

2010/11

national**grid**

Annual Report and Accounts

Business Overview

Company highlights

We have delivered another year of solid financial performance across all our businesses. Cash generated from operations was more than £4.8 billion, while adjusted operating profit and adjusted earnings per share increased by 15% and 4% respectively.



For more information visit:
www.nationalgrid.com

Revenue *

£14,343m

2009/10: £14,007m (↑ 2%)

Cash generated from operations *

£4,854m

2009/10: £4,372m (↑ 11%)

Adjusted operating profit **

£3,600m

2009/10: £3,121m (↑ 15%)

Operating profit *

£3,745m

2009/10: £3,293m (↑ 14%)

Adjusted earnings per share **

51.7p

2009/10: 49.5p (↑ 4%) (i)

Earnings per share *

63.9p

2009/10: 48.4p (↑ 32%) (i)

Capital expenditure

£3,603m

2009/10: £3,338m (↑ 8%)

Ordinary dividends

36.37p

2009/10: 33.68p (↑ 8%) (ii)

Return on equity (3 year average)

11.9%

2009/10: 11.3%

Interest cover

3.8x

2009/10: 3.9x

Rights issue

£3.2bn

after costs

* for continuing operations

† excludes the impact of exceptional items, remeasurements and stranded cost recoveries. See page 54 for more information about these adjusted profit measures

(i) Comparative earnings per share data has been restated for the impact of the scrip dividend issues and the bonus element of the rights issue

(ii) The 2009/10 dividend has been rebased for the effect of the rights issue

Our financial results are reported in sterling. The average exchange rate, as detailed on page 54, was \$1.57 to £1 in 2010/11 compared with the average rate of \$1.58 to £1 in 2009/10. Except as otherwise noted, the figures in this Report are stated in sterling or US dollars. All references to dollars or \$ are to the US currency.

- We have continued to increase our capital investment, having delivered £3.6 billion this year, including joint ventures.
- In the US, we have been through a period of intense regulatory activity as we have come to the end of several long-term fixed rate plans. Two major filing outcomes this year were for our Massachusetts gas companies and the Niagara Mohawk electricity business.
- In the UK, we remain positive about the proposed new system of regulation, RIIO (revenue = incentives + innovation + outputs), which will be used in price controls for UK Transmission and UK Gas Distribution starting in April 2013.
- Our rights issue was completed successfully last year, receiving approximately 94.2% subscription from qualifying shareholders.
- Recognising that our customers and regulators are looking for something more closely tuned to their local needs, and to help drive business performance, on 4 April 2011 we reshaped our organisational structure and moved from a global line of business model to a regional model.

Segmental reporting

The performance of our principal businesses is reported by segment, reflecting the management responsibilities and economic characteristics of each activity.

Throughout the year ended 31 March 2011, the management structure was as described on page 23. Throughout this report, the following colours are used to indicate references to a particular segment:

- Transmission
- Gas Distribution
- Electricity Distribution & Generation

Activities which do not fall within these segments are reported separately and are identified thus:

- Non-regulated businesses and other activities

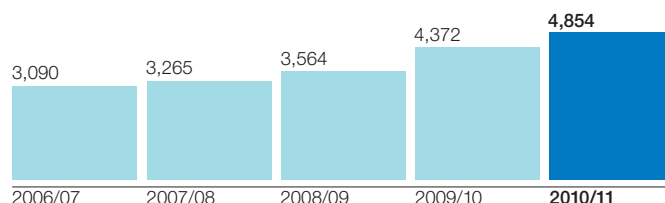
Discussion relating to the Company as a whole is identified thus:

- Company activities

In next year's Annual Report and Accounts, and in subsequent years, we will report by new segments, as described on page 22, reflecting the revised management structure.

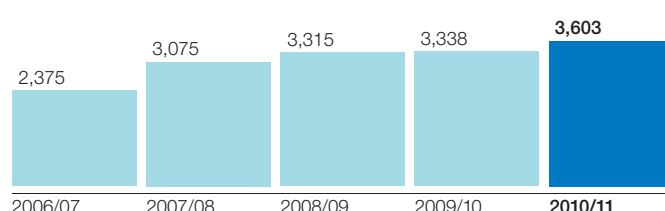
Cash generated from continuing operations

