

Operating and Financial Review

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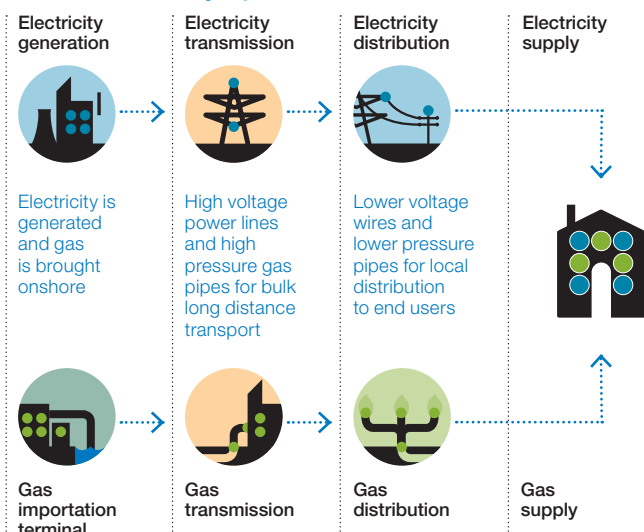
Principal operations

Our principal operations are the ownership and operation of regulated electricity and gas infrastructure networks in the UK and the US, serving around 19 million consumers directly and many more indirectly. We also have interests in related markets.

We have over 28,000 employees in the UK and US.

The performance of our principal businesses is reported by segment, reflecting the management responsibilities and economic characteristics of each activity. Our principal businesses and segments, together with other activities, are described on this page and further details are available on pages 46 to 73.

How the industry operates



Transmission

UK

The transmission of electricity and gas in the UK as owner and operator of the high voltage electricity transmission network in England and Wales, the gas national transmission system in Great Britain, electricity interconnector with France and storage facilities for LNG. The operation, but not ownership, of the electricity transmission networks in Scotland.

US

The transmission of electricity in the northeastern US as owner and operator of high voltage electricity transmission networks in upstate New York, Massachusetts, New Hampshire, Rhode Island and Vermont.

Gas Distribution

UK

The distribution of gas as owner and operator of four of Great Britain's eight gas distribution networks.

US

The distribution of gas in the northeastern US as owner and operator of gas distribution networks in upstate New York, New York City, Long Island, Massachusetts, New Hampshire and Rhode Island.

Electricity Distribution & Generation

US

The distribution and generation of electricity in the northeastern US as owner of electricity distribution networks in upstate New York, Massachusetts, New Hampshire and Rhode Island, as operator and manager of the

electricity transmission and distribution network on Long Island on behalf of the Long Island Power Authority and as a generator of electricity on Long Island.

Non-regulated businesses and other

Other services related to our main operations, principally in the UK. Includes metering services, property management, electricity interconnectors and liquefied natural gas (LNG) importation.

This Operating and Financial Review describes the main trends and factors underlying our development, performance and position during the year ended 31 March 2010 as well as those likely to affect us in the future. It has been prepared in line with the guidance provided in the Reporting Statement on the Operating and Financial Review issued by the UK Accounting Standards Board.

Organisation and structure

Organisation

Our organisational structure and executive responsibilities ensure a balance between activities that are managed locally, those managed by line of business, and those that are common throughout National Grid.

The Board of Directors has overall responsibility for the governance, strategy and management oversight of National Grid. The Executive Committee, led by the Chief Executive, is responsible for the day-to-day management of National Grid and for the execution of our strategy as approved by the Board.

Board of Directors	
Executive Committee	
Chief Executive: Steve Holliday	
Finance and shared services: Steve Lucas	
Transmission: Nick Winser	Gas Distribution: Mark Fairbairn
Electricity Distribution & Generation: Tom King	Non-regulated businesses* and other (including corporate functions and information services)

* Responsibility for our non-regulated businesses is allocated to the Executive Directors based on the nature of each business

In addition to the Executive Committee, the Board has also established a number of other Committees that assist in exercising governance over National Grid's activities. These are the Audit, Finance, Nominations, Remuneration, Risk & Responsibility and Disclosure Committees.

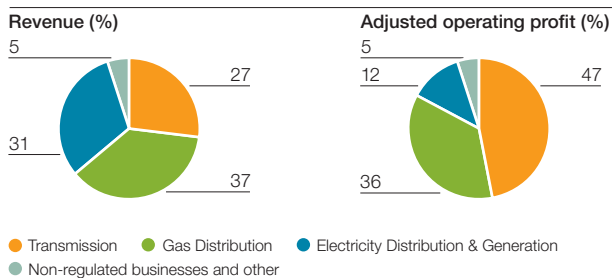
More information on the roles of the Board and its Committees can be found in the Corporate Governance section on pages 87 to 91

Business and geographic analysis

Our continuing operations are organised by lines of business as follows:

Business analysis 2009/10

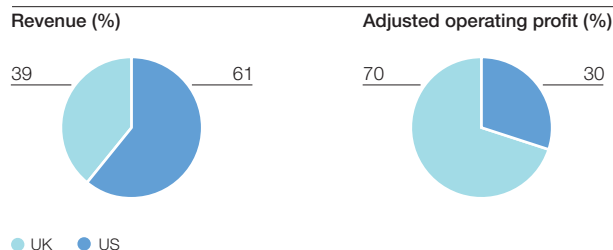
Continuing operations



Our businesses are divided between the UK and the US as follows:

Geographical analysis 2009/10

Continuing operations



The charts show revenue and adjusted operating profit from continuing operations for the year ended 31 March 2010. Adjusted operating profit excludes exceptional items, remeasurements and stranded cost recoveries.

More information on these adjustments is available on pages 38 and 39 and in Accounting policies on page 116

In the US, we purchase electricity and gas for onward sale to customers, and the amount we receive from customers for these commodities is included in revenue. We make no margin on these purchases and sales. In the UK, we do not purchase or sell the commodities, so there is no equivalent amount included in UK revenue.

History

National Grid originated from the restructurings of the UK gas industry in 1986 and the UK electricity industry in 1990. We entered the US electricity delivery market in 2000 in New England and expanded into upstate New York in 2002. We increased our UK wireless infrastructure activities in 2004 and in 2005 we sold four UK regional gas distribution networks.

In 2006, we acquired the gas distribution network in Rhode Island and, in 2007, we acquired KeySpan. We sold our UK and US wireless infrastructure operations and the Basslink electricity interconnector in Australia during 2007. In 2008, we sold the Ravenswood generation station.

More information on the history of National Grid is available in the Shareholder information section on page 191

External market

Markets in which we operate

The principal markets in which we operate are the electricity and gas markets in Great Britain and in Massachusetts, New York, Rhode Island and New Hampshire in the US.

The supply of electricity and gas in the UK and in most of the states in which we operate in the northeastern US is competitive in that consumers can choose their energy supplier. Those suppliers are then responsible for sourcing the energy from electricity generators or from gas extractors or importers as appropriate, as well as arranging for that energy to be delivered through physical delivery networks. These networks, including the ones we operate, are generally monopolies in their local areas because, for the majority of consumers, there are no alternative methods of receiving electricity or gas.

Energy delivery in the UK

In general, in the UK, energy is transported through electricity or gas transmission networks to regional electricity or gas distribution networks that then deliver energy to consumers on behalf of suppliers. This is shown in figure 1. Certain end users, primarily large industrial consumers, receive electricity or gas directly from the relevant transmission network, rather than through a distribution network (not shown in diagram).

We are the owner and operator of the high voltage electricity transmission network in England and Wales; operator, but not owner, of the two electricity transmission networks in Scotland; and owner and operator of the gas national transmission system and of four of the eight regional gas distribution networks in Great Britain. We charge electricity and gas suppliers, electricity generators and gas shippers for our services. There are 14 electricity distribution networks in the UK, owned by 7 different companies. Two companies each own an electricity transmission network in Scotland, which we operate in both cases, and three companies own the four gas distribution networks in Great Britain that we do not own. The ownership of the networks we do not own is set out below.

Network	Owner (and parent where relevant)
Electricity distribution networks in Great Britain (non National Grid)	
West Midlands	
East Midlands	Central Networks (E.ON)
North West	Electricity North West
North East	
Yorkshire	CE Electric UK (Berkshire Hathaway)
South Wales	
South West England	Western Power Distribution
London	
South East England	EDF Energy Networks (Electricité de France)
East of England	
Central and Southern Scotland	
Cheshire, Merseyside and North Wales	Scottish Power (Iberdrola)
Northern Scotland	
Central Southern England	Scottish and Southern Energy
Electricity transmission networks in Scotland (non National Grid)	
Northern Scotland	Scottish and Southern Energy
Southern Scotland	Scottish Power (Iberdrola)
Gas distribution networks in Great Britain (non National Grid)	
North of England	Northern Gas Networks
Scotland	Scotland Gas Networks (Scotia Gas)
South and South East England	Southern Gas Networks (Scotia Gas)
Wales and West of England	Wales & West Utilities

Energy delivery in the northeastern US

In most of our operating areas in the northeastern US, consumers are able to purchase their energy through independent energy suppliers. While a number of large customers have chosen suppliers other than the local utility provider, the majority of residential and small commercial consumers still purchase electricity or gas from their local electricity or gas distribution network business. The major alternative fuel source to gas is oil, which many consumers use for domestic heating purposes.

Electricity is transported either directly from generators or independent suppliers into local electricity distribution networks or via electricity transmission networks, while gas is obtained from importation terminals, gas producers or independent suppliers transported on gas transmission pipelines and then transported through local gas distribution networks. This is shown in figures 2 and 3. Certain end users, primarily large industrial customers, receive electricity or gas directly from the electricity transmission networks or inter-state gas transmission pipelines (not shown in diagram).

Our US electricity and gas distribution businesses support regulatory policies that encourage customers to purchase their energy from independent suppliers. Where this occurs, we deliver that energy to consumers on behalf of those suppliers. For the majority of consumers in our operating areas who continue to purchase their energy from us, we purchase energy from electricity generators or gas suppliers on behalf of our customers in accordance with regulatory approved arrangements. We are generally responsible for billing customers both for our delivery services and for electricity and gas consumed, on which we do not charge any additional margin.

On Long Island, we operate the electricity transmission and distribution network on behalf of its owner, the Long Island Power Authority (LIPA). We own 57 electricity generation plants on Long Island that supply power under contract to LIPA. Our agreements with LIPA also cover our provision of fuel procurement and management services.

Electricity transmission and distribution networks, including the ones we own, are members of the regional transmission operators or independent system operators that have the responsibility for balancing electricity supply with demand and for the reliability of the regional transmission network. Gas distribution networks, including the ones we own, are each responsible for balancing gas supply with demand within their respective distribution area.

There are more than 25 other companies and organisations that own or operate fuel delivery infrastructure in the northeastern US.

Other markets in which we operate

Our other businesses primarily operate in energy related markets in the UK and the US or are directly related to our regulated businesses described above. This includes our metering services businesses in the UK, incorporating our legacy regulated metering business which owns approximately 75% of the domestic gas meters in the UK, and our competitive metering services business which owns a further 11%. In addition, we have a significant property portfolio and property management business.

Current and future developments

Market structure and ownership

There have been no significant changes in either the structure or ownership of the UK energy infrastructure market during 2009/10. In the northeastern US, there have been no significant changes to the structure or ownership of the electricity and gas networks during the year, although First Energy Corp. has announced a planned acquisition of Allegheny Energy Inc., and PPL Corp. has announced a planned acquisition of E.ON AG's US utilities, both subject to regulatory approval.

Energy market developments

Both the UK and the US energy markets continue to undergo developments driven by: new sources of electricity generation, including renewables; increased focus on security of supply; and the projected increased reliance in the UK on imported gas.

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

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

In January 2010, The Crown Estate announced the successful bidders for each of the nine Round 3 offshore wind zones within UK waters. These zones have the potential to deliver up to 32 GW of renewable offshore wind generation.

In March 2010, the DECC established a new Office of Carbon Capture and Storage, which is tasked with facilitating the delivery of carbon capture and storage in the UK, and helping to promote its rapid deployment globally.

Following the UK government's support for new nuclear generation announced in January 2008, the Health and Safety Executive is currently assessing generic designs. This assessment is expected to be completed in June 2011 and consideration of specific designs can then begin. The first new nuclear generation is currently expected to be operational by 2017.

Progress is continuing on phase III of our LNG importation facility on the Isle of Grain, with commissioning expected in winter 2010/11. Once fully commissioned, it is anticipated that our facility will have the capacity to import approximately 20% of the UK's gas demand.

In the US, the administration change has brought an increased political desire to tackle the issues around climate change and security of supply. The development of smart grid technologies is expected to enable more efficient use of the transmission and distribution grid, lower line losses, greater use of renewables and the provision of information to utilities and their customers that will lead to greater investment in energy efficiency and reduced peak load demands.

These changes are expected to have an impact on all our electricity and gas transmission networks. In particular, they will require significant investment in our UK electricity and gas transmission networks, while in the US new transmission investment, asset replacement and renewable power developments will require increasing investment in our US electricity transmission and distribution networks.

Figure 1 – Energy transportation in the UK

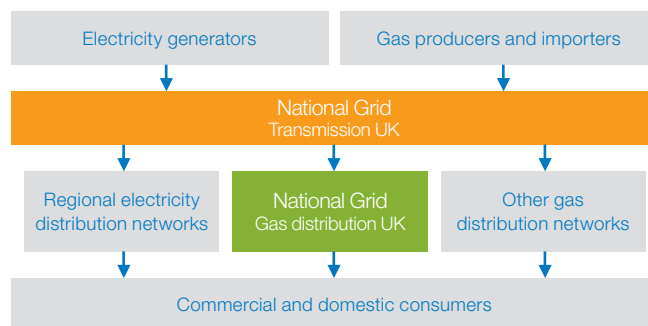


Figure 2 – Electricity transportation in the US

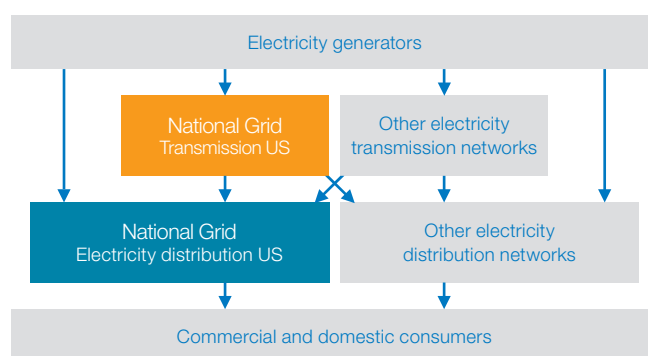
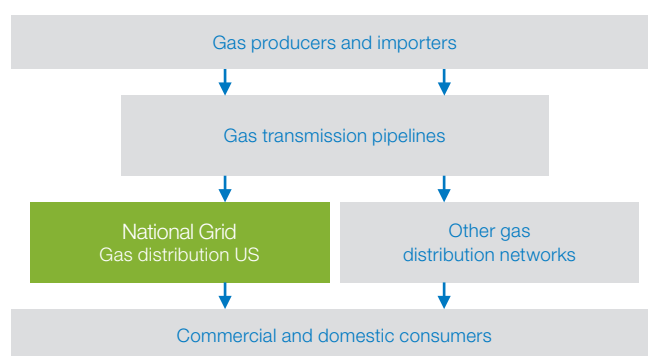


Figure 3 – Gas transportation in the US



Regulatory environment

Utility regulation

Due to our position in, and importance to, the economies we serve, our electricity and gas transmission and distribution businesses are subject to UK, European Union and US federal and state laws and regulations. Therefore, we have a number of regulators, each of which exercises power over how we operate within their respective jurisdictions.

Our principal market regulators and associated rate plans and price controls are illustrated opposite and can be summarised as follows:

UK

In the UK, energy networks are regulated by the Office of Gas and Electricity Markets (Ofgem). Ofgem operates under the direction and governance of the Gas and Electricity Markets Authority and has established price control mechanisms that restrict the amount of revenue that can be earned by regulated businesses.

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

US

In the US, public utilities are regulated by the Federal Energy Regulatory Commission (FERC) and by utility commissions in each of the states, including the New York Public Service Commission, the Massachusetts Department of Public Utilities, the Rhode Island Public Utilities Commission and the New Hampshire Public Utilities Commission. These US regulators set service standards, approve an allowed cost base, determine cost recovery and allowable levels of return and approve mergers and acquisitions of public utilities. The FERC also regulates public utility holding companies, including the US businesses of National Grid.

We have four electricity rate plans and nine sets of gas rates, covering our electricity distribution operations in upstate New York, Massachusetts, Rhode Island and New Hampshire and our gas distribution networks in upstate New York, New York City, Long Island, Massachusetts, New Hampshire and Rhode Island. Our electricity rate plan in upstate New York also covers our electricity transmission network in that state. The rates for our electricity transmission network in New England are subject to federal regulatory approval.

Our rate plans are designed to produce a specific allowed return on equity, by reference to an allowed cost base and an agreed regulatory asset base. Some rate plans include earned savings mechanisms that allow us to retain a proportion of the savings we achieve through improving efficiency, with the balance benefiting customers. We are also permitted to recover commodity and other pass-through costs which we incur, together with the recovery of stranded costs.

We have regulatory arrangements that provide for the recovery of our historical investments in generating plants that were stranded when some of our US subsidiaries divested their generation business as part of the industry restructuring and wholesale power deregulation process in New England and New York, and the recovery of certain above market costs of commodity purchase contracts that were in place at the time of restructuring and deregulation. We recover most of these costs through the rates charged to electricity customers. This revenue stream will decline as the recovery of stranded costs is completed.

Our reliability performance under certain rate plans is subject to performance targets established by the relevant regulator, under which we may be subject to monetary penalties in cases where we do not meet those targets.

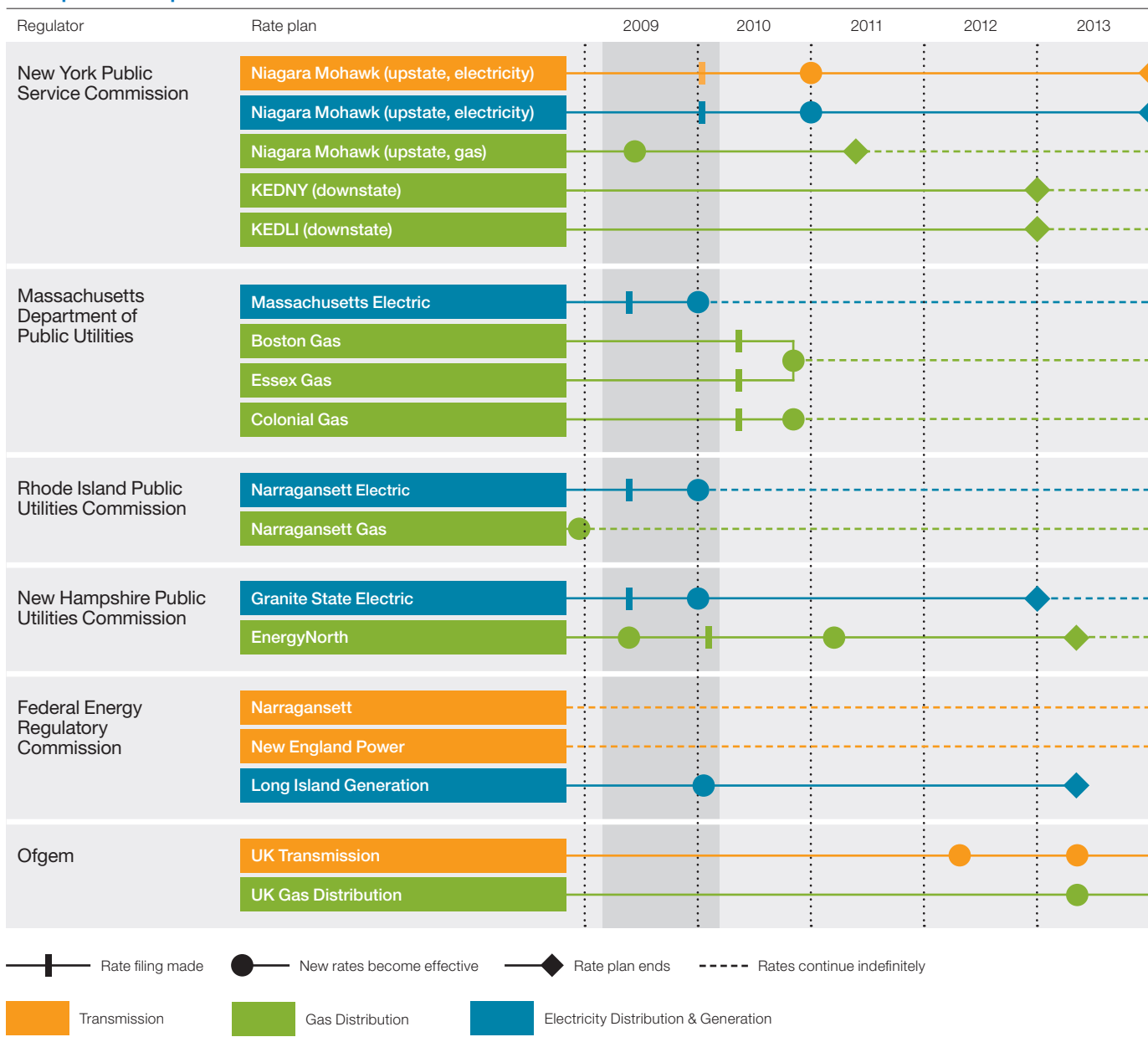
More information about the regulatory environments in which we operate, and on the nature of our rate plans and price controls, is provided in each of the regulated business sections on pages 46 to 53 (Transmission), 54 to 61 (Gas Distribution) and 62 to 69 (Electricity Distribution & Generation).

Other regulation

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

As a public company with shares and other securities listed on both the London and New York stock exchanges, we are also subject to regulation by the UK Financial Services Authority, the US Securities and Exchange Commission and the exchanges themselves.

Rate plans and price control calendar



Energy policy, regulatory and other developments

UK and European energy policy

In May 2007, the UK government published a white paper entitled Meeting the Energy Challenge. This document set out the government's strategy to address the issues of climate change and the UK's increasing reliance on imported fuel. The strategy includes: carbon dioxide (CO₂) emission reductions of about 60% by 2050; security of supply; competition in energy markets in the UK and overseas; and adequate and affordable heating for every home.

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

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

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

US energy policy

At the federal level, the Obama administration and Congress have focused on new energy and environmental legislation in two main areas: the economic stimulus bill; and emerging comprehensive climate and energy legislation. The \$787 billion American Recovery and Reinvestment Act, passed in February 2009, has significant provisions for the energy industry. The Act provides funding for the expansion of the electricity transmission network with focus on smart grid development, a broad array of energy efficiency programmes, clean fuel transportation incentives and research and development programmes.

The current Congress has made considerable progress on comprehensive climate change legislation. The American Clean Energy and Security Act passed significant cap and trade legislation out of the House of Representatives in the summer of 2009 and the Clean Energy Jobs and American Power Act was passed out of the Senate Environment and Public Works Committee later that year. There has been a bipartisan effort to craft legislation to cover not only climate change and greenhouse gas reductions, but also energy security language that would enhance domestic energy supplies from nuclear power to offshore oil and gas drilling. In President Obama's 2010 State of the Union address, he expressed his vision of a 17% goal in reduction of greenhouse gas emissions by 2020 and 80% by 2050.

Regulatory developments

UK and European regulatory developments

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

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

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

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

US regulatory developments

The principal US regulatory policy developments continue to focus on reducing carbon emissions, through significant increases in energy efficiency and the development of renewable generation. At the state level, regulatory commissions and other policymakers are pursuing carbon reduction targets by requiring reductions in electric load growth, increasing the deployment of utility energy efficiency programmes and mandating renewable generation. Revenue decoupling mechanisms, to address disincentives to utility companies implementing energy efficiency programmes, have been proposed. Massachusetts and New York regulatory bodies have instructed utilities to file decoupling proposals as part of their next rate plans. There is also an increasing interest in exploring the deployment by utilities of smart grid technologies.

Price controls and rate plans

UK price controls

The price controls for the UK electricity and gas transmission businesses were due to be reviewed during 2010 and 2011 but, as noted above, they have been delayed by a year and are now expected to be implemented in April 2013. We were subject to one year system operator price controls for our electricity and gas transmission operations for 2009/10 and new one year controls have been agreed for 2010/11.

US rate plans

In New York, we were granted a 10.2% return on equity (ROE) with a \$39.4 million revenue increase for the upstate gas business, effective from 20 May 2009.

In New Hampshire, the Public Utilities Commission issued a rate order for the gas distribution business allowing a 9.54% ROE and a revenue increase of approximately \$5 million, effective from 29 May 2009. For retail customers this decision resulted in a reduction in bills from the temporary rates set on 24 August 2008. We filed a Motion for Reconsideration to appeal the ROE determination but the Commission denied our motion. On 26 February 2010, we filed a further rate increase proposal seeking an 11.2% ROE. A decision is expected in January 2011.

In Massachusetts, the electricity distribution business was granted a revenue increase of \$42 million effective from 1 January 2010 with an additional \$24.1 million to be recovered over the subsequent four year period to recover storm costs. The Commission approved a 10.35% ROE. The Massachusetts rate case decision also allows for revenue decoupling, annual reconciliation of commodity related bad debt expense and pension expense, and a capital tracker to recover investment in the network up to \$170 million.

In Rhode Island, the Public Utilities Commission approved a revenue increase of \$23.5 million for the electricity distribution business with rates effective from 1 March 2010, retroactive to 1 January 2010. We were granted a 9.80% ROE with a capital structure of 42.75% common equity. We have submitted a filing to the Rhode Island Supreme Court requesting that the court hear our appeal of the Commission's decision and we plan to file a rate case later this year. For information on new rate plans filed, but not yet agreed by the regulators, see page 33.

For details of a rate adjustment in our power supply agreement with the Long Island Power Authority, see page 64.

Legal and related matters

An update on the ongoing Metering competition, gas distribution mains replacement reporting and KeySpan Department of Justice investigations that were reported in last year's Annual Report and Accounts is provided on pages 80 and 81. On 18 March 2010, a putative class action was commenced in New York against KeySpan and Morgan Stanley in relation to a financial swap transaction. Further details of this are also provided on page 81.

Other developments

We are currently evaluating options to allow us to exit our gas and electricity businesses in New Hampshire.

Financing developments

On 19 May 2010, the Board resolved to offer a fully underwritten rights issue to raise approximately £3.2 billion, net of expenses. The proceeds are expected to be used to fund a portion of our capital investment programme and for general corporate purposes. The capital raised will allow us to significantly increase our capital investment in the UK and assist in maintaining single A credit ratings for our UK operating companies, thereby improving our long-term competitive position.



Graeme Steele (above left), National Grid's European Policy and Interconnectors Manager, signs the foundation deed to create the European Network of Transmission System Operators – Gas.

European policy

In July 2009, the European Commission's third legislative package of energy proposals was passed. Among other things, this legislative package creates formal transmission system operator bodies for both gas and electricity. These bodies are charged with developing technical and commercial rules for cross border trading and producing 10 year network development plans. Through Board representation and working level resources, National Grid has established key roles in both organisations. Going forward, we see these organisations and the wider package of legislation as leading to greater cooperation and coordination with our neighbours in northwest Europe.

External relationships

We aim to enhance our relationships with all our external stakeholders including investors, customers, regulators, governments, suppliers and the communities we serve.

Responsibility

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

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

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

In 2009/10, there were 13.6 substantiated breaches of the Standards per 1,000 employees compared with 11.3 in 2008/09 and 11.6 in 2007/08. Offences include such things as fraud, internet and email abuse, drugs and alcohol abuse, and misuse of company vehicles and other assets. We take all breaches very seriously and disciplinary action can range from a verbal warning to dismissal.

In our 2010 employee survey, 66% (2009: 66%) of respondents considered something would be done if they reported an inappropriate business practice or an ethical issue.

We continue to enjoy external acknowledgment of our responsible business approach. In June 2009, we became one of only seven Business in the Community Platinum Plus companies, recognising our long-term commitment to operating responsibly.

The Responsibility section of our website provides performance data on a wide range of environmental, employee, economic and social issues. It also sets out our approach to assuring the corporate responsibility information and data in this report and our other public corporate responsibility reporting.

Investors

Our aim is to ensure the value of our business is fully reflected in our share price. We aim to make National Grid attractive to investors so we can finance our operations as effectively as possible.

In 2009/10, the prevailing economic conditions led to the cancellation of many investor conferences on the utilities conference calendar, but during the year we conducted over 230 investor meetings in the UK and Europe and 228 investor meetings in the US, maintaining a presence at 3 UK and European conferences and at 8 North American conferences. We presented to 11 broker sales teams, held 2 US regulatory updates and 1 UK site visit for analysts and investors.

We also presented to debt investors in the major European financial centres as well as across the US.

We operate a shareholder networking programme, the aim of which is to allow shareholders to gain a better understanding of the business. The programme includes visits to operational sites and presentations by senior managers and employees.

Customers

We aim to treat customers with respect, to communicate clearly with them, and to make their interactions with us as straightforward as possible. We aim at all times to provide a safe, reliable and efficient service to our customers.

We have a very wide range of customers, including: electricity generators and gas shippers; new developers from nuclear to wind, wave and tidal power; gas storage operators; local distribution companies; and approximately 19 million industrial, commercial and domestic consumers.

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

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

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

In the US, we implemented a new customer organisational model during the final quarter of the year, designed to increase our ability to deliver our customer objectives. The new organisation has been designed to be market driven and focused on delivering integrated energy solutions to our customers across all lines of business. For more information, see page 32.

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

Regulators

Our regulators, both in the UK and the US, are concerned with ensuring we can and do provide a safe, reliable and efficient service to our customers. Our ability to deliver that service, and to deliver returns to our investors, depends on our relationships with those regulators.

Our focus on customer service and operational excellence is a critical component of building trust with our regulators. This involves being responsive to the needs of our regulators for high quality information, complying with rules and regulations, operating in an ethical way, responding constructively to consultations and, most importantly, delivering on our promises. In the UK, we continue to work very closely with Ofgem on the renewal of our electricity transmission, gas transmission and gas distribution networks, and on expanding those networks to meet new and changing demand.

In the US, we are committed to maintaining strong relationships with our regulators at the state and federal levels. We want to ensure we deliver on our regulatory commitments, bring benefits to our customers, and shape the future regulatory agenda to deliver a clean energy economy. To that end, we have established a dedicated federal regulatory affairs team in Washington, D.C.

Suppliers

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

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

The World Resource Institute/World Business Council for Sustainable Development has developed proposals for a Scope 3 greenhouse gas emission reporting protocol. We have been selected to participate in a worldwide pilot study to road test the new protocol. We are also participating in the Carbon Disclosure Project's supply chain initiative where we will be assessing the greenhouse gas emissions of 144 of our top suppliers.

Given the scale of carbon emissions from our UK construction activities, we have undertaken pilots to develop carbon life cycle analysis tools. Working with our alliance partners, we have been driving innovation and sharing best practice in green build techniques and materials management.

We believe small businesses power the economy by creating jobs and contributing to the financial stability of our communities. It is the aim of our US supplier diversity programme to effectively expand business opportunities through outreach, purchasing exchanges and creating powerful partnerships with diverse suppliers to reach our long-term growth objectives. To help increase our base of qualified suppliers we have developed partnerships with numerous organisations that identify and/or certify suppliers.

Communities

We want to be welcomed and seen as a valued partner in the communities we serve. We will prioritise our community investment in areas where we have a business interest as well as knowledge and expertise to share.

Over the last year, we have implemented our new community impact framework.

We have continued to engage more employees in our community volunteering. Our partnership with Special Olympics Great Britain has been very successful with an 82% increase in volunteer hours in company time compared with 2008/09. A small group of our employees have been mentoring athletes. Some of the athletes spoke at the National Summer Games opening ceremony in Leicester, an event to which we sent a team of volunteers for the week. We also sponsored the Torch Run on its journey around the country. In the US, our employees have been involved in various volunteering opportunities, including Earth Day and Junior Achievement.

We continue to use the London Benchmarking Group model (for more information see www.lbg-online.net) to provide a framework for measuring and reporting our community investment contributions. In 2009/10, we invested £11 million (2008/09: £10 million; 2007/08: £9 million) in support of community programmes across our operations.

