nationalgrid

Annual Report and Accounts 2012/13
National Grid Electricity Transmission plc

Company Number 2366977

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Strategic Review

Our business

National Grid Electricity Transmission plc (National Grid Electricity Transmission) is a subsidiary of National Grid plc (National Grid), based in the UK, where we own and operate regulated electricity transmission networks. We play a vital role in connecting millions of people safely, reliably and efficiently to the energy they use.

The overall management and governance of National Grid Electricity Transmission is the responsibility of its Board of Directors. Strategic direction is determined by our parent company, National Grid. Our Directors are listed on page 26.

More information on the management structure of National Grid can be found in the National Grid Annual Report and Accounts 2012/13 and on National Grid's website at www.nationalgrid.com.

Our vision and strategy

The National Grid vision sets out its intentions and aspirations at the highest level, while its strategic objectives outline what it needs to do to achieve that vision. We share the National Grid vision and strategy.

Our vision

Connecting you to your energy today, trusted to help you meet your energy needs tomorrow

Our strategy

To be a recognised leader in the development and operation of safe, reliable and sustainable energy infrastructure, to meet the needs of our customers and communities and to generate value for our investors

Deliver operational excellence	Engage our people	Stimulate innovation	Engage externally	Embed sustainability	Drive growth

Our business model

What we do	How we do it
We are an electricity company based in the UK. We play a vital role in connecting millions of people safely, reliably and efficiently to the energy they use.	What we do and the way we do it are equally important – from setting the tone at the top and how we manage our internal controls, to matters reserved to the Board and our executive remuneration policies.
Operating environment (see page 5) **What we do** (see pages 6 - 8) **Where we operate** (see page 6)	**National Grid Board*** **National Grid governance structure*** **Internal control and risk management** (see page 9) **How executive remuneration aligns to National Grid strategy***

What did we achieve?

Our work and people underpin the prosperity and well being of our customers, communities and investors. To read about what we achieved in 2012/13 see pages 15 to 18.

National Grid Electricity Transmission is part of the National Grid group and our governance structure is incorporated and managed by the National Grid Board.

* Further information can be found in the National Grid Annual Report and accounts 2012/13 and on National Grid's website at www.nationalgrid.com.

What our vision and strategic objectives mean to us

Our vision sets out our intentions and aspirations at the highest level. Our strategic objectives set out what we believe we need to achieve to deliver our vision and be recognised as a leader in the development and operation of safe, reliable and sustainable energy infrastructure.

Deliver operational excellence – achieve excellent levels of safety, reliability, security and customer service.

Our customers, communities and other stakeholders demand safe, reliable and secure supply of their energy. This is reflected in our regulatory contracts where we are measured and rewarded on the basis of meeting our commitments to customers and other stakeholders.

Excellence in operational processes should allow us to manage our assets efficiently, deliver network improvements quickly and provide services that meet the changing demands of customers. Engagement with our customers and communities will make sure our outputs reflect their needs and priorities. It will help maximise the benefits our stakeholders derive from the value we deliver.

Engage our people – create an inclusive, high performance culture by developing all our employees.

It is through the hard work of our employees that we will achieve our vision, respond to the needs of our stakeholders and create a competitive advantage. Creating an engaged and talented team that is aligned with our strategic objectives is vital to our success. Our presence within the communities we serve, the people we work with and our opportunities to grow both individually and as a business are all important to making National Grid a good place to work.

Stimulate innovation – promote new ideas to work more efficiently and effectively.

Our commitment to promoting innovation underpins how we will run our networks more efficiently and effectively and deliver on our regulatory incentives. Across our business, we will explore new ways of thinking and working to benefit every aspect of how we deliver on our customer and stakeholder commitments.

Embedding innovation and new technology into our operations makes sure we deliver continuous improvements in the quality and cost of our services.

Engage externally – work with external stakeholders to shape UK and EU energy policy.

Policy decisions by regulators, governments and others directly affect our business. We engage widely in the energy policy debate, making sure our position and perspective shape future policy direction. We also engage with our regulators to manage uncertainty and provide the right mechanisms so we can deliver infrastructure that meets the demands of a changing energy landscape.

Embed sustainability – integrate sustainability into our decision making to create value, preserve natural resources and respect the interests of our communities.

Our long-term sustainability strategy sets our ambition to deliver these aims and to embed a culture of sustainability within our organisation. That culture will make sure we make decisions that protect and preserve natural resources and benefit the communities in which we operate. We remain committed to the National Grid targets of a 45% reduction in Scope 1 and 2 greenhouse gas emissions by 2020 and 80% by 2050.

Drive growth – grow our core business and develop future new business options.

We review investment opportunities carefully and will only invest where we can reasonably expect to earn an adequate return. Combining this disciplined approach with operational and procurement efficiencies gives us the best possible opportunity to drive strong returns and meet our commitments to investors.

How our strategy creates value

Our vision and strategic objectives explain what is important to us, so we can meet our commitments and deliver value.

Business value

Regulatory frameworks – operating under robust regulatory frameworks can help to reduce cash flow volatility. Shaping these frameworks to maintain a balance of risk and return underpins our investment proposition.

Reputation, safety and capability – our approach to safety and our reliability record underpin our reputation and brand. These are important factors that enable positive participation in regulatory discussions and the pursuit of new business opportunities.

Efficient operations – efficient capital and operational expenditure allows us to deliver regulatory outputs at a lower cash cost and reduces working capital requirements.

Maximising revenues – positive performance under incentive mechanisms, and delivery of the outputs our customers and regulatory stakeholders require, helps us to maximise allowed revenue.

Funding and cash flow management – positive net cash flows and an innovative funding strategy help to deliver long-term growth. Outperforming the allowed cost of debt can provide improved profitability.

Disciplined investment – we can achieve future revenue and earnings growth by increasing our regulatory asset value in line with regulatory capital allowances.

Customer and community value

Safety and reliability – providing reliable networks in a safe way is at the core of customer expectations.

Affordability – providing services in a cost efficient way helps to reduce the impact on customer bills.

Customer service – providing reliable services that meet the needs of our customers and communities is a crucial part of the value they receive from us.

Environmental sustainability – we aim to protect the environment and preserve resources for current and future generations.

Community engagement – we listen to the communities we serve and work to address concerns about the development of our networks. Our people volunteer for community based projects and we support educational initiatives in schools.

Operating environment

Our operations are influenced and affected by what is going on in the world around us. We shape our decision making to try and balance the impact of these external factors, so we can deliver value for our customers and other stakeholders.

Macroeconomic factors

Our price controls are agreed against the backdrop of the broader macroeconomic environment.

In the UK, low economic growth is projected in 2013 and, as a result, it is unlikely that we will see a significant decline in the unemployment rate during 2013.

The environment for infrastructure investment in the UK and Europe is evolving, with new investors continuing to be attracted to regulated assets. Sovereign wealth and infrastructure funds are becoming more prominent investors in UK assets.

Changing energy mix

Our networks exist to transmit and distribute energy from its source to its place of use. Changes to the energy mix and location of centres of supply and demand will create pressures on our networks. We may need to continue to invest in our networks to meet these challenges.

Some older coal fired power stations are closing to comply with the Large Combustion Plant Directive and recent fuel prices have reduced the economic viability of gas fired power stations to the point where some are now being mothballed or closed. Looking further ahead, a continued decline in fossil fuel fired electricity generation is to be expected if the government's carbon reduction targets are to be met. New low carbon generation will not necessarily be located in the same place as existing plant and will probably require new connections.

Energy policy

Policy decisions by governments, government authorities and others can have a direct impact on our business. They can affect the amount and location of investment required in our networks and the way we operate. They can also change our compliance obligations. Understanding the evolving policy environment is important to understanding the challenges and opportunities we have ahead.

Energy policy continues to evolve from the Climate Change Act 2008 which commits the UK government to reducing UK greenhouse gas emissions to a level at least 80% lower than a 1990 baseline by 2050.

In November 2012, the Energy Bill, which implements the main aspects of Electricity Market Reform (EMR), was introduced to parliament. EMR seeks to set out the future industry context and promote investment in low carbon generation by providing greater financial certainty to investors. The Energy Bill is expected to receive Royal Assent this year.

At a European level, the three cornerstones of sustainability, security of supply and affordability underpin energy policy.

Greater levels of market integration, interconnection and renewable generation are fundamental to achieving these policy objectives. While European developments present challenges, the significant level of investment required may create opportunities for growth.

Regulatory developments

The regulatory focus during the year has been the finalisation of the new RIIO price controls. RIIO gives greater focus to incentives and innovation than the previous regulatory regime.

The projected increase in offshore wind generation and interconnection has created a debate on the regulatory approach to electricity transmission investment – a debate we are fully engaged in. Competition is already in place for offshore development and Ofgem has stated its intent to retain the option of using greater competition for certain large onshore projects.

In addition to the investment required for new connections and to meet the challenges of changing supply and demand patterns, we need to replace ageing infrastructure.

Innovation and technology

New technology can change the way we do business. The pace of technological development in the energy sector is accelerating as new technologies take shape and approach commercial viability. HVDC technology could play an important part in the development of a more integrated electricity grid, particularly the extension of offshore links. While carbon-based generation is likely to remain a significant part of the global energy mix, carbon capture and storage technologies may become critical to governments achieving their climate change targets. Technologies such as energy storage, electric transportation and distributed generation, all have the potential to affect our networks significantly. The development of smart grids will change how loads are balanced across the distribution network. It will allow our customers to make smarter energy choices and will increase network flexibility. New consumer products, such as alternative fuelled vehicles and distributed generation, will increase demand and require new infrastructure. Innovation goes further than new technology. We need to increase the flexibility of our infrastructure to respond to developments as they arise. This can mean managing energy and networks differently, rather than creating new infrastructure to meet supply and demand changes.

What we do

Electricity

The electricity industry connects generation sources to homes and businesses via transmission and distribution networks. Electricity is sold to consumers by companies who have bought it from the generators and pay to use the networks across which it is transmitted.

The UK electricity industry has five main sectors.

Generation – other companies
Generation is the production of electricity from fossil fuel and nuclear power stations, as well as renewable sources such as wind and solar.

We do not own or operate electricity generation assets in the UK.

Interconnectors – other National Grid companies and others
Transmission grids are often interconnected so that energy can flow from one country to another. This helps provide a safe, secure, reliable and affordable energy supply for citizens and society across the region. Interconnectors also allow power suppliers to sell their energy to customers in other countries.

Great Britain is linked via interconnectors with France, Ireland, Northern Ireland and the Netherlands. National Grid owns part of the interconnectors with France and the Netherlands.

National Grid sells capacity on its UK interconnectors through auctions.

Transmission – National Grid Electricity Transmission and others
Transmission systems generally include overhead lines, underground cables and substations. They connect generation and interconnectors to the distribution system.

We own and operate the transmission network in England and Wales; we operate but do not own the Scottish networks.

Our networks comprise approximately 7,200 kilometres (4,470 miles) of overhead line, 1,400 kilometres (870 miles) of underground cable and 329 substations.

For more information on how we make money from our regulated assets, see page 7.

Distribution – other companies
Distribution systems carry lower voltage networks than transmission systems over networks of overhead wires, underground cables and substations. They take over the role of transporting electricity from the transmission network, and deliver it to consumers at a voltage they can use.

We do not own or operate electricity distribution networks.

Supply – other companies
The supply of electricity involves the purchase of electricity and selling it on to customers. It also involves customer services, billing and the collection of customer accounts.

We do not sell electricity to end users.

System operator – National Grid Electricity Transmission
As system operator (SO) for England and Wales, we coordinate and direct electricity flows onto and over the transmission system, balancing generation supply and user demand. Where necessary, we pay sources of supply and demand to increase or decrease their generation or usage.

We have the same role for the two high voltage electricity transmission networks in Scotland and we have been appointed as system operator for the offshore electricity transmission regime.

Our charges for SO services are subject to a price control approved by Ofgem.

System users pay us for connection, for using the system and balancing services.

As electricity transmission system operator, our price control includes incentives to minimise the costs and associated risks of balancing the system through buying and selling energy, as well as procuring balancing services from industry participants.

What we do

Regulation

We operate as a regulated monopoly. The regulator safeguards customer interests by setting the level of charges we are allowed to pass on, so that we provide value for money, maintain safe and reliable network, and deliver good customer service.

How we make money from our regulated assets

Our licence, established under Electricity Act 1989, as amended (the Act), requires us to develop, maintain and operate economic and efficient networks and to facilitate competition in the supply of electricity in Great Britain. The licence also gives us statutory powers, such as the right to bury our cables under public highways and the ability to use compulsory powers to purchase land to enable the conduct of our business.

Our network is regulated by Ofgem, which has established a price control mechanism that sets the amount of revenue that can be earned by our regulated business. Price control regulation is designed to ensure our interests, as a monopoly, are balanced with those of our customers. Ofgem allows us to charge reasonable, but not excessive, prices giving us a future level of revenue sufficient to meet our statutory duties and licence obligations, and also to make a reasonable return on our investment.

The price control includes a number of mechanisms to achieve its objectives, including financial incentives designed to encourage us to: continuously improve the cost and effectiveness of our services; manage and operate our network efficiently; deliver high quality services to our customers and wider stakeholder community; and invest in the development of the network in a manner that ensures long-term security of supply.

Our Electricity Transmission business operates under two separate price controls. These comprise of one covering our role as transmission owner (TO) and the other for our role as system operator (SO).

The value of our regulated assets is calculated based on the terms of our regulatory agreement. These may not be calculated on the same basis as the accounting value of assets, although the principles are similar. For example, building new assets will generally increase regulated assets and disposing of assets will generally decrease regulated assets. The value of regulated assets is also increased for inflation.

Our licence also determines the amount we are allowed to charge customers, commonly referred to as our allowed revenues. Allowed revenue is calculated based on a number of building blocks:

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

Return on equity and cost of debt – regulated assets are funded through debt or equity and the licence and regulatory agreement sets this ratio. The equity portion earns a 'return on equity' (ROE). This represents the profit we can earn on our investment in regulated assets. The debt portion earns an allowance based on the cost of debt (interest costs). The regulatory agreement uses an external benchmark interest rate as a way to incentivise us to raise debt efficiently. The benchmark interest method also provides an opportunity to outperform our regulatory allowance.

Cost of service – in establishing our regulatory agreement, our regulator considers what costs an efficiently run company would incur to operate and maintain our networks. They vary and can include costs relating to employees, office rental, IT systems and taxes, for example. Our regulator determines what is considered an efficient or prudent cost and this may be different to the actual costs we incur.

Performance against incentives – our licence includes incentives that are designed to encourage specific actions, such as reducing greenhouse gas emissions. Achieving performance beyond targets set out in these incentive mechanisms can increase our allowed revenues in the current year or a future year. Failing to achieve certain minimum targets may lead to a reduction in our allowed revenue.

Timing differences – we use our allowed revenues to determine our billing rates, which we calculate using a forecast of the quantities that will be billed. Where there is a difference between the actual and estimated quantities, the amount of revenue we collect will be different to the allowed revenue. Consequently, the over- or under-collected amounts are adjusted against the following period's allowed revenues.

Price controls up to 31 March 2013

The previous price control mechanism for our UK Electricity Transmission business expired on 31 March 2013.

2012/13 saw another good year of performance, outperforming the allowed returns.

	As at 31 March 2013
RAV	£10,145m
Allowed vanilla return	4.75%
Achieved vanilla return	5.4%
Achieved ROE	11.8%

RIIO price controls

Our regulator has introduced a new regulatory framework called RIIO (revenue = incentives + innovation + outputs) that became effective on 1 April 2013 and lasts for eight years. The building blocks of the RIIO price control are broadly similar to the historical price control, however there are some significant differences in the mechanics of the calculations.

How is revenue calculated?

Under RIIO the outputs we deliver are clearly articulated and are integrally linked to the calculation of our allowed revenue. These outputs have been determined through an extensive consultation process which has given stakeholders a greater opportunity to input to these decisions. The clarity around outputs should lead to greater transparency of our performance in delivering them.

The five key output categories are:

- Safety: ensuring the provision of a safe energy network
- Reliability (and availability): promoting networks capable of delivering long-term reliability, as well as minimising the number and duration of interruptions experienced over the price control period, and ensuring adaptation to climate change
- Environmental impact: encouraging companies to play their role in achieving broader environmental objectives – specifically facilitating the reduction of carbon emissions – as well as minimising their own carbon footprint
- Customer and stakeholder satisfaction: maintaining high levels of customer satisfaction and stakeholder engagement, and improving service levels
- Customer connections: encouraging networks to connect customers quickly and efficiently

Within each of these output categories are a number of primary and secondary deliverables, reflecting what our stakeholders want us to deliver over the coming price control period. The nature and number of these deliverables varies according to the output category, with some being linked directly to our allowed revenue, some linked to legislation, and others having only a reputational impact. Ofgem, using information submitted by us along with independent assessments, determines the efficient level of expected costs necessary to deliver them. Under RIIO this is known as totex, short for total expenditure, and is similar to the sum of controllable opex and capex under the previous price control.

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

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

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

Totex is then split between fast and slow money, a new concept under RIIO, based on a specified percentage. Fast money represents the amount of totex that we are able to recover in the current year. Slow money is added to our RAV. In addition to fast money, in each year we are allowed to collect a depreciation of and a return on our RAV. This operates in a similar way to the previous price control, although there have been changes to the asset life of our electricity transmission assets. We are also allowed to collect additional revenues related to non-controllable costs and incentives.

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

Key RIIO financial metrics

Some of the key financial metrics are included below:

Cost of equity (post-tax real)	7.0%
Cost of debt (pre-tax real)	iBoxx 10 year simple trailing average index (2.92% for 2013/14)
Notional gearing	60.0%
Implied vanilla WACC*	4.6%

*Implied vanilla WACC=cost of debt x gearing + cost of equity x (1-gearing).

	Transmission Operator	System Operator
1 Fast	15.00%	72.10%
2 Slow	85.00%	27.90%
3 Sharing	46.89%	46.89%

For more information on RIIO, including incentive mechanisms, please see the relevant investor fact sheets on the Investor Relations section of the National Grid website.

Internal control and risk management

Risks are managed within the National Grid internal control and risk management processes as a whole. National Grid Electricity Transmission is part of this and participates in the processes which are described below, in addition to its own governance processes which are subject to the UK Corporate Governance Code.

The Electricity Transmission Executive Committee is responsible for day to day management of our Electricity Transmission business. The membership of this committee comprises Directors and senior business managers. The committee is chaired by John Pettigrew, who also sits on the Executive Committee of National Grid, and is the National Grid UK Chief Operating Officer.

The System Operator Executive Committee is responsible for the strategic direction of Great Britain SO activities (Gas and Electricity combined) and the RIIO incentive and output performance measures. The membership of this committee comprises Directors and senior business managers. The committee is chaired by Nick Winser, who also sits on the Executive Committee of National Grid, and is the National Grid UK Executive Director.

Overall responsibility for management of risks lies with the Board of National Grid, which is committed to the protection of our reputation and assets, as well as safeguarding the interests of our shareholders. We achieve this through maintaining a sound system of internal control.

Oversight by the National Grid Board and its committees

National Grid's Board of Directors maintains overall responsibility for the Company's system of internal control and reviews the effectiveness of the framework annually. The National Grid Board establishes the control environment, sets risk appetite, approves policies and delegates responsibilities. Where appropriate it delegates authority to its committees.

The National Grid Audit Committee receives reports from the specialist functions and reviews the effectiveness of internal controls over financial reporting and risk management procedures. Also reviews the adequacy of the external audit process, including the effectiveness, independence and objectivity of the external auditors.

