Annual Report and Accounts 2009/10
National Grid Gas plc

Company number 2006000

Contents

Note on use of terms and abbreviations

Within these accounts, National Grid Gas plc is referred to by the abbreviation 'NGG', and National Grid plc, its ultimate parent company, by the abbreviation 'National Grid'. References to NGG, 'the Company', 'we', 'our' and 'us' refer to National Grid Gas plc itself, or to National Grid Gas plc and its subsidiaries collectively, as the context requires. A full glossary of terms used is included on page 84.

Operating and Financial Review

Operating and Financial Review contents

This Operating and Financial Review describes the main trends and factors underlying the development, performance and position of National Grid Gas plc (NGG) during the year ended 31 March 2010 as well as those likely to affect the Company in the future. 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.

Principal operations

NGG's principal operations are the ownership and operation of regulated gas infrastructure networks and the provision of gas metering services in Great Britain. NGG also has an interest in liquefied natural gas (LNG) storage facilities in Great Britain.

The performance of the principal businesses is reported by segment, reflecting the management responsibilities and economic characteristics of each activity. The principal businesses and segments, together with other activities, are as follows:

Businesses and segments	Description of principal activities
Gas Transmission	The transmission of gas in the UK as owner and operator of the gas national transmission system in Great Britain and storage facilities for LNG.
Gas Distribution	The distribution of gas as the owner and operator of four of the UK's eight gas distribution networks.
Gas Metering	The provision of regulated gas metering and meter reading services in Great Britain.
Other activities	Other activities do not constitute a segment in their own right, but comprise the provision of transportation transaction services on behalf of all the major gas network transportation companies, including those of NGG, together with corporate activities.

Gas Transmission

The Gas Transmission business comprises the following principal activities:

Gas Transmission owner
NGG owns the gas national transmission system in Great Britain. This comprises approximately 7,600 kilometres of high pressure pipe and 23 compressor stations, connecting to 8 distribution networks and to third party independent systems for onward transportation of gas to end consumers. As gas transmission owner, we own and maintain the physical assets, develop the networks to accommodate new connections and disconnections, and manage a programme of asset replacement and investment to ensure the long-term reliability of the respective networks.

Gas system operator
NGG operates the gas national transmission system. Day-to-day operation includes balancing supply and demand, maintaining satisfactory system pressures and ensuring gas quality standards are met. As gas transmission system operator, we undertake a range of activities necessary for the successful, efficient delivery of secure and reliable energy. To achieve this we ensure the system supply and demand is balanced at the end of each day. We are also required to

maintain levels of short-term gas reserves to ensure domestic and other non-interruptible gas supplies can be maintained during prolonged cold conditions.

LNG storage
NGG currently owns and operates 3 LNG storage facilities in Great Britain, following the closure of Dynevor Arms during 2009.

Gas Distribution
NGG's Gas Distribution business comprises four of the eight regional gas distribution networks in Great Britain. These networks comprise of approximately 132,000 kilometres of gas distribution pipelines. Gas is transported on behalf of approximately 26 active gas shippers from the gas national transmission system to around 10.8 million consumers.

We also manage the national gas emergency number (0800 111 999) for all of the gas distribution networks and for other transporters in Great Britain. This service, along with the enquiries line, appliance repair helpline and meter number enquiry service, handled over 3 million calls during 2009/10.

We are required to meet certain standards of service, which are established by Ofgem. These include: answering 90% of all calls to the national gas emergency number, enquiry line and meter number enquiry line within 30 seconds of the call being connected; attending 97% of reports of a gas escape or other gas emergency within the required timescale; and providing guaranteed standards of service for other transportation services, such as restoration of supply after an unplanned interruption and complaint handling. Compensation is payable for any failures to meet guaranteed standards of service.

Gas metering
The gas metering business, which is undertaken through NGG's subsidiary company National Grid Metering Limited, provides installation and maintenance services to gas suppliers in the regulated gas market. Services are provided for domestic, industrial and commercial gas meters situated throughout Great Britain.

National Grid Metering Limited is regulated by Ofgem and retains a large share of the legacy installed base of gas meters in the UK. It is subject to a tariff cap price control.

Other activities
Other activities include xoserve which delivers transportation transactional services on behalf of all the major gas network transportation companies in Great Britain, including National Grid. xoserve is jointly owned by the five major gas distribution network companies and NGG is the majority shareholder.

Organisation and structure

NGG is a subsidiary of National Grid plc (National Grid).

The continuing operations of National Grid are organised and managed by global lines of business, which include Transmission and Gas Distribution. The day-to-day management of National Grid's operations, and the execution of strategy as approved by the Board of National Grid, is carried out by the National Grid Executive Committee, which is composed of the Executive Directors of National Grid and its Company Secretary and General Counsel.

The Gas Transmission and Gas Distribution businesses of NGG form part of the global Transmission and Gas Distribution businesses of National Grid respectively.

The overall management and governance of NGG is the responsibility of its Board of Directors. The Board of Directors has established committees and sub-committees of the Board that assist it in its activities. These include the Transmission Executive Committee and the Distribution Executive Committee.

The day-to-day management of NGG's Gas Transmission business is carried on by the Transmission Executive Committee. This committee is chaired by Nick Winser, who is a Director of NGG, and who also sits on the Board and Executive Committee of National Grid and is the National Grid Executive Director responsible for the global Transmission business.

The day-to-day management of NGG's Gas Distribution business is carried on by the Distribution Executive Committee, chaired by Mark Fairbairn who is a Director of NGG, and also sits on the Board and Executive Committee of National Grid and is the National Grid Executive Director responsible for the global Gas Distribution business.

Certain activities, including safety, employee engagement and climate change, are reported on a line of business level rather than at company level. As a result, KPIs and objectives may be measured and monitored for the Transmission and Gas Distribution businesses rather than for NGG. This is discussed further under 'Vision, strategy and objectives' on page 7 and 'Performance against objectives' on page 10.

In addition to its own governance processes, NGG participates in the governance process of National Grid which is subject to the Combined Code on Corporate Governance.

More information on the business activities, organisation, structure, management and governance of National Grid can be found in the National Grid Annual Report and Accounts 2009/10 and on the National Grid website at www.nationalgrid.com. See note 30 on page 72 for further details of where these reports can be obtained.

External market

Markets in which NGG operates

The principal market in which NGG operates is the natural gas market in Great Britain.

The supply of natural gas in the UK is competitive in that consumers can choose their gas supplier. Those suppliers are then responsible for sourcing gas from gas extractors or importers as appropriate, as well as arranging for gas to be delivered through physical delivery networks. These networks, including the ones operated by NGG, are generally monopolies in their local areas as, for the majority of consumers, there are no alternative methods of receiving natural gas.

Natural gas delivery in the UK
Domestic and commercial consumers contract directly with gas suppliers who obtain the gas from shippers. Gas is transported through the national transmission system to regional gas distribution networks which deliver the gas to consumers on behalf of suppliers. Certain end users, primarily large industrial consumers, receive gas directly from the national transmission system, rather than through a distribution network.

NGG is the owner and operator of the gas national transmission system and of four of the eight regional gas distribution networks in Great Britain. We charge gas suppliers and gas shippers for our services.

The ownership of these four gas distribution networks that NGG does not own is set out in the table below.

Network	Owner (and parent where relevant)
Gas distribution networks in Great Britain (non National Grid)	
North of England	Northern Gas Networks
Scotland	Scotland Gas Networks (Scotia Gas)
South and South East England	Southern Gas Networks (Scotia Gas)
Wales and West of England	Wales & West Utilities

Other markets in which we operate
We also operate in gas related markets in the UK which are directly connected to our regulated businesses described above. Our legacy regulated metering business currently owns approximately 75% of the domestic gas meters in the UK. We also participate in the competitive market for the provision of LNG storage services in Great Britain.

Current and future developments

Market structure and ownership
There have been no significant changes in the structure of the UK gas infrastructure market or ownership during 2009/10.

Energy market developments
The UK energy markets continue to undergo developments driven by the projected increased reliance on imported gas and increased focus on security of supply.

The energy sector faces significant challenges relating to the declining gas reserves in the North Sea. Our latest forecast is that the UK will import around 46% of its gas requirements by 2010/11 and 69% by 2018/19. Other challenges include meeting the UK Government's targets on renewable generation, and the retirement of significant parts of the current generation capacity.

In November 2009, the Department of Energy and Climate Change (DECC) issued a consultation document on reforming the planning consent system for nationally significant energy infrastructure projects. The consultation period closed in February 2010 and the outcome is expected to be finalised later in 2010.

These changes are expected to impact our gas transmission and distribution networks and in particular will require significant investment to link new gas import facilities with domestic, business and industrial consumers.

More information on the external market can be found in the National Grid Annual Report and Accounts 2009/10 or on the National Grid's website at www.nationalgrid.com.

Regulatory environment

Due to NGG's position in, and importance to, the UK economy, NGG's gas transmission and distribution businesses are subject to UK and European Union laws and regulations.

Our gas transmission, distribution and metering 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 (GEMA), and has established price control mechanisms that restrict the amount of revenue that can be earned by regulated businesses.

We have six price controls comprising two for our gas transmission operations, one covering our role as transmission owner (TO) and the other for our role as system operator (SO); and one for each of our four regional gas distribution networks. The revenue that we can earn from charging for access to our UK gas systems is determined by formulas linked to the UK Retail Prices Index (RPI). These formulas are based upon Ofgem's estimates of operating expenditure, capital expenditure and asset replacement, together with an allowed rate of return on capital invested in the business, as measured by the regulatory asset value. They provide a financial incentive to operate and invest efficiently and also provide incentives by which we can gain or lose for our performance in managing system operation, in controlling internal costs, and for our service quality.

Gas Transmission
NGG holds a gas transporter licence in respect of the national transmission system in Great Britain. Under the Gas Act 1986, we have a duty to develop and maintain an efficient and economical pipeline system for the conveyance of gas. Our LNG storage business is managed as a separate business from the gas transmission business; however, some elements of its operations are regulated under our gas transporter licence.

Our price controls are typically reviewed every five years and the current price control covers the period 1 April 2007 to 31 March 2012. In December 2009, Ofgem announced that they intend to delay the implementation of the next control by one year to 2013; as a result the current control will need to be extended.

We accepted Ofgem's final proposals for the system operator scheme that applied to the year ended 31 March 2010 and we have also accepted their proposals for the one year scheme from 1 April 2010.

The key elements of the current price control is that we earn a 4.4% post-tax real rate of return on our regulatory asset value (equivalent to a 5.05% vanilla return), with a £0.9 billion baseline five year capital expenditure allowance and a £0.3 billion five year controllable operating expenditure allowance.

We are also subject to a number of incentives that can adjust our transmission network revenue. Our incentive schemes cover areas such as the cost of investment for additional capacity to facilitate new connections to the system.

Gas Distribution

We hold a single gas distribution transporter licence in the UK, which authorises us to operate the four gas distribution networks we own. Detailed arrangements for transporting gas are set out in the Uniform Network Code. This defines the roles and responsibilities of industry participants and is approved by Ofgem. Our four regional gas distribution networks each have a separate price control which determines the prices we can charge to gas shippers for our gas delivery service.

The current price control period came into force on 1 April 2008 and covers the period to 31 March 2013 providing for an allowed average revenue increase of 2% per annum above the retail price index and a 4.3% post-tax real rate of return (equivalent to 4.94% vanilla return) on our regulatory asset value. Ofgem's final proposals, at 2005/06 prices, allow a £1.6 billion five year operating expenditure allowance and a £2.5 billion baseline five year capital expenditure allowance split £1.8 billion for replacement expenditure and £0.7 billion for capital expenditure. In addition, the allowed formula revenue was decoupled from delivery volumes from 1 April 2007. This eliminated the sensitivity to warm weather and lower underlying volumes. Furthermore, from 1 October 2008 only a very small proportion of our income is recovered through the volume delivery component of our charges.

The price control formulas specify a maximum allowed revenue for each network. Each formula consists of a fixed core revenue element, cost pass-through items and a range of incentive schemes including: environmental emissions incentives; an exit capacity scheme; and innovation, environmental and community incentives.

The safety and reliability of the network is maintained principally by replacing older metallic gas main with polyethylene equivalents. Ofgem treats 50% of projected replacement expenditure as recoverable during the price control period and 50% as recoverable over future years. Each network is subject to its own main replacement incentive mechanism and retains 36% of any outperformance against Ofgem's annual cost targets as additional return or, alternatively, bears 36% of any overspend if it underperforms.

Transportation charges are set broadly to recover allowed revenue but in any year collected revenue can be more or less than allowed. Any difference is carried forward and our charges are adjusted accordingly in future periods.

Other regulation

NGG's businesses are also subject to safety legislation which is enforced by the Health and Safety Executive (HSE). Our UK gas operations work under a permissioning regime, whereby our organisation, processes and procedures are documented in safety cases that are subject to acceptance by the HSE.

In addition, as a company with debt securities listed on the London Stock Exchange and with a subsidiary with debt listed on the New York Stock Exchange, we are subject to regulation by the UK Financial Services Authority and the exchanges themselves, and are subject to rules governing an exemption from the filing requirements of the US Securities and Exchange Commission.

Energy policy, regulatory and other developments

UK and European energy policy

In May 2007 the UK government published a white paper entitled Meeting the Energy Challenge. This document set out the government's strategy to address the issues of climate change and the UK's increasing reliance on imported fuel. The strategy includes: carbon dioxide (CO_2) emission reductions of about 60% by 2050; security of supply; competition in energy markets in the UK and overseas; and adequate and affordable heating for every home.

In November 2008, the government enacted the Climate Change Act, making the UK the first country in the world to have a legally binding long-term framework to cut carbon emissions. The Act provided for targets for reductions in greenhouse gases of at least 80% by 2050, against a 1990 baseline. It also established a series of five year carbon budgets, and set up a Committee on Climate Change as an expert body to advise the government on those carbon budgets and to advise on the balance between actions to be taken at the domestic, European and international levels. In addition, in his 2009 Budget the then Chancellor Alistair Darling also promised to cut greenhouse gases by 34% by 2020 through the carbon budget provisions previously envisaged in the Act.

In 2009, the Department of Energy and Climate Change issued the UK Low Carbon Transition Plan, setting out plans to meet the 34% cut in emissions by 2020, including measures such as home energy efficiency and smart meters, and a target of 40% of the UK's electricity to be derived from low carbon sources, including nuclear, by 2020.

In December 2008, the European Union approved a number of environmental proposals. Legally binding national targets have been established that dictate the proportion of energy production to be provided from renewable sources by 2020. For the UK the target is 15%. In order to achieve this it is believed the proportion of electricity generated by renewable sources will need to rise to around 35%.

Regulatory developments

During the year ended 31 March 2010, there were no significant legislative changes in the UK relating to utility regulation.

In March 2008, Ofgem announced a review of the current RPI-X based regulatory framework. The RPI-X@20 review is an assessment of the current regulatory regime and its ability to address the challenges facing energy networks in the future. Ofgem's intention was for the output from this project to feed into the future price controls. To allow the output of RPI-X@20 to be fully incorporated into the next full transmission price control review, the current transmission price control will be rolled over one year and extended to March 2013. The current gas distribution price control is also scheduled to end in March 2013. The outcome of this review is unlikely to impact our current regulatory settlements, but could influence future price controls from 2013.

In early 2009, Ofgem launched Project Discovery, an examination of the prospects for secure and sustainable energy supplies over the next 10 to 15 years. We will continue to work with Ofgem as they consult on their range of options.

The European Commission's third legislative package of proposals for the European gas markets was passed in July 2009 and must now be implemented into UK domestic legislation by April 2011. The new legislation consists of two directives on rules for the internal gas and electricity markets, two regulations on conditions for access to those markets, and one regulation establishing an Agency for the Cooperation of Energy Regulators. The original legislation, published in September 2007, contained measures to force energy companies to unbundle their transmission businesses from supply and generation activities. The final proposals include alternatives to full unbundling. In summer 2009, the European Commission published an initial proposal for a regulation concerning security of gas supply, and National Grid has worked closely with the UK government and through Gas Infrastructure Europe to help in its development. The legislative processes are expected to be complete by the end of 2010. Key features on the new proposed regulation include improving information flows and coordination of actions in an emergency.

Price control

The price controls for the UK gas transmission business were due to be reviewed during 2010 and 2011 but they have been delayed by a year and are now expected to be implemented in April 2013.

We were subject to one year system operator price controls for our gas transmission operations for 2009/10, and new one year controls have been agreed for 2010/11.

Other developments

Security of supply and climate change

We are focused on the long-term security of supply and environmental challenges arising from the transition to a low carbon economy and the decline of the UK's gas production from the North Sea. We are also working with governmental and regulatory bodies to ensure we help facilitate the implementation of the new climate change initiatives and policy being developed around integrating increasing amounts of renewable energy.

Legal and related matters

An update on the ongoing Metering competition investigation that was reported in last year's Annual Report and Accounts and the gas distribution main replacement investigation is provided on page 22.

National Grid plc rights issue

On 20 May 2010, the Board of National Grid plc announced a fully underwritten rights issue to raise approximately £3.2 billion, net of expenses. The issue closed on 11 June 2010. The proceeds are expected to be used to fund a portion of National Grid plc's capital investment programme and for general corporate purposes.

External relationships

We aim to enhance our relationships with all of our external stakeholders including customers, regulators, governments, suppliers and the communities in which we operate.

Responsibility

Our reputation depends on the trust and confidence of our stakeholders. We will only earn this by working to the highest standards, by trusting our employees to do the right thing and by running our Company responsibly and sustainably.

National Grid's Framework for Responsible Business, in which NGG participates, first published in 2002, has been extensively revised this year to provide a clearer line of sight from National Grid's vision to how we manage our business and our day-to-day dealings with our stakeholders. Our company-wide policies and position statements, available on National Grid's website, underpin the Framework.

National Grid's Standards of Ethical Business Conduct provide a common set of practical guidelines to help ensure that our behaviours are lawful, comply with our policies and licences, and follow the values set out in the Framework and our core values. We undertake online training for employees annually to ensure they understand the Standards.

More information on National Grid's approach to corporate responsibility and business ethics is included in the Corporate Governance section of the National Grid plc Annual Report and Accounts 2009/10.

Investors

As a subsidiary company of National Grid, NGG participates in communications to both National Grid's equity shareholders and to holders of debt in NGG, supporting National Grid's programme of active communication.

Customers

We aim to treat customers with respect, to communicate clearly with them, and to make their interactions with us as straightforward as possible. We aim at all times to provide a safe, reliable and efficient service to our customers. We have a very wide range of customers, including: gas shippers, local distribution companies; and industrial, commercial and domestic consumers.

In 2009, we sought feedback from our transmission customers to understand what it was like to do business with us. They told us in a lot of cases we perform well and are knowledgeable about the industry. However, in a number of cases we let them down by our actions – including not communicating effectively and not being accessible. Using the data we gathered, a programme for 2010 has been developed to drive change in our customer focus. The programme sets out clear commitments to our customers, is driven and supported by senior management, and provides accountability and ownership for our employees.

A customer focused Transmission business will ensure we can be flexible in meeting the challenges of our changing customer base. It will allow us to respond proactively to customer requirements by meeting requests wherever we can. In cases where the regulatory frameworks prevent us from doing so, we will explain clearly the reasons and will work with the industry to adapt the frameworks for the future.

In UK Gas Distribution, we have a programme to improve customer service levels. This includes increased staff training, reviewing our processes to make them more customer focused, and a review of all our communications with customers. In addition, we are providing increased support to leaders to assist them as they engage with employees on the importance of customer service. An example of this is a short film that has been produced explaining the important role that all employees play in delivering an excellent customer service.

We recognise the difficulties the current state of the economy has caused many of our customers. We understand we have an obligation to balance the payment needs of our customers with our financial responsibility to our shareholders, our regulatory commissions and our remaining customer base. To help balance these needs, we have been implementing a comprehensive bad debt mitigation strategy which includes focusing on early intervention and customer risk segmentation allowing us to better match appropriate collection strategies to individual customers.

Regulator

Our regulator Ofgem is concerned with ensuring we can and do provide a safe, reliable and efficient service to our customers. Our ability to deliver that service, and to deliver returns to our investors, depends on our relationship with the regulator. Our focus on customer service and operational excellence is a critical component of our relationship with our regulator, underpinning the building of trust. This involves being responsive to the needs of our regulators for high quality information, complying with rules and regulations, operating in an ethical way, responding constructively to consultations and, most importantly, delivering on our promises. We continue to work very closely with Ofgem on the renewal of our gas transmission and gas distribution networks, and on expanding those networks to meet new and changing demand.

Suppliers

We aim to work in partnership with our suppliers, developing constructive relationships and working together effectively. Our objective is to develop contractual arrangements with our suppliers that align their interests with our own as far as possible and share financial risks appropriately.

Considering the environmental impact as part of our procurement decision making is key to developing our leadership position on climate change issues. We are developing a strategy to measure and reduce our supply chain carbon emissions.

Community involvement

We continue to participate in National Grid's community involvement programmes, details of which can be found in the National Grid plc Annual Report and Accounts 2009/10.

Vision, strategy and objectives

As described under ‘Organisation and structure’ on page 2, National Grid’s businesses are managed on the basis of global lines of business. As a subsidiary company of National Grid, therefore, NGG participates in the National Grid vision and strategy. The following section describes National Grid’s vision and strategy to the extent that it relates to NGG. Further details and discussion of the strategy and objectives of National Grid can be found in the National Grid Annual Report and Accounts 2009/10.

Vision

The vision is the long term aspiration for National Grid – what we want to be in the future.

We, at National Grid, will be the foremost international electricity and gas company, delivering unparalleled safety, reliability and efficiency, vital to the well-being of our customers and communities.

We are committed to being an innovative leader in energy management and to safeguarding our global environment for future generations.

Strategy

Our strategy is a medium term step in the journey towards the vision – what we are doing over the next few years. It is also the over arching principle that provides commercial context to each of the objectives. We will build on our core regulated business base and financial discipline to deliver sustainable growth and superior financial performance.

Objectives

The objectives are the building blocks of the strategy and are fundamental to our business - what we are doing now.

- Driving improvements in our safety, customer and operational performance
- Delivering strong, sustainable regulatory and long-term contracts with good returns
- Modernising and extending our transmission networks
- Becoming more efficient through transforming our operating model and increasingly aligning our processes
- Building trust, transparency and an inclusive and engaged workforce
- Developing our talent, leadership skills and capabilities
- Positively shaping the energy and climate change agenda

Line of sight

Line of sight links the vision, strategy and National Grid objectives to all our employees’ individual objectives – how what each of us does contributes to the success of the National Grid.

Our vision, strategy and Company objectives are the foundation of the annual priorities of each line of business and function.

These annual priorities form the basis of the objectives of the Executive Directors and senior managers, and then flow down the organisation to the individual objectives of every manager and employee. Consequently, the actions required to deliver the strategy are allocated and aligned with employee responsibilities.

Our aim is that every employee is able to trace their objectives through to National Grid’s objectives, strategy and vision.

Delivering the future through our strategy

We will seek to grow through replacing and expanding our core networks and investing in other organic growth opportunities relating to climate change and security of supply. In developing the future UK and EU policy and regulatory framework, we will actively influence the energy policy agenda and endeavour to position ourselves as the go-to company for current and new governments both with regard to expert opinion on matters relating to UK energy policy and climate change, and as the company of choice for delivering large energy infrastructure projects. We will look to ensure that future price controls reflect the need for substantial and timely investments to ensure climate change targets and security of supply requirements are met, while delivering acceptable and timely rates of return.

Transmission UK strategy – investment led organic growth by:

- Delivering a step change in asset replacement of our transmission infrastructure
- Delivering major new infrastructure investment to facilitate low carbon targets in the UK

Gas Distribution UK strategy – investment led organic growth by:

- Improving operating efficiency, safety and customer satisfaction through Gas Distribution front office (see page 13)
- Successfully defending our position through the next price control review

Values

This year we are emphasising the link between the line of sight and our values. It is important that we judge our achievements not just on what is delivered but also on how it is done. Our core values are: respect others and value their diversity; take ownership for driving performance; demonstrate integrity and openness in all relationships, and work as one team, one National Grid.

Responsibility

National Grid's vision, strategy and objectives are underpinned by its commitment to corporate responsibility. National Grid will operate to the highest standards of corporate governance and conduct its business in an ethical and sustainable manner.

Business drivers, risks and opportunities

Business drivers

There are many factors that influence the success of our business and the financial returns we obtain. We consider the factors described here to be our principal business drivers.

Price controls
The prices we charge for use of our gas transmission and distribution networks are determined in accordance with regulator approved price controls. These arrangements include incentives and/or penalty arrangements. The terms of these arrangements has a significant impact on our revenues.

People
The skills and talents of our employees, along with succession planning and the development of future leaders, are critical to our success. We believe that business success will be delivered through the performance of all current and future employees, and enhanced by having a workforce that is diverse in its cultural, religious and community influences.

Capital investment
Capital investment is a significant driver for organic growth. In our regulated gas networks, the prices we charge include an allowed return for capital investment determined in accordance with our price controls.

Safety, efficiency and reliability
Our ability to operate safely and reliably is of paramount importance to us, our employees, our contractors, our customers, our regulators and the communities we serve. Our financial performance is affected by our performance in these areas. Operating efficiently allows us to minimise prices to our customers and improve our own financial performance.

Relationships and responsibility
Our reputation is vitally important to us. We only earn the trust and confidence of our stakeholders by conducting business in a responsible manner. The quality of our customer service feeds through to the attitudes of regulators and is also linked to our financial performance. Our reputation depends on our behaviours being lawful and ethical, on complying with our policies and licences, and on living up to our core values.