In our 2010 employee survey, 63% (2009: 64%) of respondents considered National Grid makes a positive contribution to the communities in which we operate.



Investment recovery programme

Our US investment recovery and recycling programme helps us reduce waste and save money by reusing, selling or recycling assets. From electrical and gas equipment to office material and scrap, in 2009/10 we processed over 11,000 tonnes of material. As well as environmental and financial benefits, the programme brings social advantages. Working in partnership with Monarch Industry and Seven Hills Foundation, it provides adults with physical and mental disabilities the opportunity to experience the work environment by performing a variety of tasks.

Vision, strategy and objectives

Vision

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

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

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

Strategy

Our strategy is a medium-term step in the journey to achieve the vision – what we will be doing over the next few years.

We will build on our core UK and US, electricity and gas, regulated business base and financial discipline to deliver sustainable growth and superior financial performance.

It is also the overarching principle that provides commercial context to each of the objectives.

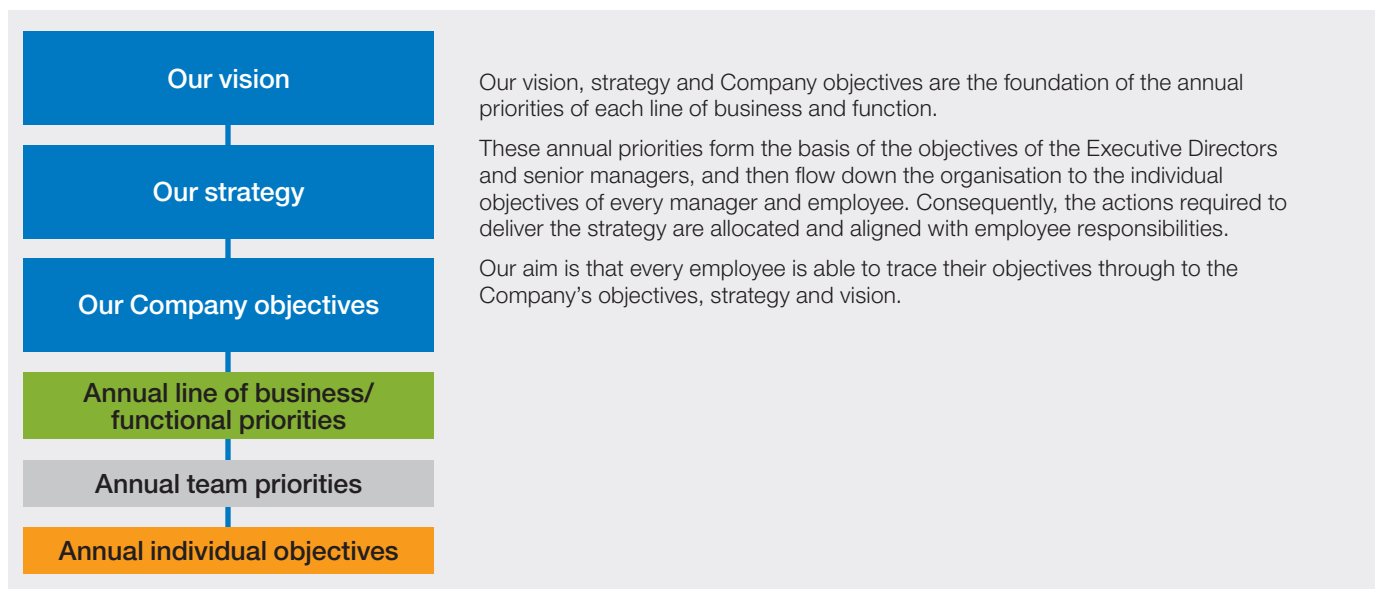
Company objectives

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

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

Line of sight

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



Delivering the future through our strategy

We recognise that the geographic areas in which we operate present different challenges, and therefore the implementation of the strategy has a different focus in the UK than in the US. The details of how we plan to deliver the strategy in each region are outlined below and the alignment of the headline priorities of each business segment is illustrated in the diagram.

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

to ensure climate change targets and security of supply requirements are met, while delivering acceptable and timely rates of return.

In the US, we will focus on filing rate plans and achieving appropriate outcomes, while also addressing our cost base. We will grow through core business customer growth, and asset replacement and network reinforcement. In developing the future US policy and regulatory framework, we will continue to drive towards achieving rate plans that deliver fair rates of returns, along with operating and capital cost recovery. We will continue to push for decoupling and the extension of energy efficiency programmes. We will also seek to achieve forward-looking rate plans, together with trackers for key areas of increase and volatility such as capital expenditure, pensions and bad debts. We also aim for rate plans to include remuneration for climate change initiatives such as smart grid, solar and transmission projects to connect renewables.

UK strategy Investment led organic growth	Transmission UK	<ul style="list-style-type: none"> → Delivering a step change in asset replacement of our transmission infrastructure → Delivering major new infrastructure investment to facilitate low carbon targets in the UK
	Gas Distribution UK	<ul style="list-style-type: none"> → Improving operating efficiency, safety and customer satisfaction through Gas Distribution front office (see page 58) → Successfully defending our position through the next price control review
US strategy Resetting the baseline and focus on growth from core	Transmission US	<ul style="list-style-type: none"> → Delivering on regulatory agreed ageing asset renewal programmes securing improved safety and reliability in our networks
	Gas Distribution US	<ul style="list-style-type: none"> → Delivering rate plans and closing performance gaps → Delivering growth through new connections and mains replacement/reinforcement → Improving customer satisfaction
	Electricity Distribution & Generation	<ul style="list-style-type: none"> → Delivering rate plans and closing performance gap → Delivering new processes and cost efficiencies that benefit customers and enhance alignment across the US business → Positioning ourselves as a utility of the future

Values

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

Responsibility

Our vision, strategy and Company objectives are underpinned by our commitment to corporate responsibility. We will operate to the highest standards of corporate governance and conduct our business in an ethical and sustainable manner.

Business drivers, risks and opportunities

Business drivers

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

Price controls and rate plans

The prices we charge for use of our electricity and gas transmission and distribution networks are determined in accordance with regulatory approved price controls in the UK and rate plans in the US. These arrangements include incentive and/or penalty arrangements. The terms of these arrangements have a significant impact on our revenues.

Multi-year contracts

Revenues in our Long Island electricity distribution and generation operations are subject to long-term contracts with the Long Island Power Authority. In addition, revenues in our Grain LNG importation terminal are determined by long-term contractual arrangements with blue chip customers.

People

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

Risks and opportunities

There are a number of risks that might cause us to fail to achieve our vision or to deliver growth in shareholder value. We can mitigate many of these risks by acting appropriately in response to the factors driving our business. The principal risks are described here. For more detail on risks, see pages 93 to 95.

Regulatory settlements and long-term contracts

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

Financial performance

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

Talent and skills

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

Objectives

We have developed the Company strategy and objectives to address the key business drivers and risks, ensuring we manage the business appropriately so as to mitigate risks and optimise opportunities. For more detail on objectives, see pages 24 and 25.

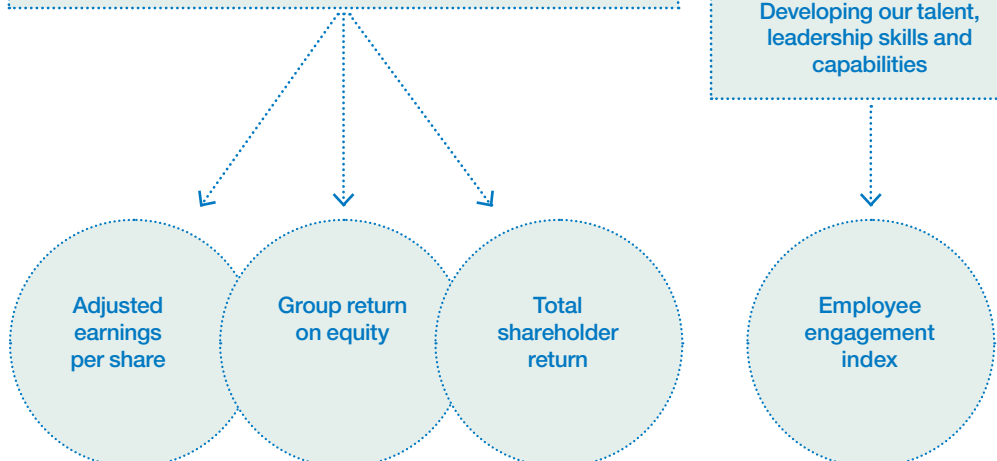
Delivering strong, sustainable regulatory and long-term contracts with good returns

Building trust, transparency, and an inclusive and engaged workforce

Developing our talent, leadership skills and capabilities

Key performance indicators (KPIs)

We use a variety of performance measures to monitor progress against our objectives. Some of these are considered to be key performance indicators and are set out here. For more detail on performance, see pages 28 to 45.



Capital investment

Capital investment is a significant driver for organic growth. In our regulated energy networks, the prices we charge include an allowed return for capital investment determined in accordance with our price controls and rate plans. Capital investment in non-regulated assets allows us to develop new revenue streams or to increase revenues from existing assets.

Safety, reliability and efficiency

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

Relationships and responsibility

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

Other investment

Investment in new businesses is also a significant driver of growth, provided we can create value through operational improvements, synergies and financial benefits. Disposals can crystallise value for shareholders, where the price on offer is better than the long-term return we can obtain ourselves or where a business does not fit with our principal operations.

Investment in our networks

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

Safety, reliability and customer service

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

Efficiency

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

Sustainability and climate change

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

Expanding our capabilities and identifying growth opportunities

Identifying, evaluating and acquiring new businesses that build on our core regulated operations are important. If we are unable to acquire businesses with the correct strategic fit it may restrict our future sustainable growth and our ability to increase shareholder value. The acquisition of new businesses is dependent on our ability to fund transactions through internal cash flows or the issuance of new debt or new shares.

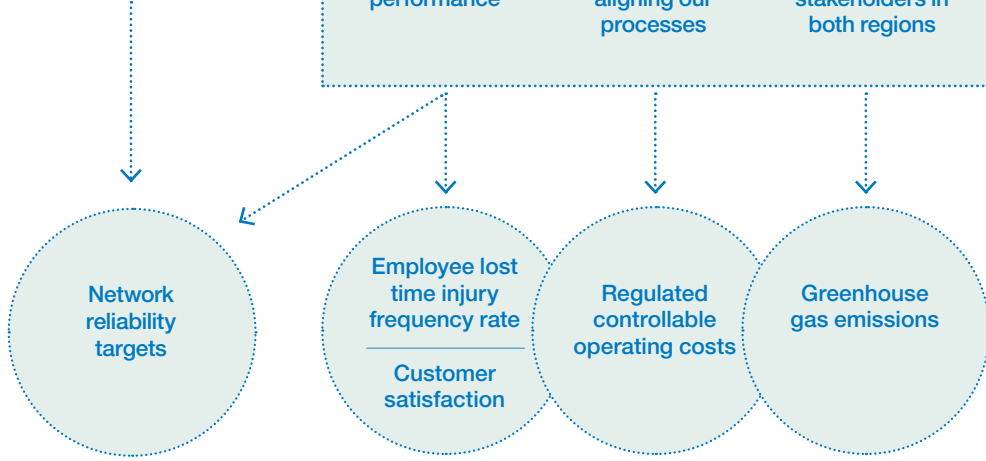
Modernising and extending our transmission and distribution networks

Driving improvements in our safety, customer and operational performance

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

Positively shaping the energy and climate change agenda with our external stakeholders in both regions

Expanding our capabilities and identifying new financeable opportunities to grow



Key performance indicators (KPIs)

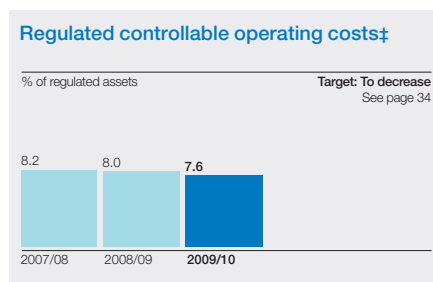
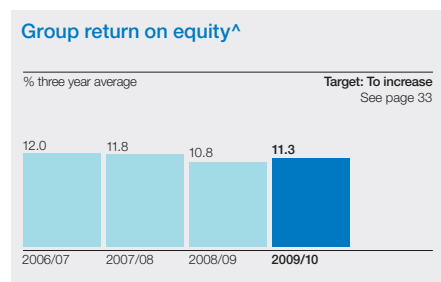
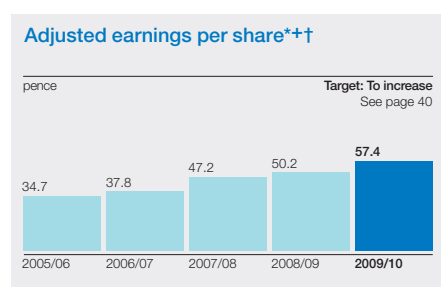
Financial KPIs

Company strategy and objectives	Financial KPIs	Definitions
Sustainable growth and superior financial performance	Adjusted earnings per share	Adjusted earnings* divided by the weighted average number of shares
	Total shareholder return	Growth in share price assuming dividends are reinvested
Delivering strong, sustainable regulatory and long-term contracts with good returns	Group return on equity	Adjusted earnings* with certain regulatory based adjustments divided by equity
Becoming more efficient through transforming our operating model and increasingly aligning our processes	Regulated controllable operating costs	Regulated controllable operating costs as a proportion of regulated assets

Our performance and the progress we have made against our strategic aims and against the objectives we have set ourselves are described below and on the following pages. Commentary on our overall financial results can be found on pages 38 to 45, and information on the performance and financial results of each line of business is set out on pages 46 to 73.

We measure the achievement of our objectives both through the use of qualitative assessments and through the monitoring of quantitative indicators. To provide a full and rounded view of our

business, we use non-financial as well as financial measures. Although all these measures are important, some are considered to be of more significance than others, and these more significant measures are designated as KPIs. Our financial and non-financial KPIs are highlighted here. KPIs are used as our primary measures of whether we are achieving our principal strategic aims of sustainable growth and superior financial performance. We also use KPIs to measure our performance against our objectives; the relationships between the objectives and the KPIs is explained above.



* Adjusted earnings excludes exceptional items, remeasurements and stranded cost recoveries
 † 2007/08 data includes continuing operations acquired with KeySpan for the period from 24 August 2007 to 31 March 2008 or as at 31 March 2008
 ^ 2007/08 results include KeySpan operations on a pro forma financial performance basis assuming the acquisition occurred on 1 April 2007
 ‡ Comparative data has been restated for the impact of the scrip dividend issues
 † Comparative data has been restated to present information on a consistent basis with the current year

Non-financial KPIs

Company objectives	Non-financial KPIs	Definitions
Modernising and extending our transmission and distribution networks	Network reliability targets	Various definitions appropriate to the relevant line of business
Driving improvements in our safety, customer and operational performance	Customer satisfaction	Our position in customer satisfaction surveys
	Employee lost time injury frequency rate	Number of employee lost time injuries per 100,000 hours worked on a 12 month basis
Building trust, transparency and an inclusive and engaged workforce	Employee engagement index	Employee engagement index calculated using responses to our annual employee survey
Positively shaping the energy and climate change agenda with our stakeholders in both regions	Greenhouse gas emissions	Percentage reduction in greenhouse gas emissions against our 1990 baseline

Network reliability targets

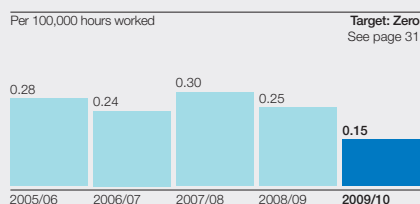
	Performance					Measure	Target
	05/06	06/07	07/08	08/09	09/10		
Electricity transmission – UK	99.9999	99.9999	99.9999	99.9999	99.9999	%	99.9999
Gas transmission – UK	100	100	100	100	100	%	100
Gas distribution – UK	99.999	99.999	99.999	99.9999	99.999	%	99.999
Electricity transmission – US	348	259	437	266	147	MWh losses	<253
Electricity distribution – US	141	121	110	114	114	Mins of outage	<122

See pages 50, 58 and 66 for additional details on network reliability

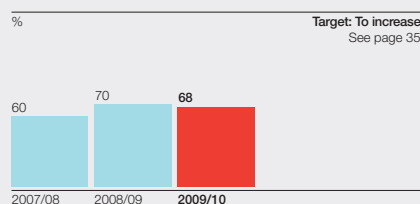
Customer satisfaction

	Performance		Measure	Target
	08/09	09/10		
Gas Distribution – UK	4th quartile	Not yet available	Quartile ranking	To improve
Gas Distribution – US: Residential	4th quartile	3rd quartile	Quartile ranking	To improve
Gas Distribution – US: Commercial	3rd quartile	2nd quartile	Quartile ranking	To improve
Electricity Distribution & Generation: Residential	4th quartile	4th quartile	Quartile ranking	To improve
Electricity Distribution & Generation: Commercial	4th quartile	3rd quartile	Quartile ranking	To improve

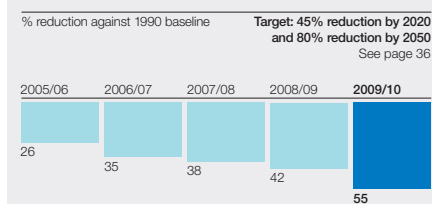
Employee lost time injury frequency rate



Employee engagement index



Greenhouse gas emissions~#



~ 2007/08 restated due to improved baseline data relating to KeySpan. Previously published figure excluding KeySpan was 30%

Our greenhouse gas emissions for 2009/10 are not fully verified at the date of this Report. Fully verified data will be published on our website in July 2010

Performance against our objectives

We use a number of detailed performance measures in addition to the key performance indicators (KPIs) shown on pages 28 and 29, reflecting the scale and complexity of our operations. We use qualitative assessments to judge progress against our objectives in areas where numerical measures are less relevant.

Changes to key performance indicators

We reported last year that we were developing a new KPI to monitor our performance on customer service. In order to measure the degree to which customers are satisfied with the service we provide, we have introduced a KPI with five components: Ofgem's UK gas distribution customer satisfaction score and the four J.D. Power and Associates customer satisfaction surveys in the US.

Ofgem requires the 8 gas distribution networks (GDNs) in Great Britain to carry out 3 types of quarterly customer satisfaction survey, covering planned works, unplanned works and connections. Respondents are asked to rate their level of satisfaction with the service provided by the GDN on a 10 point scale, where 1 is very dissatisfied and 10 is very satisfied. We calculate the average overall score for the 4 GDNs we own, compare our scores to those of the other GDNs, and report this as a component of the new KPI.

J.D. Power, an independent marketing information firm, produces a wide range of surveys of customer satisfaction, including four relating to US utilities. We use our positions in these surveys as the other components of the new KPI.

Last year, we included regulated controllable operating costs as a KPI. While this remains an important measure, and we continue to report it (see page 34), in view of our aim of building on our regulated asset base to deliver sustainable growth, we believe it is more informative to compare those costs to our total regulated assets to measure our efficiency as the business grows. We have therefore changed the KPI this year to measure our regulated controllable operating costs as a proportion of our regulated assets (regulated asset value in the UK and rate base in the US).

Performance measures and strategy

Our strategy is stated on page 24. Our performance in implementing the key elements of the strategy is measured in the following ways.

We will build on our core UK and US electricity and gas regulated business base...

We invest in our existing business in order to improve efficiency and reliability and to support our targeted dividend growth. We will also consider acquisitions in these core areas, but only where we believe we can derive added value for our investors.

Our KPIs in this area, as shown on pages 28 and 29, are total shareholder return and network reliability. Other performance measures include capital investment (see page 33), and dividend growth (see page 38).

...and financial discipline...

We seek to control operating costs, and to invest capital only where we expect to be able to obtain an acceptable return. We are committed to maintaining a single A range credit rating at the UK operating company level.

Our KPI in this area, as shown on page 28, is regulated controllable operating costs presented as a proportion of regulated assets. Other performance indicators include the vanilla return for UK businesses (see pages 50 and 57), regulatory return on equity for US businesses (see pages 50, 57 and 66), and interest cover (see page 74).

...to deliver sustainable growth...

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

Our KPIs in this area, as shown on page 29, are customer satisfaction, employee lost time injury frequency rate, employee engagement index and greenhouse gas emissions. Other performance measures include measures of gender and ethnic mix, and a number of qualitative measures, including the number of significant direct environmental incidents and value of environmental fines, together with our participation in bodies such as the RPI-X@20 advisory panel.

...and superior financial performance.

We aim to deliver superior returns to our investors, and to ensure that the value we create is reflected in our share price.

Our KPIs in this area, as shown on page 28, are total shareholder return and adjusted earnings per share. Other performance measures include adjusted operating profit for the year (see pages 38 and 41) and operating cash flows (see pages 44 to 45). A full discussion of our financial performance can be found on pages 38 to 45.

Driving improvements in our safety, customer and operational performance

We aim for operational excellence by performing to the highest standards of safety and reliability, and by improving customer service.

Safety

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

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

Employee safety

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

2009/10 saw a significant reduction in our lost time injury frequency rate to 0.15 compared with 0.25 in 2008/09 and 0.30 in 2007/08. The number of lost time injuries was 86 in 2009/10 compared with 140 in 2008/09 and 157 in 2007/08. Definitions for lost time injury and lost time injury frequency rate are included in the glossary on page 187.

The principal causes of lost time injuries are road traffic collisions, musculoskeletal injuries and slips, trips and falls. We have implemented targeted programmes during the year to change behaviours in these areas and drive performance improvements. In our 2010 employee survey, 74% (2009: 74%) of respondents felt confident that safety concerns or issues raised would be addressed and 76% (2009: 76%) of respondents considered that National Grid never compromises safety in order to meet other goals.

Contractor safety

We believe everyone who works for us is entitled to high levels of safety, whether they are a direct employee or employed by one of our contract partners. In 2009/10, there were 85 contractor lost time injuries compared with 108 in 2008/09 and 105 in 2007/08 (see figure 1). When developing safety improvement programmes, we ensure our contract partners are actively involved and believe there is a mutual benefit in sharing good practice and learning.

Public safety

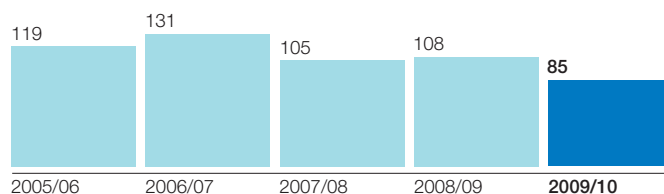
The safety of the public in the communities we serve is of prime importance to us. In 2009/10, 44 members of the public were injured as a result of our activities compared with 52 in 2008/09 and 36 in 2007/08 (see figure 2). A single incident, involving a gas explosion in a property in Shrewsbury, UK, caused 12 of these injuries. Our gas main replacement programme, the purpose of which is to reduce the safety risk relating to older metallic main, is described on page 57.

Process safety

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

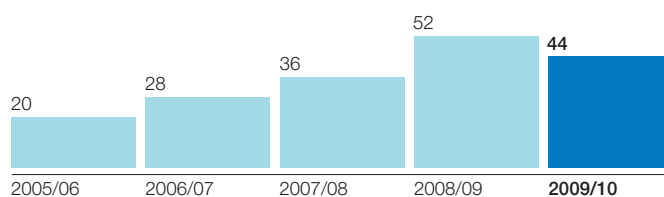
Process safety incidents are relatively rare and often have catastrophic consequences. As such, counting the number of incidents is not a good indicator of performance.

Figure 1 – Contractor lost time injuries Number Target: Zero



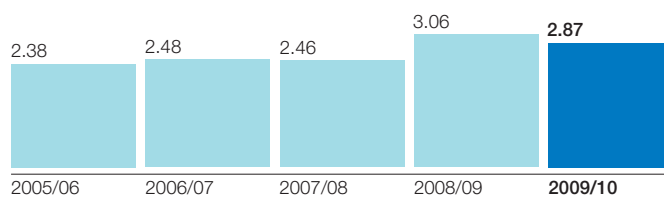
Data prior to 2008/09 excludes KeySpan.

Figure 2 – Injuries to members of the public Number Target: Zero



Data prior to 2008/09 excludes KeySpan. Includes fatalities, injuries requiring the person to attend hospital and, in the UK, any other injuries reportable under the Reporting of Injuries, Diseases and Dangerous Occurrences Regulations (RIDDOR).

Figure 3 – Employee sickness absence rate % Target: Zero



Data prior to 2008/09 excludes KeySpan.

Performance against our objectives continued

During 2009/10, we have continued to develop and report comprehensive leading and lagging indicators to measure that we have process safety risks under control. These indicators are regularly reviewed by the Executive Committee to ensure controls are in place and plans developed to close any gaps. The Health and Safety Executive was encouraged by the significant progress made in developing, reporting and embedding KPIs within the business. We have also worked to raise awareness of process safety throughout the Company, with training courses and communications to all employees.

In January 2010, we carried out a process safety culture survey with our employees, repeating a series of questions from a survey in 2008. This showed improvements in most areas over the two years and highlighted areas on which to concentrate for the future.

Employee health

Over the year, our sickness absence rate decreased to 2.87% compared with 3.06% in 2008/09 and 2.46% in 2007/08 (see figure 3 on page 31). The gathering and structuring of absence data has improved to provide more accuracy and detail. This helps to develop our health and wellbeing programmes.

This year, all employees have had an opportunity to engage with our health and wellbeing programmes. These are provided to make sure we create a healthy working environment that supports and encourages good lifestyle choices at work and at home. Through our occupational health programme, we continue to monitor the health of our 11,500 field based engineers ensuring the protection of their health from work activities and their fitness for work.

In the US, to date over 7,500 employees, supervisors and managers have completed a behavioural change programme for soft tissue injury prevention. This programme provides a framework to avoid musculoskeletal injuries and make sure employees understand how to maintain and improve their physical resilience.

In the UK, approximately 1,440 employees, including more than 500 field engineers, have taken up the option to review their lifestyle based on the results of a cardiovascular risk assessment. This has been supported by providing broad access to health kiosks and related workshops on nutrition and diet. The outcome of these reviews is that 300 employees have been referred to their family doctor for further medical investigation and support, while all employees in the programme were advised of their cardiovascular risk score and provided with a report detailing specific lifestyle improvements that would benefit them.

Across the Company, 5,500 employees took part in and completed the summer activity campaign Shape Up National Grid, a 12 week interactive team event that combined a weight management programme with an exercise and pedometer challenge.

The work being undertaken on health was recognised at this year's UK National Business Awards where we reached finalist status in the Health and Wellbeing category.

The business impact of these programmes is difficult to quantify at this stage but is expected to help improve employee performance and productivity, employee engagement levels and attendance.

Reliability

Our principal operations are critical to the functioning of the economies we serve. The reliability of our energy networks is one of our highest priorities after safety.

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

We use business specific reliability performance indicators to measure our reliability performance. More information on the reliability of each of our businesses is included in the business sections on pages 50, 58 and 66.

Customer service

We aim to impress our customers with the quality of the services we provide, with our responsiveness when things go wrong and with our dedication to continued improvement.

As noted on page 22, in the US we have implemented a new customer organisational model. The new structure consists of two groups: customer energy solutions and customer service operations.

Customer energy solutions provides customers across all lines of business with one source for all their energy needs by integrating all products and services we offer to them into one group, including energy efficiency. The Company uses its marketing and energy product expertise to deliver energy solutions that allow customers to manage their energy choices and reduce their impact on the environment. It is divided into three functions: market strategy and implementation, including focused and targeted communications; energy products, providing product expertise and regulatory support to develop new products; and energy solutions delivery, maintaining relationships with larger customers and an important local presence in our communities.

Customer service operations focuses on delivering the highest quality end-to-end experience for our customers at the lowest possible cost. It is divided into four functions: revenue cycle management, responsible for processes from billing to collection and performance metrics; customer care, providing the primary point of contact for customers through call centres and customer offices; business technology, managing short- and long-term technology priorities to ensure quality customer service; and workforce management, planning and analysis.

Improvements made during the year included: the acceptance of credit cards for bill payment; implementation of a web based outage communication tool; innovative energy efficiency campaigns; enhanced communications related to our tree trim customer programme; focus on community presence in all our operating areas; and self service website enhancements.

We are already seeing an improvement in our customer satisfaction in the US. Our rankings in the four J.D. Power and Associates customer satisfaction surveys have improved. We will continue to build upon this improvement while staying focused on the delivery of outstanding customer service.

In our 2010 employee survey, 54% (2009: 57%) of our employees believed National Grid is a good company for customers to do business with.

Further information on our customer service during the year is provided within each of the business sections on pages 50, 57 and 66.

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

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

Our group return on equity KPI allows us to monitor our performance in generating value from the investments we make. Return on equity is calculated by dividing our annual return by our equity base. Our annual return consists of earnings before exceptional items, remeasurements and stranded cost recoveries, adjusted for a number of regulatory based items including regulatory depreciation, retail price index (RPI) inflation on our UK regulatory asset value (RAV), and a pension deficit adjustment. Our equity base consists of invested capital less opening net debt. Invested capital is the opening UK RAV inflated to mid year using RPI linked inflation, plus opening US invested capital excluding stranded cost assets and assets disposed in the year, plus the closing net book value of assets and liabilities of UK based non-regulated businesses, corporate activities and joint ventures. Opening net debt is adjusted for significant individual transactions during the year such as disposal proceeds and share buybacks.

We monitor our performance using a three year average return rather than a return for a specific year. We believe this provides a better measure of our ongoing performance because it helps to reduce short-term fluctuations due to temporary market conditions such as inflation volatility. For 2009/10, our three year average return on equity was 11.3%, compared with 10.8% in 2008/09 and 11.8% in 2007/08. The increase in the year was primarily driven by an increase in UK inflation to 4.4% for the year to 31 March 2010, compared with -0.4% for the previous year.

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

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

We are actively participating in Ofgem's review of the current RPI-X based regulatory framework, which is discussed on page 20. In addition to our responses to the various consultation documents, we are also participating in the four industry working groups that Ofgem have established: innovation, investment, financing, and consumers. Ofgem anticipate that the outcome of the project will be published towards the end of 2010. It will not have any impact on the present price control, other than necessitating a one year adapted rollover of the existing price control, but it is expected that its conclusions will feed through into the review for the price control commencing April 2013.

In the US, we continue to make progress in setting new rates and moving the regulatory agenda forward. Over 60% of our asset base has had new rates since 2008. Under these new rate plans we have increased our US revenue by over \$190 million per annum. We have an aggressive rate case agenda focused on increasing revenue to ensure we are recovering all costs to operate the utilities in the US and on employing innovative rate making mechanisms to ensure we get timely recovery of costs which enable us to earn fair returns for investors.

On 29 January 2010, we filed a three year rate plan for our upstate New York electricity business requesting an initial revenue increase of \$369 million and a return on equity of 11.1%. Additionally, the filing seeks approval of a capital tracker which will provide timely recovery of our investment in the network, revenue decoupling and annual reconciliation mechanisms for certain non-controllable costs. This filing is unique in that it proposes to increase delivery revenue but mitigate the rate impact on retail customers' bills by offsetting the revenue increase with a decline in the stranded cost charges on the bills.

In Massachusetts, we filed a new rate plan for the three gas distribution companies requesting a total revenue increase of \$106 million with a return on equity of 11.3%. As in other cases, we are requesting approval of revenue decoupling, an infrastructure investment tracker, annual true-up mechanisms for commodity bad debt and pension costs, and an annual inflation adjustment factor. A decision is expected by 1 November 2010, with rates effective from that date.

In New Hampshire, we filed a new rate case for the gas distribution company on 26 February 2010. We are seeking an overall increase of \$11 million and a return on equity of 11.2%, which includes a 0.2% two year stay out premium. We proposed revenue decoupling, an expanded capital tracker, reconciling mechanisms for pensions and other post-employment benefits and for commodity related bad debt, and an inflation tracker on operations and maintenance costs.

Modernising and extending our transmission and distribution networks

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

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

Our capital investment plans reflect changing energy infrastructure requirements. Our capital investment programme in our regulated businesses usually takes place within defined regulatory frameworks that permit us to earn a return on allowed investments. Capital investment in our non-regulated businesses is based on the financial return we expect to generate.