The National Grid Finance Committee sets policy, monitors compliance and grants authority for financing decisions, taxation, insurance, pensions and trading/hedging activities in line with the National Grid Board's risk appetite.

The National Grid Safety, Environment and Health Committee (SEH) sets policies, implements initiatives and monitors compliance and reviews reports on key risks associated with progress towards our safety, environment and health objectives.

The National Grid Executive Committee reviews regular reports from specialist functions to monitor the adequacy and effectiveness of the internal control framework and takes appropriate action to safeguard the interests of the National Grid and to further our strategy and business objectives.

Supported by dedicated, specialist teams

Process owners carry out detailed assessments and response plans are developed and monitored regularly. The National Grid Board and process owners are supported by dedicated specialist teams. Those specialist teams being:

National Grid's Risk management team:

- works with the National Grid Board to determine risk appetite and establish and implement risk management policies;
- is responsible for the independent review and challenge of risk information throughout the business, compilation and analysis of risk profiles and monitoring risk management processes with the National Grid Group; and
- regularly reports on risks to the oversight bodies.

National Grid's Ethics and compliance management team:

- maintains our standards of ethical business conduct;
- promotes ethical behaviour and monitors compliance with external legal and regulatory requirements; and
- operates our whistleblower helplines and supports activities to prevent and detect bribery.

National Grid's Corporate audit team:

- develops and executes a risk-based audit plan; and
- provides independent, objective assurance to the National Grid Audit Committee, Safety, Environment and Health Committee, National Grid Executive Committee, Electricity Transmission Executive Committee and System Operator Executive Committee on the extent to which control and governance frameworks are operating effectively.

National Grid's Safety, environment and health team:

- develops policy recommendations for the National Grid Board;
- monitors safety, environment and health performance; and
- works with process owners to deliver our safety, environment and health objectives.

National Grid's Internal controls team:

- works with process owners to identify, document and test the design and operation of internal control over financial reporting; and
- helps refine and improve controls where required.

National Grid's system of internal control and, in particular, its risk management process, has been designed to support its strategic and business objectives as well as internal control over financial reporting. We aim to do this through:

- mitigating risk;
- making sure our information, including financial reporting, is accurate and reliable;
- complying with our obligations – both internal and external;
- applying sound governance practices; and
- making informed and timely decisions to further our objectives.

National Grid's internal controls are designed to manage rather than eliminate material risks. We balance the costs of internal controls with the magnitude and likelihood of the risks being managed in light of our risk appetite.

National Grid's internal control process

National Grid's internal control process is based on thorough and systematic processes that identify, assess and monitor business critical risks.

Accurate and reliable information plays a vital role in our decision making, while education, training and awareness are all important elements that help us maintain effective internal controls.

National Grid's internal control process starts with identifying risks, compliance matters and other issues. We do this through routine reviews carried out by process owners and facilitated by relevant dedicated, specialist teams. The Electricity Transmission Executive Committee records risks in our risk register, assesses the implications and consequences for National Grid and determine the likelihood of occurrence.

We put in place action plans, controls and other process improvements designed to address the risks and issues identified. National Grid assesses the effectiveness of the controls regularly and seeks independent assurance where it is appropriate to do so.

National Grid formally report the outcomes of its risk identification and control assessments to senior management and the relevant oversight bodies. This informs its decision-making and provides assurances about its internal controls to management and the Board of National Grid.

National Grid regularly monitor its action plans, other process improvements and the status of risks. The results of its review help update the process as the cycle continues.

Internal control over financial reporting

National Grid has specific internal mechanisms to govern the financial reporting process and the preparation of the Annual Report and Accounts. Its financial controls guidance sets out the fundamentals of internal control over financial reporting which are applied across the National Grid Group and its accounting guides provide guidance on its accounting policies.

Within National Grid processes we have system, transaction and oversight controls. In addition, businesses prepare detailed monthly management reports which include analysis of their results along with comparisons to relevant budgets, forecasts and prior year results. These are presented to and challenged by National Grid senior management within Finance. The National Grid Finance Director, in turn, presents a consolidated management report to the Board of National Grid.

These reviews are supplemented by quarterly performance reviews, attended by National Grid's Chief Executive and Finance Director. They discuss historical results and expected future performance and involve senior management from both operational and financial areas of the business.

The internal control processes comply with the Turnbull guidance on internal control and the requirements of the UK Corporate Governance Code.

Reviewing the effectiveness of National Grid internal control

Each year the Board of National Grid reviews the effectiveness of its internal control process, including financial reporting, to make sure it remains robust. The latest review covered the financial year to 31 March 2013.

What are the risks?

Our risk management process has identified the following principal 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. When appropriate, we implement processes, procedures and controls to minimise the likelihood of a risk occurring or the potential impact if it does occur. It is not always possible to eliminate a risk even where a response is in place and considered effective.

Risk factor	Details of the risk and examples of our responses
Potentially harmful activities	Aspects of the work we do could potentially harm employees, contractors, members of the public or the environment. 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 from our operations and properties, including those inherited from predecessor bodies, or formerly owned by us, and sites used for the disposal of our waste. 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, such as the effects of electric and magnetic fields. We are increasingly subject to regulation in relation to climate change and are affected by requirements to reduce our own carbon emissions as well as reduction in energy use by our customers. If the legal requirements become more onerous or our regulatory framework changes, then we may not be able to recover all the costs of complying with these laws and regulations. **Examples of mitigating actions** We have established safety and occupational health plans, programmes and procedures that are aimed at continuous improvements in safety performance. National Grid Group wide initiatives are supplemented with specific regional safety programmes. These are aimed at addressing specific areas so that safety is at the forefront of every employee's mind. National Grid also benchmark against other industry groups to seek and implement best practice. We continue to focus on process safety, aimed at preventing major incidents. This includes the process and procedures governing the development and design of our assets, as well as the competence of the people who will build, operate and maintain them. We monitor employee lost time injury frequency rate as a key performance indicator (KPI) as described on page 19. We also have other measures relating to personal and process safety, and use them to understand our safety strengths and identify any weaknesses we need to address.
Infrastructure and IT systems	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 failure to maintain the health of the system or network, inadequate forecasting of demand, inadequate record keeping or control of data or failure of information systems and supporting technology. This could cause us to fail to meet agreed standards of service, 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 of our control, such as the impact of weather, unlawful or unintentional acts of third parties, insufficient or unreliable supply or force majeure. Weather conditions can affect financial performance and severe weather that causes outages or damages infrastructure together with our actual or perceived response will materially adversely affect operational and potentially business performance and our reputation. Malicious attack, sabotage or other intentional acts, including cyber security breaches, may also damage our assets or otherwise significantly affect corporate activities and, as a consequence, have a material adverse impact on our business, results of operations and financial condition.

Risk factor	Details of the risk and examples of our responses
	Unauthorised access to, or deliberate breaches of, our IT systems may also seek to access and manipulate our proprietary business date or customer information. Unauthorised access to private customer information may make us liable for a violation of data privacy regulations. Even where we establish business continuity controls and security against threats against our systems, these may not be sufficient. **Examples of mitigating actions** We use industry best practices as part of our cyber security policies, processes and technologies and continually invest in cyber strategies that are commensurate with the changing nature of the security landscape.
Business performance	Current and future business performance may not meet our expectations Earnings maintenance and growth from our regulated electricity business will be affected by our ability to meet or exceed efficiency targets and service quality standards set by, or agreed with our regulator. If we do not meet these targets and standards, or if we do not implement the transformation projects we are carrying out as envisaged or are not able to shape our operating model to deliver success under RIIO, we may not achieve the expected benefits, our business may be materially adversely affected and our performance, results of operations and reputation may be materially harmed and we may be in breach of regulatory or contractual obligations. **Examples of mitigating actions** We have restructured our business, establishing end-to-end process teams aimed at improving our customer service and efficiency and building a culture of continuous improvement. We monitor network reliability, as a KPI, as described on page 19.
Law and regulation	Changes in law or regulation or decisions by governmental bodies or regulators could materially adversely affect us. Our business is subject to regulation by governments and other authorities. Changes in law or regulation or regulatory policy and precedent, including decisions of governmental bodies or regulators, 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, amended or renewed, whether consents for construction projects are granted in a timely manner or whether there has been any breach of the terms of a licence, approval or regulatory requirement; and (ii) timely recovery of incurred expenditure or obligations and other decisions relating to the impact of general economic conditions on us, our markets and customers, implications of climate change, whether aspects of our activities are contestable, the level of permitted revenues and dividend distributions for our business and in relation to proposed business development activities, could have a material adverse impact on our results of operations, cash flows, the financial condition of our business and the ability to develop the business in the future. See pages 7 to 8 which explain our regulatory environment in detail. **Examples of mitigating actions** We participate in regulatory and energy policy development and implementation to help shape the outcomes. We are working with DECC on its proposals relating to Electricity Market Reform. We have also restructured our business so we are prepared for our potential new role under Electricity Market Reform and to make sure we are well positioned to deliver value under RIIO. Our price control has ‘reopeners’ for some categories of expenditure where costs and volumes are currently uncertain; we can use these reopeners in certain circumstances to request additional allowances and

Risk factor	Details of the risk and examples of our responses
	output targets to be set when the cost and volumes become clear.
Cost escalation	Changes in foreign currency rates or interest rates or could materially impact earnings or our financial condition. Our results and net debt position may be affected because a significant proportion of our borrowings, and derivative financial instruments are affected by changes in interest rates. Furthermore, our cash flow may be materially affected as a result of settling hedging arrangements entered into to manage our interest rate exposure, or by cash collateral movements relating to derivative market values. Operating costs may increase faster than revenues. While income under our price controls is linked to the RPI, our operating costs may increase at a faster rate than RPI. The majority of our employees are members of a defined benefit pension scheme where the scheme assets are held independently of our own financial resources. If the scheme does not perform as currently expected, then we may be required to make additional contributions to the pension scheme which, to the extent they are not recoverable under our price controls, could adversely affect our results and financial condition. **Examples of mitigating actions** National Grid's treasury function manages our financial risks, including foreign currency and interest rate, to within pre-authorised parameters and under policies and guidelines approved by the Finance Committees of National Grid and National Grid Electricity Transmission.
Financing and liquidity	An inability to access capital markets at commercially acceptable interest rates could affect how we maintain and grow our business. Our business is financed through cash generated from our ongoing operations, bank lending facilities and the capital markets, particularly the long-term debt capital markets. Some of the debt we issue is rated by credit rating agencies and changes to these ratings may affect both our borrowing capacity and borrowing costs. In addition, restrictions imposed by the regulator may also limit how we service the financial requirements of our business. Financial markets can be subject to periods of volatility and shortages of liquidity, which may be exacerbated by the eurozone crisis. 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 discretionary and uncommitted elements of our proposed capital investment programme may need to be reconsidered and the manner in which we implement our strategy may need to be reassessed. Such events could have a material adverse impact on our business, results and prospects. Our regulatory agreements impose lower limits for the long-term senior unsecured debt credit ratings that we must hold and the amount of equity within our capital structures. In addition, our regulatory arrangements impose restrictions on the way we can operate and may restrict the ability of the company to engage in certain transactions including paying dividends, lending cash and levying charges. These include regulatory requirements for us to maintain adequate financial resources within the Company. The inability to meet such requirements or the occurrence of any such restrictions may have a material adverse impact on our business and financial condition. **Examples of mitigating actions** We identify short-term liquidity and long-term funding requirements by regularly producing short- and long-term cash flow forecasts, along with undertaking financial headroom analysis. The assessment of our liquidity takes into account the regulatory requirements that may restrict our ability to pay dividends from some of our operating businesses. We maintain a number of commercial paper and medium-term note programmes to facilitate short- and long-term debt issuance. We manage refinancing risk by limiting the amount of debt maturities on borrowings in each financial year.

Risk factor	Details of the risk and examples of our responses
Customers and counterparties	Customers and counterparties may not perform their obligations. Our operations are exposed to the risk that customers, suppliers, financial institutions and other whom we do business will not satisfy their obligations, which could materially adversely affect our financial position. We have significant concentrations of receivables with a small number of large electricity utilities. **Examples of mitigating actions** Security deposits or other forms of collateral may be obtained from commercial and industrial customers to reduce the risk from customer default. The Finance Committee has agreed a policy for managing financial counterparty risk. This sets exposure limits based on an individual counterparty's credit rating from independent rating agencies. We also consider other leading indicators of counterparty financial distress and reduce exposure below the approved limits, if appropriate. Where multiple financial transactions are entered into with a single financial counterparty, a netting arrangement is usually put in place to reduce our exposure to the credit risk.
Employees and others	We may fail to attract and retain employees with the competencies, values and behaviours required to deliver our strategy and vision and ensure they are engaged to act in our best interests. Our ability to implement our strategy depends on the capabilities and performance of our employees and leadership. Our ability to implement our strategy and vision may be negatively affected by loss of key personnel or an inability to attract, develop or retain appropriately qualified personnel (in particular for technical positions where availability of appropriately qualified personnel may be limited), or if significant disputes arise with our employees. As a result, there may be a material adverse effect on our business, financial condition, results of operations and prospects. There is a risk that an employee or someone acting on our behalf may breach our internal controls or internal governance framework or may contravene applicable laws and regulations. This could have an impact on our results of operations, our reputation and our relationship with our regulator and other stakeholders. **Examples of mitigating actions** During 2012, National Grid introduced a new global leadership development framework. National Grid are developing a global, centralised academy to allow us to gather and share best practice from within National Grid and from our external partners. This should help us build the skills and capabilities our business will need in the future, as well as contributing to employee development. Described on pages 15 and 16 are some of the ways National Grid seek to engage employees, including how we promote inclusion and diversity. Employee engagement is monitored as a KPI by National Grid who formally solicit employee opinions via a Group wide employee survey annually. Further information can be found in the National Grid Annual Report and Accounts 2012/13 and on National Grid's website at www.nationalgrid.com.

What did we achieve?

It has been another important year for National Grid Electricity Transmission as we secured appropriate regulatory changes and continued to bed down organisational change. Here we highlight some of the work we did, and initiatives we introduced, during 2012/13 to support our strategy.

Delivering operational excellence

Safety remains a top priority for us and we strive to improve our performance. We also recognise the vital importance of good customer service and community relationships. Our licence and regulatory agreement set our reliability targets and these are linked to our revenue streams.

Safety

Our ambition is to achieve a world-class safety level by 2015, featuring a lost time injury frequency rate of below 0.1. We intend to achieve this through a relentless leadership focus, robust safety management systems and tactical actions focused on our main risks, which may vary between regions and business areas.

Our employee lost time injury frequency rate for 2012/13 was 0.13, compared with 0.14 in 2011/12. While this represents a marginal improvement we recognise that we need to do more to achieve our ambition. We have included below some examples of our main safety initiatives, which aim to reduce incidents.

We updated our overhead line rules for work at height and guidance about the use of equipment at height. We connect office-based employees to the safety aspects of our operational activities through targeted campaigns, raising the profile of safety in the workplace and behaviours at home. Examples of our initiatives during 2012/13 include interactive experiences, screen savers and seasonal safety messages.

In 2012/13, National Grid published its company wide process safety management system and updated its process safety commitment statement. National Grid modified the global incident reporting system so it can better differentiate process related incidents to improve communication, enhance visibility and share information relating to process safety events. We have been continually increasing awareness and developing our safety culture through training initiatives, including e-learning.

Delivering customer service

We measure the success of our customer service initiatives through the Ofgem customer satisfaction studies and independent customer research.

Reliability

We aim to deliver reliability by: planning our capital investments to meet challenging demand and supply patterns; designing and building robust networks; risk-based maintenance and replacement programmes; and detailed and tested incident response plans.

For further details on our reliability performance, see page 19.

Business changes

We are restructuring our business so that we are well positioned to deliver value under RIIO and are ready for our potential new role under Electricity Market Reform.

We have completed our organisational design for senior leaders. We are consulting Transmission employees on a number of changes which, if agreed, will reduce costs and increase efficiency. We have redefined our organisational design, reducing the number of manager roles by 22% (across Gas and Electricity Transmission combined).

Engaging our people

Engaging our people helps to retain the best possible range of talent and experience, which will be necessary to meet the needs of our business. We are committed to developing our employees to the best of their abilities and to creating an inclusive and diverse culture.

We measure employee engagement through our employee opinion survey. Below we describe the results of this year's survey and highlight some of the actions that have been taken in response to previous ones.

Development

The results of our 2012 survey showed that one of the three main factors driving engagement in our Company was having opportunities for personal development. To develop the leadership capability of our next generation of managers and middle level leaders, we introduced a new global leadership development framework in 2012.

Our business has developed an education and readiness programme to raise everyone's awareness and understanding of RIIO, and how we will need to change the way we work both as an organisation and as individual employees.

In the UK, National Grid's graduate retention levels are consistently high, standing at 85% in January 2013.

We provide training and other support so that our people can build, maintain and operate our networks safely and reliably.

Appreciate

The results of past employee surveys showed us that employees see recognition as an important part of engagement. So, we have launched 'appreciate', a global recognition programme that encourages our people to recognise and reward their colleagues for a job well done. Features include career milestones and the Chairman's Awards, as well as an online system employees can use to send and receive feedback on great work they see. The system also administers non-financial awards.

Promoting inclusion & diversity
We aim to develop and operate our business with an inclusive and diverse culture, with equal opportunity in recruitment, career development, training and reward. This applies to all employees regardless of race, gender, nationality, age, disability, sexual orientation, gender identity, religion and background. Where existing employees become disabled, our policy is to provide continued employment and training wherever practical. These policies support the attraction and retention of the best people, improve effectiveness, deliver superior performance and enhance our success.

We promote inclusion & diversity both within and outside National Grid. Our female employees are able to access the Springboard and Spring Forward development programmes in the UK.

Our employee survey
The results of National Grid's 2013 survey, have helped us identify specific areas where we are performing well and those areas we need to improve. Our engagement index has fallen by eight points to 76%. It is fair to assume the extensive changes we have introduced in the UK have contributed to the fall in our engagement score. Managers receive a simple scorecard that aims to create greater leadership accountability and we produce survey reports and action plans at Company, regional, business unit, function and team levels. Managers also have access to an engagement framework. This provides them with practical tools and guidance to support them when developing action plans for their teams.

Attracting the best people
We have introduced a web-based recruitment system to improve our hiring process in the UK.

We have continued our programmes designed to inspire the engineers and scientists of the future. Last year, around 6,500 young people discovered more about energy through National Grid employees, and thousands more visited our website www.nationalgrideducation.co.uk.

Stimulating innovation

Encouraging and adopting new ideas helps us to work efficiently and effectively. This in turn helps us to access investment and growth opportunities as well as to engage with our regulators. It is essential to efficiently deliver what is required.

New sources of funds
This year we issued approximately £2 billion in new bonds and other debt to raise new capital as well as to refinance maturing debt. As we continue to invest in our networks and other assets, we will need to raise new financing in the future. To attract good pricing for our debt and maintain a strong balance sheet, we consider different options for how and where to do this.

We issued our largest maple bond – one that is issued by a foreign company in the Canadian market for Canadian investors. We achieved a nominal amount of C$750 million – the largest ever corporate maple bond at the time – and followed this two months later with a second maple bond with a nominal amount of C$400 million.

Innovation initiatives
We have continued to make good progress on developing the T-pylon and reached a major milestone this year by erecting the first full size prototype suspension pylon in January followed in April by the tension pylon. We are now conducting mechanical tests to verify the pylon's capabilities. You can read more about the project in our T-pylon blog, available on our website.