£m



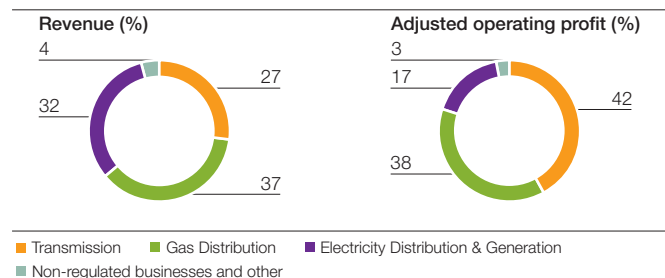
Capital expenditure including joint ventures

£m



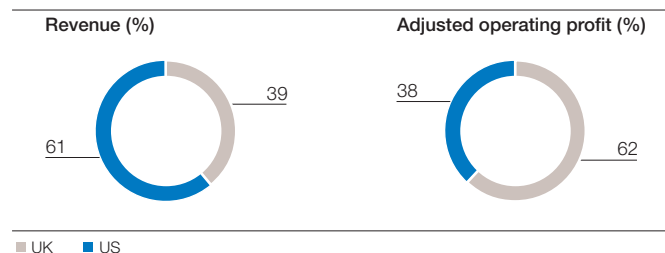
Business analysis 2010/11

Continuing operations



Geographical analysis 2010/11

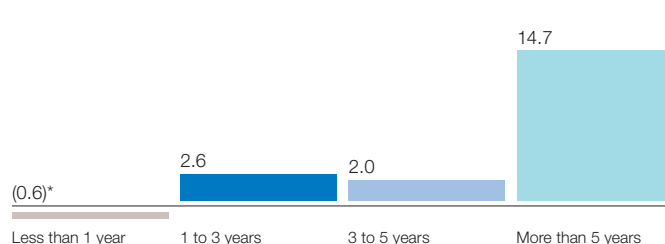
Continuing operations



Note: US revenue includes commodity price element which does not contribute to profit

Maturity of net debt at 31 March 2011

£bn



* Negative figure indicates that cash and short-term financial investments exceed debt maturities

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National Grid is an international electricity and gas company based in the UK and northeastern US. We play a vital role in connecting millions of people to the energy they use, safely, reliably and efficiently.

Directors' Report

In accordance with the requirements of the Companies Act 2006 and the UK Listing Authority's Listing, and Disclosure and Transparency rules, pages 10 to 108 comprise the Directors' Report and were approved by the Board. The location within the main body of the Annual Report of the specific requirements of the Directors' Report can be found in the checklist on page 81.

Directors' Report

If you require a full search facility, please go to the pdf of the Annual Report and Accounts 2010/11 at www.nationalgrid.com and use a word search.

Important notice

This document contains certain statements that are neither reported financial results nor other historical information. These statements are forward-looking statements within the meaning of Section 27A of the Securities Act of 1933, as amended, and Section 21E of the Securities Exchange Act of 1934, as amended. For a description of factors that could affect future results, reference should be made to the full Cautionary Statement on the back cover of this document and the Risk factors section on pages 91 to 93.

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Chairman's statement



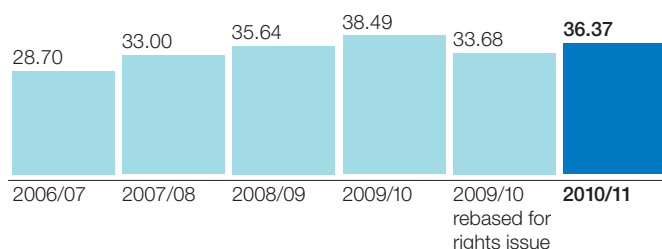
We remain confident that our strategy and new structure will allow National Grid to grow and deliver our commitment to create value for our shareholders.

The Board is proposing a recommended final dividend of

23.47p

2009/10: 21.74p (rebased for the effect of the rights issue)

Dividends per share
pence



I am delighted to report a solid set of results for 2010/11 for the Company on both sides of the Atlantic. Group adjusted operating profit has increased by 15% from £3,121 million in 2009/10 to £3,600 million in 2010/11. Adjusted earnings per share (EPS) increased 4% from last year's restated 49.5 pence per share to 51.7 pence per share, despite the dilutive effect of the rights issue.

Dividend policy

The Board is proposing a final dividend of 23.47 pence per share making a total for the 2010/11 financial year of 36.37 pence per share. This represents an increase of 8% – a growth rate which we are continuing to target for 2011/12.

Over the past nine years, since the merger with Lattice Group plc, National Grid's total dividend for the year has increased from £265 million for 2001/02 to £1,275 million for 2010/11, an increase of 381%.