Risks and opportunities

There are a number of risks that might cause us to fail to contribute to National Grid's vision or to deliver growth in its shareholder value. We can mitigate many of these risks by acting appropriately in response to the factors driving our business. The principal risks are described here. For more details on risks, see pages 22 to 24.

Regulatory settlements and long-term contracts
Our ability to obtain appropriate recovery of costs and rates of return on investment is of vital importance to the sustainability of our business. We have an opportunity to help shape the future of the regulatory environment, for example in our participation in RPI-X@20. If we fail to take these opportunities, we risk failing to achieve satisfactory returns.

Financial performance
Financial performance and operating cash flows are the basis for funding our future capital investment programmes, for servicing our borrowings and paying dividends. Failure to achieve satisfactory performance could affect our ability to deliver the returns we and our stakeholders expect.

Talent and skills
Harnessing and developing the skills and talent of our existing employees, and recruiting, retaining and developing the best new talent, will enable us to improve our capabilities. Failure to engage and develop our existing employees or to attract and retain talented employees could hamper our ability to deliver in the future.

Investment in our networks
Our future organic growth is dependent on the delivery of our capital investment plans. In order to deliver sustainable growth with superior financial performance we will need to finance our investment plans. Instability in the financial markets, loss of confidence by investors, or inadequate returns on our investment may restrict our ability to raise finance.

Safety, reliability and customer service
The operating profits and cash flows we generate are dependent on operating safely and reliably, and providing a quality service to customers. If we fail to meet our regulatory targets or the high standards we set ourselves, we risk loss of reputation as well as financial penalties imposed by regulators

Efficiency
Transforming the way we operate by simplifying and standardising our systems and processes will drive efficiency and reduce costs. Transforming our operating model will enable us to deliver increased value to shareholders. Conversely, if we do not achieve this transformation, or associated benefits in efficiency, then shareholder value will not grow as we hope or will diminish.

Sustainability and climate change
Safeguarding our global environment for future generations is dependent on integrating sustainability and climate change considerations into our business decisions, influencing legislators and regulators to reshape energy markets to address climate issues, and helping our employees, customers and suppliers to change their behaviour to be more environmentally responsible.

Key performance indicators (KPIs)

Our performance and the progress we have made against the objectives we have set ourselves are described below and on the following pages. We measure the achievement of our objectives both through the use of qualitative assessments and through the monitoring of quantitative indicators. To provide a full and rounded view of our business, we use non-financial as well as financial measures. Although all these measures are important, some are considered to be of more significance than others, and these more significant measures are designated as KPIs. Our financial and non-financial KPIs are highlighted here. KPIs are used as our primary measures of whether we are achieving our principal strategic aims of sustainable growth and superior financial performance. We also use KPIs to measure our performance against objectives; the relationships between the objectives and the KPIs is explained below. Details of other performance measures are included under Performance against objectives on page 10.

Objective	KPI/performance measure	Description and performance		Target
Financial KPIs				
Delivering superior financial performance	Adjusted operating profit	Operating profit excluding exceptional items and remeasurements **2009/10: £1,297 million** 2008/09: £1,091 million		Year on year profit increase
Delivering strong sustainable regulatory contracts with good returns	Operational return	Gas Transmission and Gas Distribution operational return against the target set by our regulator for the 5 year price control period		Achieve or exceed regulatory allowed return over 5 year price control period of:
		Gas Transmission **2009/10: 7.6%** 2008/09: 6.9%	Gas Distribution **2009/10: 6.3%** 2008/09: 5.7%	Gas Transmission 5.05% Gas Distribution 4.94%
Non-financial KPIs				
Driving improvements in safety, customer and operational performance	Employee lost time injury frequency rate	Number of employee lost time injuries per 100,00 hours worked on a 12 month basis		Zero
		Gas Transmission **2009/10: 0.16** 2008/09: 0.33	Gas Distribution **2009/10: 0.08** 2008/09: 0.23	
Modernising and extending our transmission and distribution networks	Network reliability	Reliability of Gas network as a percentage against the target set by our regulator		
		Gas Transmission **2009/10: 100%** 2008/09: 100%	Gas Distribution **2009/10: 99.999%** 2008/09: 99.999%	Gas Transmission 100% Gas Distribution 99.999%
Building transparency, trust and an inclusive and engaged workforce	Employee engagement index	Employee engagement index calculated using responses to National Grid's annual employee survey		Year-on-year increase
		Transmission business: **2009/10: 77%** 2008/09: 82%	Gas Distribution business: **2009/10: 68%** 2008/09: 70%	
Positively shaping the energy and climate change agenda	Greenhouse gas emissions	Percentage reduction in greenhouse gas emissions against our 1990 baseline Year-on-year reduction % **2009/10: 15%*** 2008/09: 4%		Year-on-year reduction

*Greenhouse gas emissions for 2009/10 are not fully verified at the date of this report. Fully verified data will be published on the National Grid plc website in July 2010.

Performance against objectives

We use a number of detailed performance measures in addition to the key performance indicators shown on the previous page, reflecting the scale and complexity of our operations. We use qualitative assessments to judge progress against our objectives in areas where numerical measures are less relevant.

Performance measures and strategy

National Grid's strategy is stated on page 7. NGG's performance in implementing the key elements of the strategy is measured in the following ways.

Efficiency and reliability

We invest in our existing business in order to improve efficiency and reliability. The KPI in this area is network reliability (see previous page) and other performance measures include capital investment (see page 12).

Financial discipline

We seek to control operating costs, and to invest capital only where we expect to be able to obtain an acceptable return. Our KPI in this area is operational returns (see previous page).

There are a number of factors that determine the extent to which growth is sustainable. We believe that operational excellence will help us to build and maintain good relationships with our customers and regulators. Managing the skills and talents of our employees helps us to recruit, retain and develop the best possible talent, creating a diverse and motivated workforce and positioning ourselves to take advantage of present and future opportunities.

Sustainable growth

Our KPIs in this area, as shown on page 9, are employee lost time injury frequency rate, employee engagement and greenhouse gas emissions. Other performance measures include; measures of gender and ethnic mix, the number of significant direct environmental incidents and value of environmental fines, together with our participation in bodies such as the RPI-X@20 advisory panel.

Financial performance

NGG aims to increase adjusted operating profit each year. Adjusted operating profit for 2009/10 was £1,297 million compared to £1,091 million in 2008/09, an increase of £206 million. Adjusted operating profit excludes exceptional items and remeasurements.

A more detailed analysis of financial performance is provided on page 14.

Driving improvements in safety, customer and operational performance

NGG aims for operational excellence by performing to the highest standards of safety and reliability and by improving customer service.

Safety

Safety is critical both to business performance and to helping to define the culture of NGG for our employees.

We recognise that our operations potentially give rise to risk and believe that we can eliminate or minimise those risks to achieve zero injuries or harm and to safeguard members of the public. NGG further believes that everyone, collectively and individually, has a part to play in achieving that aim.

Employee safety

We report our employee lost time injury frequency rate, expressed as lost time injuries per 100,000 hours worked, as a key measure that can be compared with other companies. This takes into account the number of employees and the hours worked. As well as reporting our lost time injury frequency rate, NGG also reports the number of lost time injuries.

During 2009/10 the number of lost time injuries was 11 compared with 28 in 2008/09. 2009/10 saw a significant reduction in our lost time injury frequency rate to 0.08 compared with 0.15 in 2008/09.

Definitions for lost time injury and lost time injury frequency rate are included in the glossary on page 84.

The principal causes of lost time injuries are road traffic collisions, musculoskeletal injuries and slips, trips and falls. National Grid has implemented targeted programmes during the year to change behaviours in these areas and drive performance improvements.

In Gas Transmission, during 2009/10 there were 2 lost time injuries compared with 4 in 2008/09. The lost time injury frequency rate was 0.16 in 2009/10 compared with 0.33 in 2008/09.

In Gas Distribution, lost time injuries totalled 9 in 2009/10. This is equivalent to a lost time injury frequency rate of 0.08. This compares with a total of 24 lost time injuries in 2008/09, equivalent to a lost time injury frequency rate of 0.23.

We have a programme to decommission older metallic gas main and replace it with polyethylene. The majority of this programme relates to targets agreed with the Health and Safety Executive (HSE), to replace all iron main within 30 metres of property by 2032. In 2009/10, we decommissioned more than 2,000 kilometres of metallic main, around 1,940 kilometres of which related to the HSE target, exceeding the target for the fourth consecutive year. The target for 2009/10 was 1,856 kilometres. We decommissioned over 1,850 kilometres in each of 2008/09 and 2007/08.

We identified that some of our UK main replacement activity may have been misreported. We have notified both Ofgem and the HSE, and Ofgem's investigation into this matter continues.

In Gas Metering, there was 1 employee lost time injury in 2009/10 compared with 1 in 2008/09.

Contractor safety

We believe that everyone who works for National Grid is entitled to high levels of safety, whether they are a direct employee or employed by one of our contract partners. In 2009/10, there were 16 contractor lost time injuries compared to 20 in 2008/09 and a target of zero. When developing safety improvement programmes, we ensure that our contract partners are actively involved and believe there is a mutual benefit in sharing good practice and learning.

Public safety
The safety of the public in the communities we serve is of prime importance to us. In 2009/10, 30 members of the public were injured as a result of our operations compared with 25 during 2008/09 and a target of zero. A single incident, involving a gas explosion in a property in Shrewsbury, UK, caused 12 of these injuries. Our gas mains replacement programme, the purpose of which, is to reduce the safety risk relating to older metallic main is described on the previous page.

Process safety
Operating major hazard sites means managing process safety risks is always a prime consideration in the way we run our business. We aspire to be an industry leader in this area.

Process safety incidents are relatively rare and often have catastrophic consequences. As such, counting the number of incidents is not a good indicator of performance.

During 2009/10, we have continued to develop and report comprehensive leading and lagging indicators to measure that process safety risks are under control.

Employee health
Over the year, NGG's sickness absence rate increased to 3.04% compared with 2.52% in 2008/09. The gathering and structuring of absence data has improved to provide more accuracy and detail. This helps inform our health and wellbeing programmes. This year, all National Grid employees have had an opportunity to engage with health and wellbeing programmes. Further information can be found in the National Grid plc Annual Report and Accounts 2009/10.

Reliability
NGG's principal operations are critical to the functioning of the UK economy. The reliability of our network is one of the highest priorities after safety.

Our approach to maintaining and improving reliability involves investing in infrastructure and systems to provide the operational tools and techniques necessary to manage our assets and operations to high standards; investing in the renewal of assets; investing in the skills and capabilities of our people to give them the ability to operate our networks to a high degree of service excellence; and maintaining a constant focus on reliability as one of our principal objectives, ensuring we are proactive about planning to ensure reliability and that we react quickly to factors that could compromise reliability.

Our reliability and availability performance during the year can be summarised as follows:

Network reliability information for Gas Transmission and Gas Distribution is summarised below.

Years ended 31 March	2010	2009
Gas Transmission network reliability target 100%	100%	100%
Gas Distribution network reliability target 99.999%	99.9999%	99.9999%

In the Gas Transmission system, total gas transmitted amounted to 1,150 TWh compared to 1,158 TWh in 2008/09. The winter of 2009/10 saw a maximum gas demand of 465 million standard cubic metres on 8 January 2010. This compares to the previous years' peak of 443 standard cubic metres.

Gas compressor fleet performance improved in 2009/10, with the mean time between compressor failures of 698 hours compared to 405 hours in 2008/09.

In the Gas Distribution networks, actual gas consumption in 2009/10 was 299 TWh compared with 317 TWh.

In Gas Distribution, we again achieved a very high network reliability percentage of 99.999%, which reflects a low volume of unplanned customer interruptions during the year.

We continue to focus on improving reliability, in particular in the area of gas escapes. We met the regulatory standards of service in the area of gas escapes in three out of four networks. We missed the target in the fourth network by 0.02%.

Our asset management policies promote continual improvement in how our physical assets (plant, pipes, meters and regulators) are managed throughout their life cycle from conception through construction, operation, maintenance and decommissioning.

Customer service
NGG aims 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.

Gas Distribution
The quality of service standards defined by Ofgem apply to three principal areas of activity: new connections; the telephone service; and attendance at gas emergencies. All standards have been met in 2009/10, with the exception of one gas emergency standard in one network affected by the severe winter weather where we achieved 96.98% against a standard of 97.00%. In individual cases where compensation is due as a consequence of failing to meet certain standards, NGG has processes to ensure that customers receive the statutory compensation to which they are entitled. Customer satisfaction with the levels of service provided in respect of NGG's main types of work (emergency response and repair, planned work and connections work) is measured and reported on a quarterly basis. Results of these surveys are comparable with the other distribution network operators and can be found at www.nationalgrid.com and www.ofgem.gov.uk. There is a

programme of activities within the UK to improve these scores further.

Gas Metering
Gas Metering has met 17 out of 18 standards of service in 2009/10.

Delivering strong, sustainable regulatory and long-term contracts with good returns

We will work with Ofgem and the UK government to develop the changes that are required to address climate change and security of supply in a way that is affordable for consumers and ensures timely delivery while also ensuring adequate returns for our investors.

Significant levels of investment over the next few years mean that it is vital that we optimise our regulatory returns and ensure we are appropriately compensated for our investments.

The overall regulatory framework, and the price controls which form part of this framework, provide the environment that enables us to be confident that where we act efficiently and economically and in the consumers' interest then we will receive appropriate returns.

We are actively participating in Ofgem's review of the current RPI–X based regulatory framework, which is discussed on page 3. In addition to our responses to the various consultation documents, we are also participating in the four industry working groups that Ofgem has established: innovation, investment, financing, and consumers. Ofgem anticipate that the outcome of the project will be published toward the end of 2010. It will not have any impact on the present price control, other than necessitating a one year adapted rollover of the existing price control, but it is expected that its conclusions will feed through into the review for the price control commencing April 2013.

Our aim is to meet or exceed the base financial returns in our price controls. The performance measure we use to monitor return on investment is the vanilla return. We measure the financial performance of our regulated businesses using an operational return metric comparable to the vanilla return defined in the price controls from 1 April 2007.

Details of these returns are summarised below.

Years ended 31 March	2010	2009
Gas Transmission operational return	7.6%	6.9%
Gas Distribution operational return	6.3%	5.7%

In Gas Transmission we significantly outperformed regulatory assumptions mainly as a result of a strong performance under our incentive schemes. Gas Distribution also outperformed its regulatory allowance.

Modernising and extending the network

We aim to invest the amount required to maintain a safe and reliable system, and to accommodate new patterns of supply and demand. Capital investment is one of the principal drivers to future growth.

The principal measure we use to monitor organic investment is capital expenditure, which includes investment in property, plant and equipment as well as internally created intangible assets such as software.

Our capital investment plans reflect changing energy infrastructure requirements. Our capital investment programme takes place within defined regulatory frameworks that permit us to earn a return on allowed investments.

Capital investment
Total capital expenditure during 2009/10 was £972 million compared to £1,080 million in 2008/09. More detail on capital expenditure by business is provided below.

Gas Transmission
Investment in gas transmission systems is, by its nature, variable and is largely driven by changing sources of supply and asset replacement requirements. The gas transporter licence also obliges us to provide connections and capacity on request.

Parts of the gas transmission network are reaching the end of their technical lives. These are mainly compressor stations, control systems and valves. This, together with work required to meet changing supply sources, means that the gas transmission business will continue to see a significant increase in investment and network renewal.

Capital investment in the replacement, reinforcement and extension of the Gas Transmission system in 2009/10 was £232 million, compared with £389 million in 2008/09. This mainly related to load related infrastructure on the gas transmission system. Capital investment included £13 million with respect to intangible assets, principally software applications (2008/09: £18 million).

Gas Distribution
Gross Capital investment including reinforcement, extension and replacement of the gas distribution network was £670 million in 2009/10 compared with £598 million in 2008/09. Of these amounts, £465 million in 2009/10 related to replacement expenditure that is capitalised (2008/09: £425 million) and £205 million to other capital investment (2008/09: £173 million). Expenditure on software applications included within the above amounts was £54 million (2008/09: £22 million). The increase in expenditure is primarily driven by the Gas Distribution front office system (see page 13).

Replacement expenditure increased by £40 million (9%) compared with 2008/09 reflecting an increase in workload in London ahead of the 2012 Olympics and a higher proportion of complex large diameter main. Performance under the mains replacement incentive scheme is expected to be broadly neutral in 2009/10.

In collaboration with gas alliance and coalition partnerships, NGG has replaced more than 2,000 kilometres of metallic gas main this year and more than 14,000 kilometres since 2002/03.

The vast majority of this relates to the long-term main replacement programme agreed with the Health and Safety Executive (HSE).

The increase in other capital expenditure in 2009/10 compared with 2008/09 is driven by: the spend on the replacement of Gas Distribution front office systems, work that will continue until 2011/12; completion of a major new pipeline in west London; and expenditure primarily to maintain the reliability of our gas networks.

Gas Metering
Capital expenditure invested in new and replacement meters in 2009/10 amounted to £65 million compared with £90 million in 2008/09.

In the UK, we have identified significant capital requirements over the medium term. These requirements are primarily driven by the need to replace ageing infrastructure, reinforce the network to accommodate changing sources of supply and connect new generation, including renewables.

Becoming more efficient by transforming our operating model and increasingly aligning our processes

We aim to work as one company, operating to common core principles, standards and policies to deliver National Grid's vision.

In Transmission, our common operating model project is developing a plan to prepare us for the challenges and opportunities between now and 2020. In Gas Distribution, our front office systems project aims to provide the tools to improve our performance, making them simpler to use and apply to improve our service to customers.

Business process outsourcing
National Grid announced on 8 October 2009 that, following an extensive review, we proposed to outsource some of our UK shared services activities to an external service provider. The outsourcing is expected to deliver significant benefits, process efficiencies and continuous improvement over a five year period. It will result in a reduction of around 300 agency and permanent positions and the closure of our Newcastle site. The phased transfer of activities has begun and is expected to continue throughout 2010.

Across National Grid operations, there are global functions, such as information systems and procurement which provide a common strategy, policy and key processes to drive consistency, efficiency and effectiveness. Further information can be found in the National Grid plc Annual Report and Accounts 2009/10.

Gas Transmission
Much of the focus for Transmission has been on preparing for the significant increase in capital investment that is expected in future years, including developing the longer term investment plan.

We have continued to focus on incremental efficiencies and are committed to further improving the levels of efficiency in our operations. This is how we will reduce controllable costs on an enduring basis contributing to an improved financial performance.

Gas Distribution
Our objective is to utilise the benefits of common support services to drive improvements in our operating and financial performance. In particular, we aim to adopt best practices across Gas Distribution.

The key initiatives aimed at reducing our controllable operating costs and improving efficiency are material and process standardisation, process improvements, consolidation of workforce and best practice sharing.

We are making good progress on our implementation of a new front office system for Gas Distribution in the UK. The first release of the new integrated IT solution is on track for implementation in the autumn of this year and will cover the maintenance and an early release of the emergency service solution. The full deployment of the emergency service solution will take place in the spring of 2011. We have also started the designs for the customer, repair and construction processes and will deploy these parts of the new solution during the summer and autumn of 2011.

The new enhanced capability will create a much simpler way for our people to do their work, enabling us to streamline our processes and standardise the way common functions like scheduling and dispatch are performed. This will improve productivity, provide greater assurance and controls on our performance and significantly improve our customer service.

The functionality of the new systems, which includes global positioning system (GPS) locations of our field teams and work locations, will drive improvements in efficiency. We will also have much greater visibility of work we undertake for customers and be able to provide improved response to requests to do work and customer enquiries about work in progress.

Our aim is to maintain the proper level of investment in our infrastructure to enable related operating cost reductions.

Building trust, transparency and an inclusive and engaged workforce

To better recruit, retain and develop talented people, we endeavour to engage our employees and to achieve a more inclusive workplace and diverse workforce, reflecting the composition of the communities in which we operate. Our goal is to be seen as an employer of choice across all communities.

Employee engagement
In February 2010, National Grid conducted its third annual employee survey. The response rate was the highest so far, representing 97% of National Grid's workforce.

Action plans are being developed and will form part of the management annual objective process for 2010/11 to ensure we further build upon the very encouraging survey response rate and these survey results.

Within NGG we monitor the engagement scores for the principal lines of business, Transmission and Gas Distribution. In 2009/10, Transmission employee engagement was 77% (2008/09: 82%) and Gas Distribution employee engagement was 68% (2008/09: 70%).

Inclusion and diversity

We use performance measures including the percentage of female and ethnic minority employees, as well as measuring employee perceptions in our employee survey. Inclusion and diversity measures have been built into the Company's business scorecard.

At 31 March 2010, 22.6% of NGG's employees were female and 6.7% were from ethnic minority groups, compared to 22.5% and 6.3% respectively at 31 March 2009.

For further information on National Grid's employee engagement and Inclusion and diversity can be found in the National Grid plc Annual Report and Accounts 2009/10.

Developing talent, leadership skills and capabilities

A key success factor in delivering our business objectives is having highly competent leaders at every level within the organisation driving high performance and engaging employees. This is the foundation of our talent development strategy, which focuses on the key and critical transition points individuals make during their careers.

For further information on National Grid's developing of talent, leadership and capabilities can be found in the National Grid plc Annual Report and Accounts 2009/10.

Positively shaping the energy and climate change agenda with external stakeholders

We aim to take the lead on the energy and climate change issues facing society. We will not simply react to the initiatives of other relevant bodies. Instead, we will be proactive in leading the agenda to make sure we help safeguard the environment.

Climate change

National Grid has further embedded its climate change initiative and increased its energy efficiency programmes, focusing on initiatives that are cost effective. National Grid believes its 45% by 2020 and 80% by 2050 greenhouse gas emissions reduction targets to be industry leading within the UK and US.

Further information on National Grid's climate change agenda can be found in the National Grid plc Annual Report and Accounts 2009/10.

Protecting the environment

In April 2009, National Grid published a revised environment policy, reinforcing its commitment to being an innovative leader in energy management and to safeguarding the global environment for future generations.

The performance indicators that we monitor in this area include the number of significant direct environmental incidents.In 2009/10 there were no significant environmental incidents arising directly from our operations compared to no incidents In 2008/09. There were no prosecutions by enforcing bodies resulting from these incidents.

We manage land contamination issues on an inherited portfolio of historically contaminated land dating back over 100 years. These include former manufactured gas plants, as well as former and current gas holder sites on our transmission and distribution networks. These sites can sometimes have a complex mix of contamination. The focus of our remediation programme is on managing the environmental risk by targeting those with the highest environmental risk profile and those with regulatory requirements to remediate, while returning land to productive public or private use where we can, and where it is surplus to operational requirements.

National Grid Property Limited, a fellow subsidiary company of National Grid, manages land contamination issues on NGG's behalf.

On our website (www.nationalgrid.com), we provide further information on the steps we are taking to reduce our impact on the environment, including our use of natural resources and minimising the impact on the environment of our waste.

Financial performance

In the following section we provide a more detailed analysis of the financial results.

We report our financial results and position in accordance with International Financial Reporting Standards (IFRS).

Measurement of financial performance and use of adjusted profit measures

In considering the financial performance of our businesses and segments, we analyse each of our primary financial measures of operating profit, profit before tax and profit for the year 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 our reported financial performance from year to year.

Measures of business performance are referred to in this Annual Report 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 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 virtue of their nature or 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, significant 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 we have 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. We believe 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 our overall financial performance.

Profit for the year from continuing operations

Profit for the year from continuing operations increased from £48 million in 2008/09 to £601 million in 2009/10 as a consequence of the changes in operating profit, net finance costs, exceptional finance costs and remeasurements, and taxation described in the following sections:

Adjusted earnings

	Years ended 31 March	
	2010	2009
Continuing operations	**£m**	£m
Adjusted operating profit	**1,297**	1,091
Net finance costs excluding exceptional items and remeasurements	**(254)**	(401)
Adjusted profit before taxation	**1,043**	690
Taxation excluding taxation on exceptional items and remeasurements	**(322)**	(393)
Adjusted profit for the year from continuing operations	**721**	297

Earnings

	Years ended 31 March	
	2010	2009
Continuing operations	**£m**	£m
Total operating profit	**1,110**	767
Net finance costs	**(221)**	(407)
Profit before taxation	**889**	360
Taxation	**(288)**	(312)
Profit for the year from continuing operations	**601**	48

Adjusted profit measures

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

Reconciliation of adjusted operating profit to total operating profit

	Years ended 31 March	
	2010	2009
Continuing operations	**£m**	£m
Adjusted operating profit	**1,297**	1,091
Exceptional items	**(187)**	(324)
Total operating profit	**1,110**	767

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

Reconciliation of adjusted profit before taxation to profit before taxation

	Years ended 31 March	
	2010	2009
Continuing operations	**£m**	£m
Adjusted profit before taxation	**1,043**	690
Exceptional items	**(187)**	(324)
Derivative financial remeasurements	**33**	(6)
Total profit before taxation	**889**	360

Adjusted profit before taxation is presented on the face of the consolidated income statement, under the heading profit before taxation before exceptional items and remeasurements.

Reconciliation of adjusted earnings to earnings (profit for the year from continuing operations)

	Years ended 31 March	
	2010	2009
Continuing operations	**£m**	£m
Adjusted earnings	**721**	297
Exceptional items	**(143)**	(243)
Derivative financial remeasurements	**23**	(6)
Earnings	**601**	48

Adjusted earnings is presented on the face of the consolidated income statement, under the heading profit for the year from continuing operations after taxation before exceptional items and remeasurements.