Our partnership with Manchester University in the UK has seen the development of an electrically insulating composite cross arm for transmission pylons. In future this may allow us to increase the voltage on overhead lines from 275 to 400 kV without replacing the existing pylons with taller structures.

Engaging externally

We work with external stakeholders to shape energy policy as these decisions directly affect our business. We seek to understand the expectations of all our stakeholders so we can deliver a service that meets their needs.

Regulatory agreements
We have agreed all the price control arrangements Ofgem has proposed for RIIO. For more information on RIIO see page 7 and 8.

Powering Britain's Future
We have launched a nationwide conversation about the challenges we face in delivering the energy infrastructure the country needs and minimising the impacts on communities and the environment. Our Powering Britain's Future campaign aims to raise awareness about the scale of the energy challenge facing the UK and find common ground with stakeholders and the public so we can work together to find solutions. The campaign started with a stakeholder forum in London, bringing together senior representatives from bodies including the Campaign to Protect Rural England, the consumer group Which? and the National Trust, as well as industry and government leaders. You can find out more about the campaign at www.poweringbritainsfuture.co.uk.

Talking networks
Consulting with the people who have a stake in what we do has always been fundamental to National Grid. In preparing for the new RIIO regulatory framework, we wanted to make sure we fully understood our stakeholders' priorities and could take their views into account when shaping our delivery plans.

We have continued our talking networks initiative to gather views from consumers, government, the energy sector and environmental organisations through workshops, surveys, meetings and forums. We have published the outcome of our consultations on the talking networks section of our website, describing the feedback we received and the action we are taking as a result.

Stakeholder engagement is an enduring approach that will continue through the RIIO period and beyond. Through talking networks we continue to encourage our stakeholders to let us know how we are doing, how they would like to engage with us and where we should focus our resources.

Embedding sustainability

By embedding sustainability into National Grid's decision-making we aim to create value, preserve natural resources and respect the interests of our communities.

Our approach to sustainability has involved developing our long-term strategy under the banner of Our Contribution. This responds to external drivers and input from stakeholders, drives efficiency, supports growth and profitability, and aims to:

- build a culture of sustainability within our organisation; and
- integrate sustainability into our decision-making and everyday activities, so we can protect and preserve natural resources, as well as respect the interests of the communities in which we operate.

Through our sustainability summit we worked with many of our external stakeholders to discover and define our long-term ambition for National Grid's climate change, sustainability and environmental strategy. The initial programme to deliver Our Contribution builds on projects developed through the summit. Among the initiatives has been the launch of a competition for our UK suppliers. We have challenged them to find innovative ways of implementing the principles of the circular economy, promoted by the Ellen MacArthur Foundation, into the design of the materials, plant, processes and equipment they supply to us. We have robust investigation and remediation programmes to clean up waste. We also have controls in place to minimise or mitigate releases to the environment during remediation activities. These range from containment to spill response contracts and equipment.

Climate change

This year National Grid has continued its focus on reducing greenhouse gas emissions and it remains on target to achieve its 2020 and 2050 targets of a 45% and 80% reduction in emissions.

We measure and report our emissions of the six Kyoto greenhouse gases using the methodologies set out in the *WRI/ WBCSD Greenhouse Gas Protocol: A Corporate Accounting and Reporting Standard (Revised Edition).*

Our total Scope 1 and 2 greenhouse gas emissions for 2012/13 were around 0.3 million tonnes carbon dioxide equivalent, representing a 40% reduction compared with our 1990 baseline.

National Grid Scope 1 and 2 greenhouse gas emissions are independently verified; a copy of the verification statement is available on the National Grid website.

We have continued our investigations into new technology and processes in areas such as capturing SF_6 emissions and replacements for SF_6 used in switchgear, where promising alternatives include CF_3I (trifluoroiodomethane) and vacuum circuit breaker technology. As SF_6 is 23,900 times more potent than CO_2 any reduction or elimination will play a significant role in future emission reduction programmes.

Driving growth

Growing our core businesses and developing future new business options depend on delivery of our investment plans. Combining this with operational and procurement efficiencies contributes to our ability to achieve strong returns and meet our commitment to investors.

Capital expenditure

Capital expenditure this year was £1.4 billion. Much of this work involves asset replacement but there are also a number of new initiatives.

We have fundamentally changed our partnering approach for delivering major transmission capital projects. This involves revised contracts with our electricity alliance partners that make accountability clearer. We have also introduced additional layers of competition for delivery of some aspects of our work.

Two significant projects we have been working on are the Western Link and London power tunnels.

Western Link: The Western Link is a joint project with SP Transmission, part of Iberdrola Group. It will bring renewable energy from Scotland to homes and businesses in England and Wales, via a pair of HVDC cables, approximately 422 kilometres long, between Hunterston in Scotland and Deeside in North Wales. The cable will travel for 385 kilometres under the Irish Sea before coming ashore on the Wirral and travelling underground to Deeside.

At present, the Scotland and England power transmission networks are connected by two overhead power lines and some smaller 132 kV circuits across the boundary which are of limited capacity. The Western Link will provide a further connection, easing pressure on the existing bottlenecks and helping to bring more renewable energy through the system.

A contract valued at more than £1 billion has been let by the joint venture to a consortium which will design, manufacture and construct the link. Planning applications and easements are in progress and work has started on site.

The project is expected to become operational in 2016.

London power tunnels: The aim of phase 1 of this project is to replace and upgrade five major buried 275kV cable circuits within the existing London network. Three new tunnels totalling approximately 30 kilometres are currently under construction with 15 kilometres already delivered to date. On completion, we will have energised 10 new 400kV circuits, requiring around 200 kilometres of new cable and including the construction of three new substations. The total cost of the project is around £1 billion and we have delivered around a tenth of this in 2012/13.

Strategic workforce planning
To help drive growth, we need to consider our long-term workforce needs. Our strategic workforce planning approach allows us to look ahead up to ten years and forecast these needs, based on our business plans and an ageing workforce. The approach has allowed us to plan for RIIO, identifying any gaps we may have in terms of skills and experience to meet new ways of working under the new regulatory arrangements.

Where we are heading

2012/13 has been a significant year, marking the start of a major transformation programme that will enable us to respond to our changing external and internal operating environment.

Having established an operating model that allows us to see and understand more clearly the performance of our regulated businesses, we are now focused on driving performance to make sure we meet the needs of our customers and stakeholders and deliver value under the new price controls.

In particular we will need to be sharper in our commercial relationships, driving the performance of our contractors.

We have been asked by DECC to act as delivery body for its potential electricity market reforms (see page 5). We will carry out analysis to help inform Government decisions on energy policy, as well as administering key parts of the enduring regime.

Priorities for the year ahead

- Continue to improve safety performance and maintain focus on specific areas including induced voltage.
- Build on the foundations we have established during 2012/13 and deliver under the first year of our new price control.
- Embed the organisational design through all layers of our business.
- Define and embed new ways of working.
- Continue to enhance our capabilities in process and performance excellence, as well as commercial and contract management.
- Increase innovation to help us meet the output measures we are committed to delivering under RIIO.
- Continue to work closely with DECC and Ofgem to help inform and manage security of supply through a period of significant change in the UK energy market.

Measuring performance – our KPIs

We measure the achievement of our objectives, make operational and investment decisions and reward our employees 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.

KPIs are used to measure our progress on strategic priorities, aligning with those activities that combine to deliver our strategy. Non-financial KPIs are often leading indicators of future financial performance as improvements in these measures build our competitive advantage, for example through attractive regulatory arrangements. Financial KPIs are trailing indicators of the success of past initiatives and specific programmes. They also highlight areas for further improvement and allow us to ensure our actions are culminating in sustainable long-term growth in shareholder value.

We have started a review to determine whether the current KPIs remain relevant under RIIO, as the way our allowed revenues are calculated and how they will vary according to our actual performance has changed.

It is possible that this may lead to increased volatility in our statutory revenue figures or some changes to the balance between operating and capital expenditure in the business. We will report on the new KPIs when they have been agreed with the National Grid Board.

Commentary on our overall financial results can be found on pages 20 to 25.

Financial KPI

Strategic element	Measuring performance for	KPI	Definition and performance
All	Financial outperformance	Operational return	Electricity Transmission operational return against the allowed return set by the regulator for the current price control period. **2012/13: 5.4%** 2011/12: 5.6% Allowed return: 4.75% Our target is to out perform this allowed return.

Non-financial KPIs

Strategic element	Measuring performance for	KPIs	Definition and performance
Operational excellence	Safety and reliability	Employee lost time injury frequency rate	Injuries resulting in employees taking time off work per 100,000 hours worked on a 12 month basis **2012/13: 0.13** 2011/12: 0.14 Target: zero
		Network reliability	Reliability of Electricity Transmission network as a percentage against the target set by our regulator **2012/13: 99.99999%** 2011/12: 99.999999% Target: 99.9999%
All	People	Employee engagement index	Employee engagement index calculated using responses to National Grid's annual employee survey. Target is to improve. Transmission business (Gas and Electricity combined) **2012/13: 76%** 2011/12: 84%
Innovation & efficiency	Environmental responsibility	Greenhouse gas emissions	Percentage reduction in greenhouse gas emissions. % reduction against 1990 baseline **2012/13: 40% reduction** 2011/12: 36% reduction National Grid Target: 45% reduction by 2020 and 80% reduction by 2050 (see page 3)

Financial review

Financial performance

Introduction

This year has seen good financial performance. We have seen a year of record adjusted operating profit, reflecting solid operational performance across the business and driven by increased revenue from RPI indexation and the rollover of the transmission price control. Adjusted earnings also benefited from a lower effective tax rate and higher regulated income.

In the coming year we will seek to extract additional value from the investments we have been making through our transformation programmes and restructurings and our focus on end to end process improvements, coupled with the new RIIO price control.

Continuing to deliver a good return and maintain a strong balance sheet are key targets for us in the coming years. We aim to do this through growth in assets, earnings and cash flows, supported by improved cash efficiency. Together with a robust regulatory framework we are confident that we can maintain strong, stable credit ratings and a prudent level of gearing, while delivering attractive returns.

Use of adjusted profit measures

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

The first of these components is referred to as an adjusted profit measure, also known as a business performance measure. This is the principal measure used by management to assess the performance of the underlying business.

Adjusted results exclude exceptional items and remeasurements. These items are reported collectively as the second component of the financial measures.

Note 3 on page 41 explains in detail the items which are excluded from our adjusted profit measures.

Adjusted profit measures have limitations in their usefulness compared with the comparable total profit measures as they exclude important elements of our financial performance. However, we believe that by presenting our financial performance in two components it is easier to read and interpret financial performance between periods, as adjusted profit measures are made more comparable by removing the distorting effect of the excluded items, and those items are more clearly understood if separately identified and analysed. The presentation of these two components of financial performance is additional to, and not a substitute for, the comparable total profit measures presented.

Management uses adjusted profit measures as the basis for monitoring financial performance 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. We separately monitor and disclose the excluded items as a component of our overall financial performance.

Reconciliations of adjusted profit measures to the total profit measure, that includes both components is shown in the tables below.

Reconciliation of adjusted profit measures

Reconciliation of adjusted operating profit to total operating profit

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

	Years ended 31 March	
	2013 £m	2012 £m
Adjusted operating profit	**1,040**	870
Exceptional items	**(31)**	(5)
Total operating profit	**1,009**	865

Reconciliation of adjusted operating profit to adjusted earnings and earnings

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

	Years ended 31 March	
	2013 £m	2012 £m
Adjusted operating profit	**1,040**	870
Adjusted net finance costs	**(228)**	(178)
Adjusted profit before tax	**812**	692
Adjusted taxation	**(197)**	(182)
Adjusted earnings	**615**	510
Exceptional items	**14**	65
Remeasurements	**29**	(30)
Earnings	**658**	545

Reconciliation of adjusted profit excluding timing differences to total operating profit

Adjusted operating profit excluding timing differences are discussed below.

	Years ended 31 March	
	2013	**2012**
	£m	**£m**
Adjusted operating profit excluding timing differences	**1,011**	**907**
Timing differences	**29**	**(37)**
Adjusted operating profit	**1,040**	870
Exceptional items	**(31)**	(5)
Total operating profit	**1,009**	865

Measurement of financial performance

Key performance indicators (KPIs)

Our financial KPI is set out on page 19.

Operational return

We measure our performance in generating value from the investments we make by dividing the annual return of our Electricity Transmission business by our regulatory asset base. Annual return consists of adjusted earnings, amended for a number of items including regulatory timing differences and depreciation, net financing costs and a pension deficit adjustment. Our regulatory asset base consists of invested capital, which is the opening RAV inflated to mid-year using RPI inflation. This is equivalent to the vanilla return set out in our price controls.

For 2012/13, our operational return was 5.4% compared with 5.6% in 2011/12 and a regulatory allowed return (vanilla return) of 4.75%.

Earnings

Timing

As discussed on pages 7 and 8, our allowed revenues are set in accordance with our regulatory price controls. We calculate the billing rates we charge our customers based on the estimated volume of transmission services we believe will be provided during the coming period. The actual volumes of transmission services will differ from this estimate and therefore our total actual revenue will be different from our total allowed revenue. These differences are commonly referred to as timing differences. If we collect more than the allowed level of revenue, the balance must be returned to customers in subsequent periods, and if we collect less than the allowed level of revenue we may recover the balance from customers in subsequent periods. The amounts calculated as timing differences are estimates and subject to change until the variables that determine allowed revenue are final.

Our profit for the year includes an estimated in year over-collection of £29 million (2012: £37 million under-collection) and our closing balance of estimated over-recovery at 31 March 2013 was £5 million (2012: £24 million under-recovery). All other things being equal, the majority of that balance would normally be returned to customers in the following year. The table below shows the impact of timing differences on adjusted operating profit.

	Years ended 31 March	
	2013	**2012**
	£m	**£m**
Adjusted operating profit excluding timing differences	**1,011**	907
Timing differences	**29**	(37)
Adjusted operating profit	**1,040**	870

Adjusted operating profit

Adjusted operating profit to operating profit

The results for the years ended 31 March 2013 and 2012 were as follows:

	Years ended 31 March	
	2013	**2012**
	£m	**£m**
Revenue	**3,111**	2,813
Operating costs excluding exceptional items	**(2,071)**	(1,943)
Adjusted operating profit	**1,040**	870
Exceptional items	**(31)**	(5)
Operating profit	**1,009**	865

Principal movements (2011/12 – 2012/13)

	Operating profit £m
2011/12 adjusted operating profit	**870**
Timing (1)	**66**
Net regulated income (2)	**165**
Regulated controllable operating costs (3)	**(3)**
Depreciation and amortisation (4)	**(42)**
Post retirement costs (5)	**(5)**
Other	**(11)**
2012/13 adjusted operating profit	**1,040**

Our adjusted operating profit has increased 20% to £1,040 million and is primarily due to:

1 - In year estimated over-recovery of £29 million compared with a prior year estimated under-recovery of £37 million. The closing estimated over-recovered balance is £5 million. Favourable timing differences of £66 million.

2 - Increase in regulated revenues under our price control allowances of £165 million.

Offset by:

3 - Increased costs driven by inflation, higher maintenance workload and recruitment, increase in charges under the balancing services incentive scheme and training costs associated with our capital investment programme.

4 - Higher average asset values due to the capital investment programme and some one-time asset write-offs.

5 - Increases in contribution rates for our defined benefit pension scheme.

Adjusted earnings

Adjusted earnings and earnings have been impacted by movements in adjusted operating profit as described above, as well as:

Adjusted finance costs

Adjusted net finance costs were £228 million in 2012/13, compared with £178 million in 2011/12. More information on derivatives can be found in note 9 to the consolidated financial statements.

Adjusted taxation

Adjusted taxation for 2012/13 was a charge of £197 million (2011/12: £182 million). This represents an effective tax rate of 24.3% (2011/12: 26.3%). This reduction in effective tax rate is primarily because of a 2% reduction in the UK corporation tax rate. More information on taxation can be found in note 5 to the consolidated financial statements.

Exceptional items

Exceptional charges of £31 million in 2012/13 consisted of restructuring costs (2011/12: £5 million of restructuring costs).

Exceptional finance costs and remeasurements

Financial remeasurements relate to net gains on derivative financial instruments of £38 million (2011/12: £41 million net losses). More information on exceptional finance costs and remeasurements can be found in note 4 to the consolidated financial statements.

Exceptional taxation

Taxation related to exceptional items and remeasurements changes each year in line with the nature and amount of transactions recorded. In addition, exceptional taxation in 2012/13 included an exceptional deferred tax credit of £37 million arising from a reduction in the UK corporation tax rate from 24% to 23%, applicable from 1 April 2013. Exceptional taxation in 2011/12 included an exceptional deferred tax credit of £69 million arising from a reduction in the UK corporation tax rate from 26% to 24%, applicable from 1 April 2012.

More information on exceptional items and remeasurements can be found in note 3 to the consolidated financial statements.

More information on taxation can be found in the National Grid Annual Report and Accounts 2012/13 and on National Grid's website at www.nationalgrid.com.

Financial review

Financial position and resources

Summarised balance sheet

Years ended 31 March	2013 £m	2012 £m
Intangibles	**89**	72
Property, plant and equipment	**9,548**	8,465
Current assets*	**271**	259
Current liabilities*	**(812)**	(713)
Net deferred tax liabilities	**(749)**	(746)
Provisions and other non-current liabilities	**(381)**	(351)
Pensions	**(620)**	(512)
Net debt	**(5,919)**	(5,234)
Net assets	**1,427**	1,240

* excludes amounts related to net debt and provisions reported in other lines

Intangibles
Intangibles increased by £17 million during 2012/13 to £89 million. This increase relates to software additions of £29 million offset by amortisation of £11 million.

Property, plant and equipment
Property, plant and equipment increased by £1,083 million to £9,548 million. This was principally due to capital expenditure of £1,401 million, predominantly in the extension of our regulated networks, partially offset by £314 million of depreciation.

As a result of capital expenditure in 2012/13, and after allowing for depreciation and inflation, we estimate that our RAV will increase by approximately £1 billion (2011/12: £0.7 billion).

Current assets
Current assets have increased by £12 million to £271 million. This was due to a rise in accrued income and prepayments of £17 million.

Current liabilities
Current liabilities have increased by £99 million to £812 million. This is mainly due to an increase in trade payables of £146 million.

Deferred tax liabilities
The net deferred tax liability increased by £3 million to £749 million. Refer to note 5 of the consolidated financial statements for further information.

Provisions and other non-current liabilities
Provisions and other non-current liabilities increased by £30 million to £381 million. Further information on provisions is provided in note 18 to the consolidated financial statements.

Net debt

Funding and liquidity management
Funding and treasury risk management for National Grid Electricity Transmission 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 and National Grid Electricity Transmission. The Finance Committees are responsible for regular review and monitoring of treasury activity and for approval of specific transactions, the authority for which may be 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 can be found in the 'What are the risks?' discussion starting on page 11 and in note 24 of the consolidated financial statements.

Surplus funds
Investment of surplus funds, usually in short-term fixed deposits or placements with money market funds that invest in highly liquid instruments of high credit quality, is subject to our counterparty risk management policy.

Composition of net debt

At 31 March	2013 £m	2012 £m
Cash, cash equivalents & financial investments	**920**	265
Borrowings and bank overdrafts	**(6,843)**	(5,428)
Derivatives	**4**	(71)
Total net debt	**(5,919)**	(5,234)

The increase in net debt of £685 million to £5,919 million is explained as follows:

Movement in net debt

	£m
Opening net debt at 1 April 2012	(5,234)
Factors decreasing net debt:	
- Operating cash flows	1,303
Factors increasing net debt::	
- Tax	(100)
- Non-cash movements (i)	(62)
- Dividends	(400)
- Interest	(169)
- Capital expenditure & other	(1,257)
Closing net debt at 31 March 2013	(5,919)

(i) Includes RPI inflation linked debt accretion £(66) million (2012: £(110) million).