Our planned total annual investment for 2010/11 is around £3.9 billion, including £0.2 billion in respect of investments in joint ventures.

More detail on capital expenditure is provided in the business sections on pages 51, 58, 67 and 71.

Expanding our capabilities and identifying new financeable opportunities to grow

We are committed to the growth of National Grid through organic capital expenditure and, where suitable opportunities are available, by the acquisition of new businesses.

In addition to the capital expenditure discussed above, we are actively investigating opportunities in relation to offshore

Performance against our objectives continued

transmission, possible electricity interconnectors with Belgium and with Norway, and carbon capture and storage technology.

We will consider acquiring new businesses in our core markets of electricity and gas delivery in the UK and US.

We use the aggregate consideration paid and debt assumed to monitor this investment in new businesses. There is no specific target because each investment is considered on its own merits. We also monitor synergy savings generated following an acquisition.

There have been no acquisitions during the last two years.

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

We aim to work as one company, operating to common core principles, standards and policies to deliver our vision.

As noted on page 30, we have amended our operating efficiency KPI to measure regulated controllable operating costs as a proportion of our total adjusted regulated asset base, reflecting the fact that our business is growing. This proportion has fallen to 7.6% in 2009/10 from 8.0% in 2008/09 and 8.2% in 2007/08.

In addition to the KPI, however, we continue to measure and report regulated controllable operating costs. We exclude the effects of inflation and bad debts, and present the figures on a constant currency basis, in order to be able to compare like-for-like. Regulated controllable operating costs decreased to £2,070 million in 2009/10, compared with £2,109 million in 2008/09 and £2,048 million in 2007/08.

We are organised by line of business and place primary accountability on them to meet our customer needs and regulatory obligations.

In Transmission, our common operating model project is developing a plan to prepare us for the challenges and opportunities between now and 2020. In Gas Distribution, our front office systems project aims to provide the tools to improve our performance, making them simpler to use and apply to improve our service to customers. In Electricity Distribution & Generation, we are implementing organisational design enhancements to improve our operating model and drive customer satisfaction and efficiency benefits.

Company wide functions, such as information systems and procurement, provide common strategy, policy and key processes to benefit from our scale and to drive improved consistency, efficiency and effectiveness.

Procurement

We are in the final stages of a programme to transform our procurement function. The programme has focused on developing our existing capability, and working in a more collaborative way with our business partners. We have successfully embedded a full strategic sourcing process within our global procurement operating model, which has enabled us to approach the market with an aggregated spend, encouraging us and our suppliers to work in a more aligned way.

Process improvement and technology have been at the forefront of the changes we have made. We have adopted an international system that gives us real time data on our procurement activities.

Business process outsourcing

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

Information services

We have initiated an information systems (IS) transformation programme to realise a world class global IS capability following a detailed review and benchmarking of current systems, costs and capability. The transformation involves moving from country based IS to operating at a global level with efficient shared service capabilities for solution and service delivery.

Programme objectives include: improved alignment between IS and businesses; a clear rolling strategy and architecture road map closely aligned to the wider business strategy; rationalisation and standardisation of applications; creation of solution centres of excellence; consolidation of data centres and networks and separation of critical national infrastructure systems; and leveraging of standard IS services such as email and intranet.

A new IS leadership team has been appointed and an organisational structure is being put in place. Alternative options for delivering core services are being examined including sourcing of parts of development, maintenance and infrastructure management. Significant investment is being made in building improved capabilities in business relationship management, strategy and architecture, security and risk management.

The next stages involve the completion of the sourcing assessment, and application rationalisation and virtualisation road map. The final decision on sourcing is dependent on the outcome of the assessment, and consultation with regulators, employees and unions will follow as appropriate. The transition to the new operating model will then take place starting with development in autumn 2010 through to service integration and infrastructure services in the first half of 2011.

Transmission and distribution alignment

A newly aligned electricity organisation was implemented in the US during the final quarter of 2009/10, bringing together transmission operations and delivery, electricity distribution operations and generation (transmission asset management, policy and commercial remain separate). US electricity operations are structured to provide improved customer focus and operating efficiencies through shared capabilities, enhanced regulatory relationships, reduced costs, increased productivity and better delivery of capital and maintenance work. In combining, we aim to deliver consistent processes as one single US electricity operations group under the leadership of the chief operating officer.

Building trust, transparency and an inclusive and engaged workforce

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

Employee engagement

In February 2010, we conducted our third annual employee survey. The response rate was the highest so far, with 97% of our employees taking part. Our employee engagement index, which measures how employees think, act and feel in relation to National Grid, declined slightly in 2010 to 68%, compared with 70% in 2009 and 60% in 2008.

Employees continue to believe National Grid's safety culture and supportive management are significant strengths, and they continue to receive favourable ratings. While we focused on reward for performance, vision and direction, and communication, our results slipped slightly in these categories.

In response to these results, we will continue to use line of sight to ensure greater clarity around vision and direction. We will also continue our focus on improved communication and engagement across all lines of the business.

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

Inclusion and diversity

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

As at 31 March 2010, 22.7% of our employees were female (see figure 4) and 13.5% were from ethnic minority groups (see figure 5). This compares with respectively 22.6% and 13.2% at 31 March 2009 and 22.5% and 12.3% at 31 March 2008.

To embed an inclusive culture, a number of training programmes were initiated during 2009. The Executive Committee and senior leadership team completed a full day of inclusion training. In December 2009, we launched an inclusive leadership programme for middle managers and, by April 2010, more than 750 managers had completed it. A learning module has also been built into our new employee orientation programme.

Our efforts have been recognised through a number of external awards including, for the second year running, the prestigious Stonewall Top 100 Employers in the UK and, for the third year in a row, the Human Rights Campaign's Equality Index in the US. We were also the recipient of Profiles in Diversity Journal's Innovation Award for its Women Empowered programme and Opportunity Now's Inclusive Culture award, recognising an initiative which is driving change at an organisational level.

In 2010, approximately 66% (2009: 70%) of respondents of the employee survey considered they were treated fairly by National Grid, while 78% (2009: 78%) of respondents considered that their colleagues treated them with respect and dignity.

We are fortunate to have employee resource groups focusing on a number of diversity strands including gender, ethnicity, faith, disability, sexual orientation and new hires. The groups successfully focused on delivering results in three areas: professional development opportunities for their members through workshops and learning sessions; supporting the Company's efforts in branding and community relations activities such as Special Olympics and recruiting events such as the Asian MBAs conference; and increasing overall understanding of inclusion through workshops and presentations.

97%

Employee survey response rate

68%

Employee engagement index

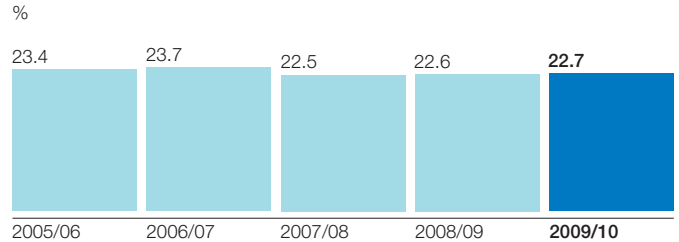
22.7%

Proportion of female employees

13.5%

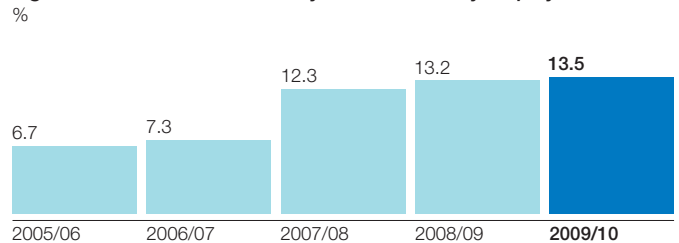
Proportion of ethnic minority employees

Figure 4 – Inclusion and diversity – female employees



Data prior to 2007/08 excludes KeySpan.

Figure 5 – Inclusion and diversity – ethnic minority employees



Data prior to 2007/08 excludes KeySpan.

Performance against our objectives continued

One of the challenges we continue to face is the retention of women and ethnic minorities. We are establishing an exit interview process to collect information that can be used to improve our retention efforts.

Developing our talent, leadership skills and capabilities

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

During the past year, and continuing into 2010/11, we have been creating targeted solutions to help employees at different points in their career maximise their performance. In 2009/10, approximately 740 front line leaders began foundations of leadership, a 15 month curriculum focused on critical foundational leadership skills; approximately 380 managers attended a one day workshop enabling them to better support their front line leaders through their development. Approximately 65 senior managers also attended a one week highly intensive and interactive development programme, expanding their understanding of the role they play in the broader National Grid; business acumen, collaboration and communication were key elements of the programme.

To complete our transitions development strategy, during 2010/11, we will be creating a development curriculum for middle managers. Underpinning this strategy is our personal effectiveness suite of solutions, which will be available to all employees, focused on a broad array of skills required to perform their roles more effectively. These flagship solutions serve as the framework for developing leaders at various levels within the Company.

Ensuring top quality technical skills is essential to our ability to operate, maintain and expand our infrastructure in a safe, reliable and efficient manner. In 2009/10, our workforce participated in over one million hours of training in the UK and US. During 2009/10, over 6,300 of our US workforce participated in annual expert training and received all of their regulatory and performance training and requalifications in a bundled approach. The programme includes all annual safety and regulatory compliance training, technical topic refreshers, and other discretionary training modules.

Our ability to continue to meet the varied learning needs and styles of our expanding and diverse employee population requires us to create quality development experiences and to deliver those experiences in highly effective and efficient ways. To this end, we are continuing to explore various learning technologies to enhance our learners' experience.

Positively shaping the energy and climate change agenda

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

We have continued to work with Ceres in the US and with the Worldwide Fund for Nature (WWF) in the UK to seek their views

on our internal and external efforts to reduce our climate change impacts and shape our positive influence on legislators and regulators. We will continue to press for ambitious national and international plans to tackle the causes and consequences of climate change as governments and others take stock of the outcome of the United Nations climate change conference COP15 in Copenhagen and build towards COP16 in Cancun, Mexico.

We have maintained our involvement with such programmes and organisations as the RPI-X@20 group and Aldersgate Group, in the UK and with the shaping of state climate change regulations in the US through our membership of the Clean Energy Group.

Climate change

We have further embedded our climate change initiative and increased our energy efficiency programmes, focusing on initiatives that are cost effective and regulated. We believe our 45% by 2020 and 80% by 2050 greenhouse gas emissions reduction targets to be industry leading within the UK and US.

Our greenhouse gas emissions for 2009/10 are not fully verified at the date of this Report. However, we estimate our Scope 1 and 2 emissions to be 8.8 million tonnes carbon dioxide equivalent, compared with 11.3 million tonnes in 2008/09 and 12.1 million tonnes in 2007/08 (assuming we had owned KeySpan for the entire year). This equates to a 55% reduction against our 1990 baseline, compared with 42% in 2008/09 and 38% in 2007/08. Fully verified data will be published in July 2010 in the responsibility section of our website, including an explanation of the large reduction in emissions compared with 2008/09 and its impact on our 2020 target.

Our 2020 and 2050 targets remain at the centre of our efforts to identify and implement measures to meet our commitment to safeguard our global environment for future generations. During 2009/10, each line of business developed five year plans for greenhouse gas reduction. The plans, adopted in April 2010, establish a trajectory to 2015 as the half way point to our 2020 target. Executive compensation is linked to performance against the plans.

We have developed a deeper understanding of our Scope 3 emissions and this is also reported on our Company website. We are participating in the World Resources Institute/World Business Council for Sustainable Development worldwide pilot study on Scope 3 emissions reporting and are one of the few utilities to do so. We will further evaluate the development of Scope 3 targets once this project is completed later in 2010.

We also recognise that customer energy efficiency is linked to the scale of our Scope 3 emissions. We have launched a campaign in the US, inviting consumers to commit to 3% year-on-year savings in their energy consumption over 10 years.

Our climate change initiative is being embedded in all areas and operations of the Company. For example, in UK construction we have undertaken pilots to develop carbon life cycle analysis tools. Working with our alliance partners, we have been driving innovation, sharing best practices in green build techniques and materials management.

In 2009, the UK government published the UK Low Carbon Transition Plan, which contained a revised assessment of carbon costs and concluded that the value of carbon used to appraise investments should be approximately doubled to £52 per tonne. We believe that a strong carbon price signal in the economy is essential to drive the right behaviours, so are evaluating the adoption of this revised value in our investment decision making processes across our operations.

It is equally important we understand the impact of past global emissions on future climate change. We have been working with the UK Met Office to understand how these changes might affect our UK and US infrastructure and future energy demand. Later in 2010, we will be one of the first companies to provide an adaptation report required under the UK Climate Change Act.

Protecting the environment

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

The number of significant environmental incidents in 2009/10 arising directly from our operations was 10, including zero contractor-related incidents (see figure 6), compared with 12, including 4, in 2008/09 and 34, including 25, in 2007/08.

Incidents outside our control resulting from third party or weather-related damage to our networks (see figure 7) were 2 compared with 1 in 2008/09 and 1 in 2007/08.

In the US, we received 4 environmental citations, compared with 6 in 2008/09 and 6 in 2007/08, but attracted no fines.

In our 2010 employee survey, 59% (2009: 62%) of respondents considered National Grid acts responsibly in all its business dealings, including environmental management.

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

We also take seriously the issues that surround electric and magnetic fields. We recognise that there is scientific uncertainty as to whether the electric and magnetic fields that are produced by some of our assets have an effect on health or not, and that this produces public concern. We monitor the science carefully but we look to relevant independent bodies such as the World Health Organization and the UK's Health Protection Agency for authoritative advice. In all our operations, as a minimum, we aim to comply with the relevant regulations, guidelines or practices in force in the different jurisdictions in which we operate. In addition, we actively support high-quality research and open communication (including a website at www.emfs.info) and we look for more constructive and less confrontational ways of handling this issue. All these activities are governed by our public position statement on electric and magnetic fields, which we review annually.

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

3%

Targeted annual energy reduction by US customers over the next 10 years

8.8m tonnes

Estimated Scope 1 and 2 greenhouse gas emissions

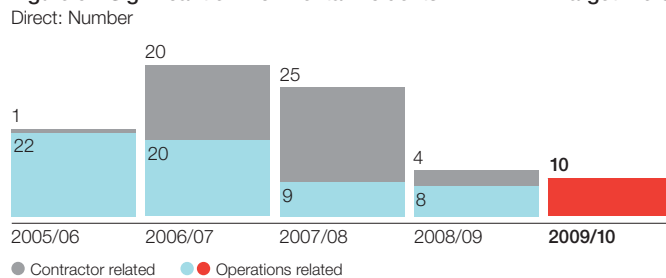
45% by 2020

Greenhouse gas emissions reduction target

80% by 2050

Greenhouse gas emissions reduction target

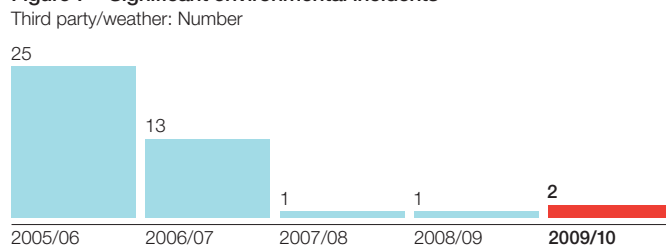
Figure 6 – Significant environmental incidents Target: Zero



Data prior to 2008/09 excludes KeySpan.

There were zero contractor related environmental incidents arising directly from our operations in 2009/10.

Figure 7 – Significant environmental incidents



Data prior to 2008/09 excludes KeySpan.

Financial performance

Financial results

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

Shareholder returns

We aim to increase our dividend each year so that shareholders receive an appropriate level of return on their investment in us. We also try to communicate with investors so that as much as possible of the value we create is reflected in our share price.

We measure total shareholder return as a key performance indicator (KPI) on a cumulative three year basis. The measure reflects changes in our share price and also assumes that dividends paid to shareholders over that period were reinvested in our shares. Cumulative total shareholder return for the period from 1 April 2007 to 31 March 2010 was -7%. This reflects the fact that equity prices generally fell sharply amid the turbulence in the financial markets during 2007/08 and 2008/09, and the recovery during 2009/10 has been insufficient to reverse the effect of those falls.

Dividends in respect of the financial year

The proposed total ordinary dividend for 2009/10 amounts to £951 million or 38.49 pence per ordinary share. This represents an increase of 8% over the previous year's ordinary dividend per share of 35.64 pence.

	2010	2009	2008	2007	2006
Dividends	pence	pence	pence	pence	pence
Interim	13.65	12.64	11.70	10.90	10.20
Final	24.84	23.00	21.30	17.80	15.90
Total	38.49	35.64	33.00	28.70	26.10

Dividends per ADS	\$	\$	\$	\$	\$
Interim	1.15	0.95	1.21	1.03	0.88
Final	1.77	1.74	2.05	1.76	1.51
Total	2.92	2.69	3.26	2.79	2.39

The total ordinary dividend per share was covered 1.5 times by adjusted earnings from continuing operations per ordinary share (2008/09 covered 1.4 times, 2007/08 covered 1.4 times) and covered 1.5 times by earnings per ordinary share from continuing operations (2008/09 covered 1.0 times, 2007/08 covered 1.8 times).

The dividend table shows the ordinary dividends paid or payable by National Grid for the past five financial years. These dividends do not include any associated UK tax credit in respect of such dividends, and represent the gross dividends declared whether settled in cash or by new shares.

For the final dividend of 2008/09, and subsequent dividends, shareholders were offered the option of a scrip dividend, whereby they could elect to receive the dividend in the form of new shares rather than cash. The uptake of the scrip dividend option represented 25% and 20% of the total final 2008/09 and interim 2009/10 dividends respectively. Shareholders are again being offered the option of a scrip dividend this year.

Dividends expressed in dollars per American Depositary Share (ADS) in the table above reflect the amounts paid or payable to ADS holders, rounded to two decimal places.

In accordance with IFRS, the final dividend proposed in respect of each financial year is reported in the financial statements for the subsequent year. As a consequence, the final dividend proposed

to shareholders for 2009/10 of 24.84 pence per share, amounting to approximately £615 million (assuming all dividends are settled in cash), will be reported in the financial statements for the year ending 31 March 2011.

Financial discipline

In order to deliver sustainable growth, we must be disciplined in the way we manage our balance sheet. The principal measure we use to monitor financial discipline is interest cover, being a measure of the cash flows we generate compared with the net interest cost of servicing our borrowings.

Our long-term target range for interest cover is between 3.0 and 3.5. Interest cover for the year ended 31 March 2010 was above our target range, increasing to 3.9 from 3.1 for the year ended 31 March 2009 (year ended 31 March 2008: 3.2). The primary reasons for the increase in 2009/10 were decreased interest expense on our index-linked debt, due to lower inflation, combined with higher levels of cash inflows from operations during the year. This was partially offset by a decrease in interest received in 2009/10 compared with prior year.

In 2006, we committed to return approximately \$1.9 billion cash between calendar years 2006 and 2011 to shareholders through a share repurchase programme based on the after-tax cash flows generated from the recovery of stranded costs in the US. Following the successful disposal of our UK wireless infrastructure operations for £2.5 billion on 3 April 2007, we announced the return of a further £1.8 billion to shareholders. We repurchased £0.6 billion of our shares in 2008/09 and £1.5 billion in 2007/08, which, together with the £0.2 billion repurchased in 2006/07, totals £2.3 billion of returns to shareholders through share repurchases.

In 2008/09, we took the decision to suspend our share repurchase programme in response to the turbulent financial environment and uncertain conditions in the capital markets.

Profit, cash flow and dividends

If we achieve our objectives we should be able to deliver continued improvements in financial performance, so that we deliver on our commitment to increase our dividend by 8% each year to 2011/12.

The KPI we use to monitor our financial performance is adjusted earnings per share. Adjusted earnings per share is basic earnings per share before exceptional items, remeasurements and stranded cost recoveries.

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

Continuing and discontinued operations

The financial results of our businesses and segments and of our other activities (as described on page 14) are presented within continuing operations. There were no discontinued operations in 2009/10. For details of our discontinued operations in previous years, see page 41.

Measurement of financial performance and use of adjusted profit measures

In considering the financial performance of our businesses and segments, we analyse each of our primary financial measures of operating profit, profit before tax, profit for the year attributable to equity shareholders and earnings per share into two components comprising; firstly, business performance, which excludes

exceptional items, remeasurements, stranded cost recoveries, and amortisation of acquisition-related intangibles; and secondly, exceptional items, remeasurements, stranded cost recoveries and amortisation of acquisition-related intangibles. Exceptional items, remeasurements, stranded cost recoveries, and amortisation of acquisition-related intangibles are excluded from the measures of business performance used by management to monitor financial performance as they are considered to distort the comparability of our reported financial performance from year to year.

Measures of business performance are referred to in this Annual Report and Accounts as adjusted profit measures in order to distinguish them clearly from the comparable total profit measures of which they are a component. Adjusted operating profit, adjusted profit before tax, adjusted earnings and adjusted earnings per share differ from total operating profit, profit before tax, profit for the year attributable to equity shareholders, and earnings per share respectively by the exclusion of exceptional items, remeasurements, stranded cost recoveries, and amortisation of acquisition-related intangibles.

Exceptional items are items of income and expense that, in the judgement of management, should be disclosed separately on the basis that they are material, either by virtue of their nature or size, and are relevant to an understanding of our financial performance. Items of income or expense that are considered by management for designation as exceptional items include such items as significant restructurings, write-downs or impairments of non-current assets, significant changes in environmental or decommissioning provisions, the integration of acquired businesses, and gains or losses on disposals of businesses or investments.

Remeasurements comprise gains or losses recorded in the income statement arising from changes in the fair value of commodity contracts and of derivative financial instruments. These fair values increase or decrease as a consequence of changes in commodity and financial indices and prices over which we have no control. Stranded cost recoveries comprise income from additional charges that we are allowed to recover from certain of our US customers arising from the divestiture of generation activities in the late 1990s. Amortisation of acquisition-related intangibles arises from intangible assets, principally customer relationships, that are only recognised as a consequence of the accounting required for a business combination. Such amortisation distorts the comparison of the financial performance of acquired businesses compared with non-acquired businesses.

Adjusted profit measures are limited in their usefulness compared with the comparable total profit measures as they exclude important elements of our financial performance, namely exceptional items, remeasurements, stranded cost recoveries and the amortisation of acquisition-related intangibles. We believe that, in separately presenting our financial performance in two components, it is easier to read and interpret financial performance between periods, as adjusted profit measures are more comparable by excluding the distorting effect of exceptional items, remeasurements, stranded cost recoveries and amortisation of acquisition-related intangibles, and exceptional items, remeasurements, stranded cost recoveries, and amortisation of acquisition-related intangibles 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, amortisation of acquisition-related intangibles and stranded cost recoveries are also reflected in budgets and forecasts. Management compensates for the limitations inherent in the use of adjusted profit measures through the separate monitoring and disclosure of exceptional items, remeasurements, stranded cost recoveries and amortisation of acquisition-related intangibles as a component of our overall financial performance.

Exchange rates

Our financial results are reported in sterling. Transactions for our US operations are denominated in dollars and so the related amounts that are reported in sterling depend on the dollar to sterling exchange rate. As the average rate of the dollar at \$1.58:£1 in 2009/10 was weaker than the average rate of \$1.54:£1 in 2008/09, the same amount of revenue, adjusted operating profit and operating profit in dollars earned in 2008/09 would have been reported as £261 million, £27 million and £23 million lower respectively if earned in 2009/10. In 2007/08 the average rate was \$2.01:£1; if the revenue, adjusted operating profit and operating profit in dollars recognised in 2007/08 was earned in 2008/09 it would have been reported as £1,938 million, £260 million and £398 million higher respectively.

However, the effect of movements in the dollar exchange rate on adjusted operating profit and operating profit in 2009/10 was largely offset by the impact of interest and tax charges denominated in dollars, when translated into sterling. This includes the effect of derivative financial instruments that swap debt raised in other currencies into dollars as part of the financing of our US operations. As a result, adjusted profit for the year and profit for the year from continuing operations for 2008/09 would have been £7 million and £5 million lower respectively if translated at the 2009/10 average exchange rate of \$1.58:£1 (2007/08: £49 million and £137 million higher respectively if translated at the 2008/09 average exchange rate of \$1.54:£1).

The balance sheet at the end of the financial year has been translated at an exchange rate of \$1.52:£1 at 31 March 2010 (\$1.44:£1 at 31 March 2009).

Profit for the year from continuing operations

Profit for the year from continuing operations increased from £922 million in 2008/09 to £1,389 million in 2009/10 (decreased from £1,575 million in 2007/08 to £922 million in 2008/09) as a consequence of the changes in operating profit, net finance costs, exceptional finance costs and remeasurements, and taxation described in the following sections.

Details of the financial results of business segments and other activities are included in the business sections on pages 46 to 73.

Earnings and earnings per share from continuing operations

In accordance with IAS 33, all earnings per share amounts for comparative periods have been restated as a result of shares issued via scrip dividends.

Financial performance continued

Adjusted earnings

	Years ended 31 March		
	2010	2009	2008
	£m	£m	£m
Continuing operations			
Adjusted operating profit	3,121	2,915	2,595
Net finance costs excluding exceptional items and remeasurements	(1,155)	(1,150)	(770)
Share of post-tax results of joint ventures	8	5	4
Adjusted profit before taxation	1,974	1,770	1,829
Taxation excluding tax on exceptional items, remeasurements and stranded cost recoveries	(553)	(517)	(579)
Adjusted profit from continuing operations	1,421	1,253	1,250
	pence	pence	pence
Adjusted earnings per share from continuing operations	57.4	50.2	47.2

Earnings

	Years ended 31 March		
	2010	2009	2008
	£m	£m	£m
Continuing operations			
Total operating profit	3,293	2,623	2,964
Net finance costs	(1,108)	(1,234)	(786)
Share of post-tax results of joint ventures	8	5	4
Profit before taxation	2,193	1,394	2,182
Taxation	(804)	(472)	(607)
Profit from continuing operations	1,389	922	1,575
	pence	pence	pence
Earnings per share from continuing operations	56.1	36.9	59.5

Earnings per share from continuing operations

See figures 1 and 2 on page 41. The following table sets out the adjusted earnings per share and earnings per share from continuing operations for 2009/10, 2008/09 and 2007/08 and reconciles the differences between them. Reconciling items are net of tax.

	Years ended 31 March		
	2010	2009	2008
	£m	£m	£m
Continuing operations			
Adjusted earnings per share	57.4	50.2	47.2
Exceptional items	(10.9)	(9.9)	(0.1)
Commodity contract remeasurements	1.7	(10.7)	5.0
Derivative financial instrument remeasurements	(1.0)	(3.0)	(1.3)
Stranded cost recoveries	8.9	10.3	8.7
Earnings per share – continuing operations	56.1	36.9	59.5

Adjusted earnings per share for 2009/10 increased by 7.2 pence, an increase of 14% compared with 2008/09 (2007/08: increased by 3.0 pence, an increase of 6% compared with 2008/09).

Earnings per share from continuing operations increased from 36.9 pence per share in 2008/09 to 56.1 pence per share in 2009/10 reflecting the increase in adjusted earnings per share, combined with the lower net exceptional items, remeasurements and stranded cost recoveries on a per share basis (2008/09: decrease from 59.5 pence per share in 2007/08 to earnings of 36.9 pence per share).

Diluted earnings per share from continuing operations were 55.8 pence per share in 2009/10 (0.3 pence lower than basic earnings per share from continuing operations), compared with 36.6 pence per share in 2008/09 (0.3 pence lower) and 59.1 pence per share in 2007/08 (0.4 pence lower). The principal reason for the dilution in 2009/10, 2008/09 and 2007/08 relates to employee share plans.

Adjusted profit measures

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

a) Reconciliation of adjusted operating profit to total operating profit

	Years ended 31 March		
	2010	2009	2008
	£m	£m	£m
Continuing operations			
Adjusted operating profit	3,121	2,915	2,595
Exceptional items	(268)	(275)	(242)
Commodity contract remeasurements	71	(443)	232
Stranded cost recoveries	369	426	379
Total operating profit	3,293	2,623	2,964

Adjusted operating profit is presented on the face of the income statement under the heading operating profit before exceptional items, remeasurements and stranded cost recoveries. See figures 3 and 4 on page 41.

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

	Years ended 31 March		
	2010	2009	2008
	£m	£m	£m
Continuing operations			
Adjusted profit before taxation	1,974	1,770	1,829
Exceptional items	(301)	(275)	(242)
Commodity contract remeasurements	70	(445)	223
Derivative financial instrument remeasurements	81	(82)	(7)
Stranded cost recoveries	369	426	379
Total profit before taxation	2,193	1,394	2,182

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

c) Reconciliation of adjusted earnings to earnings (profit for the year from continuing operations attributable to equity shareholders of the parent company)

	Years ended 31 March		
	2010	2009	2008
	£m	£m	£m
Continuing operations			
Adjusted earnings	1,418	1,250	1,247
Exceptional items	(270)	(247)	(2)
Commodity contract remeasurements	42	(266)	133
Derivative financial instrument remeasurements	(25)	(74)	(35)
Stranded cost recoveries	221	256	229
Earnings	1,386	919	1,572

Adjusted earnings is presented in note 9 to the consolidated financial statements, under the heading adjusted earnings – continuing operations.

Discontinued operations

There were no discontinued operations during 2009/10.

During 2008/09, discontinued operations included the Ravenswood generation station, KeySpan Communications and KeySpan Engineering Associates, which were sold during the year. At 31 March 2008, all of these operations were classified as held for sale on the balance sheet and their results included in discontinued operations from their acquisition under KeySpan on 24 August 2007 to 31 March 2008. In addition during 2007/08, discontinued operations included our wireless infrastructure operations in the UK and the US and the electricity interconnector in Australia that we sold during 2007/08.

We sold the Ravenswood generation station for \$2.9 billion (£1.6 billion) on 26 August 2008.

Earnings per share from discontinued operations in 2008/09 was 1.0 pence per share, including 0.6 pence per share relating to gains on the businesses sold during the year, compared with 61.2 pence per share in 2007/08, including 59.8 pence per share relating to gains on the businesses sold during the year.

Profit and total earnings per share for the year

Profit for the year from both continuing and discontinued operations was £1,389 million in 2009/10, compared with £947 million in 2008/09 and £3,193 million in 2007/08.

Total earnings per share from both continuing and discontinued operations were 56.1 pence per share in 2009/10, 37.9 pence per share in 2008/09 and 120.7 pence per share in 2007/08.

Adjusted operating profit and operating profit

During 2009/10 and 2008/09 there were no acquisitions and therefore the results for continuing operations are comparable as both contain a full year of contributions from the former KeySpan operation.

For the year ended 31 March 2008, KeySpan was acquired on 24 August 2007 and consequently only contributed seven months of results for that period. During 2007/08, KeySpan contributed \$740 million and \$911 million to the adjusted operating profit and operating profit for continuing operations respectively. During 2008/09, a full year of KeySpan operations contributed \$855 million and \$313 million to the adjusted operating profit and operating profit for continuing operations respectively.

KeySpan's operations are highly seasonal, with higher revenue and operating profit in the second half of the year driven by the winter heating season. Therefore, during 2007/08 the results of KeySpan that were consolidated provide a larger contribution on a time apportioned basis compared with a full year's contribution.

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

£1,418m

Adjusted earnings

57.4p

Adjusted earnings per share

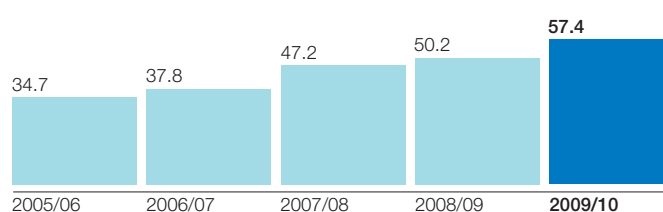
13%

Increase in adjusted earnings

14%

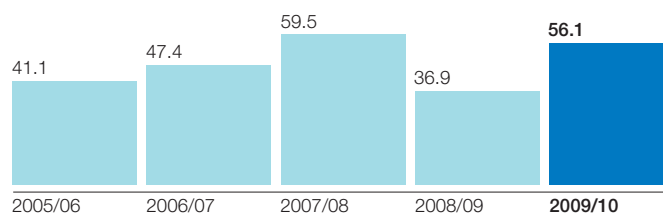
Increase in adjusted earnings per share

Figure 1 – Adjusted earnings per share from continuing operations
pence



Comparative data have been restated for the impact of the scrip dividend.

