

NATIONAL GRID PLC  
Form 20-F  
June 05, 2014  
Table of Contents

**SECURITIES AND EXCHANGE COMMISSION**

Washington, D.C. 20549

**FORM 20-F**

(Mark One)

**REGISTRATION STATEMENT PURSUANT TO SECTION 12(b) OR (g) OF THE SECURITIES EXCHANGE ACT OF 1934**

**OR**

**ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**  
**For the fiscal year ended 31 March 2014**

**OR**

**TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**

**OR**

**SHELL COMPANY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**

Date of event requiring this shell company report \_\_\_\_\_

For the transition period from \_\_\_\_\_ to \_\_\_\_\_

Commission file number: 001-14958

**NATIONAL GRID PLC**

*(Exact name of Registrant as specified in its charter)*

*England and Wales*

*(Jurisdiction of incorporation or organization)*

*1-3 Strand, London WC2N 5EH, England*

*(Address of principal executive offices)*

**Alison Kay**

**011 44 20 7004 3000**

**Facsimile No. 011 44 20 7004 3004**

**Group General Counsel and Company Secretary**

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National Grid plc

1-3 Strand London WC2N 5EH, England

*(Name, Telephone, E-mail and/or Facsimile number and Address of Company Contact Person)*

**Securities registered or to be registered pursuant to Section 12(b) of the Securities Exchange Act of 1934:**

<b>Title of each class</b>	<b>Name of each exchange on which registered</b>
Ordinary Shares of 11 17/43 pence each	The New York Stock Exchange*
American Depositary Shares, each representing five Ordinary Shares of 11 17/43 pence each	The New York Stock Exchange
6.625% Guaranteed Notes due 2018	The New York Stock Exchange
6.30% Guaranteed Notes due 2016	The New York Stock Exchange
Preferred Stock (\$100 par value-cumulative):	
3.90% Series	The New York Stock Exchange
3.60% Series	The New York Stock Exchange

\* Not for trading, but only in connection with the registration of American Depositary Shares representing Ordinary Shares pursuant to the requirements of the Securities and Exchange Commission.

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**Securities registered or to be registered pursuant to Section 12(g) of the Securities Exchange Act of 1934: None.**

**Securities for which there is a reporting obligation pursuant to Section 15(d) of the Securities Exchange Act of 1934: None.**

The number of outstanding shares of each of the issuer's classes of capital or common stock as of 31 March 2014 was

Ordinary Shares of 11 17/43 pence each 3,854,339,684

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act: Yes  No

If this report is an annual or transition report, indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934. Yes  No

Note: Checking the box above will not relieve any registrant required to file reports pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934 from their obligations under those Sections.

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days: Yes  No

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate website, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§ 232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files): Yes  No

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, or a non-accelerated filer. See definition of accelerated filer and large accelerated filer in Rule 12b-2 of the Exchange Act.

Large accelerated filer

Accelerated filer

Non-accelerated filer

Indicate by check mark which basis of accounting the registrant has used to prepare the financial statements included in this filing:

U.S. GAAP  International Financial Reporting Standards as issued by the International Accounting Standards Board  Other

If Other has been checked in response to the previous question, indicate by check mark which financial statement item the registrant has elected to follow. Item 17  Item 18

If this is an annual report, indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). Yes  No

This constitutes the annual report on Form 20-F of National Grid plc (the Company) in accordance with the requirements of the US Securities and Exchange Commission (the SEC) for the year ended 31 March 2014 and is dated 5 June 2014. Details of events occurring subsequent to the approval of the annual report on 18 May 2014 are summarised in section Further Information which forms a part of this Form 20-F. The content of the Group's website (www.nationalgrid.com/uk) should not be considered to form part of this annual report on Form 20-F.

**Table of Contents****Form 20-F Cross Reference Table**

Item	Form 20-F caption	Location in the document	Page(s)
1	<b>Identity of directors, senior management and advisors</b>	Not applicable	
2	<b>Offer statistics and expected timetable</b>	Not applicable	
3	<b>Key Information</b>		
	3A Selected financial data	Additional Information Summary consolidated financial information	186-187
		Strategic Report Financial review	6-9
		Financial Statements Unaudited commentary on consolidated cash flow statement Net debt	91
		Additional Information Other unaudited financial information Reconciliations of adjusted profit measures	182
		Additional Information Other disclosures Exchange rates	178
		Exchange Rates	Further Information
	3B Capitalization and indebtedness	Not applicable	
	3C Reasons for the offer and use of proceeds	Not applicable	
	3D Risk Factors	Additional Information Business information in detail Risk factors	167-169
4	<b>Information on the company</b>		
	4A History and development of the company	Want more information or help?	192-
			Back cover
		Additional Information Other disclosures Key milestones	179
		Strategic Report Chief Executive s review	4-5
		Strategic Report Our vision and strategy	14-15
		Strategic Report Operating environment	12-13
		Additional Information Other disclosures Articles of Association	176-177
		Financial Statements Consolidated statement of financial position Unaudited commentary on consolidated statement of financial position Property, plant and equipment	89
		Financial Statements Consolidated cash flow statement Unaudited commentary on consolidated cash flow statement Net capital expenditure	91
		Additional Information Other unaudited financial information Commentary on consolidated financial statements for the year ended 31 March 2013	183-185

## Edgar Filing: NATIONAL GRID PLC - Form 20-F

	Financial Statements Notes to the consolidated financial statements 2. Segmental analysis (c) Capital expenditure, depreciation and amortisation	95
4B Business overview	Strategic Report How our strategy creates value	21
	Additional Information Business information in detail Where we operate	166
	Strategic Report Operating environment	12-13
	Strategic Report Our vision and strategy ; What we do Electricity ; What we do Gas ; How we make money from our regulated assets ; and How our strategy creates value	14-21

**Table of Contents**

<b>Item</b>	<b>Form 20-F caption</b>	<b>Location in the document</b>	<b>Page(s)</b>
		Strategic Report Our vision and strategy Our business model	14
		Strategic Report Principal operations	29-38
		Strategic Report Non-financial KPIs	10-11
		Financial Statements Notes to the consolidated financial statements 2. Segmental analysis and unaudited commentary on the results of our principal operations by segment	93-96
		Additional Information Business information in detail Risk factors Infrastructure and IT systems We may suffer a major network failure or interruption, or may not be able to carry out critical non network operations due to the failure of technology supporting our business-critical processes ; Changes in law or regulation or decisions by governmental bodies or regulators could materially adversely affect us ; and Customers and counterparties Customers and counterparties may not perform their obligations	167 168
		Additional Information Business information in detail UK 160-165 regulation ; US regulation ; and Summary of US price controls and rate plans	169
		Strategic Report How we make money from our regulated assets	20
4C	Organizational structure	Financial Statements Notes to the consolidated financial statements 32. Subsidiary undertakings, joint ventures and associates Principal subsidiary undertakings	146
4D	Property, plants and equipment	Additional Information Business information in detail Where we operate	166
		Strategic Report What we do Electricity ; What we do and How we make money from our regulated assets	G16-20
		Strategic Report Principal operations	29-38
		Strategic Report Our vision and strategy Embed sustainability and Drive growth	15
		Strategic Report Operating environment Changing energy mix ; Energy policy ; Regulation ; and Innovation and technology	12-13
		Financial Statements Consolidated statement of financial position Unaudited commentary on consolidated statement of financial position Property, plant and equipment	89
		Additional Information Other disclosures Property, plant and equipment	179
		Financial Statements Notes to the consolidated financial statements 11. Property, plant and equipment	111-112
		Financial Statements Notes to the consolidated financial statements 19. Borrowings	119-121
4A	Unresolved staff comments	Additional Information Other disclosures Unresolved SEC staff comments	181

