 18
Motor vehicles and office equipment	3 to 10

(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, National Grid Gas 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 cash flows, 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 cash flows have not been adjusted.

Tests for impairment are carried out only if there is some indication that the carrying value of the assets may have been impaired.

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

(g) Taxation

Current tax

Current tax asset 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 tax

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 financial statements and the corresponding tax bases used in the computation of taxable profit. Deferred tax liabilities are generally recognised on all taxable temporary differences and deferred tax assets are recognised to the extent that is probable that taxable profits will be available against which deductible temporary differences can be utilised. Such assets and liabilities are not recognised if the temporary difference arises from the initial recognition (other than a business combination) of assets and liabilities in a transaction that affects neither the accounting profits nor the taxable profits.

Deferred tax liabilities are recognised on 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 when the liability is settled or the asset is realised, based on the tax rates (and tax laws) that have been enacted or substantively enacted by the balance sheet date. Deferred tax is charged or credited to the income statement, except where it relates to items charged or credited directly to equity, in which case the deferred tax is also 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 deferred income tax asset to be recovered. Unrecognised deferred tax assets are reassessed at each balance sheet date and are recognised to the extent that is has become 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 exists to set off current tax assets against current tax liabilities and when they relate to income taxes levied by the same taxation authority and it is intended to settle its current tax asset and liabilities on a net basis.

(h) Inventories

Inventories, which comprise raw materials and consumables, are stated at cost less provision for damage and obsolescence. Cost comprises acquisition cost and those costs that have been incurred in bringing the inventories to their present location and condition.

(i) Environmental costs

Provision is made for environmental costs, based on future estimated expenditures, discounted to present values. Changes in the provision arising from revised estimates or discount rates or changes in the expected timing of expenditures are recognised in the income statement. The unwinding of the discount is included within the income statement as a financing charge.

(j) Revenues

Revenue represent the sales value derived from the distribution of gas, the provision of gas metering services, and the provision of other services to customers during the year, and excludes value added tax and intra-group sales.

Revenue includes an assessment of gas transportation services supplied to customers between the date of the last meter reading and the year end.

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

(k) Pensions

The substantial majority of National Grid Gas employees are members of the defined benefit section of the National Grid UK Pension Scheme. There is no contractual arrangement or stated policy for charging the net defined benefit cost of the scheme to National Grid Gas. Accordingly National Grid Gas accounts for the scheme as if it were a defined contribution scheme. The pension charge for the year represents the contributions payable to the scheme for the period.

A share of the assets and liabilities or the actuarial gains and losses of the Scheme are not recognised in these regulatory accounting statements.

(l) Leases

Rentals under operating leases are charged to the profit and loss account on a straight-line basis over the term of the relevant lease.

(m) 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 consolidated assets of the Company after deducting all of its liabilities and is recorded at the proceeds received, net of direct issue costs.

Trade receivables are initially recognised at fair value and subsequently measured at amortised cost, less any appropriate allowances for estimated irrecoverable amounts. A provision is established for irrecoverable amounts when there is objective evidence that amounts due under the original payment terms will not be collected. Indications that the trade receivable may become irrecoverable would include financial difficulties of the debtor, likelihood of the debtor's insolvency, and default or significant failure of payment.

Loans receivable and other receivables are carried at amortised cost using the effective interest rate 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 this time, the cumulative gain or loss previously recognised in equity is included in the net profit or loss for the period. Investment income on investments classified at fair value through profit and loss and on available-for-sale investments is recognised in the income statement as it accrues.

Interest-bearing loans and overdrafts are recorded at their initial fair value which normally reflects the proceeds received, net of direct issue costs, and subsequently stated at amortised cost, inclusive of accrued interest. Any difference between the proceeds after direct issue costs and the redemption value is recognised in the income statement over the life of the borrowing.

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.

With effect from 1 April 2005, 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 and which 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. 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) are added to their cost. Such additions cease when the assets are substantially ready for their intended use. All other borrowing costs are recognised in the income statement in the period in which they are incurred.

Purchases and sales of financial assets are usually recognised on the trade date, being the date of commitment to purchase or sell the assets.

(n) Hedge accounting and derivative financial instruments

Both derivative financial instruments ('derivatives') and non-derivative financial instruments are entered into in order to manage interest rate, and foreign currency exposures and commodity price risks in respect of expected energy usage. 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 managing the interest, currency or commodity price risks associated with underlying business activities and the financing of those activities.

From 1 April 2005, the accounting policy for hedge accounting is as described below.

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 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 offsetting amount is recorded as an adjustment to the carrying value of the hedged items, with a corresponding entry in the income statement, to the extent that the adjustment to the carrying value 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 the carrying value of the hedged item at the date hedge accounting is discontinued, is amortised to the income statement using the effective interest method.

If a hedged forecast 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 of their host contracts.

Prior to 1 April 2005 and the adoption of IAS 32 and IAS 39, 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. Exchange gains and losses relating to the hedge of the net investment in overseas subsidiaries were recorded directly in equity.

(o) Share-based payments

National Grid issues equity-settled share-based payments to certain employees of National Grid Gas. 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, based on an estimate of shares that will eventually vest, is recognised on a straight-line basis over the vesting period, as an operating cost and an increase in equity. Payments made by National Grid Gas to National Grid in respect of share-based payments are recognised as a reduction in equity.

(p) Business performance, exceptional items and remeasurements

National Grid Gas's financial performance is analysed into two components: business performance, which excludes exceptional items and remeasurements; and exceptional items and remeasurements. Exceptional items and remeasurements are excluded from the measures of business performance used by management to monitor financial performance, as they are considered to distort the comparability of our reported financial performance from year to year. Business performance measures presented on the face of the income statement or in the notes to the regulatory accounting statements include operating profit before exceptional items and remeasurements, profit before tax before exceptional items and remeasurements and profit for the year before exceptional items and remeasurements.

Exceptional items and remeasurements are items of income and expenditure that, in the judgment of management, should be disclosed separately on the basis that they are material, either by their nature or their size, to an understanding of our financial performance between periods. Items of income or expense that are considered by management for designation as exceptional items include such items as significant restructurings, write-downs or impairments of non-current assets, material changes in environmental provisions and gains or losses on disposals of businesses or investments. Remeasurements comprise gains or losses recorded in the income statement arising from changes in the fair value of derivative financial instruments to the extent that hedge accounting is not achieved or is not effective.

(q) Restructuring costs
Costs arising from restructuring programmes primarily relate to redundancy costs. Redundancy costs are charged to the income statement in the year in which an irrevocable commitment is made to incur the costs and the main features of the restructuring plan have been announced to affected employees.

(r) Cash and cash equivalents
Cash and cash equivalents include cash held at bank and in hand, together with short-term highly liquid investments that are readily convertible to known amounts of cash and subject to an insignificant change in value.

(s) Equity
The businesses reported in these regulatory accounting statements do not have their own and separate share capital or reserves. Accordingly, equity is reported only in total for each business.

(t) Dividends
Dividends are recognised in the financial year in which they are approved.

(u) Key sources of estimation uncertainty
The preparation of financial statements requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities, disclosures of contingent assets and liabilities and the reported amounts of revenue and expenses during the reporting period. Actual results could differ from these estimates. Information about such judgements and estimation is contained in the accounting policies and/or the Notes to the Regulatory Accounting Statements, and the key areas are summarised below.

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

- The categorisation of certain items as exceptional and the definition of adjusted earnings – note 5.
- The exemptions adopted under IFRS including, in particular, those relating to business combinations – accounting policies note (a) Basis of preparation of regulatory accounting statements.

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

- Review of residual lives, carrying values and impairment charges for other intangible assets and property, plant and equipment – accounting policies notes (d) intangible assets other than goodwill, (e) Property, plant and equipment and (f) Impairment of assets.
- Valuation of financial instruments and derivatives – notes 17 and 18.
- Revenue recognition and assessment of unbilled revenue – accounting policies note (j) Revenues.
- Recoverability of deferred tax assets – accounting policies note (g) Taxation and note 14.
- Environmental liabilities – note 25.
- Hedge accounting and derivative financial instruments – Accounting Polices (n) Hedge accounting and derivative financial instruments.

Income statements

For the years ended 31 March	Notes	North West DN 2007 £m	East of England DN 2007 £m	West Midlands DN 2007 £m	North London DN 2007 £m	Metering 2007 £m	Meter Reading 2007 £m	De-minimis activities 2007 £m	Other activities 2007 £m	Total 2007 £m	North West DN 2006 £m	East of England DN 2006 £m	West Midlands DN 2006 £m	North London DN 2006 £m	Metering 2006 £m	Meter Reading 2006 £m	De-minimis activities 2006 £m	Other activities 2006 £m	Total 2006 £m
Total revenue		253	421	201	198	318	18	6	57	1,472	252	414	203	234	316	16	4	65	1,504
Less inter-business revenue		-	-	-	-	-	(2)	-	-	(2)	-	-	-	-	-	(2)	-	(5)	(7)
Revenue		253	421	201	198	318	16	6	57	1,470	252	414	203	234	316	14	4	60	1,497
Operating costs	4	(176)	(249)	(126)	(156)	(215)	(14)	(6)	(53)	(995)	(163)	(228)	(115)	(144)	(219)	(10)	(4)	(58)	(941)
Operating profit																			
Before exceptional items		79	175	77	44	103	2	-	4	484	96	195	93	96	97	4	-	2	583
Exceptional items	5	(2)	(3)	(2)	(2)	-	-	-	-	(9)	(7)	(9)	(5)	(6)	-	-	-	-	(27)
Total operating profit		77	172	75	42	103	2	-	4	475	89	186	88	90	97	4	-	2	556
Interest income and similar income	9	2	2	1	1	1	-	-	-	7	10	16	8	9	16	-	-	-	59
Interest expense and other finance costs																			
Before exceptional items and remeasurements	9	(39)	(59)	(29)	(34)	(33)	-	-	(1)	(195)	(30)	(48)	(25)	(28)	(44)	-	-	-	(175)
Exceptional items and remeasurements	9	(4)	(6)	(3)	(4)	(3)	-	-	-	(20)	(1)	(3)	(1)	(2)	(3)	-	-	-	(10)
Profit before taxation																			
Before exceptional items and remeasurements		42	118	49	11	71	2	-	3	296	76	163	76	77	69	4	-	2	467
Exceptional items and remeasurements	5	(6)	(9)	(5)	(6)	(3)	-	-	-	(29)	(8)	(12)	(6)	(8)	(3)	-	-	-	(37)
Total profit before taxation		36	109	44	5	68	2	-	3	267	68	151	70	69	66	4	-	2	430
Taxation																			
Before exceptional items and remeasurements	10	(22)	(52)	(23)	(14)	(27)	(1)	-	(3)	(142)	(14)	(34)	(15)	(14)	(12)	(1)	-	(1)	(91)
Exceptional items and remeasurements	10	1	2	1	1	-	-	-	-	5	2	4	2	2	1	-	-	-	11
Total taxation		(21)	(50)	(22)	(13)	(27)	(1)	-	(3)	(137)	(12)	(30)	(13)	(12)	(11)	(1)	-	(1)	(80)
Profit for the year after taxation																			
Before exceptional items and remeasurements		20	66	26	(3)	44	1	-	-	154	62	129	61	63	57	3	-	1	376
Exceptional items and remeasurements	5	(5)	(7)	(4)	(5)	(3)	-	-	-	(24)	(6)	(8)	(4)	(6)	(2)	-	-	-	(26)
Profit for the year		15	59	22	(8)	41	1	-	-	130	56	121	57	57	55	3	-	1	350

The notes on pages 49 to 87 form part of these regulatory accounting statements.

Balance sheets

At 31 March	Notes	North West DN 2007 £m	East of England DN 2007 £m	West Midlands DN 2007 £m	North London DN 2007 £m	Metering 2007 £m	Meter Reading 2007 £m	De-minimis activities 2007 £m	Other activities 2007 £m	Total 2007 £m	North West DN 2006 £m	East of England DN 2006 £m	West Midlands DN 2006 £m	North London DN 2006 £m	Metering 2006 £m	Meter Reading 2006 £m	De-minimis activities 2006 £m	Other activities 2006 £m	Total 2006 £m
Non-current assets																			
Intangible assets	12	**4**	**6**	**3**	**3**	**1**	**-**	**-**	**2**	**19**	2	2	1	1	1	-	-	-	7
Property, plant and equipment	13	**1,252**	**1,809**	**1,015**	**1,161**	**773**	**-**	**-**	**1**	**6,011**	1,164	1,704	958	1,094	829	-	-	-	5,749
Other receivables	15	**730**	**1,184**	**595**	**657**	**859**	**-**	**-**	**-**	**4,025**	730	1,184	595	657	859	-	-	-	4,025
Derivative financial assets	17	**10**	**15**	**8**	**9**	**8**	**-**	**-**	**-**	**50**	16	25	12	15	15	-	-	-	83
Total non-current assets		**1,996**	**3,014**	**1,621**	**1,830**	**1,641**	**-**	**-**	**3**	**10,105**	1,912	2,915	1,566	1,767	1,704	-	-	-	9,864
Current assets																			
Inventories	19	**3**	**4**	**2**	**2**	**4**	**-**	**-**	**-**	**15**	2	2	1	1	3	-	-	-	9
Trade and other receivables	20	**30**	**54**	**24**	**26**	**63**	**3**	**1**	**4**	**205**	53	87	38	48	95	1	1	13	336
Financial investments	16	**48**	**76**	**38**	**45**	**39**	**-**	**-**	**1**	**247**	6	9	4	5	5	-	-	-	29
Derivative financial assets	17	**2**	**2**	**1**	**1**	**1**	**-**	**-**	**-**	**7**	13	20	10	12	12	-	-	-	67
Cash and cash equivalents	21	**23**	**35**	**17**	**20**	**18**	**-**	**-**	**-**	**113**	30	48	23	27	27	-	-	1	156
Total current assets		**106**	**171**	**82**	**94**	**125**	**3**	**1**	**5**	**587**	104	166	76	93	142	1	1	14	597
Total assets		**2,102**	**3,185**	**1,703**	**1,924**	**1,766**	**3**	**1**	**8**	**10,692**	2,016	3,081	1,642	1,860	1,846	1	1	14	10,461
Current liabilities																			
Bank overdrafts	21	**(1)**	**(1)**	**-**	**(1)**	**(1)**	**-**	**-**	**-**	**(4)**	-	-	-	-	-	-	-	-	-
Borrowings	22	**(245)**	**(375)**	**(185)**	**(221)**	**(193)**	**-**	**-**	**(2)**	**(1,221)**	(140)	(217)	(107)	(123)	(123)	-	-	(3)	(713)
Derivative financial liabilities	17	**(2)**	**(3)**	**(1)**	**(2)**	**(1)**	**-**	**-**	**-**	**(9)**	(6)	(10)	(5)	(6)	(6)	-	-	-	(33)
Trade and other payables	23	**(86)**	**(162)**	**(70)**	**(54)**	**(158)**	**(3)**	**(2)**	**(15)**	**(550)**	(81)	(137)	(52)	(71)	(111)	(1)	(1)	(18)	(472)
Current tax liabilities		**-**	**(5)**	**(1)**	**-**	**(13)**	**-**	**-**	**-**	**(19)**	-	(7)	-	-	(20)	-	-	-	(27)
Provisions	25	**(6)**	**(6)**	**(3)**	**(4)**	**-**	**-**	**-**	**-**	**(19)**	(7)	(8)	(5)	(6)	-	-	-	-	(26)
Total current liabilities		**(340)**	**(552)**	**(260)**	**(282)**	**(366)**	**(3)**	**(2)**	**(17)**	**(1,822)**	(234)	(379)	(169)	(206)	(260)	(1)	(1)	(21)	(1,271)
Non-current liabilities																			
Borrowings	22	**(496)**	**(763)**	**(376)**	**(449)**	**(391)**	**-**	**-**	**(4)**	**(2,479)**	(369)	(574)	(283)	(325)	(332)	-	(1)	(8)	(1,892)
Derivative financial liabilities	17	**(11)**	**(17)**	**(9)**	**(10)**	**(9)**	**-**	**-**	**-**	**(56)**	(8)	(12)	(6)	(7)	(7)	-	-	-	(40)
Other non-current liabilities	24	**(192)**	**(301)**	**(153)**	**(164)**	**(54)**	**-**	**-**	**-**	**(864)**	(182)	(288)	(146)	(150)	(49)	-	-	-	(815)
Deferred tax liabilities	14	**(250)**	**(341)**	**(204)**	**(237)**	**(156)**	**-**	**-**	**(2)**	**(1,190)**	(224)	(310)	(187)	(219)	(182)	-	-	-	(1,122)
Provisions	25	**(21)**	**(14)**	**(7)**	**(16)**	**-**	**-**	**-**	**-**	**(58)**	(19)	(12)	(4)	(13)	-	-	-	-	(48)
Total non-current liabilities		**(970)**	**(1,436)**	**(749)**	**(876)**	**(610)**	**-**	**-**	**(6)**	**(4,647)**	(802)	(1,196)	(626)	(714)	(570)	-	(1)	(8)	(3,917)
Total liabilities		**(1,310)**	**(1,988)**	**(1,009)**	**(1,158)**	**(976)**	**(3)**	**(2)**	**(23)**	**(6,469)**	(1,036)	(1,575)	(795)	(920)	(830)	(1)	(2)	(29)	(5,188)
Net assets/(liabilities)		**792**	**1,197**	**694**	**766**	**790**	**-**	**(1)**	**(15)**	**4,223**	980	1,506	847	940	1,016	-	(1)	(15)	5,273
Total equity	26	**792**	**1,197**	**694**	**766**	**790**	**-**	**(1)**	**(15)**	**4,223**	980	1,506	847	940	1,016	-	(1)	(15)	5,273