Factors decreasing net debt

Our primary source of cash relates to operating cash flows as detailed separately below.

Factors increasing net debt

Our primary use of cash is for capital expenditure and other investing activities. This has increased by £143 million primarily due to increased investment in our business. We also utilised cash for dividends which were £200 million higher. Net interest paid was £20 million higher than prior year, reflecting higher average net debt. Tax paid was £100 million, £36 million lower than prior year due to settlement of historic tax balances in the prior year. Non-cash movements related to increases in the value of inflation linked debt and remeasurements.

Operating cash flows

Annual cash flows from our operations are largely stable over a period of years, as our electricity transmission operations are subject to multi-year price control agreements with Ofgem.

Cash flow from operations increased by £168 million in 2012/13 to £1,303 million due to the increase in operating profit, partly offset by a reduction in working capital and pension obligations.

Borrowings

The Finance Committees of National Grid and National Grid Electricity Transmission controls refinancing risk by limiting the amount of our debt maturities arising from borrowings in any one year, which is demonstrated by our maturity profile.

The maturity profile of our gross borrowings at 31 March 2013 was as follows:

	£m
Less than 1 year	685
In 1 to 2 years	-
In 2 to 3 years	158
In 3 to 4 years	200
In 4 to 5 years	625
In more than 5 years	5,175
	6,843

During the year we continued to refinance where attractive opportunities arose. We received £1,867 million of proceeds from new loans and debt issuance and repaid £637 million of borrowings during the year.

As at 31 March 2013, total borrowings of £6,843 million including bonds, bank loans and other debt had increased by £1,415 million from prior year. This increase was driven by proceeds from new loans and debt issuance, combined with fair value increases in borrowings and accretions on RPI linked debt. We expect to repay £685 million of our maturing debt in the next 12 months, and that we will be able to refinance this debt through the capital and money markets.

Further information on borrowings can be found on the debt investors' section of National Grid's website and in note 14 of the consolidated financial statements.

Derivatives

	At 31 March	
	2013	**2012**
	£m	**£m**
Interest rate swaps	**32**	21
Cross-currency interest rate swaps	**80**	72
Foreign exchange forward contracts	**1**	(5)
Forward rate agreements	**(2)**	(2)
Inflation linked swaps	**(107)**	(157)
	4	(71)

We use derivative financial instruments to manage our exposure to risks arising from fluctuations in interest rates and exchange rates. We value our derivatives by discounting all future cash flows by externally sourced market yield curves at the balance sheet date, taking into account the credit quality of both parties. The increase in our derivatives of £75 million therefore represents movements as a result of underlying market variables and composition of the derivative portfolio.

The currency exposure on our borrowings is managed through the use of cross-currency swaps and results in a net debt profile post derivatives that is almost entirely sterling.

The interest rate profile of net debt is actively managed under the constraints of our interest rate risk management policy as approved by the Finance Committees of National Grid and National Grid Electricity Transmission. Our interest rate exposure, and therefore profile, will change over time.

The table below shows the interest rate profile of our net debt before derivatives as at 31 March 2013 and the locked in impact of derivatives on our net debt as at 31 March 2013 for 2012/13 and future years. The 2013/14 position reflects the use of derivatives, including forward rate agreements to lock in interest rates in the short term. The future years' position excludes derivatives that mature within the next year.

	Pre-derivatives	Post derivatives	
	31 March 2013	2013/14	Future years
	%	%	%
Fixed	61	53	38
Floating*	(8)	-	12
RPI linked	47	47	50
	100	100	100

*We are currently in a net asset position on floating instruments and our exposure is shown as a negative in the table above.

Further details on our foreign currency and interest rate risk management can be found in the risk factors discussion starting on page 11 and in note 24(a) of the consolidated financial statements.

Pensions

We operate pension arrangements on behalf of our employees. The National Grid Electricity Group of the Electricity Supply Pension Scheme is closed to new entrants. Membership of the defined contribution section of the National Grid UK Pension Scheme is offered to all new employees. Only assets and

liabilities in respect of the National Grid Group of the Electricity Supply Pension Scheme are recognised in these financial statements.

Pension plan assets are measured at the bid market value at the balance sheet date. Plan liabilities are measured by discounting the best estimate of future cash flows to be paid out by the plans using the projected unit method. Estimated future cash flows are discounted at the current rate of return on high quality corporate bonds in UK debt markets of an equivalent term to the liability.

A summary of movements in the IAS 19 accounting deficit is set out below:

Net plan liability	£m
As at 1 April 2012	(512)
Current service cost	(29)
Expected return less interest	(11)
Curtailments, settlements and other	(4)
Actuarial gains/(losses)	
- on plan assets	134
- on plan liabilities	(266)
Employer contributions	68
As at 31 March 2013	**(620)**
Represented by:	
Plan assets	1,943
Plan liability	(2,563)
Net plan liability	(620)

The principal movements in net obligations during the year arose as a consequence of a decrease in the discount rate due to declines in corporate bond yields. Actuarial gains on plan assets reflected improvements in financial markets.

Plan assets are predominantly invested in equities, corporate bonds, gilts, property and short-term investments. Our plan is trustee administered and the trustees are responsible for setting the investment strategy and monitoring fiduciary investment performance, consulting with us where appropriate.

The investment profile of our pension plan assets as at 31 March 2013 is illustrated below:

	%
Equities	35.7
Corporate bonds	10.9
Gilts	34.1
Property	3.9
Other	15.4
	100.0

Further information on our pension and other post-retirement obligations can be found in note 23 of the consolidated financial statements.

Actuarial valuation of UK pensions

A triennial valuation is carried out for the independent trustees of our two UK defined benefit plans by professionally qualified actuaries, using the projected unit method. The next full actuarial valuations of both the National Grid UK Pension Scheme and the National Grid Electricity Group of the Electricity Supply Pensions Scheme are to be performed as at 31 March 2013 with the valuation results to be agreed by mid 2014. Further detail on the results of the last full triennial valuations performed as at 31 March 2010 can be found in note 23 to the consolidated financial statements.

Off-balance sheet items

There were no significant off-balance sheet arrangements other than the commitments and contingencies discussed below.

Commitments and contingencies

Commitments and contingencies outstanding at 31 March 2013 and 2012 are summarised in the table below:

	2013	2012
	£m	£m
Future capital expenditure contracted but not provided for	**1,941**	1,828
Total operating lease commitments	**66**	69
Other guarantees	**908**	707

The increase in capital expenditure contracted but not provided for is a result of the continued ramp up in our capital investment programme.

The other guarantees includes a guarantee provided in relation to our portion of the construction of the HVDC west coast link between Scotland and England. This guarantee expires in 2016.

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.

Further information on commitments and contingencies can be found in note 21 to the consolidated financial statements, together with information on litigation and claims.

Going concern

Having made enquiries, the Directors consider that the Company and its subsidiary undertakings 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 the Company. More details of our financial risks, including liquidity position are provided in note 24 to the consolidated financial statements. There have been no major changes to the Company's significant liquidity and solvency risks in the year.

Directors' Report

for the year ended 31 March 2013

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 during the year or subsequently were:

Andrew Agg	Appointed June 2013
Malcolm Cooper	Appointed July 2007
Stuart Humphreys	Resigned May 2013
John Pettigrew	Appointed September 2012
Paul Whittaker	Appointed July 2007
Nick Winser	Appointed April 2003

The Company has arranged, in accordance with the Companies Act 2006 and the Articles, qualifying third party indemnities against financial exposure that Directors may incur in the course of their professional duties. Equivalent qualifying third party indemnities were, and remain, in force for the benefit of those Directors who stood down from the Board during the year ended 31 March 2013. Alongside these indemnities, the Company places Directors' and Officers' liability insurance cover for each Director.

Principal activities and business review

A full description of the Company's principal activities, business, key performance indicators and principal risks and uncertainties is contained in the Strategic Review on pages 1 to 25, which are incorporated by reference into this report.

Material interests in shares

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

Dividends

An interim dividend of £400 million was paid during the year (2011/12: £200 million interim dividend). The Directors have not proposed a final dividend.

Donations

During 2012/13, some £0.04 million (2012/13 £0.4 million) was invested in support of community initiatives and relationships in the UK. There were no direct charitable donations for 2012/13 (2011/12: £nil 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 £7 million during the year (2011/12 £7 million).

Financial instruments

Details on the use of financial instruments and financial risk management are included on pages 13 to 14 in the Strategic Review.

Future developments

Details of future developments are contained in the Strategic Review.

Employee involvement

Details of how the Company involves its employees are contained in the Strategic Review on page 15, which are incorporated by reference into this report.

Policy and practice on payment of creditors

It is our policy to include in contracts or other agreements, terms of payment with suppliers. Once agreed, we aim to abide by these terms of payment. The average creditor payment period at 31 March 2013 was 30 days (19 days at 31 March 2012).

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 Company's Annual General Meeting for 2013 will be issued separately to shareholders.

By order of the Board

Andrew Agg
Director
24 June 2013

National Grid Electricity Transmission plc
1-3 Strand, London WC2N 5EH
Registered in England and Wales Number 2366977

Introduction to the financial statements

We have adopted a revised presentational format to provide shareholders and users of these financial statements with additional information and guidance and to make them easier to understand.

Throughout these financial statements we have included 'Keeping it simple' paragraphs, providing commentary in plain English on what the disclosures mean and why they are important to the understanding of our financial performance and position. We also include a number of sections highlighting 'Our strategy in action' which draw out the key elements of our business model which is set out in the Strategic Review on pages 1 to 25 and show how the disclosures reflect this strategy.

Keeping it simple

Consolidated financial statements

We are required to present certain minimum information in the primary financial statements, which together set out the overview of the results of the business for the year and financial position at year end.

The consolidated income statement shows all revenue earned and costs incurred in the year, with the difference being the overall profit for the year.

The consolidated statement of comprehensive income records certain items as prescribed by the accounting rules. For us, the majority of the income or expense included here relates to movements in actuarial assumptions on pension schemes and the associated tax impact. These items are not part of profit for the year, yet are important to allow the reader to gain a more comprehensive picture of our performance as a whole.

The consolidated statement of financial position sets out all the Group's assets and liabilities at the year end, analysed between the net assets we have for use in the business and those held for sale. As a capital intensive business, we have significant amounts of physical assets and corresponding borrowings.

The consolidated statement of changes in equity shows the additions (where it came from) and reductions (where it went) to equity. For us, the main items included here are the profit earned and dividends paid in the year.

The consolidated cash flow statement shows how the cash balance has moved during the year. Cash inflows and outflows are presented to allow users to understand how they relate to the day to day operations of the business (Operating activities); the money that has been spent or earned on assets in the year, including acquisitions of physical assets or other businesses (Investing activities); and the cash raised from debt issues and other loan borrowings or repayments (Financing activities).

Notes

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

Statement of Directors' responsibilities

The Directors are responsible for preparing the Annual Report and Accounts, including the consolidated financial statements, and the Company financial statements and the Directors' Report and the Strategic Review, 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 profit of the Company on a consolidated basis for that period.

In preparing these 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 issued by the Internal Accounting Standards Board and IFRS 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 adequate 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 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 26, 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 issued by the IASB and 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
- to the best of their knowledge the Annual Report and Accounts 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

Andrew Agg
Director
24 June 2013

Independent Auditors' report

to the Members of National Grid Electricity Transmission plc

We have audited the consolidated and Company financial statements (the "financial statements") of National Grid Electricity Transmission plc for the year ended 31 March 2013, which comprise the basis of preparation, recent accounting developments, consolidated income statement, the consolidated statement of comprehensive income, the consolidated statement of financial position, the Company balance sheet, the consolidated statement of changes in equity, the consolidated cash flow statement, the accounting policies, the Company accounting policies, 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 consolidated 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 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 Statement of Directors' Responsibilities 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 and express an opinion on 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. In addition, we read all the financial and non-financial information in the Annual Report and Accounts to identify material inconsistencies with the audited financial statements. If we become aware of any apparent material misstatements or inconsistencies we consider the implications for our report.

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 2013 and of the 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; and
- the financial statements have been prepared in accordance with the requirements of the Companies Act 2006 and, as regards the consolidated 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 on 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 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.

Stephen Snook (Senior Statutory Auditor)
for and on behalf of PricewaterhouseCoopers LLP
Chartered Accountants and Statutory Auditors
Birmingham
25 June 2013

(a) The maintenance and integrity of the Company website is the responsibility of the Directors; the work carried out by the auditors does not involve consideration of these matters and, accordingly, the auditors accept no responsibility for any changes that may have occurred to the financial statements since they were initially presented on the website.
(b) Legislation in the United Kingdom governing the preparation and dissemination of financial statements may differ from legislation in other jurisdictions.

Basis of preparation

Accounting policies describe our approach to recognising and measuring transactions in the year. Accounting policies applicable across the financial statements are shown below. Accounting policies that are specific to a component of the financial statements have been incorporated into the note that provides additional information regarding that component. This section also shows areas of judgement and key sources of estimation uncertainty in these financial statements as well as new EU endorsed accounting standards, amendments and interpretations, whether these are effective in 2013 or later years. We explain how significant changes are expected to affect our performance.

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

These consolidated financial statements were approved for issue by the Board of Directors on 24 June 2013.

These consolidated financial statements have been prepared in accordance with International Accounting Standards (IAS) and International Financial Reporting Standards (IFRS) and related interpretations as issued by the IASB and as adopted by the EU. They are prepared on the basis of all IFRS accounting standards and interpretations that are mandatory for periods ending 31 March 2013 and in accordance with the Companies Act 2006 applicable to companies reporting under IFRS and Article 4 of the EU IAS Regulation. The 2012 comparative financial information has also been prepared on this basis.

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

The consolidated financial statements have been prepared on a going concern basis following the assessment made by the Directors as set out on page 28.

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 (see accounting policy C). Actual results could differ from these estimates.

A. 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 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.

B. Foreign currencies

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

Gains and losses arising on the retranslation of monetary assets and liabilities are included in the income statement, except where the adoption of hedge accounting requires inclusion in other comprehensive income - note 9.

C. Areas of judgement and key sources of estimation uncertainty

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

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

- The categorisation of certain items as exceptional items and remeasurements and the definition of adjusted earnings – note 3.
- Hedge accounting – note 9.

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

- Presentation formats. We use the nature of expense method for our income statement and total our statement

of financial position to net assets and total equity. In the income statement, we present subtotals of total operating profit, profit before tax and profit from continuing operations, together with additional subtotals excluding exceptional items, remeasurements and stranded cost recoveries. Exceptional items, remeasurements and stranded cost recoveries are presented separately on the face of the income statement.

- Customer contributions. Contributions received prior to 1 July 2009 towards capital expenditure are recorded as deferred income and amortised in line with the depreciation on the associated asset.
- Financial instruments. We normally opt to apply hedge accounting in most circumstances where this is permitted.

Key sources of estimation uncertainty that have 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 – notes 7 and 8.
- Estimation of liabilities for pensions – note 17.
- Valuation of financial instruments and derivatives – notes 9, 14 and 24.
- Revenue recognition and assessment of unbilled revenue – note 1.
- Recoverability of deferred tax assets – note 5.
- Environmental provisions – note 18.

Recent accounting developments

New IFRS accounting standards and interpretations adopted in 2012/13

During the year ended 31 March 2013, the Company has not adopted any new IFRS, IAS or amendments issued by the IASB, or interpretations issued by the IFRS Interpretations Committee, which have had a material impact on the Company's consolidated financial statements.

New IFRS accounting standards and interpretations not yet adopted

The Company enters into a significant number of transactions that fall within the scope of IFRS 9 on financial instruments. The IASB is completing IFRS 9 in phases and the Company is evaluating the impact of the standard as it develops. It is currently expected that the standard will be required to be adopted by the Company on 1 April 2015. We are currently assessing the likely impact of this standard on the Company's consolidated financial statements.

IFRS 10 on consolidated financial statements, IFRS 11 on joint arrangements, IFRS 12 on disclosures of interests in other entities and IFRS 13 on fair value measurements and consequent amendments to IAS 27 and IAS 28 were issued in May 2011. These standards are not expected to have a significant impact on the consolidated financial statements. The standards are required to be adopted by the Company on 1 April 2013.

The amended version of IAS 19 on employee benefits, issued in June 2011 and effective for periods beginning after 1 January 2013, requires net interest to be calculated on the net defined benefit asset/(liability) using the same discount rate used to measure the defined benefit obligation. Where the expected return on assets exceeds the discount rate, the adoption of the amended standard will result in a reduction in reported net income and an increase in other comprehensive income (OCI). The impact on the Company's financial statements for the period of initial application of the amended standard will depend upon reported pension assets and liabilities and the relationship between the expected return on assets and the discount rate at the date of adoption. If the amended standard had been adopted for the year ended 31 March 2013, net income would have been reduced by £11m and OCI increased by £11m.

The amendments to IAS 1 (Presentation of Financial Statements), issued in June 2011 and effective for periods beginning on or after 1 July 2012, require entities to group items presented in OCI based on whether they are potentially reclassifiable to profit or loss subsequently. It also requires tax associated with any items presented before tax to be shown separately for each of the two groups of OCI items. These amendments are presentational only and will not affect the results of the Group when adopted. Other standards and interpretations or amendments thereto which have been issued, but are not yet effective, are not expected to have a material impact on the Company's consolidated financial statements.

Consolidated income statement

for the years ended 31 March

	Notes	2013 £m	2013 £m	2012 £m	2012 £m
Revenue	1(a)		**3,111**		2,813
Operating costs	2		**(2,102)**		(1,948)
Operating profit					
Before exceptional items	1	**1,040**		870	
Exceptional items	3	**(31)**		(5)	
Total operating profit	1		**1,009**		865
Finance income	4		**99**		107
Finance costs					
Before exceptional items and remeasurements	4	**(327)**		(285)	
Exceptional items and remeasurements	3, 4	**38**		(41)	
Total finance costs	4		**(289)**		(326)
Profit before tax					
Before exceptional items and remeasurements		**812**		692	
Exceptional items and remeasurements	3	**7**		(46)	
Total profit before tax			**819**		646
Taxation					
Before exceptional items and remeasurements	5	**(197)**		(182)	
Exceptional items and remeasurements	3, 5	**36**		81	
Total taxation	5		**(161)**		(101)
Profit after tax					
Before exceptional items and remeasurements		**615**		510	
Exceptional items and remeasurements	3	**43**		35	
Profit for the year			**658**		545

The notes on pages 38 to 65 form part of the consolidated financial statements.