Figure 2 – Earnings per share for continuing operations
pence



Comparative data have been restated for the impact of the scrip dividend.

Figure 3 – Adjusted operating profit from continuing operations
£m

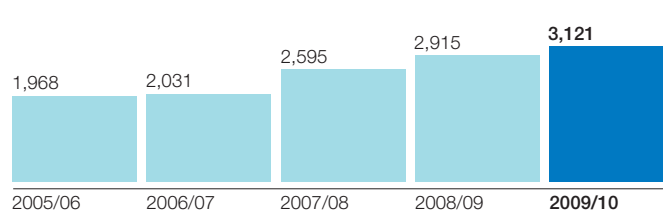
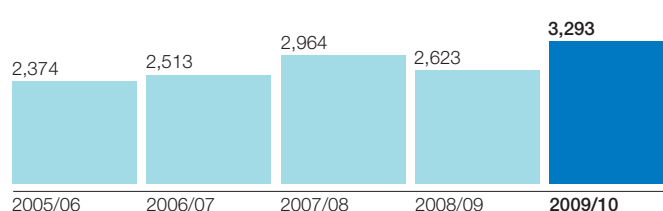


Figure 4 – Operating profit from continuing operations
£m



Financial performance continued

Revenue by operating segment

	Years ended 31 March		
	2010 £m	2009 £m	2008 £m
Continuing operations			
Transmission UK	3,460	3,487	2,956
Transmission US	405	420	299
Gas Distribution UK	1,517	1,466	1,383
Gas Distribution US	3,708	4,786	2,845
Electricity Distribution & Generation US	4,339	4,972	3,508
Other activities	738	719	642
Total segmental revenues	14,167	15,850	11,633
Less: sales between operating segments	(179)	(226)	(210)
Total	13,988	15,624	11,423

Segmental operating profit before exceptional items, remeasurements and stranded cost recoveries

	Years ended 31 March		
	2010 £m	2009 £m	2008 £m
Continuing operations			
Transmission UK	1,311	1,126	1,021
Transmission US	153	175	128
Gas Distribution UK	723	672	595
Gas Distribution US	414	612	392
Electricity Distribution & Generation US	374	265	330
Other activities	146	65	129
Adjusted operating profit	3,121	2,915	2,595

Segmental operating profit

	Years ended 31 March		
	2010 £m	2009 £m	2008 £m
Continuing operations			
Transmission UK	1,252	1,063	1,013
Transmission US	151	173	122
Gas Distribution UK	682	629	574
Gas Distribution US	448	226	487
Electricity Distribution & Generation US	701	531	696
Other activities	59	1	72
Operating profit	3,293	2,623	2,964

2009/10 compared with 2008/09

Changes in revenue and other operating income, operating costs and operating profit for 2009/10 compared with 2008/09 are summarised in the following table:

	Revenue and other operating income £m	Operating costs £m	Operating profit £m
Continuing operations			
2008/09 results	15,687	(13,064)	2,623
Add back exceptional items and remeasurements	–	718	718
Deduct stranded cost recoveries	(435)	9	(426)
2008/09 adjusted results	15,252	(12,337)	2,915
Exchange movements	(250)	223	(27)
2008/09 constant currency results	15,002	(12,114)	2,888
Transmission UK	(42)	227	185
Transmission US	(4)	(14)	(18)
Gas Distribution UK	50	1	51
Gas Distribution US	(957)	775	(182)
Electricity Distribution & Generation US	(459)	575	116
Other activities	(6)	87	81
Sales between businesses	47	(47)	–
2009/10 adjusted results	13,631	(10,510)	3,121
Exceptional items and remeasurements	–	(197)	(197)
Stranded cost recoveries	376	(7)	369
2009/10 results	14,007	(10,714)	3,293

Revenue and other operating income excluding stranded cost recoveries was £1,621 million lower than in 2008/09. This primarily reflected lower average commodity costs and delivery volumes in the US during 2009/10 compared with 2008/09 and a £250 million decrease as a result of exchange movements on our US operations. Due to the pass-through nature of our commodity costs in the US, revenues decrease if there is a fall in average commodity costs. This is not a contributing factor to the decrease in our US operating profit. Lower commodity delivery volumes in the US were primarily due to warmer weather.

There was a decrease of £44 million in other operating income, which primarily reflects a £21 million reduction in the sales of property by our property management business in the UK, and a £15 million decrease in our UK Transmission business.

The decrease in operating costs excluding exceptional items, remeasurements and stranded cost recoveries reflects a £224 million decrease as a result of exchange movements. Apart from the impact of exchange movements and lower average commodity costs, the other principal reasons for the decreased revenue and operating costs were: in Gas Distribution, decreased US regulatory income due to timing items driven by lower volumes and a one-off credit in the prior year, partially offset by higher UK regulated income; in Electricity Distribution & Generation, decreased costs reflected lower storm costs; and in Transmission, decreased UK costs reflected lower pass-through costs related to lower energy prices in 2009/10, while a small decrease in revenues primarily reflected lower interconnector capacity revenues.

Adjusted operating profit in 2009/10 was £206 million higher than 2008/09, comprising a £27 million decrease as a result of exchange movements on US operations and a net increase of £233 million from the movements in revenue, other operating income and operating costs on a constant currency basis.

Net operating exceptional charges of £268 million in 2009/10 primarily related to restructuring costs incurred in the UK and US, increases in environmental provisions resulting from changes in UK landfill tax legislation, as well as fines and provisions relating to legal action. The majority of the restructuring costs related to the ongoing KeySpan integration programme, restructuring of our LNG storage facilities, costs associated with initiatives related to the transformation of our operating model, and costs associated with outsourcing parts of our UK shared services organisation.

There were £71 million of operating remeasurement gains in 2009/10, compared with £443 million of losses in 2008/09. The gains relate to changes in the value of commodity contracts in the US carried in the balance sheet at fair value, primarily arising from movements in energy prices.

Stranded cost recoveries relate to the recovery of costs related to historical generation assets in the US that we no longer own. Such costs can be recovered from customers as permitted by regulatory agreements. Revenue and costs associated with stranded cost recoveries were £376 million and £7 million respectively (2008/09: £435 million and £9 million).

As a consequence of the increase in adjusted operating profit of £206 million, the net movement in operating exceptional items and remeasurements of £521 million and decrease in operating profit from stranded cost recoveries of £57 million, total operating profit increased by £670 million in 2009/10 to £3,293 million compared with £2,623 million in 2008/09.

2008/09 compared with 2007/08

Changes in revenue and other operating income, operating costs and operating profit for 2008/09 compared with 2007/08 can be summarised as follows:

	Revenue and other operating income £m	Operating costs £m	Operating profit £m
Continuing operations			
2007/08 results	11,498	(8,534)	2,964
Add back exceptional items and remeasurements	–	10	10
Deduct stranded cost recoveries	(382)	3	(379)
2007/08 adjusted results	11,116	(8,521)	2,595
Exchange movements	1,938	(1,678)	260
2007/08 constant currency results	13,054	(10,199)	2,855
Transmission UK	561	(456)	105
Transmission US	30	(22)	8
Gas Distribution UK	77	–	77
Gas Distribution US	1,068	(968)	100
Electricity Distribution & Generation US	454	(620)	(166)
Other activities	24	(88)	(64)
Sales between businesses	(16)	16	–
2008/09 adjusted results	15,252	(12,337)	2,915
Exceptional items and remeasurements	–	(718)	(718)
Stranded cost recoveries	435	(9)	426
2008/09 results	15,687	(13,064)	2,623

£3,121m

Adjusted operating profit

£3,293m

Operating profit

7%

Increase in adjusted operating profit

26%

Increase in operating profit

Financial performance continued

Revenue and other operating income excluding stranded cost recoveries was £4,136 million higher than in 2007/08. This primarily reflected a £1,938 million increase as a result of exchange movements on our US operations and the first full-year contribution from KeySpan.

In addition, due to the pass-through nature of our commodity costs in the US, revenues have increased during 2008/09 due to a rise in average commodity costs during 2008/09 compared with 2007/08. This has not resulted in an increase in our operating profit.

There was a decrease of £12 million in other operating income, which primarily reflects a £49 million reduction in the sales of property by our property management business in the UK, partially offset by a £30 million increase in our UK Transmission business and a net £7 million increase from the other regulated and non-regulated businesses.

The increase in operating costs excluding exceptional items, remeasurements and stranded cost recoveries reflects a £1,687 million increase as a result of exchange movements and the first full-year contribution from KeySpan.

KeySpan operations contributed £4,635 million of revenue and £4,084 million of costs excluding exceptional items, remeasurements and stranded cost recoveries in 2008/09, compared with £3,262 million and £2,782 million respectively in 2007/08, on a constant currency basis.

Apart from the impact of a full-year contribution from KeySpan and exchange movements the other principal reasons for the increased revenue and operating costs were: in Transmission, higher UK regulated revenue and interconnector auction income; in Gas Distribution, increased allowed regulatory revenue and increased revenue due to colder weather partially offset by higher bad debt costs; and in Electricity Distribution & Generation, increased revenue, storm costs and depreciation.

Adjusted operating profit in 2008/09 was £320 million higher than 2007/08, comprising a £260 million increase as a result of exchange movements on US operations and a net increase of £60 million from the movements in revenue, other operating income and costs on a constant currency basis.

Net operating exceptional charges of £275 million in 2008/09 primarily related to restructuring costs incurred in the UK and US and increases in environmental provisions resulting from significant movements in discount rates during the year. The majority of the restructuring costs related to the ongoing KeySpan integration programme, restructuring of our LNG storage facilities, and costs associated with initiatives related to the transformation of our operating model.

There were £443 million of operating remeasurement losses in 2008/09, compared with £232 million of gains in 2007/08.

Revenue and costs associated with stranded cost recoveries were £435 million and £9 million respectively (2007/08: £382 million and £3 million).

As a consequence of the increase in adjusted operating profit of £320 million, the net movement in operating exceptional items and remeasurements of £708 million and increase in operating profit from stranded cost recoveries of £47 million, total operating profit decreased by £341 million in 2008/09 to £2,623 million, compared with £2,964 million in 2007/08.

Net finance costs

Net finance costs excluding exceptional items and remeasurements was £1,155 million in 2009/10, compared with £1,150 million in 2008/09. The slight increase primarily reflected an increase in our net pension interest due to a fall in plan assets and lower expected returns on assets, partially offset by a lower effective interest rate due to lower RPI and LIBOR rates.

Net finance costs excluding exceptional items and remeasurements was £380 million higher in 2008/09 compared with £770 million in 2007/08. The increase was a consequence of higher average debt balances following the KeySpan acquisition, exchange movements and increased pension interest, partially offset by a lower effective interest rate reflecting lower floating and RPI linked rates.

Exceptional finance costs and remeasurements

There were £33 million of exceptional finance costs during 2009/10 relating to the early redemption of debt.

There were no exceptional finance costs in 2008/09 or in 2007/08.

Financial remeasurements relate to net gains on derivative financial instruments of £81 million (2008/09: losses £82 million; 2007/08: losses of £7 million) and the financial element of commodity contract revaluations, totalling £1 million (2008/09: £2 million; 2007/08: £9 million).

Taxation

A net charge of £804 million arose in 2009/10 comprising a £553 million charge on profit before tax excluding exceptional items, remeasurements and stranded cost recoveries, and a £251 million charge on exceptional items, remeasurements and stranded cost recoveries, compared with £472 million in 2008/09 (comprising a £517 million charge and a £45 million credit respectively) and £607 million in 2007/08 (comprising £579 million and £28 million charges respectively).

In 2009/10, exceptional items, remeasurements and stranded cost recoveries included a £41 million tax charge due to a change in US tax legislation under the Patient Protection and Affordable Care Act.

In 2008/09, exceptional items, remeasurements and stranded cost recoveries included a £49 million charge for increased deferred tax liabilities due to a change in the UK industrial buildings allowance regime. In 2007/08, it included an exceptional tax credit of £170 million relating to the release of deferred tax provisions arising from the change in the UK corporation tax rate.

The effective tax rates before and after exceptional items, remeasurements and stranded cost recoveries were 28.0% and 36.7% respectively (2008/09: 29.2% and 33.9%; 2007/08: 31.7% and 27.8%).

Cash flows

Cash flows from operating activities

See figure 5 on page 45. Cash generated from continuing operations was £4,372 million in 2009/10, compared with £3,564 million in 2008/09 and £3,265 million in 2007/08. This included cash outflows for continuing operations relating to exceptional items of £135 million, £131 million and £132 million respectively and cash inflows from stranded cost recoveries of £361 million, compared with £359 million and £278 million respectively.

After reflecting cash flows relating to discontinued operations and tax paid, net cash inflow from operating activities was £4,516 million, compared with £3,413 million in 2008/09 and £3,165 million in 2007/08. This included net corporate tax receipts amounting to £144 million in 2009/10 (which includes a £381 million refund resulting from a change in tax treatment on repairs expenditure in the US), £143 million tax payments in 2008/09 and £110 million payments in 2007/08.

Cash flows from investing activities

Cash outflows from investing activities were £2,332 million in 2009/10, compared with an outflow of £1,998 million in 2008/09 and an outflow of £3,023 million in 2007/08. There were no payments in respect of business acquisitions in 2009/10 and 2008/09, compared with £3,502 million spent on acquiring KeySpan in 2007/08.

Net proceeds from sales of financial investments were £805 million (2008/09: £99 million; 2007/08: £45 million). Proceeds from sales of subsidiaries, joint ventures and other investments were £6 million in 2009/10 (2008/09: £nil; 2007/08: £55 million).

Excluding acquisitions and disposals of financial investments, cash outflows for continuing operations decreased in 2009/10 by £9 million compared with 2008/09. Investing activities of discontinued operations were £nil in the period compared with a cash inflow of £1,049 million in 2008/09 (2007/08: £3,050 million inflow).

Cash flows from financing activities

Net cash outflows from financing activities were £2,212 million in 2009/10, compared with £877 million in 2008/09 and £1,592 million in 2007/08. This reflected net outflows from borrowings of £499 million (2008/09: £1,641 million inflow; 2007/08: £1,589 million inflow) and £7 million of share repurchases (2008/09: £627 million; 2007/08: £1,498 million).

Payments to providers of finance, in the form of interest and dividends, totalled £1,691 million in 2009/10 compared with £1,899 million in 2008/09 and £1,680 million in 2007/08.

Net interest cash outflows increased from £976 million in 2008/09 to £982 million in 2009/10 (increased from £694 million in 2007/08 to £976 million in 2008/09).

Dividends paid to shareholders decreased from £838 million in 2008/09 to £688 million in 2009/10 (increased from £780 million in 2007/08 to £838 million in 2008/09) reflecting that 25% and 20% of shareholders elected to take the final 2008/09 dividend and the interim 2009/10 dividend respectively in the form of a scrip dividend rather than cash.

£4,372m

Cash generated from operations

28.0%

Effective tax rate before exceptional items, remeasurements and stranded cost recoveries

23%

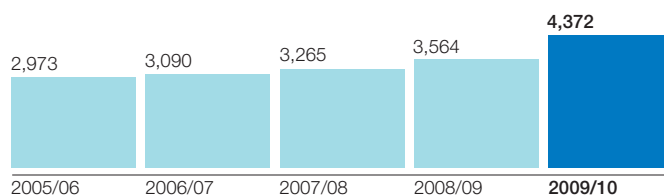
Increase in cash flows from operations

£688m

Dividends paid to shareholders in cash

Figure 5 – Operating cash flows

£m



Transmission



Adjusted operating profit

£1,464m

2008/09: £1,301m

Capital investment

£1,494m

2008/09: £1,441m

Employees

3,953

2008/09: 3,874

UK energy transmitted

1,436 TWh

2008/09: 1,454 TWh

This year we have delivered nearly £1.5 billion worth of electricity and gas projects to upgrade and reinforce ageing infrastructure and adapt our networks to cope with changing sources of energy.

Our fundamental priorities remain safety, reliability and efficiency. We have also created an enhanced line of sight from National Grid's objectives to Transmission's objectives and annual priorities.

We are focused on the long-term security of supply and environmental challenges arising from the transition to a low carbon economy.

This section should be read in conjunction with the rest of this Operating and Financial Review

Key Facts

- Circuit length of over 27,800 kilometres of electrical overhead line
- Over 850 kilometres of underground cable
- 286 TWh of electricity transmitted in the UK
- Over 7,600 kilometres of gas pipeline
- 1,150 TWh of gas throughput

About Transmission

Our Transmission business operates in both the UK and the US. As a consequence of the different economic and regulatory environments, we report the results of Transmission as two segments: Transmission UK and Transmission US.

Principal operations

Transmission UK

Electricity transmission owner

We own the electricity transmission system in England and Wales. Our electricity assets comprise a route length of over 7,200 kilometres of overhead line, mainly consisting of double circuits, about 713 kilometres of underground cable and 338 substations at 242 sites.

Electricity system operator

We are the national electricity transmission system operator, responsible for managing the operation of both the England and Wales transmission system that we own and also the two high voltage electricity transmission networks in Scotland, which we do not own. Day-to-day operation of the Great Britain electricity transmission system involves the continuous real-time matching of demand and generation output, ensuring the stability and security of the power system and the maintenance of satisfactory voltage and frequency. We are also designated as system operator for the new offshore electricity transmission regime.

Gas transmission owner

We own the gas national transmission system in Great Britain. This comprises approximately 7,600 kilometres of high pressure pipe and 23 compressor stations, connecting to 8 distribution networks and to third party independent systems for onward transportation of gas to end consumers.

Gas system operator

We operate the gas national transmission system. Day-to-day operation includes balancing supply and demand, maintaining satisfactory system pressures and ensuring gas quality standards are met.

French interconnector

We own and operate the UK assets, and a portion of the subsea cables, that comprise the electricity interconnector between England and France as part of a joint arrangement with the French transmission operator.

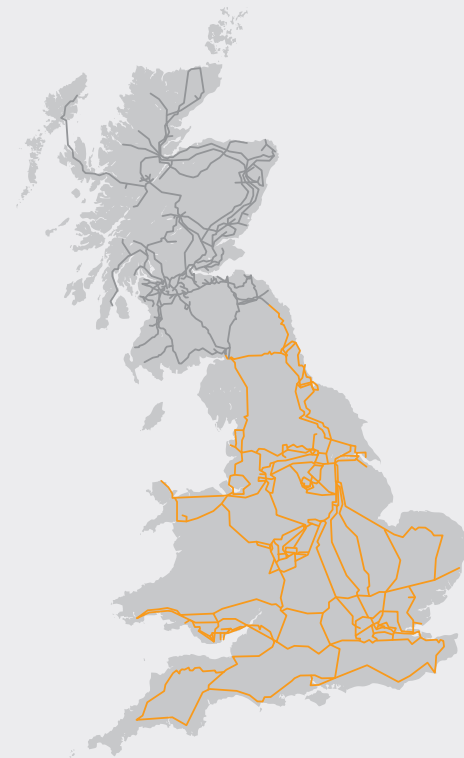
LNG storage

We own and operate three liquefied natural gas (LNG) storage facilities in Great Britain following the closure of Dynevor Arms during 2009.

As electricity transmission owner and gas transmission owner, we own and maintain the physical assets, develop the networks to accommodate new connections and disconnections, and manage a programme of asset replacement and investment to ensure the long-term reliability of the respective networks.

As electricity transmission system operator and gas transmission system operator, we undertake a range of activities necessary for the successful, efficient delivery of secure and reliable energy. In the case of electricity, this involves the continuous real-time balancing of supply and demand, and management of balancing services that include commercial arrangements with market participants that enable electricity demand or generation output to be varied. In the case of gas, we ensure the system supply and demand is balanced at the end of each day. We are also required to maintain levels of short-term gas reserves to ensure domestic and other non-interruptible gas supplies can be maintained during prolonged cold conditions.

Transmission UK – electricity system



Operational highlights 2009/10

- Currently upgrading transmission capacity connecting Scotland and England.
- Identification of substantial programme of further investment which will also help support UK government in meeting its climate change targets.
- Permanent strategies for mobile flood defences developed with deployment planned to start late 2010.
- London cable tunnels reinforcement work ongoing to secure supply.

— Scottish electricity transmission system
 — English and Welsh electricity transmission system

338

UK electricity substations

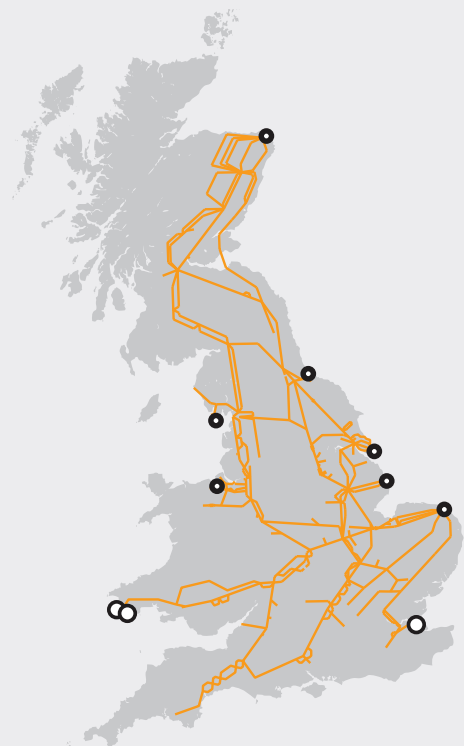
99.9999%

UK transmission electrical system reliability

£7.5bn

UK electricity transmission regulatory asset value

Transmission UK – gas system



Operational highlights 2009/10

- Started construction of Easington to Paull 26 km pipeline to facilitate gas supplies on the east coast.
- Started construction of Wormington to Sapperton 44 km pipeline to meet gas demand in southwest.
- Decommissioning of Bathgate, Peterstow and Scunthorpe compressor stations underway.
- Working with Scottish Power to develop CO₂ transportation in Scotland and with other parties to develop a carbon capture and storage solution in the Humber area.

— Gas transmission system
 ● Terminal
 ○ LNG terminal (on east coast Grain LNG, owned by National Grid, on west coast two terminals at Milford Haven, not owned by National Grid)

23

UK gas compressor stations

100%

UK gas transmission system reliability

£4.5bn

UK gas transmission regulatory asset value

Transmission continued

Transmission US

Electricity transmission owner

We own and operate an electricity transmission network of approximately 13,800 kilometres spanning upstate New York, Massachusetts, Rhode Island, New Hampshire and Vermont. Our US electricity transmission facilities operate at voltages ranging from 69 kV to 345 kV and comprise nearly 13,700 kilometres of overhead line, nearly 140 kilometres of underground cable and 525 substations.

We are the largest electricity transmission service provider in New England and New York by reference to the length of these high voltage transmission lines.

Canadian interconnector

We own and operate a 224 kilometre direct current transmission line rated at 450 kV that is a key section of an interconnector between New England and Canada.

As one of several transmission owners, we work with two distinct independent system operators (ISOs) in New England and New York. These non profit system operator entities for New England and New York are responsible for operating organised wholesale markets for energy, for operating reserves and capacity, for maintaining the operating reliability of the New England and New York networks, for coordinating the activities of the transmission owners, and for managing transparent expansion planning processes for transmission.

Regulation

Transmission UK

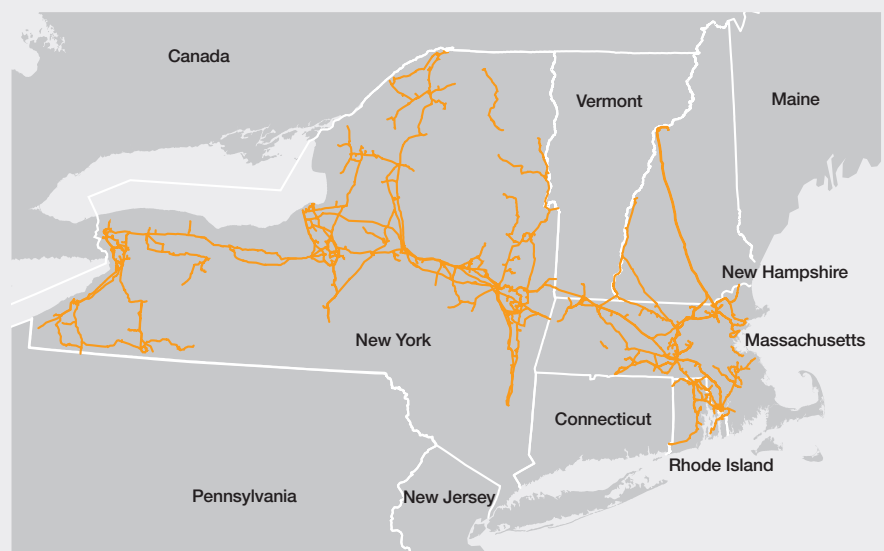
Through our subsidiary, National Grid Electricity Transmission plc, we are the sole holder of an electricity transmission licence for England and Wales. This licence also covers our role as system operator for the transmission networks in Great Britain. Under the Electricity Act 1989, we have a duty to develop and maintain an efficient, coordinated and economical system of electricity transmission and to facilitate competition in the supply and generation of electricity.

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

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

We accepted Ofgem's final proposals for the system operator schemes that applied to the year ended 31 March 2010 for both

Transmission US – electricity networks



— Electricity network

Operational highlights 2009/10

- Significant expenditure on asset replacement to increase system reliability.
- Capital investment delivered in New York in line with KeySpan merger commitment.
- New England East-West Solution (NEEWS) project is under way to enhance the transmission system in three states.
- Five year contract signed with the Northeast Power Alliance to support investment programme in New York.

525

US electricity substations

98.8%

US electricity system availability

\$1.1bn

US transmission rate base

Zero

Lost time injuries

gas transportation and electricity transmission. We also accepted their proposals for the one year schemes from 1 April 2010.

The key elements of the current price controls for both gas and electricity transmission are that we earn a 4.4% post-tax real rate of return on our regulatory asset value (equivalent to a 5.05% vanilla return), with a £4.4 billion baseline five year capital expenditure allowance and a £1.2 billion five year controllable operating expenditure allowance.

In addition, we are subject to a number of incentives that can adjust our transmission network revenue. For electricity transmission these include incentives for transmission network reliability, sulphur hexafluoride (SF₆) losses, efficiency and balancing services. For gas transmission, our incentive schemes cover areas such as the cost of investment for additional capacity to facilitate new connections to the system.

Transmission US

Revenue for our transmission business in New England and New York is collected from transmission customers, including from our Electricity Distribution & Generation business, pursuant to tariffs approved by state utility commissions and by the Federal Energy Regulatory Commission (FERC).

In New York, our current rates allow for capital expenditure on our transmission network based on historic levels, which are significantly lower than required to maintain a safe and reliable network. Over recent years our investment has been three to four times greater than the levels in the rate plan. In January 2010, we filed to establish new rates in line with forecast investment levels. If approved, the new rates would take effect from 1 January 2011. In addition, we have petitioned for additional revenues with respect to incremental capital expenditure for the 2008 calendar year. We anticipate making additional petitions for deferred recovery of qualifying incremental investment for calendar years 2009 and 2010.

In New England, the transmission tariff allows for recovery of, and a return on, capital expenditures as new investment enters service, bringing immediate revenue benefits.

In New York, Massachusetts and Rhode Island, we are subject to penalties if the reliability of our electricity distribution and transmission networks fails to meet specific targets related to customer impacts.

External market, energy policy and regulatory and other developments

In addition to the external market developments described on page 17 and the energy policy and regulatory developments described on pages 20 and 21, the following developments are relevant to the Transmission business.

Security of supply and climate change

We are focused on the long-term security of supply and environmental challenges arising from the transition to a low carbon economy and the decline of the UK's gas production from the North Sea. We are working with the UK electricity generators and Ofgem to ensure that the connection of renewable generation to the transmission network can be facilitated quickly and within our current licensing framework. In the US, we have major projects under way to increase the capacity of the transmission system to meet future demand. We are also working with governmental and regulatory bodies to ensure we help facilitate the implementation of the new climate change initiatives and policy being developed around integrating increasing amounts of renewable energy.

Other UK developments

The price controls contain allowances for transmission reinforcement works to accommodate the growing impact of renewable energy from Scotland.

Network access is being sought by just under 100 renewable generation projects in Scotland totalling approximately 9.5 GW, each with connection agreements with National Grid. The need for anticipatory investment is underpinned by continuing large amounts of activity in the generation market. At our latest connections update, as of 1 April we have signed agreements for the connection of 71.8 GW of generation, connecting across the period 2010 to 2025. This generation is mainly combined cycle gas turbines, offshore wind and nuclear, but also includes onshore wind, clean coal and waste/biomass plant. In addition to demonstrating the requirements for the Electricity Networks Strategy Group reinforcements, these generation connections drive further increases in our load related investment requirements. We have continued to work closely with the Scottish transmission companies to find innovative solutions to advancing new generation projects in Scotland. We have introduced measures to allow generators who are ready and able to connect to do so before wider reinforcement works. Importantly, on 8 May 2009, Ofgem confirmed that they will agree derogations from the GB Security and Quality Standards of Supply to advance the connection of 450 MW of Scottish renewable generation.

We continue to develop a strategic plan for our networks up to 2050, recognising the unique role they play in meeting the UK's climate change objectives. In respect of electricity transmission, our plan is consistent with meeting the UK's 2020 renewables target and remaining on track to meet the 2050 greenhouse gas reduction target. Comprising mainly onshore infrastructure investment, this plan has been shared with, and is supported by, the multi agency Electricity Networks Strategy Group. This plan will facilitate the connection of up to 34 GW of new renewable wind generation. These new connections will occur alongside an increasing replacement of the ageing generation fleet.

US regulatory developments

US federal policy is reshaping the discussion on how best to integrate renewable energy and mitigate climate change. Draft legislation is being developed in the US Senate. The legislation, if enacted, would implement a national renewable energy standard and give new authority that would allow FERC to take a larger role in siting and permitting of transmission infrastructure and a greater role in transmission planning to integrate large amounts of renewable energy. In anticipation of new legislation, FERC has begun discussions to assess how best to reform current regional transmission planning processes, including cost allocation and recovery, and how best to leverage the participation of renewable resources in wholesale energy markets. Support has been voiced by 29 state governors for the national renewable energy standard and for transmission investment to support both onshore and offshore wind development to boost wind resources.

The New England governors adopted the New England Governors' Renewable Blueprint, which is based on a study conducted by ISO New England and which identified transmission expansion that would be needed if large scale onshore and offshore wind resources and Canadian hydroelectric imports were available. The study was conducted to strengthen federal support of more local and regional development of renewable resources and has found that significant amounts of transmission investment will be needed within New England to meet the region's renewable targets.

New York has developed a State Energy Plan, which puts in place a goal of increasing investments in in-state energy supplies and

Transmission continued

investment in energy and transportation infrastructure to meet the state's renewable resource requirement of 30% by 2015.

Performance against our objectives

National Grid's progress against the Company objectives is set out on pages 30 to 45. We include below further information specific to Transmission with respect to the objectives that are closely aligned to the lines of business.

Driving improvements in our safety, customer and operational performance

Our objectives are to reduce employee lost time injuries to zero and to support generators and distribution network customers, including our own networks operated by Gas Distribution in the UK and Electricity Distribution & Generation in the US, in delivering energy efficiently and effectively to consumers, in particular in connecting new sources of supply to our transmission networks.

Safety

In the UK, during 2009/10 there were 10 lost time injuries compared with 8 in 2008/09 and 15 in 2007/08. The lost time injury frequency rate was 0.17 in 2009/10 compared with 0.14 in 2008/09 and 0.28 in 2007/08.

Our US electricity transmission lost time injury frequency rate decreased to zero in 2009/10 from 0.20 in 2008/09. There were no lost time injuries in 2009/10 compared with 2 in 2008/09.

Customer service

Our transmission customer service activities principally relate to facilitating new connections and maintaining existing relationships with the customers who are already connected. In the US, much of the interconnection work with our transmission customers is performed in conjunction with the system operators in the areas within which we operate.

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

Our aim is to meet or exceed the base financial returns in our price controls in the UK and our rate plans in the US.

The performance measures we use to monitor our return on investment are the vanilla return in the UK and the return on equity per rate plan in the US.