**Table of Contents**

<b>Item</b>	<b>Form 20-F caption</b>	<b>Location in the document</b>	<b>Page(s)</b>
<b>5</b>	<b>Operating and financial review and prospects</b>		
	5A Operating results	Strategic Report Financial review	6-9
		Strategic Report Operating environment	12-13
		Additional Information Business information in detail UK regulation ; US regulation ; and Summary of US price controls and rate plans	160-165
		Strategic Report Principal operations	29-38
		Financial Statements Consolidated income statement Unaudited commentary on the consolidated income statement	85
		Financial Statements Notes to the consolidated financial statements 2. Segmental analysis Unaudited commentary on the results of our principal operations by segment	96
		Additional Information Other unaudited financial information	182-185
		Financial Statements Notes to the consolidated financial statements 30. Financial risk management (d) Currency risk	140-141
	5B Liquidity and capital resources	Strategic Report Financial review	6-9
		Corporate Governance Going concern	52
		Financial Statements Consolidated cash flow statement	90-91
		Additional Information Business information in detail Risk factors Financing and liquidity An inability to access capital markets at commercially acceptable interest rates could affect how we maintain and grow our business	169
		Financial Statements Notes to the consolidated financial statements 2. Segmental analysis Unaudited commentary on the results of our principal operations by segment	96
		Financial Statements Notes to the consolidated financial statements 26. Net debt	130-131
		Financial Statements Notes to the consolidated financial statements 19. Borrowings	119-121
		Financial Statements Notes to the consolidated financial statements 15. Derivative financial instruments	114-116
		Additional Information Business information in detail Federal Energy Regulatory Commission Short-term borrowing extension	164
		Additional Information Directors Report disclosures Material interests in shares	174
		Material Interests in Shares	Further Information
	5C Research and development, patents and licenses, etc.	Additional Information Directors Report disclosures Research and development	174
	5D Trend information	Strategic Report Financial review	6-9
		Strategic Report Principal operations	29-38
		Strategic Report Operating environment	12-13
	5E Off-balance sheet arrangements	Financial Statements Unaudited commentary on consolidated statement of financial condition Off balance sheet items	89

**Table of Contents**

<b>Item</b>	<b>Form 20-F caption</b>	<b>Location in the document</b>	<b>Page(s)</b>
	5F Tabular disclosure of contractual obligations	Financial Statements Notes to the consolidated financial statements 27. Commitments and contingencies	132
	5G Safe Harbor	Important notice	1
		Want more information or help? Cautionary statement	Back cover
<b>6</b>	<b>Directors, senior management and employees</b>		
	6A Directors and senior management	Corporate Governance Our Board	43
		Additional Information Directors Report disclosures Board biographies	171-173
	6B Compensation	Corporate Governance Remuneration Report	58-73
		Financial Statements Notes to the consolidated financial statements 3. Operating costs (c) Key management compensation	98
		Financial Statements Notes to the consolidated financial statements 22. Pensions and other post-retirement benefits	122-125
		Financial Statements Notes to the consolidated financial statements 29. Actuarial information on pensions and other post-retirement benefits	133-136
		Share Ownership	Further Information
	6C Board practices	Corporate Governance Our Board	43-48
		Additional Information Directors Report disclosures	171-175
		Corporate Governance Audit Committee ; Finance Committee ; Safety, Environment and Health Committee ; Nominations Committee ; Executive Committee ; and Management committees	49-57
		Corporate Governance Remuneration Report Annual statement from the Remuneration Committee chairman	58-59
		Corporate Governance Remuneration Report Future policy table Executive Directors	60-63
		Corporate Governance Remuneration Report Future policy table Non-executive Directors (NEDs)	63
		Corporate Governance Remuneration Report Service contracts and policy on payment for loss of office and Dates of Directors service contracts/letters of appointment	65
	6D Employees	Financial Statements Notes to the consolidated financial statements 3. Operating costs (b) Number of employees	97
		Additional Information Other disclosures Employees	178
	6E Share ownership	Corporate Governance Remuneration Report Shareholding requirement and Differences in remuneration policy for all employees	64
		Corporate Governance Remuneration Report Statement of Directors shareholdings and share interests (audited information)	70-71



**Table of Contents**

<b>Item</b>	<b>Form 20-F caption</b>	<b>Location in the document</b>	<b>Page(s)</b>
		Corporate Governance Remuneration Report Annual report on remuneration	67-73
		Additional Information Other disclosures The All-employee Share Plans Share ownership	181  Further Information
<b>7</b>	<b>Major shareholders and related party transactions</b>		
	7A Major shareholders	Additional Information Directors Report disclosures Material interests in shares Material interests in shares	174  Further Information
	7B Related party transactions	Financial Statements Notes to the consolidated financial statements 28. Related party transactions	133
	7C Interests of experts and counsel	Not applicable	
<b>8</b>			
	<b>Financial information</b>		
	8A Consolidated statements and other financial information	Financial Statements Report of Independent Registered Public Accounting Firm Audit opinion for Form 20-F Financial Statements Basis of preparation Financial Statements Recent accounting developments Financial Statements Consolidated income statement ; Consolidated statement of comprehensive income ; Consolidated statement of changes in equity ; Consolidated statement of financial position ; and Consolidated cash flow statement Financial Statements Notes to the consolidated financial statements analysis of items in the primary statements Financial Statements Notes to the consolidated financial statements supplementary information	81  82-83 83 84-91  92-131 132-154
	8B Significant changes	Strategic Report Chairman s statement Subsequent Events	2-3 Further Information
<b>9</b>			
	<b>The offer and listing</b>		
	9A Offer and listing details	Additional Information Other disclosures The offer and listing Price history Price History	181  Further Information
		Additional Information Directors Report disclosures Share price Exchange Rates	175  Further Information
	9B Plan of distribution	Not applicable	
	9C Markets	Additional Information Directors Report disclosures Share price	175
	9D Selling shareholders	Not applicable	
	9E Dilution	Not applicable	
	9F Expenses of the issue	Not applicable	
<b>10</b>	<b>Additional information</b>		
	10A Share capital	Not applicable	
	10B Memorandum and articles of association	Additional Information Other disclosures Articles of Association and Corporate governance practices: differences from New York Stock Exchange (NYSE) listing standards	176-177