Safety

Safety is at the core of our business and remains a top priority for the Board. We understand that our operations potentially give rise to risk and that, if our assets are not properly controlled, they could have severe consequences for our employees, customers and surrounding communities. We believe that through our safety management processes and the professionalism of our trained people, we can mitigate risks and eradicate injuries. Everyone at National Grid has a part to play in this.

Weather challenges

Both the UK and US encountered difficult weather conditions this year, resulting in high demand for both gas and electricity. In December 2010, we had the coldest UK weather conditions for 100 years and in the US, our territories suffered huge snow blizzards. During this period, we experienced a significant increase in emergency calls. In 2010, heavy rain caused severe flooding in Rhode Island leaving over 5,000 customers without power.

Our people worked tirelessly to restore gas and electricity connections. In such conditions, I am constantly impressed by the hard work and dedication of all our employees on both sides of the Atlantic.

Reorganisation and investment

We have listened to what our customers and regulators want from us. With effect from 4 April 2011, we reshaped our organisation in the UK and, in particular, the US to help us become more responsive and effective. Importantly, we are engaged in further cost reductions in our US operations and these, together with current and future regulatory submissions, should enable us to generate an overall return in the 9–10% range on our US investments. The Chief Executive's review on page 6 provides important detail on these strategic moves.

During 2010/11 we had, as planned, a further uplift in our capital investment to £3.6 billion, including joint ventures. This will help us deliver the infrastructure that the future energy industry requires.

Reorganisation and investment on this scale makes for operational challenges. The Board has confidence in the management team to deliver these value creation opportunities for all our stakeholders.

Operating responsibly

Operating our businesses in a socially and environmentally responsible way is fundamental to the way we operate and to delivering sustainable profits and long-term value to our investors.

I am delighted that we have extended our Special Olympics Great Britain (SOGB) charity partnership, as Premier Partner, for a further three years through to 2013. In 2011, we are launching the SOGB Sports Development Fund to enable grassroots sports clubs to gain funding to build capacity in the disability sports sector.

The Young Offenders Programme, in association with the companies now involved, continues to be successful. The programme provides skills, training and employment for offenders nearing the end of their sentence and I am encouraged by the career progression of the young people who have completed it.

In the US, our partnership with United Way continues to thrive. Throughout the year, our employees give up their time and money for the United Way campaign to help improve and provide assistance to communities throughout our service area. In 2010,

we donated more than \$3 million (£1.9 million) to the United Way campaign. I feel proud of our employees who continue to recognise the importance of giving, especially during these financially trying times.

Governance

Our Board continues to be committed to leading practice in corporate governance and in setting the right tone at the top. Our Directors have a broad and diverse range of complementary skills and specialised knowledge. I am satisfied, as confirmed again by this year's Board performance review, that our Board operates effectively, is properly engaged on critical matters and all Directors set aside the time required to fulfil their duties. We continue to put significant effort into succession planning for Executives, Non-executive Directors and all senior management.

Our people

Steve Lucas retired from the Board as Finance Director at the end of December 2010. The Board and I valued Steve's contribution during his 10 years' service with National Grid and with Lattice Group plc.

In November 2010, Andrew Bonfield joined the Board as our new Finance Director. Andrew's significant financial experience will play a pivotal role in assisting us to meet the challenges and opportunities that lie ahead.

Following the reorganisation, Mark Fairbairn stepped down from the Board and left the Company at the end of March 2011. Mark made a significant contribution during his 21 years. He was a valued colleague during a period of considerable change for National Grid.

I regret to announce that John Allan will step down from the Board at this year's AGM. This is due to his increasing commitments externally, especially since he became Chairman of WorldPay in April. The Board and I are sorry to see John leave and we wish him every success for the future.

I would like to take this opportunity to thank Steve, Mark and John for their valuable input towards the success of National Grid and to welcome Andrew to the Board.

The Board continues to place increasing emphasis on the development of our people and is pleased by the ongoing talent management and development work. We are also ensuring the recruitment and development programmes for our young recruits and graduates are among the leading programmes in the industry.

The Chairman's Awards have again recognised the outstanding achievements of many of our employees who aim above and beyond their normal day-to-day job requirements. This year, over 120 submissions were received in areas such as safety, health, environment, community contribution, customer delivery and inclusion and diversity.