We measure the financial performance of our UK regulated businesses using an operational return metric comparable to the vanilla return defined in the UK price controls from 1 April 2007. In our electricity transmission operations, we achieved a 6.6% operational return in 2009/10 (2008/09: 4.7%), ahead of regulatory assumptions. In our gas transmission operations, we achieved a 7.6% return in 2009/10 (2008/09: 6.9%), significantly outperforming regulatory assumptions mainly as a result of a strong performance under our incentive schemes.

In the US, we measure our financial performance against the allowed regulatory return on equity under the terms of our rate plans or rate agreements. In New England, we achieved a weighted average 11.8% return on equity, in line with the prior year. In New York, our electricity transmission activities are combined with electricity distribution under a single rate plan and the combined returns for these activities are included within the Electricity Distribution & Generation business commentary on page 66.

Modernising and extending our transmission and distribution networks

We aim to meet or exceed network reliability and availability objectives. We are on track to deliver our planned capital investment programme involving approximately £3.6 billion of capital expenditure between 1 April 2010 and 31 March 2012.

Works to upgrade the two double circuits connecting Scotland and England are under way and due for completion in 2010 at a total cost of around £110 million. Further works are being carried out to increase the capability of the transmission system in the northeast and northwest of England so that increased transfers from Scotland can be transported to demand centres in England and Wales. The further works will be completed in 2011 at a total cost of around £230 million.

In the US, we have worked with other transmission owners and the ISOs in New York and New England and secured Department of Energy funding for transmission smart grid investments. In the UK, we have also agreed with Ofgem to commit significant investment into planning new infrastructure to connect low carbon power generation. In addition, we have committed to developing new processes to enable investment in new physical network capacity, which provides customers with easier access to our network.

Reliability

In the UK, the total amount of electricity transmitted in 2009/10 was 286 TWh compared with 296 TWh for 2008/09 and 303 TWh for 2007/08. Gas transmitted amounted to 1,150 TWh, compared with 1,158 TWh in 2008/09 and 1,134 TWh in 2007/08.

In the UK, the winter of 2009/10 saw demand from the electricity transmission network in England and Wales hit a peak of 52.7 GW. This compares with 52.9 GW in 2008/09 and 54.2 GW in 2007/08.

2009/10 saw a maximum gas demand of 465 million standard cubic metres on 8 January 2010, 5% higher than last year's peak of 443 million standard cubic metres.

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

Measure	Years ended 31 March		
	2010	2009	2008
UK electricity transmission network reliability – target 99.9999%	99.9999%	99.9999%	99.9999%
UK gas transmission network reliability – target 100%	100%	100%	100%
US electricity transmission network reliability – target < 253 MWh	147 MWh	266 MWh	437 MWh
UK average annual availability for electricity transmission network	94.76%	94.64%	95.09%
UK electricity system availability at winter peak demand	97.55%	97.7%	98.0%
UK gas compressor fleet performance – mean time between failures	698 hrs	405 hrs	259 hrs
US annual network availability	98.8%	98.8%	98.6%

In the US, the summer of 2009 saw demand from the electricity transmission networks in New England and New York hit a combined peak of 12.6 GW. This compares with 13.0 GW in 2008 and 13.2 GW in 2007. Our electricity system reliability performance broadly improved over the previous year as well as the average of the previous five years. However, continued improvement remains an objective for 2010/11.

Capital investment

UK investment

Investment in electricity and gas transmission systems is, by its nature, variable and is largely driven by changing sources of supply and asset replacement requirements. The gas transporter and electricity transmission licences also oblige us to provide connections and capacity upon request.

We have increased our level of investment as we replace parts of our UK electricity network as the assets reach the end of their useful lives. In addition, parts of the gas transmission network are reaching the end of their technical lives. These are mainly compressor stations, control systems and valves. This, together with work required to meet changing supply sources, means that the UK electricity and gas transmission business will continue to see a significant increase in investment and network renewal.

Capital investment in the replacement, reinforcement and extension of the UK electricity and gas transmission systems in 2009/10 was £1,254 million, compared with £1,259 million in 2008/09 and £1,600 million in 2007/08. This mainly related to UK electricity transmission investment including Thames Estuary reinforcement, our London cable tunnels project and transmission investment to facilitate connection of renewable generation. The balance of the UK investment was principally driven by load related infrastructure on our gas transmission system. Capital investment included £21 million with respect to intangible assets, principally software applications (2008/09: £18 million, 2007/08: £22 million).

US investment

Capital investment in the replacement, reinforcement and extension of the US electricity transmission networks in 2009/10 was £240 million, compared with £182 million in 2008/09 and £111 million in 2007/08. After excluding the £5 million effect of exchange movements capital investment increased by £63 million in 2009/10 compared with 2008/09. The change principally reflects an increase in regional reliability projects in New England and additional asset replacement in New York to increase system reliability.

We expect increasing investment in New England to deliver our regional system expansion projects including the New England East-West Solution (NEEWS) project. NEEWS is designed to address reliability problems in the southern New England transmission system and involves improvements to the transmission systems of National Grid and Northeast Utilities. In total it has an estimated cost of approximately \$2.1 billion (£1.4 billion), with National Grid's share estimated at approximately \$0.6 billion (£0.4 billion). The project represents the most significant addition to the New England 345 kV transmission system since it was first built. Other investment projects in New York will also deliver our asset replacement plans and maintain the reliability of the system.

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

Key areas of focus for our Transmission business in 2009/10 have been safety, securing funds for anticipatory investment in the UK, better operational planning and establishing regional delivery ventures in the US.

Much of the focus for Transmission has been on preparing for the significant increase in capital investment that is expected in future years. In the UK, this has included developing the longer-term investment plan. In the US, we finalised contracts with two

regional delivery ventures that are now delivering a substantial portion of our capital investment plan.

In the US, we have also established a combined transmission and distribution electricity operations function, which brings together our transmission and distribution operations departments under one chief operating officer to capture efficiencies.

The new operational planning way of working brings together consistent planning information from all parties across a longer timeframe. This has improved the alignment of workload, resources and system access across multiple years between National Grid and supply chain partners to drive the efficient and timely delivery of work on our assets.

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

Expanding our capabilities and identifying new financeable opportunities to grow

In the UK, we have identified significant capital requirements over the medium term. These requirements are primarily driven by the need to replace ageing infrastructure, reinforce the network to accommodate changing sources of supply and connect new generation, including renewables. We have also identified other potential opportunities to invest in related infrastructure such as offshore transmission networks and carbon capture and storage. These investments are discretionary and we are committed to further evaluation, including establishing suitable remuneration regimes, before we allocate funds to invest. In addition, some of these opportunities may go through a competitive process.



US regional delivery ventures

The magnitude of transmission investment required in the US encouraged us to review our approach, aiming to ensure we continue to deliver our investment programme safely and efficiently. In April 2009, we signed a 5 year regional delivery venture contract for projects in New England. This, combined with a separate regional delivery venture in upstate New York, will contribute around \$1.7 billion towards National Grid's investment programme over the next 5 years.

Transmission continued

Financial performance

Our combined adjusted operating profit, excluding exceptional items, for Transmission in the UK and the US of £1,464 million was 13% higher than 2008/09, which in turn was 10% higher than in 2007/08, both on a constant currency basis.

Financial results – Transmission UK

The results for the Transmission UK segment for the years ended 31 March 2010, 2009 and 2008 were as follows:

	Years ended 31 March		
	2010 £m	2009 £m	2008 £m
Revenue and other operating income	3,475	3,517	2,956
Operating costs excluding exceptional items and remeasurements	(2,164)	(2,391)	(1,935)
Adjusted operating profit	1,311	1,126	1,021
Exceptional items	(59)	(63)	(8)
Operating profit	1,252	1,063	1,013

2009/10 compared with 2008/09

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

	Revenue and other operating income £m	Operating costs £m	Operating profit £m
2008/09 results	3,517	(2,454)	1,063
Add back exceptional items	–	63	63
2008/09 adjusted results	3,517	(2,391)	1,126
Allowed revenues	169	–	169
Timing on recoveries	20	–	20
BSIS	(197)	227	30
French interconnector	(26)	–	(26)
Depreciation	–	(20)	(20)
Other	(8)	20	12
2009/10 adjusted results	3,475	(2,164)	1,311
Exceptional items	–	(59)	(59)
2009/10 results	3,475	(2,223)	1,252

UK adjusted operating profit, excluding exceptional items, increased by £185 million or 16% in 2009/10 compared with 2008/09.

Revenue and other operating income decreased by £42 million in 2009/10 compared with 2008/09. UK regulated revenues increased by £169 million, largely driven by inflation driven revenue increases under the UK price control allowance; however, this was more than offset by a fall in the recovery of incentivised costs associated with balancing the electricity system (Balancing Service Incentive Scheme – BSIS). As expected, revenues from our French interconnector business were lower in 2009/10, down by £26 million on 2008/09, as demand for capacity returned closer to normal levels. Other movements comprise lower LNG auction revenues and lower pass-through costs.

Operating costs, excluding exceptional items, decreased by £227 million in 2009/10 compared with 2008/09 largely reflecting the fall in incentivised BSIS costs. As expected, depreciation and amortisation increased by £20 million as a result of increasing capital investment. Other items decreased costs by £20 million, principally because of lower pass-through costs recovered through revenue.

The £59 million exceptional charge in 2009/10 consists of a £41 million charge for LNG storage and £18 million towards establishing global shared services and IT functions. The £41 million charge relates to the restructuring of our LNG storage facilities.

2008/09 compared with 2007/08

The principal movements between 2007/08 and 2008/09 can be summarised as follows:

	Revenue and other operating income £m	Operating costs £m	Operating profit £m
2007/08 results	2,956	(1,943)	1,013
Add back exceptional items	–	8	8
2007/08 adjusted results	2,956	(1,935)	1,021
Allowed revenues	232	–	232
Timing on recoveries	(20)	–	(20)
BSIS	318	(330)	(12)
French interconnector	43	(4)	39
Depreciation	–	3	3
Other	(12)	(125)	(137)
2008/09 adjusted results	3,517	(2,391)	1,126
Exceptional items	–	(63)	(63)
2008/09 results	3,517	(2,454)	1,063

Revenue and other operating income increased by £561 million in 2008/09 compared with 2007/08, mainly driven by recovery of higher incentivised BSIS costs and an increase in allowed revenues. French interconnector revenue was up £43 million due to higher capacity auction revenues. Other movements mainly comprise lower LNG storage auction income.

Operating costs, excluding exceptional items, increased by £456 million in 2008/09 compared with 2007/08. This was primarily due to higher incentivised BSIS costs relating to higher constraint, margin and energy balancing costs (largely covered by the revenue increase above). Higher other operating costs reflect an increase in gas shrinkage costs, due to higher energy prices, and higher pass-through costs.

The increase in UK adjusted operating profit in 2008/09 reflects the movements in revenue and operating costs, excluding exceptional items, as described above.

The £63 million exceptional charge in 2008/09 primarily consists of a £50 million charge relating to the restructuring of our LNG storage facilities.

Financial results – Transmission US

The average exchange rates used to translate the results of US operations during 2009/10, 2008/09 and 2007/08 were \$1.58:£1, \$1.54:£1 and \$2.01:£1 respectively.

	Years ended 31 March		
	2010 £m	2009 £m	2008 £m
Revenue	405	420	299
Operating costs excluding exceptional items	(252)	(245)	(171)
Adjusted operating profit	153	175	128
Exceptional items	(2)	(2)	(6)
Operating profit	151	173	122

2009/10 compared with 2008/09

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

	Revenue £m	Operating costs £m	Operating profit £m
2008/09 results	420	(247)	173
Add back exceptional items	–	2	2
2008/09 adjusted results	420	(245)	175
Exchange movements	(11)	7	(4)
2008/09 constant currency results	409	(238)	171
Allowed revenues	4	–	4
Timing on recoveries – revenues	(13)	–	(13)
Timing on recoveries – pass-through costs	5	(7)	(2)
Other	–	(7)	(7)
2009/10 adjusted results	405	(252)	153
Exceptional items	–	(2)	(2)
2009/10 results	405	(254)	151

Adjusted operating profit decreased by £22 million in 2009/10, of which £4 million was caused by the movement in exchange rates when compared with 2008/09. On a constant currency basis, revenue decreased by £4 million and operating costs increased by £14 million, resulting in an £18 million, or 11%, decrease in adjusted operating profit in 2009/10.

A key reason for the 2009/10 profit decrease was the timing of recoveries under our New York rate plan, which resulted in a £15 million reduction. Excluding the timing of recoveries, our allowed revenues increased by £4 million in 2009/10. This growth was mainly in New England, where increased capital investment has delivered rate base growth of approximately 7% on last year.

Operating costs were £14 million higher in 2009/10 on a constant currency basis. This included £7 million for higher regulatory assessment costs in New York, which are fully recoverable as pass-through costs. The remaining cost increase of £7 million resulted from higher depreciation and decommissioning costs, directly related to the growth in our capital programme and investment in system reliability improvements.

The £2 million exceptional charge in 2009/10 related to restructuring costs arising from the integration of the operations acquired with KeySpan, including one time costs associated with pension and retiree welfare plan amendments.

2008/09 compared with 2007/08

The principal movements between 2007/08 and 2008/09 can be summarised as follows:

	Revenue £m	Operating costs £m	Operating profit £m
2007/08 results	299	(177)	122
Add back exceptional items	–	6	6
2007/08 adjusted results	299	(171)	128
Exchange movements	91	(52)	39
2007/08 constant currency results	390	(223)	167
Allowed revenues	25	–	25
Timing on recoveries	4	–	4
Other	1	(22)	(21)
2008/09 adjusted results	420	(245)	175
Exceptional items	–	(2)	(2)
2008/09 results	420	(247)	173

Adjusted operating profit increased by £47 million in 2008/09, of which £39 million was caused by the movement in exchange rates when compared with 2007/08. On a constant currency basis, revenue and operating costs increased by £30 million and £22 million respectively, resulting in an £8 million, or 5%, increase in adjusted operating profit in 2008/09.

Allowed revenues increased by £25 million in 2008/09. This growth was in New England, where we have seen the benefit of our investment in regional reliability projects coming through in higher sustainable revenue streams.

In addition, revenue was £4 million higher in 2008/09 because of the timing of recoveries under our New York rate plan.

Operating costs were £22 million higher, on a constant currency basis, in 2008/09 than in 2007/08 reflecting our commitment to improve the operational performance of the networks in both New England and New York. The majority of the increase was driven by reliability enhancements and maintenance programmes aimed at improving system reliability. In addition, both depreciation and property taxes have increased as a direct consequence of the growth in network capital investment brought into service.

The £2 million exceptional charge in 2008/09 relates to restructuring costs arising from the integration of the operations acquired with KeySpan.

Gas Distribution



Adjusted operating profit

£1,137m

(2008/09: £1,284m)

Capital investment

£1,079m

(2008/09: £1,019m)

Employees

9,828

(2008/09: 9,534)

Gas delivered

500 TWh

(2008/09: 522 TWh)

We continue to share best practice between the UK and US to improve our efficiency and make our operating practices more consistent.

In aggregate across our networks we replaced in excess of 2,000 kilometres of metallic main in the UK and 362 kilometres in the US helping to improve the safety and reliability of our networks.

This section should be read in conjunction with the rest of this Operating and Financial Review

Key Facts

- Around 190,000 kilometres of gas pipeline
- Delivery of 299 TWh of gas in the UK and 201 TWh in the US
- Around 10.8 and 3.5 million consumers in the UK and US respectively

About Gas Distribution

Our Gas Distribution business operates in both the UK and the US. As a consequence of the differences in the respective economic and regulatory environments, we report the results of Gas Distribution as two segments: Gas Distribution UK and Gas Distribution US.

Principal operations

Gas Distribution UK

Our Gas Distribution UK segment comprises four of the eight regional gas distribution networks in Great Britain.

Our networks comprise approximately 132,000 kilometres of gas distribution pipeline and we transport gas on behalf of approximately 26 active gas shippers from the gas national transmission system to around 10.8 million consumers.

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

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

In our UK networks, actual gas consumption was 299 TWh compared with 317 TWh in 2008/09.

Gas Distribution US

Our Gas Distribution US segment comprises gas distribution networks providing services to around 3.5 million consumers across the northeastern US, located in service territories in upstate New York, New York City, Long Island, Massachusetts, New Hampshire and Rhode Island. We are actively seeking to increase our customer base in these areas and in 2009/10 added more than 44,000 new gas heating customers.

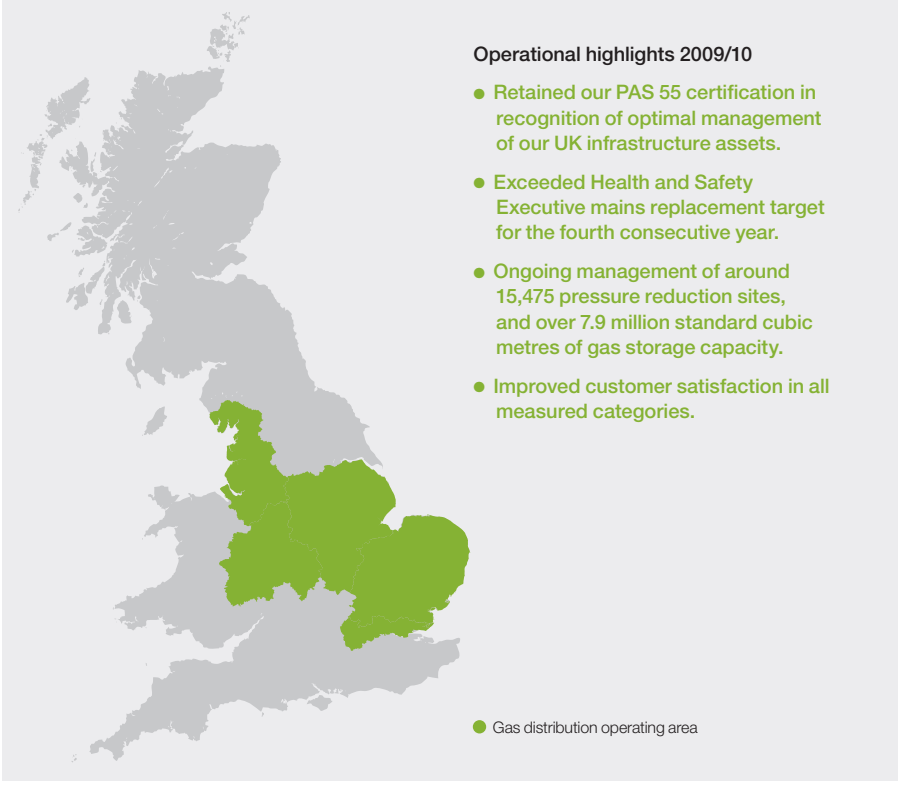
Our network of approximately 58,000 kilometres of gas pipeline serves an area of approximately 26,400 square kilometres.

In the US, in addition to the operation and maintenance of each of our gas distribution networks, we are also responsible for billing, customer service and supply services.

We maintain a diversified and flexible portfolio of gas supply and storage assets, and are able to deliver additional benefits to customers and shareholders by optimising these assets. We are the largest shipper on major inter-state pipelines, including Tennessee, Dominion, Algonquin and Iroquois.

We supplement gas from the inter-state pipeline system with liquefied natural gas (LNG) and propane facilities in 19 locations during peak cold weather conditions. During winter 2009/10, the US gas network supported consumption of more than 201 TWh compared with 205 TWh in 2008/09.

Gas Distribution UK – operating area



Operational highlights 2009/10

- Retained our PAS 55 certification in recognition of optimal management of our UK infrastructure assets.
- Exceeded Health and Safety Executive mains replacement target for the fourth consecutive year.
- Ongoing management of around 15,475 pressure reduction sites, and over 7.9 million standard cubic metres of gas storage capacity.
- Improved customer satisfaction in all measured categories.

0.09

UK lost time injury frequency rate

£7.0bn

Estimated UK regulatory asset value

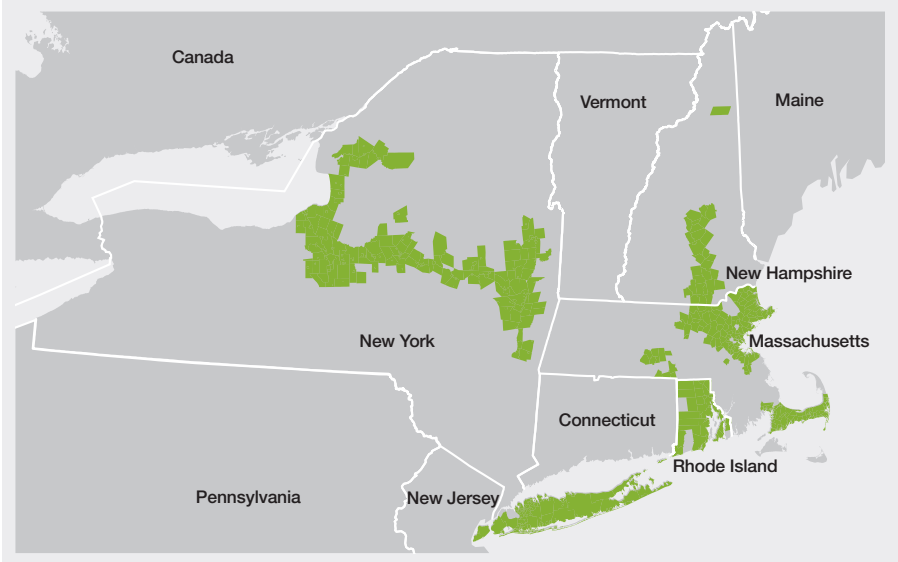
10.8m

Gas consumers served in the UK

132,000 km

Gas pipeline in the UK

Gas Distribution US – operating area



Operational highlights 2009/10

- More than 44,000 new gas heating customers.
- Reduced lost time injuries by over 36%.
- Met all regulatory standards of service regarding service quality indices and performance measures.
- Retained PAS 55 certification in recognition of optimal management of our US infrastructure assets.

0.29

US lost time injury frequency rate

\$7.4bn

Estimated US rate base

3.5m

Gas consumers served in the US

58,000 km

Gas pipeline in the US

Gas Distribution continued

Regulation

Gas Distribution UK

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

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

As at 31 March 2010, our regulatory asset value was estimated at approximately £7.0 billion.

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

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

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

Gas Distribution US

Gas Distribution US operates under franchise agreements that provide us with certain rights and obligations regarding gas facilities and the provision of gas service within each state in which we operate. In addition, there are federal and state laws and regulations covering both general business practices and the gas business in particular, especially with respect to safety, energy transactions, customer sales and service, levels of performance, rates, finances and environmental concerns.

Except for residential and small commercial consumers in Rhode Island and residential consumers in New Hampshire, consumers may purchase their supply from independent providers. The majority of gas supplied to consumers in the US is sold by regulated utilities to their customers. Regulated utilities, such as our gas distribution companies, purchase gas from gas producers and gas transporters, and then transport this gas on

the independent inter-state pipeline system and into the regulated utilities' gas distribution networks for onward delivery to customers. Our gas distribution companies receive gas from the inter-state pipeline system at 94 gate stations. The inter-state pipeline system and local gas distribution networks are also used to deliver gas on behalf of customers who purchase gas from independent suppliers or direct from gas producers.

Depending on the jurisdiction, delivery prices are set either by actual sales volumes and costs incurred in an historical test year, or by rate plans based on estimates of costs and volumes expected to be delivered, which may differ from actual amounts. A significant proportion of our costs are gas purchases for supply to customers. Our charges to customers are designed to recover these costs with no profit margin. Prices are adjusted from time to time to ensure any over- or under-recovery is returned to or recovered from our customers. There can be timing differences between costs being incurred and prices being adjusted.

Certain of our rate plans include earnings sharing arrangements, which allow us to retain some of the benefit of efficiency improvements in excess of those built into rate plan assumptions. Generally, we retain all the benefits up to a certain level of return on equity, after which the balance is returned to customers. The following is a summary of the key features and allowed returns within our filed and approved rate plans.

Rate plan	Equity return	Equity to debt ratio	Sharing arrangements
New York City and Long Island	9.8%	45/55	100% to 10.5% 50% to 12.5% 35% to 13.5% nil above 13.5%
Upstate New York	10.2%	44/56	100% to 11.35% 50% to 13.6% 25% to 15.6% 10% above 15.6%
Boston, MA	10.2%	50/50	100% to 14.2% 75% above 14.2%
Essex, MA	11.2%	55/45	None
Colonial, MA	11.2%	46/54	None
Rhode Island	10.5%	48/52	50% to 11.5% 25% above 11.5%
New Hampshire	9.54%	50/50	None

We also have a number of service standards for our operations. If certain identified minimum service standards are not achieved, penalties may be imposed.

External market, energy policy and regulatory and other developments

In addition to the external market developments described on page 17 and the energy policy and regulatory developments described on pages 20 and 21, the following developments are relevant to the Gas Distribution business.

New York

The downstate New York rate plans allow us to request recovery or refund of certain costs and forecasted expenses which vary from rate plan allowances. Such costs include: site investigation and environmental remediation; property tax; and pension and other post-employment benefit expenses. On 29 January 2010, the companies made a filing with the New York Public Service Commission (NYPSC) to request up to \$65 million in cost recovery per year over five years. A decision is expected by December 2010.

The Niagara Mohawk plan also allows us to adjust rates for certain costs that vary from rate plan allowances.

Massachusetts

On 16 December 2009, we filed a request with the Massachusetts Department of Public Utilities to merge Boston Gas and Essex Gas into a single corporate entity. Our goal is to align the corporate structure with the current operational structure. A decision is expected during the first half of 2010/11.

On 16 April 2010, we filed our Massachusetts gas rate plans. Further details are provided on page 33.

New Hampshire

On 13 November 2009, the New Hampshire Public Utilities Commission denied our Motion for Reconsideration in which we requested an increase in the allowed return on equity. On 26 February 2010, we filed a new proposed rate increase. Further details are provided on page 33.

A decision is expected in early 2011, with temporary rates effective from June 2010. These rates would recover approximately \$5.5 million.

We are currently evaluating options to allow us to exit our gas and electricity businesses in New Hampshire.

Performance against our objectives

National Grid's progress against the Company objectives is set out on pages 30 to 37. We include below further information specific to Gas Distribution with respect to the objectives that are closely aligned to the lines of business.

Driving improvements in our safety, customer and operational performance

Our objective is to reduce employee lost time injuries to zero, to meet customer service objectives agreed with our regulator and to be within the first quartile of customer satisfaction in the territories we operate in.

Safety

Lost time injuries totalled 42 in 2009/10, of which 9 were in the UK and 33 in the US. This is equivalent to a lost time injury frequency rate of 0.19. This compares with a total of 76 lost time injuries in 2008/09, 24 in the UK and 52 in the US, equivalent to a lost time injury frequency rate of 0.35.

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

As detailed on page 80, we identified that some of our UK main replacement activity may have been misreported. We have notified both Ofgem and the HSE, and Ofgem's investigation into this matter continues.

Customer service

In the UK, quality of service standards defined by Ofgem apply to three principal areas of activity: new connections; the telephone service; and attendance at gas emergencies. All standards have been met in 2009/10, with the exception of one gas emergency standard in one network affected by the severe winter weather where we achieved 96.98% against a standard of 97%. In individual cases where compensation is due as a consequence of failing to meet certain standards, we have processes to ensure that customers receive the statutory compensation to which they are entitled. Customer satisfaction with the levels of service provided in respect of our main types of work (emergency response and repair, planned work and connections work) is measured and reported on a quarterly basis. Results of these surveys are comparable with the other distribution network operators and can be found at www.nationalgrid.com and www.ofgem.gov.uk.

For gas utility businesses in the US, J.D. Power and Associates formulate an annual survey and customer satisfaction rating. In 2009/10, we improved results for commercial customer satisfaction from third quartile to second quartile and residential customer satisfaction scores also improved from fourth quartile to third quartile.

There is a programme of activities within the UK and US to improve these scores further.

In the US, our Gas Distribution business met all regulatory requirements regarding service quality indices and performance measures. These standards are set by state regulatory agencies and cover operational activities including, but not limited to: damage prevention; leak repair; emergency response; inspections; meter changes; and main and service replacements.

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

Our aim is to meet or exceed the base financial returns in our price controls in the UK and our rate plans in the US.

The performance indicators we use to monitor our return on investment are the vanilla return in the UK and the return on equity per rate plan in the US.

Gas Distribution UK achieved a 6.3% vanilla return in 2009/10, exceeding the regulatory allowance. The following is a summary of returns under our US rate plans:

Regulatory entity	Rate base ⁽ⁱ⁾		Return on equity ⁽ⁱⁱ⁾		Allowed return current
	2009	2008	2009	2008	
KEDNY	\$2,350m	\$2,294m	11.2%	11.9%	9.8%
KEDLI	\$1,899m	\$1,795m	10.5%	11.1%	9.8%
Mass. Gas	\$1,536m	\$1,488m ⁽ⁱⁱⁱ⁾	2.9%	8.3%	10.6%
Energy North	\$193m	\$191m	3.8%	4.4%	9.5%
Narragansett	\$337m	\$337m	6.7% ^(iv)	7.6%	10.5%
Niagara Mo. Gas	\$1,103m	\$1,067m	3.8%	4.8%	10.2%

(i) Estimate of rate base using filed regulatory returns at 31 December or an alternative US GAAP based invested capital measure where recent rate base filings are either not available or where the actual rate base currently excludes certain regulatory asset balances.

(ii) Based on regulatory returns for the 12 months ended 31 December.

(iii) 2008 rate base has been restated to exclude \$937 million of goodwill.

(iv) Return is -0.7% before normalising for one time bad debt adjustments.

Gas Distribution continued

Current returns for our downstate New York and Long Island gas businesses are above our allowed returns. We are in the third year of a five year rate plan for each of these businesses. Returns for our gas businesses in Rhode Island, New Hampshire and upstate New York are below our allowed returns. We filed a rate case in New Hampshire on 26 February 2010 and are awaiting approval from the regulators. In upstate New York, a two year rate plan that increased rates by \$39.4 million and has a 10.2% return on equity went into effect on 20 May 2009. Rates will be revised on 20 May 2010 and we have filed to increase rates by \$14 million as of that date. In our Massachusetts gas businesses, we filed rate plans on 16 April 2010.

Modernising and extending our transmission and distribution networks

Our objectives are to meet regulatory targets and to have zero loss of supply incidents. We are on track to deliver capital investment by 2012 in line with our UK price control allowance and supported by our US rate plans.

Reliability

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

In both the UK and US, we continue to focus on improving reliability, in particular in the area of gas escapes. In the US, workable gas escape backlog has been reduced by 25% over the previous year. In the UK, we met the regulatory standards of service in the area of gas escapes in three out of our four networks. We missed the target in the fourth network by 0.02%.

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

Capital investment

During 2009/10, we successfully delivered £1,079 million of capital investment (2008/09: £1,019 million; 2007/08: £702 million) and plan to invest a further £2 billion by 31 March 2012.

UK capital investment

Gross investment including reinforcement, extension and replacement of the UK gas distribution network was £670 million in 2009/10 compared with £598 million in 2008/09 and £514 million in 2007/08. Of these amounts, £465 million in 2009/10 related to replacement expenditure (2008/09: £425 million; 2007/08: £353 million) and £205 million to other capital investment (2008/09: £173 million; 2007/08: £161 million). Expenditure on software applications included within the above amounts was £54 million (2008/09: £22 million; 2007/08: £18 million). The increase in expenditure is primarily driven by the Gas Distribution front office system (see below).

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

In collaboration with our gas alliance and coalition partners, we have replaced more than 2,000 kilometres of metallic gas main

this year and more than 14,000 kilometres since 2002/03. The vast majority of this relates to the long-term gas main replacement programme agreed with the HSE.

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

US capital investment

Capital expenditure in the replacement, reinforcement and extension of our US gas distribution networks was £409 million in 2009/10 (2008/09: £421 million; 2007/08: £188 million).

After excluding the effect of exchange movements of £11 million in 2009/10 compared with 2008/09, capital expenditure decreased by £1 million. This reflects lower growth and reliability programmes largely offset by higher main and service replacements.