**Table of Contents**

<b>Item</b>	<b>Form 20-F caption</b>	<b>Location in the document</b>	<b>Page(s)</b>
		Additional Information Directors Report disclosures Share capital	174-175
	10C Material contracts	Additional Information Other disclosures Material contracts	179
	10D Exchange controls	Additional Information Other disclosures Exchange controls	178
	10E Taxation	Additional Information Other disclosures Taxation	179-181
	10F Dividends and paying agents	Not applicable	
	10G Statement by experts	Not applicable	
	10H Documents on display	Additional Information Other disclosures Documents on display	178
	10I Subsidiary information	Not applicable	
<b>11</b>			
	<b>Quantitative and qualitative disclosures about market risk</b>		
	11A Quantitative information about market risk	Financial Statements Notes to the consolidated financial statements 15. Derivative financial instruments	114-116
		Financial Statements Notes to the consolidated financial statements 30. Financial risk management (a) Credit risk ; (b) Liquidity risk ; (c) Interest rate risk ; (d) Currency risk ; (e) Commodity risk ; (f) Capital risk management ; and (g) Fair value analysis	137-144
		Strategic Report Financial review	6-9
	11B Qualitative information about market risk	Financial Statements Notes to the consolidated financial statements 15. Derivative financial instruments	114-116
		Financial Statements Notes to the consolidated financial statements 30. Financial risk management (a) Credit risk ; (b) Liquidity risk ; (c) Interest rate risk ; (d) Currency risk ; (e) Commodity risk ; (f) Capital risk management ; and (g) Fair value analysis	137-144
		Strategic Report Financial review	6-9
		Additional Information Risk factors	167-169
<b>12</b>	<b>Description of securities other than equity securities</b>		
	12A Debt securities	Not applicable	
	12B Warrants and rights	Not applicable	
	12C Other securities	Not applicable	
	12D American depository shares	Additional Information Other disclosures Description of securities other than equity securities: depository fees and charges	178
		Additional Information Other disclosures Depository payments to the Company	177
		Additional Information Definitions and glossary of terms	188-191
<b>13</b>		Not applicable	
	<b>Defaults, dividend arrearages and delinquencies</b>		
<b>14</b>		Not applicable	
	<b>Material modifications to the rights of security holders and use of proceeds</b>		
<b>15</b>		Additional Information Internal control Disclosure controls and Internal control over financial reporting	170
	<b>Controls and procedures</b>		

**Table of Contents**

<b>Item</b>	<b>Form 20-F caption</b>	<b>Location in the document</b>	<b>Page(s)</b>
<b>16</b>	16A Audit committee financial expert	Corporate Governance Audit Committee Experience	49
	16B Code of ethics	Additional Information Other disclosures Code of Ethics	177
	16C Principal accountant fees and services	Corporate Governance Audit Committee External audit	51
		Financial Statements Notes to the consolidated financial statements 3. Operating costs (e) Auditors remuneration	98
	16D Exemptions from the listing standards for audit committees	Not applicable	
	16E Purchases of equity securities by the issuer and affiliated purchasers	Not applicable	
	16F Change in registrant s certifying accountant	Not applicable	
	16G Corporate governance	Additional Information Other disclosures Corporate governance practices: differences from New York Stock Exchange (NYSE) listing standards	177
	16H Mine safety disclosure	Not applicable	
<b>17</b>	<b>Financial statements</b>	Not applicable	
<b>18</b>	<b>Financial statements</b>	Financial Statements Company accounting policies	155
		Financial Statements Basis of preparation	82-83
		Financial Statements Recent accounting developments	83
		Financial Statements Consolidated income statement ; Consolidated statement of comprehensive income ; Consolidated statement of changes in equity ; Consolidated statement of financial position ; and Consolidated cash flow statement	84-91
		Financial Statements Notes to the consolidated financial statements analysis of items in the primary statements	92-131
		Financial Statements Notes to the consolidated financial statements supplementary information	132-154
		Financial Statements Report of Independent Registered Public Accounting Firm Audit opinion for Form 20-F Filed with the SEC	81
<b>19</b>	<b>Exhibits</b>		

**Table of Contents**

**Table of Contents**

**Table of Contents**

Strategic Report	Corporate Governance	Financial Statements	Additional Information	01
------------------	----------------------	----------------------	------------------------	----

**Contents**

**Strategic Report pages 02 to 41**

02	<u>Chairman’s statement</u>
04	<u>Chief Executive’s review</u>
06	<u>Financial review</u>
10	<u>Non-financial KPIs</u>
12	<u>Operating environment</u>
14	<u>Our vision and strategy</u>
16	<u>What we do</u>
20	<u>How we make money from our regulated assets</u>
21	<u>How our strategy creates value</u>
22	<u>Internal control and risk management</u>
26	<u>How executive remuneration aligns to Company strategy</u>
29	<u>Principal operations</u>
40	<u>People</u>

**Corporate Governance pages 42 to 73**

The Corporate Governance Report, introduced by the Chairman, contains details about the activities of the Board and its committees during the year, including reports from the Audit, Nominations, Remuneration,

**Finance, and Safety, Environment and Health Committees, as well as details of our shareholder engagement activities.**

<b>42</b>	<u>Corporate Governance contents</u>
<b>57</b>	<u>Directors Report statutory and other disclosures</u>
<b>58</b>	<u>Remuneration Report</u>

## **Financial Statements pages 74 to 159**

**Including the independent auditors reports, consolidated financial statements prepared in accordance with IFRS and notes to the consolidated financial statements, as well as the Company financial statements prepared in accordance with UK GAAP.**

<b>74</b>	<u>Contents of financial statements</u>
<b>75</b>	<u>Introduction to the financial statements</u>
<b>76</b>	<u>Statement of Directors responsibilities</u>
<b>77</b>	Independent auditors report
<b>81</b>	<u>Report of Independent Registered Public Accounting Firm</u>

## **Additional Information pages 160 to the inside back cover**

**Additional disclosures and information, definitions and glossary of terms, summary consolidated financial information and other useful information for shareholders, including contact details for more information or help.**

<b>160</b>	<u>Contents of Additional Information</u>
<b>188</b>	<u>Definitions and glossary of terms</u>



[Glossary](#)

We use a number of technical terms and abbreviations within this document. For brevity, we do not define terms or provide explanations every time they are used; please refer to the glossary on pages 188 to 191 for this information.