Operating profit

Operating profit for 2009/10 and 2008/09 is as follows:

	Years ended 31 March	
	2010	2009
Continuing operations	**£m**	£m
Revenue	**2,747**	2,574
Other operating income	**14**	27
Operating costs	**(1,651)**	(1,834)
Total operating profit	**1,110**	767
Comprising:		
Adjusted operating profit	**1,297**	1,091
Exceptional items	**(187)**	(324)
Total operating profit	**1,110**	767

The following tables set out the consolidated revenue, adjusted operating profit and operating profit by segment.

Revenue is analysed by segment as follows:

	Years ended 31 March	
	2010	2009
Continuing operations	**£m**	£m
Gas Transmission	**934**	813
Gas Distribution	**1,516**	1,466
Gas Metering	**329**	340
Other activities	**45**	43
Total segmental revenues	**2,824**	2,662
Less: sales between business segments	**(77)**	(88)
Revenue	**2,747**	2,574

Operating profit before exceptional items is analysed by segment as follows:

	Years ended 31 March	
	2010	2009
Continuing operations	**£m**	£m
Gas Transmission	**450**	321
Gas Distribution	**711**	668
Gas Metering	**148**	125
Other activities	**(12)**	(23)
Adjusted operating profit	**1,297**	1,091

Total operating profit is analysed by segment as follows:

	Years ended 31 March	
	2010	2009
Continuing operations	**£m**	£m
Gas Transmission	**350**	56
Gas Distribution	**667**	610
Gas Metering	**106**	124
Other activities	**(13)**	(23)
Total operating profit	**1,110**	767

2009/10 compared with 2008/09

Changes in revenue and other operating income, operating costs and operating profit for 2009/10 compared with 2008/09 can be summarised as follows:

Continuing operations	Revenue and other operating income £m	Operating costs £m	Operating profit £m
2008/09 results	2,601	(1,834)	**767**
Add back 2008/09 exceptional items	-	324	**324**
2008/09 adjusted results	2,601	(1,510)	**1,091**
Gas Transmission	111	18	**129**
Gas Distribution	53	(10)	**43**
Gas Metering	(10)	33	**23**
Other activities	1	10	**11**
Sales between businesses	5	(5)	**-**
2009/10 adjusted results	2,761	(1,464)	**1,297**
2009/10 exceptional items	-	(187)	**(187)**
2009/10 results	2,761	(1,651)	**1,110**

Revenue and other operating income in 2009/10 was £160 million higher than in 2008/09, primarily as a result of higher Gas Transmission and Gas Distribution revenues. Operating costs excluding exceptional items decreased by £46 million; as a result of a reduction in the costs of Gas Metering, partly offset by higher operating costs in Gas Transmission and Gas Distribution. As a consequence, adjusted operating profit was £206 million higher than 2008/09.

Net operating exceptional charges of £187 million in 2009/10 were £137 million lower than 2008/09. These relate to restructuring costs of £72 million, an increase in environmental provisions of £14 million due to a change in landfill tax legislation during the year, other charges of £43 million including those associated with the Metering business, and pension deficit charges of £58 million arising from contributions to the National Grid UK Pension Scheme under the recovery plan agreed with the trustees.

Total operating profit increased by £343 million compared to 2008/09 as a result of the £206 million increase in adjusted operating profit and the £137 million decrease in operating exceptional charges.

Net finance costs

Net interest excluding exceptional finance costs and remeasurements decreased by £147 million from 2008/09 to 2009/10. This is primarily explained by lower interest rates.

Financial remeasurements relate to net gains on derivative financial instruments of £33 million in 2009/10, compared with £6 million net losses in 2008/09.

Taxation
The net tax charge of £288 million in 2009/10 comprised a £322 million charge on adjusted profit before tax and a £34 million credit on exceptional items and remeasurements. This compares with a net charge of £312 million in 2008/09, comprising a £393 million charge on adjusted profit before tax and a £81 million credit on exceptional items and remeasurements.

The effective tax rate before and after exceptional items and remeasurements was 31% and 32% respectively (2008/09: 57% and 87%), compared with a standard UK corporation tax rate of 28% in both years.

Cash flows
Cash flows from operating activities
Cash generated from continuing operations was £1,872 million in 2009/10 compared with £1,005 million in 2008/09. This included cash outflows relating to exceptional items of £123 million and £261 million respectively.

There was a net corporate tax payment in 2009/10 of £309 million compared with £71 million in 2008/09.

The net cash inflow from operating activities after taxation was £1,563 million in 2009/10, compared with £934 million in 2008/09.

Cash flows from investing activities
Cash outflows from investing activities were £266 million in 2009/10 compared to £1,447 million in 2008/09. Cash outflows to purchase property, plant and equipment and intangible fixed assets, net of disposal proceeds, were £952 million in 2009/10 compared to £989 million in 2008/09. Interest received was £3 million in 2009/10 compared to £19 million in 2008/09. Net cash inflows from the disposal of financial investments were £683 million in 2009/10 compared to net cash outflows from acquisitions of £491 million in 2008/09.

Cash flows from financing activities
The net cash outflow from financing activities was £1,301 million in 2009/10 compared to a cash inflow of £504 million in 2008/09. This reflected net outflows from loans of £725 million (2008/09: £1,122 million inflow) and net payments to providers of finance, in the form of interest and dividends, of £576 million (2008/09: £618 million).

Net interest cash outflows decreased from £299 million in 2008/09 to £273 million in 2009/10.

Dividends in respect of the financial year

	2010	2009
	£m	£m
Interim	**300**	300

The table above shows the ordinary dividends paid or payable by NGG in respect of the last two financial years. These dividends do not include any associated UK tax credit in respect of such dividends.

Financial performance by segment

Gas Transmission

Financial performance
The results for the Gas Transmission segment for the years ended 31 March 2010 and 2009 were as follows:

	Years ended 31 March	
	2010	2009
	£m	£m
Revenue	**934**	812
Other operating income	**14**	25
Operating costs excluding exceptional items	**(498)**	(516)
Adjusted operating profit	**450**	321
Exceptional items	**(100)**	(265)
Operating profit	**350**	56

The principal movements in operating profit between 2008/09 and 2009/10 can be summarised as follows:

	Revenue and other operating income	Operating costs	Operating profit
	£m	£m	£m
2008/09 operating profit	837	(781)	56
Add back 2008/09 exceptional items	-	265	265
2008/09 adjusted operating profit	837	(516)	**321**
Allowed revenues	50	-	**50**
Timing of recoveries	72	-	**72**
Depreciation and amortisation	-	(4)	**(4)**
Other	(11)	22	**11**
2009/10 adjusted operating profit	948	(498)	**450**
2009/10 exceptional items	-	(100)	**(100)**
2009/10 operating profit	948	(598)	**350**

Revenue and other operating income increased by £111 million driven by an increase in allowed revenues and a £72 million timing impact on recoveries.

Operating costs excluding exceptional items decreased by £18 million in 2009/10 compared to 2008/09. Depreciation and amortisation increased by £4 million as a result of increasing capital investment.

Exceptional charges of £100 million in 2009/10 are made up of pension deficit payments of £54 million, and restructuring costs, primarily a £41 million charge relating to the restructuring of our LNG storage facilities. Exceptional charges of £265 million in 2008/09 are made up of pension deficit payments of £212 million, and restructuring costs, primarily a £50 million charge relating to the restructuring of our LNG storage facilities.

As a consequence of these items, adjusted operating profit, excluding exceptional items, increased by £129 million in

2009/10 compared with 2008/09, while operating profit after exceptional items increased by £294 million.

Gas Distribution

Financial performance

The results for the Gas Distribution segment for the years ended 31 March 2010 and 2009 were as follows:

	Years ended 31 March	
	2010	2009
Continuing operations	**£m**	£m
Revenue	**1,516**	1,466
Other operating income	**-**	2
Operating costs excluding exceptional items	**(805)**	(800)
Adjusted operating profit	**711**	668
Exceptional items	**(44)**	(58)
Total operating profit	**667**	610

The principal movements in operating profit between 2008/09 and 2009/10 can be summarised as follows:

Continuing operations	Revenue and other operating income £m	Operating costs £m	Operating profit £m
2008/09 operating profit	1,468	(858)	**610**
Add back 2008/09 exceptional items	-	58	**58**
2008/09 adjusted operating profit	1,468	(800)	**668**
Allowed revenues	85	-	**85**
Timing of recoveries	(28)	-	**(28)**
Pass-through costs	-	5	**5**
Non-formula costs	(14)	9	**(5)**
Other revenues and costs	5	(19)	**(14)**
2009/10 adjusted operating profit	**1,516**	**(805)**	**711**
2009/10 exceptional items	**-**	**(44)**	**(44)**
2009/10 operating profit	**1,516**	**(849)**	**667**

Revenue and other operating income increased by £48 million in 2009/10 compared with 2008/09. Allowed revenue was up £85 million, driven by the five year price control that came into effect on 1 April 2008 and incentive gains through the efficient management of capacity requirements and improved pressure management. This was partially offset by an estimated £28 million timing impact on recoveries.

The net year-on-year timing impact against allowed revenue was a reduction of £28 million as in 2009/10 there was a net surplus of £19 million, comprising the under-recovery of £1 million relating to the previous year and a £20 million under-recovery for 2009/10, compared with a net gain of £9 million in 2008/09, comprising a £1 million under-recovery in 2008/09 offset by £10 million under-recovery from 2007/08.

Operating costs for 2009/10, excluding exceptional items, were largely in line with 2008/09. Efficiency savings through strong operating cost performance, together with other minor items, were largely offset by higher costs associated with severe winter weather conditions and higher depreciation charge. Non-formula costs were £9 million lower reflecting reduced workload.

Exceptional charges of £44 million in 2009/10 included an increase in the environmental provision of £14 million, reflecting changes in landfill tax legislation, with the remaining £30 million made up of restructuring, transformation costs, which include system related projects costs, and pension deficit charges. This compared with a £58 million charge in 2008/09.

As a consequence of the above, adjusted operating profit excluding exceptional items was £43 million higher in 2009/10 than 2008/09, an increase of 6%. Including exceptional items, operating profit was £57 million higher in 2009/10 than 2008/09, an increase of 9%.

Gas Metering

Financial performance

The results for the Gas Metering segment for the years ended 31 March 2010 and 2009 were as follows:

	Years ended 31 March	
	2010	2009
	£m	£m
Revenue	**329**	340
Operating costs excluding exceptional items	**(181)**	(215)
Adjusted operating profit	**148**	125
Exceptional items	**(42)**	(1)
Total operating profit	**106**	124

The increase in adjusted operating profit is largely due to a reduction in operating costs.

Other activities

Other activities comprises xoserve, which delivers transportation transactional services on behalf of all the major gas network transportation companies in Great Britain, including our Gas Transmission and Gas Distribution businesses, and corporate overheads that are not borne by individual businesses.

Financial results

The results for other activities for the years ended 31 March 2010 and 2009 were as follows:

	Years ended 31 March	
	2010	2009
	£m	£m
Revenue	**45**	43
Operating costs excluding exceptional items	**(57)**	(66)
Operating loss	**(12)**	(23)

Financial position and financial management

Going concern

Having made enquiries, the Directors consider that NGG and its subsidiaries have adequate resources to continue in business for the foreseeable future and that it is therefore appropriate to adopt the going concern basis in preparing the consolidated and individual financial statements of NGG. More details on

NGG's liquidity position are provided under the heading Liquidity and treasury management below and in note 28 to the consolidated financial statements.

Financial position

Balance sheet

The balance sheet at 31 March 2010 can be summarised as follows:

	Assets £m	Liabilities £m	Net assets £m
Property, plant and equipment and non-current intangible assets	10,939	-	10,939
Current assets and liabilities	331	(887)	(556)
Other non-current assets and liabilities	5,611	(1,214)	4,397
Deferred tax	-	(1,890)	(1,890)
Total before net debt	16,881	(3,991)	12,890
Net debt	964	(7,823)	(6,859)
Total as at 31 March 2010	**17,845**	**(11,814)**	**6,031**
Total as at 31 March 2009	18,432	(12,662)	5,770

The £261 million increase in net assets from £5,770 million at 31 March 2009 to £6,031 million at 31 March 2010 resulted from the profit for the year from continuing operations of £601 million, net losses recognised directly in equity of £48 million, other movements in equity of £8 million and dividends paid of £300 million.

Net debt

Net debt decreased by £21 million from £6,880 million at 31 March 2009 to £6,859 million at 31 March 2010. Cash flows from operations net of tax of £1,563 million were offset by capital expenditure, net of disposals, of £952 million, dividends paid of £300 million and net interest paid of £273 million, together with fair value and other movements of £17 million.

At 31 March 2010, net debt comprised borrowings of £7,672 million including bank overdrafts of £15 million, less derivative financial instruments with a net carrying value of £486 million, cash and cash equivalents of £1 million, and financial investments of £326 million (31 March 2009: borrowings of £8,672 million including bank overdrafts of £10 million less derivative financial instruments with a net carrying value of £783 million, and financial investments of £1,009 million).

The maturity of borrowings is shown in note 17 to the consolidated financial statements.

Capital structure

We monitor the regulatory asset value (RAV) gearing within the Gas Transmission and Gas Distribution businesses. This is calculated as net debt expressed as a percentage of RAV, and indicates the level of debt employed to fund the regulated businesses. It is compared with the level of RAV gearing indicated by Ofgem as being appropriate for these businesses, at around 60%.

To calculate RAV gearing for the regulated Gas Transmission and Gas Distribution businesses we exclude an element of the debt that is associated with the Gas Metering business. RAV gearing as at 31 March 2010 was 57% compared to 60% as at 31 March 2009.

Liquidity and treasury management

Treasury policy

Funding and treasury risk management for NGG is carried out by the treasury function of National Grid under policies and guidelines approved by the Finance Committees of the Boards of National Grid plc and National Grid Gas plc. The Finance Committees have authority delegated from the relevant Boards and are responsible for regular review and monitoring of treasury activity and for the approval of specific transactions, the authority for which may be further delegated.

The primary objective of the treasury function is to manage the funding and liquidity requirements of National Grid. A secondary objective is to manage the associated financial risks, in the form of interest rate risk and foreign exchange risk, to within acceptable boundaries. Further details of the management of funding and liquidity and the main risks arising from our financing activities are set out below, as are the policies for managing these risks, including the use of financial derivatives, which are agreed and reviewed by the Boards and the Finance Committees.

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.

Commodity derivatives entered into in respect of gas commodities are used in support of the business's operational requirements and their use is explained on page 21.

Current condition of the financial markets

During 2009/10, there has been a partial recovery in the global economic situation, following the crisis in the banking system, the failure of individual banks and increased restrictions on lending across the capital and money markets in 2008/09. Credit spreads have narrowed significantly. With our low risk business model and cash flows that are largely stable over a period of years, we were able to access the markets during 2008/09 and have continued to do so in 2009/10, having issued £366 million of long-term debt into the capital markets. We remain confident of our ability to access the public debt markets in the future. The cost of our new long-term debt has fallen over the last year, decreasing from around 6.0% in 2008/09 to around 3.0% in 2009/10. This reflects the increase in credit spreads demanded by lenders more than offset by the fall in headline interest rates.

Cash flow and cash flow forecasting

Cash flows from operations are largely stable over a period of years, although they do depend on the timing of customer payments. Our gas transmission and distribution operations are subject to multi-year price control agreements with our regulator, Ofgem.

Both short-term and long-term cash flow forecasts are produced regularly to assist the treasury function in identifying short-term liquidity and long-term funding requirements,and we seek to enhance our cash flow forecasting processes on an ongoing basis. Cash flow forecasts, supplemented by a financial headroom analysis, are monitored regularly to assess funding adequacy for at least a 12 month period.

As part of our regulatory arrangements, our operations are subject to a number of restrictions on the way we can operate. These include regulatory 'ring fences' that requires us to maintain adequate financial resources and restricts our ability to undertake transactions between certain National Grid subsidiary companies including paying dividends, lending cash or levy charges.

Funding and liquidity management
We maintain medium-term note and commercial paper programmes to facilitate long and short-term debt issuance into capital and money markets.

At 31 March 2010, NGG had a $2.5 billion US commercial paper programme (unutilised), a $1.25 billion Euro commercial paper programme (unutilised) and a €10.0 billion Euro medium-term note programme (€5.7 billion issued).

In addition we have both committed and uncommitted bank borrowing facilities that are available for general corporate purposes to support our liquidity requirements. At 31 March 2010, the Company had £700 million of long-term committed facilities (undrawn). Subsequent to year end these facilities were renewed at a reduced level and now stand at £425 million, expiring in April 2014.

We invest surplus funds on the money markets, usually in the form of short-term fixed deposits and placements with money market funds that are invested in highly liquid instruments of high credit quality. Investment of surplus funds is subject to our counterparty risk management policy, and we continue to believe that our cash management and counterparty risk management policies provide appropriate liquidity and credit risk management. Details relating to cash, short-term investments and other financial assets at 31 March 2010 are shown in notes 15 and 16 to the consolidated financial statements.

We believe that maturing amounts in respect of contractual obligations as shown in commitments and contingencies in note 24 to the consolidated financial statements can be met from existing cash and investments, operating cash flows and other financings that we reasonably expect to be able to secure in the future, together with the use of committed facilities if required.

Credit ratings
It is a condition of the regulatory ring-fence around the Company that it uses reasonable endeavours to maintain an investment grade credit rating. As of 31 March 2010, the long-term senior unsecured debt and short-term debt credit ratings respectively provided by Moody's Investor Services, Standard & Poor's and Fitch were as follows (all with outlooks of stable):

Moody's Investor Services	A3/P2
Standard & Poor's	A-/A2
Fitch	A/F2

Use of derivative financial instruments
As part of our business operations, including our treasury activities, we are exposed to risks arising from fluctuations in interest rates and exchange rates. We use financial instruments, including financial derivatives, to manage exposures of this type. Our policy is not to use financial derivatives for trading purposes. More details on derivative financial instruments are provided in note 12 to the consolidated financial statements.

Refinancing risk management
Refinancing risk within National Grid is controlled mainly by limiting the amount of debt maturities arising on borrowings in any financial year.

Note 17 to the consolidated financial statements sets out the contractual maturities of our borrowings over the next five years, with total contracted borrowings maturing over 42 years. We expect to be able to refinance this debt through the capital and money markets as we have done during the year to 31 March 2010.

Interest rate risk management
Our interest rate exposure arising from borrowings and deposits is managed by the use of fixed and floating rate debt and derivative financial instruments, including interest rate swaps, swaptions and forward rate agreements. The interest rate risk management policy followed by National Grid 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 an extreme movement in interest rates, neither the interest cost nor the total financing cost is expected to exceed preset limits with a high degree of certainty.

Some of NGG's bonds in issue are inflation-linked, that is their cost is linked to changes in the UK Retail Prices Index (RPI). We believe that these bonds provide an appropriate hedge for revenues and our regulatory asset values that are also RPI linked under our price control formulas.

The performance of the treasury function in interest rate risk management is measured by comparing the actual total financing costs of the National Grid debt with those of a passively managed benchmark portfolio with set ratios of fixed rate to floating-rate debt, to identify the impact of actively managing National Grid's interest rate risk. This is monitored regularly by the Finance Committee of National Grid.

Within the constraints of our interest rate risk management policy, and as approved by the Finance Committee, we actively manage our interest rate exposure and therefore the interest rate profile shown at 31 March 2010 will change over time.

In 2010/11, we expect the financing costs of National Grid to continue to benefit from low short-term interest rates, some of which have already been locked in using short-term interest rate derivatives, although we expect this to be offset by higher inflation affecting our index-linked debt.

More information on the interest rate profile of our debt is included in note 28 (a) to the consolidated financial statements.

Foreign exchange risk management

We have a policy of managing our foreign exchange transaction risk by hedging contractually committed foreign exchange transactions over a prescribed minimum size. This covers a minimum of 75% of such transactions occurring in the next six months and a minimum of 50% of such transactions occurring six to twelve months in the future. Cover generally takes the form of forward sale or purchase of foreign currencies and must always relate to forecast underlying operational cash flows.

In addition, we are exposed to currency exposures on borrowings in currencies other than sterling, principally the euro and dollar. This currency exposure is managed through the use of cross-currency swaps, so that post derivatives the currency profile is almost entirely sterling.

More details can be found in note 28 to the consolidated financial statements.

Counterparty risk management

Counterparty risk arises from the investment of surplus funds and from the use of derivative instruments, and from commercial contracts entered into by the businesses, including commodity contracts. The National Grid Finance Committee has agreed a policy for managing such risk. This policy sets limits as to the exposure that National Grid can have with any one counterparty, based on that counterparty's credit rating from independent credit rating agencies. National Grid's exposure to individual counterparties is monitored daily and counterparty limits are regularly updated for changes in credit ratings. The treasury function is responsible for managing the policy. Where contracts carrying credit risk are entered into outside the Treasury function, part of the relevant counterparty limit can be allocated to the business area involved. This ensures that National Grid's overall exposure is managed within the appropriate limit.

Where multiple transactions are entered into with a single counterparty, a master netting arrangement is usually put in place to reduce our exposure to credit risk of that counterparty. When transacting interest rate and exchange rate derivatives, 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.

Further information on the management of counterparty risk is provided in note 28(c) to the consolidated financial statements.

Valuation and sensitivity analysis

We calculate the fair value of debt and financial derivatives by discounting all future cash flows by the market yield curve at the balance sheet date, including the credit spread for debt, and in the case of financial derivatives, taking into account the credit quality of both parties. 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.

For debt and derivative instruments held, we utilise a sensitivity analysis technique to evaluate the effect that changes in relevant rates or prices would have on the market value of such instruments.

As described in note 28(e) to the consolidated financial statements, movements in financial indices would have the following estimated impact on the financial statements as a consequence of changes in the value of financial instruments.

Years ended 31 March	2010		2009	
	Income statement £m	Other compre-hensive income £m	Income statement £m	Other compre-hensive income £m
UK Retail Prices Index ± 0.50%	**10**	**-**	10	-
UK interest rates ± 0.50%	**5**	**16**	7	16

Commodity contracts

Gas purchased for our own use relates to the operation of our gas transmission and gas distribution networks.

In our Gas Transmission operation we are obliged to offer for sale, through a series of auctions both short and long term, a predetermined quantity of entry capacity for every day in the year at predefined locations. Where, on the day, the gas transmission system's capability is constrained, such that gas is prevented from entering the system for which entry capacity rights have been sold, then the Gas Transmission business is required to buy back those entry capacity rights sold in excess of system capability. Forward and option contracts are used to reduce the risk and exposure to on-the-day entry capacity prices.

Commitments and contingencies

Commitments and contingencies outstanding at 31 March 2010 and 2009 are summarised in the table below:

	2010 **£m**	2009 £m
Future capital expenditure contracted but not provided for	**533**	480
Total operating lease commitments	**77**	75
Other commitments and contingencies	**209**	150

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

We propose to meet all of our commitments from existing cash and investments, operating cash flows, existing credit facilities, future facilities and other financing that we reasonably expect to be able to secure in the future.

Details of material litigation as at 31 March 2010

Metering competition investigation

On 25 February 2008, the Gas and Electricity Markets Authority (GEMA) announced it had decided we breached Chapter II of the Competition Act 1998 and Article 82 (now Article 102) of the Treaty on the Functioning of the European Union and fined us £41.6 million. We appealed GEMA's decision to the Competition Appeal Tribunal (the Tribunal), which upheld the appeal in part in April 2009 and reduced the fine to £30 million. We appealed further to the Court of Appeal in respect of certain aspects of the Tribunal's judgement. On 23 February 2010, in a reserved judgement, the Court of Appeal decided that it would not interfere with the judgement of the Tribunal save that it further reduced the fine to £15 million. On 22 March 2010, we applied to the Supreme Court for leave to appeal the Court of Appeal's judgement.

As at 31 March 2010, we have provided for the fine together with associated costs and have provided against certain trade receivables and other balance sheet items. Without prejudice to our position in relation to appealing the Court of Appeal's judgement, the £15 million fine was paid to GEMA on 1 April 2010.

Gas distribution mains replacement investigation

In October 2008, we informed Ofgem that mains replacement activity carried out by the UK Gas Distribution business may have been misreported. Ofgem's investigation continues, so that at present it is too early to determine the likely outcome of the investigation and any potential consequences as a result of it, including the quantum of any amounts that may become payable.

Related party transactions

We provide services to and receive services from related parties, principally fellow subsidiary companies of National Grid. In the year ended 31 March 2010, NGG charged £21 million and received charges of £146 million from related parties (other than Directors and key managers), compared with £19 million and £358 million respectively in 2008/09.

Further information relating to related party transactions is contained within note 25 to the consolidated financial statements. Details of key management compensation and amounts paid to Directors are included within notes 3(c) and 3(d) to the consolidated financial statements respectively.

Retirement arrangements

The substantial majority of our employees are members of the National Grid UK Pension Scheme, which is operated by Lattice Group plc, an intermediate holding company of NGG. We do not provide any other post-retirement benefits. 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 NGG, we account for the scheme as if it were a defined contribution scheme and do not recognise any share of the assets and liabilities of the scheme.

Actuarial position

The last completed full actuarial valuation of the National Grid UK Pension Scheme was as at 31 March 2007. This concluded that the pre-tax funding deficit was £442 million in the defined benefit section on the basis of the funding assumptions. Employer cash contributions for the ongoing cost of this plan are currently being made at a rate of 29.4% of pensionable payroll.