These regulatory accounting statements were approved by the Board of National Grid Gas plc on 25 July 2007 and signed on its behalf by:

Mark Fairbairn Director **Nick Winser** Director

Statement of recognised income and expense

For the years ended 31 March	Notes	North West DN 2007 £m	East of England DN 2007 £m	West Midlands DN 2007 £m	North London DN 2007 £m	Metering 2007 £m	Meter Reading 2007 £m	De-minimis activities 2007 £m	Other activities 2007 £m	Total 2007 £m
Net gains/(losses) taken to equity in respect of cash flow hedges		**1**	**1**	**-**	**1**	**1**	**-**	**-**	**-**	**4**
Transferred to profit or loss on cash flow hedges		**2**	**3**	**1**	**1**	**1**	**-**	**-**	**-**	**8**
Tax on items taken directly to or transferred from equity	10	**(1)**	**(1)**	**-**	**(1)**	**(1)**	**-**	**-**	**-**	**(4)**
Net income/(expense) recognised directly in equity		**2**	**3**	**1**	**1**	**1**	**-**	**-**	**-**	**8**
Profit for the year		**15**	**59**	**22**	**(8)**	**41**	**1**	**-**	**-**	**130**
Total recognised income and expense for the year		**17**	**62**	**23**	**(7)**	**42**	**1**	**-**	**-**	**138**
Effect of change in accounting policy – IAS 39(i)		**-**	**-**	**-**	**-**	**-**	**-**	**-**	**-**	**-**

For the years ended 31 March	Notes	North West DN 2006 £m	East of England DN 2006 £m	West Midlands DN 2006 £m	North London DN 2006 £m	Metering 2006 £m	Meter Reading 2006 £m	De-minimis activities 2006 £m	Other activities 2006 £m	Total 2006 £m
Net gains/(losses) taken to equity in respect of cash flow hedges		(1)	(3)	(1)	(2)	(3)	-	-	-	(10)
Transferred to profit or loss on cash flow hedges		(1)	-	-	-	(1)	-	-	-	(2)
Tax on items taken directly to or transferred from equity	10	-	1	-	-	-	-	-	-	1
Net income/(expense) recognised directly in equity		(2)	(2)	(1)	(2)	(4)	-	-	-	(11)
Profit for the year		56	121	57	57	55	3	-	1	350
Total recognised income and expense for the year		54	119	56	55	51	3	-	1	339
Effect of change in accounting policy – IAS 39(i)		(5)	(7)	(4)	(4)	(7)	-	-	-	(27)

(i) IAS 32 ‘Financial Instruments: Disclosure and Presentation’ and IAS 39 ‘Financial Instruments: Recognition and Measurement’ were adopted prospectively with effect from 1 April 2005, in accordance with the transition provisions of IFRS 1.

Cash flow statements

For the years ended 31 March	Notes	North West DN 2007 £m	East of England DN 2007 £m	West Midlands DN 2007 £m	North London DN 2007 £m	Metering 2007 £m	Meter Reading 2007 £m	De-minimis activities 2007 £m	Other activities 2007 £m	Total 2007 £m	North West DN 2006 £m	East of England DN 2006 £m	West Midlands DN 2006 £m	North London DN 2006 £m	Metering 2006 £m	Meter Reading 2006 £m	De-minimis activities 2006 £m	Other activities 2006 £m	Total 2006 £m
Cash flows from operating activities																			
Operating profit		77	172	75	42	103	2	-	4	475	89	186	88	90	97	4	-	2	556
Adjustments for:																			
Exceptional items		2	3	2	2	-	-	-	-	9	7	9	5	6	-	-	-	-	27
Depreciation and amortisation		41	59	31	34	138	-	-	-	303	39	55	25	34	144	-	-	-	297
Profit on disposal of property, plant and equipment		(2)	(1)	(3)	-	(2)	-	-	-	(8)	-	-	-	-	-	-	-	-	-
Share-based payment charge		2	3	1	2	-	-	-	-	8	-	-	-	-	-	-	-	-	-
Changes in working capital		49	65	43	22	38	(1)	1	5	222	(18)	(25)	(16)	(18)	(10)	-	(1)	(11)	(99)
Changes in provisions		4	6	3	4	-	-	-	-	17									
Cash flows relating to exceptional items		(8)	(9)	(4)	(4)	-	-	-	-	(25)	(20)	(17)	(23)	(16)	-	-	-	-	(76)
Cash generated from / (used in) operations		165	298	148	102	277	1	1	9	1,001	97	208	79	96	231	4	(1)	(9)	705
Tax received / (paid)		5	-	-	5	-	-	-	-	10	6	(27)	20	12	(80)	(1)	-	-	(70)
Net cash inflow / (outflow) from operating activities		170	298	148	107	277	1	1	9	1,011	103	181	99	108	151	3	(1)	(9)	635
Cash flows from investing activities																			
Purchases of intangible assets		(3)	(5)	(2)	(2)	-	-	-	(2)	(14)	(1)	-	-	(1)	(1)	-	-	-	(3)
Purchases of property, plant and equipment		(136)	(173)	(93)	(105)	(89)	-	-	(1)	(597)	(118)	(154)	(78)	(105)	(57)	-	-	-	(512)
Disposals of property, plant and equipment		3	1	3	-	2	-	-	-	9	1	1	-	-	-	-	-	-	2
Purchases of financial investments		(42)	(67)	(34)	(40)	(34)	-	-	(1)	(218)	(5)	(7)	(3)	(4)	(4)	-	-	-	(23)
Loan to immediate parent		-	-	-	-	-	-	-	-	-	(496)	(809)	(409)	(449)	(608)	-	-	-	(2,771)
Net cash used in investing activities		(178)	(244)	(126)	(147)	(121)	-	-	(4)	(820)	(619)	(969)	(490)	(559)	(670)	-	-	-	(3,307)
Net cash flow from operating activities less cash used in investing activities		(8)	54	22	(40)	156	1	1	5	191	(516)	(788)	(391)	(451)	(519)	3	(1)	(9)	(2,672)

Cash flow statements (continued)

For the years ended 31 March	Notes	North West DN 2007 £m	East of England DN 2007 £m	West Midlands DN 2007 £m	North London DN 2007 £m	Metering 2007 £m	Meter Reading 2007 £m	De-minimis activities 2007 £m	Other activities 2007 £m	Total 2007 £m	North West DN 2006 £m	East of England DN 2006 £m	West Midlands DN 2006 £m	North London DN 2006 £m	Metering 2006 £m	Meter Reading 2006 £m	De-minimis activities 2006 £m	Other activities 2006 £m	Total 2006 £m
Cash flows from financing activities																			
Net increase/(decrease) in borrowings and derivatives (i)		**257**	**391**	**193**	**248**	**155**	**-**	**(1)**	**(5)**	**1,238**	602	942	467	532	610	(1)	1	11	3,164
Interest received		**2**	**2**	**1**	**1**	**1**	**-**	**-**	**-**	**7**	10	16	8	9	16	-	-	-	59
Interest paid		**(42)**	**(65)**	**(32)**	**(37)**	**(37)**	**-**	**-**	**(1)**	**(214)**	(33)	(53)	(28)	(30)	(49)	-	-	-	(193)
Exceptional finance costs on repayment of debt		**(4)**	**(7)**	**(4)**	**(4)**	**(4)**	**-**	**-**	**-**	**(23)**	-	-	-	-	-	-	-	-	-
Dividends paid to shareholders		**(213)**	**(389)**	**(186)**	**(176)**	**(281)**	**(1)**	**-**	**-**	**(1,246)**	(33)	(70)	(33)	(33)	(31)	(2)	-	(1)	(203)
Net cash (used in) / generated from financing activities		**-**	**(68)**	**(28)**	**32**	**(166)**	**(1)**	**(1)**	**(6)**	**(238)**	546	835	414	478	546	(3)	1	10	2,827
Net (decrease) / increase in cash and cash equivalents		**(8)**	**(14)**	**(6)**	**(8)**	**(10)**	**-**	**-**	**(1)**	**(47)**	30	47	23	27	27	-	-	1	155
Cash and cash equivalents at start of the year		**30**	**48**	**23**	**27**	**27**	**-**	**-**	**1**	**156**	-	1	-	-	-	-	-	-	1
Cash and cash equivalents at end of the year	21	**22**	**34**	**17**	**19**	**17**	**-**	**-**	**-**	**109**	30	48	23	27	27	-	-	1	156

(i) As borrowings and derivatives have been allocated to the businesses as at 31 March, it is not meaningful to further analyse the movements in allocated borrowings and derivatives between proceeds from loans received, repayment of loans and net movements in short-term borrowings and derivatives, as is required by IAS 7. Therefore, only the net movement is presented.

Notes to the regulatory accounting statements

1. Adoption of new accounting standards

New IFRS accounting standards and interpretations adopted in 2006/07

During the year ended 31 March 2007, National Grid Gas has adopted the following amendments to standards and interpretations. None of these had a material impact on consolidated results or assets and liabilities.

- International Financial Reporting Interpretations Committee (IFRIC) 4 'Determining whether an arrangement contains a lease' provides guidance on determining whether arrangements which convey the right to use an asset in return for a series of payments should be accounted for in accordance with IAS 17 'Leases'.
- IFRIC 5 'Rights to Interests arising from Decommissioning, Restoration and Environmental Rehabilitation Funds' addresses the issues of how a contributor to such a fund should account for its interest in the fund and how obligations to make additional contributions should be accounted for.
- IFRIC 6 'Liabilities arising from participating in a specific market – Waste electrical and electronic equipment' relates to the European Union's Directive on waste electrical and electronic equipment, which deals with the responsibility of producers for the backlog of waste for goods sold to private households.
- IFRIC 7 'Applying the restatement approach under IAS 29, Financial reporting in hyperinflationary economies' deals with what is meant by the phrase 'measuring unit current at the balance sheet date' and also with how an entity accounts for opening deferred tax items in its restated financial statements.
- Amendment to IAS 39 'Financial Instruments: Recognition and Measurement: The Fair Value Option' restricts the ability of entities to designate financial assets and liabilities as at fair value through profit or loss to those financial instruments that meet certain specified conditions. Amendment to IAS 39 'Financial Instruments: Recognition and Measurement', and IFRS 4 'Insurance Contracts: Financial Guarantee Contracts' define a financial guarantee contract and specify which accounting standard will apply to such contracts. Generally, financial guarantee contracts are within the scope of IAS 39. However, where the issuer of a financial guarantee contract has previously asserted that it regards such contracts as insurance contracts, then they may elect to apply either IAS 39 or IFRS 4 to those contracts. The Company accounts for such contracts as insurance contracts.
- Amendment to IAS 21 'The Effects of Changes in Foreign Exchange Rates' clarifies the requirements of IAS 21 regarding an entity's investment in foreign operations and, in particular, the treatment of monetary items entered into as net investment hedges.

New IFRS accounting standards and interpretations not yet adopted

National Grid Gas has yet to adopt the following standards and interpretations. These will be adopted on 1 April 2007, but are not expected to have a material impact on consolidated results or assets and liabilities.

- IFRIC 8 'Scope of IFRS 2' addresses the issue of whether IFRS 2 'Share-Based Payment' applies to transactions in which the entity cannot identify specifically some or all of the goods or services received.
- IFRIC 9 'Reassessment of Embedded Derivatives' prohibits reassessment of the treatment of embedded derivatives subsequent to initial recognition unless there is a change in the terms of the contract that significantly modifies the cash flows that otherwise would be required under the contract, in which case reassessment is required.
- IFRIC 10 'Interim financial reporting and impairment' states that any impairment losses on goodwill and certain financial assets recognised in an interim financial statement may not be reversed in subsequent interim or annual financial statements.
- IFRIC 11, 'IFRS 2 – Group and treasury share transactions' provides guidance on whether share-based transactions involving treasury shares or involving subsidiary undertakings (for instance, options over a parent's shares) should be accounted for as equity-settled or cash-settled share-based payment transactions.

New IFRS accounting standards and interpretations not yet endorsed by the EU

- IFRS 8 'Operating segments' sets out the requirements for the disclosure of information about an entity's operating segments and about the entity's products and services, the geographical areas in which it operates and its major customers. IFRS 8 achieves convergence with the US accounting standard, FAS 131 'Disclosures about Segments of an Enterprise and Related Information' with minor differences. If this standard had been implemented in the year ended 31 March 2007, it is not expected that it would have had a material impact on consolidated results or the presentation of those results.
- Amendment to IAS 23 'Borrowing costs' removes the option of immediately recognising as an expense borrowing costs that relate to assets that take a substantial period of time to get ready for use or sale. Implementation of this amendment is not expected to have any impact on consolidated results or consolidated assets and liabilities as National Grid Gas's accounting policy is to capitalise borrowing costs.
- IFRIC 12, 'Service concession arrangements' applies to contractual arrangements whereby a private sector operator participates in the development, financing, operation and maintenance of infrastructure for public sector services, for example, under private finance initiative contracts (PFI) contracts. The impact of this interpretation on consolidated results or consolidated assets and liabilities has not yet been assessed.

2. Reconciliation to the annual report and accounts of National Grid Gas plc

These regulatory accounting statements only comprise certain businesses and activities of National Grid Gas plc. They do not include those businesses and activities which are reported in the NTS regulatory accounting statements or those four DNs which were sold on 1 June 2005. Reconciliations between these regulatory accounting statements and the National Grid Gas plc Annual Report and Accounts 2006/07 are provided below. Copies of the National Grid Gas plc Annual Report and Accounts 2006/07 are available from the Company Secretary, 1-3 Strand, London WC2N 5EH.

	These regulatory accounting statements **2007** **£m**	NTS regulatory accounting statements **2007** **£m**	Sold DNs **2007** **£m**	Inter -business **2007** **£m**	National Grid Gas annual report and accounts **2007** **£m**	These regulatory accounting statements 2006 £m	NTS regulatory accounting statements 2006 £m	Sold DNs 2006 £m	Inter -business 2006 £m	National Grid Gas annual report and accounts 2006 £m
Income statements										
Revenue	**1,472**	**741**	-	**(14)**	**2,199**	1,504	756	-	(16)	2,244
Total operating profit/(loss)	**475**	**303**	**-**	**-**	**778**	556	280	(1)	-	835
Net finance costs	**(208)**	**(63)**	**-**	**-**	**(271)**	(126)	(52)	(31)	-	(209)
Taxation	**(137)**	**(95)**	**-**	**-**	**(232)**	(80)	(56)	-	-	(136)
Profit for the year from discontinued operations	**-**	**-**	**13**	**-**	**13**	-	-	2,494	-	2,494
Profit for the year	**130**	**145**	**13**	**-**	**288**	350	172	2,462	-	2,984
Balance sheets										
Non-current assets	**10,105**	**4,446**	**-**	**-**	**14,551**	9,864	3,931	-	-	13,795
Current assets	**587**	**340**	**-**	**-**	**927**	597	378	44	-	1,019
Total assets	**10,692**	**4,786**	**-**	**-**	**15,478**	10,461	4,309	44	-	14,814
Current liabilities	**(1,822)**	**(1,049)**	**(8)**	**-**	**(2,879)**	(1,271)	(708)	(16)	-	(1,995)
Non-current liabilities	**(4,647)**	**(1,969)**	**(16)**	**-**	**(6,632)**	(3,917)	(1,382)	(14)	-	(5,313)
Total liabilities	**(6,469)**	**(3,018)**	**(24)**	**-**	**(9,511)**	(5,188)	(2,090)	(30)	-	(7,308)
Net assets	**4,223**	**1,768**	**(24)**	**-**	**5,967**	5,273	2,219	14	-	7,506
Called up share capital					**45**					45
Share premium account					**204**					204
Retained earnings					**4,435**					5,985
Cash flow hedge reserve					**(49)**					(60)
Other reserves					**1,332**					1,332
Total shareholders' equity	**4,223**	**1,768**	**(24)**	**-**	**5,967**	5,273	2,219	14	-	7,506
Cash flow statements										
Net cash inflow/(outflow) from operating activities	**1,011**	**406**	**-**	**-**	**1,417**	635	176	(60)	-	751
Net cash (used in)/from investing activities	**(820)**	**(681)**	**28**	**-**	**(1,473)**	(3,307)	(1,317)	6,567	-	1,943
Net cash from/(used in) financing activities	**(238)**	**267**	**(28)**	**-**	**1**	2,827	1,206	(6,508)	-	(2,475)
Net increase/(decrease) in cash and cash equivalents	**(47)**	**(8)**	**-**	**-**	**(55)**	155	65	(1)	-	219
Cash and cash equivalents at start of year	**156**	**67**	**-**	**-**	**223**	1	2	1	-	4
Cash and cash equivalents at end of year	**109**	**59**	**-**	**-**	**168**	156	67	-	-	223

The NTS regulatory accounting statements are published on the Investors pages of the National Grid plc website: www.nationalgrid.com.