Consolidated statement of comprehensive income

for the years ended 31 March

	Notes	**2013 £m**	2012 £m
Profit for the year		**658**	545
Other comprehensive loss:			
Actuarial net losses	17	**(132)**	(121)
Deferred tax on actuarial net losses	5	**28**	26
Net losses in respect of cash flow hedges		**(3)**	(55)
Transferred to profit or loss on cash flow hedges		**43**	6
Deferred tax on cash flow hedges	5	**(10)**	11
Other comprehensive loss for the year		**(74)**	(133)
Total comprehensive income for the year		**584**	412

Consolidated statement of financial position

as at 31 March

	Notes	2013 £m	2012 £m
Non-current assets			
Intangible assets	7	**89**	72
Property, plant and equipment	8	**9,548**	8,465
Derivative financial assets	9	**409**	337
Total non-current assets		**10,046**	8,874
Current assets			
Inventories	10	**30**	28
Trade and other receivables	11	**239**	229
Financial and other investments	12	**917**	265
Derivative financial assets	9	**44**	20
Current tax asset		**2**	2
Cash and cash equivalents	13	**3**	-
Total current assets		**1,235**	544
Total assets		**11,281**	9,418
Current liabilities			
Borrowings	14	**(685)**	(749)
Derivative financial liabilities	9	**(118)**	(26)
Trade and other payables	15	**(812)**	(713)
Provisions	18	**(21)**	(11)
Total current liabilities		**(1,636)**	(1,499)
Non-current liabilities			
Borrowings	14	**(6,158)**	(4,679)
Derivative financial liabilities	9	**(331)**	(402)
Other non-current liabilities	16	**(284)**	(257)
Deferred tax liabilities	5	**(749)**	(746)
Pension obligations	17	**(620)**	(512)
Provisions	18	**(76)**	(83)
Total non-current liabilities		**(8,218)**	(6,679)
Total liabilities		**(9,854)**	(8,178)
Net assets		**1,427**	1,240
Equity			
Called up share capital	19	**44**	44
Retained earnings		**1,417**	1,260
Cash flow hedge reserve		**(34)**	(64)
Total equity		**1,427**	1,240

These consolidated financial statements set out on pages 38 to 65 were approved by the Board of Directors on 24 June 2013 and were signed on its behalf by:

Paul Whittaker Director

Andrew Agg Director

Consolidated statement of changes in equity

for the years ended 31 March

	Called up share capital £m	Retained earnings £m	Cash flow hedge reserve £m	Total equity £m
At 1 April 2011	44	1,006	(26)	1,024
Profit for the year	-	545	-	545
Total other comprehensive income/(loss) for the year	-	(95)	(38)	(133)
Total comprehensive income/(loss) for the year	-	450	(38)	412
Equity dividends	-	(200)	-	(200)
Share-based payment	-	3	-	3
Tax on share-based payment	-	1	-	1
At 31 March 2012	44	1,260	(64)	1,240
Profit for the year	-	658	-	658
Total other comprehensive income/(loss) for the year	-	(104)	30	(74)
Total comprehensive income/(loss) for the year	-	554	30	584
Equity dividends	-	(400)	-	(400)
Share-based payment	-	3	-	3
Tax on share-based payment	-	-	-	-
At 31 March 2013	**44**	**1,417**	**(34)**	**1,427**

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 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 cash flow hedge reserve on interest rate swap contracts will be continuously transferred to the income statement until the borrowings are repaid. The amount due to be released from reserves to the income statement next year is £3m, with the remainder due to be released with the same maturity profile as borrowings due after more than one year.

Consolidated cash flow statement

for the years ended 31 March

	Notes	**2013 £m**	2012 £m
Cash flows from operating activities			
Total operating profit	1	**1,009**	865
Adjustments for:			
Exceptional items	3	**31**	5
Depreciation and amortisation		**325**	276
Share-based payment charge		**3**	3
Changes in working capital		**2**	77
Changes in pension obligations		**(35)**	(81)
Changes in provisions		**(14)**	1
Cash flows relating to exceptional items		**(18)**	(11)
Cash flows generated from operations		**1,303**	1,135
Tax paid		**(100)**	(136)
Net cash inflow from operating activities		**1,203**	999
Cash flows from investing activities			
Purchases of intangible assets		**(29)**	(29)
Purchases of property, plant and equipment		**(1,232)**	(1,092)
Disposal of property, plant and equipment		**4**	7
Interest received		**3**	-
Net movement in short-term financial investments		**(652)**	(261)
Net cash flow used in investing activities		**(1,906)**	(1,375)
Cash flows from financing activities			
Proceeds from loans received		**1,867**	403
Repayment of loans		**(637)**	(77)
Net movements in short-term borrowings and derivatives		**52**	403
Interest paid		**(172)**	(149)
Dividends paid to shareholders		**(400)**	(200)
Net cash flow generated from/(used in) financing activities		**710**	380
Net increase/(decrease) in cash and cash equivalents	20(a)	**7**	4
Cash and cash equivalents at the start of the year (i)		**(4)**	(8)
Net cash and cash equivalents at the end of the year (i)	13	**3**	(4)

(i) Net of bank overdrafts of £nil (2012: £4m).

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

1. Segmental analysis

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

Our strategy in action
We work with our regulators to obtain robust regulatory agreements that balance the risks we face with the opportunity to deliver reasonable returns for our investors. Our regulated business earns revenue for the transmission services it has provided during the year. The revenue recognised may differ from the revenue allowed under our regulatory agreements and differences are adjusted against future prices.

Revenue primarily represents the sales value derived from the transmission of electricity, together with the sales value derived from the provision of other services to customers during the year. It excludes value added (sales) tax and intra-group sales.

Revenue includes an assessment of unbilled energy and transportation services supplied to customers between the date of the last meter reading and the year end, but not invoiced at year end. This is estimated based on historical consumption and weather patterns.

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, no liability is recognised, as such an adjustment relates to the provision of future services. Similarly no asset is recognised where a regulatory agreement permits adjustments to be made to future prices in respect of an under-recovery.

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

Electricity Transmission	High-voltage electricity transmission networks in the UK

Other activities relate to other commercial operations not included within the above segment and corporate activities.

All of the Company's sales and operations take place within the UK.

(a) Revenue

	2013 Total sales £m	2012 Total sales £m
Operating segment		
Electricity Transmission	**3,110**	2,811
Other activities	**1**	2
	3,111	2,813

All sales are to third parties.
In the UK, there was a cumulative over-recovery of £5m* as at 31 March 2013 (2012: £24m* under-recovery).
*Unaudited

Analysis of revenue by major customer:	**2013 £m**	2012 £m
Customer A	**566**	440
Customer B	**438**	451
Customer C	**406**	290
Customer D	**372**	329
Customer E	**296**	328

Revenue was generated from the Electricity Transmission business.

1. Segmental analysis continued

(b) Operating profit/(loss)

	Before exceptional items		After exceptional items	
	2013	2012	**2013**	2012
	£m	£m	**£m**	£m
Operating segment				
Electricity Transmission	**1,049**	876	**1,018**	871
Other activities	**(9)**	(6)	**(9)**	(6)
	1,040	870	**1,009**	865

(c) Capital expenditure and depreciation

	Capital expenditure		Depreciation and amortisation	
	2013	2012	**2013**	2012
	£m	£m	**£m**	£m
Operating segment				
Electricity Transmission	**1,429**	1,154	**325**	282
Other activities	**1**	-	**-**	-
	1,430	1,154	**325**	282
By asset type				
Property, plant and equipment	**1,401**	1,125	**314**	272
Other non-current intangible assets	**29**	29	**11**	10
	1,430	1,154	**325**	282

2. Operating costs

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

	Before exceptional items		Exceptional items		Total	
	2013	2012	**2013**	2012	**2013**	2012 *
	£m	£m	**£m**	£m	**£m**	£m
Depreciation and amortisation	**325**	282	**-**	-	**325**	282
Payroll costs	**104**	121	**16**	3	**120**	124
Rates	**98**	98	**-**	-	**98**	98
Balancing Service Incentive Scheme	**805**	818	**-**	-	**805**	818
Payments to other UK network owners	**487**	407	**-**	-	**487**	407
Other	**252**	217	**15**	2	**267**	219
	2,071	1,943	**31**	5	**2,102**	1,948

(a) Payroll costs

	2013	2012
	£m	£m
Wages and salaries	**152**	137
Social security costs	**16**	14
Pension costs (note 17)	**33**	28
Share-based payment	**3**	3
Severance costs (excluding pension costs)	**8**	3
	212	185
Less: payroll costs capitalised	**(92)**	(61)
	120	124

2. Operating costs continued

(b) Number of employees, including Directors

	31 March 2013 Number	Monthly Average 2013 Number	Monthly Average 2012 Number
UK	**3,229**	**3,125**	2,871

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

(c) Key management compensation

	2013 £m	2012 £m
Salaries and short-term employee benefits	**3**	3
Post-retirement benefits	**1**	2
Share-based payment	**2**	1
	6	6

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

(d) Directors' emoluments

The aggregate amount of emoluments paid (excluding social security, pensions and share-based payment) to Directors of the company in respect of qualifying services for 2013 was £1,472,572 (2012: £1,185,681).

Five of the directors exercised share options during 2013 (2012: Four of the directors exercised share options).

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 2013, retirement benefits were accruing to five Directors under a defined benefit scheme (2012: four directors, under a defined benefit scheme).

The aggregate emoluments for the highest paid Director were £759,432 for 2013 (2012: £760,780); and total accrued annual pension at 31 March 2013 for the highest paid Director was £191,418 (2012: £175,339).

The aggregate amount of loss of office payments to Directors for 2013 was £nil (2012: £nil).

(e) Auditors' remuneration

	2013 £m	2012 £m
Audit services		
Audit of the parent Company's individual and consolidated financial statements	**0.2**	0.2
Other services supplied		
Fees payable to the Company's auditors for audit related assurance services	**0.1**	0.1

Fees payable to the Company's auditors for audit related assurance services represent fees payable for services in relation to engagements which are required to be carried out by the auditors. In particular this includes fees for audit reports on regulatory returns.

3. Exceptional items and remeasurements

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

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

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, integration of acquired businesses, gains or losses on disposals of businesses or investments and debt redemption costs as a consequence of transactions such as significant disposals or issues of equity.

Costs arising from restructuring programmes include redundancy costs. Redundancy costs are charged to the income statement in the year in which a 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 commodity contracts and of derivative financial instruments to the extent that hedge accounting is not achieved or is not effective. These fair values increase or decrease because of changes in commodity and financial indices and prices over which we have no control.

	2013 £m	2012 £m
Included within operating profit:		
Exceptional items:		
Restructuring costs (i)	**(31)**	(5)
	(31)	(5)
Included within finance costs:		
Remeasurements:		
Net gains/(losses) on derivative financial instruments (ii)	**38**	(41)
	38	(41)
Total included within profit before taxation	**7**	(46)
Included within taxation:		
Exceptional credit arising on items not included in profit before tax:		
Deferred tax credit arising on the reduction in UK corporation tax rate (iii)	**37**	69
Tax on exceptional items	**8**	1
Tax on remeasurements (ii)	**(9)**	11
	36	81
Total exceptional items and remeasurements after taxation	**43**	35
Analysis of total exceptional items and remeasurements after tax:		
Total exceptional items after taxation	**14**	65
Total remeasurements after taxation	**29**	(30)
Total	**43**	35

(i) Restructuring costs for year include: costs related to the restructuring of our UK operations of £26m in preparedness for delivering RIIO and transformation-related initiatives of £5m. For the year ended 31 March 2012, restructuring costs included costs relating to transformation-related initiatives of £5m.

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

(iii) The exceptional tax credit arises from a reduction in the UK corporation tax rate from 24% to 23% (2012: from 26% to 24%) included and enacted in the Finance Act 2012 and applicable from 1 April 2013. These reductions have resulted in a decrease in deferred tax liabilities.

4. Finance income and costs

Keeping it simple

This note details the interest income generated on our financial assets and the interest expense incurred on financial liabilities. It also includes the expected return on pension assets, which is offset by the interest payable on pension obligations. In reporting business performance, we adjust net financing costs to exclude any net gains or losses on derivative financial instruments included in remeasurements.

	2013 £m	2012 £m
Finance income		
Expected return on pension plan assets	**96**	107
Interest income on financial instruments:		
Bank deposits and other financial assets	**3**	-
Finance income	**99**	107
Finance costs		
Interest on pension plan obligations	**(107)**	(112)
Interest expense on finance liabilities held at amortised cost:		
Bank loans and overdrafts	**(7)**	(5)
Other borrowings	**(278)**	(275)
Derivatives	**(25)**	21
Unwinding of discount on provisions	**(4)**	(4)
Other interest	**(1)**	(3)
Less: interest capitalised (i)	**95**	93
Finance costs before exceptional items and remeasurements	**(327)**	(285)
Remeasurements:		
Net gains/(losses) on derivative financial instruments included in remeasurements (ii):		
Ineffectiveness on derivatives designated as:		
Fair value hedges (iii)	**1**	3
Cash flow hedges	**(5)**	5
Derivatives not designated as hedges or ineligible for hedge accounting	**42**	(49)
	38	(41)
Remeasurements included within finance costs	**38**	(41)
Finance costs	**(289)**	(326)
Net finance costs	**(190)**	(219)

(i) Interest on funding attributable to assets in the course of construction was capitalised during the year at a rate of 4.8% (2012: 5.7%).

(ii) Includes a net foreign exchange loss on financing activities of £22m (2012: £34m gain). These amounts are offset by foreign exchange gains and losses on derivative financial instruments measured at fair value.

(iii) Includes a net gain on instruments designated as fair value hedges of £25m (2012: £74m gain), offset by a net loss of £24m (2012: £71m loss) arising from the fair value adjustments to the carrying value of debt.

5. Taxation

Keeping it simple

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

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

Current tax assets and liabilities are measured at the amounts expected to be recovered from or paid to the taxation authorities. The tax rates and tax laws used to compute the amounts are those that are enacted or substantively enacted by the reporting date.
The calculation of the Group's total tax charge involves a degree of estimation and judgement, and management periodically evaluates positions taken in tax returns with respect to situations in which applicable tax regulation is subject to interpretation and establishes provisions where appropriate on the basis of amounts expected to be paid to the tax authorities.

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

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

Deferred tax liabilities are recognised on taxable temporary differences arising on investments in subsidiaries and jointly controlled entities except where the 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 reporting date.

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

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

Tax charged/(credited) to the income statement

	2013 £m	2012 £m
Tax before exceptional items and remeasurements	**197**	182
Exceptional tax on items not included in profit before tax (note 3)	**(37)**	(69)
Tax on other exceptional items and remeasurements	**1**	(12)
Tax on total exceptional items and remeasurements (note 3)	**(36)**	(81)
Total tax charge	**161**	101

Taxation as a percentage of profit before tax

	2013 %	2012 %
Before exceptional items and remeasurements	**24.3**	26.3
After exceptional items and remeasurements	**19.7**	15.6

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

	2013 £m	2012 £m
Current tax		
UK Corporation tax at 24% (2012: 26%)	**143**	78
UK Corporation tax adjustment in respect of prior years	**(3)**	1
Total current tax	**140**	79
Deferred tax		
UK Deferred tax	**20**	25
UK Deferred tax adjustment in respect of prior years	**1**	(3)
Total deferred tax	**21**	22
Total tax charge	**161**	101

5. Taxation continued

Tax (credited)/charged to other comprehensive income and equity

	2013 £m	2012 £m
Corporation tax		
Share-based payment	**-**	(1)
Deferred tax		
Cash flow hedges	**10**	(11)
Actuarial (losses)/gains	**(28)**	(26)
	(18)	(38)
Total tax recognised in the statement of other comprehensive income	**(18)**	(37)
Total tax relating to share-based payment recognised directly in equity	**-**	(1)
	(18)	(38)

The tax charge for the year after exceptional items and remeasurements is lower (2012: lower) than the standard rate of corporation tax in the UK of 24% (2012: 26%):

	Before exceptional items and remeasure-ments 2013 £m	**After exceptional items and remeasure-ments 2013 £m**	Before exceptional items and remeasure-ments 2012 £m	After exceptional items and remeasure-ments 2012 £m
Profit before tax				
Before exceptional items and remeasurements	**812**	**812**	692	692
Exceptional items and remeasurements	**-**	**7**	-	(46)
Profit before tax	**812**	**819**	692	646
Profit before tax multiplied by UK corporation tax rate of 24% (2012: 26%)	**195**	**197**	180	168
Effects of:				
Adjustments in respect of prior years	**(2)**	**(2)**	(2)	(2)
Expenses not deductible for tax purposes	**5**	**5**	5	5
Non-taxable income	**(2)**	**(3)**	-	-
Impact of share-based payment	**1**	**1**	(1)	(1)
Deferred tax impact of change in UK tax rate	**-**	**(37)**	-	(69)
Total tax charge	**197**	**161**	182	101
	%	**%**	%	%
Effective tax rate	**24.3**	**19.7**	26.3	15.6

Factors that may affect future tax charges

A reduction in the UK corporation tax rate to 21% from 1 April 2014 was announced in the Autumn Statement and a further reduction to 20% from April 2015 was announced in the 2013 UK Budget Report. These reductions have not been substantively enacted and have not been reflected in these financial statements. The Group’s tax charge will reflect these reductions in the UK corporation tax rate once the changes have been enacted.

5. Taxation continued

Taxation included within the statement of financial position
The following are the major deferred tax assets and liabilities recognised, and the movements thereon, during the current and prior reporting periods:

Deferred tax (assets)/liabilities

	Accelerated tax depreciation £m	Share-based payment £m	Pensions £m	Financial instruments £m	Other net temporary differences £m	Total £m
Deferred tax assets at 31 March 2011	-	(6)	(121)	(9)	(6)	(142)
Deferred tax liabilities at 31 March 2011	903	-	-	-	-	903
At 1 April 2011	903	(6)	(121)	(9)	(6)	761
(Credited)/charged to income statement	(7)	-	24	-	5	22
(Credited) to other comprehensive income	-	-	(26)	(11)	-	(37)
At 31 March 2012	896	(6)	(123)	(20)	(1)	746
Deferred tax assets at 31 March 2012	-	(6)	(123)	(20)	(2)	(151)
Deferred tax liabilities at 31 March 2012	896	-	-	-	1	897
At 31 March 2012	896	(6)	(123)	(20)	(1)	746
Charged/(credited) to income statement	14	1	8	-	(2)	21
(Credited)/charged to other comprehensive income	-	-	(28)	10	-	(18)
At 31 March 2013	**910**	**(5)**	**(143)**	**(10)**	**(3)**	**749**
Deferred tax assets at 31 March 2013	-	(5)	(143)	(10)	(4)	(162)
Deferred tax liabilities at 31 March 2013	910	-	-	-	1	911
At 31 March 2013	**910**	**(5)**	**(143)**	**(10)**	**(3)**	**749**

Deferred tax assets and liabilities are only offset where there is a legally enforceable right of offset and there is intention to settle the balances net. The deferred tax balances (after offset) for statement of financial position purposes consist solely of deferred tax liabilities of £749m (2012: £746m).

At the balance sheet date there were no material current deferred tax assets or liabilities (2012: £nil).

6. Dividends

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

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

The following table shows the dividends paid to equity shareholders:

	2013		2012	
	pence (per ordinary share)	**£m**	pence (per ordinary share)	£m
Ordinary dividends				
Interim dividend for the year ended 31 March 2013	**91.47**	**400**	-	-
Interim dividend for the year ended 31 March 2012	**-**	**-**	45.74	200

7. Intangible assets

Keeping it simple

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

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

Other intangible assets are tested for impairment only if there is some indication that the carrying value of the assets may have been impaired. Impairments of assets are calculated as the difference between the carrying value of the asset and the recoverable amount, if lower. Where such an asset does not generate cash flows that are independent from other assets, the recoverable amount of the cash-generating unit to which that asset belongs is estimated.

Impairments are recognised in the income statement and are disclosed separately.

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

Internally generated intangible assets, such as software, are recognised only if: an asset is created that can be identified; it is probable that the asset created will generate future economic benefits; and 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	up to 8

	Software £m
Cost at 1 April 2011	191
Additions	29
Disposals	(53)
Reclassifications between categories (i)	3
Cost at 31 March 2012	170
Additions	29
Disposals	-
Reclassifications between categories (i)	(1)
Cost at 31 March 2013	198
Accumulated amortisation at 1 April 2011	(141)
Amortisation charge for the year	(10)
Disposals	53
Accumulated amortisation at 31 March 2012	(98)
Amortisation charge for the year	(11)
Disposals	-
Accumulated amortisation at 31 March 2013	(109)
Net book value at 31 March 2013	**89**
Net book value at 31 March 2012	72

(i) Reclassifications represents amounts transferred to property, plant and equipment (see note 8).