**Table of Contents**



**02 National Grid Annual Report and Accounts 2013/14**

**Chairman's statement**

*Our vision statement 'Connecting you to your energy today, trusted to help you meet your energy needs tomorrow' emphasises the importance of trust, which we earn not just by meeting our commitments, but by making sure that we do so in the right way.*

It has been an important and challenging year for National Grid and the energy sector in general on both sides of the Atlantic.

revenue in our principal UK businesses. The commentary on differences and regulated revenue adjustments contained in the Financial review on page 08 aims to help understanding of this matter.

**The Board is proposing a recommended final dividend of**

Although we did not experience any major storm-related outages in our service areas during 2013/14, severe winter weather conditions – the polar vortex in the US and serious flooding in the UK – continued to test the resilience of our networks. I am pleased to report these have performed well as a result of prudent investments in past years, as well as the commitment of our people.

**27.54p**

The Board has recommended an increase in the final dividend to 27.54p (2012/13: 26.36p) per ordinary share (\$2.3107 per American Depositary Share). If approved, this will bring the full-year dividend to 42.03p per ordinary share (\$3.4801 per American Depositary Share), an increase of 2.9% over the 40.85p per ordinary share in respect of the financial year ending 31 March 2013.

Energy policies in both the UK and US strive to find an acceptable balance between affordability to the ultimate consumers, security of supply and sustainability considerations. Particularly since last

**Effective governance**

We have developed a new remuneration policy to align more

September, the focus of UK media and political attention has been moving between each of these three factors, with no enduring consensus of what constitutes the optimum position.

In the UK, the eight year RIIO settlement we accepted in February 2013 incentivises us to be as efficient as possible while ensuring that savings we achieve can be shared with consumers. Through these incentives we can maximise our efforts to help hard-pressed consumers and deliver good returns to our shareholders.

### Transparency

In our continuing efforts to be fair, balanced and understandable in our reporting we are including additional information this year and explaining some technical matters in greater detail, so that we are as transparent as we can be.

In particular, I draw your attention to one aspect of our results. There have always been differences between IFRS reported results and underlying economic performance; however, one of the benefits of the RIIO price control regime is that it provides greater transparency of regulatory adjustments to

closely with RIIO, the continued evolution of our US business and shareholder value creation. The policy will be subject to shareholder approval at the AGM in July – a requirement of recent legislation. You can read our full Remuneration Report, introduced by Jonathan Dawson, our new Remuneration Committee Chairman, on page 58.

As we describe on page 07, the high level of take-up of the scrip dividend in the last couple of years led to concerns about the potential dilutive effect of this option. This meant that we decided not to offer the scrip element for the 2013/14 interim dividend paid in January this year, as our forecast capital investment programme was already fully funded. I do appreciate, from the letters sent to me, that this caused some dissatisfaction. We have now identified a way of offering the scrip option for both the full-year and interim dividend, which balances shareholders' appetite for the scrip dividend option with our cash requirements. At the AGM we are seeking approval for the allotment and buy-back authorities we need to do this. The scrip dividend option has been offered for the 2013/14 final dividend subject to shareholder approval of the relevant resolutions at the AGM.

**Table of Contents**

<b>Strategic Report</b>	<b>Corporate Governance</b>	<b>Financial Statements</b>	<b>Additional Information</b>	<b>03</b>
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Nick Winsor, Executive Director UK, will step down from the Board in July 2014 at the AGM. He will continue with his roles as President of the European Network of Transmission System Operators for Electricity (ENTSO-E) and as Chairman of National Grid Electricity Transmission (NGET) and National Grid Gas (NGG) through to July 2015 before leaving the Company. After July 2015, the role of President of ENTSO-E will no longer be undertaken within the Company, and arrangements for a smooth handover of Nick's other responsibilities will be announced in due course.

contributed £1.4 billion in taxes in the UK alone. Additionally, we estimate we support more than 28,500 jobs in the first tier of our supply chain – companies that are our suppliers across the globe.

**Governance**  
pages 42 – 57

We aim to develop and operate our business with an inclusive and diverse culture. You can read more about our approach to diversity on page 41, as well as our Board diversity policy on page 56.

**Looking ahead**

This year we have welcomed Therese Esperdy and John Pettigrew to our Board and we will be saying goodbye to Maria Richter following the AGM.

Over the next 12 months the UK and US will see a dynamic political environment. In the UK, the Scottish independence referendum later this year and the general election in 2015 are likely to increase the focus on issues such as the affordability and security of energy supply, as will the proposed review of the energy industry by the Competition and Markets Authority.

During Maria's 10 years with the Company she has made a significant contribution to the Board and Finance Committee in particular and I would like to thank her for her commitment and wish her all the best in her future endeavours.

In the US, the mid-term US Congressional elections are on the

Therese, who will be taking over as chairman of the Finance Committee from Maria, brings a wealth of corporate finance and debt market experience to our Board. We have also appointed a new Executive Director, John Pettigrew. John joined National Grid as a graduate entrant in 1991 and has been a member of the Executive Committee for nearly two years.

horizon, together with the gubernatorial elections (election of the state governor) in New York, Rhode Island and Massachusetts. We expect debate to continue on essential infrastructure, resilience and sustainability, including our Connect21 dialogue with stakeholders. You can read more about Connect21 on page 35.

The appointments of Therese and John have been part of a significant transition of the Board over the last three years through which we have secured a broad range of skills, experience, perspectives and challenge. Together with strong teamwork, I believe these qualities are contributing towards an effective Board, which will continue to set the right tone from the top, helping to meet the challenges ahead.

Our people have a crucial role to play in meeting the opportunities ahead. I would like to thank our employees for their hard work and dedication over the past year. Rising to the challenges brought by severe weather and changes within the industry, they have continued to make National Grid a company we can be proud of.

### Being a responsible business

Our vision statement 'Connecting you to your energy today, trusted to help you meet your energy needs tomorrow' emphasises the importance of trust, which we earn not just by meeting our commitments, but by making sure that we do so in the right way. That is why how we work is as important as what we do, and why doing the right thing is at the core of everything we do.

During 2013/14 we spent time reinforcing the standards we expect of our employees in terms of ethical behaviour. As part of this, we have sent our employees a refreshed copy of 'Doing the Right Thing', which is our guide to ethical business conduct.

We contribute to the communities in which we operate directly and indirectly in many ways. We maintain and operate the critical infrastructure needed to keep the lights on

and the heating working across the UK and northeastern US; we employ more than 23,000 people; and in 2013/14

**Table of Contents**

**04 National Grid Annual Report and Accounts 2013/14**

**Chief**

**Executive s  
review**

*We need to be even more flexible and agile as customer needs change, so we can respond faster and more efficiently.*

It has been a year of solid performance for National Grid against a backdrop of intense public focus on energy prices, as well as new regulatory frameworks in both the UK and US.

Safety is, as always, at the heart of the way we operate. In the UK we achieved an employee lost time injury frequency rate (IFR) of below 0.1. This is a world-class performance and I am incredibly proud of our teams who have worked so hard to get us to this significant milestone. You can read more about this achievement on page 10. The challenge now is to replicate this performance in the US, where we have more work to do. We will never let up on our relentless focus on safety.