Contributions

In addition to ongoing employer contributions we made additional deficit contributions to the scheme of £58 million during 2009/10 as a final payment to clear in full the deficit revealed by the 2007 valuation.

The next valuation of the scheme is due as at 31 March 2010.

Principal risks and uncertainties

Risk management

Identifying, evaluating and managing risks is integral to the way we run our business. National Grid continues to have 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. An output from this process is information that provides assurance to management and thus helps safeguard our assets and reputation. NGG participates in this enterprise wide process.

More information on National Grid's risk management process can be found the in the National Grid Annual Report and Accounts 2009/10.

Risk factors

The risk management process has identified the following risk factors that could have a material adverse effect on our business, financial condition, results of operations and reputation as well as the value and liquidity of our securities. Not all of these factors are within our control. In addition, other factors besides those listed below may have an adverse effect on NGG.

Changes in law or regulation and decisions by governmental bodies or regulators could have a material adverse effect on our results of operations.

Our businesses are subject to regulation by governments and other authorities. Consequently, changes in law or regulation or regulatory policy and precedent in the countries in which we operate could materially adversely affect us. Decisions or rulings concerning, for example: (i) whether licences, approvals or agreements to operate or supply are granted or are renewed or whether there has been any breach of the terms of a licence, approval, or regulatory requirement; (ii) timely recovery of incurred expenditure or obligations, the ability to pass through commodity costs, a decoupling of energy usage and revenue and other decisions relating to the impact of general economic conditions on us, our markets and customers, implications of climate change, the level of permitted revenues and dividend distributions for our businesses and in relation to proposed business development activities; and (iii) structural changes in regulation (including as a result of Ofgem's RPI-X@20 review), could have a material adverse impact on our results of operations, cash flows, the financial condition of our businesses and the ability to develop those businesses in the future. For further information, see the Operating and Financial Review and, in particular, the external market, regulatory environment and energy policy, regulatory and other developments sections and the business description sections.

Breaches of, or changes in, environmental or health and safety laws or regulations could expose us to increased costs, claims for financial compensation and adverse regulatory consequences, as well as damaging our reputation.
Aspects of our activities are potentially dangerous, such as the operation and maintenance of gas transmission and distribution networks. 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 our operations that are not currently regarded or proved to have adverse effects but could become so. We are subject to laws and regulations relating to pollution, the protection of the environment, and the use and disposal of hazardous substances and waste materials. These expose us to costs and liabilities relating to our operations and our properties whether current, including those inherited from predecessor bodies, or formerly owned by us and sites used for the disposal of our waste. The cost of future environmental remediation obligations is often inherently difficult to estimate and uncertainties can include the extent of contamination, the appropriate corrective actions and our share of the liability. We are also subject to laws and regulations governing health and safety matters protecting the public and our employees. We are increasingly subject to regulation in relation to climate change. We commit significant expenditure toward complying with these laws and regulations and to meeting our obligations under negotiated settlements. If additional requirements are imposed or our ability to recover these costs under relevant regulatory framework changes, this could have a material adverse impact on our businesses and our results of operations and financial position. Furthermore, any breach of these regulatory or contractual obligations, or even incidents that do not amount to a breach, could materially adversely affect our results of operations and our reputation.

For further information about environmental, climate change and health and safety matters relating to our business, see the Our Responsibility section of National Grid plc's website at www.nationalgrid.com.

Network failure or interruption, the inability to carry out critical non-network operations and damage to infrastructure may have significant material adverse impacts on both our financial position and reputation.
We may suffer a major network failure or interruption or may not be able to carry out critical non network operations. Operational performance could be materially adversely affected by a failure to maintain the health of the system or network, inadequate forecasting of demand or inadequate record keeping or failure of information systems and supporting technology. This could cause us to fail to meet agreed standards of service or incentive and reliability targets or be in breach of a licence, approval, regulatory requirement or contractual obligation, and even incidents that do not amount to a breach could result in adverse regulatory and financial consequences, as well as harming our reputation. In addition to these risks, we may be affected by other potential events that are largely outside our control such as the impact of weather (including as a result of climate change), unlawful or unintentional acts of third parties or force majeure. Weather conditions, including prolonged periods of adverse weather, can affect financial performance and severe weather that causes outages or damages infrastructure will materially adversely affect operational and potentially business performance and our reputation. Terrorist attack, sabotage or other intentional acts may also damage our assets or otherwise significantly affect corporate activities and as a consequence have a material adverse impact on our results of operations and financial condition.

Our 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 our regulated electricity business will be affected by our ability to meet or exceed efficiency and integration targets and service quality standards set by, or agreed with, our regulators. In addition, from time to time, we publish cost and efficiency savings targets for our business. To meet these targets and standards, we must continue to improve operational performance, service reliability and customer service and continue to invest in the development of our information technology. If we do not meet these targets and standards, we may not achieve the expected benefits, our business may be materially adversely affected and our performance, results of operations and our reputation may be materially harmed.

Our reputation may be harmed if consumers of gas suffer a disruption to their supply.
Our gas transmission and distribution businesses are responsible for transporting available gas. We consult with, and provide information to, regulators, governments and industry participants about future demand and the availability of supply. However, where there is insufficient supply, our role is to manage the relevant network safely and reliably which, in extreme circumstances, may require us to disconnect consumers, which may damage our reputation.

We are subject to restrictions with respect to our borrowing and debt arrangements, and our funding costs and access to financing may be adversely affected by

changes to credit ratings and by prolonged periods of market volatility or illiquidity.
We are subject to certain covenants and restrictions in relation to our listed debt securities and our bank lending facilities. In addition, restrictions imposed by regulators may also limit the manner in which we service the financial requirements of our business.

Our business is financed through cash generated from ongoing operations and the capital markets, particularly the long-term debt capital markets. The maturity and repayment profile of debt we use to finance investments often does not correlate to cash flows from our assets. As a result we access commercial paper and money markets and longer-term bank and capital markets as sources of finance. Some of the debt we issue is rated by credit rating agencies and changes to these ratings may affect both our borrowing capacity and the cost of those borrowings. As evidenced during recent periods, financial markets can be subject to periods of volatility and shortages of liquidity and if we were unable to access the capital markets or other sources of finance at competitive rates for a prolonged period, our cost of financing may increase, the uncommitted and discretionary elements of our proposed capital investment programme may need to be reconsidered and the manner in which we implement our strategy may need to reassessed. The occurrence of any such events could have a material adverse impact on our business, results of operations and prospects.

Our results of operations could be affected by deflation or inflation.
Our income under our price controls is linked to the retail price index. Therefore if the UK economy suffers from a prolonged period of deflation, our revenues may decrease, which may not be offset by reductions in operating costs. Conversely during a period of inflation our operating costs may increase without a corresponding increase in the retail price index and therefore without a corresponding increase in revenues. Such increased costs may materially adversely affect our results of operations. In addition, even where increased costs are recoverable under our price controls there may be a delay in our ability to recover our increased costs.

Future funding requirements of our pension schemes could materially adversely affect our results of operations.
Substantially all of our employees are members of a defined benefit pension scheme where the scheme assets are held independently of our own financial resources. Estimates of the amount and timing of future funding for this 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 require us to make additional contributions to these pension schemes which, to the extent they are not recoverable under our price controls, could materially adversely affect our results of operations and financial condition.

New or revised accounting standards, rules and interpretations could have an adverse effect on our reported financial results. Changes in law and accounting standards could increase our effective rate of tax.
The accounting treatment under International Financial Reporting Standards (IFRS), as adopted by the European Union, of, among other things, replacement expenditure, rate regulated entities, pension and post-retirement benefits, derivative financial instruments and commodity contracts, significantly affect the way we report our financial position and results of operations. New or revised standards and interpretations may be issued which could have a significant impact on the financial results and financial position that we report. The effective rate of tax we pay may be influenced by a number of factors including changes in law and accounting standards, the results of which could increase that rate and therefore have a material adverse and therefore have a material adverse impact on our results of operations.

Customers and counterparties to our transactions may fail to perform their obligations, which could harm our results of operations.

Our operations are exposed to the risk that customers and counterparties to our transactions that owe us money or commodities will not perform their obligations, which could materially adversely affect our financial position. This risk is most significant where there are concentrations of receivables from utilities and their affiliates, as well as industrial customers and other purchasers and may also arise where customers are unable to pay us as a result of increasing commodity prices or adverse economic conditions.

The loss of key personnel or the inability to attract, train or retain qualified personnel could affect our ability to implement our strategy and have a material adverse effect on our business, financial condition, results of operations and prospects.
Our ability to implement our long-term business strategy depends on the capabilities and performance of our personnel. Loss of key personnel or an inability to attract, train or retain appropriately qualified personnel (in particular for technical positions where availability of appropriately qualified personnel may be limited) could affect our ability to implement our long-term business strategy and may have a material adverse effect on our business, financial condition, results of operations and prospects.

Accounting policies

Basis of accounting

The consolidated financial statements present the results of NGG for the years ended 31 March 2010 and 2009 and financial position as at 31 March 2010 and 2009. They have been prepared using the accounting policies shown, in accordance with International Financial Reporting Standards (IFRS).

In complying with IFRS, we are also complying with the version of IFRS that has been endorsed by the European Union for use by listed companies.

IFRS differ from UK Generally Accepted Accounting Principles (UK GAAP).

Choices permitted under IFRS

IFRS provide certain options available within accounting standards. Material choices NGG has made, and continues to make, include the following:

Presentation formats
We use the nature of expense method for our income statement and total our balance sheet to net assets and total equity.

In the income statement, we present subtotals of total operating profit, profit before tax and profit from continuing operations, together with additional subtotals excluding exceptional items and remeasurements. Exceptional items and remeasurements are presented on the face of the income statement.

Capital contributions
Contributions received prior to 1 July 2009 towards capital expenditure are recorded as deferred income and amortised in line with depreciation on the associated asset.

Financial instruments
We normally opt to apply hedge accounting in most circumstances where this is permitted.

Critical accounting policies

The application of accounting principles requires us 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, we evaluate our estimates using historical experience, consultation with experts and other methods that we consider reasonable in the particular circumstances to ensure compliance with IFRS. Actual results may differ significantly from our estimates, the effect of which will be recognised in the period in which the facts that give rise to the revision become known.

Certain accounting policies, described below, 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 our accounting policies set out in our consolidated financial statements.

Estimated economic lives of property, plant and equipment
The reported amounts for depreciation of property, plant and equipment and amortisation of non-current intangible assets can be materially affected by the judgments exercised in determining their estimated economic lives.

Carrying value of assets and potential for impairments
The carrying value of assets recorded in the consolidated balance sheet could be materially reduced if an impairment were to be assessed as being required. Impairment reviews are carried out 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
Revenue includes an assessment of transportation services supplied to customers between the date of the last invoice and the year end. Changes to the estimate of the transportation services supplied during this period would have an impact on the reported results.

Estimates of unbilled revenues amounted to £184 million at 31 March 2010 compared with £189 million at 31 March 2009.

Assets and liabilities carried at fair value
Certain 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 judgements on, in particular, future movements in exchange and interest rates.

Hedge accounting
Derivative financial instruments are used to hedge certain economic exposures arising from movements in exchange and interest rates or other factors that could affect either the value of the Company'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 the relevant eligibility, documentation and effectiveness testing requirements are met. 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 National Grid UK Pension Scheme were a defined contribution scheme as there is neither a contractual arrangement, nor a

stated policy under which the company is charged for the costs of providing pensions.

A change in these arrangements may lead to the company 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 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 the company's financial performance and 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, 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 the company has no control.

Provisions
Provisions are made for liabilities, the timing and amount of which is uncertain. 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.

Tax estimates
The tax charge is based on the profit for the year and tax rates in effect. Current tax assets and liabilities arising from transfer pricing adjustments, which are expected to be fully recovered through group relief, are recognised where material. Further adjustments are recognised when tax returns are submitted to the tax authorities. The determination of appropriate provisions for taxation requires us to take into account anticipated decisions of tax authorities and estimate its ability to utilise tax benefits through future earnings and tax planning.

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

Revenue accruals
A 10% change in our estimate of unbilled revenues at 31 March 2010 would result in an increase or decrease in our recorded net assets and profit for the year by approximately £13 million net of tax.

Asset useful lives
An increase in the useful economic lives of assets of one year on average would reduce our annual depreciation charge on property, plant and equipment by £14 million (pre-tax) and our annual amortisation charge on intangible assets by £2 million (pre-tax).

Hedge accounting
If using our derivative financial instruments, hedge accounting had not been achieved during the year ended 31 March 2010 then the profit for the year would have been £131 million lower than that reported net of tax, and net assets would have been £79 million lower.

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 £49 million.

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 our provisions of approximately £17 million.

Accounting developments

Accounting standards, amendments to standards and interpretations adopted in 2009/10

In preparing our consolidated financial statements we have complied with International Financial Reporting Standards, International Accounting Standards and interpretations applicable for 2009/10. The standards, amendments to standards and interpretations adopted during 2009/10 are discussed in the financial statements on page 36. None of these resulted in a material change to our consolidated results, assets or liabilities in 2009/10 or in those of previous periods.

Accounting standards, amendments to standards and interpretations not yet adopted

New accounting standards, amendments to standards and interpretations which have been issued but not yet adopted by National Grid are discussed in the financial statements on page 37.

Directors' Report

for the year ended 31 March 2010

In accordance with the requirements of the Companies Act 2006 and UK Listing Authority's Listing, Disclosure and Transparency Rules, the following sections describe the matters that are required for inclusion in the Directors' Report and were approved by the Board. Further details of matters required to be included in the Directors' Report are incorporated by reference into this report, as detailed below.

Directors

The Directors serving as at the date of this report were:

Malcolm Cooper	Appointed June 2007
Mark Fairbairn	Appointed June 2003
Stuart Humphreys	Appointed July 2008
Paul Whittaker	Appointed June 2007
Adam Wiltshire	Appointed June 2006
Nick Winser	Appointed July 2003

Directors' and Officers' liability insurance cover is arranged and qualifying third party indemnities are in place for each Director.

Principal activities and business review

A full description of the Company's principal activities, businesses and principal risks and uncertainties is contained in the Operating and Financial Review on pages 1 to 26, which are incorporated by reference into this report.

Material interests in shares

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

Dividends

During the year, interim dividends totalling £300 million were paid (2008/09: £300 million interim dividend). The Directors have not proposed a final dividend.

Donations

During 2009/10, some £2.6 million (2008/09: £2.7 million) was invested in support of community initiatives and relationships in the UK. There were no direct charitable donations for 2009/10 (2008/09: £0.5 million).

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

Research and development

Expenditure on research and development was £10 million during the year (2008/09: £4 million).

Financial instruments

Details on the use of financial instruments and financial risk management are included on pages 18 to 22 in the Operating and Financial Review.

Future developments

Details of future developments are contained in the Operating and Financial Review.

Employee involvement

NGG, as a part of National Grid, has well established and effective arrangements through electronic mail, intranet and in-house publications and briefing meetings, at each business location and company wide, for communication and consultation with both employees and trade union representatives, and for communication of performance, strategy and operating model, together with significant business issues. NGG recognises the importance of aligning employee and shareholder interests, and is committed to employee share ownership through the National Grid plc Share Incentive Plan and Sharesave scheme, which are open to all employees.

Policy and practice on payment of creditors

It is NGG's policy to include in contracts or other agreements, terms of payment with suppliers. Once agreed, NGG aims to abide by these terms of payment. The average creditor payment period at 31 March 2010 was 17 days (16 days at 31 March 2009).

Audit information

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

Annual General Meeting

Notice of the NGG's Annual General Meeting for 2010 will be issued separately to shareholders.

On behalf of the Board

Adam Wiltshire
Director
2 July 2010

National Grid Gas plc, 1-3 Strand, London WC2N 5EH
Registered in England and Wales Number 2006000

Statement of Directors' responsibilities

The Directors are responsible for preparing the Annual Report and Accounts, including the consolidated financial statements and the Company financial statements, in accordance with applicable law and regulations.

Company law requires the Directors to prepare financial statements for each financial year. Under that law the Directors have prepared the consolidated financial statements in accordance with International Financial Reporting Standards (IFRS) as adopted by the European Union, and the Company financial statements in accordance with applicable law and United Kingdom Accounting Standards (United Kingdom Generally Accepted Accounting Practice, UK GAAP). In preparing the consolidated financial statements, the Directors have also elected to comply with IFRS, issued by the International Accounting Standards Board (IASB). Under company law the Directors must not approve the financial statements unless they are satisfied that they give a true and fair view of the state of affairs of the Company on a consolidated and individual basis and of the consolidated profit of the Company for that period.

In preparing those financial statements, the Directors are required to:

- select suitable accounting policies and then apply them consistently;
- make judgements and estimates that are reasonable and prudent;
- state that the consolidated financial statements comply with IFRS as adopted by the European Union, and with regard to the Company financial statements that applicable UK Accounting Standards have been followed, subject to any material departures disclosed and explained in the financial statements; and
- prepare the consolidated financial statements and Company financial statements on a going concern basis unless it is inappropriate to presume that the Company, on a consolidated and individual basis, will continue in business, in which case there should be supporting assumptions or qualifications as necessary.

The Directors are responsible for keeping proper accounting records that are sufficient to show and explain the company's transactions and disclose with reasonable accuracy at any time the financial position of the Company on a consolidated and individual basis and to enable them to ensure that the consolidated financial statements comply with the Companies Act 2006 and Article 4 of the IAS Regulation and the Company financial statements comply with the Companies Act 2006. They are also responsible for safeguarding the assets of the Company and its subsidiaries and hence for taking reasonable steps for the prevention and detection of fraud and other irregularities.

Each of the Directors, whose names are listed in the Directors report on page 27, confirms that, to the best of their knowledge:

- The consolidated financial statements and the Company financial statements, which have been prepared in accordance with IFRS as adopted by the European Union and UK GAAP respectively, give a true and fair view of the assets, liabilities, financial position and profit of the Company on a consolidated and individual basis; and
- The Annual Report includes a fair review of the development and performance of the business and the position of the Company on a consolidated and individual basis, together with a description of the principal risks and uncertainties that it faces.

By order of the Board

Adam Wiltshire
Director
2 July 2010

Independent Auditors' report to the Members of National Grid Gas plc

We have audited the consolidated and Company financial statements (the ''financial statements'') of National Grid Gas plc for the year ended 31 March 2010 which comprise the consolidated income statement, the consolidated statement of comprehensive income, the consolidated and Company balance sheets, the consolidated statement of changes in equity, the consolidated cash flow statement, the accounting policies and Company accounting policies, the adoption of new accounting standards, the notes to the consolidated financial statements and the notes to the Company financial statements. The financial reporting framework that has been applied in the preparation of the financial statements is applicable law and International Financial Reporting Standards (IFRS) as adopted by the European Union. The financial reporting framework that has been applied in the preparation of the parent Company financial statements is applicable law and United Kingdom Accounting Standards (United Kingdom Generally Accepted Accounting Practice).

Respective responsibilities of directors and auditors

As explained more fully in the Directors' Responsibilities Statement set out on page 28, the Directors are responsible for the preparation of the financial statements and for being satisfied that they give a true and fair view. Our responsibility is to audit the financial statements in accordance with applicable law and International Standards on Auditing (UK and Ireland). Those standards require us to comply with the Auditing Practices Board's Ethical Standards for Auditors.

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

Scope of the audit of the financial statements

An audit involves obtaining evidence about the amounts and disclosures in the financial statements sufficient to give reasonable assurance that the financial statements are free from material misstatement, whether caused by fraud or error. This includes an assessment of: whether the accounting policies are appropriate to the group's and Company's circumstances and have been consistently applied and adequately disclosed; the reasonableness of significant accounting estimates made by the Directors; and the overall presentation of the financial statements.

Opinion on financial statements

In our opinion:

- the financial statements give a true and fair view of the state of the group's and of the Company's affairs as at 31 March 2010 and of its group's profit and cash flows for the year then ended;
- the consolidated financial statements have been properly prepared in accordance with IFRS as adopted by the European Union;
- the Company financial statements have been properly prepared in accordance with United Kingdom Generally Accepted Accounting Practice (UK GAAP); and
- the financial statements have been prepared in accordance with the requirements of the Companies Act 2006 and, as regards the group financial statements, Article 4 of the IAS Regulation.

Opinion on other matters prescribed by the Companies Act 2006

In our opinion the information given in the Directors' Report for the financial year for which the financial statements are prepared is consistent with the financial statements.

Matters of which we are required to report by exception

We have nothing to report in respect of the following:

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

- adequate accounting records have not been kept by the parent Company, or returns adequate for our audit have not been received from branches not visited by us; or
- the Company financial statements are not in agreement with the accounting records and returns; or
- certain disclosures of Directors' remuneration specified by law are not made; or
- we have not received all the information and explanations we require for our audit.

Phil Harrold (Senior Statutory Auditor)
for and on behalf of PricewaterhouseCoopers LLP
Chartered Accountants and Statutory Auditors
Birmingham
2 July 2010

Accounting policies

for the year ended 31 March 2010

A. Basis of preparation of consolidated financial statements under IFRS

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

These consolidated financial statements were approved for issue by the Board of Directors on 2 July 2010.

These consolidated financial statements have been prepared in accordance with International Financial Reporting Standards (IFRS) as issued by the International Accounting Standards Board and as adopted by the European Union. They are prepared on the basis of all IFRS accounting standards and interpretations that are mandatory for periods ending 31 March 2010 and in accordance with the Companies Act 2006 applicable to companies reporting under IFRS and Article 4 of the European Union IAS regulation. The 2009 comparative financial information has also been prepared on this basis.

The consolidated financial statements have been prepared on a historical cost basis, except for the revaluation of derivative financial instruments and investments classified as available for sale.

These consolidated financial statements are presented in pounds sterling, which is the functional currency of the Company.

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.

B. Basis of consolidation

The consolidated financial statements incorporate the financial statements of the Company and its subsidiaries.

A subsidiary is defined as an entity controlled by the Company. Control is achieved where the Company has the power to 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 UK generally accepted accounting principles (UK GAAP) used in the individual financial statements of the Company and its subsidiaries into line with those used by the Company in its consolidated financial statements under IFRS. Inter-company transactions are eliminated.

C. Foreign currencies

Transactions in currencies other than the functional currency of the Company or subsidiary concerned are recorded at the rates of exchange prevailing on the dates of the transactions. At each 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.

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 that have a functional currency different from the Company's functional currency of sterling 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 consolidated translation reserve.

D. Intangible assets

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

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

Intangible assets under development are not amortised. Other non-current intangible assets are amortised on a straight-line basis over their estimated useful economic lives. The principal amortisation periods for categories of intangible assets are:

Amortisation periods	Years
Software	3 to 5

Intangible emission allowances are accounted for in accordance with accounting policy T.

E. Property, plant and equipment

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

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

Property, plant and equipment include assets in which the Company's interest comprises legally protected statutory or contractual rights of use.

Additions represent the purchase or construction of new assets, including capital expenditure for safety and environmental assets, and extensions to, enhancements to, or replacement of existing assets.

Contributions received prior to 1 July 2009 towards the cost of property, plant and equipment are included in trade and other payables as deferred income and credited on a straight-line basis to the income statement over the estimated economic useful lives of the assets to which they relate.

Contributions received post 1 July 2009 are recognised in revenue immediately, except where the contributions are consideration for a future service, in which case they are recognised initially as deferred income and revenue is subsequently recognised over the period in which the service is provided.

Depreciation is not provided on freehold land or assets in the course of construction. Other property, plant and equipment are depreciated, principally on a straight-line basis, at rates estimated to write off their book values over their estimated useful economic lives. In assessing estimated useful economic lives, which are reviewed on a regular basis, consideration is given to any contractual arrangements and operational requirements 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 in the table below:

Depreciation periods	Years
Freehold and leasehold buildings	up to 50
Plant and machinery	
– mains, services and regulating equipment	30 to 100
– meters and metering equipment	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, the recoverable amount of the cash-generating unit to which that asset belongs is estimated. 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.

Material impairments are recognised in the income statement and are disclosed separately.

G. Taxation

Current tax

Current tax assets and liabilities for the current and prior periods are measured at the amount expected to be recovered from or paid to the taxation authorities. The tax rates and tax laws used to compute the amount are those that are enacted or substantively enacted by the balance sheet date. Management periodically evaluates positions taken in tax returns with respect to situations in which applicable tax regulation is subject to interpretation and establishes provisions where appropriate on the basis of amounts expected to be paid to the tax authorities.

Current tax assets and liabilities arising from transfer pricing adjustments, which are expected to be fully recovered through group relief, are initially estimated and recognised where material. Further adjustments are recognised when tax returns are submitted to the tax authorities.

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 Company 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 it 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 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 current tax assets and liabilities on a net basis.

H. Discontinued operations

Cash flows and operations that relate to a major component of the business that has been sold are shown separately from continuing operations.

I. Inventories

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

J. 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.

K. Revenue

Revenue represents the sales value derived from the transmission and distribution of gas and the provision of gas metering services during the year. It excludes value added tax and intra-group sales.

The sales value for the transmission and distribution of gas is largely determined from the amount of system capacity sold for the year and the amount of gas transported in the year, evaluated at contractual prices on a monthly basis. Where revenue for the year exceeds the maximum amount permitted by regulatory agreement and adjustments will be made to future prices to reflect this over-recovery, a liability for the over-recovery is not recognised as such an adjustment to future prices relates to the provision of future services. Similarly, an asset is not recognised where a regulatory agreement permits adjustments to be made to future prices in respect of an under-recovery.

The sales value for the provision of gas metering services is largely derived from monthly contractual charges for the provision of individual meters under long-term contractual arrangements.