After excluding the effect of exchange movements of £58 million in 2008/09 compared with 2007/08, capital expenditure increased by £175 million. The primary reason for the increase arose from five months of additional activities from the gas distribution network of KeySpan acquired in August 2007.

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

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

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

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

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

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

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

Financial performance

Adjusted operating profit was £1,137 million in 2009/10 compared with £1,284 million in 2008/09 and £987 million in 2007/08.

Financial results – Gas Distribution UK

The results for our Gas Distribution UK segment for the years ended 31 March 2010, 2009 and 2008 were as follows:

	Years ended 31 March		
	2010 £m	2009 £m	2008 £m
Revenue	1,517	1,466	1,383
Other operating income	1	2	8
Operating costs excluding exceptional items	(795)	(796)	(796)
Adjusted operating profit	723	672	595
Exceptional items	(41)	(43)	(21)
Operating profit	682	629	574

2009/10 compared with 2008/09

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

	Revenue and other operating income £m	Operating costs £m	Operating profit £m
2008/09 results	1,468	(839)	629
Add back exceptional items	–	43	43
2008/09 adjusted results	1,468	(796)	672
Allowed revenues	85	–	85
Timing on recoveries	(28)	–	(28)
Pass-through costs	–	5	5
Non-formula	(14)	9	(5)
Other revenue and costs	7	(13)	(6)
2009/10 adjusted results	1,518	(795)	723
Exceptional items	–	(41)	(41)
2009/10 results	1,518	(836)	682

Revenue and other operating income in Gas Distribution UK increased by £50 million in 2009/10 compared with 2008/09. Allowed revenues were up £85 million, driven by the five year price control that came into effect on 1 April 2008 and incentive gains through the efficient management of our capacity requirements and improved pressure management. This was partially offset by an estimated £28 million timing impact on recoveries and a decline in non-formula revenue primarily driven by a drop in non-regulated meter work activities.

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

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



Improving customer relations by reducing congestion

Traffic congestion is a cost to the economy, with any solution for easing congestion improving the experience of road users and delivering environmental benefits by reducing pollution from slow moving vehicles. Traditional road plates to cover excavations are heavy, difficult to store and require mechanical means to install on site. These difficulties have led to the practice of lane closures and traffic control when working in highways. Following an investigation by Gas Distribution, an alternative solution was identified that introduces a modular trench plating system, providing quick and easy installation over excavations.



Emergency water ingress

During winter 2009/10, over 6,000 properties were affected by a number of separate water ingress incidents resulting in significant loss of supply. In particular, as Christmas 2009 approached, the skills and commitment of our UK gas distribution team were put to the test by 2 major incidents affecting over 4,000 properties in southeast England. In both cases a burst water pipe created a hole in our low pressure main, resulting in water entering our network. Our engineers and support team applied their skills and determination each day up to and during the Christmas period to restore the gas supply.

Gas Distribution continued

Exceptional charges of £41 million in 2009/10 included an increase in the environmental provision of £14 million, reflecting changes in landfill tax legislation, with the remaining £27 million made up of restructuring and transformation costs, which include system related projects costs. This compared with a £43 million charge in 2008/09.

As a consequence of the above, adjusted operating profit excluding exceptional items was £51 million higher in 2009/10 than 2008/09, an increase of 8%. Including exceptional items, operating profit was £53 million higher in 2009/10 than 2008/09, an increase of 8%.

2008/09 compared with 2007/08

The principal movements between 2007/08 and 2008/09 can be summarised as follows:

	Revenue and other operating income £m	Operating costs £m	Operating profit £m
2007/08 results	1,391	(817)	574
Add back exceptional items	–	21	21
2007/08 adjusted results	1,391	(796)	595
Allowed revenues	90	–	90
Timing on recoveries	(15)	–	(15)
Pass-through costs	–	(9)	(9)
Non-formula	9	(12)	(3)
Other revenue and costs	(7)	21	14
2008/09 adjusted results	1,468	(796)	672
Exceptional items	–	(43)	(43)
2008/09 results	1,468	(839)	629

Revenue and other operating income in Gas Distribution UK increased by £77 million in 2008/09 compared with 2007/08. Allowed revenue was up £90 million, driven by the five year price control that came into effect on 1 April 2008 and incentive gains through the efficient management of our capacity requirements and improved pressure management. This was partially offset by a £15 million timing impact on recoveries. In addition, a growth in other revenue was primarily driven by non-regulated meter work activities.

The net year-on-year timing impact against allowed revenues was a reduction of £15 million as in 2008/09 there was a net benefit of £10 million, comprising the under-recovery of £20 million relating to the previous year, partially offset by a £10 million under-recovery for 2008/09, compared with a net benefit of £25 million in 2007/08, comprising a £20 million under-recovery in 2007/08 offset by £45 million under-recovery from 2006/07. Operating costs for 2008/09, excluding exceptional items, were in line with 2007/08. Efficiency savings through strong operating cost performance, together with other minor items, were offset by £9 million higher pass-through costs due to an increase in business rates following the changes in rateable values introduced from 1 April 2005 and shrinkage costs due to higher gas prices. Non-formula costs were £12 million higher because of increased meter work and other non-formula activities.

Exceptional charges of £43 million in 2008/09 include an increase in the environmental provision of £13 million with the remaining £30 million made up of restructuring and transformation costs, which include system related projects costs. This compared with a £21 million charge in 2007/08.

Financial results – Gas Distribution US

The average exchange rates used to translate the results of US operations during 2009/10, 2008/09 and 2007/08 were \$1.58:£1, \$1.54:£1 and \$2.01:£1 respectively.

	Years ended 31 March		
	2010 £m	2009 £m	2008 £m
Revenue	3,708	4,786	2,845
Operating costs excluding exceptional items and remeasurements	(3,294)	(4,174)	(2,453)
Adjusted operating profit	414	612	392
Exceptional items and remeasurements	34	(386)	95
Operating profit	448	226	487

2009/10 compared with 2008/09

The principal movements between 2008/09 and 2009/10 can be summarised as follows.

	Revenue £m	Operating costs £m	Operating profit £m
2008/09 results	4,786	(4,560)	226
Add back exceptional items	–	52	52
Add back remeasurements	–	334	334
2008/09 adjusted results	4,786	(4,174)	612
Exchange movements	(121)	105	(16)
2008/09 constant currency results	4,665	(4,069)	596
Pass-through costs	(965)	965	–
Rate increases	32	–	32
Economic impact on volumes	(38)	–	(38)
Timing on recoveries	56	(171)	(115)
Merchant function charge	(14)	–	(14)
Long Island property tax recoveries	(39)	–	(39)
Bad debt expense	–	5	5
Other revenues and costs	11	(24)	(13)
2009/10 adjusted results	3,708	(3,294)	414
Exceptional items	–	(18)	(18)
Remeasurements	–	52	52
2009/10 results	3,708	(3,260)	448

Revenue and operating costs excluding exceptional items and remeasurements decreased by £957 million and £775 million respectively in 2009/10 compared with 2008/09 on a constant currency basis, a decrease of 21% and 19% respectively.

Revenue decreased by £957 million in 2009/10 compared with 2008/09. Net of higher pass-through costs of £965 million, revenue increased by £8 million.

Gas Distribution US benefited from approved rate increases/delivery rate adjustments in our downstate New York, Long Island, upstate New York, Rhode Island and New Hampshire operating areas of £32 million. The economic downturn had an adverse impact of £38 million and timing impacts included recoveries of NYPSC 18-A assessments of £44 million and other of £12 million. Lower recoveries of gas inventory carrying charges of £14 million, and cessation of Long Island property tax collections of £39 million were partially offset by increases in other revenues of £11 million. These increases include load additions of approximately 44,000 customers contributing £29 million, which was partially offset by a decrease in volumes driven by warmer

than normal weather and normal conservation/attrition totalling £29 million.

The weather in 2009/10 was significantly warmer than 2008/09. As measured in degree heating days, weather in 2009/10 across our US gas territories was approximately 4% warmer than normal and was approximately 8% warmer than 2008/09.

Operating costs, excluding pass-through costs and exceptional items, were £190 million higher in 2009/10 compared with 2008/09, primarily driven by adverse timing impacts in the recovery of gas cost deferrals of £103 million, higher spending in energy efficiency programmes of £10 million, and NYPSC 18-A assessment expenses of £58 million. Other cost increases of £24 million were partly offset by lower bad debt expenses of £5 million due to lower reserve requirements.

Exceptional charges of £18 million in 2009/10 related to integration and transformation initiatives, including the cost of voluntary early retirements and costs relating to US healthcare reform, while favourable mark-to-market commodity contract remeasurement gains were recorded as a consequence of higher energy prices compared with contracted amounts as at 31 March 2010. The gains from these transactions will be realised in subsequent periods and passed on to consumers.

2008/09 compared with 2007/08

The principal movements between 2007/08 and 2008/09 can be summarised as follows:

	Revenue £m	Operating costs £m	Operating profit £m
2007/08 results	2,845	(2,358)	487
Add back exceptional items	–	(95)	(95)
2007/08 adjusted results	2,845	(2,453)	392
Exchange movements	873	(753)	120
2007/08 constant currency results	3,718	(3,206)	512
KeySpan contribution	902	(896)	6
Pass-through costs	69	(69)	–
Rate increases	32	–	32
Weather and volumes	22	–	22
Timing on recoveries	(6)	52	46
Merchant function charge	38	–	38
Energy efficiency programme	19	(12)	7
Bad debt expense	–	(29)	(29)
Other revenues and costs	(8)	(14)	(22)
2008/09 adjusted results	4,786	(4,174)	612
Exceptional items	–	(52)	(52)
Remeasurements	–	(334)	(334)
2008/09 results	4,786	(4,560)	226

Revenue and operating costs excluding exceptional items and remeasurements increased by £1,068 million and £968 million respectively in 2008/09 compared with 2007/08 on a constant currency basis, an increase of 29% and 30% in each case. The rise in revenue and operating cost primarily arose from an increase in contributions from KeySpan operations in 2008/09 reflecting the first full year of ownership since acquisition in August 2007.

Revenue increased by £1,068 million in 2008/09 compared with 2007/08. Revenue from KeySpan operations increased by £902 million compared with 2007/08. The remaining £166 million

was primarily driven by New York, Long Island, Rhode Island, and New Hampshire rate increases of £32 million, colder weather and higher consumption of £22 million, higher recoveries of gas inventory carrying charges of £38 million, higher pass-through costs of £69 million, and other increases of £5 million.

The weather in 2008/09 was significantly colder than 2007/08. As measured in heating degree days, weather in 2008/09 across National Grid's US gas territories was approximately 5% colder than normal and was approximately 8% colder than 2007/08.

Operating costs, excluding exceptional items, were £968 million higher in 2008/09 compared with 2007/08. The increase in costs of KeySpan operations in 2008/09 was £896 million on a constant currency basis. The remaining increase of £72 million was a result of higher commodity pass-through costs, an increase in maintenance costs and higher bad debt expense as a result of the economic downturn partially offset by a favourable overcollection in commodity costs.

Exceptional charges of £52 million in 2008/09 related to integration initiatives, including the cost of voluntary early redundancies, while adverse mark-to-market commodity contract remeasurement losses were recorded as a consequence of lower energy prices compared with contracted amounts as at 31 March 2009. The losses from these transactions will be realised in subsequent periods and recovered from consumers.



Gas main replacement

As part of our ongoing replacement programme, which includes the HSE target of replacing 54,600 km of iron main around the UK we invested £465 million in 2009/10. Contributing to safety, security of supply and meeting regulatory obligations, the programme is seeing metallic main being replaced with yellow polyethylene pipes which are flexible and resistant to corrosion. National Grid continually strives to minimise the disruption and inconvenience associated with the street works required to deliver this replacement programme. Where possible we use no dig techniques, trenchless working and directional drilling to achieve this goal. We also endeavour to coordinate our work with local authorities and the activities of other utilities, such as our collaboration in 2009 with Thames Water, where gas and water mains were simultaneously replaced in Tower Hill.

Electricity Distribution & Generation



Adjusted operating profit

£374m

(2008/09: £265m)

Capital investment

£372m

(2008/09: £355m)

Employees

8,344

(2008/09: 8,251)

Electricity delivered

62 TWh

(2008/09: 65 TWh)

Our customers are at the heart of everything we do. We continue to invest in our distribution and generation systems to create sustained improvements in our system reliability. We believe that increased energy efficiency and the use of smart technologies is the best way to help our customers control their energy costs and address the issue of climate change.

In 2009, we met all our regulatory reliability targets and achieved internal targets moving us towards top quartile reliability performance.

Severe storms affected our service territories during the winter, causing service interruptions for thousands of customers. Our emergency response plans were highly effective in restoring service efficiently and safely.

[This section should be read in conjunction with the rest of this Operating and Financial Review](#)

Key Facts

- Over 116,800 kilometres of circuit
- Approximately 3.4 million customers
- 666 substations
- 57 generation units at 13 locations across Long Island
- LIPA network serving 1.1 million customers over 24,100 kilometres of circuit and 177 substations, delivering 22 TWh of electricity

About Electricity Distribution & Generation

Our Electricity Distribution & Generation business operates in the northeastern US and is reported as a single segment in our financial statements.

Principal operations

Electricity Distribution

We are responsible for building, operating and maintaining our electricity distribution networks in Massachusetts, Rhode Island, New Hampshire and upstate New York. We also maintain and operate the electricity transmission and distribution system on Long Island owned by the Long Island Power Authority (LIPA), providing energy to homes, small businesses, and large commercial and industrial enterprises.

Through our electricity distribution networks, we serve approximately 3.4 million electricity customers over a network of approximately 116,800 circuit kilometres (72,600 miles) in New England and upstate New York.

The LIPA service territory covers approximately 3,200 square kilometres (1,200 square miles), encompassing nearly 90% of Long Island's total land area. LIPA owns approximately 2,100 kilometres (1,300 miles) of transmission line facilities that deliver power to approximately 177 substations in its electricity system. From these substations, approximately 24,100 circuit kilometres (15,000 miles) of distribution facilities distribute electricity to 1.1 million customers.

Our responsibilities include managing the day-to-day operations and maintenance of LIPA's transmission and distribution system, providing services to LIPA's retail customers and managing the delivery of the energy that we produce under contract to LIPA.

Generation

We own 57 electricity generation units on Long Island that together provide 4.1 GW of power under contract to LIPA.

Our plants consist of oil and gas fired steam turbine, gas turbine and diesel driven generating units ranging from 2 to 375 MW. Any available power not needed to meet LIPA's requirements is made available for sale in the open market.

Energy procurement

Within our US Electricity Distribution & Generation and Gas Distribution businesses, we are responsible for the planning, procurement and administration of gas and electricity commodity supply for our customers. We conduct business with various energy companies in order to supply approximately 14 billion standard cubic metres of natural gas and 35 TWh of electricity annually across 4 states. In addition to providing our customers with stable and low cost electricity supply, we are committed to helping the states in which we operate to achieve their Renewable Portfolio Standards and satisfy recent legislative requirements by working with renewable project developers and other stakeholders to bring new sustainable resources online cost effectively.

Through our fuel management services, we procure gas and fuel oil to supply the 68 power generation units on Long Island under contract by LIPA, of which we own 57. Until 31 December 2009, we also purchased energy, capacity and ancillary services in the open market on LIPA's behalf.

Regulation

Customer bills typically comprise a commodity rate, covering the cost of electricity delivered, and a delivery rate, covering our electricity delivery service.

Depending on the jurisdiction, delivery prices are set either by actual sales volumes and costs incurred in an historical test year, or by rate plans based on estimates of costs and volumes expected to be delivered, which may differ from actual amounts. A substantial proportion of our costs, in particular electricity purchases for supply to customers, are pass-through costs. Our charges to customers are designed to recover these costs with no profit margin. Prices are adjusted from time to time to ensure any over- or under-recovery is returned to or recovered from our customers. There can be timing differences between costs being incurred and prices being adjusted.

Our Long Island generation plants sell capacity to LIPA under a contract, approved by the Federal Energy Regulatory Commission (FERC), which provides a similar economic effect to cost of service rate regulation.

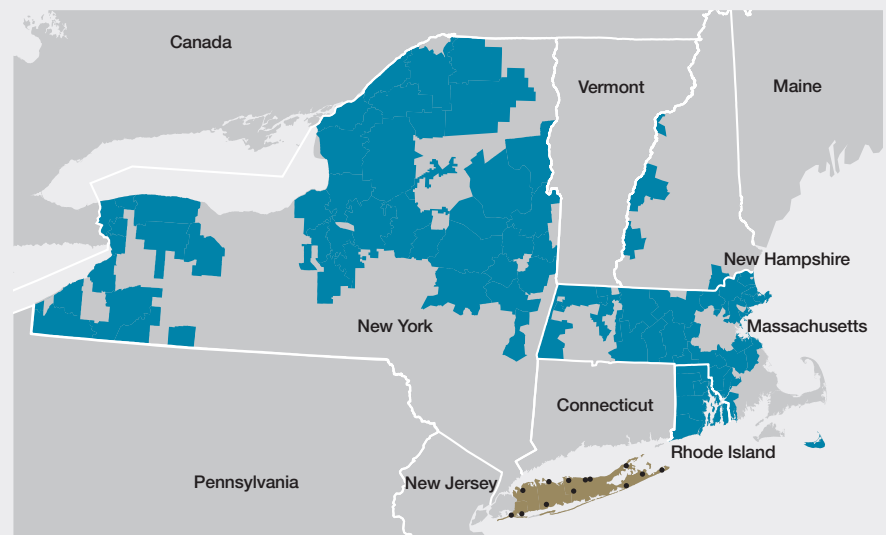
In each state in which we operate, we are allowed to retain some of the benefit of efficiency improvements in excess of those built into rate plan assumptions. Typically we retain all the benefits up to a certain level of return on equity, after which we retain only a proportion of the benefits, with the balance returned to customers. A summary of the key features of our rate plans is provided opposite.

Rate plan	Equity return	Equity to debt ratio	Efficiency gains retained
Upstate New York (Niagara Mohawk)	10.6%	48.5/51.5	100% to 11.75% 50% to 14% 25% to 16% 10% above 16%
Massachusetts	10.35%	49.99/50.01	50% above 10.35%
Rhode Island (Narragansett Electric)	9.8%	42.75/57.25	50% from 9.8% to 10.8% 25% above 10.8%
New Hampshire	9.67%	50/50	50% above 11%

The upstate New York rate plan also allows for subsequent recovery of specified electricity related costs and revenue items that have occurred since the rate plan was established, once these amounts exceed individual item thresholds and \$100 million (£66 million) in total. These deferral account items include changes from the levels of pension and post-retirement benefit expenses from levels specified in the rate plan, as well as various other items, including storms, environmental remediation costs, and certain rate discounts provided to customers, together with costs and revenues from changes in tax, accounting and regulatory requirements.

We also have a number of service standards for our operations. Many of these service standards have penalties if we do not achieve certain specified minimum standards.

Electricity Distribution & Generation – operating area



Operational highlights 2009/10

- Achieved PAS 55 certification for Long Island transmission, distribution and generation.
- Achieved all regulatory targets.
- Filed annual five year investment plan with New York Public Service Commission totalling \$2.86 billion.

41%

Reduction in lost time injury frequency rate

\$614m

Planned investment in our networks in 2010/11

Electricity Distribution & Generation continued

External market, energy policy and regulatory and other developments

In addition to the external market developments described on page 17 and the energy policy and regulatory developments described on pages 20 and 21, the following developments are relevant to the Electricity Distribution & Generation business.

Solar filing

Under the Green Communities Act, Massachusetts utilities are permitted to construct, own and operate up to 50 MW of solar generation, subject to approval by the Massachusetts Department of Public Utilities (DPU). On 23 October 2009, the Massachusetts DPU approved our proposal to construct, own and operate approximately 5 MW of solar generation on 5 separate properties that we own. We are permitted to recover the costs of each site and a return on our investment. We are currently in the construction phase of project development and we expect construction of the sites to continue throughout the remainder of the year.

New York smart grid

On 14 January 2010, we filed a petition with the New York Public Services Commission (NYPSC) seeking approval for a modified smart grid programme. The \$123 million programme includes the Company's contribution to three sub projects, which are the recipient of Department of Energy (DOE) matching funds and additional investments sought directly from the NYPSC. The proposed smart grid programme includes approximately 40,000 customers in the Syracuse, NY area.

The three smart grid sub projects that are the subject of matching funds from the DOE and in which we are a partner have been approved by the NYPSC. On 1 April 2010, we filed a methodology with the NYPSC by which we would recover our investments in these projects from customers.

Massachusetts wind power

On 7 May 2010, we signed an agreement with Cape Wind to buy clean power from the first large-scale offshore wind farm in the US. The contract has been filed with the Massachusetts DPU for approval. Cape Wind is expected to come online by the end of 2012. Under the contract, National Grid would purchase 50% of the wind farm's output, including renewable energy certificates as well as capacity and energy, beginning in 2013.

Massachusetts smart grid

On 1 April 2009, we filed a petition with the Massachusetts DPU in response to the Massachusetts Green Communities Act seeking approval for an approximately \$57 million smart grid programme in the northwest section of Worcester, MA. The pilot programme would reach approximately 15,000 homes and small businesses and features new services to customers delivered through a holistically designed smart grid. The technology proposed includes smart meters, home energy automation and advanced power network management tools. The proposed smart grid pilot has three broad objectives: it will enable customers to actively manage energy use; create the tools for National Grid to optimise the performance of the network; and provide capability to integrate renewable energy generation technologies to the distribution grid. A decision is expected by 1 August 2010.

LIPA power supply agreement (PSA) rate adjustment

On 5 January 2010, the FERC approved a settlement agreement for a rate increase for the power supplied to LIPA. Rates pursuant to the PSA are in effect until May 2013. The settlement agreement

set a revenue requirement of \$436 million and a rate increase of \$66 million, at a return on equity of 10.75%. The PSA also allows for certain annual rate adjustments, such as pension and other post-retirement benefit expenses, property tax increases and certain inflationary increases.

Upstate New York capital expenditure rate filing

In New York, capital expenditure in the rate plan for electricity distribution remains set at historic levels that are significantly lower than those currently required to maintain a safe and reliable network. We filed a supplemental petition in April 2009 for deferred recovery of incremental investments in 2008 totalling \$9 million. In 2010, we anticipate petitioning for deferred recovery of qualifying incremental investment for calendar year 2009.

On 29 January 2010, we filed our annual five year capital investment plan with the NYPSC totalling \$2.86 billion.

Upstate New York electricity rate plan

On 29 January 2010, we filed a three year rate proposal, which includes a revenue increase of \$369 million and a return on equity of 11.1%, effective from 1 January 2011, while allowing us to continue our significant investment in the electricity transmission and distribution system to meet the growing and changing needs of customers. The plan would have little or no impact on typical customer delivery bills. The proposed revenue increase represents recovery of costs we expect to incur in excess of current rate levels. To offset this, we have proposed to defer the full recovery of stranded costs and instead will spread them over an additional three years to the end of 2014. The filing also proposed a revenue decoupling mechanism as required by the NYPSC. We also proposed to enhance our support programmes for qualifying low income customers, increasing programme funding by approximately \$9 million and increasing credits to qualifying customers in our low income customer assistance affordability programme and the low income credit programme.

Massachusetts and Rhode Island rate plans

In 2009, we filed in Massachusetts and Rhode Island rate adjustments effective from 1 January 2010 and 1 March 2010 respectively. Each filing included a request for an increase in revenue to fund distribution operations, a revenue decoupling mechanism proposal to further encourage aggressive pursuit of energy efficiency, and the ability to pass through actual pension and other post-retirement benefit costs. On 30 November 2009, the Massachusetts regulators ruled on our request. The allowed increase in revenue of \$42 million, reflects an allowed return on equity of 10.35%, approval of a revenue decoupling mechanism that includes recovery of incremental investment pursuant to a maximum allowable threshold of up to \$170 million, and approval of the pass through of pension and other post-retirement benefit costs. Rates went into effect on 1 January 2010.

On 9 February 2010, the Rhode Island regulator ruled on our request, allowing an increase in revenue of \$23.5 million, reflecting an allowed return on equity of 9.80% and an equity ratio of 42.75%. The regulator denied our revenue decoupling mechanism proposal and our pass through of pension and other post-retirement benefit costs. On 20 April 2010, we filed a petition with the Rhode Island Supreme Court requesting that it review the legality and reasonableness of the regulator's decision. We plan to file a new rate case later this year.

New Hampshire

We are currently evaluating options to allow us to exit our gas and electricity businesses in New Hampshire.

Niagara Mohawk management audit

New York law provides the NYPSC with the authority to conduct a management audit of utilities operating within the state every five years. Consequently, the NYPSC ordered an audit of Niagara Mohawk's electricity business in 2008. The final audit report contained 44 recommendations for improvement. On 16 December 2009, the NYPSC approved the management audit findings. We had already recognised many of the recommendations and actions were under way, particularly the Electricity Distribution & Generation transformation effort. The implementation plan was filed with NYPSC on 29 January 2010. We will file quarterly update reports to the NYPSC staff.

Performance against our objectives

National Grid's progress against the Company objectives is set out on pages 30 to 37. We include below further information specific to Electricity Distribution & Generation with respect to the objectives that are closely aligned to the lines of business.

Driving improvements in our safety, customer and operational performance

Our objectives are to reduce employee lost time injuries to zero, to meet customer service objectives agreed with our regulators and to be within the upper quartile of customer satisfaction in the territories in which we operate.

Safety

The number of employee lost time injuries in Electricity Distribution & Generation decreased to 23 compared with 37 in 2008/09. Our lost time injury frequency rate for 2009/10 was 0.13, representing a 41% decrease over the prior year's rate of 0.22. Improvement programmes implemented in 2009/10 were aimed at aligning our merged operations in key areas of safety and occupational health management and to promote a positive safety culture. The key safety initiatives during 2009/10 were as follows:

- developing and implementing a comprehensive approach to enhancing safety by driving consistent safety improvement initiatives across all areas, through the safety performance committee (SPC) structure;
- building on the safe and unsafe acts (SUSA) programme to eliminate at risk behaviour while reinforcing safe behaviour and identifying and implementing corrective measures identified by the SPC through analysis of trends from SUSA visits;
- improving the quality of the job brief process by redesigning the process to improve risk assessment and hazard identification, and implementing enhancements in the field;
- reducing road traffic accidents by undertaking targeted defensive driving training for high risk employees in accordance with the current guidelines; and
- improving the quality of near miss reports and the process for actions and feedback to employees by implementing a new communication programme to promote quality reporting that may prevent injuries.

In 2010/11, our safety objectives include implementing sustainable programmes focused on embedding process safety with a robust set of KPIs, a further focus on the quality of root cause analysis with a standardisation of analysis tools, and the detailed analysis of high potential incidents.



Electric transportation

National Grid is taking part in a comprehensive research and demonstration collaboration with Ford Motor Company, Electric Power Research Institute and other electricity utilities to advance the development of electric transportation infrastructure. We are using a pre production Ford Escape plug in hybrid electric vehicle as a test bed to demonstrate the integration with smart grid technology.



We invested this year to make our generating stations greener

We have recently completed upgrading the first of four units at our generating station in Northport, Long Island. This involved installing advanced turbine components to improve efficiency and reduce emissions. The efficiency improvements on this first unit will reduce annual fuel consumption and carbon dioxide emissions by over 25,000 tonnes per year – equivalent to removing an estimated 4,780 cars each doing 12,000 miles a year from the road in the US.

Electricity Distribution & Generation continued

Customer service

Reliable and efficient customer services are priorities for National Grid. Improvements in our operations and how customers conduct their business with us have led to improvements in customer satisfaction. A key customer satisfaction metric is the J.D. Power and Associates customer satisfaction study. A global marketing information company, J.D. Power conducts independent and unbiased surveys of customer satisfaction, product quality and buyer behaviour. In the most recent surveys we improved our ranking, moving into the third quartile performance in three of the four surveys.

We continue to enhance the experience customers have with us, giving them the channels and options they want to conduct their business with us. Our contact and support centre successfully completed 2009 with all regulatory service level and customer satisfaction targets having been exceeded.

Customer satisfaction also comes from helping customers manage their energy expenses. With a US customer communications initiative, 3% Less, we urged customers to pledge to use 3% less energy every year for the next 10 years. By reducing energy consumption, customers can better manage their energy costs and reduce carbon emissions, helping not only their own finances, but our planet. Being the energy management partner for our customers helps foster a stronger relationship with them and builds goodwill among other constituents. The initiative was recognised by the Edison Electric Institute, the association of US shareholder owned electricity companies, which awarded us a 2009 Advocacy Excellence Award in January 2010.

We continue to help customers to be more energy efficient through our energy efficiency programmes. For more than 20 years we have offered a comprehensive portfolio of energy efficiency programmes to help customers reduce energy consumption, saving them money while reducing greenhouse gas emissions. The success of these programmes was recognised by the US Environmental Protection Agency which awarded us a 2009 ENERGY STAR Sustained Excellence Award.

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

Our aim is to meet or exceed the base financial returns in our rate plans by delivering on long-term contracts that provide value.

A summary of returns under our rate plans is provided below.

Regulatory entity	Rate base ⁽ⁱ⁾		Return on equity ⁽ⁱⁱ⁾		Allowed return current
	2009	2008	2009	2008	
Niagara Mohawk (Electric)	\$4,375m	\$4,609m	5.1%	6.7%	10.6%
Massachusetts (Electric)	\$1,494m	\$1,495m	4.7%	7.0%	10.35%
Narragansett Electric (Distribution only)	\$548m	\$564m	(2.9)%	2.3%	9.8%
Long Island Generation	\$503m	\$574m	13.5%	7.1%	10.75%

(i) Estimate of rate base using filed regulatory returns at 31 December or an alternative US GAAP based invested capital measure where recent rate base filings are either not available or where the actual rate base currently excludes certain regulatory asset balances.

(ii) Based on regulatory returns for the 12 months ended 31 December.

Our US electricity businesses are coming out of long-term rate plans and have requested increases in revenue to support their operations. We filed and received approval for increased revenue for our Massachusetts and Rhode Island (Narragansett) electricity operations as the actual returns earned (adjusted for Narragansett's share of merger savings) were below allowed returns, primarily due to higher levels of investment and continued cost pressures, particularly bad debts and storm costs. The revenue increases were effective from 1 January 2010 in both Massachusetts and Rhode Island. As discussed on page 21, our Massachusetts regulator approved full recovery of commodity-related bad debt and working capital costs, a revenue decoupling mechanism, full recovery of pension and other post-retirement costs, and recovery of capital investment up to a maximum of \$170 million per annum.

In New York, the regulatory return on equity includes electricity transmission, electricity distribution and stranded cost recoveries. For the year ended 31 December 2009, the return was 5.1%, adjusted for the Company's share of merger savings allocated to electricity and certain one-off costs. Although the long-term electricity rate plan concludes on 31 December 2011, in response to the decreasing returns for our New York electricity operations, we filed a three year rate plan on 29 January 2010, and updated that request on 3 May 2010, to adjust our delivery rates that, if approved, would take effect on 1 January 2011. The request, as discussed on page 33, includes an increase in distribution and transmission revenue of \$369 million, a revenue decoupling mechanism and recovery of capital investment we make above the level included in the rate plan. To mitigate the impact to our customers, we have proposed to reshape the recovery of our stranded costs, lengthening the time over which we are recovering these legacy costs. We anticipate a regulatory decision sometime in December 2010.

Our Long Island generation business filed with FERC for a rate increase effective from 1 February 2009, subject to refund. LIPA and National Grid Generation filed a settlement on 23 October 2009 with a FERC administrative law judge that provides for a revenue requirement of \$436 million, a rate increase of approximately \$66 million, a return on equity of 10.75% and a capital structure of 50% debt and 50% equity. FERC approved the settlement on 5 January 2010. The Order accepting the settlement was subject to rehearing until 4 February 2010. There were no requests for rehearing and, as such, the settlement became effective from 1 March 2010 and refunds retroactive to 1 February 2009, including interest, were issued in March 2010.

Modernising and extending our transmission and distribution networks

In addition to meeting reliability performance targets agreed with our regulators, our objectives are to improve reliability and to deliver our capital investment programme.

Reliability

Our customers depend on a reliable electricity distribution service. Upstate New York met its regulatory targets for the second consecutive year, Massachusetts for the third and Rhode Island for the fourth, while New Hampshire's performance was the best since 2003 and Long Island met all targets with the best reliability performance under the contract with LIPA.