2. Reconciliation to the annual report and accounts of National Grid Gas plc (continued)

Sold DNs represent the results, assets and liabilities attributed to the four DNs sold by National Grid Gas on 1 June 2005. Further details of these sales are provided in the National Grid Gas Annual Report and Accounts 2005/06. These sold DNs are not presented as discontinued operations within these regulatory accounting statements, as they each hold their own separate gas transporter licence and are not within the scope of the gas transporter licence under which these regulatory accounting statements are prepared. The regulatory accounting statements for each of these four sold DNs are not prepared by National Grid Gas.

3. Metering business

The following table provides an analysis of the values of metering services provided in the geographical area of each DN owned by National Grid Gas, pursuant to Standard Special Condition A10 of National Grid Gas's gas transporter licences.

	North West DN **2007** **£m**	East of England DN **2007** **£m**	West Midlands DN **2007** **£m**	North London DN **2007** **£m**	Other (i) **2007** **£m**	Total **2007** **£m**	North West DN 2006 £m	East of England DN 2006 £m	West Midlands DN 2006 £m	North London DN 2006 £m	Other (i) 2006 £m	Total 2006 £m
Revenue	**11**	**16**	**9**	**12**	**270**	**318**	10	14	9	9	274	316

(i) Other comprises metering services provided other than in accordance with Standard Special Condition A10 or within the geographical areas of DNs which are not reported within these regulatory accounting statements.

4. Operating costs

	North West DN 2007 £m	East of England DN 2007 £m	West Midlands DN 2007 £m	North London DN 2007 £m	Metering 2007 £m	Meter Reading 2007 £m	De-minimis activities 2007 £m	Other activities 2007 £m	Total 2007 £m	North West DN 2006 £m	East of England DN 2006 £m	West Midlands DN 2006 £m	North London DN 2006 £m	Metering 2006 £m	Meter Reading 2006 £m	De-minimis activities 2006 £m	Other activities 2006 £m	Total 2006 £m
Before exceptional items																		
Depreciation of property, plant and equipment	40	58	31	34	138	-	-	-	301	36	52	24	31	143	-	-	-	286
Amortisation of intangible assets	1	1	-	-	-	-	-	-	2	3	3	1	3	1	-	-	-	11
Payroll costs	39	51	28	38	14	1	1	31	203	39	53	28	35	9	1	1	17	183
Other operating charges:																		
Purchases of gas	9	11	7	6	-	-	-	-	33	11	14	9	8	-	-	-	-	42
Rates	30	59	23	28	-	-	-	-	140	25	49	19	24	-	-	-	-	117
Other operating charges	55	66	35	48	63	13	5	22	307	42	48	29	37	66	9	3	41	275
	174	246	124	154	215	14	6	53	986	156	219	110	138	219	10	4	58	914
Exceptional items																		
Payroll costs	2	2	1	1	-	-	-	-	6	5	7	4	5	-	-	-	-	21
Other operating charges:																		
Other operating charges	-	1	1	1	-	-	-	-	3	2	2	1	1	-	-	-	-	6
	2	3	2	2	-	-	-	-	9	7	9	5	6	-	-	-	-	27
Total																		
Depreciation of property, plant and equipment	40	58	31	34	138	-	-	-	301	36	52	24	31	143	-	-	-	286
Amortisation of intangible assets	1	1	-	-	-	-	-	-	2	3	3	1	3	1	-	-	-	11
Payroll costs (note 6(a))	41	53	29	39	14	1	1	31	209	44	60	32	40	9	1	1	17	204
Other operating charges:																		
Purchases of gas	9	11	7	6	-	-	-	-	33	11	14	9	8	-	-	-	-	42
Rates	30	59	23	28	-	-	-	-	140	25	49	19	24	-	-	-	-	117
Other operating charges	55	67	36	49	63	13	5	22	310	44	50	30	38	66	9	3	41	281
	176	249	126	156	215	14	6	53	995	163	228	115	144	219	10	4	58	941
Operating costs include:																		
Consumption of inventories	1	2	1	1	-	-	-	-	5	2	2	1	1	-	-	2	-	8
Research and development costs	-	-	-	-	-	-	-	-	-	-	1	-	-	-	-	-	-	1
Operating lease rentals:																		
Plant and machinery	1	2	1	1	-	-	-	-	5	2	2	1	1	-	-	-	-	6
Other	2	3	2	2	1	-	-	-	10	2	3	2	2	1	-	-	1	11

Auditor's remuneration for the National Grid Gas and its subsidiaries amounted to £0.4m (2006: £0.5m) for statutory audit services, £0.4m (2006: £0.2m) for other services provided pursuant to legislation (primarily fees for audit reports on regulatory returns and for reports under section 404 of the US Public Company Accounting Reform and Investor Protection Act of 2002 (Sarbanes-Oxley)) and £nil (2006: £0.2m) for tax advisory services.

5. Exceptional items and remeasurements

Exceptional items and remeasurements are items of income and expenditure that, in the judgement of management, should be disclosed separately on the basis that they are material, either by their nature or their size, to an understanding of National Grid Gas's financial performance and significantly distort the comparability of financial performance between periods. Items of income or expense that are considered by management for designation as exceptional items include such items as significant restructurings, write-downs or impairments of non-current assets, material changes in environmental provisions and gains or losses on disposals of businesses or investments. Remeasurements comprise gains or losses recorded in the income statement arising from changes in the fair value of derivative financial instruments to the extent that hedge accounting is not achieved or is not effective.

	North West DN 2007 £m	East of England DN 2007 £m	West Midlands DN 2007 £m	North London DN 2007 £m	Metering 2007 £m	Meter Reading 2007 £m	De-minimis activities 2007 £m	Other activities 2007 £m	Total 2007 £m	North West DN 2006 £m	East of England DN 2006 £m	West Midlands DN 2006 £m	North London DN 2006 £m	Metering 2006 £m	Meter Reading 2006 £m	De-minimis activities 2006 £m	Other activities 2006 £m	Total 2006 £m
Exceptional items																		
Restructuring costs (i)	**2**	**3**	**2**	**2**	**-**	**-**	**-**	**-**	**9**	7	9	5	6	-	-	-	-	27
Total exceptional items included within operating profit	**2**	**3**	**2**	**2**	**-**	**-**	**-**	**-**	**9**	7	9	5	6	-	-	-	-	27
Exceptional finance costs (ii)	**4**	**7**	**4**	**4**	**4**	**-**	**-**	**-**	**23**	-	-	-	-	-	-	-	-	-
Remeasurements – net (gains) / losses on derivative financial instruments (iii)	**-**	**(1)**	**(1)**	**-**	**(1)**	**-**	**-**	**-**	**(3)**	1	3	1	2	3	-	-	-	10
Total exceptional items and remeasurements included within finance costs	**4**	**6**	**3**	**4**	**3**	**-**	**-**	**-**	**20**	1	3	1	2	3	-	-	-	10
Total exceptional items and remeasurements before taxation	**6**	**9**	**5**	**6**	**3**	**-**	**-**	**-**	**29**	8	12	6	8	3	-	-	-	37
Tax on restructuring costs (i)	**(1)**	**(1)**	**(1)**	**-**	**-**	**-**	**-**	**-**	**(3)**	(2)	(3)	(2)	(1)	-	-	-	-	(8)
Tax on exceptional finance costs (ii)	**(1)**	**(2)**	**(1)**	**(2)**	**(1)**	**-**	**-**	**-**	**(7)**	-	-	-	-	-	-	-	-	-
Tax on derivative financial instrument remeasurements (iii)	**1**	**1**	**1**	**1**	**1**	**-**	**-**	**-**	**5**	-	(1)	-	(1)	(1)	-	-	-	(3)
Tax on exceptional items and remeasurements	**(1)**	**(2)**	**(1)**	**(1)**	**-**	**-**	**-**	**-**	**(5)**	(2)	(4)	(2)	(2)	(1)	-	-	-	(11)
Total exceptional items and remeasurements	**5**	**7**	**4**	**5**	**3**	**-**	**-**	**-**	**24**	6	8	4	6	2	-	-	-	26

(i) Restructuring costs relate to planned cost reduction programmes. These included pension curtailment costs arising as a result of redundancies of £3m (2006: £nil).

(ii) Exceptional finance costs represent debt redemption costs related to the restructuring of the debt portfolio.

(iii) Remeasurements – net (gains)/losses on derivative financial instruments comprise non-cash gains and losses arising on derivative financial instruments reported in the income statement. These exclude gains and losses for which hedge accounting has been effective, which have been recognised directly in equity or offset by adjustments to the carrying value of debt. The tax charge includes a £4m charge (2006: £nil) in respect of prior years.

6. Payroll costs and employees

a) Payroll costs

	North West DN 2007 £m	East of England DN 2007 £m	West Midlands DN 2007 £m	North London DN 2007 £m	Metering 2007 £m	Meter Reading 2007 £m	De-minimis activities 2007 £m	Other activities 2007 £m	Total 2007 £m	North West DN 2006 £m	East of England DN 2006 £m	West Midlands DN 2006 £m	North London DN 2006 £m	Metering 2006 £m	Meter Reading 2006 £m	De-minimis activities 2006 £m	Other activities 2006 £m	Total 2006 £m
Wages and salaries	39	53	28	37	10	1	1	23	192	39	56	28	35	7	1	1	14	181
Social security costs	4	4	3	3	1	-	-	2	17	4	5	2	3	1	-	-	1	16
Pension costs	11	14	7	9	3	-	-	6	50	13	16	10	11	1	-	-	2	53
Share-based payments	1	1	1	1	-	-	-	-	4	1	1	1	1	-	-	-	-	4
Severance costs	1	1	1	1	-	-	-	-	4	1	1	1	1	-	-	-	-	4
	56	73	40	51	14	1	1	31	267	58	79	42	51	9	1	1	17	258
Less:																		
Amounts capitalised	(15)	(20)	(11)	(12)	-	-	-	-	(58)	(14)	(19)	(10)	(11)	-	-	-	-	(54)
	41	53	29	39	14	1	1	31	209	44	60	32	40	9	1	1	17	204

b) Average number of employees

	North West DN 2007	East of England DN 2007	West Midlands DN 2007	North London DN 2007	Metering 2007	Meter Reading 2007	De-minimis activities 2007	Other activities 2007	Total 2007	North West DN 2006	East of England DN 2006	West Midlands DN 2006	North London DN 2006	Metering 2006	Meter Reading 2006	De-minimis activities 2006	Other activities 2006	Total 2006
United Kingdom	1,095	1,519	804	1,064	275	23	20	640	5,440	1,229	1,701	881	1,052	228	25	19	431	5,566

Information is not available on the actual number of employees by regulatory business, as many of National Grid Gas's activities are undertaken on a centralised or shared services basis. Therefore, National Grid Gas employee numbers have been apportioned between the different regulatory businesses relative to wages and salaries.

c) Key management compensation

As the amounts are relatively small, key management compensation is only shown for the aggregate of the businesses reported in these regulatory accounting statements.

	Total 2007 £m	Total 2006 unaudited £m
Salaries and short-term employee benefits	2	2
Post-employment benefits	1	1
Share based payments	1	1
	4	4

Key management comprises those Directors on the Board of National Grid Gas plc with a designated responsibility for gas distribution, metering or corporate activities, together with those Executive Directors of National Grid plc who have designated managerial responsibility for National Grid Gas's gas distribution, metering or corporate activities.

6. Payroll costs and employees (continued)

d) Share option and award schemes

National Grid operates three principal forms of share option and award plans in which National Grid Gas's employees and Directors participate. These are an employee Sharesave scheme, a Performance Share Plan and the Deferred Share Plan. In addition, there are two historical plans under which awards are outstanding, but no further awards are being granted. These are the Executive Plan and the Share Matching Plan. Information on these schemes is only available for National Grid Gas as a whole and not in respect of the businesses and activities included in these regulatory accounting statements. The information in respect of National Grid Gas can be found in its annual report and accounts, available from the Company Secretary, 1-3 Strand, London WC2N 5EH.

7. Directors emoluments

The businesses reported in these regulatory accounting statements are not entities with statutory Directors. Accordingly, there are no relevant Directors' emoluments. Details of the emoluments of the Directors of National Grid Gas are provided in the Director's report on page 33.

8. Pensions

Substantially all National Grid Gas's employees are members of the defined benefit section of the National Grid UK Pension Scheme (the 'scheme'). There is no contractual arrangement or stated policy for charging the net defined benefit cost of the scheme to National Grid Gas. Accordingly, National Grid Gas accounts for the scheme as if it were a defined contribution scheme.

The scheme provides final salary defined benefits for employees who joined prior to 31 March 2002 and defined contribution benefits for employees joining from 1 April 2002. The scheme is funded with assets held in a separate trustee administered fund. It is subject to independent actuarial 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 latest full actuarial valuation was carried out by Watson Wyatt LLP at 31 March 2006. The aggregate market value of the scheme's assets was £12,743m and the value of the assets represented approximately 97% of the actuarial value of benefits due to members, calculated on the basis of pensionable earnings and service at 31 March 2006 on an ongoing basis and allowing for projected increases in pensionable earnings. There was a funding deficit of £371m on the valuation date.

The results of the actuarial valuation carried out at 31 March 2006 showed that, based on long-term financial assumptions, the contribution rate required to meet future benefit accrual was 32% of pensionable earnings (29% employers and 3% employees). The ongoing contribution rate does not include an allowance for administration expenses. These contributions are reviewed annually. From 1 April 2007, the rate used for the recovery of administration costs was 3.7% of salary. Employers are currently, therefore, paying a total contribution rate of 32.7%.

In line with the agreement made after the 2003 valuation, no funding of the deficit identified in the 2006 actuarial valuation will need to be provided to the scheme until the outcome of the actuarial assessment at 31 March 2007 is known. At this point, National Grid will pay the gross amount of any deficit up to a maximum amount of £520m (£364m net of tax) into the scheme. Until the 31 March 2007 actuarial valuation has been completed, National Grid has arranged for banks to provide the trustees of the National Grid UK Pension Scheme with letters of credit. The main conditions under which these letters of credit could be drawn relate to events that would imperil the interests of the scheme, such as National Grid Gas plc becoming insolvent or National Grid failing to make agreed payments into the scheme.

The following disclosures relate to the scheme as a whole and include amounts not recognised in these regulatory accounting statements, but which are recognised in the accounts of National Grid plc.

	2007 **£m**	2006 £m
Amounts recognised in the balance sheet of National Grid plc		
Present value of fund obligations	**12,814**	13,246
Fair value of plan assets	**12,865**	12,739
	51	(507)
Present value of unfunded obligations	**(14)**	(21)
Asset/(liability) in the balance sheet	**37**	(528)

8. Pensions (continued)

	2007 £m	2006 £m
Changes in the present value of the defined benefit obligation		
Opening defined benefit obligation	**13,267**	12,662
Current service cost	**64**	69
Interest cost	**636**	655
Actuarial (gains)/losses	**(564)**	1,207
Curtailment gain on redundancies	**(9)**	(23)
Curtailment gain on the sale of DNs	**-**	(168)
Settlement on the sale of DNs	**-**	(589)
Gains on settlement	**-**	(20)
Special termination benefits	**19**	43
Curtailment cost – augmentations	**2**	5
Employee contributions	**7**	8
Benefits paid	**(594)**	(582)
Closing defined benefit obligation	**12,828**	13,267
Changes in the fair value of plan assets		
Opening fair value of plan assets	**12,739**	11,853
Expected return on plan assets	**643**	694
Actuarial gains/(losses)	**(9)**	1,274
Assets distributed on settlements and transfers	**-**	(609)
Employer contributions	**93**	100
Employee contributions	**7**	8
Benefits paid	**(593)**	(581)
Expenses paid	**(15)**	-
Closing fair value of plan assets	**12,865**	12,739
Expected contributions to defined benefit plans in the following year		45

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

	2007 %	2006 %
Equities	**33.2**	38.4
Corporate bonds	**19.8**	20.4
Gilts	**34.9**	31.0
Property	**8.7**	8.6
Other	**3.4**	1.6
Total	**100.0**	100.0

8. Pensions (continued)

The principal assumptions used were:

	2007	2006
	%	%
Discount rate (i)	**5.4**	4.9
Expected return on plan assets	**5.8**	5.8
Rate of increase in salaries	**4.2**	3.9
Rate of increase in pensions in payment and deferred pensions	**3.3**	3.0
Rate of increase in Retail Price Index	**3.4**	2.9

(i) The discount rate for pension liabilities has been determined by reference to appropriate yields prevailing in the UK debt markets at the balance sheet date.
(ii) A promotional age related scale has been used where appropriate.
(iii) The assumptions allow for future improvements in mortality.

The assumed life expectations for a retiree at age 65 are as follows:

	Years
Today:	
Males	20.0
Females	22.3
In 20 years:	
Males	21.2
Females	23.4

Sensitivities at 31 March 2007 – all other assumptions held constant:

- A 0.1% reduction in the discount rate would lead to an increase in the pension and other post-retirement obligation of £200m and an increase in the annual pension cost of £2m.
- A 0.5% increase in the long-term rate of increase in salaries would lead to an increase in the pension and other post-retirement obligation of £78m and an increase in the annual pension cost of £2m.
- An increase of one year to life expectations at age 60 would lead to an increase in the pension and other post-retirement obligation of £403m and to an increase in the annual pension cost of £2m.

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 the 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 target asset allocation for the scheme is 36% equities, 56% bonds and 8% property and other.