L. Segmental information

Segmental information is based on the information the Board of Directors uses internally for the purposes of evaluating the performance of operating segments and determining resource allocation between operating segments. The Board of Directors is deemed to be the chief operating decision-maker and assesses the performance of operations principally on the basis of operating items before exceptionals and remeasurements.

M. Pensions

The substantial majority of NGG's 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 NGG. Accordingly, the Scheme is recognised 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 financial statements.

N. Leases

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

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

Assets held under finance leases are depreciated over the shorter of their useful life and the lease term.

O. Financial instruments

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

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. Trade payables are initially recognised at fair value and subsequently measured at amortised cost.

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 recognised at fair value plus, in the case of available-for-sale financial investments, directly related incremental transaction costs and are subsequently carried at fair value on the balance sheet. Changes in the fair value of investments classified as 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 income statement for the period. Investment income on investments classified as fair value through profit and loss and on available-for-sale investments is recognised using the effective interest rate method and taken through interest income in the income statement.

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

Borrowing costs directly attributable to the acquisition, construction or development 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.

Derivative financial instruments are recorded at fair value, and where fair value of a derivative is positive, it is carried as a derivative asset and where negative, as a derivative liability. Assets and liabilities on different transactions are only netted if the transactions are with the same counterparty, a legal right to set-off exists and the cash flows are intended to be settled on a net basis. Gains and losses arising from changes in the fair value are included in the income statement in the period they arise.

No adjustment is made with respect to derivative clauses embedded in financial instruments or other contracts that are closely related to those instruments or contracts. In particular, interest payments on UK RPI debt are linked to movements in the UK retail price index. The link to RPI is considered to be an embedded derivative, which is closely related to the underlying debt instrument based on the view that there is a strong relationship between interest rates and inflation in the UK economy. Consequently these embedded derivatives are not accounted for separately from the debt instrument. Where there are embedded derivatives in host contracts not closely related, the embedded derivative is separately accounted for as a derivative financial instrument and recorded at fair value.

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 with an amount equal to the nominal amount of the shares issued included in the share capital account and the balance recorded in the share premium account.

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

P. Hedge accounting

The Company and its subsidiaries enter into both derivative financial instruments (derivatives) and non-derivative financial instruments in order to manage interest rate and foreign currency exposures, and commodity price risks associated with underlying business activities and the financing of those activities.

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

Firstly, 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.

Secondly, fair value hedge accounting offsets the changes in the fair value of the hedging instrument against the change in the fair value of the hedged item in respect to the risk being hedged. These changes are recognised in the income statement to the extent the fair value hedge is effective. Adjustments made to the carrying amount of the hedged item for fair value hedges will be amortised over the remaining life, in line with the hedged item.

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 rate 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.

Q. Share-based payments

National Grid issues equity-settled share-based payments to certain employees of the Company and its subsidiaries.

Equity-settled share-based payments are measured at fair value at the date of grant based on an estimate of the number of shares that will eventually vest. This fair value is recognised on a straight-line basis over the vesting period, as an operating cost and an increase in equity. Payments made by the Company to National Grid in respect of share-based payments are recognised as a reduction in equity.

R. Business performance and exceptional items and remeasurements

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

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 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, pension deficit payments or impairments of non-current assets, significant changes in environmental provisions, and gains or losses on disposals of businesses or investments.

Costs arising from restructuring programmes primarily relate to redundancy costs, impairment of assets, and site decommissioning 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.

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.

S. Other operating income

Other operating income primarily relates to profits or losses arising on the disposal of properties arranged by National Grid's property management business, which is considered to be part of normal recurring operating activities but which does not represent revenue, income from the sale of emission allowances, and pension deficit recovery.

T. Emission allowances

Emission allowances, which relate to the emissions of carbon dioxide, are recorded as an intangible asset within current assets and are initially recorded at cost, and subsequently at the lower of cost and net realisable value. For allocations of emission allowances granted by the UK Government, cost is deemed to be equal to fair value at the date of allocation. Receipts of such grants are treated as deferred income and are recognised in the income statement in the period in which carbon dioxide emissions are made. A provision is recorded in respect of the obligation to deliver emission allowances and charges are recognised in the income statement in the period in which carbon dioxide emissions are made.

Income from the sale of emission allowances is reported as part of other operating income.

U. Cash and cash equivalents

Cash and cash equivalents include cash held at bank and in hand, together with short-term highly liquid investments with an original maturity of less than three months that are readily convertible to known amounts of cash and subject to an insignificant change in value and bank overdrafts, which are reported in borrowings.

V. Other reserves

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

W. Dividends

Interim dividends are recognised when they become payable to the Company's shareholders. Final dividends are recognised in the financial year in which they are approved.

X. Areas of judgement and key sources of estimation uncertainty

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

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

- The categorisation of certain items as exceptional items and remeasurements and the definition of adjusted earnings – note 4.
- The exemptions adopted on transition to IFRS on 1 April 2004.
- The recognition of defined benefit pension costs as if the National Grid UK Pension Scheme was a defined contribution scheme – accounting policy M.
- Hedge accounting – accounting policy P.

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 intangible assets and property, plant and equipment – accounting policies D, E and F.
- Valuation of financial instruments and derivatives – notes 12, 15 and 27.
- Revenue recognition and assessment of unbilled revenue – accounting policy K.
- Environmental provisions – note 21.

Adoption of new accounting standards

New IFRS accounting standards and interpretations adopted in 2009/10

During the year ended 31 March 2010, NGG adopted the following International Financial Reporting Standards (IFRS), International Accounting Standards (IAS) or amendments and interpretations by the International Financial Reporting Interpretations Committee (IFRIC). The impact of IFRIC 18 is to increase operating profit for the year ended 31 March 2010 and reduce liabilities at 31 March 2010 by £10m. In accordance with the transition provisions of IFRIC 18 'Transfers of assets from customers', comparative amounts have not been restated. None of the other pronouncements had a material impact on NGG's consolidated results or assets and liabilities.

IFRIC 18 on transfers of assets from customers	Addresses arrangements whereby an entity receives items of property, plant and equipment or cash which the entity must use to connect customers to a network or provide access to a supply of goods or services, or both.
IAS 1 revised on the presentation of financial statements	Requires changes to the presentation of financial statements and adopts revised titles for the primary statements, although companies may continue to use the existing titles.
Amendment to IFRS 7 on improving disclosures about financial instruments	Introduces a three-level hierarchy for fair value measurement disclosures and requires entities to provide additional disclosures about the relative reliability of fair value measurements. In addition, the amendment clarifies and enhances existing requirements for the disclosure of liquidity risk. The additional information required by this amendment can be found in note 28.
IFRS 8 on 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.
IAS 23 revised on 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.
IFRIC 13 on customer loyalty programmes	Clarifies that the sale of goods or services together with customer award credits (for example, loyalty points or the right to free products) is accounted for as a multiple-element transaction. The consideration received from the customer is allocated between the components of the arrangement based on their fair values, which will defer the recognition of some revenue.
Amendment to IFRS 2 on share-based payments	Clarifies the definition of vesting conditions and the accounting treatment of cancellations. Vesting conditions are defined as either service conditions or performance conditions. Cancellations by employees are accounted for in the same way as cancellations by the Company.
Amendments to IAS 32 and IAS 1 on puttable financial instruments and obligations arising on liquidation	Addresses the classification as a liability or as equity of certain puttable financial instruments and instruments, or components thereof, which impose upon an entity an obligation to deliver a pro rata share of net assets on liquidation.
Amendment to IFRS 1 First-time Adoption of International Financial Reporting Standards and IAS 27 Consolidated and Separate Financial Statements on the cost of an Investment in a Subsidiary, Jointly Controlled Entity or Associate	Permits investments to be recognised on first-time adoption of IFRS at cost or deemed cost (fair value or previous GAAP carrying amount) and removes the requirement to recognise dividends out of pre-acquisition profits as a reduction in the cost of the investment.
Improvements to IFRS 2008	Contains amendments to various existing standards.
IFRIC 15 on agreements for the construction of real estate	Addresses the timing of revenue recognition for entities engaged in the construction of real estate for their customers.
IFRIC 16 on hedges of a net investment in a foreign operation	Clarifies that a hedged risk may be designated at any level in a group and hedging instruments may be held by any company in a group (except the foreign entity being hedged), that net investment hedge accounting may not be adopted in respect of a presentation currency and that on disposal the amounts to be reclassified from equity to profit or loss are any cumulative gain or loss on the hedging instrument and the cumulative translation difference on the foreign operation disposed of.
Amendment to IAS 39 Financial Instruments: Recognition and measurement: Reclassification of Financial Assets: Effective Date and Transition	Clarifies the effective date of the reclassification of financial assets.
Amendments to IAS 39 and IFRIC 9 on embedded derivatives	Requires reassessment of whether an embedded derivative should be separated out if a financial asset is reclassified out of the fair value through profit or loss category.

New IFRS accounting standards and interpretations not yet adopted

The following standards and interpretations were not effective for the year ended 31 March 2010. None of these are expected to have a material impact on NGG's consolidated results or assets and liabilities.

IFRS 3R on business combinations	Makes a number of changes to the accounting for business combinations, including requirements that all payments to purchase a business are to be recorded at fair value at the acquisition date, with some contingent payments subsequently remeasured at fair value through income; an option to calculate goodwill based on the parent's share of net assets only or to include goodwill related to the minority interest; and a requirement that all transaction costs be expensed. IFRS 3R has been adopted by the Company with effect from 1 April 2010.
IAS 27R on consolidated and individual financial statements	Requires the effects of all transactions with non-controlling interests to be recorded in equity if there is no change in control. The revised standard also specifies the accounting when control is lost. IAS 27R has been adopted by the Company with effect from 1 April 2010.
Amendment to IAS 39 Financial Instruments: Recognition and measurement on eligible hedged items	Prohibits designating inflation as a hedgeable component of an instrument, unless cash flows relating to the separate inflation component are contractual and also prohibits the designation of a purchased option in its entirety as the hedge of a one-sided risk in a forecast transaction. The amendment to IAS 39 has been adopted by the Company with effect from 1 April 2010.
Revised IFRS 1 on first-time adoption of IFRS	Changes the structure, while retaining the substance, of the previously issued version of IFRS 1. The revised version of IFRS 1 has been adopted by the Company with effect from 1 April 2010.
IFRIC 17 on distribution of non-cash assets to owners	Requires such a distribution to be measured at the fair value of the asset and any difference between the carrying amount of the asset and its fair value to be recognised in profit or loss. IFRIC 17 has been adopted by the Company with effect from 1 April 2010.
Improvements to IFRS 2009	Contains amendments to various existing standards. The amendments have been adopted by the Company with effect from 1 April 2010.
Amendment to IFRS 2 on group cash settled share based payments	Clarifies the scope and accounting for group cash settled share based payment transactions in separate or individual financial statements when there is no obligation to settle the share based payment transaction. The amendment to IFRS 2 has been adopted by the Company with effect from 1 April 2010.
Amendment to IFRS 1 on first time adoption of IFRS	Provides additional exemptions for first time adopters. The amendment to IFRS 1 will be adopted by the Company with effect from 1 April 2010, subject to endorsement by the European Union.
Amendment to IAS 32 on classification of rights issues	Defines as an equity instrument a financial instrument that gives the holder the right to acquire a fixed number of the entity's equity instruments for a fixed amount of any currency, if the financial instrument is offered pro rata to all existing owners of the same class of non-derivative equity instruments. The amendment to IAS 32 has been adopted by the Company with effect from 1 April 2010.
Revised IAS 24 on related party disclosures	Simplifies the definition of a related party and provides a partial exemption for government-related entities. The revised version of IAS 24 will be adopted by the Company with effect from 1 April 2011, subject to endorsement by the European Union.
IFRS 9 on financial instruments	Requires that financial assets should be classified as at either amortised cost or fair value on the basis of the entity's business model and contractual cash flows. IFRS 9 will be adopted by the Company with effect from 1 April 2013, subject to endorsement by the European Union.
IFRIC 19 on extinguishing financial liabilities with equity instruments	Clarifies that equity instruments issued to extinguish a financial liability should be measured at fair value, unless fair value cannot reasonably be determined in which case the fair value of the liabilities extinguished should be used. IFRIC 19 will be adopted by the Company with effect from 1 April 2011, subject to endorsement by the European Union.
Amendment to IFRIC 14 on prepayments of a minimum funding requirement	Permits an entity to treat early payments of contributions to cover a minimum funding requirement as an asset. The amendment to IFRIC 14 will be adopted by the Company with effect from 1 April 2011, subject to endorsement by the European Union.
Amendment to IFRS 1 on comparative IFRS 7 disclosures	Provides limited disclosure exemptions in respect of financial instruments for first-time adopters of IFRS. The amendment to IFRS 1 will be adopted by the Company with effect from 1 April 2011, subject to endorsement by the European Union.

Consolidated income statement

for the years ended 31 March

	Notes	**2010 £m**	**2010 £m**	2009 £m	2009 £m
Revenue	1(a)		**2,747**		2,574
Other operating income	2		**14**		27
Operating costs	3		**(1,651)**		(1,834)
Operating profit					
Before exceptional items	1(b)	**1,297**		1,091	
Exceptional items	4	**(187)**		(324)	
Total operating profit	1(b)		**1,110**		767
Interest income and similar income	6		**3**		18
Interest expense and other finance costs					
Before exceptional items and remeasurements	6	**(257)**		(419)	
Exceptional items and remeasurements	4, 6	**33**		(6)	
	6		**(224)**		(425)
Profit before taxation					
Before exceptional items and remeasurements		**1,043**		690	
Exceptional items and remeasurements	4	**(154)**		(330)	
Total profit before taxation			**889**		360
Taxation					
Before exceptional items and remeasurements	7	**(322)**		(393)	
Exceptional items and remeasurements	4, 7	**34**		81	
Total taxation	7		**(288)**		(312)
Profit after taxation					
Before exceptional items and remeasurements		**721**		297	
Exceptional items and remeasurements	4	**(120)**		(249)	
Profit for the year			**601**		48
Profit for the year			**601**		48
Attributable to:					
Equity shareholders of the parent			**600**		47
Minority interests			**1**		1
			601		48

The notes on pages 43 to 72 form part of the consolidated financial statements.

The results reported above relate to continuing operations.

Consolidated statement of comprehensive income

for the years ended 31 March

	Notes	2010 £m	2009 £m
Profit for the year		**601**	48
Other comprehensive income:			
Net (loss)/gain taken to equity in respect of cash flow hedges		**(71)**	60
Transferred to profit or loss on cash flow hedges		**5**	(5)
Tax on items taken directly to or transferred from equity	7	**18**	(16)
Other comprehensive (expense)/income for the year		**(48)**	39
Total comprehensive income for the year		**553**	87
Total comprehensive income attributable to:			
Equity shareholders of the parent		**552**	86
Minority interests		**1**	1
		553	87

Consolidated balance sheet

at 31 March

	Notes	2010 £m	2009 £m
Non-current assets			
Intangible assets	9	**131**	77
Property, plant and equipment	10	**10,808**	10,359
Other non-current assets	11	**5,611**	5,611
Derivative financial assets	12	**565**	688
Total non-current assets		**17,115**	16,735
Current assets			
Inventories and other intangible assets	13	**43**	34
Trade and other receivables	14	**288**	450
Financial investments	15	**326**	1,009
Derivative financial assets	12	**72**	204
Cash and cash equivalents	16	**1**	-
Total current assets		**730**	1,697
Total assets	1(d)	**17,845**	18,432
Current liabilities			
Borrowings	17	**(449)**	(1,421)
Derivative financial liabilities	12	**(30)**	(67)
Trade and other payables	18	**(806)**	(814)
Current tax liabilities		**(19)**	(34)
Provisions	21	**(62)**	(51)
Total current liabilities		**(1,366)**	(2,387)
Non-current liabilities			
Borrowings	17	**(7,223)**	(7,251)
Derivative financial liabilities	12	**(121)**	(42)
Other non-current liabilities	19	**(1,104)**	(1,107)
Deferred tax liabilities	20	**(1,890)**	(1,777)
Provisions	21	**(110)**	(98)
Total non-current liabilities		**(10,448)**	(10,275)
Total liabilities		**(11,814)**	(12,662)
Net assets		**6,031**	5,770
Equity			
Called up share capital		**45**	45
Share premium account		**204**	204
Retained earnings		**4,492**	4,184
Cash flow hedge reserve		**(44)**	4
Other reserves		**1,332**	1,332
Shareholder's equity		**6,029**	5,769
Minority interest		**2**	1
Total equity		**6,031**	5,770

These financial statements, comprising the consolidated income statement, consolidated statement of comprehensive income, consolidated balance sheet, consolidated statement of changes in equity, consolidated cash flow statement, accounting policies, adoption of new accounting standards and the notes to the consolidated financial statements 1 to 31, were approved by the Board of Directors on 2 July 2010 and were signed on its behalf by:

Paul Whittaker Director

Adam Wiltshire Director

Consolidated statement of changes in equity

	Called up share capital £m	Share premium account £m	Cash flow hedge reserve £m	Other reserves £m	Retained earnings £m	Total shareholders' equity £m	Minority interest £m	Total equity £m
As at 1 April 2008	45	204	(35)	1,332	4,434	5,980	-	5,980
Total comprehensive income for the year	-	-	39	-	47	86	1	87
Equity dividends	-	-	-	-	(300)	(300)	-	(300)
Share-based payments	-	-	-	-	6	6	-	6
Tax on share-based payments	-	-	-	-	(3)	(3)	-	(3)
As at 31 March 2009	45	204	4	1,332	4,184	5,769	1	5,770
Total comprehensive income for the year	-	-	(48)	-	600	552	1	553
Equity dividends	-	-	-	-	(300)	(300)	-	(300)
Share-based payments	-	-	-	-	8	8	-	8
At 31 March 2010	**45**	**204**	**(44)**	**1,332**	**4,492**	**6,029**	**2**	**6,031**

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

Gains and losses recognised in the cash flow hedge reserve as of 31 March 2010 will be continuously transferred to the income statement until the borrowings are repaid (note 17).

The amount of the cash flow hedge reserve due to be released from reserves to the income statement within the next year is £4m, with the remaining amount due to be released with the same maturity profile as borrowings in note 17.

Consolidated cash flow statement

for the years ended 31 March

	Notes	2010 £m	2009 £m
Cash flows from operating activities			
Total operating profit		**1,110**	767
Adjustments for:			
Exceptional items	4	**187**	324
Depreciation and amortisation	1(c)	**432**	415
Profit on disposal of property, plant and equipment		**9**	(2)
Share based payment charge		**8**	6
Changes in working capital		**242**	(245)
Changes in provisions		**7**	1
Cash flows relating to exceptional items		**(123)**	(261)
Cash generated from operations		**1,872**	1,005
Tax paid		**(309)**	(71)
Net cash inflow from operating activities		**1,563**	934
Cash flows from investing activities			
Purchases of intangible assets		**(68)**	(32)
Purchases of property, plant and equipment		**(884)**	(957)
Disposals of property, plant and equipment		**-**	14
Interest received		**3**	19
Purchases of financial investments		**(307)**	(500)
Disposal of financial investments		**990**	9
Net cash flow used in investing activities		**(266)**	(1,447)
Cash flows from financing activities			
Proceeds from loans received		**306**	1,829
Repayment of loans		**(930)**	(1,389)
Net movements in short-term borrowings and derivatives		**(101)**	682
Interest paid		**(276)**	(318)
Dividends paid to shareholders	8	**(300)**	(300)
Net cash flow used in/from financing activities		**(1,301)**	504
Net decrease in cash and cash equivalents		**(4)**	(9)
Cash and cash equivalents at the start of the year (i)		**(10)**	(1)
Net cash and cash equivalents at the end of the year (i)	16	**(14)**	(10)

(i) Net of bank overdraft of £15m (2009: £10m).

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

1. Segmental analysis

The Board of Directors is NGG's chief operating decision making body (as defined by IFRS 8). The segmental analysis is based on the information the Board of Directors uses internally for the purposes of evaluating the performance of operating segments and determining resource allocation between segments. The performance of operating segments is assessed principally on the basis of operating profit before exceptional items and remeasurements. The following table describes the main activities for each operating segment:

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

Other activities relate to the xoserve business which provides transportation transaction services on behalf of all the major gas network transportation companies, including ourselves, together with corporate activities.

NGG's segments are unchanged from those reported in the financial statements for the year ended 31 March 2009. All of the Company's sales and operations take place within the UK.

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

a) Revenue

	Total sales 2010 £m	**Sales between businesses 2010 £m**	**Sales to third parties 2010 £m**	Total sales 2009 £m	Sales between businesses 2009 £m	Sales to third parties 2009 £m
Operating segments - continuing operations						
Gas Transmission	**934**	**-**	**934**	813	1	812
Gas Distribution	**1,516**	**55**	**1,461**	1,466	65	1,401
Gas Metering	**329**	**-**	**329**	340	1	339
Other activities	**45**	**22**	**23**	43	21	22
	2,824	**77**	**2,747**	2,662	88	2,574

The table above represents revenue from continuing operations only, as disclosed in the consolidated income statement. There was no revenue from discontinued operations.

b) Operating profit

	Before exceptional items		After exceptional items	
	2010 £m	2009 £m	**2010 £m**	2009 £m
Operating segments - continuing operations				
Gas Transmission	**450**	321	**350**	56
Gas Distribution	**711**	668	**667**	610
Gas Metering	**148**	125	**106**	124
Other activities	**(12)**	(23)	**(13)**	(23)
	1,297	1,091	**1,110**	767

The table above represents operating profit from continuing operations only, as disclosed in the consolidated income statement. Discontinued operations had no operating results during the year.

1. Segmental analysis continued

c) Capital expenditure and depreciation

	Capital expenditure		Depreciation and amortisation	
	2010 £m	2009 £m	**2010 £m**	2009 £m
Operating segments - continuing operations				
Gas Transmission	**232**	389	**127**	123
Gas Distribution	**670**	598	**201**	177
Gas Metering	**65**	90	**102**	113
Other activities	**5**	3	**2**	2
	972	1,080	**432**	415

Capital expenditure comprises additions to property, plant and equipment and intangible assets amounting to £904m (2009: £1,048m) and £68m (2009: £32m) respectively. There was no capital expenditure in respect of discontinued operations.

Depreciation and amortisation includes depreciation of property, plant and equipment and amortisation of intangible assets amounting to £413m (2009: £400m) and £19m (2009: £15m) respectively. There was no depreciation and amortisation in respect of discontinued operations.

d) Total assets

	Total assets	
	2010 £m	2009 £m
Operating segments - continuing operations		
Gas Transmission	**3,990**	3,866
Gas Distribution	**6,592**	6,139
Gas Metering	**662**	729
Other activities	**4**	7
	11,248	10,741
Unallocated	**6,597**	7,691
	17,845	18,432

Unallocated total assets include amounts owed by fellow subsidiaries, cash and cash equivalents, taxation, financial investments and derivative assets.

2. Other operating income

Other operating income includes income on disposal of properties as a result of property management, emissions trading income, and pension deficit recovery.

3. Operating costs

	Before exceptional items		Exceptional items		Total	
	2010	2009	**2010**	2009	**2010**	2009
	£m	£m	**£m**	£m	**£m**	£m
Depreciation of property, plant and equipment	**413**	400	**-**	-	**413**	400
Amortisation of intangible assets	**19**	15	**-**	-	**19**	15
Payroll costs	**255**	266	**16**	12	**271**	278
Other operating charges:						
Purchases of gas	**156**	172	**-**	-	**156**	172
Rates	**247**	236	**-**	-	**247**	236
Other	**374**	421	**171**	312	**545**	733
	1,464	1,510	**187**	324	**1,651**	1,834
Operating costs include:						
Consumption of inventories					**3**	4
Research expenditure					**10**	4
Operating lease rentals:						
Plant and machinery					**6**	5
Other					**10**	11

(a) Payroll costs

	2010	2009
	£m	£m
Wages and salaries	**267**	258
Social security costs	**24**	23
Other pension costs	**45**	54
Share-based payments	**8**	6
Severance costs (excluding pension costs)	**13**	5
	357	346
Less: payroll costs capitalised	**(86)**	(68)
	271	278

(b) Number of employees, including Directors

	31 March 2010 Number	**Average 2010 Number**	Average 2009 Number
UK			
Continuing operations	**6,302**	6,311	6,650

The vast majority of employees are either directly or indirectly employed in the transmission and distribution of gas.

(c) Key management compensation

	2010	2009
	£m	£m
Salaries and short-term employee benefits	**3**	3
Post-employment benefits	**2**	1
Share-based payments	**2**	1
	7	5

Key management comprises the Board of Directors of the Company together with those Executive Directors of National Grid plc who have managerial responsibility for any of the businesses of NGG and who are not also Directors of the Company.

3. Operating costs continued

(d) Directors' emoluments

The aggregate amount of emoluments paid to Directors in respect of qualifying services for 2010 was £1,476,935 (2009: £1,355,133). There were no payments in respect of compensation for loss of office in either year.

The highest paid Director and five other Directors exercised share options during 2010 (2009: highest paid Director and two other 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 2010, retirement benefits were accruing to six Directors under a defined benefit scheme (2009: six Directors under a defined benefit scheme).

The aggregate emoluments for the highest paid Director were £500,781 for 2010 (2009: £500,716); and total accrued annual pension at 31 March 2010 for the highest paid Director was £99,419 (2009: £85,676).