We have realised significant benefits from our multi-year reliability enhancement programme, helping to achieve our regulatory and internal targets. We will continue to replace ageing underground

cables, overhead lines, protection/control systems and substation infrastructure as part of our asset replacement programme, and continue our ongoing reliability enhancement programme. This programme also includes feeder hardening and inspection and maintenance. Feeder hardening involves upgrading our overhead electricity circuits by replacing aged and deteriorated components and protecting against lightning strikes and animal contacts. Our inspection and maintenance programme involves increasing our preventative maintenance and repair activities to find potential faults before they occur to improve reliability and public safety.

We will also continue our vegetation management programme across all operating areas, increasing our focus on dealing with hazardous trees.

We plan to invest over \$600 million in our networks across New England and New York during 2010/11, delivering on our commitment to invest \$1.47 billion in upstate New York over five years. In addition, with the asset replacement programme agreed with LIPA, we will be managing an estimated \$250 million investment in distribution and transmission infrastructure on behalf of LIPA.

Capital investment

Capital investment in the replacement, reinforcement and extension of our US electricity distribution networks was £372 million in 2009/10, £355 million in 2008/09 and £257 million in 2007/08. After excluding the effect of exchange movements of £9 million in 2009/10 compared with 2008/09, capital investment increased by £26 million.

This primarily reflected higher distribution line spending associated with our feeder hardening and inspection and maintenance programmes of £12 million, improvement in substation asset condition in the New England region of £15 million, higher renewables spend relating to our investment in 5 MW of solar generation in Massachusetts of £3 million and site renovations at our Northborough and Syracuse facilities of £16 million. This has been partially offset by lower spend on leased fleet vehicles due to the timing of contract negotiations of £5 million, lower capitalisation of pension related costs of £6 million and lower storm related costs of £6 million.

After excluding the effect of exchange movements of £79 million in 2008/09 compared with 2007/08, capital investment increased by £19 million. This primarily reflected a £10 million increase from a full year of generation capital expenditure compared with a partial year in 2007/08 following the KeySpan acquisition, higher investment at the Port Jefferson and Northport generating stations of £7 million, increased capital related storm costs of £6 million and other investment including asset replacement of £23 million. This higher expenditure was partially offset by decreased capital lease additions of £15 million relating to vehicles and a lower need for investment in new business installations of £12 million, as a result of the downturn in the US economy.

We have a global initiative to adopt best in class asset management policies and procedures, with all businesses aiming to become PAS 55 certified. PAS 55 is an industry standard for minimum level of competency and processes to ensure a company's asset management objectives can be fulfilled efficiently and effectively.

We have achieved PAS 55 certification for generation, Long Island transmission and distribution and our distribution assets in upstate New York and New England.

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

Our focus includes completing our remaining transformation initiatives, delivering the benefits of our alignment, and driving continuous improvement and process excellence.

Transforming operations

During the year, we delivered on many initiatives in our transformation programme, including agreement with our upstate New York and New England labour unions on alignment with the operating model, centralised scheduling, asset management and consolidating control centres on Long Island.

The implementation of transformation initiatives will increasingly deliver common processes and cost efficiencies across our business.

Efficiency

By making our processes more efficient, we help to create value for shareholders and provide superior service to our customers.

We will continue to evolve the business and gain alignment in transmission and distribution. In conjunction with the transmission and distribution alignment and delivery of remaining transformation initiatives, we will focus on the following priorities:

- development of a US inventory management model;
- development and implementation of optimal fleet sourcing strategies;
- development and implementation of an operations performance model;
- implementation of the advanced energy consumption initiative; and
- implementation of a cost conscious savings initiative.

Improving efficiency is central to our vision and we remain clear about our responsibility to ensure our operations are as efficient as possible for our customers, communities and regulators.

Customer organisation consolidation

We implemented a new customer organisational model during the final quarter of 2009/10 designed to increase our ability to deliver our customer objectives. The new organisation has been designed to be market driven and focused on delivering integrated energy solutions to our customers including energy efficiency. It will provide customers with a source for their energy needs while striving to continuously improve and benchmark performance.

Electricity Distribution & Generation continued

Financial performance

Adjusted operating profit was £116 million higher in 2009/10 than 2008/09 on a constant currency basis, an increase of 45% largely driven by lower storm costs as a result of the ice storm experienced in December 2008, higher generation profits which reflect the new rate filing and improved LIPA contribution partially offset by higher pass-through costs that primarily relate to the purchase of electricity. Further information is included below.

Financial results

The results of the Electricity Distribution & Generation segment for the years ended 31 March 2010, 2009 and 2008 were as follows:

	Years ended 31 March		
	2010 £m	2009 £m	2008 £m
Revenue excluding stranded cost recoveries	3,963	4,537	3,126
Operating costs excluding exceptional items and remeasurements	(3,589)	(4,272)	(2,796)
Adjusted operating profit	374	265	330
Exceptional items	(61)	(51)	(104)
Remeasurements	19	(109)	91
Stranded cost recoveries	369	426	379
Operating profit	701	531	696

2009/10 compared with 2008/09

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

	Revenue and other operating income £m	Operating costs £m	Operating profit £m
2008/09 results	4,972	(4,441)	531
Add back exceptional items	–	51	51
Add back remeasurements	–	109	109
Add back stranded cost recoveries	(435)	9	(426)
2008/09 adjusted results	4,537	(4,272)	265
Exchange movements	(115)	108	(7)
2008/09 adjusted results at constant currency	4,422	(4,164)	258
Pass-through costs	(440)	411	(29)
Volume, price and weather	(9)	–	(9)
LIPA capital recovery	(29)	29	–
Generation	32	8	40
LIPA contribution	(19)	37	18
Storms	–	80	80
Other direct costs	–	(6)	(6)
Other	6	16	22
2009/10 adjusted results	3,963	(3,589)	374
Exceptional items	–	(61)	(61)
Remeasurements	–	19	19
Stranded cost recoveries	376	(7)	369
2009/10 results	4,339	(3,638)	701

Excluding stranded cost recoveries, revenue reduced by £459 million in 2009/10 on a constant currency basis compared with 2008/09. This was primarily due to lower pass-through costs, of which purchased electricity is the main component. These commodity costs are recovered in full from customers although the recovery of costs can occur in more than one financial year, resulting in a year-on-year operating profit impact.

Revenues also decreased compared with 2008/09 reflecting lower LIPA contribution and LIPA capital recovery partly offset by higher generation revenues. LIPA capital recovery relates to assets which are owned by LIPA but are constructed on behalf of LIPA by National Grid. These costs are fully recoverable. LIPA also contributes under management contracts for the ongoing maintenance of these assets. Generation revenues increased following the reset of generation capacity charges as a result of the new FERC rate order filing. These changes were retrospectively applied to 1 February 2009.

Excluding stranded cost recoveries, operating costs decreased by £575 million on a constant currency basis. This was primarily due to lower purchased electricity costs as referred to above, lower storm costs as the levels of storm activity in 2009/10 were considerably lower than 2008/09 reflecting the impact of the December 2008 ice storm, and lower costs associated with LIPA distribution and generation.

Exceptional costs for 2009/10 primarily related to the electricity distribution operations transformation initiatives, environmental costs associated with site remediation in New England and New York, costs associated with US healthcare reform and merger integration costs which primarily relate to pension and retiree welfare plan amendments.

2008/09 compared with 2007/08

The principal movements between 2007/08 and 2008/09 can be summarised as follows:

	Revenue and other operating income £m	Operating costs £m	Operating profit £m
2007/08 results	3,508	(2,812)	696
Add back exceptional items	–	104	104
Add back remeasurements	–	(91)	(91)
Add back stranded cost recoveries	(382)	3	(379)
2007/08 adjusted results	3,126	(2,796)	330
Exchange movements	957	(856)	101
2007/08 adjusted results at constant currency	4,083	(3,652)	431
Purchased electricity	176	(187)	(11)
Volume, price and weather	6	–	6
LIPA capital recovery	74	(74)	–
Generation	124	(114)	10
LIPA contribution	77	(65)	12
Bad debt expense	–	(14)	(14)
Storms	–	(74)	(74)
Other direct costs	–	(53)	(53)
Depreciation and amortisation	–	(10)	(10)
Other	(3)	(29)	(32)
2008/09 adjusted results	4,537	(4,272)	265
Exceptional items	–	(51)	(51)
Remeasurements	–	(109)	(109)
Stranded cost recoveries	435	(9)	426
2008/09 results	4,972	(4,441)	531

Comparability of our financial results between 2008/09 and 2007/08 is affected by having a full year contribution from KeySpan operations in 2008/09 compared with a partial contribution in 2007/08 following the acquisition on 24 August 2007. In 2008/09, KeySpan operations contributed £662 million, £607 million and £55 million to revenue and other operating income (excluding stranded cost recoveries), adjusted operating costs and adjusted operating profit respectively, compared with £383 million, £350 million and £33 million in 2007/08 on a constant currency basis.

Excluding stranded cost recoveries, revenue increased by £454 million in 2008/09 on a constant currency basis as compared with 2007/08. This was primarily due to the recognition of LIPA capital recoveries, LIPA contribution and generation revenues reflecting the full year KeySpan contribution. Revenues from the generation business also increased compared with 2007/08 reflecting a full year KeySpan contribution. Generation revenues also increased following the reset of generation capacity charges which were retrospectively applied to January 2008. There is a corresponding increase in costs partly offsetting some of this benefit.

Revenues also increased compared with 2007/08 reflecting the pass-through of higher purchased electricity costs. The recovery of these costs is described opposite.

Excluding stranded cost recoveries, operating costs increased by £620 million on a constant currency basis. This was primarily due to the higher costs associated with LIPA distribution and generation and purchased electricity as referred to above, in addition to higher storm costs associated mainly with the December 2008 ice storm.

The £166 million decrease on a constant currency basis in adjusted operating profit in 2008/09 compared with 2007/08 was primarily due to higher storm costs, higher capital related costs, which impacted depreciation and other direct costs, and higher purchased electricity, partially offset by the benefits of a full year of KeySpan.

Exceptional costs for 2008/09 primarily related to the electricity distribution operation's transformation initiatives and merger related integration costs.



Solar developments

In late 2009, the Massachusetts regulator approved National Grid's proposal to install approximately 5 MW of solar electricity generation – the biggest installation in the state. The largest of these projects is being constructed in Greater Boston, next to National Grid's multicoloured LNG tank. This was formerly a manufactured gas plant site and, as a result, the contaminated land has limited uses, making it an ideal site for a solar project. The site will include 6,300 solar panels spread over 6 acres of land, providing up to 1.3 MW of power.

Non-regulated businesses and other



Adjusted operating profit

£146m

(2008/09: £65m)

Capital investment

£307m

(2008/09: £427m)

Employees

3,533*

(2008/09: 3,597*)

LNG imported to the UK through Isle of Grain (tonnes)

3.4m

(2008/09: 1.2m)

* Excluding shared services employees

The majority of our non-regulated businesses and other activities either operate in markets related to those of our principal businesses or provide support to our own businesses.

Construction of phase III at our liquefied natural gas (LNG) importation terminal on the Isle of Grain continues on track for completion in winter 2010/11. The site currently has annual import capacity of 9.8 million tonnes and by winter 2010/11, with the phase III expansion, it will have the capacity to import 14.8 million tonnes per annum, around 20% of the UK's forecast gas demand.

During the year, the OnStream portfolio of meters increased by approximately 627,000 assets, comprising approximately 410,000 gas and 217,000 electricity meters.

This section should be read in conjunction with the rest of this Operating and Financial Review.

About our non-regulated businesses

Our non-regulated businesses and other activities are located principally in the UK. For reporting purposes, they do not constitute a segment, but are instead reported within other activities.

Principal operations

In addition to our principal lines of business, other activities comprise the following other operations and corporate activities.

Metering

National Grid Metering and OnStream provide installation and maintenance services to energy suppliers in the regulated and unregulated markets respectively. OnStream also provides meter reading services. Our metering businesses provide services for an asset base of about 20 million domestic, industrial and commercial meters.

xoserve

xoserve delivers transportation transactional services on behalf of all the major gas network transportation companies in Great Britain, including National Grid. xoserve is jointly owned by the five major gas distribution network companies and our UK Transmission business is the majority shareholder.

Grain LNG

National Grid Grain LNG was the first new LNG importation terminal constructed in the UK for some 30 years, with construction divided into phases I and II (both fully operational) and III (under construction).

US non-regulated businesses

Includes LNG storage, LNG road transportation, unregulated transmission pipelines and West Virginia gas fields.

Fulcrum

Fulcrum operates across the UK mainland and offers multi-utility connections and environmental services for all customer categories. As a gas transporter, Fulcrum designs, constructs, owns and operates distribution systems.

UK Property

National Grid Property is responsible for managing our occupied properties in the UK, and for the management, clean up and disposal of surplus sites, most of which are former gasworks.

Blue-NG

Blue-NG is a joint venture between National Grid and 20C Ltd to construct and operate a new type of highly efficient power station that makes use of the requirement to reduce pressure at pressure stations, while generating renewable electricity and heat.

BritNed

BritNed is a joint venture between National Grid and TenneT, the Dutch transmission system operator, to build and operate a 1,000 MW, 260 km subsea electricity link between The Netherlands and the UK.

Corporate activities and shared services function

Corporate activities comprise central overheads, insurance and expenditure incurred on business development.

Business drivers

The principal business drivers for our non-regulated businesses and other activities include the following:

Multi-year contractual arrangements

OnStream has a long-term contract with British Gas for the provision of gas and electricity meters (but see Current and future developments below), and a range of contracts with other suppliers.

Phase I of Grain LNG is underpinned by a long-term contract with BP/Sonatrach. Phase II, completed in December 2008, is underpinned by long-term contracts signed with Centrica, Gaz de France Suez and Sonatrach. Phase III, due to be commissioned in winter 2010/11, also has long-term contracts for all the capacity with E.ON, Iberdrola and Centrica.

Competition

OnStream operates in the competitive market for the provision of new meters and its revenues are therefore determined by how successful it is in obtaining business from customers.

Capital investment

OnStream are investing in technology such as smart metering capabilities to grow our metering business. There is also significant investment in infrastructure projects such as Grain LNG and BritNed.

Efficiency

Efficiency in delivering capital programmes and in operating our businesses and corporate activities result in driving improved financial performance.

External market and regulatory environment

With the exception of National Grid Metering and Fulcrum's independent gas transporter (IGT) business, our non-regulated businesses and other activities are only indirectly affected by the relevant regulatory regimes. National Grid Metering, in its capacity as National Grid Gas's service provider, is regulated by Ofgem. It retains a large share of the legacy installed base of gas meters in the UK and is subject to a tariff cap price control. Fulcrum's IGT business is regulated under the terms of its gas transporter licence.

OnStream operates in the competitive market for the provision of new meters to gas and electricity suppliers who wish to install or replace meters as required. Grain LNG has been granted exemptions by Ofgem from the regulated third party access provisions for phases I, II and III of its development. These exemptions introduced certain obligations for effective measures to allow third parties to access unused capacity and are similar in nature to those in place at other new UK gas supply projects.

Current and future developments

To support the government's mandate to install smart meters in every home by 2020, OnStream has developed dual fuel smart capabilities. It has also developed an innovative smart metering solution and has secured its first dual fuel smart metering contract, all of which is designed to enable OnStream to become the smart metering provider of choice in the market.

Metering competition investigation

An update on the ongoing metering competition investigation that was reported in last year's Annual Report and Accounts is provided on page 80.

British Gas metering insourcing programme

British Gas, OnStream's most significant customer, has reviewed its strategy with regard to its metering operations and has decided to take some of these activities in-house. This decision

will adversely impact OnStream's future workload. However, meters fitted for British Gas customers continue to earn revenue for the life of the asset.

Performance against our objectives

National Grid's progress against the Company objectives is set out on pages 30 to 37. We include below further specific information with respect to the objectives that are closely aligned to our non-regulated businesses and other activities.

Driving improvements in our safety, customer and operational performance

Our objectives include zero employee lost time injuries and to operate reliably. We also aim to improve the quality of service to our customers.

There was a decrease in the total number of employee lost time injuries in non-regulated businesses and other activities to 11 in 2009/10 compared with 17 in 2008/09.

National Grid Metering has met 17 out of 18 standards of service in 2009/10 and 2008/09.

Expanding our capabilities and identifying new financeable opportunities to grow

We are on track to deliver on our capital investment programme for non-regulated businesses and other activities.

During 2009/10, we invested £307 million in our non-regulated businesses and other activities, £120 million lower than in 2008/09, which had been £44 million higher than in 2007/08.

We invested £121 million (2008/09: £137 million; 2007/08: £126 million) in our metering businesses. OnStream continued to invest in new and replacement meters, and smart metering capabilities. National Grid Metering invested in new and replacement meters.

We continued to invest in our Grain LNG facility, with capital expenditure of £117 million in 2009/10 compared with £213 million in 2008/09. The investment related mainly to the continued construction on phase III. Phase III involves construction of a second unloading jetty, an additional 190,000 cubic metre LNG storage tank and associated processing equipment. Phase III is expected to increase the capacity available at the terminal to 14.8 million tonnes per annum, equivalent to around 20% of anticipated UK gas demand for 2010/11. The total planned investment in phase III is approximately £300 million, excluding capitalised interest and gas blending expenditure.

During 2009/10, we invested £69 million in the remaining non-regulated and other activities compared with £77 million in 2008/09. The 2009/10 investment consists of: £40 million within our US operations, principally hardware and software costs relating to SAP implementation; £15 million on our UK property business; £6 million within our xoserve business; and £4 million on both the US non-regulated and Fulcrum businesses.

In addition to the capital expenditure discussed above, we have invested a further £86 million (2008/09: £73 million; 2007/08: £21 million) in joint venture arrangements. The majority of this expenditure related to BritNed, in which we invested £60 million. During the year, work has progressed well on the construction of the link. The civil construction work at both converter station sites in the UK and The Netherlands is now largely complete and

Non-regulated businesses and other continued

work continues to install the electrical equipment. This work is progressing well and is on course for completion in the second half of 2010. Over 90% of the cable which will join the two converter stations has been manufactured, and activity during 2009 included the shore landing in The Netherlands and a section of cable off the UK coast. The shore landing in the UK and the remaining subsea cable lengths will be laid during 2010 in anticipation of the link being fully operational in the first quarter of 2011.

During 2009/10, £19 million was invested in the Blue-NG joint venture to enable finalisation of the development phase and commence construction (2008/09: £2.5 million). Construction contracts for the first two sites are in place and detailed design work is well under way.

Together with our Belgian counterpart, Elia, we are developing an electricity interconnector which will have a nominal capacity of 1,000 MW and is expected to be operational around 2017. The interconnector will comprise approximately 150 km of subsea cable and a converter station in each country connecting to the high voltage transmission systems.

In conjunction with our Norwegian counterpart, Statnett, we have announced plans to investigate further the feasibility of an electricity interconnector linking the UK and Norway. The link would have a nominal capacity of 1,000-1,500 MW and would be capable of allowing connections from offshore generators.

Financial performance

The results for non-regulated businesses and other activities for the years ended 31 March 2010, 2009 and 2008 were as follows:

	Years ended 31 March		
	2010 £m	2009 £m	2008 £m
Revenue	738	719	642
Operating income	3	31	67
Operating costs excluding exceptional items	(595)	(685)	(580)
Adjusted operating profit	146	65	129
Exceptional items	(87)	(64)	(57)
Operating profit	59	1	72

2009/10 compared with 2008/09

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

	Revenue and other operating income £m	Operating costs £m	Operating profit £m
2008/09 results	750	(749)	1
Add back exceptional items	–	64	64
2008/09 adjusted results	750	(685)	65
Exchange movements	(3)	3	–
2008/09 constant currency results	747	(682)	65
Metering	3	26	29
Property	(31)	36	5
Grain LNG	63	(33)	30
US non-regulated businesses	(20)	27	7
Other activities	(21)	31	10
2009/10 adjusted results	741	(595)	146
Exceptional items	–	(87)	(87)
2009/10 results	741	(682)	59

Revenue and other operating income from non-regulated businesses and other activities decreased by £9 million in 2009/10. The principal reason for this was a decrease in revenue and other operating income in our Property business. Due to the ongoing downturn in the property market, we are not seeking to sell our non operational sites surplus to our requirements, as we believe that we can derive greater shareholder value by their retention. In addition, revenue and other operating income from our US non-regulated businesses was £20 million lower at constant currency, reflecting lower volumes of work together with reductions in gas prices.

Partially offsetting these reductions, revenue at Grain LNG was £63 million higher, reflecting the first full year of operations of phase II.

Operating costs excluding exceptional items decreased by £90 million in 2009/10 compared with 2008/09. Property costs were £36 million lower, reflecting our decision to defer sales of our surplus sites in current market conditions. Metering costs were £26 million lower, as a result of lower depreciation charges on our meters and lower meter workforce costs. In addition, operating costs at our US non-regulated businesses were £27 million lower at constant currency, due to lower volumes and gas prices. Offsetting these decreases, operating costs at Grain LNG were £33 million higher due to a full year of operations of phase II.

Contributions to adjusted operating profit included: £162 million (2008/09: £133 million) from Metering; £6 million (2008/09: £1 million) from Property; £51 million (2008/09: £21 million) from Grain LNG; and £3 million profit (2008/09: £4 million loss) from US non-regulated businesses.

Exceptional items of £87 million in 2009/10 included a £41 million charge in Metering relating to a £15 million fine levied upon us by the Gas and Electricity Markets Authority, and a further £26 million in respect of associated costs and provisions against receivables and other balance sheet items. For further information on this, please refer to note 28(f) on page 152. An environmental charge of £28 million has been recognised in our Property business as a result of changes in landfill tax legislation in the UK. Restructuring costs of £17 million have been incurred in our US

non-regulated businesses and corporate activities. In addition, £1 million has also been incurred in our US non-regulated businesses for US healthcare costs arising from recent legislative changes.

2008/09 compared with 2007/08

The principal movements between 2008/09 and 2007/08 can be summarised as follows:

	Revenue and other operating income £m	Operating costs £m	Operating profit £m
2007/08 results	709	(637)	72
Add back exceptional items	–	57	57
2007/08 adjusted results	709	(580)	129
Exchange movements	17	(17)	–
2007/08 constant currency results	726	(597)	129
Metering	7	22	29
Property	(49)	(43)	(92)
Grain LNG	33	(24)	9
US non-regulated businesses	51	(53)	(2)
Other activities	(18)	10	(8)
2008/09 adjusted results	750	(685)	65
Exceptional items	–	(64)	(64)
2008/09 results	750	(749)	1

Revenue primarily increased due to a full year of contribution from the US non-regulated businesses acquired with KeySpan, a £33 million increase in revenue from Grain LNG and a £17 million increase in 2007/08 due to movements in exchange rates. The increased revenue from Grain LNG is due to a full year contribution from phase I of the facility and three months contribution from phase II. These increased revenues were partially offset by a decrease of £49 million in revenue and other operating income in our Property business. This resulted from a decrease in the level of property sales in 2008/09, reflecting the significant decrease in property prices during 2008/09.

Operating costs excluding exceptional items increased by £105 million in 2008/09 compared with 2007/08 primarily reflecting an increase resulting from a full year of contribution from the US non-regulated businesses acquired with KeySpan. In addition, Property and Grain LNG were £43 million and £24 million higher respectively. This was partially offset by a fall in metering costs.

Contributions to adjusted operating profit include: £133 million (2007/08: £104 million) from Metering; £1 million (2007/08: £93 million) from Property; £21 million (2007/08: £12 million) from Grain LNG; and a loss of £4 million (2007/08: loss £2 million) from US non-regulated businesses.

Exceptional items of £64 million in 2008/09 primarily relate to our Property business that recognised a £24 million exceptional charge relating to significant changes to our environmental provision, and £40 million relating to restructuring charges incurred in the US non-regulated businesses and corporate activities. The environmental charge arose as a result of an increase in estimated site remediation costs following changes in landfill tax legislation in the UK and the significant reduction in the discount rate driven by a fall in the risk free rates in light of instability in the financial markets. The real discount rate used in the UK decreased from 2.5% in 2007/08 to 2.0% in 2008/09.



Grain LNG centre of excellence

Following further recent expansion, Grain LNG is one of the world's largest importation facilities making a vital contribution to UK energy supply security. The commercial arrangements in place are underpinned by long-term contracts with our customers, allowing them flexibility over how they use their contracted capacity. This model has enabled the investment needed in the facility, allowing the business to meet market and customer demands.

A further above ground tank and regasification plant as well as a second jetty have been built and will be operational by winter 2010/11. We are continuing to consult with the market to determine the level of interest in further growth.

Through Grain LNG, we have created a centre of excellence within LNG that will provide benefits for National Grid, its customers and shareholders, and the wider UK energy industry.

Financial position and financial management

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 liquidity position are provided under the heading Funding and liquidity management on page 76 and in note 32(d) to the consolidated financial statements.

Financial position

Balance sheet

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

	Assets £m	Liabilities £m	Net assets £m
Property, plant and equipment and non-current intangible assets	31,244	–	31,244
Goodwill and non-current investments	5,588	–	5,588
Current assets and liabilities	2,700	(3,541)	(841)
Other non-current assets and liabilities	162	(3,381)	(3,219)
Post-retirement obligations	–	(3,098)	(3,098)
Deferred tax	–	(3,324)	(3,324)
Total before net debt	39,694	(13,344)	26,350
Net debt	3,859	(25,998)	(22,139)
Total as at 31 March 2010	43,553	(39,342)	4,211
Total as at 31 March 2009	44,467	(40,483)	3,984

The increase in net assets from £3,984 million at 31 March 2009 to £4,211 million at 31 March 2010 resulted from: the profit for the year of £1,389 million; losses recognised directly in equity of £508 million; dividends payable net of scrip issues of £689 million; and other items totalling £35 million.

Net debt

Net debt decreased by £534 million from £22,673 million at 31 March 2009 to £22,139 million at 31 March 2010. Cash flow from operations of £4.5 billion was offset by capital expenditure of £3.2 billion, payment of dividends of £0.7 billion, and net interest paid of £1.0 billion, resulting in a net cash outflow of £0.4 billion. The impact of the movement in the dollar exchange rate on our dollar denominated debt and other fair value movements decreased net debt by £0.9 billion. A five year history of net debt is shown in figure 1.

At 31 March 2010, net debt comprised borrowings of £25,124 million (2009: £26,793 million) including bank overdrafts of £29 million (2009: £17 million), less cash and cash equivalents of £720 million (2009: £737 million), financial investments of £1,397 million (2009: £2,197 million) and derivative financial instruments with a net carrying value of £868 million (2009: £1,186 million).

The maturity of borrowings at 31 March 2010 is provided in note 21 to the consolidated financial statements and illustrated in figure 3. The maturity of net debt, defined as borrowings plus derivative financial liabilities, less cash and cash equivalents, current financial investments and derivative financial assets, is illustrated in figure 2.

Capital structure

The principal measure of our balance sheet efficiency is our interest cover ratio as described under financial discipline on page 38. Our target long-term range for interest cover is between 3.0

and 3.5, which we believe is consistent with single A range long-term senior unsecured debt credit ratings within our main UK operating companies, National Grid Electricity Transmission plc (NGET plc) and National Grid Gas plc (NGG plc).

Interest cover for the year ended 31 March 2010 increased to 3.9 from 3.1 for the year ended 31 March 2009. The increase occurred as a result of higher operating cash flows and lower interest payments.

Gearing at 31 March 2010 and 31 March 2009, calculated as net debt expressed as a percentage of net debt plus net assets shown in the balance sheet, amounted to 84% and 85% respectively. We do not consider that this standard gearing ratio is an appropriate measure of our balance sheet efficiency as it does not reflect the economic value of the assets of our UK and US regulated businesses.

In addition, we monitor the regulatory asset value (RAV) gearing within each of NGET plc and the regulated transmission and distribution businesses within NGG plc. This is calculated as net debt expressed as a percentage of RAV, and indicates the level of debt employed to fund our UK regulated businesses. It is compared with the level of RAV gearing indicated by Ofgem as being appropriate for these businesses, at around 60%. The table below shows the RAV gearing for NGET plc and for the regulated transmission and distribution businesses within NGG plc as at 31 March 2010 and 31 March 2009. To calculate RAV gearing for the regulated transmission and distribution businesses within NGG plc, we exclude an element of debt that is associated with funding the metering business within NGG plc which no longer has a RAV associated with it.

	2010 %	2009 %
RAV gearing		
Regulated transmission and distribution businesses		
within National Grid Gas plc	57	60
National Grid Electricity Transmission plc	56	58

Some of our regulatory agreements impose lower limits for the long-term senior unsecured debt credit ratings that certain companies within the group must hold or the amount of equity within their capital structures. These requirements are monitored on a regular basis in order to ensure compliance. One of the key limits requires National Grid plc to hold an investment grade long-term senior unsecured debt credit rating. We believe that our aim of maintaining single A range long-term senior unsecured debt credit ratings within our main UK operating companies is consistent with this.

Rights issue

On 19 May 2010, the Board resolved to offer a fully underwritten rights issue to raise approximately £3.2 billion, net of expenses. The proceeds are expected to be used to fund a portion of our capital investment programme and for general corporate purposes. The capital raised will allow us to increase our capital investment in the UK significantly, and assist in maintaining single A credit ratings for our UK operating companies, thereby improving our long-term competitive position.

Liquidity and treasury management

Treasury policy

Funding and treasury risk management for National Grid is carried out by the treasury function under policies and guidelines approved by the Finance Committee of the Board. The Finance Committee (for further details see page 89) has authority delegated from the Board, and is responsible for the regular

review and monitoring of treasury activity and for the approval of specific transactions, the authority for which may be further delegated.

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

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

Commodity derivatives entered into in respect of gas and electricity commodities are used in support of the operational requirements of the business and the policy regarding their use is explained on page 78.

Current condition of the financial markets

During 2009/10, there has been a partial recovery in the global economic situation, following the crisis in the banking system, the failure of individual banks and increased restrictions on lending across the capital and money markets in 2008/09. Credit spreads have narrowed significantly. With our low risk business model and cash flows that are largely stable over a period of years, we were able to access the markets during 2008/09 and have continued to do so in 2009/10, having issued £1,993 million of long-term debt into the capital markets. In addition, we have issued £119 million of commercial paper, all of which remained outstanding as at 31 March 2010. At 1 April 2009, we had drawn down £105 million of uncommitted bank lines for short-term liquidity purposes, all of which was repaid by 31 March 2010. We remain confident of our ability to access the public debt markets in the future. The cost of our new long-term debt has fallen over the last few years, decreasing from around 6.7% in 2007/08 to around 4.6% in 2009/10. This reflects the increase in credit spreads demanded by lenders more than offset by the fall in headline interest rates.

Cash flow and cash flow forecasting

Cash flows from our operations are largely stable over a period of years. Our electricity and gas transmission and distribution operations in the UK and US are subject to multi-year rate agreements with regulators. In the UK, we have largely stable annual cash flows. However, in the US our short-term cash flows are dependent on the price of gas and electricity and the timing of customer payments. The regulatory mechanisms for recovering costs from customers can result in very significant cash flow swings from year to year. Significant changes in volumes in the US, for example as a consequence of abnormally mild or extreme weather or economic conditions affecting the level of demand, can affect cash inflows in particular. In addition, our cash flows arising in the US are exposed to movements in the dollar exchange rate, although our foreign exchange risk management policy aims to limit this exposure. Further detail is provided under the foreign exchange risk management section on page 78.