9. Finance income and costs

	North West DN 2007 £m	East of England DN 2007 £m	West Midlands DN 2007 £m	North London DN 2007 £m	Metering 2007 £m	Meter Reading 2007 £m	De-minimis activities 2007 £m	Other activities 2007 £m	Total 2007 £m
Interest income on financial instruments	**2**	**2**	**1**	**1**	**1**	**-**	**-**	**-**	**7**
Interest income and similar income	**2**	**2**	**1**	**1**	**1**	**-**	**-**	**-**	**7**
Interest expense on financial liabilities held at amortised cost	**(36)**	**(56)**	**(28)**	**(32)**	**(32)**	**-**	**-**	**(1)**	**(185)**
Exceptional debt redemption costs	**(4)**	**(7)**	**(4)**	**(4)**	**(4)**	**-**	**-**	**-**	**(23)**
Interest on derivatives	**(1)**	**(1)**	**-**	**-**	**(1)**	**-**	**-**	**-**	**(3)**
Other interest	**(1)**	**(2)**	**(1)**	**(2)**	**-**	**-**	**-**	**-**	**(6)**
Unwinding of discount on provisions	**(1)**	**-**	**-**	**-**	**-**	**-**	**-**	**-**	**(1)**
Less: interest capitalised	**-**	**-**	**-**	**-**	**-**	**-**	**-**	**-**	**-**
Interest expense	**(43)**	**(66)**	**(33)**	**(38)**	**(37)**	**-**	**-**	**(1)**	**(218)**
Net gains/(losses) on derivative financial instruments:									
On derivatives designated as fair value hedges	**1**	**2**	**1**	**1**	**1**	**-**	**-**	**-**	**6**
On derivatives designated as cash flow hedges	**-**	**1**	**-**	**-**	**1**	**-**	**-**	**-**	**2**
On derivatives not designated as hedges or ineligible for hedge accounting	**(1)**	**(2)**	**-**	**(1)**	**(1)**	**-**	**-**	**-**	**(5)**
Net gains/(losses) on derivative financial instruments	**-**	**1**	**1**	**-**	**1**	**-**	**-**	**-**	**3**
Interest expense and other finance costs	**(43)**	**(65)**	**(32)**	**(38)**	**(36)**	**-**	**-**	**(1)**	**(215)**
Net finance costs	**(41)**	**(63)**	**(31)**	**(37)**	**(35)**	**-**	**-**	**(1)**	**(208)**
Comprising:									
Interest income and similar income	**2**	**2**	**1**	**1**	**1**	**-**	**-**	**-**	**7**
Interest expense and other finance costs:									
Before exceptional items and remeasurements	**(39)**	**(59)**	**(29)**	**(34)**	**(33)**	**-**	**-**	**(1)**	**(195)**
Exceptional items and remeasurements	**(4)**	**(6)**	**(3)**	**(4)**	**(3)**	**-**	**-**	**-**	**(20)**
	(41)	**(63)**	**(31)**	**(37)**	**(35)**	**-**	**-**	**(1)**	**(208)**

	North West DN 2006 £m	East of England DN 2006 £m	West Midlands DN 2006 £m	North London DN 2006 £m	Metering 2006 £m	Meter Reading 2006 £m	De-minimis activities 2006 £m	Other activities 2006 £m	Total 2006 £m
Interest income on financial instruments	10	16	8	9	16	-	-	-	59
Interest income and similar income	10	16	8	9	16	-	-	-	59
Interest expense on financial liabilities held at amortised cost	(28)	(44)	(23)	(26)	(43)	-	-	-	(164)
Exceptional debt redemption costs	-	-	-	-	-	-	-	-	-
Interest on derivatives	-	(1)	-	-	(1)	-	-	-	(2)
Other interest	(2)	(3)	(2)	(2)	-	-	-	-	(9)
Unwinding of discount on provisions	-	-	-	(1)	-	-	-	-	(1)
Less: interest capitalised	-	-	-	1	-	-	-	-	1
Interest expense	(30)	(48)	(25)	(28)	(44)	-	-	-	(175)
Net gains/(losses) on derivative financial instruments:									
On derivatives designated as fair value hedges	(1)	(3)	(1)	(2)	(3)	-	-	-	(10)
On derivatives designated as cash flow hedges	-	1	-	-	1	-	-	-	2
On derivatives not designated as hedges or ineligible for hedge accounting	-	(1)	-	-	(1)	-	-	-	(2)
Net gains/(losses) on derivative financial instruments	(1)	(3)	(1)	(2)	(3)	-	-	-	(10)
Interest expense and other finance costs	(31)	(51)	(26)	(30)	(47)	-	-	-	(185)
Net finance costs	(21)	(35)	(18)	(21)	(31)	-	-	-	(126)
Comprising:									
Interest income and similar income	10	16	8	9	16	-	-	-	59
Interest expense and other finance costs:									
Before exceptional items and remeasurements	(30)	(48)	(25)	(28)	(44)	-	-	-	(175)
Exceptional items and remeasurements	(1)	(3)	(1)	(2)	(3)	-	-	-	(10)
	(21)	(35)	(18)	(21)	(31)	-	-	-	(126)

9. Finance income and costs (continued)

Interest income on financial instruments comprises interest income from bank deposits and other financial assets.

Interest expense on financial liabilities held at amortised cost comprises interest on bank loans and overdrafts £8m (2006: £10m) and interest on other borrowings £177m (2006: £154m).

Interest on the funding attributable to assets in the course of construction was capitalised during the year at a rate of 5.9% (2006: 6.0%).

Derivative net gains on fair value hedges includes a net loss on the hedging instruments of £22m (2006: £9m net loss) offset by a net gain of £28m (2006: £1m net loss) from the fair value adjustments to the carrying value of debt.

10. Taxation

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

	North West DN 2007 £m	East of England DN 2007 £m	West Midlands DN 2007 £m	North London DN 2007 £m	Metering 2007 £m	Meter Reading 2007 £m	De-minimis activities 2007 £m	Other activities 2007 £m	Total 2007 £m	North West DN 2006 £m	East of England DN 2006 £m	West Midlands DN 2006 £m	North London DN 2006 £m	Metering 2006 £m	Meter Reading 2006 £m	De-minimis activities 2006 £m	Other activities 2006 £m	Total 2006 £m
United Kingdom																		
Corporation tax at 30%	**(15)**	**2**	**(4)**	**(13)**	**37**	**1**	**-**	**1**	**9**	-	19	5	1	35	1	-	1	62
Adjustment in respect of prior years (i)	**9**	**13**	**7**	**8**	**10**	**-**	**-**	**-**	**47**	(4)	(7)	(3)	(4)	(5)	-	-	-	(23)
Deferred tax (ii)	**26**	**33**	**18**	**18**	**(21)**	**-**	**-**	**2**	**76**	16	18	11	15	(19)	-	-	-	41
	20	**48**	**21**	**13**	**26**	**1**	**-**	**3**	**132**	12	30	13	12	11	1	-	1	80
Overseas																		
Corporate tax (iii)	**1**	**1**	**1**	**-**	**1**	**-**	**-**	**-**	**4**	-	-	-	-	-	-	-	-	-
Adjustment in respect of prior years	**-**	**1**	**-**	**-**	**-**	**-**	**-**	**-**	**1**	-	-	-	-	-	-	-	-	-
	1	**2**	**1**	**-**	**1**	**-**	**-**	**-**	**5**	-	-	-	-	-	-	-	-	-
Taxation	**21**	**50**	**22**	**13**	**27**	**1**	**-**	**3**	**137**	12	30	13	12	11	1	-	1	80
Comprising:																		
Taxation – excluding exceptional items and remeasurements	**22**	**52**	**23**	**14**	**27**	**1**	**-**	**3**	**142**	14	34	15	14	12	1	-	1	91
Taxation – exceptional items and remeasurements (note 5)	**(1)**	**(2)**	**(1)**	**(1)**	**-**	**-**	**-**	**-**	**(5)**	(2)	(4)	(2)	(2)	(1)	-	-	-	(11)
	21	**50**	**22**	**13**	**27**	**1**	**-**	**3**	**137**	12	30	13	12	11	1	-	1	80

(i) The UK corporation tax charge includes a tax credit of £13m (2006: credit of £6m) which relates to exceptional items and remeasurements.

(ii) The deferred tax charge includes a charge relating to prior years of £nil (2006: deferred tax credit of £7m) before exceptional items and remeasurements and £4m (2006: deferred tax credit of £7m) after exceptional items and remeasurements respectively. The 2006 amount includes a current year credit relating to exceptional items and remeasurements of £4m.

(iii) The overseas corporate tax charge of £4m relates to exceptional items and remeasurements (2006: credit of £1m relating to exceptional items and remeasurements).

10. Taxation (continued)

Taxation on items charged to equity

	North West DN 2007 £m	East of England DN 2007 £m	West Midlands DN 2007 £m	North London DN 2007 £m	Metering 2007 £m	Meter Reading 2007 £m	De-minimis activities 2007 £m	Other activities 2007 £m	Total 2007 £m	North West DN 2006 £m	East of England DN 2006 £m	West Midlands DN 2006 £m	North London DN 2006 £m	Metering 2006 £m	Meter Reading 2006 £m	De-minimis activities 2006 £m	Other activities 2006 £m	Total 2006 £m
Deferred tax charge/(credit) on revaluation of cash flow hedges	1	1	-	1	1	-	-	-	4	-	(1)	-	-	-	-	-	-	(1)
Tax charge/(credit) recognised in the statement of recognised income and expense	1	1	-	1	1	-	-	-	4	-	(1)	-	-	-	-	-	-	(1)
Deferred tax credit on employee share schemes	-	-	-	-	(1)	-	-	-	(1)	(1)	(1)	-	(1)	-	-	-	-	(3)
Corporate tax credit on employee share schemes	-	(1)	-	-	-	-	-	-	(1)	-	-	-	-	-	-	-	-	-
	1	-	-	1	-	-	-	-	2	(1)	(2)	-	(1)	-	-	-	-	(4)

The overall tax charge for the period is higher (2006: lower) than the standard rate of corporation tax in the UK (30%). The differences are explained below:

	North West DN 2007 £m	East of England DN 2007 £m	West Midlands DN 2007 £m	North London DN 2007 £m	Metering 2007 £m	Meter Reading 2007 £m	De-minimis activities 2007 £m	Other activities 2007 £m	Total 2007 £m	North West DN 2006 £m	East of England DN 2006 £m	West Midlands DN 2006 £m	North London DN 2006 £m	Metering 2006 £m	Meter Reading 2006 £m	De-minimis activities 2006 £m	Other activities 2006 £m	Total 2006 £m
Profit before taxation before exceptional items and remeasurements	42	118	49	11	71	2	-	3	296	76	163	76	77	69	4	-	2	467
Multiplied by UK corporation tax rate of 30% (2005: 30%)	13	35	14	3	22	1	-	1	89	23	49	23	23	20	1	-	1	140
Effects of:																		
Adjustments in respect of previous years	9	14	7	8	10	-	-	-	48	(4)	(7)	(3)	(4)	(5)	-	-	-	(23)
Expenses not deductible for tax purposes	-	1	-	-	-	-	-	-	1	1	1	1	1	-	-	-	-	4
Non-taxable income	-	(1)	-	-	(1)	-	-	-	(2)	(1)	(2)	(1)	(1)	(1)	-	-	-	(6)
Impact of employee share schemes	1	1	-	1	-	-	-	1	4	(1)	(1)	-	-	-	-	-	-	(2)
Other	(1)	2	2	2	(4)	-	-	1	2	(4)	(6)	(5)	(5)	(2)	-	-	-	(22)
Total taxation before exceptional items and remeasurements	22	52	23	14	27	1	-	3	142	14	34	15	14	12	1	-	1	91
Effective income tax rate before exceptional items and remeasurements	52%	44%	47%	127%	38%	50%	-	100%	48%	18%	21%	20%	18%	17%	25%	-	50%	19%

10. Taxation (continued)

	North West DN 2007 £m	East of England DN 2007 £m	West Midlands DN 2007 £m	North London DN 2007 £m	Metering 2007 £m	Meter Reading 2007 £m	De-minimis activities 2007 £m	Other activities 2007 £m	Total 2007 £m	North West DN 2006 £m	East of England DN 2006 £m	West Midlands DN 2006 £m	North London DN 2006 £m	Metering 2006 £m	Meter Reading 2006 £m	De-minimis activities 2006 £m	Other activities 2006 £m	Total 2006 £m
Profit before taxation	**36**	**109**	**44**	**5**	**68**	**2**	**-**	**3**	**267**	68	151	70	69	66	4	-	2	430
Multiplied by UK corporation tax rate of 30% (2005: 30%)	**11**	**32**	**13**	**2**	**20**	**1**	**-**	**1**	**80**	20	45	21	21	20	1	-	1	129
Effects of:																		
Adjustments in respect of previous years	**11**	**14**	**7**	**8**	**12**	**-**	**-**	**-**	**52**	(4)	(7)	(3)	(4)	(5)	-	-	-	(23)
Expenses not deductible for tax purposes	**-**	**1**	**-**	**-**	**-**	**-**	**-**	**-**	**1**	1	1	1	1	-	-	-	-	4
Non-taxable income	**(1)**	**(1)**	**-**	**-**	**(1)**	**-**	**-**	**-**	**(3)**	(1)	(2)	(1)	(1)	(1)	-	-	-	(6)
Adjustment in respect of foreign tax rates	**-**	**1**	**-**	**-**	**-**	**-**	**-**	**-**	**1**	-	-	-	-	-	-	-	-	-
Impact of employee share schemes	**1**	**1**	**-**	**1**	**-**	**-**	**-**	**1**	**4**	(1)	(1)	-	-	-	-	-	-	(2)
Other	**(1)**	**2**	**2**	**2**	**(4)**	**-**	**-**	**1**	**2**	(3)	(6)	(5)	(5)	(3)	-	-	-	(22)
Total taxation	**21**	**50**	**22**	**13**	**27**	**1**	**-**	**3**	**137**	12	30	13	12	11	1	-	1	80
Effective income tax rate	**58%**	**46%**	**50%**	**260%**	**40%**	**50%**	**-**	**100%**	**51%**	18%	20%	19%	17%	17%	25%	-	50%	19%

Factors that may affect future tax charges

A number of changes to the UK Corporation tax system were announced in the March 2007 Budget Statement, but had not been substantively enacted at the balance sheet date and, therefore, are not included in these regulatory accounting statements.

The effect of the changes subsequently enacted in the 2007 Finance Act has not yet been fully determined, but is expected to reduce the allocated deferred tax liability provided at 31 March 2007 by approximately £86m in the year ending 31 March 2008 and increase profit for the year by the same amount. The estimated impact on deferred tax on other recognised gains and losses included in equity is not expected to be significant. This decrease in deferred tax is due to the reduction in the corporation tax rate from 30 per cent to 28 per cent with effect from 1 April 2008. The impact of other announced changes to the UK Corporation Tax system has not yet been assessed.

11. Dividends

	North West DN 2007 £m	East of England DN 2007 £m	West Midlands DN 2007 £m	North London DN 2007 £m	Metering 2007 £m	Meter Reading 2007 £m	De-minimis activities 2007 £m	Other activities 2007 £m	Total 2007 £m	North West DN 2006 £m	East of England DN 2006 £m	West Midlands DN 2006 £m	North London DN 2006 £m	Metering 2006 £m	Meter Reading 2006 £m	De-minimis activities 2006 £m	Other activities 2006 £m	Total 2006 £m
Ordinary dividends																		
Interim dividend for 2007	**18**	**73**	**27**	**-**	**52**	**1**	**-**	**-**	**171**	-	-	-	-	-	-	-	-	-
Final dividend for 2006	**195**	**316**	**159**	**176**	**229**	**-**	**-**	**-**	**1,075**	-	-	-	-	-	-	-	-	-
Interim dividend for 2006	**-**	**-**	**-**	**-**	**-**	**-**	**-**	**-**	**-**	33	70	33	33	31	2	-	1	203
	213	**389**	**186**	**176**	**281**	**1**	**-**	**-**	**1,246**	33	70	33	33	31	2	-	1	203

National Grid Gas plc is prohibited from declaring a dividend or other distribution unless it has certified to Ofgem that it is in compliance in all material respects with certain regulatory obligations, including a requirement to ensure it has sufficient financial resources and facilities to enable it to carry on its business and a requirement to use all reasonable endeavours to maintain an investment grade rating.