(e) Auditors' remuneration

	2010 £m	2009 £m
Audit services		
Audit of parent Company and consolidated financial statements	**0.2**	0.3
Other services		
Other services supplied pursuant to legislation	**0.2**	0.2

Other services supplied pursuant to legislation represents fees payable for services in relation to engagements which are required to be carried out by the auditor. In particular, this includes fees for audit reports on regulatory returns and fees for reports under section 404 of the US Public Company Accounting Reform and Investor Protection Act of 2002 (Sarbanes-Oxley).

4. Exceptional items and remeasurements

	2010 £m	2009 £m
Exceptional items - restructuring costs (i)	**(72)**	(83)
Exceptional items - environmental related provisions (ii)	**(14)**	(13)
Exceptional items - other (iii)	**(43)**	-
Pension deficit charges (iv)	**(58)**	(228)
Total exceptional items included within operating profit	**(187)**	(324)
Remeasurements - gains on derivative financial instruments (v)	**33**	(6)
Total exceptional items and remeasurements included within finance costs	**33**	(6)
Total exceptional items and remeasurements before taxation	**(154)**	(330)
Exceptional tax item - deferred tax charge arising from changes to the IBAs regime (vi)	**-**	(23)
Tax on exceptional items - restructuring costs (i)	**20**	23
Tax on exceptional items - other (iii)	**8**	-
Tax on exceptional items - pension deficit charges (iv)	**16**	81
Tax on remeasurements - derivative financial instruments (v)	**(10)**	-
Tax on exceptional items and remeasurements	**34**	81
Total exceptional items and remeasurements after taxation	**(120)**	(249)
Total exceptional items after taxation	**(143)**	(243)
Total derivative financial instrument remeasurements after taxation	**23**	(6)
Total exceptional items and remeasurements after taxation	**(120)**	(249)

(i) Restructuring costs include the further restructuring of our Liquefied Natural Gas (LNG) storage facilities of £39m (2009: £50m), transformation related initiatives of £10m (2009: £20m), costs associated with the outsource of elements of our Shared Services organisation of £9m (2009: £nil), pension curtailment costs as a result of redundancies of £10m (2009: £9m), and other business reorganisation costs.

(ii) Environmental provision related charges include £14m arising from changes in landfill tax legislation in the UK (2009: £8m). The prior year amount included a £5m charge arising from movements in discount rates due to reductions in market risk free rates.

(iii) Other costs for the year ended 31 March 2010 include £41m related to a fine of £15m together with associated costs, provisions against receivables and other balance sheet items (2009: £nil). For further details on the fine levied upon NGG by the Gas and Electricity Markets Authority (GEMA) refer to note 24(f).

(iv) Pension deficit charges arise from recovery plan contributions to the National Grid UK Pension Scheme.

(v) Remeasurements - gains on derivative financial instruments comprise gains and losses arising on derivative financial instruments reported in the income statement. These exclude gains and losses for which hedge accounting has been effective, which have been recognised directly in equity or offset by adjustments to the carrying value of debt

(vi) The exceptional tax charge in the prior period arose from changes to industrial buildings allowances (IBA) in the 2008 Finance Act. This resulted in an increase in deferred tax liabilities.

5. Pensions

Substantially all of NGG's 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 NGG. Accordingly, the Company accounts for the scheme as if it were a defined contribution scheme. For further details regarding the nature and terms of the scheme and the actuarial assumptions used to value the associated assets and pension obligations, refer to note 26.

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

	2010 £m	2009 £m
Amounts recognised in the consolidated balance sheet of National Grid plc		
Present value of funded obligations	**(13,483)**	(10,771)
Fair value of plan assets	**13,352**	11,040
	(131)	269
Present value of unfunded obligations	**(23)**	(15)
Net (liability)/asset	**(154)**	254

	2010 £m	2009 £m
Changes in the present value of the defined benefit obligation		
Opening defined benefit obligation (including unfunded obligations)	**(10,786)**	(11,831)
Current service cost	**(37)**	(47)
Interest cost	**(713)**	(762)
Actuarial (losses)/gains	**(2,607)**	1,244
Curtailment gains on redundancies	**6**	3
Special termination benefits	**(17)**	(11)
Curtailment cost - augmentations	**(3)**	(5)
Employee contributions	**(5)**	(7)
Benefits paid (including unfunded obligations)	**656**	630
Closing defined benefit obligation (including unfunded obligations)	**(13,506)**	(10,786)

	2010 £m	2009 £m
Changes in the fair value of plan assets		
Opening fair value of plan assets	**11,040**	12,660
Actual return on plan assets	**2,822**	(1,356)
Employer contributions	**156**	373
Employee contributions	**5**	7
Benefits paid (including unfunded obligations)	**(656)**	(630)
Expenses paid	**(15)**	(14)
Closing fair value of plan assets	**13,352**	11,040
Expected contributions to defined benefit plans in the following year	**65**	120

6. Finance income and costs

	2010 £m	2009* £m
Interest income on financial instruments (i)	**3**	18
Interest income and similar income	**3**	18
Interest expense on financial liabilities held at amortised cost:		
Interest on bank loans and overdrafts	**(13)**	(41)
Interest on other borrowings	**(284)**	(404)
Interest on derivatives	**42**	7
Other interest	**(8)**	(6)
Unwinding of discount on provisions	**(2)**	(3)
Less: interest capitalised (ii)	**8**	28
Interest expense	**(257)**	(419)
Net gains on derivative financial instruments included in remeasurements:		
Ineffectiveness on derivatives designated as fair value hedges (iii)	**25**	-
Ineffectiveness on derivatives designated as cash flow hedges	**3**	(7)
On derivatives not designated as hedges or ineligible for hedge accounting	**5**	1
Net gains/(losses) on derivative financial instruments included in remeasurements (iv)	**33**	(6)
Interest expense and other finance costs	**(224)**	(425)
Net finance costs	**(221)**	(407)
Comprising:		
Interest income and similar income	**3**	18
Interest expense and other finance costs		
Before exceptional items and remeasurements	**(257)**	(419)
Exceptional items and remeasurements	**33**	(6)
	(221)	(407)

*Comparatives have been restated to present items on a basis consistent with the current year classification.

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

(ii) Interest on funding attributable to assets in the course of construction was capitalised during the year at a rate of 3.6% (2009: 6.2%).

(iii) Includes a net loss on instruments designated as fair value hedges of £85m (2009: £245m gain) offset by a net gain of £110m arising from the fair value adjustments to the carrying value of debt (2009: £245m loss).

(iv) Includes a net foreign exchange gain on financing activities of £84m (2009: £383m loss). These amounts are offset by foreign exchange gains and losses on derivative financial instruments measured at fair value.

7. Taxation

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

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

	Before exceptional items and remeasurements		Exceptional items and remeasurements		Total	
	2010 £m	2009 £m	**2010 £m**	2009 £m	**2010 £m**	2009 £m
United Kingdom						
Corporation tax at 28%	**196**	180	**(34)**	(105)	**162**	75
Corporation tax adjustment in respect of prior years	**(5)**	105	**-**	-	**(5)**	105
	191	285	**(34)**	(105)	**157**	180
Deferred tax	**129**	110	**-**	24	**129**	134
Deferred tax adjustment in respect of prior years	**2**	(2)	**-**	-	**2**	(2)
	131	108	**-**	24	**131**	132
Total tax charge/(credit)	**322**	393	**(34)**	(81)	**288**	312

Taxation on items (credited)/charged to equity

	2010 £m	2009 £m
Deferred tax (credit)/charge on revaluation of cash flow hedges	**(18)**	14
Tax (credit)/charge recognised in consolidated statement of comprehensive income	**(18)**	14
Deferred tax charge on share-based payments recognised directly in equity	**-**	2
	(18)	16

The tax charge for the year after exceptional items and remeasurements is higher (2009: higher) than the standard rate of corporation tax in the UK of 28% (2009: 28%). The differences are explained below:

	Before exceptional items and remeasure-ments 2010 £m	**After exceptional items and remeasure-ments 2010 £m**	Before exceptional items and remeasure-ments 2009 £m	After exceptional items and remeasure-ments 2009 £m
Profit before taxation				
Before exceptional items and remeasurements	**1,043**	**1,043**	690	690
Exceptional items and remeasurements	**-**	**(154)**	-	(330)
Profit before taxation from continuing operations	**1,043**	**889**	690	360
Profit on continuing operations multiplied by the rate of corporation tax in the UK of 28% (2009: 28%)	**292**	**249**	193	101
Effects of:				
Adjustments in respect of prior years	**(3)**	**(3)**	103	103
Expenses not deductible for tax purposes	**3**	**4**	7	7
Non-taxable income	**-**	**-**	(1)	(1)
Impact of employee share schemes	**-**	**-**	2	2
Other	**30**	**38**	89	100
Total taxation from continuing operations	**322**	**288**	393	312
	%	**%**	%	%
At the effective income tax rate	**30.9**	**32.4**	57.0	86.7

7. Taxation continued

Factors that may affect future tax charges

A number of changes to the UK Corporation Tax system were announced in the 2010 Budget Report which have been enacted in the 2010 Finance Act. The impact of these is not considered to be material to the future tax charge in the UK.

Further changes were announced in the UK Government's Emergency Budget on 22 June 2010. This included a reduction in the main corporation tax rate from the current 28% to 24% comprising a 1% per annum reduction over the course of a four year period commencing from 1 April 2011. In addition, the rate of capital allowances on assets in the main pool is expected to fall from 20% to 18% and long life assets from 10% to 8% from 1 April 2012. We are in the process of evaluating the impact these changes will have on future tax charges.

Additionally, the worldwide debt cap, which restricts the amount of finance expense available for UK tax purposes, will apply for accounting periods ended 31 March 2011 onwards but is not expected to have a material effect on our future tax charge.

There is currently ongoing consultation on the reform of the controlled foreign company legislation. The outcome of the consultation process will not be known for some time and we will monitor the impact of the taxation on our holdings in our overseas operations.

Furthermore a number of additional issues will also be the subject of future consultation such as a possible general anti-avoidance rule. We will monitor the impact of these proposals on our future tax charge.

8. Dividends

The following table shows the dividends paid to equity shareholders:

	2010 pence (per ordinary share)	**2010 £m**	2009 pence (per ordinary share)	2009 £m
Ordinary dividends				
Interim dividend for the year ended 31 March 2010	**7.61**	**300**	-	-
Interim dividend for the year ended 31 March 2009	**-**	**-**	7.61	300
	7.61	**300**	7.61	300

9. Intangible assets

	Software £m
Non-current	
Cost at 1 April 2008	125
Additions	32
Disposals	(8)
Cost at 31 March 2009	149
Additions	68
Disposals	(1)
Reclassifications (i)	5
Cost at 31 March 2010	221
Amortisation at 1 April 2008	(65)
Amortisation charge for the year	(15)
Disposals	8
Amortisation at 31 March 2009	(72)
Amortisation charge for the year	(19)
Disposals	1
Amortisation at 31 March 2010	(90)
Net book value at 31 March 2010	**131**
Net book value at 31 March 2009	77

(i) Represents reclassification between categories - see note 10.

Current other intangible assets are presented together with inventories in note 13 and consist of emissions allowances of £15m (2009: £5m).

10. Property, plant and equipment

	Land and buildings £m	Plant and machinery £m	Assets in the course of construction £m	Motor vehicles and office equipment £m	Total £m
Cost at 1 April 2008	92	13,563	550	629	14,834
Additions	7	991	9	41	1,048
Disposals	-	(16)	-	(4)	(20)
Reclassifications	10	239	(235)	(14)	-
Cost at 31 March 2009	109	14,777	324	652	15,862
Additions	15	817	23	49	904
Disposals	(3)	(64)	-	(32)	(99)
Reclassifications (i)	-	302	(318)	11	(5)
Cost at 31 March 2010	121	15,832	29	680	16,662
Depreciation at 1 April 2008	(28)	(4,581)	-	(472)	(5,081)
Depreciation charge for the year	(9)	(344)	-	(47)	(400)
Impairment (ii)	-	(30)	-	-	(30)
Disposals	-	4	-	4	8
Reclassifications	(6)	6	-	-	-
Depreciation at 31 March 2009	(43)	(4,945)	-	(515)	(5,503)
Depreciation charge for the year	(11)	(347)	-	(55)	(413)
Impairment (ii)	-	(26)	(3)	-	(29)
Disposals	3	56	-	32	91
Reclassifications	-	-	-	-	-
Depreciation at 31 March 2010	(51)	(5,262)	(3)	(538)	(5,854)
Net book value at 31 March 2010	**70**	**10,570**	**26**	**142**	**10,808**
Net book value at 31 March 2009	66	9,832	324	137	10,359

(i) Represents reclassification between categories - see note 9.

(ii) Relates a to write down of property, plant and equipment items in the LNG storage business.

The net book value of land and buildings comprised:

	2010 £m	2009 £m
Freehold	**49**	41
Short leasehold (under 50 years)	**21**	25
	70	66

The cost of property, plant and equipment at 31 March 2010 included £132m (2009: £124m) relating to interest capitalised.

Included within trade and other payables and other non-current liabilities at 31 March 2010 are contributions to the cost of property, plant and equipment amounting to £25m (2009: £24m) and £1,038m (2009: £1,027m) respectively.

11. Other non-current assets

	2010 £m	2009 £m
Loans and receivables - amounts owed by parent	**5,611**	5,611

The amount owed by the parent is non-contractual and accordingly its fair value equals its book value.

12. Derivative financial instruments

For further information and a detailed description of our derivative financial instruments and hedge type designations, refer to note 27. The fair value by designated hedge type can be analysed as follows:

	2010			2009		
	Asset £m	**Liabilities £m**	**Total £m**	Asset £m	Liabilities £m	Total £m
Fair value hedges						
Interest rate swaps	**65**	**-**	**65**	98	-	98
Cross-currency interest rate swaps	**275**	**(6)**	**269**	488	(11)	477
	340	**(6)**	**334**	586	(11)	575
Cash flow hedges						
Interest rate swaps	**-**	**(55)**	**(55)**	1	(31)	(30)
Cross-currency interest rate swaps	**185**	**-**	**185**	210	(4)	206
	185	**(55)**	**130**	211	(35)	176
Derivatives not in a formal hedge relationship						
Interest rate swaps	**74**	**(75)**	**(1)**	53	(57)	(4)
Cross-currency interest rate swaps	**35**	**-**	**35**	39	-	39
Forward exchange forward contracts	**1**	**-**	**1**	3	-	3
Forward rate agreements	**-**	**(13)**	**(13)**	-	(6)	(6)
	110	**(88)**	**22**	95	(63)	32
	635	**(149)**	**486**	892	(109)	783
Hedge positions offset within derivative instruments	**2**	**(2)**	**-**	-	-	-
Total	**637**	**(151)**	**486**	892	(109)	783

The maturity of derivative financial instruments is as follows:

	2010			2009		
	Assets £m	**Liabilities £m**	**Total £m**	Assets £m	Liabilities £m	Total £m
In one year or less	**72**	**(30)**	**42**	204	(67)	137
Current	**72**	**(30)**	**42**	204	(67)	137
In more than one year, but not more than two years	**-**	**(6)**	**(6)**	-	-	-
In more than two years, but not more than three years	**15**	**(19)**	**(4)**	-	-	-
In more than three years, but not more than four years	**140**	**(22)**	**118**	5	(6)	(1)
In more than four years, but not more than five years	**-**	**(2)**	**(2)**	160	(19)	141
In more than five years	**410**	**(72)**	**338**	523	(17)	506
Non-current	**565**	**(121)**	**444**	688	(42)	646
	637	**(151)**	**486**	892	(109)	783

For each class of derivative the notional contract* amounts are as follows:

	2010 £m	2009 £m
Interest rate swaps	**(3,154)**	(2,924)
Cross-currency interest rate swaps	**(1,748)**	(1,707)
Foreign exchange forward contracts	**(39)**	(15)
Forward rate agreements	**(1,730)**	(3,345)
	(6,671)	(7,991)

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

13. Inventories and other intangible assets

	2010 £m	2009 £m
Raw materials and consumables	**28**	29
Other intangible assets	**15**	5
	43	34

Other intangible assets consists of emission allowances.

14. Trade and other receivables

	2010 £m	2009 £m
Trade receivables	**59**	47
Amounts owed by fellow subsidiaries	**22**	179
Other receivables	**5**	7
Prepayments and accrued income	**202**	217
	288	450

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.

Provision for impairment of receivables

	£m
At 1 April 2008	2
Release of provision	1
At 31 March 2009	3
Additions net of recoveries	15
At 31 March 2010	**18**

As at 31 March 2010, trade receivables of £2m (2009: £8m) were past due but not impaired. The ageing analysis of these trade receivables is as follows:

	2010 £m	2009 £m
Up to 3 months past due	**-**	3
3 to 6 months past due	**1**	2
Over 6 months past due	**1**	3
	2	8

For further information about wholesale credit risk refer to note 28(c).

15. Financial investments

	2010 £m	2009 £m
Current		
Available-for-sale investments - investments in short term money funds	**307**	990
Loans and receivables - amounts due from fellow subsidiaries	**19**	19
	326	1,009

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 - for further information on our treasury related credit risk refer to note 28. None of the financial investments are past due or impaired.

16. Cash and cash equivalents

	2010 £m	2009 £m
Cash at bank and short-term deposits	**1**	-
Cash and cash equivalents excluding bank overdrafts	**1**	-
Bank overdrafts	**(15)**	(10)
Net cash and cash equivalents	**(14)**	(10)

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 ranging between one day and three months, depending on immediate cash requirements, and earn interest at the respective short-term deposit rates.

17. Borrowings

The following table analyses borrowings, including bank overdrafts:

	2010 £m	2009 £m
Current		
Bank loans	**243**	275
Bonds	**115**	895
Other loans	**2**	2
Borrowings from fellow subsidiaries	**74**	239
Bank overdrafts (note 16)	**15**	10
	449	1,421
Non-current		
Bank loans	**659**	602
Bonds	**6,165**	6,229
Other loans	**149**	170
Borrowings from fellow subsidiaries	**250**	250
	7,223	7,251
Total borrowings	**7,672**	8,672

Total borrowings are repayable as follows:	2010 £m	2009 £m
In one year or less	**449**	1,421
In more than one year, but not more than two years	**251**	1
In more than two years, but not more than three years	**222**	250
In more than three years, but not more than four years	**730**	221
In more than four years, but not more than five years	**134**	752
In more than five years other than by instalments	**5,886**	6,027
	7,672	8,672

The fair value of borrowings at 31 March 2010 was £7,765m (2009: £7,760m). 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.

The notional amount outstanding of the debt portfolio as at 31 March 2010 was £7,819m (2009: £8,805m).

Collateral is placed with or received from any counterparty where we have entered into a credit support annex to the ISDA Master Agreement once the current mark-to-market valuation of the trades between the parties exceeds an agreed threshold. Included in current bank loans is £240m (2009: £273m) in respect of cash received under collateral agreements. No cash has been placed under collateral agreements.

In addition to the borrowings detailed above, subsequent to 31 March 2010 NGG drew down amounts totalling £300 million on loan agreements signed prior to the year end.

As at 31 March 2010, the Company had committed credit facilities of £700m (2009: £755m) of which £700m was undrawn (2009: £755m undrawn). These undrawn facilties expire within one year.

All of the unused facilities at 31 March 2010 and at 31 March 2009 were held as back-up to commercial paper and similar borrowings.

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

18. Trade and other payables

	2010 £m	2009 £m
Trade payables	**439**	382
Amounts owed to fellow subsidiaries	**125**	209
Social security and other taxes	**72**	62
Other payables	**34**	33
Deferred income	**136**	128
	806	814

Due to their short maturities, the fair value of trade and other payables (excluding deferred income) approximates to their book value.
All trade and other payables are recorded at amortised cost.

19. Other non-current liabilities

	2010	2009
	£m	£m
Trade payables	**-**	18
Other payables	**4**	-
Deferred income	**1,100**	1,089
	1,104	1,107

The fair value of trade and other payables approximates to their book value.
All other non current liabilities are recorded at amortised cost.

20. Deferred tax assets and liabilities

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

	Accelerated tax depreciation £m	Employee share options £m	Financial instruments £m	Other net temporary differences £m	Total £m
Deferred tax assets at 31 March 2008	-	(5)	-	(14)	(19)
Deferred tax liabilities at 31 March 2008	1,602	-	14	32	1,648
At 1 April 2008	1,602	(5)	14	18	1,629
Charged/(credited) to income statement	134	-	(2)	-	132
Charged to equity	-	2	14	-	16
At 31 March 2009	1,736	(3)	26	18	1,777
Deferred tax assets at 31 March 2009	-	(3)	-	(14)	(17)
Deferred tax liabilities at 31 March 2009	1,736	-	26	32	1,794
At 1 April 2009	1,736	(3)	26	18	1,777
Charged/(credited) to income statement	141	-	(5)	(5)	131
Credited to equity	-	-	(18)	-	(18)
At 31 March 2010	**1,877**	**(3)**	**3**	**13**	**1,890**
Deferred tax assets at 31 March 2010	-	(3)	-	(19)	(22)
Deferred tax liabilities at 31 March 2010	1,877	-	3	32	1,912
At 31 March 2010	**1,877**	**(3)**	**3**	**13**	**1,890**

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 (2009: £nil).

Deferred tax assets in respect of capital losses of £15m (2009: £24m) have not been recognised as their future recovery is uncertain or not currently anticipated. The capital losses are available to carry forward indefinitely. The capital losses can be offset against specific types of future capital gains.

21. Provisions

	Environmental £m	Emissions £m	Restructuring £m	Other £m	Total provisions £m
At 1 April 2008	44	5	21	46	116
Additions	13	6	34	16	69
Release of unused amounts	-	(9)	-	-	(9)
Unwinding of discount	2	-	-	1	3
Utilised	(3)	-	(12)	(15)	(30)
At 31 March 2009	56	2	43	48	149
Additions	14	4	30	11	59
Release of unused amounts	-	-	-	(2)	(2)
Unwinding of discount	2	-	-	-	2
Utilised	(2)	-	(25)	(9)	(36)
At 31 March 2010	**70**	**6**	**48**	**48**	**172**

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

	2010 £m	2009 £m
Current	**62**	51
Non-current	**110**	98
	172	149

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 plc (discounted using a nominal rate of 2.0%). The anticipated timing of the cash flows for statutory decontamination cannot be predicted with certainty, but they are expected to be incurred over the next 50 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. We have made our 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 2010 relating to gas site decontamination was £110m (2009: £85m), being the best undiscounted estimate of the liability having regard to the uncertainties referred to above.

Emissions provision

The provision for emission costs is expected to be settled using emission allowances granted or purchased.

Restructuring provision

At 31 March 2010, £26m of the total restructuring provision (2009: £19m) related to the restructuring of our Liquefied Natural Gas (LNG) storage facilities and £5m consisted of provisions for the disposal of surplus leasehold interests and rates payable on surplus properties (2009: £5m). The expected payment dates for property restructuring costs remain uncertain. The remainder of the restructuring provision related to business reorganisation costs, to be paid over the next two years.

Other provisions

Other provisions at 31 March 2010 include £6m (2009: £12m) in respect of property transfer costs related to the sales of four UK gas distribution networks and £21m (2009: £21m) in respect of employer liability claims. The payment dates for the property transfer costs are uncertain but should largely be over the next two years. In accordance with insurance industry practice, the estimates for employer liability claims are based on experience from previous years and, therefore, there is no identifiable payment date associated with these items.

22. Share capital

	Number of shares 2010 millions	Number of shares 2009 millions	2010 £m	2009 £m
At 31 March 2009 and 2010 - ordinary shares of $1^{2}/_{15}$p each				
Allotted, called up and fully paid	**3,944**	3,944	**45**	45

23. Consolidated cash flow statement

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

	2010 £m	2009 £m
Movement in cash and cash equivalents	**(4)**	(9)
(Decrease)/increase in financial investments	**(683)**	491
Decrease/(increase) in borrowings and derivatives	**725**	(1,122)
Net interest paid	**268**	310
Change in net debt resulting from cash flows	**306**	(330)
Changes in fair value of financial assets and liabilities	**(33)**	47
Net interest charge	**(252)**	(423)
Movement in net debt (net of related derivative financial instruments) in the year	**21**	(706)
Net debt at the start of the year	**(6,880)**	(6,174)
Net debt (net of related derivative financial instruments) at the end of the year	**(6,859)**	(6,880)

b) Analysis of changes in net debt

	Cash and cash equivalents £m	Bank overdrafts £m	Net cash £m	Financial investments £m	Borrowings £m	Derivatives £m	Total debt £m
At 1 April 2008	5	(6)	(1)	518	(6,810)	119	(6,174)
Cash flow	(5)	(4)	(9)	476	(1,401)	604	(330)
Fair value gains and losses	-	-	-	-	(6)	53	47
Interest charges	-	-	-	15	(445)	7	(423)
At 31 March 2009	-	(10)	(10)	1,009	(8,662)	783	(6,880)
Cash flow	1	(5)	(4)	(686)	1,100	(104)	306
Fair value gains and losses	-	-	-	-	202	(235)	(33)
Interest charges	-	-	-	3	(297)	42	(252)
At 31 March 2010	**1**	**(15)**	**(14)**	**326**	**(7,657)**	**486**	**(6,859)**

Notes to the consolidated financial statements - supplementary information

24. Commitments and contingencies

a) Future capital expenditure

	2010 £m	2009 £m
Contracted for but not provided	**533**	480

b) Lease commitments

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

	2010 £m	2009 £m
Amounts due:		
In one year or less	**16**	12
In more than one year, but not more than two years	**11**	10
In more than two years, but not more than three years	**9**	8
In more than three years, but not more than four years	**8**	7
In more than four years, but not more than five years	**7**	6
In more than five years	**26**	32
	77	75

The majority of the leases are in respect of properties.

c) Amounts receivable under sublease arrangements

The total of future minimum sublease payments expected to be received under non-cancellable subleases is £5m (2009: £2m).

d) Other commitments, contingencies and guarantees

The value of other commitments, contingencies and guarantees at 31 March 2010 amounted to £209m (2009: £150m), including gas purchase commitments amounting to £43m (2009: £70m), and guarantees relating to certain property obligations of a National Grid group undertaking of £1m (2009: £1m).

e) Parent Company loan guarantees on behalf of subsidiaries

The Company has guaranteed the repayment of principal sums, any associated premium and interest on specific loans due from its financial subsidiaries to third parties. At 31 March 2010, the sterling equivalent amounted to £1,168m (2009: £1,487m).

f) Litigation and claims

We reported in previous Annual Reports and Accounts a decision by the Gas and Electricity Markets Authority (GEMA) to fine National Grid £41.6m for a breach of the UK Competition Act 1998 in respect of term contracts with gas suppliers entered into by our metering services business in 2004. This decision was overturned in part and the fine reduced to £30m by the Competition Appeal Tribunal in April 2009 and the fine was further reduced to £15m by the Court of Appeal in a reserved judgement (not otherwise affecting the Competition Appeal Tribunal's judgement) issued in February 2010. On 22 March 2010, National Grid applied for leave to appeal the Court of Appeal's judgement to the Supreme Court.