Despite the freezing and protracted winter in the US and the wettest winter on record in the UK, we achieved one of our best years in terms of reliability, keeping the

We have adapted our ways of working so we can meet the needs of our customers and stakeholders and deliver value under RIIO. For example, we used innovative techniques to protect a section of the pipeline that carries gas from the liquefied natural gas (LNG) importation terminal in west Wales, prior to the construction of a new road. This meant we were able to meet the timescales of the local authority building the road without disrupting gas supply to consumers.

In the US, it has been the first year of working under the new upstate New York and Rhode Island regulatory contracts and I am pleased that we have performed well in both cases. You can read more about developments in our US rate filings and regulatory environment on page 164.

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lights on and the gas flowing. The investment we made in bolstering our flood defences in the UK protected potentially vulnerable assets such as substations, even though in some cases the surrounding areas suffered considerable flooding.

In the US, our reliability performance was excellent as a result of continued targeted resiliency investment and management of our networks.

The introduction of RIIO in the UK has been an appropriate development for our industry. If we can outperform against the incentives it offers and find ways to reduce our costs, the benefits are shared with our customers. Getting ready for RIIO has been a significant challenge for the UK business, but I am delighted to say that we have made a good start.

There have also been significant Government and regulatory policy changes affecting our business in the UK, including the introduction of Electricity Market Reform (EMR) and the evolution of the system operator role in the long-term planning of the network.

We have introduced Connect21, our thinking on advancing the USA's natural gas and electricity infrastructure beyond its 20th century limitations (see page 35). Another priority in the US was the transition of the operation and maintenance of the Long Island Power Authority's (LIPA) electric transmission and distribution system on Long Island to Public Service Electric and Gas Company - Long Island (PSEG-LI). We successfully handed over the contract on 31 December 2013 and have entered into a transition services agreement with LIPA/PSEG-LI.

US enterprise resource planning system stabilisation continued, remedying the errors of poor implementation from the prior year. Over the course of the year, the US business made significant progress in the activities required to upgrade the system, with implementation expected in mid-2014. The focus is now on reducing the ongoing costs associated with the complex manual processes that are required to compensate for identified weaknesses in internal controls over financial reporting in the US. While these control weaknesses have not reduced the quality of financial statements



**Table of Contents**

<b>Strategic Report</b>	<b>Corporate Governance</b>	<b>Financial Statements</b>	<b>Additional Information</b>	<b>05</b>
-------------------------	-----------------------------	-----------------------------	-------------------------------	-----------

produced, they have necessitated significant additional cost.

Overall, the business remains on track to successfully conclude the programme during 2014, with expected costs unchanged from the guidance provided last year.

We have focused on improving our end-to-end operating processes throughout the year. This has involved using hard facts and data to identify and prioritise areas for improvement, as well as harnessing ideas to help find more efficient ways of working to meet our stakeholders' needs.

An area we know we can improve is customer service. We saw some good results such as reduced complaints in the UK and our scores for UK Gas Transmission, as well as increases in three out of our four US customer satisfaction scores. However, we know that we are not fully meeting our customers' expectations for our gas connections process in the UK and US. We will stay focused on getting this right.

**People**

I was really pleased to see that the results of our 2014 employee opinion survey, completed by 78% of our employees, included an engagement score of 71% an increase of eight percentage points over the previous survey and our highest engagement score since we started conducting Group-wide employee opinion surveys.

**Principal operations**

pages 29 39

I was also pleased to attend a series of celebrations to mark 40 years' service for more than 300 of our employees in both the UK and US. I am delighted that so many of our people have forged productive and committed careers at National Grid that have spanned such a long time. Yet at the same time, it serves as a reminder about the scale of the challenge we have in our industry to make sure we have enough people with the skills and experience we need in the future.

**People**

pages 40 41

It is a significant challenge on both sides of the Atlantic. In the UK, for example, around 89,000 people are needed

In the US, we supply gas and electricity to customers who have chosen us as their supplier. Our regulatory agreements allow us to recover the costs we incur when we buy gas and electricity. During 2013/14 we saw an increase in complaints about higher energy bills – a consequence of the colder weather affecting commodity costs during the winter.

Energy prices have been the subject of a continued high-profile debate in the UK. At National Grid, we believe transparency is crucial, explaining to customers the breakdown of the bill they receive. In the UK, we are investing significantly in our UK networks, but the impact of network costs on bills will remain flat in real terms over the RIIO period (2013/14 – 2020/21), based on the forecast revenues derived from Ofgem’s Final Proposals for RIIO.

In terms of our UK network upgrade plans, we are pleased with progress on the London Power Tunnels project and have now started site works on the HVDC link connecting Scotland and England. This joint venture with SP Transmission will support the export of low carbon Scottish generation.

In the US, our Brooklyn/Queens Interconnect project will connect our existing natural gas distribution systems in Brooklyn and Queens, which will ensure greater reliability and safety, provide additional capacity and meet future energy needs for customers. This is the first new gas pipeline to be installed in the area in 50 years.

annually to meet demand in the UK’s engineering sector over the next decade. Yet only around 51,000 are joining the profession each year. In the US, by 2018, STEM occupations will account for about 1.1 million new jobs and 1.3 million replacement positions due to STEM workers leaving the workforce.

To help address this shortage, National Grid is running, or is involved with, a number of programmes and initiatives in the UK and US aimed at encouraging young people to study STEM subjects you can read more about these initiatives on page 40.

### Our priorities for next year

**Safety** – build on our strong UK performance and focus our efforts on delivering consistent world-class safety performance across the organisation;

**Customer-focused execution** – in the UK, continue our strong start to RIIO; underpin energy security through our interconnector and infrastructure investment strategy. In the US, complete stabilisation of our enterprise resource system; perform strongly against our current regulatory rate plans while shaping the future; and

**Stakeholders** – continue to engage with our stakeholders in the US, UK and EU to understand their changing energy needs and to shape energy policy.

**Steve Holliday**

We are determined to embed sustainability by seeking to combine innovation, engagement and efficiency – an example of which was a trial in the UK, working with manufacturers, construction partners and our procurement teams to re-manufacture aluminium overhead line conductors.

**Table of Contents**

06 National Grid Annual Report and Accounts 2013/14

**Financial  
review**

*We have delivered another year of solid financial performance with a good start under RIIO in the UK and consolidation of underlying improvements in the US.*

**Our financial KPIs**

**Adjusted earnings per share**

**Adjusted operating profit**

Our adjusted operating profit has increased by £25 million (1%) to £3,664 million. Across our three UK businesses operating under the new RIIO framework, adjusted operating profit was up £34 million. Allowed revenues increased in Electricity Transmission and Gas Distribution and fell in Gas Transmission. The resultant increase in revenue was offset by higher controllable costs, higher depreciation as a result of continued investment and adverse movements in timing year on year.