12. Intangible assets

	North West DN 2007 £m	East of England DN 2007 £m	West Midlands DN 2007 £m	North London DN 2007 £m	Metering 2007 £m	Meter Reading 2007 £m	De-minimis activities 2007 £m	Other activities 2007 £m	Total 2007 £m	North West DN 2006 £m	East of England DN 2006 £m	West Midlands DN 2006 £m	North London DN 2006 £m	Metering 2006 £m	Meter Reading 2006 £m	De-minimis activities 2006 £m	Other activities 2006 £m	Total 2006 £m
Non-current																		
Cost at 1 April	7	10	5	6	2	1	-	-	31	7	11	6	6	1	1	-	-	32
Additions	3	5	2	2	-	-	-	2	14	1	-	-	1	1	-	-	-	3
Disposals	-	-	-	-	-	-	-	-	-	(1)	(1)	(1)	(1)	-	-	-	-	(4)
Cost at 31 March	10	15	7	8	2	1	-	2	45	7	10	5	6	2	1	-	-	31
Amortisation at 1 April	(5)	(8)	(4)	(5)	(1)	(1)	-	-	(24)	(3)	(6)	(4)	(3)	-	(1)	-	-	(17)
Amortisation charge for the year	(1)	(1)	-	-	-	-	-	-	(2)	(3)	(3)	(1)	(3)	(1)	-	-	-	(11)
Disposals	-	-	-	-	-	-	-	-	-	1	1	1	1	-	-	-	-	4
Amortisation at 31 March	(6)	(9)	(4)	(5)	(1)	(1)	-	-	(26)	(5)	(8)	(4)	(5)	(1)	(1)	-	-	(24)
Net book value at 31 March	**4**	**6**	**3**	**3**	**1**	**-**	**-**	**2**	**19**	2	2	1	1	1	-	-	-	7

Intangible assets comprise internally developed computer software and related licences.

13. Property, plant and equipment

Land and buildings

	North West DN 2007 £m	East of England DN 2007 £m	West Midlands DN 2007 £m	North London DN 2007 £m	Metering 2007 £m	Meter Reading 2007 £m	De-minimis activities 2007 £m	Other activities 2007 £m	Total 2007 £m	North West DN 2006 £m	East of England DN 2006 £m	West Midlands DN 2006 £m	North London DN 2006 £m	Metering 2006 £m	Meter Reading 2006 £m	De-minimis activities 2006 £m	Other activities 2006 £m	Total 2006 £m
Cost at 1 April	11	14	6	6	1	-	-	-	38	9	12	5	5	-	-	-	-	31
Additions	2	3	1	1	-	-	-	-	7	2	2	2	1	-	-	-	-	7
Disposals	(1)	-	-	-	-	-	-	-	(1)	-	-	(1)	-	-	-	-	-	(1)
Reclassifications and transfers	1	2	-	-	-	-	-	-	3	-	-	-	-	1	-	-	-	1
Cost at 31 March	13	19	7	7	1	-	-	-	47	11	14	6	6	1	-	-	-	38
Depreciation at 1 April	(4)	(4)	(1)	(2)	-	-	-	-	(11)	(3)	(4)	(1)	(1)	-	-	-	-	(9)
Charge for the year	(1)	(1)	-	-	-	-	-	-	(2)	(1)	-	(1)	(1)	-	-	-	-	(3)
Disposals	-	-	-	-	-	-	-	-	-	-	-	1	-	-	-	-	-	1
Reclassifications and transfers	1	-	(1)	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-
Depreciation at 31 March	(4)	(5)	(2)	(2)	-	-	-	-	(13)	(4)	(4)	(1)	(2)	-	-	-	-	(11)
Net book value at 31 March	**9**	**14**	**5**	**5**	**1**	**-**	**-**	**-**	**34**	7	10	5	4	1	-	-	-	27
Which comprises:																		
Freehold	**7**	**11**	**4**	**4**	**1**	**-**	**-**	**-**	**27**	7	8	5	3	1	-	-	-	24
Long leasehold	**-**	**-**	**-**	**-**	**-**	**-**	**-**	**-**	**-**	-	1	-	-	-	-	-	-	1
Short leasehold	**2**	**3**	**1**	**1**	**-**	**-**	**-**	**-**	**7**	-	1	-	1	-	-	-	-	2
	9	**14**	**5**	**5**	**1**	**-**	**-**	**-**	**34**	7	10	5	4	1	-	-	-	27

Plant and machinery

	North West DN 2007 £m	East of England DN 2007 £m	West Midlands DN 2007 £m	North London DN 2007 £m	Metering 2007 £m	Meter Reading 2007 £m	De-minimis activities 2007 £m	Other activities 2007 £m	Total 2007 £m	North West DN 2006 £m	East of England DN 2006 £m	West Midlands DN 2006 £m	North London DN 2006 £m	Metering 2006 £m	Meter Reading 2006 £m	De-minimis activities 2006 £m	Other activities 2006 £m	Total 2006 £m
Cost at 1 April	1,559	2,347	1,275	1,464	1,724	-	-	-	8,369	1,459	2,216	1,205	1,372	1,716	-	-	-	7,968
Additions	115	143	80	87	82	-	-	-	507	102	133	67	93	64	-	-	-	459
Disposals	(3)	(1)	-	(1)	(6)	-	-	-	(11)	(2)	(2)	3	(1)	(56)	-	-	-	(58)
Reclassifications and transfers	(1)	(2)	-	3	-	-	-	-	-	-	-	-	-	-	-	-	-	-
Cost at 31 March	1,670	2,487	1,355	1,553	1,800	-	-	-	8,865	1,559	2,347	1,275	1,464	1,724	-	-	-	8,369
Depreciation at 1 April	(430)	(688)	(337)	(394)	(905)	-	-	-	(2,754)	(401)	(648)	(312)	(367)	(821)	-	-	-	(2,549)
Charge for the year	(30)	(45)	(26)	(29)	(135)	-	-	-	(265)	(28)	(43)	(20)	(26)	(140)	-	-	-	(257)
Disposal of undertakings	-	-	-	-	-	-	-	-	-	(3)	(3)	(2)	(3)	-	-	-	-	(11)
Disposals	3	1	-	1	6	-	-	-	11	1	1	(3)	1	56	-	-	-	56
Reclassifications and transfers	1	1	1	(1)	-	-	-	-	2	1	5	-	1	-	-	-	-	7
Depreciation at 31 March	(456)	(731)	(362)	(423)	(1,034)	-	-	-	(3,006)	(430)	(688)	(337)	(394)	(905)	-	-	-	(2,754)
Net book value at 31 March	**1,214**	**1,756**	**993**	**1,130**	**766**	**-**	**-**	**-**	**5,859**	1,129	1,659	938	1,070	819	-	-	-	5,615

13. Property, plant and equipment (continued)

Assets in the course of construction

	North West DN 2007 £m	East of England DN 2007 £m	West Midlands DN 2007 £m	North London DN 2007 £m	Metering 2007 £m	Meter Reading 2007 £m	De-minimis activities 2007 £m	Other activities 2007 £m	Total 2007 £m	North West DN 2006 £m	East of England DN 2006 £m	West Midlands DN 2006 £m	North London DN 2006 £m	Metering 2006 £m	Meter Reading 2006 £m	De-minimis activities 2006 £m	Other activities 2006 £m	Total 2006 £m
Cost at 1 April	-	-	-	2	-	-	-	-	2	5	8	4	7	-	-	-	-	24
Additions	4	6	3	7	-	-	-	-	20	-	1	-	3	-	-	-	-	4
Reclassifications and transfers	(1)	(2)	(1)	-	-	-	-	-	(4)	(5)	(9)	(4)	(8)	-	-	-	-	(26)
Cost at 31 March	3	4	2	9	-	-	-	-	18	-	-	-	2	-	-	-	-	2
Net book value at 31 March	**3**	**4**	**2**	**9**	**-**	**-**	**-**	**-**	**18**	-	-	-	2	-	-	-	-	2

Motor vehicles and office equipment

	North West DN 2007 £m	East of England DN 2007 £m	West Midlands DN 2007 £m	North London DN 2007 £m	Metering 2007 £m	Meter Reading 2007 £m	De-minimis activities 2007 £m	Other activities 2007 £m	Total 2007 £m	North West DN 2006 £m	East of England DN 2006 £m	West Midlands DN 2006 £m	North London DN 2006 £m	Metering 2006 £m	Meter Reading 2006 £m	De-minimis activities 2006 £m	Other activities 2006 £m	Total 2006 £m
Cost at 1 April	96	124	52	59	43	-	-	-	374	87	114	58	59	-	-	-	-	318
Additions	6	9	3	4	1	-	-	1	24	11	13	6	6	-	-	-	-	36
Disposals	(5)	(6)	(2)	(2)	-	-	-	-	(15)	-	(1)	(1)	(1)	-	-	-	-	(3)
Reclassifications and transfers	5	7	6	5	(1)	-	-	-	22	(2)	(2)	(11)	(5)	43	-	-	-	23
Cost at 31 March	102	134	59	66	43	-	-	1	405	96	124	52	59	43	-	-	-	374
Depreciation at 1 April	(68)	(89)	(37)	(41)	(34)	-	-	-	(269)	(64)	(83)	(43)	(44)	-	-	-	-	(234)
Charge for the year	(9)	(12)	(5)	(5)	(3)	-	-	-	(34)	(7)	(9)	(3)	(4)	(3)	-	-	-	(26)
Disposals	5	6	2	2	-	-	-	-	15	-	1	1	1	-	-	-	-	3
Reclassifications and transfers	(4)	(4)	(4)	(5)	-	-	-	-	(17)	3	2	8	6	(31)	-	-	-	(12)
Depreciation at 31 March	(76)	(99)	(44)	(49)	(37)	-	-	-	(305)	(68)	(89)	(37)	(41)	(34)	-	-	-	(269)
Net book value at 31 March	**26**	**35**	**15**	**17**	**6**	**-**	**-**	**1**	**100**	28	35	15	18	9	-	-	-	105

13. Property, plant and equipment (continued)

Total property, plant and equipment

	North West DN 2007 £m	East of England DN 2007 £m	West Midlands DN 2007 £m	North London DN 2007 £m	Metering 2007 £m	Meter Reading 2007 £m	De-minimis activities 2007 £m	Other activities 2007 £m	Total 2007 £m	North West DN 2006 £m	East of England DN 2006 £m	West Midlands DN 2006 £m	North London DN 2006 £m	Metering 2006 £m	Meter Reading 2006 £m	De-minimis activities 2006 £m	Other activities 2006 £m	Total 2006 £m
Cost at 1 April	1,666	2,485	1,333	1,531	1,768	-	-	-	8,783	1,560	2,350	1,272	1,443	1,716	-	-	-	8,341
Additions	127	161	87	99	83	-	-	1	558	115	149	75	103	64	-	-	-	506
Disposals	(9)	(7)	(2)	(3)	(6)	-	-	-	(27)	(2)	(3)	1	(2)	(56)	-	-	-	(62)
Transfers	4	5	5	8	(1)	-	-	-	21	(7)	(11)	(15)	(13)	44	-	-	-	(2)
Cost at 31 March	1,788	2,644	1,423	1,635	1,844	-	-	1	9,335	1,666	2,485	1,333	1,531	1,768	-	-	-	8,783
Depreciation at 1 April	(502)	(781)	(375)	(437)	(939)	-	-	-	(3,034)	(468)	(735)	(356)	(412)	(821)	-	-	-	(2,792)
Charge for the year	(40)	(58)	(31)	(34)	(138)	-	-	-	(301)	(36)	(52)	(24)	(31)	(143)	-	-	-	(286)
Disposal of undertakings	-	-	-	-	-	-	-	-		(3)	(3)	(2)	(3)	-	-	-	-	(11)
Disposals	8	7	2	3	6	-	-	-	26	1	2	(1)	2	56	-	-	-	60
Transfers	(2)	(3)	(4)	(6)	-	-	-	-	(15)	4	7	8	7	(31)	-	-	-	(5)
Depreciation at 31 March	(536)	(835)	(408)	(474)	(1,071)	-	-	-	(3,324)	(502)	(781)	(375)	(437)	(939)	-	-	-	(3,034)
Net book value at 31 March	**1,252**	**1,809**	**1,015**	**1,161**	**773**	**-**	**-**	**1**	**6,011**	1,164	1,704	958	1,094	829	-	-	-	5,749

The cost of property, plant and equipment at 31 March 2007 included £2m (2006: £2m) relating to interest capitalised.

Included within trade and other payables and other non-current liabilities at 31 March 2007 are contributions to the cost of property, plant and equipment amounting to £22m (2006: £23m) and £814m (2006: £770m) respectively.

During the course of the year, the useful lives of certain plant and machinery assets of the metering business have been reviewed resulting in a net reduction in a £12 million increase in the depreciation charge for the year.

14. Deferred tax assets and liabilities

Deferred tax assets/(liabilities) by source

	Accelerated tax depreciation £m	Employee share options £m	Mark to market £m	Other net temporary differences £m	Total £m
Deferred tax assets at 1 April 2005	-	4	-	8	12
Deferred tax liabilities at 1 April 2005	(1,072)	-	-	(49)	(1,121)
At 1 April 2005	(1,072)	4	-	(41)	(1,109)
First time adoption of IAS 39	-	-	(11)	24	13
At 1 April 2005	(1,072)	4	(11)	(17)	(1,096)
(Charged)/credited to income statement	(57)	1	3	12	(41)
Credited to equity	-	3	1	-	4
Transfers	22	2	-	(13)	11
At 31 March 2006	(1,107)	10	(7)	(18)	(1,122)
Deferred tax assets at 31 March 2006	-	10	-	13	23
Deferred tax liabilities at 31 March 2006	(1,107)	-	(7)	(31)	(1,145)
At 31 March 2006	(1,107)	10	(7)	(18)	(1,122)
(Charged)/credited to income statement	(64)	(6)	-	(6)	(76)
Credited to equity	-	2	(5)	-	(3)
Transfers	-	-	-	11	11
At 31 March 2007	**(1,171)**	**6**	**(12)**	**(13)**	**(1,190)**
Deferred tax assets at 31 March 2007	-	6	-	9	15
Deferred tax liabilities at 31 March 2007	(1,171)	-	(12)	(22)	(1,205)
	(1,171)	6	(12)	(13)	(1,190)

14. Deferred tax assets and liabilities (continued)

Deferred tax assets/(liabilities) by business

	North West DN £m	East of England DN £m	West Midlands DN £m	North London DN £m	Metering £m	Meter Reading £m	De-minimis activities £m	Other activities £m	Total £m
Deferred tax assets at 1 April 2005	2	3	1	2	4	-	-	-	12
Deferred tax liabilities at 1 April 2005	(220)	(306)	(180)	(210)	(205)	-	-	-	(1,121)
At 1 April 2005	(218)	(303)	(179)	(208)	(201)	-	-	-	(1,109)
First time adoption of IAS 39	2	4	1	1	5	-	-	-	13
At 1 April 2005	(216)	(299)	(178)	(207)	(196)	-	-	-	(1,096)
(Charged)/credited to income statement	(16)	(18)	(11)	(15)	19	-	-	-	(41)
Credited to equity	1	2	-	1	-	-	-	-	4
Transfers	7	5	2	2	(5)	-	-	-	11
At 31 March 2006	(224)	(310)	(187)	(219)	(182)	-	-	-	(1,122)
Deferred tax assets at 31 March 2006	3	6	2	3	9	-	-	-	23
Deferred tax liabilities at 31 March 2006	(227)	(316)	(189)	(222)	(191)	-	-	-	(1,145)
At 31 March 2006	(224)	(310)	(187)	(219)	(182)	-	-	-	(1,122)
(Charged)/credited to income statement	(26)	(33)	(18)	(18)	21	-	-	(2)	(76)
Charged to equity	(1)	(1)	-	(1)	-	-	-	-	(3)
Transfers	1	3	1	1	5	-	-	-	11
At 31 March 2007	**(250)**	**(341)**	**(204)**	**(237)**	**(156)**	**-**	**-**	**(2)**	**(1,190)**
Deferred tax assets at 31 March 2007	3	4	2	2	4	-	-	-	15
Deferred tax liabilities at 31 March 2007	(253)	(345)	(206)	(239)	(160)	-	-	(2)	(1,205)
	(250)	**(341)**	**(204)**	**(237)**	**(156)**	**-**	**-**	**(2)**	**(1,190)**

Deferred tax assets are all offset against deferred tax liabilities.

At the balance sheet date there were no material current deferred tax assets or liabilities (2006: £nil).

15. Other non-current receivables

	North West DN 2007 £m	East of England DN 2007 £m	West Midlands DN 2007 £m	North London DN 2007 £m	Metering 2007 £m	Meter Reading 2007 £m	De-minimis activities 2007 £m	Other activities 2007 £m	Total 2007 £m	North West DN 2006 £m	East of England DN 2006 £m	West Midlands DN 2006 £m	North London DN 2006 £m	Metering 2006 £m	Meter Reading 2006 £m	De-minimis activities 2006 £m	Other activities 2006 £m	Total 2006 £m
Other receivables	**-**	**1**	**-**	**-**	**1**	**-**	**-**	**-**	**2**	-	1	-	-	1	-	-	-	2
Amounts owed by parent undertaking	**730**	**1,183**	**595**	**657**	**858**	**-**	**-**	**-**	**4,023**	730	1,183	595	657	858	-	-	-	4,023
	730	**1,184**	**595**	**657**	**859**	**-**	**-**	**-**	**4,025**	730	1,184	595	657	859	-	-	-	4,025

The amount owed by the parent is non-contractual and accordingly its fair value equals its book value. The fair value of other non-current receivables approximates to their book value.