8. Property, plant and equipment

Keeping it simple

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

Our strategy in action

We operate an electricity transmission business and therefore have a significant physical asset base. We continue to invest in our networks to maintain reliability, create new customer connections and ensure our networks have the flexibility and resilience necessary to meet future challenges. Our business plan envisages these additional investments will be funded through a mixture of cash generated from operations and the issue of new debt.

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

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

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

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 useful economic 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. No depreciation is provided on freehold land or assets in the course of construction.

Other items of property, plant and equipment are depreciated, on a straight-line basis, at rates estimated to write off their book values over their estimated useful economic lives. In assessing estimated useful economic lives, consideration is given to any contractual arrangements and operational requirements relating to particular assets. The assessments of estimated useful economic lives and residual values of assets are performed annually. Unless otherwise determined by operational requirements, the depreciation periods for the principal categories of property, plant and equipment are, in general, as shown in the table below:

Depreciation periods	Years
Freehold and leasehold buildings	up to 50
Plant and Machinery	
- Electricity Transmission plant	15-60
Motor vehicles and office equipment	up to 7

Gains and losses on disposals are determined by comparing the proceeds with the carrying amount and are, depending on their magnitude, recognised as an exceptional item within operating profit in the income statement.

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

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

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

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

	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 2011	327	8,805	1,737	103	10,972
Additions	21	72	1,028	4	1,125
Disposals	(2)	(84)	-	(27)	(113)
Reclassifications between categories	92	804	(906)	7	(3)
Cost at 31 March 2012	438	9,597	1,859	87	11,981
Additions	31	55	1,311	4	1,401
Disposals	-	(99)	(5)	(13)	(117)
Reclassifications between categories	46	556	(626)	25	1
Cost at 31 March 2013	515	10,109	2,539	103	13,266
Accumulated depreciation at 1 April 2011	(43)	(3,231)	-	(82)	(3,356)
Depreciation charge for the year	(8)	(256)	-	(8)	(272)
Disposals	1	84	-	27	112
Reclassifications between categories	(1)	4	-	(3)	-
Accumulated depreciation at 31 March 2012	(51)	(3,399)	-	(66)	(3,516)
Depreciation charge for the year	(13)	(291)	-	(10)	(314)
Disposals	-	99	-	13	112
Reclassifications between categories	(1)	1	-	-	-
Accumulated depreciation at 31 March 2013	(65)	(3,590)	-	(63)	(3,718)
Net book value at 31 March 2013	**450**	**6,519**	**2,539**	**40**	**9,548**
Net book value at 31 March 2012	387	6,198	1,859	21	8,465

(i) Reclassifications represents amounts transferred between categories and to intangible assets (see note 7).

8. Property, plant and equipment continued

	2013 £m	2012 £m
Information in relation to property, plant and equipment:		
Capitalised interest included within cost	**925**	831
Contributions to cost of property, plant and equipment included within:		
Trade and other payables	**7**	7
Non-current liabilities	**245**	222

9. Derivative financial instruments

Keeping it simple
A derivative is a financial instrument used to manage the risk associated with fluctuations in the value of certain assets or liabilities. In accordance with Board approved policies, we use derivatives to manage our exposure to fluctuations in interest rate and foreign exchange rate on borrowings and other contractual cash flows.
Derivative financial instruments are initially recognised at fair value and subsequently remeasured at fair value at each reporting date. Changes in fair values are recorded in either the income statement or other comprehensive income depending on the applicable accounting standards.
Analysis of these derivatives and the various methods used to calculate their respective fair values is detailed below and in note 24.

Derivatives are financial instruments that derive their value from the price of an underlying item such as interest rates, foreign exchange, credit spreads, commodities, equity or other indices. Derivatives enable their users to manage their exposure to these market or credit risks. We use derivatives to manage the interest rate and foreign exchange risks from our financing portfolio and this enables the optimisation of the overall cost of accessing debt capital markets.

Derivative financial instruments are recorded at fair value through profit or loss. Where the 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 reported net 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 the changes in fair value are included in the income statement in the period they arise.

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

Where possible, derivatives 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, cash flow hedges or net investment hedges.

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

Fair value hedges
Fair value hedges principally consist of interest rate and cross-currency swaps that are used to protect against changes in the fair value of fixed-rate, long-term financial instruments due to movements in market interest rates. For qualifying fair value hedges, all changes in the fair value of the derivative and changes in the fair value of the item in relation to the risk being hedged are 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.

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

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

When a forecast transaction is no longer expected to occur, the cumulative gain or loss that was reported in equity is transferred to the income statement.

Where a non-financial asset or a non-financial liability results from a forecasted transaction or firm commitment being hedged, the amounts deferred in equity are included in the initial measurement of that non-monetary asset or liability.

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

9. Derivative financial instruments continued

Discontinuation of hedge accounting

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

Embedded derivatives

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. 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.

Our use of derivatives may entail a derivative transaction qualifying for one or more hedge type designations under IAS 39. The fair value amounts by designated hedge type can be analysed as follows:

	2013			2012		
	Assets £m	**Liabilities £m**	**Total £m**	Assets £m	Liabilities £m	Total £m
Fair value hedges						
Interest rate swaps	**114**	**-**	**114**	97	-	97
Cross-currency interest rate swaps	**63**	**-**	**63**	63	-	63
	177	**-**	**177**	160	-	160
Cash flow hedges						
Interest rate swaps	**-**	**(74)**	**(74)**	-	(66)	(66)
Cross-currency interest rate swaps	**17**	**-**	**17**	9	-	9
Foreign exchange forward contracts	**3**	**(2)**	**1**	-	(5)	(5)
Inflation linked swaps	**4**	**(6)**	**(2)**	2	(5)	(3)
	24	**(82)**	**(58)**	11	(76)	(65)
Derivatives not in a formal hedge relationship						
Interest rate swaps	**245**	**(253)**	**(8)**	181	(191)	(10)
Forward rate agreements	**-**	**(2)**	**(2)**	-	(2)	(2)
Inflation linked swaps	**7**	**(112)**	**(105)**	5	(159)	(154)
	252	**(367)**	**(115)**	186	(352)	(166)
Total	**453**	**(449)**	**4**	357	(428)	(71)

The maturity of derivative financial instruments is as follows:

	2013			2012		
	Assets £m	**Liabilities £m**	**Total £m**	Assets £m	Liabilities £m	Total £m
Current	**44**	**(118)**	**(74)**	20	(26)	(6)
In 1 - 2 years	**1**	**-**	**1**	18	(20)	(2)
In 2 - 3 years	**47**	**(1)**	**46**	-	(1)	(1)
In 3 - 4 years	**16**	**(54)**	**(38)**	57	(1)	56
In 4 - 5 years	**7**	**(1)**	**6**	14	(53)	(39)
More than 5 years	**338**	**(275)**	**63**	248	(327)	(79)
Non-current	**409**	**(331)**	**78**	337	(402)	(65)
Total	**453**	**(449)**	**4**	357	(428)	(71)

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

	2013 £m	2012 £m
Interest rate swaps	**(4,159)**	(3,842)
Cross-currency interest rate swaps	**(1,846)**	(631)
Foreign exchange forward contracts	**(577)**	(596)
Forward rate agreements	**(1,158)**	(1,769)
Inflation linked swaps	**(630)**	(627)
Total	**(8,370)**	(7,465)

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

10. Inventories

Keeping it simple
Inventories represent assets that we intend to use in order to generate revenue in future periods, either by selling the asset itself or by using it to fulfil a service to a customer (consumables) or to maintain our network.
Inventories, which comprise raw materials, spares and consumables, are stated at cost, calculated on a weighted average basis, less provision for damage and obsolescence.

Cost comprises direct materials and those costs that have been incurred in bringing the inventories to their present location and condition.

	2013 £m	2012 £m
Raw materials, spares and consumables	**30**	28

The above table includes a £15m provision for obsolescence against raw materials and consumables at 31 March 2013 (2012: £14m).

11. Trade and other receivables

Keeping it simple
Trade and other receivables are amounts which are due from our customers for services we have provided. Other receivables also include prepayments made by us, for example, property lease rentals paid in advance.
Trade, loan and other receivables are initially recognised at fair value and subsequently measured at amortised cost, less any appropriate allowances for estimated irrecoverable amounts. A provision is established for irrecoverable amounts when there is objective evidence that amounts due under the original payment terms will not be collected.

	2013 £m	2012 £m
Trade receivables	**16**	14
Amounts owed by fellow subsidiaries	**9**	20
Prepayments and accrued income	**208**	191
Other receivables	**6**	4
	239	229

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. All other receivables are recorded at amortised cost. The provision as at 31 March 2013 £1m (2011/12: £2m).

12. Financial and other investments

Keeping it simple
Financial investments and other investments includes two main categories. Assets that are classified as available-for-sale typically represent investments in short-term money funds and quoted investments in equities or bonds of other companies. The second category is loans and receivables which includes cash balances that cannot be readily used in operations, principally collateral pledged for certain borrowings and restricted cash balances relating to our UK pension schemes.

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.

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

Available-for-sale financial investments are recognised at fair value plus, directly related incremental transaction costs, and are subsequently carried at fair value in the statement of financial position. Changes in the fair value of available-for-sale investments are recognised directly in 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 is recognised using the effective interest method and taken through interest income in the income statement.
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 that are consistent with techniques commonly used by the relevant market. The techniques use observable market data.

	2013 £m	2012 £m
Current		
Loans and receivables - amounts due from fellow subsidiaries	**8**	34
Loans and receivables - restricted cash balances (i)	**228**	227
Available-for-sale investments	**681**	4
Total financial and other investments	**917**	265

(i) Comprises collateral placed with counterparties with whom we have entered into a credit support annex to the ISDA Master Agreement £219m (2012: £224m) and secured bank accounts with charges in favour of the UK pension schemes Trustees of £9m (2012: £3m).

Available-for-sale investments are recorded at fair value. Due to their short maturities, the carrying value of loans and receivables approximates their fair value.

13. Cash and cash equivalents

Keeping it simple

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

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

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

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

Net cash and cash equivalents held in currencies other than sterling have been converted into sterling at year-end exchange rates. For further information on currency exposures, refer to note 24(a)(i).

	2013 **£m**	2012 £m
Cash at bank and short-term deposits	3	-
Cash and cash equivalents excluding bank overdrafts	**3**	-
Bank overdrafts	**-**	(4)
Net cash and cash equivalents	**3**	(4)

The carrying amounts of net cash and cash equivalents approximate to their fair value.

14. Borrowings

Keeping it simple

We borrow money primarily in the form of bonds and bank loans. These are for a fixed term and may have fixed or floating interest rates. As indicated in note 9, we use derivatives to manage risks associated with interest rates and foreign exchange.

Our strategy in action

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

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

	2013 **£m**	2012 £m
Current		
Bank overdrafts	**-**	4
Bank loans	**84**	244
Bonds	**579**	43
Borrowings from fellow subsidiaries	**22**	458
	685	749
Non-current		
Bank loans	**404**	300
Bonds	**5,458**	4,092
Borrowings from fellow subsidiaries	**296**	287
	6,158	4,679
Total borrowings	**6,843**	5,428

Total borrowings are repayable as follows:	**2013** **£m**	2012 £m
Less than 1 year	**685**	749
In 1 - 2 years	**-**	510
In 2 - 3 years	**158**	-
In 3 - 4 years	**200**	170
In 4 - 5 years	**625**	200
More than 5 years other than by instalments	**5,175**	3,799
	6,843	5,428

The fair value of borrowings at 31 March 2013 was £7,778m (2012: £6,030m). Market values, where available, have been used to determine fair value. 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 2013 was £6,610m (2012: £5,248m).

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 £83m (2012: £44m) in respect of cash received under collateral agreements.

At 31 March 2013, we had committed credit facilities of £715m (2012: £715m) of which £715m was undrawn (2012: £715m undrawn). Subsequent to the year end these facilities were re-negotiated to £820m for a further five years. All of the unused facilities at 31 March 2013 and at 31 March 2012 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.

15. Trade and other payables

Keeping it simple

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

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

	2013 £m	2012 £m
Trade payables	**612**	466
Amounts owed to fellow subsidiaries	**86**	53
Deferred income	**64**	155
Social security and other taxes	**32**	18
Other payables	**18**	21
	812	713

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.

16. Other non-current liabilities

Keeping it simple

Other non-current liabilities includes deferred income which will not be recognised as income until after 31 March 2014. It also includes payables that are not due until after that date.

	2013 £m	2012 £m
Deferred income	**270**	247
Other payables	**14**	10
	284	257

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

17. Pensions

Keeping it simple

Substantially all of National Grid Electricity Transmission's employees are members of the National Grid Electricity Group of the Electricity Supply Pension Scheme, which is a defined benefit scheme or of the defined contribution section of the National Grid UK Pension Scheme. The fair value of plan assets and present value of defined benefit obligations are updated annually. For further details of the National Grid Electricity Group of the Electricity Supply Pension Scheme terms and the actuarial assumptions used to value the associated assets and obligations, see note 23.

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

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

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

The cost of providing benefits in a defined benefit scheme is determined using the projected unit method, with actuarial valuations being carried out at each reporting date.

The Group's obligation in respect of the defined benefit pension scheme is calculated separately by estimating the amount of future benefit that employees have earned for their pensionable service in the current and prior periods.

That benefit is discounted to determine its present value and the fair value of scheme assets and any unrecognised past service cost is then deducted. The discount rate used is the yield at the valuation date on high quality corporate bonds.

The Group takes advice from independent actuaries relating to the appropriateness of the assumptions which include life expectancy of members, expected salary and pension increases, inflation and the return on scheme assets. We note that comparatively small changes in the assumptions used may have a significant effect on the income statement and statement of financial position.

The liabilities of the defined benefit scheme are measured by discounting the best estimate of future cash flows to be paid using the projected unit method. This method is an accrued benefits valuation method that makes allowance for projected earnings. These calculations are performed by a qualified actuary.

Actuarial gains and losses are recognised in full in the period in which they occur in the statement of other comprehensive income.

17. Pensions continued

Amounts recognised in the income statement and statement of other comprehensive income:

	2013 £m	2012 £m
Included within payroll costs		
Defined contribution scheme costs	**7**	5
Defined benefit scheme costs:		
Current service cost	**29**	26
Contributions from other employers	**(7)**	(5)
Curtailment gains on redundancies	**(2)**	(1)
Cost of contractual termination on redundancies	**6**	3
	33	28
Included within finance income and costs		
Interest cost	**107**	112
Expected return on plan assets	**(96)**	(107)
	11	5
Included within other comprehensive income		
Actuarial loss during the year	**(132)**	(121)
Cumulative actuarial loss	**(445)**	(313)

Amounts recognised in the statement of financial position

	2013 £m	2012 £m
Present value of funded obligations	**(2,529)**	(2,223)
Fair value of plan assets	**1,943**	1,739
	(586)	(484)
Present value of unfunded obligations	**(34)**	(28)
Net liability	**(620)**	(512)

	2013 £m	2012 £m
Changes in the present value of the defined benefit obligations (including unfunded obligations)		
Opening defined benefit obligations	**(2,251)**	(2,065)
Current service cost	**(29)**	(26)
Interest cost	**(107)**	(112)
Actuarial losses	**(266)**	(138)
Net increase in liabilities from redundancies	**(4)**	(2)
Employee contributions	**(2)**	(2)
Benefits paid	**96**	93
Net transfers	**-**	1
Closing defined benefit obligation	**(2,563)**	(2,251)
Changes in the fair value of plan assets		
Opening fair value of plan assets	**1,739**	1,598
Expected return on plan assets	**96**	107
Actuarial gains	**134**	17
Employer contributions	**68**	109
Employee contributions	**2**	2
Benefits paid	**(96)**	(93)
Net transfers	**-**	(1)
Closing fair value of plan assets	**1,943**	1,739
Actual return on plan assets	**230**	124
Expected contributions to plans in the following year	**65**	65

18. Provisions

Keeping it simple

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

The main estimates relate to environmental costs for various sites we own or have owned which require restoration or remediation and other provisions, including lease contracts we have entered into that are now unprofitable.

Our strategy in action

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

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

Provision is made for environmental costs, based on future estimated expenditures, discounted to present values. An initial estimate of environmental costs attributable to property, plant and equipment is recorded as part of the original cost of the related property, plant and Changes in the provision arising from revised estimates or discount rates or changes in the expected timing of expenditures that relate to property, plant and equipment are recorded as adjustments to their carrying value and depreciated prospectively over their remaining estimated useful economic lives; otherwise such changes are recognised in the income statement.

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

	Environmental £m	Other £m	Total provisions £m
At 1 April 2011	73	23	96
Additions	-	3	3
Utilised	(1)	(4)	(5)
Unwinding of discount	4	-	4
Unused amounts reversed	-	(4)	(4)
At 31 March 2012	76	18	94
Additions	4	17	21
Utilised	(2)	(7)	(9)
Unwinding of discount	4	-	4
Unused amounts reversed	(11)	(2)	(13)
At 31 March 2013	**71**	**26**	**97**

	2013 £m	2012 £m
Current	**21**	11
Non-current	**76**	83
	97	94

Environmental provision

The environmental provision is calculated on an discounted basis and represents the estimated environmental restoration and remediation costs relating to a number of sites owned and managed by the Company. Cash flows are expected to be incurred between 2013 and 2060. The undiscounted amount is £110m (2012: £124m), and the real discount rate is 2.0%.

A number of uncertainties affect the calculation of the provision, including the impact of regulation, the accuracy of the site surveys, unexpected contaminants, transportation costs, the impact of alternative technologies and changes in the discount rate. The provision incorporates our best estimate of the financial effect of these uncertainties, but future material changes in any of the assumptions could materially impact on the calculation of the provision and hence the income statement.

Other provisions

Other provisions include employer liability claims of £7m (2012: £8m). In accordance with insurance industry practice, these estimates are based on experience from previous years and there is therefore no identifiable payment date.

The remainder of the provision relates to restructuring, business reorganisation costs and the majority is expected to be utilised during 2014.

19. Share capital

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

	Number of shares millions	£m
At 31 March 2012 and 2013 - ordinary shares of 10p each		
Allotted, called-up and fully paid	437	44

20. Net Debt

Keeping it simple
Net debt represents the amount of cash and financial investments held, less borrowings, overdrafts and related derivatives.
The movement in cash and cash equivalents is reconciled to movements in net debt.