Our US Regulated business was £129 million lower, reflecting a weaker dollar, the end of Niagara Mohawk deferral recoveries at March 2013, higher controllable costs due to inflation, and increased insurance costs following major storms last year. These were partially offset by the non-recurrence of the major storm costs incurred last year.

Other activities adjusted operating profit was £120 million higher, driven by higher profits in the French interconnector, non-recurrence of Superstorm Sandy costs in our insurance captive, and improved performance in our Metering business. These were partially offset by increased spend on

the stabilisation of new US information systems.

### **Adjusted earnings**

Our adjusted net interest charge was slightly lower than 2012/13 at £1,108 million, reflecting the weaker dollar.

Our adjusted tax charge was £38 million lower at £581 million. This was mainly due to a 1% decrease in the UK statutory corporation tax rate in the year, a change in the UK/US profit mix and changes in tax provisions in respect of prior years. As a result of this, our effective tax rate for 2013/14 was 22.5% (2012/13: 24.4%).

The earnings performance described above has translated into adjusted EPS growth in 2013/14 of 2.6p (5%) (2012/13: 5.4p, 12%).

### **Adjusted EPS<sup>1</sup>**

pence

1. All comparatives restated for IAS 19 (revised). See note 1 on page 92.

In accordance with IAS 33, all EPS and adjusted EPS amounts for comparative periods have been restated as a result of shares issued via scrip dividends and the bonus element of the 2010 rights issue.

## **Measurement of financial performance**

We describe our results principally on an adjusted basis and explain the rationale for this on page 182. We present results on an adjusted basis before exceptional items, remeasurements and stranded cost recoveries.

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See page 182 for further details and reconciliations from the adjusted profit measures to IFRS, under which we report our financial results and position. The comparative numbers have been restated for the adoption of IAS 19 (revised) Employee benefits . See further detail in note 1 on page 92.

A reconciliation between reported operating profit and adjusted operating profit is provided below. Further commentary on movements in the income statement is provided on page 85.

<b>£m</b>	<b>Year ended 31 March</b>		
	<b>2014</b>	<b>2013</b>	<b>2012</b>
<b>Total operating profit</b>	<b>3,735</b>	<b>3,749</b>	<b>3,535</b>
Exceptional items	(55)	84	122
Remeasurements commodity contracts	(16)	(180)	94
Stranded cost recoveries		(14)	(260)
Adjusted operating profit	3,664	3,639	3,491
Adjusted net finance costs	(1,108)	(1,124)	(1,090)
Share of post-tax results of joint ventures	28	18	7
Adjusted taxation	(581)	(619)	(697)
Attributable to non-controlling interests	12	(1)	(2)
<b>Adjusted earnings</b>	<b>2,015</b>	<b>1,913</b>	<b>1,709</b>

Adjusted EPS	54.0p	51.4p	46.0p
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### Group return on equity (RoE)

We measure our performance in generating value for our shareholders by dividing our annual return by our equity base.

Group RoE has increased during the year to 11.4%, due to the impact of major storms in the prior year. Excluding major storms, Group RoE has decreased by 30bps reflecting the end of Niagara Mohawk deferral recoveries, together with higher controllable costs and system costs in the US. These negative impacts were partially offset by French interconnector performance and the lower UK tax rate.

### Group return on equity

%

**Our revised**

**financial KPIs**

page 09

**Exchange rates**

page 85

**Use of adjusted  
profit measures**

page 182

**Reconciliations  
of adjusted profit  
measures**

page 182



**Table of Contents**

<b>Strategic Report</b>	<b>Corporate Governance</b>	<b>Financial Statements</b>	<b>Additional Information</b>	<b>07</b>
-------------------------	-----------------------------	-----------------------------	-------------------------------	-----------

We have changed the way we present our financial information in the Strategic Report to remove duplication. As a result, the analysis here focuses on our KPIs and other performance measures we use to monitor our business performance. Analysis of our financial performance and position at 31 March 2014, including the performance of our principal operations, has been relocated to the financial statements, however this analysis still forms part of our Strategic Report financial review. See page 75 for further information. See pages 183 to 185 for commentary on our financial performance and position for the year ended 31 March 2013 compared with 2012.

**Regulated asset growth**

Our regulated assets have increased by 3% (£1 billion) to £34.7 billion, reflecting the continued high levels of investment in our networks in both the UK and US. Maintaining efficient growth in our regulated assets ensures we are well positioned to continue providing consistently high levels of service to our customers and increases our revenue allowances in future years.

The Board is confident that growth in assets, earnings and cash flows, supported by improving cash efficiency and an exposure to attractive regulatory markets, should help the Group to maintain strong, stable credit ratings and a consistent prudent level of gearing, while delivering attractive returns for shareholders.

**How we make money from our regulated assets**  
page 20

The UK regulatory asset value (RAV) increased by £1.1 billion, reflecting inflation and significant capital expenditure in our UK Electricity Transmission business in particular. The US rate base decreased by £0.1 billion. Foreign exchange movements decreased the rate base reported in sterling by £0.9 billion. Offsetting this, investment in the

**Other performance measures**

**Dividend growth**

During the year we generated £1.3 billion of sustainable business net cash flow after our capital expenditure programmes. This has enabled the growth of the dividend in line with RPI, being 2.9%(2012/13: dividend

**UK regulation**  
pages 160 162

networks and working capital movements increased rate base by £0.8 billion.

growth of 4%), taking into account the recommended final dividend of 27.54p.

US regulation

pages 162 165

**Total regulated assets and regulated asset growth**

£bn

The high level of take-up of this scrip option in the last couple of years has led to concerns about the potential dilutive effect on value of this option. This meant that we decided not to offer the scrip element for the 2013/14 interim dividend paid in January this year, as our forecast capital programme was already fully funded. We continue to offer the scrip option for the year-end dividend.

**Year ended 31 March**

%	2014	2013	2012
Dividend growth	3	4	8

1. US rate base calculated as at 31 December for these years.

2. Estimated figure until the conclusion of the regulatory reporting cycle.

**Cash generated from operations**

Cash generated from operations was £4,419 million (2012/13: £4,037 million). Adjusted operating profit before depreciation, amortisation and impairment was £81 million higher year on year. Changes in working capital improved by £351 million over the prior year, principally in the US due to the timing of receivables from LIPA relating to Superstorm Sandy, higher commodity costs and weather differences year on year. Partially offsetting these improvements, cash outflows relating to exceptional items were £38 million higher due to reorganisation in the UK and LIPA MSA transition costs in the US.

**Value added**

Our dividend is an important part of our returns to shareholders along with growth in the value of the asset base attributable to equity investors. These are reflected in the value added metric that will underpin our approach to sustainable decision making and long-term incentive arrangements.

**UK regulated return on equity**

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Overall value added in the year was £2.1 billion or 57.2p per share as set out below:

The UK RoE has decreased 90bps to 12.7%, reflecting the new regulatory arrangements under the RIIO framework in place from this year. This performance represents 260bps outperformance over allowed returns.