16. Financial investments

	North West DN 2007 £m	East of England DN 2007 £m	West Midlands DN 2007 £m	North London DN 2007 £m	Metering 2007 £m	Meter Reading 2007 £m	De-minimis activities 2007 £m	Other activities 2007 £m	Total 2007 £m	North West DN 2006 £m	East of England DN 2006 £m	West Midlands DN 2006 £m	North London DN 2006 £m	Metering 2006 £m	Meter Reading 2006 £m	De-minimis activities 2006 £m	Other activities 2006 £m	Total 2006 £m
Current																		
Available for sale investments – Investments in short-term UK money funds	**38**	**60**	**30**	**35**	**31**	**-**	**-**	**1**	**195**	6	9	4	5	5	-	-	-	29
Amounts due from fellow subsidiaries	**9**	**15**	**8**	**9**	**8**	**-**	**-**	**-**	**49**	-	-	-	-	-	-	-	-	-
Loans and receivables – restricted cash balances	**1**	**1**	**-**	**1**	**-**	**-**	**-**	**-**	**3**	-	-	-	-	-	-	-	-	-
	48	**76**	**38**	**45**	**39**	**-**	**-**	**1**	**247**	6	9	4	5	5	-	-	-	29

Available-for-sale investments are recorded at their fair value. The fair value of loans and receivables approximates to their book value.

The maximum exposure to credit risk at the reporting date is the fair value of the financial instruments – refer to note 18 for further information on treasury related credit risk. None of the financial instruments are past due or impaired.

Investments in short term UK money funds and restricted cash balances comprise floating rate interest bearing investments. Loans due from fellow subsidiaries are non-interest bearing.

Restricted cash balances represent cash posted by National Grid Gas plc its subsidiaries under collateral agreements.

The carrying amounts of financial investments and restricted cash balances are denominated in sterling.

17. Derivative financial instruments

Derivatives are financial instruments that derive their value from the price of an underlying item such as interest rates, foreign exchange, credit spreads, commodities and equity or other indices. Derivatives enable their users to alter exposure to market or credit risks. National Grid Gas uses derivatives to manage both treasury and operational market risks.

Derivatives are carried at fair value and are shown in the balance sheet as separate totals of assets and liabilities. Asset values represent the cost of replacing all transactions with a fair value in our favour assuming that all relevant counterparties default at the same time, and that the transactions can be replaced immediately in the market. Liability values represent the cost to counterparties of replacing all their transactions with a fair value in their favour in the case of default. Derivative assets and liabilities on different transactions are only netted if the transactions are with the same counterparty, a legal right of set-off exists and the cash flows are intended to be settled on a net basis.

Treasury financial instruments

Derivatives are used for hedging purposes in the management of exposure to market risks. This enables the optimisation of the overall cost of accessing debt capital markets, and to mitigate the market risk which would otherwise arise from the maturity and other profiles of National Grid Gas's assets and liabilities.

Hedging policies using derivative financial instruments are further explained in note 18. Derivatives that are held as hedging instruments are formally designated as hedges as defined in IAS 39. Derivatives may qualify as hedges for accounting purposes if they are fair value hedges or cash flow hedges. These are described as follows:

17. Derivative financial instruments (continued)

Fair value hedges

Fair value hedges principally consist of interest rate and cross-currency swaps that are used to protect against changes in the fair value of fixed-rate, long-term financial instruments due to movements in market interest rates. For qualifying fair value hedges, all changes in the fair value of the derivative and changes in the fair value of the item in relation to the risk being hedged are recognised in the income statement. If the hedge relationship is terminated, the fair value adjustment to the hedged item continues to be reported as part of the basis of the item and is amortised to the income statement as a yield adjustment over the remainder of the hedging period.

Cash flow hedges

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

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

The gains and losses on ineffective portions of such derivatives are recognised immediately in the income statement.

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 or on the balance sheet. 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

National Grid Gas'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 more 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 interest expense and other finance costs.

Operational financial instruments

Commodity derivatives are used to manage commodity prices associated with gas distribution operations. As these contracts are for normal usage in our operations and are not settled net, they are carried at cost and are recognised within trade receivables or payables as appropriate.

17. Derivative financial instruments (continued)

The following information on derivative financial instruments largely comprises a simple apportionment of such information in respect of National Grid Gas plc as reported in its annual report and accounts. Accordingly, disclosures are only provided in total and not by regulatory business.

National Grid Gas's use of derivatives may entail a derivative transaction qualifying for one or more hedge type designations under IAS 39. The fair value and their notional amounts by designated hedge type can be analysed as follows:

	2007				2006			
	Asset		Liability		Asset		Liability	
	Fair value £m	Notional amount £m	Fair value £m	Notional amount £m	Fair value £m	Notional amount £m	Fair value £m	Notional amount £m
Fair value hedges								
Interest rate swaps	**1**	**(77)**	**(8)**	**(354)**	17	(166)	(5)	(573)
Cross-currency interest rate swaps	**31**	**(519)**	**(41)**	**(222)**	59	(535)	(41)	(311)
	32	**(596)**	**(49)**	**(576)**	76	(701)	(46)	(884)
Cash flow hedges								
Interest rate swaps	**2**	**(186)**	**(2)**	**(124)**	27	(109)	(8)	(240)
Cross-currency interest rate swaps	**17**	**(319)**	**(5)**	**(14)**	39	(288)	(4)	(15)
Foreign exchange forward contracts	**-**	**(2)**	**-**	**(17)**	1	(27)	(2)	(29)
	19	**(507)**	**(7)**	**(155)**	67	(424)	(14)	(284)
Derivative instruments not in a formal hedging relationship								
Interest rate swaps	**6**	**(567)**	**(7)**	**(301)**	7	(119)	(11)	(253)
Cross-currency interest rate swaps	**-**	**-**	**(2)**	**(5)**	-	(4)	(2)	(5)
Foreign exchange forward contracts	**-**	**-**	**-**	**-**	-	-	-	20
	6	**(567)**	**(9)**	**(306)**	7	(123)	(13)	(238)
Total	**57**	**(1,670)**	**(65)**	**(1,037)**	150	(1,248)	(73)	(1,406)

The maturity of derivative financial instruments is as follows:

	2007		2006	
	Assets £m	Liabilities £m	Assets £m	Liabilities £m
In one year or less	**7**	**(9)**	67	(33)
Current	**7**	**(9)**	67	(33)
In more than one year but not more than two years	**15**	**(3)**	2	(1)
In more than two years but not more than three years	**8**	**(5)**	18	(3)
In more than three years but not more than four years	**-**	**-**	12	(3)
In more than four years but not more than five years	**-**	**-**	-	-
In more than five years	**27**	**(48)**	51	(33)
Non-current	**50**	**(56)**	83	(40)
	57	**(65)**	150	(73)

18. Financial risk factors

National Grid Gas's activities expose it to a variety of financial risks: market risk (including currency risk; fair value interest rate risk; cash flow interest rate risk), credit risk and liquidity risk. The overall risk management programme focuses on the unpredictability of financial markets and seeks to minimise potential adverse effects on financial performance. Derivative financial instruments are used to hedge certain risk exposures.

Risk management is carried out by a central treasury department under policies approved by the Board of Directors of National Grid plc. This department identifies, evaluates and hedges financial risks in close co-operation with the operating units. The National Grid plc Board provides written principles for overall risk management, as well as written policies covering specific areas, such as foreign exchange risk, interest rate risk, credit risk, use of derivative financial instruments and non-derivative financial instruments, and investment of excess liquidity as discussed further in National Grid Gas's treasury policy, described on pages 23 to 25.

The information provided below in respect of financial risk factors includes financial amounts which are simple apportionments of such amounts in respect of National Grid Gas plc, as reported in its annual report and accounts. Accordingly, disclosures are only provided in total and not by regulatory business.

(a) Market risk

Foreign exchange risk

National Grid Gas raises finance in various currencies and is exposed to foreign exchange risk arising from related currency exposures. Foreign exchange risk arises from future commercial transactions and recognised assets and liabilities.

With respect to near term foreign exchange risk, National Grid Gas uses foreign exchange forwards to manage foreign exchange transaction exposure. Its policy is to hedge a minimum percentage of known contracted foreign currency flows in the period out to six months and also in the period six to twelve months in order to mitigate foreign currency movements in the intervening period. Where cash forecasts are uncertain, National Grid Gas generally covers a percentage of the foreign currency flows depending on the certainty of the cash flows.

During 2007 and 2006, derivative financial instruments were used to manage foreign currency risk as follows:

	2007					2006				
	Sterling £m	Euro £m	US dollar £m	Other £m	Total £m	Sterling £m	Euro £m	US dollar £m	Other £m	Total £m
Cash and cash equivalents	**113**	**-**	**-**	**-**	**113**	156	-	-	-	156
Financial investments	**247**	**-**	**-**	**-**	**247**	29	-	-	-	29
Bank overdrafts	**(4)**	**-**	**-**	**-**	**(4)**	-	-	-	-	-
Borrowings	**(3,006)**	**(161)**	**(315)**	**(218)**	**(3,700)**	(1,380)	(457)	(487)	(281)	(2,605)
Pre-derivative position	**(2,650)**	**(161)**	**(315)**	**(218)**	**(3,344)**	(1,195)	(457)	(487)	(281)	(2,420)
Derivative effect	**(705)**	**181**	**298**	**218**	**(8)**	(1,261)	561	496	281	77
Net debt position	**(3,355)**	**20**	**(17)**	**-**	**(3,352)**	(2,456)	104	9	-	(2,343)

Cash flow and fair value interest rate risk

There are no significant interest-bearing assets maintained on an ongoing basis. The income and operating cash flows are substantially independent of changes in market interest rates.

Interest rate risk arises from long-term borrowings. Borrowings issued at variable rates expose National Grid Gas to cash flow interest rate risk. Borrowings issued at fixed rates expose National Grid Gas to fair value interest rate risk. The interest rate risk management policy, as further explained on page 24, is to minimise the finance costs (being interest costs and changes in the market value of debt). Some of National Grid Gas's borrowings issued are index-linked, that is their cost is linked to changes in the UK Retail Prices Index (RPI). Management believes that these borrowings provide a good hedge for revenues and regulatory asset values that are also RPI-linked.

18. Financial risk factors (continued)

Cash flow and fair value interest rate risk (continued)

The following table sets out the carrying amount, by contractual maturity, of borrowings that are exposed to interest rate risk before taking into account interest rate swaps:

	2007 £m	2006 £m
Fixed interest rate borrowings		
In one year or less	**(197)**	(651)
In more than one year but not more than two years	**(272)**	(170)
In more than two years but not more than three years	**(320)**	(298)
In more than three years but not more than four years	**-**	(355)
In more than four years but not more than five years	**-**	-
In more than five years	**(719)**	(877)
	(1,508)	(2,351)
Floating interest rate borrowings (including RPI)	**(2,192)**	(254)
Total borrowings	**(3,700)**	(2,605)

During 2007 and 2006, net debt was managed using derivative instruments to hedge interest rate risk as follows:

	2007					2006				
	Fixed rate £m	Floating rate £m	RPI (i) £m	Other (ii) £m	Total £m	Fixed rate £m	Floating rate £m	RPI (i) £m	Other (ii) £m	Total £m
Cash and cash equivalents	**-**	**113**	**-**	**-**	**113**	-	156	-	-	156
Financial investments	**-**	**198**	**-**	**49**	**247**	-	29	-	-	29
Bank overdrafts	**-**	**(4)**	**-**	**-**	**(4)**	-	-	-	-	-
Borrowings	**(1,508)**	**(1,169)**	**(1,023)**	**-**	**(3,700)**	(2,351)	(254)	-	-	(2,605)
Pre-derivative position	**(1,508)**	**(862)**	**(1,023)**	**49**	**(3,344)**	(2,351)	(69)	-	-	(2,420)
Derivative effect	**636**	**(644)**	**-**	**-**	**(8)**	1,560	(1,483)	-	-	77
Net debt position	**(872)**	**(1,506)**	**(1,023)**	**49**	**(3,352)**	(791)	(1,552)	-	-	(2,343)

(i) Represents financial instruments which are linked to the UK retail prices index.

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

18. Financial risk factors (continued)

(b) Credit risk

Credit risk is managed on a portfolio basis for the National Grid group as a whole. Credit risk arises from cash and cash equivalents, derivative financial instruments and deposits with banks and financial institutions, as well as credit exposures to wholesale and retail customers, including outstanding receivables and committed transactions.

Treasury related credit risk

Counterparty risk arises from the investment of surplus funds and from the use of derivative instruments. National Grid Gas's limits are managed by National Grid plc, as explained in Treasury policies on page 24.

As at 31 March 2007 and 2006, National Grid Gas had a number of exposures to individual counterparties. In accordance with treasury policies and exposure management practices, counterparty credit exposure limits are continually monitored and no individual exposure is considered significant in the ordinary course of treasury management activity. It is not expected that there will be any significant losses from non-performance by these counterparties.

The counterparty exposure under allocated derivative financial contracts as shown in note 17 was £57m (2006: £150m); after netting agreements it was £41m (2006: £102m). This exposure is further reduced by collateral received as shown in note 22.

Wholesale and retail credit risk

The DNs' principal commercial exposure is governed by the credit rules within the Uniform Network Code. These lay down the level of credit relative to the regulatory asset value for each credit rating. The Metering business's principal commercial exposure is governed by long-term contracts with gas suppliers which require monthly payment. Sales to retail customers, such as those requiring connections, are usually settled in cash or using major credit cards. Management does not expect any significant losses of receivables that have not been provided for as shown in note 20.

(c) Liquidity analysis

National Grid Gas manages its liquidity requirements by the use of both short- and long-term cash flow forecasts. These forecasts are supplemented by a financial headroom position which is used to demonstrate funding adequacy for at least a 12-month period.

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

	At 31 March 2007					At 31 March 2006				
	Due within 1 year £m	Due between 1 and 2 years £m	Due between 2 and 3 years £m	Due 3 years and beyond £m	Total £m	Due within 1 year £m	Due between 1 and 2 years £m	Due between 2 and 3 years £m	Due 3 years and beyond £m	Total £m
Non-derivative financial liabilities										
Borrowings	**(1,171)**	**(302)**	**(324)**	**(2,147)**	**(3,944)**	(644)	(199)	(340)	(1,726)	(2,909)
Interest payments on borrowings (i)	**(107)**	**(88)**	**(71)**	**(1,373)**	**(1,639)**	(114)	(98)	(78)	(629)	(919)
Other non-interest bearing liabilities	**(477)**	**(5)**	**-**	**-**	**(482)**	(426)	(32)	-	-	(458)
Derivative financial liabilities										
Derivative contracts – receipts	**32**	**22**	**6**	**73**	**133**	55	31	26	183	295
Derivative contracts – payments	**(34)**	**(18)**	**(8)**	**(102)**	**(162)**	(34)	(30)	(7)	(45)	(116)
	(1,757)	**(391)**	**(397)**	**(3,549)**	**(6,094)**	(1,163)	(328)	(399)	(2,217)	(4,107)

(i) The interest on borrowings is calculated based on borrowings held at 31 March without taking into account future issues. Floating rate interest is estimated using a future interest rate curve as at 31 March.

18. Financial risk factors (continued)

(d) Sensitivity analysis at 31 March 2007

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 UK interest rates and the UK Retail Prices Index.

The analysis excludes the impact of movements in market variables on the carrying value of 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 and the proportion of financial instruments in foreign currencies are all constant and on the basis of the hedge designations in place at 31 March 2007 and 31 March 2006, respectively. As a consequence, this sensitivity analysis relates to the position at these dates and is not representative of the year then ended, as all of these varied.

The following assumptions were made in calculating the sensitivity analysis:

- the balance sheet sensitivity to interest rates relates only to derivative financial instruments and available-for-sale investments, 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;
- 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 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; and
- sensitivity to the Retail Prices Index does not take into account any changes to revenue or operating costs that are affected by the Retail Prices Index or inflation generally.

Using the above assumptions, the following table shows the illustrative effect on the income statement and items that are recognised directly in equity that would result from reasonably possible movements in changes in the UK Retail Prices Index and UK interest rates, before the effects of tax.

	2007		2006 (i)	
	Income statement -/+ £m	Equity -/+ £m	Income statement -/+ £m	Equity -/+ £m
UK Retail Prices Index +/- 0.5%	**5**	**-**	-	-
UK interest rates +/- 0.5%	**7**	**10**	7	14

(i) Comparatives have been restated in respect of a calculation error made when preparing the 2005/06 annual report and accounts on which the regulatory accounting statements were based.

19. Inventories

	North West DN 2007 £m	East of England DN 2007 £m	West Midlands DN 2007 £m	North London DN 2007 £m	Metering 2007 £m	Meter Reading 2007 £m	De-minimis activities 2007 £m	Other activities 2007 £m	Total 2007 £m	North West DN 2006 £m	East of England DN 2006 £m	West Midlands DN 2006 £m	North London DN 2006 £m	Metering 2006 £m	Meter Reading 2006 £m	De-minimis activities 2006 £m	Other activities 2006 £m	Total 2006 £m
Raw materials and consumables	**3**	**4**	**2**	**2**	**4**	**-**	**-**	**-**	**15**	2	2	1	1	3	-	-	-	9

20. Trade and other receivables

	North West DN 2007 £m	East of England DN 2007 £m	West Midlands DN 2007 £m	North London DN 2007 £m	Metering 2007 £m	Meter Reading 2007 £m	De-minimis activities 2007 £m	Other activities 2007 £m	Total 2007 £m	North West DN 2006 £m	East of England DN 2006 £m	West Midlands DN 2006 £m	North London DN 2006 £m	Metering 2006 £m	Meter Reading 2006 £m	De-minimis activities 2006 £m	Other activities 2006 £m	Total 2006 £m
Trade receivables	**6**	**10**	**5**	**6**	**2**	**-**	**1**	**-**	**30**	7	11	5	7	3	-	-	3	36
Amounts owed by fellow subsidiaries	**3**	**11**	**3**	**3**	**24**	**-**	**-**	**1**	**45**	22	39	15	20	51	-	1	6	154
Other receivables	**4**	**6**	**3**	**4**	**4**	**-**	**-**	**-**	**21**	5	7	4	4	5	-	-	2	27
Prepayments and accrued income	**17**	**27**	**13**	**13**	**33**	**3**	**-**	**3**	**109**	19	30	14	17	36	1	-	2	119
	30	**54**	**24**	**26**	**63**	**3**	**1**	**4**	**205**	53	87	38	48	95	1	1	13	336

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

The carrying amounts of trade and other receivables are denominated in sterling.