The Board and I welcome the findings and recommendations of the Davies Review 'Women on boards', of which I was a member. The review has set targets for the appointment of women to Boards and Executive Committees. We are already in a stronger position than many companies on gender diversity with two female Non-executive Director members of the Board. We also have two female members of the Executive Committee. We intend to take steps to improve this position further and be well positioned to meet the 2015 target of 25%.

Outlook

As a Board, we remain confident that our strategy and new structure will allow National Grid to grow and deliver our commitment to create value for our shareholders. Our relentless focus on safety will continue and our passion around reliability remains alongside our contribution to a low carbon economy. We will maintain our drive on efficiency and progress the important work we are doing to develop our people to their highest potential.

I would like to thank all our employees and pay tribute to their dedication, professionalism and their loyalty to National Grid. Collectively, they make the difference.

Sir John Parker
Chairman



SEPTEMBER 2010

Investing in the communities we serve remains a high priority for us. In September 2010, we joined City Year London. City Year is a project that has a proven track record of improving young lives and 2010/11 is City Year London's first programme. It follows in the footsteps of our longer standing successful partnership with City Year US. Aged between 18 and 25, City Year London's Corps members are mentors, tutors and role models in local schools and communities. It offers National Grid the opportunity to be part of something that not only has huge potential to make a difference to the lives of children and young people, but also enhances our schools and community engagement programme especially around our major infrastructure projects in London.



Chief Executive's review



National Grid is at the heart of one of the greatest challenges in society today: the creation of new sustainable energy solutions for the future as well as the development of an energy system that can underpin our economic prosperity in the 21st century.

2010/11 has been a challenging year as National Grid continues to drive investment, ensuring our new and existing customers are connected to the energy they need and that we provide them with an excellent service. This investment also delivers growth and value for our shareholders. National Grid remains central to developing the energy policy and regulatory agenda in the UK and in the northeastern US, ensuring we are investing for the future.

Financials

During 2010/11, we delivered solid financial performance across all our businesses, although this performance was flattered by significant timing benefits not expected to recur. Our US businesses performed particularly well this year, with customer growth and income from new rate plans contributing significantly. We achieved an important milestone with phase III of our Grain LNG terminal beginning commercial operations in December 2010, providing extra security in time for winter. Overall, we delivered another year of significant investment in assets and growth in operating profit.

Safety

Following a large reduction in lost time injury frequency rate from 0.25 in 2008/09 to 0.15 in 2009/10, most of these gains have been maintained this year. At the end of 2010/11, our lost time injury frequency rate was at 0.18 and the number of lost time injuries was 96 compared with 86 in 2009/10. The principal causes were road traffic collisions, musculoskeletal injuries and slips, trips and falls.

We challenge ourselves hard to improve our safety performance, and we remain extremely focused on this, having reduced our lost time injury frequency rate by 36% over the last five years. We continue to push improvements in process safety, reporting key performance indicators up to Executive level.

In 2010/11, we continued to align our approach to process safety management across the Company, with the development of a major accident hazard framework.

Strategy

Our priorities for 2010/11 have been focused on our increased investment, US regulatory progress and changes in UK regulation.

We continue to invest in a controlled and disciplined manner and remain on track to deliver a significant increase in capital investment, having delivered £3.6 billion (including joint ventures) this year. This is largely driven by increases in the UK Transmission business, building and installing a grid that will be fit for the future. We expect another year of significant investment and, looking ahead, are on target to invest a total of £19 billion in the four years to the end of March 2015.

In the US, we have been through a period of intense regulatory activity as we have come to the end of several long-term fixed rate plans. Through all our rate filings, we are trying to ensure we have the right cost of service allowances to meet our customers' needs and the ability to earn an appropriate return for investors. Two major filing outcomes this year were for our Massachusetts gas companies and the Niagara Mohawk electricity business. New rates were effective from 1 November 2010 and 1 January 2011 respectively. Overall, the decision on the Massachusetts gas companies' rate case was satisfactory. However, we were disappointed with the outcome for Niagara Mohawk and we continue to review the impact of these rate case outcomes and reset our regulatory filing plans for 2011/12 accordingly.

In the UK, we remain positive about the proposed new system of regulation, RII (revenue = incentives + innovation + outputs), which will be used in price controls for UK Transmission and UK Gas Distribution starting April 2013. Our networks will need to change substantially in the next 20 years, both in terms of their configuration and in the way that they operate in real time. We are in the early stages of the process, but we are pleased to see that Ofgem has rightly focused on innovation and incentives and is aware of the need to provide adequate returns and cash flow.