As at 31 March 2010, we have provided for the fine together with associated costs and have provided against certain trade receivables and other balance sheet items. Without prejudice to our position in relation to appealing the Court of Appeal's judgement, the £15m fine was paid to GEMA on 1 April 2010.

In October 2008, we informed Ofgem that our mains replacement activity carried out by the Distribution business may have been misreported. Ofgem's investigation continues, so that at present it is too early to determine the likely outcome of the investigation, including the quantum of any amounts likely to be payable and any potential consequences as a result of it.

25. Related party transactions

The following information is provided in accordance with IAS 24, Related party disclosures, as being material transactions with related parties during the year. These transactions are with fellow subsidiaries of National Grid and a pension plan, in the normal course of business and are summarised below.

	Parent		Other related parties		Total	
	2010 £m	2009 £m	**2010 £m**	2009 £m	**2010 £m**	2009 £m
Income:						
Goods and services supplied	**-**	-	**21**	19	**21**	19
Expenditure:						
Services received	**-**	-	**35**	76	**35**	76
Corporate services received	**-**	-	**16**	21	**16**	21
Charges in respect of pensions costs	**-**	-	**78**	238	**78**	238
Charges in respect of share-based payments	**-**	-	**7**	6	**7**	6
Interest received on borrowings from fellow subsidiaries	**-**	-	**-**	(3)	**-**	(3)
Interest paid on borrowings from fellow subsidiaries	**-**	2	**10**	18	**10**	20
	-	2	**146**	356	**146**	358
Outstanding balances at 31 March in respect of income, expenditure and settlement of corporation tax:						
Amounts receivable	**-**	-	**22**	179	**22**	179
Amounts payable	**-**	-	**125**	209	**125**	209
Advances to fellow subsidiaries (due within one year):						
At 1 April	**19**	19	**-**	-	**19**	19
Advances	**-**	-	**-**	-	**-**	-
At 31 March	**19**	19	**-**	-	**19**	19
Advances to parent (due after more than one year):						
At 1 April and 31 March	**5,611**	5,611	**-**	-	**5,611**	5,611
Borrowings payable to fellow subsidiaries (amounts due within one year):						
At 1 April	**-**	186	**239**	361	**239**	547
Advances	**-**	-	**-**	197	**-**	197
Repayments	**-**	(186)	**(165)**	(319)	**(165)**	(505)
At 31 March	**-**	-	**74**	239	**74**	239
Borrowings payable to fellow subsidiaries (amounts due after more than one year):						
At 1 April	**-**	-	**250**	-	**250**	-
Advances	**-**	-	**-**	250	**-**	250
At 31 March	**-**	-	**250**	250	**250**	250

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

No amounts have been provided at 31 March 2010 (2009: £nil) and no expense has been recognised during the year (2009: £nil) in respect of bad or doubtful debts for related party transactions.

Details of guarantees provided in respect of related parties are provided in note 24.

Details of key management compensation are provided in note 3(c).

26. Actuarial information on pensions

The National Grid UK Pension Scheme is funded with assets held in a separate trustee administered fund. The scheme is subject to independent actuarial valuation 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 employees and the proceeds from the scheme's assets, are expected to be sufficient to fund the benefits payable under the 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 latest full actuarial valuation was carried out by Towers Watson as at 31 March 2007. The aggregate market value of the scheme's assets was £12,923m and the value of the assets represented 97% of the actuarial value of benefits due to members, calculated on the basis of pensionable earnings and service at 31 March 2007 on an ongoing basis and allowing for projected increases in pensionable earnings. There was a funding deficit of £442m (£309m net of tax) on the valuation date in light of which National Grid agreed a recovery plan with the trustees.

The actuarial valuation showed that, based on long-term financial assumptions, the contribution rate required to meet future benefit accrual was 32.4% of pensionable earnings (29.4% employers and 3% employees). In addition, the employers pay an allowance for administration expenses which was 3.2% of pensionable earnings for 2009/10, giving a total Company rate of 32.6% of pensionable earnings. These employer contribution rates will be reviewed at the next valuation on 31 March 2011, whilst the administration rate is reviewed annually.

In accordance with the recovery plan agreed with the trustees at the 2007 valuation date, NGG paid contributions of £58m (£42m net of tax) during the year which ensured that the deficit reported in the 2007 valuation was paid in full. Contributions to the scheme during the year to March 2011 are expected to comprise ongoing normal contributions only.

Asset allocations and actuarial assumptions

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

	2010	2009
	%	%
Equities	**34.7**	33.9
Corporate bonds	**34.5**	34.7
Gilts	**22.0**	21.0
Property	**6.2**	5.5
Other	**2.6**	4.9
Total	**100.0**	100.0

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 scheme. 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 current target asset allocation for the scheme is 33% equities, 59% bonds and 8% property and other.

The principal actuarial assumptions used were:	**2010** %	2009 %
Discount rate (i)	**5.6**	6.8
Expected return on plan assets	**6.2**	6.4
Rate of increase in salaries (ii)	**4.7**	3.8
Rate of increase in pensions in payment and deferred pensions	**3.8**	3.0
Rate of increase in Retail Prices Index	**3.8**	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.

The assumed life expectations for a retiree at age 65 are as follows:	**2010**	2009
	years	years
Today:		
Males	20.8	20.8
Females	23.3	23.2
In 20 years:		
Males	23.2	23.1
Females	25.6	25.5

Sensitivities analysed - all other assumptions held constant:

	Change in pension obligations		Change in annual pension cost	
	2010	2009	**2010**	2009
	£m	£m	**£m**	£m
0.1% increase in discount rate	**210**	143	**2**	1
0.5% increase in long term rate of increase in salaries	**85**	51	**4**	2
Increase of one year to life expectancies at age 60	**430**	269	**2**	1

27. Supplementary information on 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, or other indices. Derivatives enable their users to alter exposure to market or credit risks. We use derivatives to manage our treasury risks.

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 mitigates the market risk which would otherwise arise from the maturity and other profiles of its assets and liabilities.

Hedging policies using derivative financial instruments are further explained in note 28. 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:

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 life of the hedged item.

Cash flow hedges

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

Derivatives not in a formal hedge relationship

Our policy is not to use derivatives for trading purposes. However, due to the complex nature of hedge accounting under IAS 39 some derivatives may not qualify for hedge accounting, or are specifically not designated as a hedge where natural offset is more appropriate.

Changes in the fair value of any derivative instruments that do not qualify for hedge accounting are recognised immediately in remeasurements within the income statement.

28. Financial risk

Our activities expose us to a variety of financial risks: market risk (including foreign exchange risk; fair value interest rate risk and 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 related to financial activities is carried out by a central treasury department under policies approved by the Boards of Directors of National Grid plc and NGG. This department identifies, evaluates and hedges financial risks in close co-operation with the operating units. The 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 our treasury policy, described on page 19 of the Operating and Financial Review.

(a) Market risk

(i) Foreign exchange risk

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

With respect to near term foreign exchange risk, we use foreign exchange forwards to manage foreign exchange transaction exposure. Our policy is to hedge a minimum percentage of known contracted foreign currency flows in order to mitigate foreign currency movements in the intervening period. Where cash forecasts are less certain, we generally cover a percentage of the foreign currency flows depending on the level of agreed probability for those future cash flows.

During the years ended 31 March 2010 and 2009, derivative financial instruments were used to manage foreign exchange risk as follows:

	2010				
	Sterling £m	**Euro £m**	**US dollar £m**	**Other £m**	**Total £m**
Cash and cash equivalents	**1**	**-**	**-**	**-**	**1**
Financial investments	**326**	**-**	**-**	**-**	**326**
Borrowings*	**(5,510)**	**(1,119)**	**(713)**	**(330)**	**(7,672)**
Pre-derivative position	**(5,183)**	**(1,119)**	**(713)**	**(330)**	**(7,345)**
Derivative effect	**(1,687)**	**1,129**	**714**	**330**	**486**
Net debt position	**(6,870)**	**10**	**1**	**-**	**(6,859)**

	2009				
	Sterling £m	Euro £m	US dollar £m	Other £m	Total £m
Cash and cash equivalents	-	-	-	-	-
Financial investments	1,008	1	-	-	1,009
Borrowings*	(6,296)	(1,323)	(793)	(260)	(8,672)
Pre-derivative position	(5,288)	(1,322)	(793)	(260)	(7,663)
Derivative effect	(1,582)	1,332	773	260	783
Net debt position	(6,870)	10	(20)	-	(6,880)

*Includes bank overdrafts

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

28. Financial risk continued

(a) Market risk continued

(ii) Cash flow and fair value interest rate risk

Interest rate risk arises on NGG's borrowings. Borrowings issued at variable rates expose NGG to cash flow interest rate risk. Borrowings issued at fixed rates expose NGG to fair value interest rate risk. Our interest rate risk management policy as further explained on page 20 is to minimise the finance costs (being interest costs and changes in the market value of debt) subject to certain constraints. Some of our borrowings issued are index-linked, that is their cost is linked to changes in the UK Retail Prices Index (RPI). We believe that these borrowings provide a hedge for revenues and regulatory asset values that are also RPI-linked.

Interest rate risk arising from our financial investments is primarily variable being mainly composed of short dated money funds.

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:

	2010 £m	2009 £m
Fixed interest rate borrowings		
In one year or less	**(98)**	(702)
In more than one year but not more than two years	**(1)**	(1)
In more than two years but not more than three years	**(22)**	-
In more than three years but not more than four years	**(730)**	(21)
In more than four years but not more than five years	**-**	(752)
In more than five years	**(2,777)**	(2,952)
	(3,628)	(4,428)
Floating interest rate borrowings (including RPI)	**(4,044)**	(4,243)
Non-interest bearing borrowings	**-**	(1)
Total borrowings	**(7,672)**	(8,672)

During the years ended 31 March 2010 and 2009, net debt was managed using derivative instruments to hedge interest rate risk as follows:

	2010				
	Fixed rate £m	**Floating rate £m**	**RPI (i) £m**	**Other (ii) £m**	**Total £m**
Cash and cash equivalents	**1**	**-**	**-**	**-**	**1**
Financial investments	**-**	**326**	**-**	**-**	**326**
Borrowings*	**(3,628)**	**(914)**	**(3,130)**	**-**	**(7,672)**
Pre-derivative position	**(3,627)**	**(588)**	**(3,130)**	**-**	**(7,345)**
Derivative effect	**756**	**(387)**	**117**	**-**	**486**
Net debt position (iii)	**(2,871)**	**(975)**	**(3,013)**	**-**	**(6,859)**

	2009				
	Fixed rate £m	Floating rate £m	RPI(i) £m	Other (ii) £m	Total £m
Financial investments	-	1,009	-	-	1,009
Borrowings*	(4,428)	(1,146)	(3,097)	(1)	(8,672)
Pre-derivative position	(4,428)	(137)	(3,097)	(1)	(7,663)
Derivative effect	1,407	(876)	249	3	783
	(3,021)	(1,013)	(2,848)	2	(6,880)

*Includes bank overdrafts

(i) The post-derivative impact represents financial instruments linked to UK RPI.

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

(iii) The post derivative impact includes short dated derivative contracts maturing within 12 months of the balance sheet date.

28. Financial risk continued

(b) Fair value disclosures

The following is an analysis of our financial instruments measured at fair value. They are reported in a tiered hierarchy based on the valuation methodology described on page 21, and reflecting the significance of market observable inputs.

The levels are classified as follows:

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

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

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

The best evidence of fair value is a quoted price in an actively traded market. In the event that the market for a financial instrument is not active, a valuation technique is used.

The fair value classification of our financial assets and financial liabilities is as follows:

	2010			
	Level 1 £m	Level 2 £m	Level 3 £m	Total £m
Assets				
Available-for-sale investments	**307**	**-**	**-**	**307**
Derivative financial instruments	**-**	**635**	**2**	**637**
	307	**635**	**2**	**944**
Liabilities				
Derivative financial instruments	**-**	**(151)**	**-**	**(151)**
	-	**(151)**	**-**	**(151)**
Total	**307**	**484**	**2**	**793**

The financial instruments classified as level 3 are currency swaps where the currency forward curve is illiquid.

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

	Derivative financial instruments £m
At 1 April 2009	**(1)**
Total recognised income and expense for the year (i)	**3**
Settlements	**-**
At 31 March 2010	**2**

(i) Gains of £3m are attributable to assets or liabilities held at the end of the reporting period.

28. Financial risk continued

(c) Credit risk

Credit risk is managed on a portfolio basis for National Grid 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. Our limits are managed by the central treasury department of National Grid plc, as explained in our treasury policy on page 21.

As at 31 March 2010 and 2009, we had a number of exposures to individual counterparties. In accordance with our 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. We do not expect any significant losses from non-performance by these counterparties.

The counterparty exposure under derivative financial contracts as shown in note 12 was £637m (2009: £892m); after netting agreements it was £550m (2009: £847m). This exposure is further reduced by collateral received as shown in note 17.

Wholesale and retail credit risk

Our 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. 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 14.

(d) Liquidity analysis

We determine our liquidity requirements by the use of both short and long term cash flow forecasts. These forecasts are supplemented by a financial headroom analysis which is used to assess funding adequacy for at least a 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 2010	**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	**(330)**	**(252)**	**(221)**	**(7,091)**	**(7,894)**
Interest payments on borrowings (i)	**(248)**	**(253)**	**(256)**	**(3,819)**	**(4,576)**
Other non-interest bearing liabilities	**(473)**	**(4)**	**-**	**-**	**(477)**
Derivative financial liabilities					
Derivative contracts - receipts	**135**	**77**	**91**	**893**	**1,196**
Derivative contract - payments	**(60)**	**(41)**	**(48)**	**(637)**	**(786)**
Total at 31 March 2010	**(976)**	**(473)**	**(434)**	**(10,654)**	**(12,537)**

At 31 March 2009	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	(1,519)	-	-	(7,285)	(8,804)
Interest payments on borrowings (i)	(274)	(255)	(262)	(4,038)	(4,829)
Other non-interest bearing liabilities	(415)	-	-	-	(415)
Derivative financial liabilities					
Derivative contract - receipts	450	125	57	674	1,306
Derivative contract - payments	(41)	(35)	(28)	(428)	(532)
Total at 31 March 2009	(1,799)	(165)	(233)	(11,077)	(13,274)

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

28. Financial risk continued

(e) Sensitivity analysis

Financial instruments affected by market risk include borrowings, deposits and derivative financial instruments. The following analysis illustrates 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 2010 and 31 March 2009, respectively. As a consequence, this sensitivity analysis relates to the positions at those dates and is not representative of the years 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 other deposits are carried at amortised cost and so their carrying value does not change as interest rates move;
- the sensitivity of accrued interest to movements in interest rates is calculated on net floating rate exposures on debt, deposits and derivative instruments;
- 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 impact 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, after the effects of tax.

	2010		2009	
	Income statement -/+ £m	**Other Equity Reserves -/+ £m**	Income statement -/+ £m	Other Equity Reserves -/+ £m
UK Retail Prices Index +/- 0.50%	**10**	**-**	10	-
UK interest rates +/- 0.50%	**5**	**16**	7	16

The income statement sensitivities impact interest expense and financial instrument remeasurements.

(f) Capital and risk management

NGG's objective when managing capital is to safeguard its ability to continue as a going concern and to remain within regulatory constraints. The principal measure of balance sheet efficiency is gearing calculated as net debt expressed as a percentage of regulatory asset value. The gearing ratio at 31 March 2010 was 57% compared with 60% at 31 March 2009. We regularly review and maintain or adjust the capital structure as appropriate in order to manage the level of gearing.

Our licence and some of our bank loan agreements impose lower limits for the long-term credit ratings that the Company must hold. These requirements are monitored on a regular basis in order to ensure compliance.

29. Share options and reward plans

National Grid operates three principal forms of share option and award plans in which our employees and Directors participate. These are an employee Sharesave scheme, a Performance Share Plan (PSP) and Deferred Share Plan.

Active share plans

The Sharesave scheme is savings related where, under normal circumstances, share options are exercisable on completion of a three or a five-year Save-As-You-Earn contract. The exercise price of options granted represents 80% of the market price at the time of the invitation.

Under the PSP, awards have been made to Directors and approximately 121 senior employees. Awards made in 2004 have lapsed. For awards made from 2005, the criteria was amended so that 50% is based on National Grid's Total Shareholder Return (TSR) performance when compared to the FTSE 100 and 50% is based on the annualised growth of National Grid's earnings per share compared to the growth in RPI (the general index of retail prices for all items). Awards are delivered in National Grid plc shares.

Under the Deferred Share Plan, one half of any bonus earned by Executive Directors of National Grid plc and a predetermined part of any bonus earned by other Directors and senior employees is automatically deferred into National Grid shares. The shares are held in trust for three years before release.

Additional information in respect of active share schemes

	2010 **000s**	2009 000s
Performance share plan		
Awards of ordinary share equivalents at 1 April	**1,287**	990
Awards made	**561**	402
Lapses/forfeits	**(19)**	(58)
Exercises	**(582)**	(54)
Transfers (i)	**-**	7
Awards of ordinary share equivalents at 31 March	**1,247**	1,287
Conditional awards available for release at 31 March	**-**	268
Deferred share plan		
Awards of ordinary share equivalents at 1 April	**99**	66
Awards made	**32**	47
Lapses/forfeits	**-**	-
Exercises	**(60)**	(14)
Awards of ordinary share equivalents at 31 March	**71**	99
Conditional awards available for release at 31 March	**-**	-

(i) Transfers arise from employees moving between National Grid Gas and other companies in the National Grid group.

Non-active share plans

We also have a number of historical plans under which awards are still outstanding, but no further awards will be granted. These include the Executive Share Option Plan and the Share Matching Plan.

The Executive Share Option Plan applied to senior executives, including Executive Directors of National Grid plc. Options granted were subject to the achievement of performance targets related to National Grid's TSR over a three-year period and those for 2000 are subject to a final retest in 2010 after which they will lapse if the performance criteria is not met. The share options are generally exercisable between the third and tenth anniversaries of the date of grant if the relevant performance target is achieved.

The Share Matching Plan applied to Executive Directors of National Grid plc and other Directors and senior employees whereby a predetermined part of each participant’s bonus entitlement is automatically deferred into National Grid plc shares (known as qualifying shares) and a matching award may be exercised under the Plan after a three-year period, provided the Director or senior employee remains employed by National Grid.

Additional information in respect of non-active share schemes

	2010 **000s**	2009 000s
Share matching plan		
Awards at 1 April	**16**	**20**
Awards exercised	**(4)**	**(4)**
Awards of ordinary share equivalents at 31 March	**12**	**16**
Conditional awards available for release at 31 March	**12**	**16**

29. Share options and reward plans continued

Share options

Movements in options to subscribe for ordinary shares under National Grid's various option schemes for the two years ended 31 March 2010 and 31 March 2009 is shown below:

	Sharesave scheme options		Executive Plan options		Total options
	Weighted average price £	millions	Weighted average price £	millions	millions
At 31 March 2008	4.85	10.3	4.51	0.1	10.4
Granted	4.88	4.1	-	-	4.1
Lapsed - expired	5.97	(1.1)	-	-	(1.1)
Exercised	3.84	(1.3)	-	-	(1.3)
Transfers (i)	-	-	-	-	-
At 31 March 2009	4.86	12.0	4.57	0.1	12.1
Granted	5.20	2.4	-	-	2.4
Lapsed - expired	5.41	(0.6)	-	-	(0.6)
Exercised	3.96	(2.4)	-	-	(2.4)
At 31 March 2010	**5.10**	**11.4**	**4.59**	**0.1**	**11.5**

Included within options outstanding at 31 March 2010 and 31 March 2009 were the following options which were exercisable:

At 31 March 2010	**5.15**	**0.5**	**4.41**	**0.1**	**0.6**
At 31 March 2009	4.85	0.1	4.40	0.1	0.2

(i) Transfers arise from employees moving between National Grid Gas and other companies in the National Grid group.

The weighted average remaining contractual life of options in the employee Sharesave scheme at 31 March 2010 was 2 years and 1 month. These options have exercise prices between £3.17 and £6.55.

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

	2010 £	2009 £
Sharesave scheme options	**5.74**	6.99
Executive Plan options	**6.03**	6.81

Additional information in respect of share options

Options outstanding and exercisable and their weighted average exercise prices for the respective ranges of exercise prices and years at 31 March 2010 are as follows:

	Weighted average exercise price of exercisable options £	Number exercisable	Weighted average exercise price of outstanding options £	Number outstanding	Exercise price per share pence	Normal dates of exercise years
Executive plan	-	-	5.27	16,693	526.00-531.50	2004-2011
	4.41	61,858	4.41	61,858	434.25-460.25	2000-2013
	4.41	61,858	4.57	78,551		

29. Share options and reward plans continued

Share-based payment charges

The charge to the income statement for the year ended 31 March 2010 was £8m (2009: £6m).

Awards under share option plans

The average share prices at the date of options being granted, the average price of the options granted and their estimated average fair values during each of the two financial years ended 31 March were as follows:

	2010	2009
Average share price	**676.0p**	684.0p
Average exercise price	**520.0p**	488.0p
Average fair value	**287.9p**	166.8p

These amounts have been calculated in respect of options where the exercise price is less than the market price at the date of grant.

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

	2010	2009
Dividend yield (%)	**5.0**	5.0
Volatility (%)	**22.4-26.1**	22.4-26.1
Risk-free investment rate (%)	**2.5**	2.5
Average life (years)	**4.0**	3.9

The fair values of awards under the Sharesave scheme have been calculated using the Black-Scholes European model. This is considered appropriate given the short exercise window of sharesave options. The fair values of awards made in 2009 and 2008 onwards have been calculated by reference to the 2006 Black-Scholes European model calculation.

Volatility was derived based on the following and is assumed to revert from its current implied level to its long run mean based historical volatility under (ii) below:

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

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

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

Awards under other share scheme plans

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

	2010	2009
Average share price	**598.2p**	670.1p
Average fair value	**355.6p**	458.1p

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

	2010	2009
Dividend yield (%)	**4.4**	4.4
Risk-free investment rate (%)	**2.5**	2.5

Fair values have been calculated using a Monte Carlo simulation model for awards with total shareholder return performance conditions made prior to 1 April 2006. The fair value of awards made in 2008 and 2007 has been calculated by reference to the 2006 Monte Carlo simulation model calculation. Fair values of awards with performance conditions based on earnings per share have been calculated using the share price at date of grant less the present value of dividends foregone during the performance period.

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

30. Ultimate parent company

National Grid Gas plc's immediate parent Company is National Grid Gas Holdings Limited. The ultimate parent Company and controlling party is National Grid plc. Both of these companies are incorporated in Great Britain and are registered in England and Wales. National Grid plc consolidates the accounts of National Grid Gas plc. Copies of the consolidated accounts of National Grid plc may be obtained from the Company Secretary, 1-3 Strand, London WC2N 5EH.

31. Principal subsidiary undertakings

	Principal activity	Holding
National Grid Gas Finance (No 1) plc	Financing	100%
National Grid Metering Limited	Gas metering services	100%
British Transco International Finance BV (incorporated in the Netherlands)	Financing	100%
British Transco Finance Inc. (incorporated in the US)	Financing	100%
British Transco Capital Inc. (incorporated in the US)	Financing	100%
British Transco Finance (No. 1) Limited	Financing	100%
British Transco Finance (No. 2) Limited	Financing	100%
British Transco Finance (No. 3) Limited	Financing	100%
British Transco Finance (No. 5) Limited	Financing	100%
xoserve Limited	Gas transportation transaction services	56.57%

A full list of all subsidiaries and associated undertakings is available from the Company Secretary of the Company.

Company accounting policies

for the year ended 31 March 2010

A. Basis of preparation of individual financial statements under UK GAAP

These individual financial statements of the Company have been prepared in accordance with applicable UK accounting and financial reporting standards and the Companies Act 2006.

The individual financial statements of the Company have been prepared on a historical cost basis, except for the revaluation of financial instruments.

These financial statements are presented in pounds sterling because that is the currency of the primary economic environment in which the Company operates.

The Company has not presented its own profit and loss account as permitted by section 408 of the Companies Act 2006. The Company has taken the exemption from preparing a cash flow statement under the terms of FRS 1 (revised 1996) ‘Cash Flow Statements’.