£bn at constant currency	Year ended 31 March		Change £bn
	2014	2013	
UK regulated assets <sup>1</sup>	25.2	24.3	+0.9
US regulated assets <sup>2</sup>	11.2	10.3	+0.9
Other invested capital	1.7	1.5	+0.2
<b>Total assets</b>	<b>38.1</b>	<b>36.1</b>	<b>+2.0</b>
Dividend paid			<b>+1.1</b>
Movement in goodwill			
Net debt	(21.2)	(20.2)	-1.0
<b>Value added</b>			<b>+2.1</b>
<b>Value added per share</b>			<b>57.2p</b>

**UK return on equity**  
%

1. Consists of regulated asset values and other regulatory assets and liabilities of the UK businesses regulated under RIIO price controls.

2. US regulated assets increased from \$17.2 billion to \$18.7 billion in the year. These represent rate base plus assets outside of rate base, including working capital.

**Table of Contents**



**08 National Grid Annual Report and Accounts 2013/14**

**Financial**

**review**

continued

**US regulated return on equity**

The US RoE has decreased 20bps to 9.0%, mainly driven by lower allowed rates in our KEDNY and Long Island Generation businesses following the introduction of new rate plans during the year.

**US return on equity**

%

**Interest cover**

The principal measure we use to monitor financial discipline is interest cover, which is a measure of the cash flows we generate compared with the net interest cost of servicing our borrowings. The table below shows our interest cover for the last three years.

Times	Year ended 31 March		
	2014	2013	2012
Interest cover	4.1	3.9	3.9

**Return on capital employed**

The increase in interest cover in 2013/14 reflects flat finance costs year on year. Our target long-term range for interest cover is in excess of 3 times.

**Our operations performance at a glance**

**Business analysis 2013/14**

%

**Adjusted operating profit**

RoCE provides a performance comparison between our regulated UK and US businesses and is one of the measures that we use to make strategic and investment decisions about our portfolio of businesses. The table below shows the RoCE for our businesses over the last five years:

**Return on capital employed**

%

The UK RoCE has decreased from 8.6% to 8.0% in 2013/14, reflecting the new RIIO regulatory allowances, including lower cost of debt allowance, higher gearing assumption in the gas businesses, and the inclusion of our share of exceptional costs. The decrease in the US RoCE from 7.1% to 6.4% is primarily due to the end of Niagara Mohawk deferral recoveries and controllable cost increases. Excluding the impact of major storm costs, the US RoCE would have been 7.7% in 2012/13.

Further details on our capital management and credit ratings can be found in note 30 (f) and on the debt investors section of our website.

**Timing and regulated revenue adjustments**

As described on page 20, our allowed revenues are set in accordance with our regulatory price controls or rate plans. We calculate the tariffs we charge our customers based on the estimated volume of energy we expect will be delivered during the coming period. The actual volumes delivered will differ from this estimate. Therefore, our total actual revenue will be different from our total allowed revenue. These differences are commonly referred to as timing differences.

If we collect more than the allowed level of revenue, the balance must be returned to customers in subsequent periods, and if we collect less than the allowed level of revenue we may recover the balance from customers in subsequent periods. In the US, a substantial portion of our costs are pass-through costs (including commodity and energy efficiency costs) and are fully recoverable from our customers. Timing differences between costs of this type being incurred and their recovery through revenue are also included in timing.

The amounts calculated as timing differences are estimates and subject to change until the variables that determine allowed revenue are final.

## Net debt

We expect our net debt to continue to grow for the next few years as we fund our capital investment programmes and enhance our networks. We continue to borrow at attractive rates when needed and believe that the level of net debt remains appropriate for our business. Our five year net debt trend is shown on page 91.

Our operating profit for the year includes a total estimated in-year under-collection of £42 million (2012/13: £16 million over-collection). Our closing balance at 31 March 2014 was £60 million over-recovered.

In the UK, there was a cumulative under-recovery of £57 million at 31 March 2014 (2013: under-recovery of £5 million). All other things being equal, the majority of that balance will normally be recoverable from customers starting in the year ending 31 March 2016.

**Table of Contents**

<b>Strategic Report</b>	<b>Corporate Governance</b>	<b>Financial Statements</b>	<b>Additional Information</b>	<b>09</b>
-------------------------	-----------------------------	-----------------------------	-------------------------------	-----------

In the US, cumulative timing over-recoveries at 31 March 2014 were £117 million (2013: £110 million). The majority of that balance will be returned to customers next year.

In addition to the timing adjustments described above, following the start of the RIIO price controls in the UK, outperformance against allowances as a result of the totex incentive mechanism, together with changes in output-related allowances included in the original price control, will almost always be adjusted in future revenue recoveries, typically starting in two years time.

Our current IFRS revenues and earnings include the amounts that will need to be repaid but exclude amounts that will be recovered in future periods. Such adjustments

In the US, accumulated regulatory entitlements to future revenue net of over- or under-recoveries amounted to £1,027 million at 31 March 2014 (2013: £1,311 million). These entitlements cover a range of different areas, with the most significant being environmental remediation and pension assets, as well as deferred storm costs.

All regulatory entitlements are recoverable (or repayable) over different periods, which are agreed with the regulators to match the expected payment profile for the liabilities. As at 31 March 2014, these extend until 2059.

### Major storms

Despite the very cold winter across much of the US, there were no major storms in 2013/14. In 2012/13, two major storms in the US, Superstorm Sandy and Storm Nemo, as well as a number of smaller storms, had a material effect on the results of National Grid, reducing operating profit by

### Non-financial KPIs

pages 10 11

### Our vision and strategy

pages 14 15

will form an important part of the continuing difference between reported IFRS results and underlying economic performance based on our regulatory obligations.

£136 million.

The table below shows adjusted operating profit and operating profit for the past three years, excluding the impact of timing differences and major storms.

For our UK regulated businesses as a whole, regulated revenue adjustments totalled £106 million in the year. This is based on our estimates of: work carried out in line with allowances; in expectation of future allowances; or work avoided altogether either as a result of us finding innovative solutions or of the need being permanently removed.

	Year ended 31 March		
	2014 £m	2013 £m	2012 £m
<b>Excluding the impact of timing differences and major storms</b>			
Adjusted operating profit	3,706	3,759	3,589
Operating profit	3,777	3,869	3,633

### Our revised financial KPIs

KPI	Definition	2013/14 result
<b>Adjusted EPS</b>	Adjusted earnings divided by the weighted average number of shares.	54.0p
		11.4%



<b>Group RoE</b>	Adjusted earnings with certain regulatory-based adjustments divided by equity.	
<b>Regulated asset growth</b>	Growth in the total UK RAV and US rate base versus the prior year.	3%
<b>Value added</b>	Annual growth in our assets after deducting dividends, goodwill and net debt.	£2.1bn

We measure the achievement of our objectives, make operational and investment decisions and reward our employees using both qualitative assessments and 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 more significant than others, and these are designated as KPIs.