Both short- and long-term cash flow forecasts are produced regularly to assist the treasury function in identifying short-term liquidity and long-term funding requirements, and we seek to

£43.6bn

Total assets

£4.2bn

Net assets

£22.1bn

Net debt

3.9x

Interest cover

Figure 1 - Net debt at 31 March
£bn

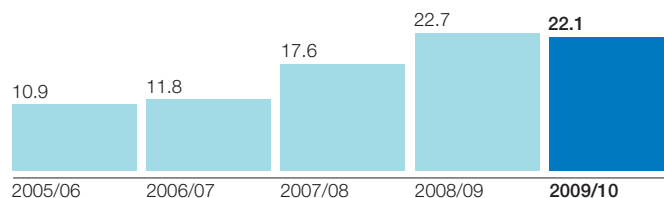


Figure 2 - Maturity of net debt at 31 March 2010
£bn

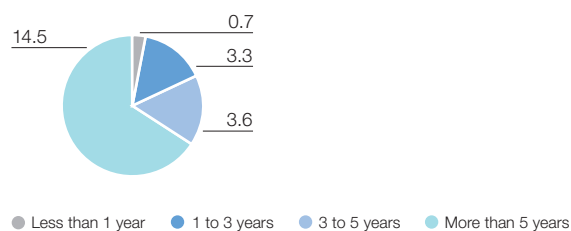
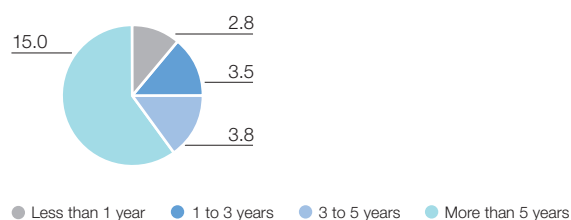


Figure 3 - Maturity of borrowings at 31 March 2010
£bn



Financial position and financial management continued

enhance our cash flow forecasting processes on an ongoing basis. Cash flow forecasts, supplemented by a financial headroom analysis, are monitored regularly to assess funding adequacy for at least a 12 month period.

As part of our regulatory arrangements, our operations are subject to a number of restrictions on the way we can operate. These include regulatory 'ring fences' that require us to maintain adequate financial resources within certain parts of our operating businesses and restrict our ability to undertake transactions between certain subsidiary companies including paying dividends, lending cash and levying charges. Our assessment of National Grid's liquidity takes into account these restrictions.

Funding and liquidity management

We maintain a number of medium-term note and commercial paper programmes in both the UK and the US to facilitate long- and short-term debt issuance into the capital and money markets. National Grid plc also has a Securities and Exchange Commission registered debt shelf in place to facilitate long-term debt issuance specifically into the US capital markets. The table below shows the programmes we had as at 31 March 2010, together with the level of utilisation of each:

Programme	Amount	Status
National Grid plc		
US commercial paper programme	\$3.0 billion	Unutilised
US SEC-registered debt shelf	Unlimited	\$1.0 billion issued
Euro commercial paper programme	\$1.5 billion	£94 million (equivalent) issued
National Grid Electricity Transmission plc		
US commercial paper programme	\$1.0 billion	Unutilised
Euro commercial paper programme	\$1.0 billion	€30 million issued
National Grid plc and National Grid Electricity Transmission plc		
Euro medium-term note programme	€15.0 billion	€9.0 billion issued
National Grid Gas plc		
US commercial paper programme	\$2.5 billion	Unutilised
Euro commercial paper programme	\$1.25 billion	Unutilised
Euro medium-term note programme	€10.0 billion	€5.7 billion issued
National Grid USA		
US commercial paper programme	\$2.0 billion	Unutilised
Euro medium-term note programme	€4.0 billion	€0.1 billion issued

At 31 March 2010, we had signed a £360 million index-linked loan agreement with the European Investment Bank, of which £60 million had been drawn. Since that date a further £180 million has been drawn, and the remaining £120 million will be drawn by 30 June 2010.

In addition, we have both committed and uncommitted bank borrowing facilities that are available for general corporate purposes to support our liquidity requirements. The vast majority of our committed borrowing facilities are used to provide back up to our commercial paper programmes or other specific debt issuances. These have never been drawn and there is currently no intention to draw them in the future.

During the year, the \$850 million short-term committed facility within National Grid plc expired and was renewed at a slightly reduced level and now stands at \$810 million. National Grid USA is also a named borrower under this facility, which includes an option to draw down under the facility for a fixed term of up to 12 months.

The table below shows the bank facilities we had as at 31 March 2010. None of the committed facilities were drawn at any time during the year.

Facility	Amount
National Grid plc and National Grid USA	
Short-term committed facilities	\$810 million
National Grid plc	
Long-term committed facilities	£830 million
Long-term committed facilities	\$280 million
National Grid Gas plc	
Long-term committed facilities	£700 million
National Grid Electricity Transmission plc	
Long-term committed facilities	£425 million
National Grid's US subsidiaries	
Committed facilities	\$530 million
National Grid plc and certain subsidiaries	
Uncommitted borrowing facilities	£528 million

Note 34 to the consolidated financial statements shows the maturity profile of undrawn committed borrowing facilities in sterling at 31 March 2010.

To facilitate debt issuance into the capital and money markets, many of the companies within National Grid maintain credit ratings. At 31 March 2010, the long-term senior unsecured debt and short-term debt credit ratings respectively provided by Moody's Investor Services, Standard & Poor's and Fitch Ratings were as follows (all with outlooks of stable):

Facility	Moody's	S&P	Fitch
National Grid plc	Baa1/P2	BBB+/A2	BBB+/F2
National Grid Holdings One plc	–	BBB+/A2	–
National Grid Electricity Transmission plc	A3/P2	A-/A2	A/F2
National Grid Gas plc	A3/P2	A-/A2	A/F2
National Grid Gas Holdings Ltd	A3	A-*	A
National Grid USA	A3/P2	BBB+/A2	–
Niagara Mohawk Power Corp.	A3	A-/A2	–
Massachusetts Electric Co.	A3/P2	A-/A2	–
New England Power Co.	A3/P2	A-/A2	–
The Narragansett Electric Co.	A3	A-/A2	–
KeySpan Corporation	Baa1/P2	A-/A2	A-
The Brooklyn Union Gas Company	A3	A	A+
KeySpan Gas East Corporation	A3	A	A
Boston Gas Company	Baa1	A-	–
Colonial Gas Company	A3	A-*	–
National Grid Generation LLC	Baa1^	A-*	–

* Corporate credit rating
^ Issuer rating

We invest surplus funds on the money markets, usually in the form of short-term fixed deposits and placements with money market funds that are invested in highly liquid instruments of high

credit quality. Investment of surplus funds is subject to our counterparty risk management policy, and we continue to believe that our cash management and counterparty risk management policies provide appropriate liquidity and credit risk management. Details relating to cash, short-term investments and other financial assets at 31 March 2010 are shown in notes 14 and 20 to the consolidated financial statements.

We believe that maturing amounts in respect of contractual obligations as shown in commitments and contingencies in note 28 to the consolidated financial statements can be met from existing cash and investments, operating cash flows and other financings that we reasonably expect to be able to secure in the future, together with the use of committed facilities if required.

Following the Board resolving to offer a fully underwritten Rights Issue for approximately £3.2 billion, net of expenses, due to be announced on 20 May 2010, and assuming its successful completion, we are of the opinion that it will not be necessary to raise additional funding for working capital purposes in the 12 month period from the date of this Annual Report. However, in line with our normal treasury practice we may continue to access the markets in order to manage actively our debt portfolio, optimise our finance costs and manage our refinancing risk.

Use of derivative financial instruments

As part of our business operations, including our treasury activities, we are exposed to risks arising from fluctuations in interest rates and exchange rates. We use financial instruments, including derivative financial instruments, to manage exposures of this type. Our policy is not to use derivative financial instruments for trading purposes.

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

Refinancing risk management

The Board controls refinancing risk mainly by limiting the amount of debt maturities arising on borrowings in any financial year.

Note 21 to the consolidated financial statements sets out the contractual maturities of our borrowings over the next 5 years, with the total contracted borrowings maturing over 49 years. This shows that, at 31 March 2010, we have £2.8 billion of debt maturing in 2010/11, and no more than £2.1 billion of debt maturing in each of the next four financial years. We expect to be able to refinance this debt through the capital and money markets, as we have done during the year to 31 March 2010.

Interest rate risk management

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

Some of the bonds in issue from NGET plc and NGG plc are inflation-linked, that is their cost is linked to changes in the UK retail price index (RPI). We believe that these bonds provide an appropriate hedge for revenues and our regulatory asset values that are also RPI linked under our price control formulae in the UK.

A3/BBB+

Moody's/S&P senior unsecured ratings for National Grid USA

A3/A-/A

Moody's/S&P/Fitch senior unsecured ratings for NGG plc and NGET plc

Baa1

Moody's senior unsecured rating for National Grid plc

BBB+

S&P and Fitch senior unsecured ratings for National Grid plc

Figure 4 – Interest rate profile pre-derivatives at 31 March 2010 %

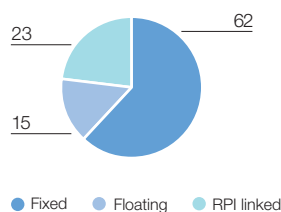


Figure 5 – Interest rate profile post-derivatives at 31 March 2010 %

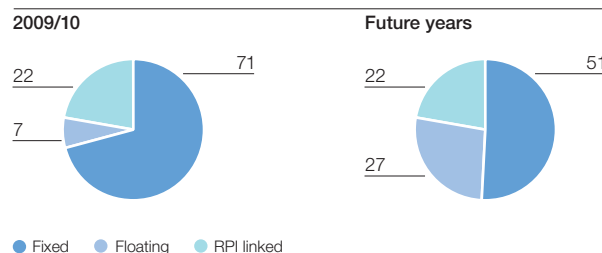
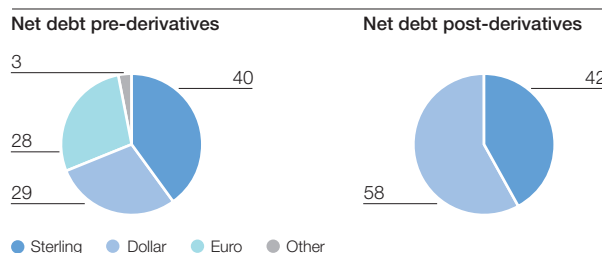


Figure 6 – Currency profile at 31 March 2010 %



Financial position and financial management continued

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

Figure 4 on page 77 shows the interest rate profile of our net debt before derivatives.

Figure 5 on page 77 shows the impact, as at 31 March 2010, of derivatives on our net debt for 2010/11 and for future years. The 2010/11 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.

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

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

More information on the interest rate profile of our debt is included in note 32 to the consolidated financial statements.

Foreign exchange risk management

The principal foreign exchange risk to which we are exposed is translation risk arising from assets and liabilities denominated in dollars. In relation to these risks, our objective is to maintain the ratio of dollar denominated financial liabilities to dollar denominated gross assets between 85% and 95%, by using debt and foreign exchange derivatives, so as to provide an economic offset of our cash flows that arise in dollars against the servicing of those liabilities.

We have a policy of managing our foreign exchange transaction risk by hedging contractually committed foreign exchange transactions occurring in currencies other than the dollar over a prescribed minimum size. This covers a minimum of 75% of such transactions occurring in the next 6 months and a minimum of 50% of such transactions occurring between 6 and 12 months in the future. In addition, where foreign currency cash flow forecasts are uncertain and a judgement has to be made, our policy is to hedge a proportion of such cash flows based on the likelihood of them occurring, with the aim of hedging substantially all the cash flows without overhedging. Cover generally takes the form of forward sale or purchase of foreign currencies and must always relate to forecast underlying operational cash flows.

The result of this hedging activity is that National Grid's cash flow has limited exposure to foreign currencies.

In addition, we are exposed to currency exposures on borrowings in currencies other than sterling and the dollar, principally the euro. This currency exposure is managed through the use of cross-currency swaps, so that post-derivatives the currency profile of our debt is almost entirely sterling/dollar, as shown in figure 6 on page 77.

More details can be found in note 32 to the consolidated financial statements.

Counterparty risk management

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

Where multiple transactions are entered into with a single counterparty, a master netting arrangement is usually put in place to reduce our exposure to credit risk in relation to that counterparty. When transacting interest rate and exchange rate derivatives, we use standard International Swap Dealers Association (ISDA) documentation, which provides for netting in respect of all transactions governed by a specific ISDA agreement with a counterparty.

Further information on the management of counterparty risk is provided in note 32 to the consolidated financial statements.

Valuation and sensitivity analysis

We calculate the fair value of debt and financial derivatives by discounting all future cash flows by the market yield curve, at the balance sheet date, including the credit spread for debt, and, in the case of financial derivatives, taking into account the credit quality of both parties. The market yield curve for each currency is obtained from external sources for interest and foreign exchange rates. In the case of derivative instruments that include options, the Black-Scholes model is used to calculate fair value.

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

As described in note 32 to the consolidated financial statements, movements in financial indices would have the following estimated impact on the financial statements as a consequence of changes in the value of financial instruments. This analysis does not take account of the change in value in our income stream or in the value of our US operations that certain of these financial instruments are being used to hedge.

	2009/10		2008/09	
	Income statement £m	Other equity reserves £m	Income statement £m	Other equity reserves £m
UK retail price index $\pm 0.50\%$	17	–	17	–
UK interest rates $\pm 0.50\%$	51	71	67	77
US interest rates $\pm 0.50\%$	52	14	63	13
US dollar exchange rate $\pm 10\%$	68	623	55	880

Commodity contracts

We purchase electricity and gas in order to supply our customers in the US and also to meet our own energy requirements, primarily in the UK. We also enter into physical and financial

derivative transactions to manage electricity and gas cost volatility on behalf of customers in the US. Substantially all our costs of purchasing electricity and gas for supply to customers are recoverable at an amount equal to cost. The timing of recovery of these costs can vary between financial periods leading to an under- or over-recovery within any particular financial period.

Our US operating companies participate in the physical and financial markets related only to those commodities for which we or our customers have a physical market requirement, and transact only within pre-defined risk parameters. These parameters are approved by the energy procurement risk management committee, which operates in accordance with authority delegated to it by the Finance Committee and Executive Committee of the Board.

The most significant gas purchases for our own use relate to the operation of our gas transmission and gas distribution networks, mainly in the UK. We also purchase fuel for our vehicle fleets in the UK. In the US, we also sell gas produced by our West Virginia gas fields.

In the US, we also have a management contract with ConocoPhillips, under which we and ConocoPhillips share the responsibilities for managing upstream gas distribution assets associated with our Massachusetts gas distribution operations, as well as providing city gate delivered supply. This contract allows for both parties to employ derivative instruments to maximise the profitability of the portfolio of gas distribution assets. Profits associated with these activities are shared between us, ConocoPhillips and our customers in Massachusetts. This contract expires on 31 March 2011.

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

Our UK electricity transmission operations have also entered into electricity options, pursuant to the requirement to stabilise the electricity market in Great Britain through the operation of the British Electricity Trading and Transmission Arrangements (BETTA). The contracts are for varying terms and have been entered into so that we have the ability to deliver electricity as required to meet our obligations under our UK electricity transmission licence. We have not and do not expect to enter into any significant derivatives in connection with our Great Britain national electricity transmission system operator role.

Energy purchase contracts

The majority of our electricity contracts and certain of our gas contracts are entered into to meet our expected purchase, sale or usage requirements and so are accounted for as ordinary sales or purchase contracts. These include contractual commitments to purchase energy under long-term contracts amounting to £3,535 million as at 31 March 2010 (2009: £3,645 million) of which £1,566 million is due within one year (2009: £990 million). Further information is included in note 28 to the consolidated financial statements.

Commodity purchase contracts accounted for as derivative contracts

Certain of our forward purchases of electricity, gas and electricity capacity do not meet the own use exemption for accounting purposes and hence are accounted for as derivatives. Mark-to-market changes in the value of these contracts are reflected through earnings under the heading of commodity remeasurements. The fair value of these contracts includes contracts with a positive value of £51 million (2009: £35 million), recorded as assets in our balance sheet and contracts with a negative value of £228 million (2009: £155 million) recorded as liabilities.

Commodity purchase contracts accounted for as derivatives include contracts for the forward purchase of electricity that reverted to us as part of the settlement arising from USGen's bankruptcy in 2005, which were originally entered into prior to the restructuring of the electricity industry in New England. The electricity purchased under these contracts is not required for our normal activities and is sold in the energy markets at prices which are currently significantly below the amount we are required to pay. The fair value of these contracts amounted to a £127 million liability at 31 March 2010 (2009: £121 million liability).

Derivative financial instruments linked to commodity prices

We also enter into derivative financial instruments linked to commodity prices, including index-linked swaps and futures contracts. These derivative financial instruments are used to reduce market price volatility and are principally used to manage commodity prices associated with our gas and electricity delivery operations in the US on behalf of our customers.

Derivative financial instruments are carried at fair value in the balance sheet and mark-to-market changes in the value of these contracts are reflected through earnings under commodity remeasurements with the exception of those related to our West Virginia gas fields that are designated as cash flow hedges.

We use NYMEX electricity and natural gas futures to reduce the cash flow variability associated with the purchase price for a portion of future electricity and gas purchases associated with certain of our electricity and gas distribution operations in the US. These had a negative fair value at 31 March 2010 of £41 million (2009: £59 million), but the liability on the balance sheet has been reduced by the amount of collateral paid to counterparties in respect of these contracts due to accounting netting requirements for such instruments.

In addition, we utilise over-the-counter swaps and options to reduce the cash flow variability associated with the purchase price for a portion of future electricity and gas purchases associated with certain of our electricity and gas distribution operations in the US. These had a net negative fair value at 31 March 2010 of £45 million (2009: £190 million).

We also utilise over-the-counter gas swaps in the US to hedge the cash flow variability associated with forecast sales of a portion of gas production from our West Virginia gas fields. At 31 March 2010, we had hedge positions in place for approximately 54% of our estimated 2010 and 2011 gas production (2009: 66% of our estimated 2009 and 2010 gas production), net of gathering costs. We use forward prices from a third party vendor to value these swap positions.

Sensitivity analysis

As described in note 33(d) to the consolidated financial statements, movements in commodity prices would have the following estimated impact on the financial statements in the value

Financial position and financial management continued

of commodities. This analysis does not take account of any change in the composition of our commodity portfolio.

	2009/10		2008/09*	
	Income statement £m	Other equity reserves £m	Income statement £m	Other equity reserves £m
10% increase in commodity prices	71	(1)	33	(1)
10% decrease in commodity prices	(64)	1	(43)	1

* Prior year comparatives have been restated to be consistent on a post-tax basis

Commitments and contingencies

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

	2010 £m	2009* £m
Future capital expenditure contracted but not provided for	1,738	1,626
Total operating lease commitments	926	1,085
Power commitments	3,535	3,645
Other commitments, contingencies and guarantees	2,119	1,846

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

The energy commitments shown in the commitments and contingencies table above reflect obligations to purchase energy under long-term contracts. These contracts are used in respect of our normal sale and purchase requirements and do not include commodity contracts carried at fair value as described above.

We propose to meet all 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.

Contractual obligations at 31 March 2010

The table of contractual obligations shown below analyses our long-term contractual obligations according to payment period.

Purchase obligations reflect commitments under power contracts and future capital expenditure contracted for but not provided. The other long-term liabilities reflected in the balance sheet at 31 March 2010 comprise commodity contracts carried at fair value and other creditors that represent contractual obligations falling due after more than one year.

Interest on borrowings is calculated based on borrowings at 31 March 2010 and does not reflect future debt issues. Floating-rate interest has been estimated using future interest rate curves at 31 March 2010.

	Less than 1 year £m	1-3 years £m	3-5 years £m	More than 5 years £m	Total £m
Financial liabilities					
Borrowings	2,390	3,422	3,707	15,220	24,739
Interest payments on borrowings	915	1,719	1,412	8,417	12,463
Finance lease liabilities	30	73	34	135	272
Other non interest-bearing liabilities	2,287	265	–	–	2,552
Derivatives payments	859	1,568	575	1,299	4,301
Derivatives receipts	(1,027)	(1,820)	(1,022)	(1,213)	(5,082)
Commodity contracts	488	203	64	37	792
Other contractual obligations					
Capital commitments	1,376	284	67	11	1,738
Operating leases	91	163	172	500	926
Energy commitments	1,566	1,064	627	278	3,535
Total at 31 March 2010	8,975	6,941	5,636	24,684	46,236

Off balance sheet arrangements

There were no significant off balance sheet arrangements other than the contractual obligations and commitments and contingencies described above.

Details of material litigation as at 31 March 2010

We were not party to litigation that we considered to be material as at 31 March 2010. Save as set out below, there have been no governmental, legal or arbitration proceedings in the last 12 months which may have or have had significant effects on the Company's financial position or profitability.

Metering competition investigation

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

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

Gas Distribution mains replacement investigation

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

KeySpan Department of Justice investigation

As previously reported, in May 2007 KeySpan received a civil investigative demand (CID) from the Antitrust Division of the United States Department of Justice (DOJ), requesting the production of documents and information relating to its investigation of competitive issues in the New York City electricity capacity market prior to our acquisition of KeySpan. In April 2008, we received a second CID in connection with this matter.

On 22 February 2010, DOJ filed a proposed final judgement in the US District Court for the Southern District of New York. Under the terms of the proposed settlement, DOJ and KeySpan have agreed that KeySpan will pay \$12 million in full and final resolution of DOJ's CIDs. This agreement contains no admissions of wrongdoing by KeySpan and remains subject to court approval, which is currently anticipated later in 2010.

KeySpan class action

On 18 March 2010, a putative class action was commenced against KeySpan and Morgan Stanley in the Supreme Court for the State of New York in Bronx County. The complaint alleges four causes of action based on the core allegation that the financial swap transaction between KeySpan and Morgan Stanley dated 18 January 2006 caused customers of Consolidated Edison, Inc. to overpay for electricity between May 2006 and February 2008. The complaint seeks compensatory damages of not less than \$160 million, as well as punitive damages plus legal costs. We believe that the complaint and its allegations are without merit.

Related party transactions

We provide services to and receive services from related parties, principally joint ventures. In the year ended 31 March 2010, we charged £5 million and received charges of £74 million from related parties (other than Directors) compared with £4 million and £44 million in 2008/09 and £3 million and £33 million in 2007/08.

Further information relating to related party transactions is contained within note 29 to the consolidated financial statements. Details on amounts paid to Directors are included within the Directors' Remuneration Report on pages 98 to 108.

Retirement arrangements

We operate pension arrangements on behalf of our employees in both the UK and the US and also provide post-retirement healthcare and life insurance benefits to qualifying retirees in the US.

In the UK, the defined benefit section of the National Grid UK Pension Scheme and the National Grid section of the Electricity Supply Pension Scheme (National Grid Electricity Supply Pension Scheme) are closed to new entrants. Membership of the defined contribution section of the National Grid UK Pension Scheme is offered to all new employees in the UK.

In the US, we operate a number of pension plans, which provide both defined benefits and defined contribution benefits.

We also provide post-retirement benefits other than pensions to the majority of employees in the US. Benefits include health care and life insurance coverage to eligible retired employees. Eligibility is based on certain age and length of service requirements and in most cases retirees must contribute to the cost of their coverage.

Net pension and other post-retirement obligations

The following table summarises the pension and other post-retirement obligations recorded in the consolidated financial statements:

Net plan asset/(liability)	UK £m	US £m	Total £m
As at 1 April 2009	(154)	(2,657)	(2,811)
Exchange movements	–	140	140
Current service cost	(50)	(88)	(138)
Expected return less interest	(76)	(136)	(212)
Curtailments, settlements and other	(17)	(38)	(55)
Actuarial gains/(losses)			
– on plan assets	2,420	772	3,192
– on plan liabilities	(3,038)	(885)	(3,923)
Employer contributions	269	440	709
As at 31 March 2010	(646)	(2,452)	(3,098)
Plan assets	14,883	4,253	19,136
Plan liabilities	(15,529)	(6,705)	(22,234)
Net plan liability	(646)	(2,452)	(3,098)

The amounts recorded in the balance sheet are based on accounting standards which require pension obligations to be calculated on a different basis from that used by the actuaries to determine the funding we need to make into each arrangement. The principal movements in net pension obligations during the year arose as a consequence of actuarial losses on plan liabilities principally as a consequence of using lower discount rates to calculate the present value of these obligations, partially offset by actuarial gains on plan assets.

Actuarial position

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

The last completed full actuarial valuation of National Grid Electricity Supply Pension Scheme was as at 31 March 2007. This concluded that the pre-tax funding deficit was £405 million on the basis of the funding assumptions. Employer cash contributions for the ongoing cost of this plan are currently being made at a rate of 20.5% of pensionable payroll.

Contributions

In addition to ongoing employer contributions, we have agreed to make additional deficit contributions to certain of the above plans as follows:

- National Grid UK Pension Scheme: the Company made deficit contributions of £59 million during 2009/10 which ensured that the deficit reported at the 2007 valuation was paid in full; and
- National Grid Electricity Supply Pension Scheme: the Company made deficit contributions of £90 million during 2009/10 and anticipates no further payments in the year to 31 March 2011, in line with the recovery plan.

The next valuations of these schemes are due as at 31 March 2010.

In accordance with our funding policy for US pension and other post-retirement benefit plans, we expect to contribute approximately £414 million to these plans during 2010/11.

Plan assets

Our plans are trustee administered and the trustees are responsible for setting the investment strategy and monitoring investment performance, consulting with us where appropriate.

Accounting policies

Basis of accounting

The consolidated financial statements present our results for the years ended 31 March 2010, 2009 and 2008 and our financial position as at 31 March 2010 and 2009. They have been prepared using the accounting policies shown, in accordance with International Financial Reporting Standards (IFRS).

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

Choices permitted under IFRS

IFRS provides certain options available within accounting standards. Material 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 balance sheet to net assets and total equity.

In the income statement, we present subtotals of total operating profit, profit before tax and profit from continuing operations, together with additional subtotals excluding exceptional items, 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. For net investment hedges, we have chosen to use the spot rate method, rather than the alternative forward rate method.

Timing of goodwill impairment reviews

Goodwill impairment reviews are carried out annually in the final quarter of the financial year.

Critical accounting policies

The application of accounting principles requires us to make estimates, judgements and assumptions that may affect the reported amounts of assets, liabilities, revenue and expenses and the disclosure of contingent assets and liabilities in the accounts. On an ongoing basis, we evaluate our estimates using historical experience, consultation with experts and other methods that we consider reasonable in the particular circumstances to ensure compliance with IFRS. Actual results may differ significantly from our estimates, the effect of which will be recognised in the period in which the facts that give rise to the revision become known.

Certain accounting policies, described below, have been identified as critical accounting policies, as these policies involve particularly complex or subjective decisions or assessments. The discussion of critical accounting policies below should be read in conjunction with the description of our accounting policies set out in the consolidated financial statements on pages 112 to 117.

Revenue

Revenue includes an assessment of energy and accruals for transportation services, supplied to customers between the date of the last meter reading and the year end. Changes to the estimate of the energy or transportation services supplied during this period would have an impact on our reported results.

Unbilled revenues at 31 March 2010 are estimated at £415 million in the US and £308 million in the UK compared with £522 million and £315 million respectively at 31 March 2009.

Estimated economic lives of property, plant and equipment

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

Hedge accounting

We use derivative financial instruments to hedge certain economic exposures arising from movements in exchange and interest rates or other factors that could affect either the value of our assets or liabilities or our future cash flows. Movements in the fair values of derivative financial instruments may be accounted for using hedge accounting where we meet the relevant eligibility, documentation and effectiveness testing requirements. If a hedge does not meet the strict criteria for hedge accounting, or where there is ineffectiveness or partial ineffectiveness, then the movements will be recorded in the income statement immediately instead of being recognised in other comprehensive income or by being offset by adjustments to the carrying value of debt.

Exceptional items, remeasurements and stranded cost recoveries

Exceptional items, remeasurements and stranded cost recoveries are items of income and expense that, in the judgement of management, should be disclosed separately on the basis that they are material, either by their nature or their size, to an understanding of our financial performance and distort the comparability of our financial performance between periods.

Items of income or expense that are considered by management for designation as exceptional items include such items as significant restructurings, write-downs or impairments of non-current assets, significant changes in environmental or decommissioning provisions, integration of acquired businesses and gains or losses on disposals of businesses or investments.

Remeasurements comprise gains or losses recorded in the income statement arising from changes in the fair value of commodity contracts and of derivative financial instruments. These fair values increase or decrease as a consequence of changes in commodity and financial indices and prices over which we have no control.

Stranded cost recoveries relate to the recovery, through charges to electricity customers in upstate New York and in New England, of costs mainly incurred prior to divestiture of generation assets.

Tax estimates

Our tax charge is based on the profit for the year and tax rates in effect. The determination of appropriate provisions for taxation requires us to take into account anticipated decisions of tax authorities and estimate our ability to utilise tax benefits through future earnings and tax planning.

Carrying value of assets and potential for impairments

The carrying value of assets recorded in the consolidated balance sheet could be materially reduced if an impairment were to be assessed as being required. Impairment reviews are carried out either when a change in circumstance is identified that indicates an asset might be impaired or, in the case of goodwill, annually. An impairment review involves calculating either or both of the fair value or the value in use of an asset or group of assets and comparing with the carrying value in the balance sheet.

These calculations involve the use of assumptions as to the price that could be obtained for, or the future cash flows that will be generated by, an asset or group of assets, together with an appropriate discount rate to apply to those cash flows.

Assets and liabilities carried at fair value

Certain assets and liabilities, principally financial investments, derivative financial instruments and certain commodity contracts, are carried in the balance sheet at their fair value rather than historical cost.

The fair value of financial investments is based on market prices, as is that of derivative financial instruments where market prices exist. Other derivative financial instruments and those commodity contracts carried at fair value are valued using financial models, which include judgements on, in particular, future movements in exchange and interest rates as well as equity and commodity prices.

Provisions

Provisions are made for liabilities, the timing and amount of which is uncertain. These include provisions for the cost of environmental restoration and remediation, decommissioning of nuclear facilities we no longer own but to which we still have a responsibility to contribute, restructuring, and employer and public liability claims.

Calculations of these provisions are based on estimated cash flows relating to these costs, discounted at an appropriate rate where significant. The amounts and timing of cash flows relating to these liabilities are based on management estimates supported by external consultants.

Pensions and other post-retirement obligations

Pensions and other post-retirement benefit obligations recorded in the balance sheet are calculated actuarially using a number of assumptions about the future, including inflation, salary increases, length of service and pension and investment returns, together with the use of a discount rate to calculate the present value of the obligation.

These assumptions can have a significant impact on both the pension obligation recorded in the balance sheet and on the net charge recorded in the income statement.

Energy commitments

Our energy commitments relate to contractual commitments to purchase electricity or gas to satisfy physical delivery requirements to our customers or for energy that we use ourselves. In management's judgement these commitments meet the normal purchase, sale or usage exemption in IAS 39 and are not recognised in the financial statements.

If these commitments were judged not to meet the exemption under IAS 39 they would have to be carried in the balance sheet at fair value as derivative instruments, with movements in their fair value shown in the income statement under remeasurements.

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

Revenue accruals

A 10% change in our estimate of unbilled revenues at 31 March 2010 would result in an increase or decrease in our recorded net assets and profit for the year by approximately £47 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 £39 million (pre-tax) and our annual amortisation charge on intangible assets by £7 million (pre-tax).

Hedge accounting

If using our derivative financial instruments, hedge accounting had not been achieved during the year ended 31 March 2010 then the profit after tax for the year would have been £341 million higher than that reported net of tax, and net assets would have been £299 million lower.

Assets carried at fair value

A 10% change in assets and liabilities carried at fair value would result in an increase or decrease in the carrying value of derivative financial instruments and commodity contract liabilities of £87 million and £22 million respectively.

Provisions

A 10% change in the estimates of future cash flows estimated in respect of provisions for liabilities would result in an increase or decrease in our provisions of approximately £171 million.

Pensions and other post-retirement obligations

Our pension and post-retirement obligations are sensitive to the actuarial assumptions used. A 0.1% increase in the discount rate, a 0.5% increase in the rate of salary increases or an increase of one year in life expectancy would result in a change in the net obligation of £317 million, £166 million and £670 million and a change in the annual pension cost of £4 million, £8 million and £5 million respectively.

Accounting developments

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

In preparing our consolidated financial statements we have complied with International Financial Reporting Standards, International Accounting Standards and interpretations applicable for 2009/10. The standards, amendments to standards and interpretations adopted during 2009/10 are discussed in the consolidated financial statements on page 118. None of these resulted in a material change to our consolidated results, assets or liabilities in 2009/10 or in those of previous periods.

Accounting standards, amendments to standards and interpretations not yet adopted

New accounting standards, amendments to standards and interpretations which have been issued but not yet adopted by National Grid are discussed in the consolidated financial statements on page 119.