Provision for impairment of receivables

As the amounts in respect of impairment of receivables are small, they have not been reported by regulatory business.

	Total £m
At 1 April 2005	3
Release of provision	(2)
Uncollected amounts written-off net of recoveries	2
At 31 March 2006	3
Release of provision	(1)
Uncollected amounts written-off net of recoveries	1
At 31 March 2007	**3**

20. Trade and other receivables (continued)

As at 31 March 2007, trade receivables of £3m (2006: £2m) were past due but not impaired. The ageing analysis of these trade receivables is as follows:

	2007 £m	2006 £m
Up to 3 months past due	**1**	-
3 to 6 months past due	**1**	1
Over 6 months past due	**1**	1
	3	2

Further information about wholesale and retail credit risk is provided in note 18.

21. Cash and cash equivalents

	North West DN 2007 £m	**East of England DN 2007 £m**	**West Midlands DN 2007 £m**	**North London DN 2007 £m**	**Metering 2007 £m**	**Meter Reading 2007 £m**	**De-minimis activities 2007 £m**	**Other activities 2007 £m**	**Total 2007 £m**	North West DN 2006 £m	East of England DN 2006 £m	West Midlands DN 2006 £m	North London DN 2006 £m	Metering 2006 £m	Meter Reading 2006 £m	De-minimis activities 2006 £m	Other activities 2006 £m	Total 2006 £m
Cash at bank and in-hand	**-**	**1**	**-**	**-**	**-**	**-**	**-**	**-**	**1**	-	-	-	-	-	-	-	-	-
Short-term deposits	**23**	**34**	**17**	**20**	**18**	**-**	**-**	**-**	**112**	30	48	23	27	27	-	-	1	156
Cash and cash equivalents	**23**	**35**	**17**	**20**	**18**	**-**	**-**	**-**	**113**	30	48	23	27	27	-	-	1	156
Bank overdrafts	**(1)**	**(1)**	**-**	**(1)**	**(1)**	**-**	**-**	**-**	**(4)**	-	-	-	-	-	-	-	-	-
Net cash and cash equivalents	**22**	**34**	**17**	**19**	**17**	**-**	**-**	**-**	**109**	30	48	23	27	27	-	-	1	156

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

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

Net cash and cash equivalents are held in sterling.

22. Borrowings

The following table analyses allocated total borrowings, excluding bank overdrafts:

	North West DN 2007 £m	East of England DN 2007 £m	West Midlands DN 2007 £m	North London DN 2007 £m	Metering 2007 £m	Meter Reading 2007 £m	De-minimis activities 2007 £m	Other activities 2007 £m	Total 2007 £m	North West DN 2006 £m	East of England DN 2006 £m	West Midlands DN 2006 £m	North London DN 2006 £m	Metering 2006 £m	Meter Reading 2006 £m	De-minimis activities 2006 £m	Other activities 2006 £m	Total 2006 £m
Current																		
Bank loans	**3**	**5**	**2**	**3**	**3**	**-**	**-**	**-**	**16**	11	18	9	9	10	-	-	-	57
Other bonds	**44**	**68**	**34**	**41**	**35**	**-**	**-**	**-**	**222**	126	195	96	111	112	-	-	3	643
Other loans	**-**	**1**	**-**	**-**	**-**	**-**	**-**	**-**	**1**	1	1	1	1	-	-	-	-	4
Borrowings from fellow subsidiaries	**198**	**301**	**149**	**177**	**155**	**-**	**-**	**2**	**982**	2	3	1	2	1	-	-	-	9
	245	**375**	**185**	**221**	**193**	**-**	**-**	**2**	**1,221**	140	217	107	123	123	-	-	3	713
Non-current																		
Bank loans	**49**	**76**	**37**	**44**	**39**	**-**	**-**	**1**	**246**	27	42	21	25	25	-	-	-	140
Other bonds	**434**	**667**	**329**	**393**	**342**	**-**	**-**	**3**	**2,168**	341	531	262	299	307	-	1	8	1,749
Other loans	**13**	**20**	**10**	**12**	**10**	**-**	**-**	**-**	**65**	1	1	-	1	-	-	-	-	3
	496	**763**	**376**	**449**	**391**	**-**	**-**	**4**	**2,479**	369	574	283	325	332	-	1	8	1,892
Total borrowings	**741**	**1,138**	**561**	**670**	**584**	**-**	**-**	**6**	**3,700**	509	791	390	448	455	-	1	11	2,605

Allocated total borrowings are repayable as follows:

	North West DN 2007 £m	East of England DN 2007 £m	West Midlands DN 2007 £m	North London DN 2007 £m	Metering 2007 £m	Meter Reading 2007 £m	De-minimis activities 2007 £m	Other activities 2007 £m	Total 2007 £m	North West DN 2006 £m	East of England DN 2006 £m	West Midlands DN 2006 £m	North London DN 2006 £m	Metering 2006 £m	Meter Reading 2006 £m	De-minimis activities 2006 £m	Other activities 2006 £m	Total 2006 £m
In 1 year or less	**245**	**375**	**185**	**221**	**193**	**-**	**-**	**2**	**1,221**	140	217	107	123	123	-	-	3	713
Between 1 and 2 years	**60**	**92**	**45**	**54**	**47**	**-**	**-**	**-**	**298**	38	59	29	34	34	-	-	1	195
Between 2 and 3 years	**64**	**98**	**49**	**58**	**50**	**-**	**-**	**1**	**320**	64	98	49	56	57	-	-	1	325
Between 3 and 4 years	**-**	**-**	**-**	**-**	**-**	**-**	**-**	**-**	**-**	69	108	53	60	62	-	1	2	355
Between 4 and 5 years	**-**	**-**	**-**	**-**	**-**	**-**	**-**	**-**	**-**	-	-	-	-	-	-	-	-	-
In more than 5 years other than by instalments	**372**	**573**	**282**	**337**	**294**	**-**	**-**	**3**	**1,861**	198	309	152	175	179	-	-	4	1,017
	741	**1,138**	**561**	**670**	**584**	**-**	**-**	**6**	**3,700**	509	791	390	448	455	-	1	11	2,605

22. Borrowings (continued)

The carrying amounts of allocated borrowings are denominated in the following currencies:

	North West DN 2007 £m	East of England DN 2007 £m	West Midlands DN 2007 £m	North London DN 2007 £m	Metering 2007 £m	Meter Reading 2007 £m	De-minimis activities 2007 £m	Other activities 2007 £m	Total 2007 £m	North West DN 2006 £m	East of England DN 2006 £m	West Midlands DN 2006 £m	North London DN 2006 £m	Metering 2006 £m	Meter Reading 2006 £m	De-minimis activities 2006 £m	Other activities 2006 £m	Total 2006 £m
Sterling	**602**	**924**	**455**	**545**	**475**	**-**	**-**	**5**	**3,006**	270	418	207	237	241	-	1	6	1,380
Euro	**33**	**50**	**24**	**29**	**25**	**-**	**-**	**-**	**161**	89	140	68	78	80	-	-	2	457
Dollar	**63**	**97**	**48**	**57**	**49**	**-**	**-**	**1**	**315**	94	148	73	85	85	-	-	2	487
Other currencies	**43**	**67**	**34**	**39**	**35**	**-**	**-**	**-**	**218**	56	85	42	48	49	-	-	1	281
	741	**1,138**	**561**	**670**	**584**	**-**	**-**	**6**	**3,700**	509	791	390	448	455	-	1	11	2,605

The allocated fair value of borrowings at 31 March 2007 was £3,672m (2006: £2,608m). 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.

None of National Grid Gas's borrowings are secured by charges over the assets of National Grid Gas.

The allocated notional amount of borrowings outstanding as at 31 March 2007 was £3,943m (2006: £2,875m).

Collateral is placed with or received from any counterparty where National Grid Gas has entered into a credit support annex to the ISDA Master Agreement once the current mark-to-market valuation of the trades between the parties exceeds an agreed threshold. Included in current bank loans is £16m (2006: £nil) in respect of cash received under collateral agreements. Cash placed under collateral agreements is shown in note 16.

As at 31 March 2007, National Grid Gas plc had committed credit facilities of £840m (2006: £865m) of which £840m was undrawn (2006: £865m undrawn).

Undrawn committed borrowing facilities of National Grid Gas plc

	2007 £m	2006 £m
Expiring:		
In one year or less	**-**	25
In more than two years	**840**	840
	840	865

All of the unused facilities at 31 March 2007 and at 31 March 2006 were held as back-up to commercial paper and similar borrowings.

23. Trade and other payables

	North West DN 2007 £m	East of England DN 2007 £m	West Midlands DN 2007 £m	North London DN 2007 £m	Metering 2007 £m	Meter Reading 2007 £m	De-minimis activities 2007 £m	Other activities 2007 £m	Total 2007 £m	North West DN 2006 £m	East of England DN 2006 £m	West Midlands DN 2006 £m	North London DN 2006 £m	Metering 2006 £m	Meter Reading 2006 £m	De-minimis activities 2006 £m	Other activities 2006 £m	Total 2006 £m
Trade payables	**45**	**65**	**30**	**16**	**62**	**2**	**1**	**11**	**232**	43	67	22	37	54	1	1	5	230
Amounts owed to fellow subsidiaries	**9**	**37**	**11**	**8**	**74**	**1**	**-**	**2**	**142**	13	26	9	12	36	-	-	3	99
Social security and other taxes	**15**	**33**	**14**	**12**	**17**	**-**	**-**	**1**	**92**	11	22	10	9	17	-	-	1	70
Other payables	**4**	**5**	**3**	**4**	**-**	**-**	**-**	**1**	**17**	2	3	1	2	-	-	-	1	9
Deferred income	**13**	**22**	**12**	**14**	**5**	**-**	**1**	**-**	**67**	12	19	10	11	4	-	-	8	64
	86	**162**	**70**	**54**	**158**	**3**	**2**	**15**	**550**	81	137	52	71	111	1	1	18	472

Due to their short maturities, the fair value of trade and other payables approximates to their book value.

The carrying amounts of trade and other payables are denominated in sterling.

24. Other non-current liabilities

	North West DN 2007 £m	East of England DN 2007 £m	West Midlands DN 2007 £m	North London DN 2007 £m	Metering 2007 £m	Meter Reading 2007 £m	De-minimis activities 2007 £m	Other activities 2007 £m	Total 2007 £m	North West DN 2006 £m	East of England DN 2006 £m	West Midlands DN 2006 £m	North London DN 2006 £m	Metering 2006 £m	Meter Reading 2006 £m	De-minimis activities 2006 £m	Other activities 2006 £m	Total 2006 £m
Other payables	**1**	**1**	**-**	**-**	**-**	**-**	**-**	**-**	**2**	-	1	-	-	1	-	-	-	2
Deferred income	**191**	**300**	**153**	**164**	**54**	**-**	**-**	**-**	**862**	182	287	146	150	48	-	-	-	813
	192	**301**	**153**	**164**	**54**	**-**	**-**	**-**	**864**	182	288	146	150	49	-	-	-	815

The fair value of trade and other payables approximates to their book value.

The carrying amounts of trade and other payables are denominated in sterling.

25. Provisions

	North West DN £m	East of England DN £m	West Midlands DN £m	North London DN £m	Metering £m	Meter Reading £m	De-minimis activities £m	Other activities £m	Total £m	North West DN £m	East of England DN £m	West Midlands DN £m	North London DN £m	Metering £m	Meter Reading £m	De-minimis activities £m	Other activities £m	Total £m
Environmental																		
At 1 April	18	9	4	13	-	-	-	-	44	17	8	4	12	-	-	-	-	41
Unwinding of discount	1	-	-	-	-	-	-	-	1	-	-	-	1	-	-	-	-	1
Utilised	(1)	-	-	-	-	-	-	-	(1)	(1)	-	-	(1)	-	-	-	-	(2)
Transfers	-	-	-	-	-	-	-	-	-	2	1	-	1	-	-	-	-	4
At 31 March	**18**	**9**	**4**	**13**	**-**	**-**	**-**	**-**	**44**	18	9	4	13	-	-	-	-	44
Restructuring																		
At 1 April	8	11	5	6	-	-	-	-	30	16	16	19	13	-	-	-	-	64
Additions	2	3	2	1	-	-	-	-	8	7	9	5	6	-	-	-	-	27
Utilised	(6)	(8)	(4)	(4)	-	-	-	-	(22)	(20)	(18)	(25)	(16)	-	-	-	-	(79)
Transfers	-	-	-	-	-	-	-	-	-	5	4	6	3	-	-	-	-	18
At 31 March	**4**	**6**	**3**	**3**	**-**	**-**	**-**	**-**	**16**	8	11	5	6	-	-	-	-	30
Other																		
At 1 April	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-
Additions	5	5	3	4	-	-	-	-	17	-	-	-	-	-	-	-	-	-
At 31 March	**5**	**5**	**3**	**4**	**-**	**-**	**-**	**-**	**17**	-	-	-	-	-	-	-	-	-
Total																		
At 1 April	26	20	9	19	-	-	-	-	74	33	24	23	25	-	-	-	-	105
Additions	7	8	5	5	-	-	-	-	25	7	9	5	6	-	-	-	-	27
Unwinding of discount	1	-	-	-	-	-	-	-	1	-	-	-	1	-	-	-	-	1
Utilised	(7)	(8)	(4)	(4)	-	-	-	-	(23)	(21)	(18)	(25)	(17)	-	-	-	-	(81)
Transfers	-	-	-	-	-	-	-	-	-	7	5	6	4	-	-	-	-	22
At 31 March	**27**	**20**	**10**	**20**	**-**	**-**	**-**	**-**	**77**	26	20	9	19	-	-	-	-	74

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

	North West DN £m	East of England DN £m	West Midlands DN £m	North London DN £m	Metering £m	Meter Reading £m	De-minimis activities £m	Other activities £m	Total £m	North West DN £m	East of England DN £m	West Midlands DN £m	North London DN £m	Metering £m	Meter Reading £m	De-minimis activities £m	Other activities £m	Total £m
Current	6	6	3	4	-	-	-	-	19	7	8	5	6	-	-	-	-	26
Non-current	21	14	7	16	-	-	-	-	58	19	12	4	13	-	-	-	-	48
	27	**20**	**10**	**20**	**-**	**-**	**-**	**-**	**77**	26	20	9	19	-	-	-	-	74

25. Provisions (provisions)

Environmental provision

The environmental provision represents the net present value of the estimated statutory decontamination costs of old gas manufacturing sites owned by National Grid Gas (discounted using a nominal rate of 5.55%). The anticipated timing of the cash flows for statutory decontamination cannot be predicted with certainty, but they are expected to be incurred over the financial years 2008 to 2055 with some 33% of the spend projected to be spent over the next five years.

There are a number of uncertainties that affect the calculation of the provision for gas site decontamination, including the impact of regulation, the accuracy of the site surveys, unexpected contaminants, transportation costs, the impact of alternative technologies and changes in the discount rate. National Grid Gas has made its best estimate of the financial effect of these uncertainties in the calculation of the provision, but future material changes in any of the assumptions could materially impact on the calculation of the provision and hence the income statement.

The undiscounted amount of the provision at 31 March 2007 relating to gas site decontamination was £70m (2006: £72m), being the undiscounted best estimate of the liability having regard to the uncertainties referred to above.

Restructuring provision

At 31 March 2007, £7m of the total restructuring provision (2006: £10m) consisted of provisions for the disposal of surplus leasehold interests and rates payable on surplus properties. The expected payment dates for property restructuring costs remain uncertain. The remainder of the restructuring provision related to business reorganisation costs, largely to be paid within the next financial year.

Other provisions

Other provisions at 31 March 2007 include £17m (2006: £nil) in respect of employer liability claims. The employer liability claims are based on prior claims experience and, therefore, there is no identifiable payment date associated with these items.

26. Reconciliation of movements in total equity

The businesses included in these regulatory accounting statements do not have their own separate share capital and reserves. Accordingly the equity of each business is only shown in total.