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

	2013 £m	2012 £m
Increase in cash and cash equivalents	**7**	4
Increase in financial investments	**652**	261
(Increase) in borrowings and related derivatives	**(1,282)**	(729)
Net interest paid on the components of net debt	**169**	149
Change in net debt resulting from cash flows	**(454)**	(315)
Changes in fair value of financial assets and liabilities and exchange movements	**36**	(90)
Net interest charge on the components of net debt	**(307)**	(259)
Other non-cash movements*	**40**	-
Movement in net debt (net of related derivative financial instruments) in the year	**(685)**	(664)
Net debt (net of related derivative financial instruments) at start of year	**(5,234)**	(4,570)
Net debt (net of related derivative financial instruments) at end of year	**(5,919)**	(5,234)

(b) Analysis of changes in net debt

	Cash and cash equivalents £m	Bank overdrafts £m	**Net cash and cash equivalents £m**	Financial investments £m	Borrowings £m	Derivatives £m	**Total £m**
At 1 April 2011	-	(8)	**(8)**	4	(4,658)	92	**(4,570)**
Cash flow	-	4	**4**	261	(445)	(135)	**(315)**
Fair value gains and losses and exchange movements	-	-	**-**	-	(41)	(49)	**(90)**
Interest charges	-	-	**-**	-	(280)	21	**(259)**
At 31 March 2012	-	(4)	**(4)**	265	(5,424)	(71)	**(5,234)**
Cash flow	3	4	**7**	649	(1,085)	(25)	**(454)**
Fair value gains and losses and exchange movements	-	-	**-**	-	(49)	85	**36**
Interest charges	-	-	**-**	3	(285)	(25)	**(307)**
Other non-cash movements	-	-	**-**	-	-	40	**40**
At 31 March 2013	3	-	**3**	917	(6,843)	4	**(5,919)**
Balances at 31 March 2013 comprise:							
Non-current assets	-	-	**-**	-	-	409	**409**
Current assets	3	-	**3**	917	-	44	**964**
Current liabilities	-	-	**-**	-	(685)	(118)	**(803)**
Non-current liabilities	-	-	**-**	-	(6,158)	(331)	**(6,489)**
	3	-	**3**	917	(6,843)	4	**(5,919)**

Notes to the consolidated financial statements - supplementary information

This section includes information that is important to enable a full understanding of our financial position, particularly areas of potential risk that could affect us in the future.

21. Commitments and contingencies

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

Future capital expenditure	2013 £m	2012 £m
Contracted for but not provided	**1,941**	1,828
Operating lease commitments		
Amounts due:		
Less than 1 year	**14**	13
In 1 - 2 years	**11**	11
In 2 - 3 years	**8**	9
In 3 - 4 years	**7**	7
In 4 - 5 years	**6**	7
More than 5 years	**20**	22
	66	69

Other commitments, contingencies and guarantees
Guarantees in respect of a former associate amounting to £14m (2012: £14m). These are open ended.

Guarantees in the normal course of business and entered into on normal commercial terms amounted to £908m (2012: £707m). These include guarantees of certain obligations for construction of the HVDC West Coast link amounting to £618m (2012: £691m) expiring in 2016.

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

22. Related party transactions

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

The following material transactions are with fellow subsidiaries of National Grid plc, a joint venture and a pension plan, and are in the normal course of business.

	Parent		Other related parties		Total	
	2013 £m	2012 £m	**2013 £m**	2012 £m	**2013 £m**	2012 £m
Income:						
Goods and services supplied (i)	**-**	-	**21**	19	**21**	19
Interest received on advances to fellow subsidiaries	**-**	-	**3**	-	**3**	-
	-	-	**24**	19	**24**	19
Expenditure:						
Services received (ii)	**-**	-	**(98)**	(27)	**(98)**	(27)
Corporate services received	**-**	-	**(11)**	(9)	**(11)**	(9)
Interest paid on borrowings from fellow subsidiaries	**(4)**	(1)	**(13)**	(9)	**(17)**	(10)
	(4)	(1)	**(122)**	(45)	**(126)**	(46)
Outstanding balances at 31 March in respect of income, expenditure and settlement of corporation tax:						
Amounts receivable (iii)	**-**	-	**12**	21	**12**	21
Amounts payable	**-**	-	**(86)**	(53)	**(86)**	(53)
Advances to fellow subsidiaries (amounts due within one year):						
At 1 April	**2**	2	**32**	2	**34**	4
Advances	**-**	-	**(26)**	30	**(26)**	30
At 31 March	**2**	2	**6**	32	**8**	34
Borrowings payable to fellow subsidiaries (amounts due within one year):						
At 1 April	**(10)**	(10)	**(448)**	(195)	**(458)**	(205)
Advances	**-**	-	**-**	(259)	**-**	(259)
Repayments	**-**	-	**436**	6	**436**	6
At 31 March	**(10)**	(10)	**(12)**	(448)	**(22)**	(458)
Borrowings payable to fellow subsidiaries (amounts due after one year):						
At 1 April	**-**	-	**(287)**	-	**(287)**	-
Advances	**-**	-	**(9)**	(287)	**(9)**	(287)
At 31 March	**-**	-	**(296)**	(287)	**(296)**	(287)

(i) Includes £4m in respect of joint ventures (2012: £3m).
(ii) Includes £53m in respect of joint ventures (2012: £15m).
(iii) Includes £3m in respect of joint ventures (2012: £1m).

Amounts receivable from or payable to related parties in respect of income and expenditure are ordinarily settled one month in arrears. 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 2013 (2012: £nil) and no expense recognised during the year (2012: £nil) in respect of bad or doubtful debts for related party transactions.

Details of key management compensation are provided in note 2(c) and information relating to pension fund arrangements is disclosed in notes 17 and 23.

23. Actuarial information on pensions

Keeping it simple
Further details of the defined benefit scheme terms and the actuarial assumptions used to value the associated assets and obligations are set out in this note.
When deciding on these assumptions we take independent actuarial advice. Comparatively small changes in the assumptions used may have a significant effect on the overall deficit or surplus of a defined benefit scheme.

The National Grid Electricity Group of the Electricity Supply Pension Scheme is funded with assets held in a separate trustee administered fund. The arrangements are subject to independent actuarial valuations at least every three years and following consultation and agreement with us, the qualified actuary certifies the rate of employer's contribution, which, together with the specified contributions payable by the employees and proceeds from the scheme's assets, are expected to be sufficient to fund the benefits payable under the scheme. The last full actuarial valuations were carried out as at 31 March 2010 and the 2013 valuation process has commenced.

Latest full actuarial valuation	31 March 2010
Actuary	Aon Hewitt
Market value of scheme assets at latest valuation	£1,531m
Actuarial value of benefits due to members	£(2,038)m
Market value as percentage of benefits	75%
Funding deficit	£507m
Funding deficit (net of tax)	£390m

We have started discussions with our employee and trade union partners to ensure our defined benefit scheme is affordable and sustainable for the future.

The 2010 actuarial valuation showed that, based on long-term financial assumptions, the contribution rate required to meet future benefit accrual was 29.6% of pensionable earnings (23.7% employers and an average of 5.9% employees). The employer contribution rate will be reviewed as part of the 2013 actuarial valuation.

Following the 2010 actuarial valuation, National Grid and the Trustees agreed a recovery plan that will see the funding deficit repaid by 31 March 2027. Under the schedule of contributions, payments of £45m were made in 2010/11 and 2011/12 and a further payment of £38m was made in 2012/13. Thereafter, an annual payment of £38m is due to be made, rising in line with RPI. As part of this agreement, National Grid has established a secured bank account with a charge in favour of the Trustees. The balance of the bank account at 31 March 2013 was £9m. The funds in the bank account will be paid to the scheme in the event that National Grid Electricity Transmission plc (NGET) is subject to an insolvency event, or ceases to hold a licence granted under the Electricity Act 1989. The funds in the bank account will be released back to National Grid if the scheme moves into surplus.
National Grid has also agreed to make a payment in respect of the deficit up to a maximum of £220m should certain triggers be breached; namely if NGET ceases to hold the licence granted under the Electricity Act 1989 or NGET's credit rating by two out of three specified agencies falls below certain agreed levels for a period of 40 days.

The scheme closed to new members from 1 April 2006. A defined contribution arrangement was offered to new hires from this date. National Grid is currently reviewing the defined contribution arrangement it offers to employees and new hires in the UK.

Asset allocations

	2013 %	2012 %
Equities	**35.7**	40.0
Gilts	**34.1**	33.6
Corporate bonds	**10.9**	11.7
Hedge funds	**6.8**	6.6
Property	**3.9**	3.8
Cash (awaiting investment)	**1.8**	2.0
Other	**6.8**	2.3
Total	**100.0**	100.0

The current target asset allocation is 45% equities and 55% for bonds, property and other assets.

Actuarial assumptions

The expected long-term rate of return on assets has been set reflecting the price inflation expectation, the expected real return on each major asset class and the long-term asset allocation strategy adopted for each 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 independent actuaries.

	2013 %	2012 %
Discount rate (i)	**4.3**	4.8
Expected return on plan assets	**4.3**	5.7
Rate of increase in salaries (ii)	**4.4**	4.2
Rate of increase in pensions in payment and deferment	**3.2**	3.0
Rate of increase in Retail Prices Index	**3.4**	3.2

(i) The discount rates for pension liabilities have been determined by reference to appropriate yields on high quality corporate bonds prevailing in the UK and US debt markets at the reporting date.

(ii) A promotional scale has been used where appropriate.

23. Actuarial information on pensions continued

Actuarial assumptions continued

	2013 years	2012 years
Assumed life expectations for a retiree at age 65		
Today:		
Males	**24.7**	24.6
Females	**25.0**	24.9
In 20 years:		
Males	**27.6**	27.4
Females	**28.3**	28.2

The history of the present value of obligations, the fair value of the plan assets and experience adjustments is as follows:

	2013 £m	2012 £m	2011 £m	2010 £m	2009 £m
Present value of funded and unfunded obligations	**(2,563)**	(2,251)	(2,065)	(2,024)	(1,553)
Fair value of plan assets	**1,943**	1,739	1,598	1,531	1,145
	(620)	(512)	(467)	(493)	(408)
Difference between expected and actual return on plan assets	**134**	17	(17)	279	(301)
Experience (losses)/gains on plan liabilities	**6**	(4)	(1)	45	(19)
Actuarial (losses)/gains on plan liabilities	**(266)**	(138)	9	(432)	224

24. Financial risk

Keeping it simple

Our activities expose us to a variety of financial risks: market risk, including foreign exchange risk, fair value interest rate risk, cash flow interest rate risk; credit risk; and liquidity risk. Our overall risk management programme focuses on the unpredictability of financial markets and seeks to minimise potential volatility on financial performance. We use financial instruments, including derivative financial instruments, to manage risks of this type.

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

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

(a) Market risk

(i) Foreign exchange risk

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

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

During 2013 and 2012, derivative financial instruments were used to manage foreign currency risk as follows:

	2013			
	Sterling £m	**Euro £m**	**Other £m**	**Total £m**
Cash and cash equivalents	**3**	**-**	**-**	**3**
Financial investments	**917**	**-**	**-**	**917**
Borrowings (i)	**(4,810)**	**(778)**	**(1,255)**	**(6,843)**
Pre-derivative position	**(3,890)**	**(778)**	**(1,255)**	**(5,923)**
Derivative effect	**(2,008)**	**757**	**1,255**	**4**
Net debt position	**(5,898)**	**(21)**	**-**	**(5,919)**

	2012			
	Sterling £m	Euro £m	Other £m	Total £m
Financial investments	261	4	-	265
Borrowings (i)	(4,636)	(601)	(191)	(5,428)
Pre-derivative position	(4,375)	(597)	(191)	(5,163)
Derivative effect	(846)	584	191	(71)
Net debt position	(5,221)	(13)	-	(5,234)

(i) Includes bank overdrafts

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

24. Financial risk continued

(a) Market risk continued

(ii) Cash flow and fair value interest rate risk

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

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

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

The table in note 14 (borrowings) sets out the carrying amount, by contractual maturity, of borrowings that are exposed to interest rate risk before taking into account interest rate swaps.

During 2013 and 2012, net debt was managed using derivative instruments to hedge interest rate risk as follows:

	2013				
	Fixed rate £m	**Floating rate £m**	**RPI £m**	**Other(i) £m**	**Total £m**
Cash and cash equivalents	**-**	**3**	**-**	**-**	**3**
Financial investments	**-**	**916**	**-**	**1**	**917**
Borrowings (iii)	**(3,597)**	**(436)**	**(2,805)**	**(5)**	**(6,843)**
Pre-derivative position	**(3,597)**	**483**	**(2,805)**	**(4)**	**(5,923)**
Derivative effect	**415**	**(401)**	**(10)**	**-**	**4**
Net debt position (ii)	**(3,182)**	**82**	**(2,815)**	**(4)**	**(5,919)**

	2012				
	Fixed rate £m	Floating rate £m	RPI £m	Other(i) £m	Total £m
Financial investments	-	264	-	1	265
Borrowings (iii)	(1,928)	(899)	(2,596)	(5)	(5,428)
Pre-derivative position	(1,928)	(635)	(2,596)	(4)	(5,163)
Derivative effect	(44)	36	(63)	-	(71)
Net debt position (ii)	(1,972)	(599)	(2,659)	(4)	(5,234)

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

(ii) The impact of 2013/14 (2012: 2012/13) maturing short-dated interest rate derivatives is included.

(iii) Includes bank overdrafts.

24. Financial risk continued

(b) Fair value analysis

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

	2013				2012			
	Level 1 £m	**Level 2 £m**	**Level 3 £m**	**Total £m**	Level 1 £m	Level 2 £m	Level 3 £m	Total £m
Assets								
Available-for-sale investments	**681**	**-**	**-**	**681**	4	-	-	4
Derivative financial instruments	**-**	**406**	**47**	**453**	-	300	57	357
	681	**406**	**47**	**1,134**	4	300	57	361
Liabilities								
Derivative financial instruments	**-**	**(355)**	**(94)**	**(449)**	-	(284)	(144)	(428)
Total	**681**	**51**	**(47)**	**685**	4	16	(87)	(67)

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

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

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

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

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

	2013 Level 3 valuation £m	2012 Level 3 valuation £m
At 1 April	**(87)**	53
Net gains/(losses) for the year (i)	**43**	(25)
Purchases	**-**	(112)
Settlements	**(3)**	(3)
At 31 March	**(47)**	(87)

(i) Gains of £43m (2012: £25m loss) are attributable to assets or liabilities held at the end of the reporting period and have been recognised in finance costs in the income statement.

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

	2013 Income Statement £m	2012 Income Statement £m
+20 basis point change in LPI market curve	**(38)**	(34)
-20 basis point change in LPI market curve	**37**	31

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

(c) Credit risk

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

24. Financial risk continued

(c) Credit risk continued

Treasury credit risk

Counterparty risk arises from the investment of surplus funds and from the use of derivative instruments. The Company's limits are managed by the central treasury department of National Grid, as explained in the 'What are the risks?' on pages 11 to 14.

As at 31 March 2012 and 2013, we had a number of exposures to individual counterparties. In accordance with our treasury policies, counterparty credit exposure utilisations are monitored daily against the counterparty credit limits. Counterparty credit ratings and market conditions are reviewed continually with limits being revised and utilisation adjusted, if appropriate. Management does not expect any significant losses from non performance by these counterparties.

The counterparty exposure under derivative financial contracts as shown in note 9 was £453m (2012: £357m); after netting agreements it was £290m (2012: £246m). This exposure is further reduced by collateral received as shown in note 14.

Wholesale and retail credit risk

Our principal commercial exposure is governed by the credit rules within the regulated Connection and Use of System Code. This lays down the level of credit relative to the regulatory asset value for each credit rating. We have no retail credit risk. Management does not expect any significant losses of receivables.

(d) Liquidity analysis

Our policy is to 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 24 month period.

We believe our contractual obligations, including those shown in commitments and contingencies in note 21 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.

Our debt agreements and banking facilities contain covenants, including those relating to the periodic and timely provision of financial information by the issuing entity, and in addition, certain of our loan agreements assume current ratnig levels. Failure to comply with these covenants, or to obtain waivers of those requirements, could in some cases trigger a right, at the lender's discretion, to require repayment of some of our debt. These requirements are monitored on a regular basis.

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

At 31 March 2013	Due within 1 year	Due between 1 and 2 years	Due between 2 and 3 years	Due 3 years and beyond	Total
Non-derivative financial liabilities					
Borrowings	**(608)**	**-**	**(140)**	**(5,862)**	**(6,610)**
Interest payments on borrowings (i)	**(226)**	**(200)**	**(201)**	**(2,943)**	**(3,570)**
Other non-interest bearing liabilities	**(630)**	**(14)**	**-**	**-**	**(644)**
Derivative financial liabilities					
Derivative contracts - receipts	**166**	**141**	**92**	**373**	**772**
Derivative contracts - payments	**(150)**	**(106)**	**(52)**	**(431)**	**(739)**
Total at 31 March 2013	**(1,448)**	**(179)**	**(301)**	**(8,863)**	**(10,791)**

At 31 March 2012	Due within 1 year	Due between 1 and 2 years	Due between 2 and 3 years	Due 3 years and beyond	Total
Non-derivative financial liabilities					
Borrowings	(702)	(500)	-	(4,046)	(5,248)
Interest payments on borrowings (i)	(171)	(167)	(144)	(2,563)	(3,045)
Other non-interest bearing liabilities	(487)	(10)	-	-	(497)
Derivative financial liabilities					
Derivative contracts - receipts	126	169	37	170	502
Derivative contracts - payments	(70)	(233)	(38)	(120)	(461)
Total at 31 March 2012	(1,304)	(741)	(145)	(6,559)	(8,749)

(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 forward interest rate curve as at 31 March. Payments are included on the basis of the earliest date on which the Company can be required to settle.

24. Financial risk continued

(e) Capital risk management

Our objectives when managing capital are: to safeguard our ability to continue as a going concern, to remain within regulatory constraints of our regulated operating company and to maintain an efficient mix of debt and equity funding thus achieving an optimal capital structure and cost of capital.

Maintaining appropriate credit ratings for our regulated company is an important aspect of our capital risk management strategy and balance sheet efficiency. We monitor our balance sheet efficiency by regulatory asset value (RAV) gearing calculated as net debt expressed as a percentage of RAV, and indicates the level of debt employed to fund our regulated business. The RAV gearing ratio at 31 March 2013 was 58% compared with 57% at 31 March 2012. We regularly review and maintain or adjust the capital structure as appropriate in order to manage the level of RAV gearing. It is compared with the level of RAV gearing indicated by Ofgem as being appropriate for our business, at around 60%.

25. Sensitivities on areas of estimation and uncertainty

Keeping it simple

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

Revenue accruals

A 10% change in our estimate of unbilled revenues at 31 March 2013 would result in an increase or decrease in our recorded net assets and profit for the year of approximately £15 million (2012: £16 million) net of tax.

Asset useful lives

An increase in the economic useful lives of assets of one year on average would reduce our annual depreciation charge on property, plant and equipment by £8 million (2012: £7 million) (pre-tax) and our annual amortisation charge on intangible assets by £1 million (2012: £nil million) (pre-tax).

Hedge accounting

If using our derivative financial instruments, hedge accounting had not been achieved during the year ended 31 March 2013, then the profit after tax for the year would have been £17 million (2012: £17 million) higher and net assets would have been £18 million higher (2012: £53 million higher).

Provisions

A 10% change in the estimates of future cash flows in respect of provisions for liabilities would result in an increase or decrease in our provisions of approximately £10 million (2012: £9 million).

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 £nil million (2012: £7 million).

Pensions and other post retirement benefits

The impact of increases in the discount rate, salary inflation and life expectancy is shown in the table below. The effect of a change in the discount rate, driven by changes in corporate bond interest rates, would be expected to have a partial offset due to the related effects on asset values.

	Change in pensions and other post retirement obligations		Change in annual pensions and other post retirement costs	
	2013	2012	**2013**	2012
	£m	£m	**£m**	£m
Sensitivities (all other assumptions held constant):				
0.1% change in discount rate	**32**	35	**1**	1
0.5% change in long-term rate of increase in salaries	**40**	33	**2**	2
Change of one year to life expectations at age 60	**78**	62	**1**	1

25. Sensitivities on areas of estimation and uncertainty continued

Financial risk

Our financial instruments are sensitive to changes in market variables, being UK interest rates and UK RPI rates. The changes in market variables impacts the valuation of our borrowings, deposits and derivative financial instruments. The following analysis illustrates the sensitivity of our financial instruments to the changes in market variables.