In accordance with exemptions under FRS 8 ‘Related party disclosures’, the Company has not disclosed transactions with related parties, as the Company’s financial statements are presented together with its consolidated financial statements. Furthermore, in accordance with exemptions under FRS 29 ‘Financial Instruments: Disclosures’, the Company has not presented the financial instruments disclosures required by the standard, as disclosures which comply with the standard are included in the consolidated financial statements.

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.

B. Foreign currencies

Transactions in currencies other than the functional currency of the Company are recorded at the rates of exchange prevailing on the dates of the transactions. At each balance sheet date, monetary assets and liabilities that are denominated in foreign currencies are retranslated at closing exchange rates. Gains and losses arising on retranslation of monetary assets and liabilities are included in the profit and loss account.

C. Tangible fixed assets

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

Tangible fixed assets include assets in which the Company’s interest comprises legally protected statutory or contractual rights of use.

Additions represent the purchase or construction of new assets, extensions to, or significant increases in, the capacity of tangible fixed assets.

Contributions received towards the cost of tangible fixed assets are included in creditors as deferred income and credited on a straight-line basis to the profit and loss account over the life of the assets.

Depreciation is not provided on freehold land or assets in the course of construction. Other tangible fixed assets are depreciated principally on a straight-line basis, at rates estimated to write off their book values over their estimated useful economic lives. In assessing estimated useful economic lives, which are reviewed on a regular basis, consideration is given to any contractual arrangements and operational requirements relating to particular assets. Unless otherwise determined by operational requirements, the depreciation periods for the principal categories of tangible fixed assets are, in general, as shown in the table below:

Depreciation periods	Years
Freehold and leasehold properties	up to 50
Plant and machinery:	
– Mains, services and regulating equipment	30 to 100
– Meters and metering equipment	5 to 18
Motor vehicles and office equipment	3 to 10

D. Fixed asset investments

Investments held as fixed assets are stated at cost less any provisions for impairment.

E. Impairment of fixed assets

Impairments of fixed assets are calculated as the difference between the carrying values of the net assets of income generating units, including where appropriate, investments, and their recoverable amounts. Recoverable amount is defined as the higher of net realisable value or estimated value in use at the date the impairment review is undertaken. Net realisable value represents the amount that can be generated through the sale of assets. Value in use represents the present value of expected future cash flows discounted on a pre-tax basis, using the estimated cost of capital of the income generating unit.

Impairment reviews are carried out if there is some indication that impairment may have occurred, or where otherwise required to ensure that fixed assets are not carried above their estimated recoverable amounts. Impairments are recognised in the profit and loss account, and, where material, are disclosed as exceptional. Impairment reversals are recognised when, in management’s opinion, the reversal is permanent.

F. Taxation

Current tax for the current and prior periods is provided at the amount expected to be paid (or recovered) using the tax rates and tax laws that have been enacted or substantively enacted by the balance sheet date. Current tax assets and liabilities arising from transfer pricing adjustments, which are expected to be fully recovered through group relief, are initially estimated and recognised in the current year where material. Further adjustments are recognised when tax returns are submitted to the tax authorities.

Deferred tax is provided in full on timing differences which result in an obligation at the balance sheet date to pay more tax, or the right to pay less tax, at a future date, at tax rates expected to apply when the timing differences reverse, based on tax rates and tax laws that have been enacted or substantively enacted by the balance sheet date. Timing differences arise from the inclusion of items of income and expenditure in taxation computations in periods different from those in which they are included in the financial statements. Deferred tax assets are recognised to the extent that it is regarded as more likely than not that they will be recovered. Deferred tax assets and liabilities are not discounted.

G. Stocks

Stocks are stated at cost less provision for deterioration and obsolescence.

H. Environmental costs

Environmental costs, based on discounted future estimated expenditures expected to be incurred, are provided for in full. The unwinding of the discount is included within the profit and loss account as a financing charge.

I. Revenue

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

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

J. Replacement expenditure

Replacement expenditure is recognised within operating costs and represents the cost of planned maintenance of mains and services assets by replacing or lining sections of pipe. This expenditure is principally undertaken to repair and maintain the safety of the network and is written off as incurred. Expenditure that enhances the performance of mains and services assets is treated as an addition to tangible fixed assets.

K. Pensions

The substantial majority of the Company's 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 the Company. Accordingly, the Scheme is recognised in these Company financial statements 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 Company financial statements.

L. Leases

Operating lease payments are charged to the profit and loss account on a straight-line basis over the term of the 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 assets of the Company after deducting all of its liabilities and is recorded at the proceeds received, net of direct issue costs.

Loans receivable are carried at amortised cost using the effective interest rate method less any allowance for estimated impairments. A provision is established for impairments when there is objective evidence that the Company will not be able to collect all amounts due under the original terms of the loan. Interest income, together with losses when the loans are impaired, is recognised on an effective interest rate basis in the profit and loss account.

Current asset financial investments are recognised at fair value plus directly related incremental transaction costs and are subsequently carried at fair value on the balance sheet. 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 net profit or loss for the period. Investment income on investments classified as available-for-sale is recognised in the profit and loss account as it accrues.

Borrowings, which include interest-bearing loans, UK Retail Prices Index (RPI) linked debt and overdrafts, are recorded at their initial fair value which normally reflects the proceeds received, net of direct issue costs less any repayments. Subsequently these are stated at amortised cost, using the effective interest rate method. Any difference between proceeds and the redemption value is recognised over the term of the borrowing in the profit and loss account using the effective interest rate method.

Derivative financial instruments are recorded at fair value, and where the fair value of a derivative is positive, it is carried as a derivative asset and where negative, as a liability. 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. Gains and losses arising from changes in fair value are included in the profit and loss account in the period they arise.

Where derivatives are embedded in other financial instruments that are closely related to those instruments, no adjustment is made with respect to such derivative clauses. Otherwise the derivative is recorded separately at fair value on the balance sheet.

The fair values on financial instruments measured at fair value that are quoted in active markets are based on bid prices for assets held and offer prices for issued liabilities. When independent prices are not available, fair values are determined by using valuation techniques which are consistent with techniques commonly used by the relevant market. The techniques use observable market data.

N. Hedge accounting

The Company enters into derivative financial instruments ('derivatives') and non-derivative financial instruments in order to manage interest rate and foreign currency exposures, with a view to managing these risks associated with the Company's underlying business activities and the financing of those activities. The principal derivatives used include interest rate swaps, forward rate agreements, currency swaps and forward foreign currency contracts.

Hedge accounting allows derivatives to be designated as a hedge of another (non-derivative) financial instrument, to mitigate the impact of potential volatility in the profit and loss account. The Company uses two hedge accounting methods.

Firstly, changes in the carrying value of financial instruments that are designated and effective as hedges of future cash flows ('cash flow hedges') are recognised directly in equity and any ineffective portion is recognised immediately in the profit and loss account. Amounts deferred in equity in respect of cash flow hedges are subsequently recognised in the profit and loss account in the same period in which the hedged item affects net profit or loss.

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

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

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

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

O. Parent Company guarantees

The Company has guaranteed the repayment of the principal and any associated premium and interest on specific loans due from certain subsidiary undertakings to third parties. In the event of default or non-performance by the subsidiary, the Company recognises such guarantees as insurance contracts, at fair value with a corresponding increase in the carrying value of the investment.

P. Share-based payments

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

Q. Restructuring costs

Costs arising from the Company's restructuring programmes primarily relate to redundancy costs. Redundancy costs are charged to the profit and loss account in the period in which the Company becomes irrevocably committed to incurring the costs and the main features of the restructuring plan have been announced to affected employees.

R. Emission allowances

Emission allowances, which relate to the emissions of carbon dioxide, are recorded as an intangible asset within current assets and are initially recorded at cost, and subsequently at the lower of cost and net realisable value. For allocations of emission allowances granted by the UK Government, cost is deemed to be equal to fair value at the date of allocation. Receipts of such grants are treated as deferred income and are recognised in the income statement in the period in which carbon dioxide emissions are made. A provision is recorded in respect of the obligation to deliver emission allowances and charges are recognised in the income statement in the period in which carbon dioxide emissions are made.

S. Dividends

Interim dividends are recognised when they become payable to the Company's shareholders. Final dividends are recognised in the financial year in which they are approved.

Company balance sheet

at 31 March

	Notes	2010 £m	2009 £m
Fixed assets			
Tangible assets	6	**6,925**	6,810
Investments	7	**17**	17
		6,942	6,827
Current assets			
Stock	8	**43**	34
Debtors (amounts falling due within one year)	9	**297**	449
Debtors (amounts falling due after more than one year)	9	**5,619**	5,617
Derivative financial instruments (amounts falling due within one year)	10	**72**	122
Derivative financial instruments (amounts falling due after more than one year)	10	**565**	688
Current asset investments		**398**	1,031
		6,994	7,941
Creditors (amounts falling due within one year)			
Borrowings	13	**(1,161)**	(1,793)
Derivative financial instruments	10	**(30)**	(67)
Other creditors		**(813)**	(817)
	11	**(2,004)**	(2,677)
Net current assets		**4,990**	5,264
Total assets less current liabilities		**11,932**	12,091
Creditors (amounts falling due after more than one year)			
Borrowings	13	**(6,637)**	(6,871)
Derivative financial instruments	10	**(121)**	(42)
Other creditors		**(718)**	(734)
	12	**(7,476)**	(7,647)
Provisions for liabilities and charges	14	**(986)**	(957)
Net assets employed		**3,470**	3,487
Capital and reserves			
Called up share capital	15	**45**	45
Share premium account	16	**204**	204
Cash flow hedge reserve	16	**(44)**	3
Other reserves	16	**1,332**	1,332
Profit and loss account	16	**1,933**	1,903
Total shareholders' funds		**3,470**	3,487

Commitments and contingencies are shown in note 17 to the Company financial statements.

The notes on pages 77 to 83 form part of the individual financial statements of the Company, which were approved by the Board of Directors on 2 July 2010 and were signed on its behalf by:

Paul Whittaker Director

Adam Wiltshire Director

Notes to the Company financial statements

1. Adoption of new accounting standards

New financial reporting standards (FRS) and abstracts adopted in 2009/10

During the year the Company has adopted the following FRSs and abstracts. None of these had a material impact on the Company's results or assets and liabilities.

Amendment to FRS 20 on share-based payments	Clarifies the definition of vesting conditions and the accounting treatment of cancellations. Vesting conditions are defined as either service conditions or performance conditions. Cancellations by employees are accounted for in the same way as cancellations by the Company.
Improvements to FRS 2008	Contains amendments to various existing standards.
UITF 46 on hedges of a net investment in a foreign operation	Clarifies that hedged risk may be designated at any level in a group and hedging instruments may be held by any Company in a group (except the foreign entity being hedged), that net investment hedge accounting may not be adopted in respect of a presentation currency and that on disposal the amounts to be reclassifed from equity to profit or loss are any cumulative gain or loss on the hedging instrument and the cumulative translation difference on the foreing operation disposed of.
Amendment to FRS 29 on improving financial instrument disclosures	Enhances disclosures about fair value and liquidity risk.
Amendment to FRS for Companies Act changes	Makes consequential amendments to FRS to reflect provisions of the Companies Act 2006.
Amendments to FRS 26 and UITF 42 on embedded derivatives	Requires reassessment of whether an embedded derivative should be seperated out if a financial asset is reclassified out of the fair value through profit or loss category.

New FRS not yet adopted

The Company has yet to adopt the following FRS. However, it is not expected to have a material impact on the Company's results or assets and liabilities.

Amendment to FRS 25 on puttable financial instruments and obligations arising on liquidation	Addresses the classification as a liability or as equity of certain puttable financial instruments and instruments, or components thereof, which impose upon an entity an obligation to deliver a pro rata share of net assets on liquidation. The amendments to FRS 25 have been adopted by the Company with effect from 1 April 2010.
Amendment to FRS 26 Financial Instruments: Recognition and measurement on eligible hedged items	Prohibits designating inflation as a hedgeable component of an instrument, unless cash flows relating to the separate inflation component are contractual and also prohibits the designation of a purchased option in its entirety as the hedge of a one-sided risk in a forecast transaction. The amendments to FRS 26 have been adopted by the Company with effect from 1 April 2010.
Amendment to FRS 8 on related party disclosures	Changes the definition of related party to be the same as that in law and provides an exemption only in respect of wholly-owned subsidiaries, rather than 90% subsidiaries as previously permitted. The amendments to FRS 8 have been adopted by the Company with effect from 1 April 2010.
FRS 30 on heritage assets	Sets out disclosure requirements in respect of assets that are held and maintained principally for their contribution to knowledge and culture. FRS 30 has been adopted by the Company with effect from 1 April 2010.
Amendment to FRS 20 on group cash settled share based payments	Clarifies the scope and accounting for group cash settled share based payment transactions in separate and individual financial statements when there is no obligation to settle the share based payment transaction. The amendment to FRS 20 will be adopted by the Company with effect from 1 April 2010.
Improvements to FRS 2009	Contains amendments to various existing standards. The amendments have been adopted by the Company with effect from 1 April 2010.
Amendment to FRS 25 on classification of rights issues	Defines as an equity instrument a financial instrument that gives the holder the right to acquire a fixed number of the entity's equity instrument for a fixed amount of any currency, if the financial instrument is offered pro rata to all existing owners of the same class of non-derivative equity instruments. The amendment to FRS 25 has been adopted by the Company with effect from 1 April 2010.

2. Auditors' remuneration

Auditors' remuneration in respect of the Company is set out below:

	2010 £m	2009 £m
Audit services		
Audit fee of Company	**0.2**	0.3
Other services		
Other services supplied pursuant to legislation	**0.2**	0.2

Other services supplied pursuant to legislation represents fees payable for services in relation to engagements which are required to be carried out by the auditor. In particular, this includes fees for audit reports on regulatory returns and fees for reports under section 404 of the US Public Company Accounting Reform and Investor Protection Act of 2002 (Sarbanes-Oxley).

3. Number of employees, including Directors

	2010 Average number	2009 Average number
United Kingdom - continuing operations	**5,678**	6,016

4. Directors' emoluments
Details of Directors' emoluments are provided in note 3(d) to the consolidated financial statements.

5. Pensions
Substantially all the Company's 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 the Company. Accordingly, the Company accounts for the scheme as if it were a defined contribution scheme.

The disclosures required by FRS 17 are provided in notes 5 and 26 to the consolidated financial statements.

6. Tangible fixed assets

	Land and buildings £m	Plant and machinery £m	Assets in the course of construction £m	Motor vehicles and office equipment £m	Total £m
Cost at 1 April 2009	109	10,024	324	773	11,230
Additions	14	352	17	117	500
Disposals	(3)	(66)	-	(31)	(100)
Reclassifications	-	302	(318)	16	-
Cost at 31 March 2010	120	10,612	23	875	11,630
Depreciation at 1 April 2009	(43)	(3,804)	(1)	(572)	(4,420)
Depreciation charge for the year	(11)	(291)	(2)	(71)	(375)
Disposals	3	56	-	31	90
Depreciation at 31 March 2010	(51)	(4,039)	(3)	(612)	(4,705)
Net book value at 31 March 2010	**69**	**6,573**	**20**	**263**	**6,925**
Net book value at 31 March 2009	66	6,220	323	201	6,810

The net book value of land and buildings comprised:

	2010 £m	2009 £m
Freehold	**48**	41
Short leasehold (under 50 years)	**21**	25
	69	66

The cost of tangible fixed assets at 31 March 2010 included £132m (2009: £124m) relating to interest capitalised.

Included within creditors (amounts falling due within one year) and creditors (amounts falling due after more than one year) are contributions to the cost of tangible fixed assets amounting to £17m (2009: £17m) and £651m (2009: £655m) respectively.

7. Investments

	Shares in subsidiary undertakings £m
Cost and net book value at 31 March 2009 and 31 March 2010	17

The names of the principal subsidiary undertakings are included in note 31 to the consolidated financial statements.
The directors believe that the carrying value of the investments is supported by their underlying net assets.

8. Stock

	2010 £m	2009 £m
Raw materials and consumables	**43**	34

9. Debtors

	2010 £m	2009 £m
Amounts falling due within one year:		
Trade debtors	**58**	44
Amounts owed by fellow subsidiary undertakings	**24**	183
Corporation tax	**10**	-
Other debtors	**5**	4
Prepayments and accrued income	**200**	218
	297	449
Amounts falling due after more than one year:		
Other debtors	**8**	6
Amounts owed by immediate parent undertaking	**5,611**	5,611
	5,619	5,617
Total debtors	**5,916**	6,066

10. Derivative financial instruments

The fair value of derivative financial instruments shown on the balance sheet is as follows:

	2010			2009		
	Assets £m	Liabilities £m	Total £m	Assets £m	Liabilities £m	Total £m
Amounts falling due in one year	**72**	**(30)**	**42**	122	(67)	55
Amounts falling due after more than one year	**565**	**(121)**	**444**	688	(42)	646
	637	**(151)**	**486**	810	(109)	701

For each class of derivative the notional contract* amounts are as follows:

	2010 £m	2009 £m
Interest rate swaps	**(3,154)**	(2,924)
Cross-currency interest rate swaps	**(1,748)**	(1,525)
Foreign exchange forward contracts	**(39)**	(15)
Forward rate agreements	**(1,730)**	(3,345)
	(6,671)	(7,809)

*The notional contract amounts of derivatives indicate the gross nominal value of transactions outstanding at the balance sheet date

11. Creditors (amounts falling due within one year)

	2010 £m	2009 £m
Derivative financial instruments (note 10)	**30**	67
Borrowings (note 13)	**1,161**	1,793
Trade creditors	**277**	259
Amounts owed to Group undertakings	**4**	8
Amounts owed to fellow subsidiary undertakings	**152**	204
Corporation tax	**-**	31
Social security and other taxes	**73**	63
Other creditors	**34**	30
Accruals and deferred income	**273**	222
	2,004	2,677

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

	2010 £m	2009 £m
Derivative financial instruments (note 10)	**121**	42
Borrowings (note 13)	**6,637**	6,871
Other creditors	**4**	18
Deferred income	**714**	716
	7,476	7,647

Deferred income mainly comprises contributions to capital projects.

13. Borrowings

The following table analyses the Company's borrowings:

	2010 £m	2009 £m
Amounts falling due within one year:		
Bank loans and overdrafts	**261**	286
Bonds	**111**	625
Borrowings from Group undertakings	**713**	393
Borrowings from fellow subsidiary undertakings	**74**	487
Other loans	**2**	2
	1,161	1,793
Amounts falling due after more than one year:		
Bank loans	**659**	602
Bonds	**5,579**	5,641
Borrowings from Group undertakings	**250**	458
Other loans	**149**	170
	6,637	6,871
Total borrowings	**7,798**	8,664
Total borrowings are repayable as follows:		
In one year or less	**1,161**	1,793
More than one year, but not more than two years	**251**	1
More than two years, but not more than three years	**222**	250
More than three years, but not more than four years	**730**	221
More than four years, but not more than five years	**134**	752
More than five years, other than by instalments	**5,300**	5,647
	7,798	8,664

The notional amount outstanding of the Company's debt portfolio at 31 March 2010 was £7,355m (2009: £8,166m).

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

14. Provisions for liabilities and charges

	Environmental £m	Emissions £m	Restructuring £m	Deferred taxation £m	Other £m	Total £m
At 1 April 2009	56	2	43	808	48	957
Charged to profit and loss account	14	4	28	27	11	84
Transferred to reserves	-	-	-	(18)	-	(18)
Utilised	(2)	-	(25)	-	(10)	(37)
Released	-	-	-	-	(2)	(2)
Unwinding of discount	2	-	-	-	-	2
At 31 March 2010	**70**	**6**	**46**	**817**	**47**	**986**

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 plc (discounted using a nominal rate of 2.0%). The anticipated timing of the cash flows for statutory decontamination cannot be predicted with certainty, but they are expected to be incurred over the next 50 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. We have made our 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 2010 relating to gas site decontamination was £110m (2009: £85m), being the best undiscounted estimate of the liability having regard to the uncertainties referred to above.

Emissions provision

The provision for emission costs is expected to be settled using emission allowances granted or purchased.

Restructuring provision

At 31 March 2010, £26m of the total restructuring provision (2009: £19m) related to the restructuring of our Liquefied Natural Gas (LNG) storage facilities and £5m consisted of provisions for the disposal of surplus leasehold interests and rates payable on surplus properties (2009: £5m). The expected payment dates for property restructuring costs remain uncertain. The remainder of the restructuring provision related to business reorganisation costs, to be paid over the next two years.

Other provisions

Other provisions at 31 March 2010 include £6m (2009: £12m) in respect of property transfer costs related to the sales of four UK gas distribution networks and £21m (2009: £21m) in respect of employer liability claims. The payment dates for the property transfer costs are uncertain but should largely be over the next two years. In accordance with insurance industry practice, the estimates for employer liability claims are based on experience from previous years and, therefore, there is no identifiable payment date associated with these items.

Deferred taxation comprises:

	2010 £m	2009 £m
Accelerated capital allowances	**832**	796
Other timing differences	**(15)**	12
	817	808

Deferred tax assets in respect of capital losses of £15m (2009: £24m) have not been recognised as their future recovery is uncertain or not currently anticipated. The capital losses are available to carry forward indefinitely. The capital losses can be offset against specific types of future capital gains.

There are no other significant unrecognised deferred tax assets or liabilities (2009: £nil).

15. Called up share capital

	Number of shares 2010 millions	Number of shares 2009 millions	**2010 £m**	2009 £m
At 31 March 2009 and 2010 - ordinary shares of $1^{2}/_{15}$p each				
Allotted, called up and fully paid	**3,944**	3,944	**45**	45

National Grid Gas plc is a wholly owned subsidiary undertaking of National Grid Gas Holdings plc.

16. Reserves

	Cash flow hedge reserve £m	Share premium account £m	Capital redemption reserve £m	Profit and loss account £m
At 1 April 2009	3	204	1,332	1,903
Profit for the year	-	-	-	322
Dividends	-	-	-	(300)
Net loss recognised directly in reserves	(47)	-	-	-
Share-based payments	-	-	-	8
At 31 March 2010	**(44)**	**204**	**1,332**	**1,933**

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

The Company has not presented its own profit and loss account as permitted by section 408 of the Companies Act 2006. The Company's profit after taxation was £322m (2009: £164m loss).

17. Commitments and contingencies

a) Future capital expenditure

As at 31 March 2010, the Company had placed contracts for capital expenditure (tangible fixed assets) amounting to £532m (2009: £480m).

b) Lease commitments

At 31 March 2010, the Company's total operating lease commitments for the financial year ending 31 March 2011 amounted to £15m (2009 commitments for 2010: £12m) and are analysed by lease expiry date as follows:

	Land and buildings		Other		Total	
	2010 £m	2009 £m	**2010 £m**	2009 £m	**2010 £m**	2009 £m
Expiring:						
In one year or less	**1**	1	**1**	1	**2**	2
In more than one year, but not more than five years	**5**	1	**4**	3	**9**	4
In more than five years	**4**	6	**-**	-	**4**	6
	10	8	**5**	4	**15**	12

c) Other commitments and contingencies

The value of other commitments, contingencies and guarantees at 31 March 2010 amounted to £209m (2009: £150m), including gas purchase commitments amounting to £43m (2009: £70m), and guarantees relating to certain property obligations of a National Grid group undertaking of £1m (2009: £1m).

d) Parent Company loan guarantees on behalf of subsidiary undertakings

The Company has guaranteed the repayment of principal sums, any associated premium and interest on specific loans due from its financial subsidiaries to third parties. At 31 March 2010, the sterling equivalent amounted to £1,168m (2009: £1,487m).

e) Litigation and claims

We reported in previous Annual Reports and Accounts a decision by the Gas and Electricity Markets Authority (GEMA) to fine National Grid £41.6m for a breach of the UK Competition Act 1998 in respect of term contracts with gas suppliers entered into by our metering services business in 2004. This decision was overturned in part and the fine reduced to £30m by the Competition Appeal Tribunal in April 2009 and the fine was further reduced to £15m by the Court of Appeal in a reserved judgement (not otherwise affecting the Competition Appeal Tribunal's judgement) issued in February 2010. On 22 March 2010, National Grid applied for leave to appeal the Court of Appeal's judgement to the Supreme Court.

As at 31 March 2010, we have provided for the fine together with associated costs and have provided against certain trade receivables and other balance sheet items. Without prejudice to our position in relation to appealing the Court of Appeal's judgement, the £15m fine was paid to GEMA on 1 April 2010.

In October 2008, we informed Ofgem that our mains replacement activity carried out by the Distribution business may have been misreported. Ofgem's investigation continues, so that at present it is too early to determine the likely outcome of the investigation, including the quantum of any amounts likely to be payable and any potential consequences as a result of it.

Glossary and definitions

References to NGG, the 'Company', 'we', 'our', and 'us', refer to National Grid Gas plc itself or to National Grid Gas plc and its subsidiaries collectively, depending on context.

bcm
Billion cubic metres

FRS
UK Financial Reporting Standard

GAAP
Generally accepted accounting principles

GW
Gigawatt, 10^9 watts

GWh
Gigawatt hours

HSE
Health and Safety Executive

IAS
International Accounting Standard

IFRIC
International Financial Reporting Standards Interpretations Committee

IFRS
International Financial Reporting Standard

KPI
Key Performance Indicator

LNG
Liquefied natural gas

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

mcm
Million cubic metres

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

Ofgem
The Office of Gas and Electricity Markets

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

RAV
Regulatory asset value

TW
Terawatt, 10^{12} watts

TWh
Terawatt hours

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