In January 2011, we announced substantial changes to the way in which we will organise National Grid and the way in which we will deliver services to our customers. Recognising that our customers and regulators are looking for something more closely tuned to their local needs, from 4 April 2011 we evolved from a global line of business model to a regional model with Tom King, Executive Director US, and Nick Winsor, Executive Director UK, supported by Company wide and regional functions. While we retain our global perspective when setting strategic direction and policy for National Grid, the new structure will support a tighter focus on local issues in the US to help improve our performance and focus on customers.

Investing for the future

The energy industry between now and 2050 is set to change dramatically. The Climate Change Act in the UK requires an 80% cut in greenhouse gas emissions, compared with 1990 levels, by 2050. Meeting these targets will require us within the UK to reduce the average emissions associated with the electricity produced from current levels of around 500g CO₂ per kWh to around 50g by 2030.

This transition to a low carbon economy is set against a background of increasing population, challenging economic times and ageing power plant. Events through the year in North Africa and the Middle East have emphasised concerns around rising energy prices and the volatility of the potential future generation mix.

Approximately a quarter of the UK's existing power plants will close by 2023. Many of these old coal and nuclear stations will be replaced with renewable generation, new gas and nuclear stations. National Grid will play a vital role in connecting this new generation to the grid. We currently have a total of 64.1 GW of generation with signed connection agreements to connect to the transmission network by the end of 2020, including 35.8 GW of renewable generation.

In addition, an increasing number of our assets are reaching the end of their lives and we are already in the midst of a significant programme of replacement and renewal. This presents us with a tremendous opportunity to invest in the latest technology and ensure we have a network that will meet the future challenges as part of our investment programme.

People and talent

My own focus on our people continues as does our commitment to developing them to the best of their abilities. During 2010/11, over 1,000 first line leaders in both the UK and US enrolled on the Foundations of Leadership programme. Across the UK and US, we are actively working with organisations such as the National Technician Council, Business in the Community and the US Chamber of Commerce's Business LEADs Institute on encouraging science, technology, engineering and maths (STEM) studies. We are working closely with schools and colleges to enthuse and inspire young students about science and engineering.

Following feedback from the business, we postponed the 2011 employee survey. The 97% response rate from the 2010 survey gave us a huge amount of data to work with and our teams are now working more deeply on their action plans. We have also seen lots of change across the business this year and felt it was important to allow us to focus on executing these changes effectively. The next Company wide survey will take place in 2012.

As part of our increased investment in the UK and supporting delivery of a low carbon economy, we will need to invest in our people and increase our resources.

By 2020, National Grid will need to recruit around 2,500 engineers across the UK – a mixture of experienced engineers, apprentices, foundation engineers and graduates.

Efficiency

We have reduced even further our controllable operating costs. Compared to the same period last year, they are down 2% to £2,216 million. In the US, we successfully delivered the \$200 million KeySpan synergy savings by 31 March 2011. In the UK Gas Distribution business, we began to implement our new asset and work system. This investment, of over £200 million, includes a new integrated work scheduling and dispatch system and will drive efficiencies and improve the service we can provide to customers. The recent reorganisation of our business will enable us to move to a more focused and efficient organisation, reducing our costs in the US by a further \$200 million.

Looking forward

Our job at National Grid is to connect people to the energy they use. We hold a privileged position – we sit at the centre of the energy system. That puts us right at the heart of one of the greatest challenges in society today: the creation of new sustainable energy solutions for the future as well as the development of an energy system that can underpin our economic prosperity in the 21st century.

Our priorities for 2011/12 will be:

- delivery of our ongoing capital investment programme;
- working with Ofgem on shaping the future UK regulatory framework; and
- embedding the new organisational structure and improving regulated returns across the US business.

Steve Holliday
Chief Executive



APRIL 2011

BritNed, our 260 km electrical interconnector between Great Britain and the Netherlands, went live after three years of construction. The €600 million (£500 million) joint venture between National Grid and Dutch TenneT, will allow BritNed customers to participate in European and UK markets. This 1,000 MW, two way electricity high voltage direct current (HVDC) interconnector will make a significant contribution to the security and diversity of electricity supplies in both Great Britain and the Netherlands. It will also help to facilitate further competition by improving connection with Europe. The direct current converter thyristor valves (pictured) are housed in a hall 900 m² x 20 m tall.