The following main assumptions were made in calculating the sensitivity analysis:

- 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 2013 and 2012 respectively;
- the statement of financial position sensitivity to interest rates relates only to derivative financial instruments and available-for-sale investments, as debt and other deposits are carried at amortised cost and so their carrying value does not change as interest rates move;
- the sensitivity of accrued interest to movements in interest rates is calculated on net floating rate exposures on debt, deposits and derivative instruments;
- changes in the carrying value of derivatives from movements in interest rates of designated cash flow hedges are assumed to be recorded fully within equity.

Using the above assumptions, and a number of others which have a far smaller impact overall, the following table shows the illustrative effect on the income statement and items that are recognised directly in equity that would result from reasonably probable movements in the UK RPI and UK interest rates, after the effects of tax.

	2013		2012	
	Income statement -/+ £m	**Other Equity Reserves -/+ £m**	Income statement -/+ £m	Other Equity Reserves -/+ £m
UK RPI +/- 0.50%*	**11**	**-**	9	-
UK interest rates +/- 0.50%	**1**	**26**	4	17

*Excludes sensitivities to Limited Price Inflation Index. Further details on sensitivities are provided in note 24(b).

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

26. Ultimate parent company

Keeping it simple

This note shows the immediate and ultimate parent companies for these consolidated financial statements.

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

27. Principal subsidiary undertakings

Keeping it simple

While we present consolidated results in these financial statements as if we were one company, our structure is such that there are a number of subsidiaries and joint ventures that contribute to the overall result.

The Company does not consolidate its wholly owned subsidiary Elexon Limited, which is the electricity market Balancing and Settlement Code company for Great Britain, as it has no control over Elexon.

The Company's principal joint venture included in the financial statements at 31 March 2013 is NGET/SPT Upgrades Ltd (50% of ordinary shares held) whose principal activity is construction services.

Company accounting policies

for the year ended 31 March 2013

Keeping it simple

We are required to include the stand-alone balance sheet of our ultimate parent Company, National Grid Electricity Transmission plc, under the Companies Act 2006 and the following disclosures provide additional information to shareholders.

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. They have been prepared on an historical cost basis, except for the revaluation of financial instruments, and are presented in pounds sterling, which is the currency of the primary economic environment in which the Company operates. The 2012 comparative financial information has also been prepared on this basis.

The individual financial statements have been prepared on a going concern basis following the assessment made by the Directors as set out in the Directors report on page 29.

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'.

The Company has taken advantage of the exemptions in FRS 8 'Related Party Disclosures' from disclosing transactions with other members of the National Grid plc group of companies.

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.

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 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 buildings	up to 50
Plant and Machinery	
- Electricity Transmission plant	15-60
Motor vehicles and office equipment	up to 7

D. Fixed asset investments

Investments held as fixed assets are stated at cost less any provisions for impairment. Investments are reviewed for impairment if events or changes in circumstances indicate that the carrying amount may not be recoverable. Impairments are calculated such that the carrying value of the fixed asset investment is the lower of its cost or recoverable amount. Recoverable amount is the higher of its net realisable value and its value-in-use.

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.

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 of electricity and the provision of related services during the year, including an assessment of services provided but not invoiced as at the year end and excludes value added tax and intra-group sales.

The sales value for the transmission of electricity is largely determined from the amount of electricity transmitted in the year and system capacity sold for the year, evaluated at contractually determined prices or recovery rates. The sales value for the provision of balancing services is based on the amount of system balancing costs incurred.

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.

Income arising from the sale of properties as a result of our property management activities is reported as other operating income.

J. Pensions

For defined benefit pension schemes, the regular service cost of providing retirement benefits to employees during the period, together with the cost of any benefits relating to past service, are recognised within operating costs.

The interest cost on retirement benefit scheme liabilities and the expected return on scheme assets during the year, are recognised in the profit and loss account within net interest.

The actuarial value of pension liabilities, net of the market value of the assets of the scheme are recognised as a liability in the balance sheet, net of the related deferred tax asset.

The difference between the actual and expected returns on scheme assets and the experience gains or losses arising on scheme liabilities, together with gains or losses arising from changes in actuarial assumptions, are recognised directly in equity within the profit and loss account reserve.

K. Leases

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

L. Financial instruments

The Company's accounting policies under UK GAAP, namely FRS 25 'Financial Instruments: Presentation', FRS 26 'Financial Instruments: Measurement' and FRS 29 'Financial Instruments: Disclosures', are the same as the Group's accounting policies under IFRS, namely IAS 32 'Financial Instruments: Presentation', IAS 39 'Financial Instruments: Recognition and Measurement' and IFRS 7 'Financial Instruments: Disclosures'. The Company applies these policies only in respect of the financial instruments that it has, namely investments, derivative financial instruments, debtors, cash at bank and in hand, borrowings and creditors.

The policies are set out in notes 9, 11, 12, 13, 14 and 15 to the consolidated financial statements. The Company is taking the exemption for financial instruments disclosures, because IFRS 7 disclosures are given in notes 24 and 25 to the consolidated financial statements.

M. Hedge accounting

The Company applies the same accounting policy as the Group in respect of fair value hedges and cash flow hedges. This policy is set out in note 9 to the consolidated financial statements.

N. 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.

O. 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.

P. Dividends

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

Company balance sheet

as at 31 March

	Notes	2013 £m	2012 £m
Fixed assets			
Tangible assets	4	**9,637**	8,537
		9,637	8,537
Current assets			
Stocks	5	**30**	28
Debtors	6	**240**	231
Derivative financial instruments (amounts falling due within one year)	7	**44**	20
Derivative financial instruments (amounts falling due after more than one year)	7	**409**	337
Investments	8	**917**	265
Cash at bank and in hand		**3**	-
		1,643	881
Creditors (amounts falling due within one year)			
Borrowings	11	**(685)**	(749)
Derivative financial instruments	7	**(118)**	(26)
Other creditors		**(817)**	(718)
	9	**(1,620)**	(1,493)
Net current assets/(liabilities)		**23**	(612)
Total assets less current liabilities		**9,660**	7,925
Creditors (amounts falling due after more than one year)			
Borrowings	11	**(6,158)**	(4,679)
Derivative financial instruments	7	**(331)**	(402)
Other creditors		**(285)**	(257)
	10	**(6,774)**	(5,338)
Provisions for liabilities	12	**(970)**	(940)
Net assets before pension liability		**1,916**	1,647
Net pension liability	13	**(461)**	(376)
Net assets		**1,455**	1,271
Capital and reserves			
Called up share capital	14	**44**	44
Cash flow hedge reserve	15	**(34)**	(64)
Profit and loss account	15	**1,445**	1,291
Total shareholders' funds		**1,455**	1,271

The notes on pages 70 to 75 form part of the individual financial statements of the Company, which were approved by the Board of Directors on 24 June 2013 and were signed on its behalf by:

Paul Whittaker Director

Andrew Agg Director

Notes to the Company financial statements

1. Auditors' remuneration

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

	2013 £m	2012 £m
Audit services		
Audit fee of parent company and consolidated financial statements	**0.2**	0.2
Other services		
Fees payable to the Company's auditors for audit related assurance services	**0.1**	0.1

Fees payable to the Company's auditors for audit related assurance services represents fees payable for services in relation to engagements which are required to be carried out by the auditors. In particular this includes fees for audit reports on regulatory returns.

2. Number of employees, including Directors

	2013 Average number	2012 Average number
United Kingdom	**3,125**	2,871

3. Directors' emoluments

Details of Directors' emoluments are provided in note 2(d) to the consolidated financial statements.

4. 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 2012	438	9,597	1,859	257	12,151
Additions	31	55	1,311	33	1,430
Disposals	-	(102)	(2)	(13)	(117)
Reclassifications	46	556	(626)	24	-
Cost at 31 March 2013	515	10,106	2,542	301	13,464
Depreciation at 1 April 2012	(51)	(3,399)	-	(164)	(3,614)
Depreciation charge for the year	(13)	(291)	-	(21)	(325)
Disposals	-	99	-	13	112
Reclassifications	(1)	1	-	-	-
Depreciation at 31 March 2013	(65)	(3,590)	-	(172)	(3,827)
Net book value at 31 March 2013	**450**	**6,516**	**2,542**	**129**	**9,637**
Net book value at 31 March 2012	387	6,198	1,859	93	8,537

The net book value of land and buildings comprised:

	2013 £m	2012 £m
Freehold	**368**	307
Long leasehold (over 50 years)	**3**	3
Short leasehold (under 50 years)	**79**	77
	450	387

The cost of tangible fixed assets at 31 March 2013 included £925m (2012: £831m) 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 £7m (2012: £7m) and £245m (2012: £222m) respectively.

5. Stocks

	2013 £m	2012 £m
Raw materials, spares and consumables	**30**	28

6. Debtors

	2013 £m	2012 £m
Amounts falling due within one year:		
Trade debtors	**15**	14
Amounts owed by fellow subsidiary undertakings	**9**	20
Other debtors	**8**	6
Prepayments and accrued income	**208**	191
	240	231

7. Derivative financial instruments

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

	2013			2012		
	Assets	Liabilities	Total	Assets	Liabilities	Total
Amounts falling due in one year	**44**	**(118)**	**(74)**	20	(26)	(6)
Amounts falling due after more than one year	**409**	**(331)**	**78**	337	(402)	(65)
	453	**(449)**	**4**	357	(428)	(71)

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

	2013 £m	2012 £m
Interest rate swaps	**(4,159)**	(3,842)
Cross-currency interest rate swaps	**(1,846)**	(631)
Foreign exchange forward currency	**(577)**	(596)
Forward rate agreements	**(1,158)**	(1,769)
Inflation linked swaps	**(630)**	(627)
	(8,370)	(7,465)

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

8. Investments

	2013	2012
	£m	£m
Loans and receivables - amounts due from fellow subsidiaries	**8**	34
Loans and receivables - restricted cash balances (i)	**228**	227
Available-for-sale investments	**681**	4
	917	265

(i) Comprises collateral placed with counterparties with whom we have entered into a credit support annex to the ISDA Master Agreement £219m (2012: £224m), and secured bank accounts with charges in favour of the UK pension schemes Trustees of £9m (2012: £3m).

9. Creditors (amounts falling due within one year)

	2013	2012
	£m	£m
Borrowings (note 11)	**685**	749
Derivative financial instruments (note 7)	**118**	26
Trade creditors	**438**	315
Amounts owed to fellow subsidiary undertakings	**90**	58
Social security and other taxes	**32**	18
Other creditors	**15**	15
Accruals and deferred income	**242**	312
	1,620	1,493

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

	2013	2012
	£m	£m
Borrowings (note 11)	**6,158**	4,679
Derivative financial instruments (note 7)	**331**	402
Other creditors	**14**	10
Deferred income	**271**	247
	6,774	5,338

Deferred income mainly comprises contributions to capital projects.

11. Borrowings

The following table analyses the company's total borrowings:

	2013 £m	2012 £m
Amounts falling due within one year:		
Bank overdrafts	**-**	4
Bank loans	**84**	244
Bonds	**579**	43
Borrowings from fellow subsidiary undertakings	**22**	458
	685	749
Amounts falling due after more than one year		
Bank loans	**404**	300
Bonds	**5,458**	4,092
Borrowings from fellow subsidiary undertakings	**296**	287
	6,158	4,679
Total borrowings	**6,843**	5,428

	2013 £m	2012 £m
Total borrowings are repayable as follows:		
Less than 1 year	**685**	749
In 1 - 2 years	**-**	510
In 2 - 3 years	**158**	-
In 3 - 4 years	**200**	170
In 4 - 5 years	**625**	200
More than 5 years other than by instalments	**5,175**	3,799
	6,843	5,428

The notional amount outstanding of the Company's debt portfolio at 31 March 2013 was £6,610m (2012: £5,248m).

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

12. Provisions for liabilities and charges

	Deferred taxation £m	Environ-mental £m	Other £m	Total £m
At 1 April 2012	846	76	18	940
Credited to profit and loss account	17	(7)	15	25
Transferred to reserves	10	-	-	10
Unwinding of discount	-	4	-	4
Utilised	-	(2)	(7)	(9)
At 31 March 2013	**873**	**71**	**26**	**970**

Details of the environmental provision and other provisions are shown in note 18 to the consolidated financial statements.

Deferred taxation

Deferred taxation provided in the financial statements comprises:

	2013 £m	2012 £m
Accelerated capital allowances	**889**	867
Other timing differences, excluding pensions liability	**(16)**	(21)
Included within provisions for liabilities and charges	**873**	846
Pensions liability	**(138)**	(118)
	735	728

At 31 March 2013 there are no material unrecognised deferred tax assets (2012: £nil).

13. Pensions

Substantially all of the Company's employees are members of either the National Grid Electricity Group of the Electricity Supply Pension Scheme (the Scheme) which is a defined benefit pension scheme or the defined contribution section of the National Grid UK pension scheme. Further details of the Scheme and the actuarial assumptions used to value the associated assets and pension obligations are provided in notes 17 and 23 to the consolidated financial statements.

Amounts recognised in the balance sheet of the Company are as follows:

	2013 £m	2012 £m
Present value of funded obligations	**(2,509)**	(2,205)
Fair value of plan assets	**1,943**	1,739
	(566)	(466)
Present value of unfunded obligations	**(33)**	(28)
Net liability in the balance sheet	**(599)**	(494)
Related deferred tax asset	**138**	118
Net pension liability	**(461)**	(376)

Changes in the present value of the defined benefit obligations (including unfunded obligations)		
Opening defined benefit obligations	**2,233**	2,049
Current service cost	**30**	27
Interest cost	**106**	111
Actuarial losses	**264**	137
Net increase in liabilities from redundancies	**3**	1
Employee contributions	**2**	2
Benefits paid	**(96)**	(93)
Net transfers	**-**	(1)
Closing defined benefit obligations	**2,542**	2,233

Changes in the fair value of plan assets		
Opening fair value of plan assets	**1,739**	1,598
Expected return on plan assets	**97**	107
Actuarial losses/(gains)	**134**	17
Employer contributions	**67**	109
Employee contributions	**2**	2
Benefits paid	**(96)**	(93)
Net transfers	**-**	(1)
Closing fair value of plan assets	**1,943**	1,739

14. Called-up share capital

	Number of shares 2013 millions	Number of shares 2012 millions	**2013 £m**	2012 £m
At 31 March 2012 and 2013 - ordinary shares of 10p each				
Allotted, called-up and fully paid	**437**	437	**44**	44

15. Reserves

	Cash flow hedge reserve £m	Profit and loss account £m
At 1 April 2012	(64)	1,291
Actuarial losses (net of tax)	-	(103)
Net expense transferred to equity in respect of cash flow hedges (net of tax)	30	-
Share-based payments	-	3
Tax on share-based payments	-	-
Profit for the year	-	654
Dividends	-	(400)
At 31 March 2013	**(34)**	**1,445**

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 tax for the year was £654m (2012: £547m).

16. Reconciliation of movement in shareholders' funds

	2013	2012
	£m	£m
Profit for the year after taxation	**654**	547
Dividends (i)	**(400)**	(200)
Profit/(loss) for the financial year	**254**	347
Net gains recognised directly in reserves	**(73)**	(132)
Share-based payments	**3**	3
Net increase/(decrease) in shareholders' funds	**184**	218
Opening shareholders' funds	**1,271**	1,053
Closing shareholders' funds	**1,455**	1,271

(i) For further details of dividends paid and payable to shareholders, refer to note 6 in the consolidated financial statements.

17. Commitments and contingencies

(a) Future capital expenditure

	2013	2012
	£m	£m
Contracted for but not provided	**1,941**	1,828

(b) Lease commitments

At 31 March 2013, the Company's total operating lease commitments for the financial year ending 31 March 2014 amounted to £14m (2012 commitments for 2013: £13m) and are analysed by lease expiry date as follows:

	Land and buildings		Other		Total	
	2013	2012	**2013**	2012	**2013**	2012
	£m	£m	**£m**	£m	**£m**	£m
Expiring:						
In one year or less	**1**	-	**1**	-	**2**	-
In more than one year, but not more than five years	**1**	2	**5**	5	**6**	7
In more than five years	**6**	6	**-**	-	**6**	6
	8	8	**6**	5	**14**	13

The Company's total commitments under non-cancellable operating leases were as follows:

	2013	2012
	£m	£m
Amounts:		
In one year or less	**14**	13
In more than one year, but not more than two years	**11**	11
In more than two years, but not more than three years	**8**	9
In more than three years, but not more than four years	**7**	7
In more than four years, but not more than five years	**6**	7
In more than five years	**20**	22
	66	69

(c) Other commitments, contingencies and guarantees

Guarantees in respect of a former associate amounting to £14m (2012: £14m). These are open ended.

Guarantees in the normal course of business and entered into on normal commercial terms amounted to £908m (2012: £707m). These include guarantees of certain obligations for construction of the HVDC West Coast link amounting to £618m (2012: £691m) expiring in 2016.

Glossary and definitions

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

BSIS
The Balancing Services Incentive Scheme, an incentive arrangement applicable to the Company's electricity transmission arrangements.

Delivery Body
Under the Energy Bill currently being considered by the UK Parliament, National Grid Electricity Transmission's system operator function would provide independent evidence and analysis to the UK Government to inform its decisions on the key rules and parameters to achieve the Government's policy objectives under Electricity Market Reform. As proposed, National Grid Electricity Transmission would administer the capacity mechanism, including running the annual capacity auctions, managing the allocation of contracts for difference to low carbon generators and reporting to Government annuallly on performance against the Government's delivery plan. Detailed roles and responsibilities for all market participants, including the Delivery Body, will be finalised within secondary legislation enacted under the Energy Act 2013, due to be in force from summer 2014.

Electricity Market Reform (EMR)
An energy policy initiative, introduced by the Energy Bill currently being considered by the UK Parliament, designed to provide greater financial certainty to investors in low carbon generation by guaranteeiing a price for electricity generated.

EU
European Union

FRS
UK Financial Reporting Standard.

GAAP
Generally accepted accounting principles.

GHG
Greenhouse gas

GW
Gigawatt, 10^9 watts.

GWh
Gigawatt hours.

HSE
Health and Safety Executive.

IAS
International Accounting Standard.

IASB
International Accounting Standards Board

IFRIC
The International Financial Reporting Interpretations Committee, which provides guidance on how to apply accounting standards.

IFRS
International Financial Reporting Standard.

KPI
Key Performance Indicator.

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

National Grid
National Grid plc, the ultimate parent company of National Grid Electricity Transmission plc and its controlling party.

Ofgem
The Office of Gas and Electricity Markets.

Regulatory asset value (RAV)
The value ascribed by Ofgem to the capital employed in the licensed business. It is an estimate of the initial market value of the regulated asset base at privatisation, plus subsequent allowed additions at historic costs, less the deduction of annual regulatory depreciation. Deductions are also made to reflect the value realised from the disposal of certain assets that formed part of the regulatory asset base. It is also indexed to the RPI to allow for effects inflation.

Regulated controllable operating costs
Total operating costs under IFRS less depreciation and certain regulatory costs where, under our regulatory agreements, mechanisms are in place to recover such costs in current or future periods.

RIIO
The revised regulatory framework issued by Ofgem which was implemented in the eight year price controls which started on 1 April 2013.

RPI
UK Retail Prices Index

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

TW
Terawatt, 10^{12} watts.

TWh
Terawatt hours.

National Grid Electricity Transmission plc
1-3 Strand, London WC2N 5EH, United Kingdom
Registered in England and Wales No. 2366977