	North West DN £m	East of England DN £m	West Midlands DN £m	North London DN £m	Metering £m	Meter Reading £m	De-minimis activities £m	Other activities £m	Total £m
At 31 March 2005	455	629	411	471	178	(11)	-	-	2,133
First time adoption of IAS 39	(5)	(7)	(4)	(4)	(7)	-	-	-	(27)
At 1 April 2005	450	622	407	467	171	(11)	-	-	2,106
Net expense recognised directly in equity (i)	(2)	(2)	(1)	(2)	(4)	-	-	-	(11)
Profit for the year	56	121	57	57	55	3	-	1	350
Equity dividends	(33)	(70)	(33)	(33)	(31)	(2)	-	(1)	(203)
Share-based payments	-	-	-	-	(1)	-	-	-	(1)
Tax on share-based payments	1	1	-	1	-	-	-	-	3
Transfers (ii)	508	834	417	450	826	10	(1)	(15)	3,029
At 31 March 2006	980	1,506	847	940	1,016	-	(1)	(15)	5,273
Net income recognised directly in equity	2	3	1	1	1	-	-	-	8
Profit for the year	15	59	22	(8)	41	1	-	-	130
Equity dividends	(213)	(389)	(186)	(176)	(281)	(1)	-	-	(1,246)
Other movements in minority interests	-	-	-	-	-	-	-	(1)	(1)
Share-based payments	1	2	1	1	3	-	-	-	8
Tax on share-based payments	-	1	-	-	1	-	-	-	2
Transfers (ii)	7	15	9	8	9	-	-	1	49
At 31 March 2007	**792**	**1,197**	**694**	**766**	**790**	**-**	**(1)**	**(15)**	**4,223**

(i) The amount of net expense recognised directly in equity for the year ended 31 March 2006 has been restated to include tax on items taken directly to or transferred from equity, which was incorrectly shown separately in the 2005/06 regulatory accounting statements.

(ii) Transfers comprise the effects of changes in the allocation of assets and liabilities between the regulatory businesses over the financial year and the reallocation of funding movements related to the four DNs sold on 1 June 2005. Transfers in 2005/06 mainly comprise the reallocation of funding following the sales of the four DNs.

National Grid Gas is prohibited from declaring a dividend or other distribution unless it has certified that it is in compliance in all material respects with certain regulatory obligations, including a requirement to ensure it has sufficient financial resources and facilities to enable it to carry on its business and a requirement to use all reasonable endeavours to maintain an investment grade credit rating.

27. Cash flow statement

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

	North West DN 2007 £m	East of England DN 2007 £m	West Midlands DN 2007 £m	North London DN 2007 £m	Metering 2007 £m	Meter Reading 2007 £m	De-minimis activities 2007 £m	Other activities 2007 £m	Total 2007 £m	North West DN 2006 £m	East of England DN 2006 £m	West Midlands DN 2006 £m	North London DN 2006 £m	Metering 2006 £m	Meter Reading 2006 £m	De-minimis activities 2006 £m	Other activities 2006 £m	Total 2006 £m
Movement in cash and cash equivalents	(8)	(14)	(6)	(8)	(10)	-	-	(1)	(47)	30	47	23	27	27	-	-	1	155
Increase/(decrease) in financial investments	42	67	34	40	34	-	-	1	218	5	7	3	4	4	-	-	-	23
(Increase)/decrease in borrowings and derivatives	(258)	(391)	(193)	(248)	(155)	-	1	5	(1,239)	(602)	(942)	(467)	(532)	(610)	1	(1)	(11)	(3,164)
Net interest paid	43	68	34	38	40	-	-	1	224	21	35	17	19	33	-	-	-	125
Change in net debt resulting from cash flows	(181)	(270)	(131)	(178)	(91)	-	1	6	(844)	(546)	(853)	(424)	(482)	(546)	1	(1)	(10)	(2,861)
Changes in fair value of financial assets and liabilities	2	5	2	3	3	-	-	-	15	(4)	(6)	(3)	(3)	(6)	-	-	-	(22)
Net interest charge	(39)	(62)	(31)	(35)	(36)	-	-	(1)	(204)	(18)	(29)	(15)	(17)	(28)	-	-	-	(107)
Funding transfers (i)	4	7	5	4	4	-	-	-	24	529	868	435	475	843	(1)	-	-	3,149
Movement in net debt in the year	(214)	(320)	(155)	(206)	(120)	-	1	5	(1,009)	(39)	(20)	(7)	(27)	263	-	(1)	(10)	159
Net debt at the start of year	(458)	(711)	(352)	(402)	(409)	-	(1)	(10)	(2,343)	(400)	(659)	(329)	(357)	(639)	-	-	-	(2,384)
Impact of adoption of IAS 32 and IAS 39	-	-	-	-	-	-	-	-	-	(19)	(32)	(16)	(18)	(33)	-	-	-	(118)
Net debt at end of year	(672)	(1,031)	(507)	(608)	(529)	-	-	(5)	(3,352)	(458)	(711)	(352)	(402)	(409)	-	(1)	(10)	(2,343)
Comprising:																		
Cash and cash equivalents	22	34	17	19	17	-	-	-	109	30	48	23	27	27	-	-	1	156
Financial investments	48	76	38	45	39	-	-	1	247	6	9	4	5	5	-	-	-	29
Borrowings	(741)	(1,138)	(561)	(670)	(584)	-	-	(6)	(3,700)	(509)	(791)	(390)	(448)	(455)	-	(1)	(11)	(2,605)
Derivatives	(1)	(3)	(1)	(2)	(1)	-	-	-	(8)	15	23	11	14	14	-	-	-	77
	(672)	(1,031)	(507)	(608)	(529)	-	-	(5)	(3,352)	(458)	(711)	(352)	(402)	(409)	-	(1)	(10)	(2,343)

(i) Reallocation of funding. The funding transfers in the year ended 31 March 2006 largely arise following the sales of four DNs on 1 June 2005.

27. Cash flow statement (continued)

b) Analysis of changes in net debt

	At 1 April 2005 £m	Impact of adoption of IAS 32 and IAS 39 £m	Cash flow £m	Fair value gains and losses £m	Interest charges £m	Funding transfers (i) £m	At 31 March 2006 **£m**	Cash flow £m	Fair value gains and losses £m	Interest charges £m	Funding transfers (i) £m	**At 31 March 2007 £m**
Cash and cash equivalents	1	-	155	-	-	-	156	(43)	-	-	-	**113**
Bank overdrafts	-	-	-	-	-	-	-	(4)	-	-	-	**(4)**
	1	-	155	-	-	-	156	(47)	-	-	-	**109**
Financial investments	6	-	(36)	-	59	-	29	211	-	7	-	**247**
Borrowings	(2,391)	(148)	(2,986)	(46)	(164)	3,130	(2,605)	(914)	3	(208)	24	**(3,700)**
Derivatives	-	30	6	24	(2)	19	77	(94)	12	(3)	-	**(8)**
Net debt at end of year	(2,384)	(118)	(2,861)	(22)	(107)	3,149	(2,343)	(844)	15	(204)	24	**(3,352)**

(i) Reallocation of funding. The funding transfers in the year ended 31 March 2006 largely arise following the sales of four DNs on 1 June 2005.

28. Related party transactions

The following tables provide an estimated analysis of the incidence of National Grid Gas's transactions with related parties in these regulatory accounting statements. These related party transactions were in the normal course of business. Unless otherwise indicated, the related parties were other subsidiaries of National Grid. Additional information on related party transactions is provided in note 33.

	North West DN **2007 £m**	East of England DN **2007 £m**	West Midlands DN **2007 £m**	North London DN **2007 £m**	Metering **2007 £m**	Meter Reading **2007 £m**	De-minimis activities **2007 £m**	Other activities **2007 £m**	Total **2007 £m**	North West DN 2006 £m	East of England DN 2006 £m	West Midlands DN 2006 £m	North London DN 2006 £m	Metering 2006 £m	Meter Reading 2006 £m	De-minimis activities 2006 £m	Other activities 2006 £m	Total 2006 £m
Sales																		
Goods and services supplied	**1**	**1**	**1**	**1**	**-**	**9**	**5**	**5**	**23**	1	1	1	1	-	7	3	9	23
Expenditure																		
Services received	**20**	**28**	**15**	**18**	**1**	**-**	**-**	**1**	**83**	26	43	21	30	1	-	-	2	123
Corporate services received	**3**	**5**	**3**	**3**	**-**	**-**	**-**	**-**	**14**	2	3	2	2	-	-	-	-	9
Charges in respect of pension costs	**2**	**2**	**1**	**2**	**3**	**-**	**-**	**1**	**11**	5	3	3	1	1	-	-	1	14
Charges in respect of share based payments	**-**	**-**	**-**	**-**	**-**	**-**	**-**	**-**	**-**	-	1	-	-	-	-	-	-	1
Interest paid on borrowings from parent undertaking	**8**	**12**	**6**	**7**	**6**	**-**	**-**	**-**	**39**	1	2	1	1	1	-	-	-	6
Interest paid on borrowings from other group undertakings	**1**	**2**	**1**	**1**	**1**	**-**	**-**	**-**	**6**	3	4	1	3	1	-	-	-	12
	34	**49**	**26**	**31**	**11**	**-**	**-**	**2**	**153**	37	56	28	37	4	-	-	3	165

28. Related party transactions (continued)

	North West DN 2007 £m	East of England DN 2007 £m	West Midlands DN 2007 £m	North London DN 2007 £m	Metering 2007 £m	Meter Reading 2007 £m	De-minimis activities 2007 £m	Other activities 2007 £m	Total 2007 £m	North West DN 2006 £m	East of England DN 2006 £m	West Midlands DN 2006 £m	North London DN 2006 £m	Metering 2006 £m	Meter Reading 2006 £m	De-minimis activities 2006 £m	Other activities 2006 £m	Total 2006 £m
Outstanding balances at 31 March in respect of sales, expenditure and group tax relief																		
Amounts receivable	**3**	**11**	**3**	**3**	**24**	**-**	**-**	**1**	**45**	22	39	15	20	51	-	1	6	154
Amounts payable	**9**	**37**	**11**	**8**	**74**	**1**	**-**	**2**	**142**	13	26	9	12	36	-	-	3	99
Amount payable by parent due after more than one year																		
At 1 April	730	1,183	595	657	858	-	-	-	4,023	234	374	186	208	250	-	-	-	1,252
Advances	-	-	-	-	-	-	-	-	-	496	809	409	449	608	-	-	-	2,771
At 31 March	**730**	**1,183**	**595**	**657**	**858**	**-**	**-**	**-**	**4,023**	730	1,183	595	657	858	-	-	-	4,023
Borrowings from parent due within one year																		
At 1 April	-	1	-	-	-	-	-	-	1	14	23	11	14	38	-	-	-	100
Transfers	-	-	-	-	-	-	-	-	-	7	11	6	7	19	-	-	-	50
Advances	486	739	366	435	381	-	-	5	2,412	-	-	-	-	-	-	-	-	-
Repayments	(314)	(479)	(237)	(282)	(247)	-	-	(3)	(1,562)	(21)	(33)	(17)	(21)	(57)	-	-	-	(149)
At 31 March	**172**	**261**	**129**	**153**	**134**	**-**	**-**	**2**	**851**	-	1	-	-	-	-	-	-	1
Borrowings from fellow subsidiaries due within one year																		
At 1 April	2	2	1	2	1	-	-	-	8	9	15	8	9	26	-	-	-	67
Transfers	-	-	-	-	-	-	-	-	-	5	7	4	5	12	-	-	-	33
Advances	24	38	19	22	20	-	-	-	123	-	-	-	-	-	-	-	-	-
Repayments	-	-	-	-	-	-	-	-	-	(12)	(20)	(11)	(12)	(37)	-	-	-	(92)
At 31 March	**26**	**40**	**20**	**24**	**21**	**-**	**-**	**-**	**131**	2	2	1	2	1	-	-	-	8

Amounts receivable from or payable to related parties in respect of sales and expenditure are ordinarily settled one month in arrears. The amount receivable from the parent and due after more than one year is not subject to any specific settlement terms and does not bear interest. Borrowings from fellow subsidiaries are repayable on demand and bear interest at commercial rates.

No amounts have been provided at 31 March 2007 (2006: £nil) and no expense recognised during the year (2006: £nil) in respect of impairment of amounts due from related parties.

Details of guarantees provided in respect of related parties are provided in note 29(c).

Details of key management compensation are provided in note 6(c).

29. Commitments and contingencies

a) Future capital expenditure

	North West DN 2007 £m	East of England DN 2007 £m	West Midlands DN 2007 £m	North London DN 2007 £m	Metering 2007 £m	Meter Reading 2007 £m	De-minimis activities 2007 £m	Other activities 2007 £m	Total 2007 £m	North West DN 2006 £m	East of England DN 2006 £m	West Midlands DN 2006 £m	North London DN 2006 £m	Metering 2006 £m	Meter Reading 2006 £m	De-minimis activities 2006 £m	Other activities 2006 £m	Total 2006 £m
Contracted for but not provided	**81**	**66**	**63**	**57**	**5**	**-**	**-**	**-**	**272**	61	41	41	66	4	-	-	-	213

b) Lease commitments

Allocated total commitments in respect of non-cancellable operating leases are as follows:

	North West DN 2007 £m	East of England DN 2007 £m	West Midlands DN 2007 £m	North London DN 2007 £m	Metering 2007 £m	Meter Reading 2007 £m	De-minimis activities 2007 £m	Other activities 2007 £m	Total 2007 £m	North West DN 2006 £m	East of England DN 2006 £m	West Midlands DN 2006 £m	North London DN 2006 £m	Metering 2006 £m	Meter Reading 2006 £m	De-minimis activities 2006 £m	Other activities 2006 £m	Total 2006 £m
Payments due																		
In 1 year or less	**2**	**2**	**1**	**1**	**1**	**-**	**-**	**-**	**7**	3	5	1	2	-	-	-	1	12
Between 1 and 2 years	**1**	**2**	**1**	**1**	**-**	**-**	**-**	**-**	**5**	2	3	1	2	1	-	-	1	10
Between 2 and 3 years	**1**	**1**	**1**	**1**	**-**	**-**	**-**	**-**	**4**	2	2	1	1	-	-	-	1	7
Between 3 and 4 years	**-**	**1**	**-**	**1**	**-**	**-**	**-**	**-**	**2**	1	2	1	2	-	-	-	1	7
Between 4 and 5 years	**1**	**1**	**-**	**1**	**-**	**-**	**-**	**-**	**3**	2	2	1	1	-	-	-	-	6
In more than 5 years	**4**	**5**	**4**	**4**	**1**	**-**	**-**	**-**	**18**	7	11	7	8	2	-	-	3	38
	9	**12**	**7**	**9**	**2**	**-**	**-**	**-**	**39**	17	25	12	16	3	-	-	7	80

c) Other commitments and contingencies

The total value of other commitments, contingencies and guarantees of National Grid Gas plc at 31 March 2007 amounted to £213m (2006: £154m), including performance guarantees amounting to £6m (2006: £4m), relating to certain property obligations of a National Grid group undertaking, and BG Group related commitments and contingencies amounting to £7m (2006: £7m).

d) Parent company loan guarantees on behalf of subsidiary undertakings

National Grid Gas plc has guaranteed the repayment of principal sums, any associated premium and interest on specific loans due from its financial subsidiary undertakings to third parties. At 31 March 2007, the sterling equivalent amounted to £1,147m (2006: £1,430m).

30. Ultimate parent company

National Grid Gas plc's immediate parent company is National Grid Gas Holdings plc. The ultimate parent company, and controlling party, is National Grid plc, which is registered in England and Wales. Both National Grid Gas Holdings plc and National Grid plc consolidate the accounts of National Grid Gas plc. Copies of the consolidated accounts of National Grid Gas Holdings plc and copies of the consolidated accounts of National Grid plc may be obtained from the Company Secretary's Office, National Grid plc, 1-3 Strand, London WC2N 5EH.

31. Subsidiaries

The principal subsidiaries of National Grid Gas plc at 31 March 2007 and included in these regulatory accounting statements, either in whole or in part, are listed below.

	Country of operation and incorporation	Activity	Holding
National Grid Metering Limited	UK	Gas Metering Services	100%
British Transco International Finance B.V.	The Netherlands	Financing	100%
British Transco Finance Inc.	USA	Financing	100%
British Transco Capital Inc.	USA	Financing	100%
British Transco Finance (No 1) Limited	UK	Financing	100%
British Transco Finance (No 2) Limited	UK	Financing	100%
British Transco Finance (No 3) Limited	UK	Financing	100%
British Transco Finance (No 5) Limited	UK	Financing	100%
Xoserve Limited	UK	Gas transportation billing services	56.57%

A full list of all subsidiary and associated undertakings is available from the Company Secretary of National Grid Gas plc.

Definitions

bcm
Billion cubic meters

condition, the
Standard Special Condition A30 of either of National Grid Gas plc's Gas Transporter Licences

DN
Distribution Network

GAAP
Generally accepted accounting principles

group
National Grid Gas plc and its subsidiaries

HSE
Heath and Safety Executive

IAS
International Accounting Standard

IFRS
International Financial Reporting Standard

licence, the
Either of National Grid Gas plc's Gas Transporter Licences issued under the Utilities Act 2000

LNG
Liquefied natural gas

Lost time injury
A work-related injury which causes a person to be absent from work for at least one normal shift after the shift on which the injury occurs, because the person is unfit to perform his or her duties

mcm
Million cubic metres

National Grid
National Grid plc the ultimate parent company of National Grid Gas plc and its controlling party

National Grid Gas
National Grid Gas plc and/or its subsidiaries or any of them as the context requires

non-National Grid Gas business
Any business of National Grid that is not being undertaken by National Grid Gas or a subsidiary of National Grid Gas

NTS
The gas National Transmission System

Ofgem
The Office of Gas and Electricity Markets

tonnes CO_2 equivalent
Measure of greenhouse gas emissions in relation to the impact of carbon dioxide

TW
Terawatt, 10^{12} watts

TWh
Terawatt hours

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