KPIs are used to measure our progress on strategic priorities, aligning with those activities that combine to deliver our strategy. Financial KPIs are trailing indicators of the success of past initiatives and specific programmes. They also highlight areas for further improvement and allow us to make sure our actions culminate in sustainable long-term growth in shareholder value.

We have changed our financial KPIs during 2013/14 to reflect the changing metrics used to monitor the Group following RIIO. We have included value added, a new metric that we use to

monitor the value delivered to shareholders through dividends and growth in the value of National Grid's assets net of the growth in net debt. A derivative of this metric, value growth, is also used to incentivise our Executive Directors. See page 58 for further detail on our remuneration policy.

We have included regulated asset growth, as this is a measure of the ability of the business to generate revenue in the future. While we continue to focus on efficient capital expenditure, the value of our regulated assets drives our revenue allowances in future years.

We have stopped reporting our regulated controllable operating costs metric. This was included to monitor cost control, but following the introduction of RIIO, all our businesses' activities are focused on costs, through innovative and efficient delivery of high-quality services. Our ability to control costs is also reflected in the adjusted EPS and Group RoE metrics, which are based on our adjusted earnings.

**Table of Contents**



**10 National Grid Annual Report and Accounts 2013/14**

**Non-financial  
KPIs**

*Non-financial KPIs are often leading indicators of future financial performance. Improvements in these measures build our competitive advantage.*

**Employee lost time injury frequency rate (IFR)**

per 100,000 hours worked

**Definition**

Number of employee lost time injuries per 100,000 hours worked in a 12 month period.

Our ambition is to achieve a world-class safety performance by 2015, featuring an IFR of below 0.1, with a target for 2013/14 of 0.15. We intend to achieve this through a relentless leadership focus, robust safety management systems and tactical actions focused on our main risks, which may vary between regions and business areas.

**Strategic element**

**Deliver operational excellence**

**Goal**

Zero

Our IFR for 2013/14 was 0.14, better than our target for the year. This is compared with 0.17 in 2012/13, illustrating positive progress towards our world-class target. Our IFR for the UK was 0.06 and for the US it was 0.19.

**UK Principal operations**

pages 29 33

**US Principal operations**

pages 35 37

**Network reliability**

**Definition**

Various definitions appropriate to the relevant business area.

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

**Strategic element**

**Deliver operational excellence**

**Performance**

						Measure	Target	UK Principal operations pages 29 33
	2009/10	2010/11	2011/12	2012/13	2013/14		2013/14	
UK Electricity Transmission	99.9999	99.9999	99.999999	99.99999	<b>99.99999</b>	%	<b>99.9999</b>	US Principal operations pages 35 37
UK Gas Transmission	100	100	100	100	<b>100</b>	%	<b>100</b>	
UK Gas Distribution	99.999	99.999	99.999	99.999	<b>99.999</b>	%	<b>99.999</b>	
Electricity Transmission US	147	414	518 <sup>1</sup>	346	<b>118</b>	MWh losses	<b>308</b>	
Electricity US: Commercial	114	123	121	105 <sup>2</sup>	<b>107</b>	Minutes of outage	*	

\* Targets are set jurisdictionally by operating company.  
1. 2011/12 result restated to reflect final data.

2. 2012/13 result excludes New Hampshire, which was sold during the year.

**Customer satisfaction**

**Definition**

We measure customer satisfaction through our position in customer satisfaction surveys.

**Strategic element**

**Deliver operational excellence**

	Performance					Measure	Target
	2009/10	2010/11	2011/12	2012/13	2013/14		

UK Electricity Transmission	n/a	n/a	n/a	n/a	<b>7.4</b>	Score out of 10	6.9 <sup>1</sup>
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**UK Principal operations**

pages 29 33

UK Gas Transmission	n/a	n/a	n/a	n/a	<b>7.2</b>	Score out of 10	6.9 <sup>1</sup>
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**US Principal operations**

pages 35 37

UK Gas Distribution	4th	4th	3rd	3rd	*	Quartile ranking	Improve
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Gas distribution US: Residential	3rd	2nd	3rd	3rd	<b>2nd</b>	Quartile ranking	Improve
----------------------------------	-----	-----	-----	-----	------------	------------------	---------

	2nd	4th	3rd	4th	<b>4th</b>	Quartile ranking	Improve
--	-----	-----	-----	-----	------------	------------------	---------

Gas  
distribution  
US:  
Commercial

	4th	3rd	3rd	3rd	<b>2nd</b>	Quartile ranking	Improve
--	-----	-----	-----	-----	------------	------------------	---------

Electricity  
US:  
Residential

	3rd	2nd	2nd	3rd	<b>2nd</b>	Quartile ranking	Improve
--	-----	-----	-----	-----	------------	------------------	---------

Electricity  
US:  
Commercial

\* Under RIIO-GD1, our customer satisfaction results are now reported on an annual basis, rather than quarterly, which was how we reported them under our previous price control. We will publish the results on our website in the summer as part of our commitment to our stakeholders, and in our Annual Report and Accounts for 2014/15.

1. 6.9 represents our baseline target, set by Ofgem, for reward or penalty under RIIO.

**Table of Contents**

<b>Strategic Report</b>	<b>Corporate Governance</b>	<b>Financial Statements</b>	<b>Additional Information</b>	<b>11</b>
-------------------------	-----------------------------	-----------------------------	-------------------------------	-----------

**For more information about our strategy and strategic elements see**

pages 14 15

**Employee engagement index**

%

**Definition**

Employee engagement index calculated using responses to our employee survey.

**Target**

To increase

We measure employee engagement through our employee opinion survey. The results of our 2014 survey, which was completed by 78% of our employees, have helped us identify specific areas where we are performing well and those areas we need to improve.

**Strategic element**

**Engage our people**

**People**

pages 40 41

Our engagement index has risen by eight points to 71%, our highest engagement score since we started conducting Group-wide employee opinion surveys.

Managers receive a scorecard that aims to create greater leadership accountability and we produce survey reports and action plans at Company, regional, business unit, function and team levels.

## Greenhouse gas emissions

% reduction against 1990 baseline

### Definition

Percentage reduction in greenhouse gas emissions against our 1990 baseline.

We continue to look for innovations and efficiencies that will help us achieve these targets. In 2013 we significantly improved our scores in the CDP Global 500 ratings and were admitted for the first time to the Global Leaders Index for carbon disclosure.

**Strategic element**

**Embed sustainability**

### Target

45% reduction by 2020 and

80% reduction by 2050

We measure and report our greenhouse gas emissions in accordance with the WRI/WBCSD Greenhouse Gas Protocol: Corporate Accounting and Reporting Standard (Revised Edition) for all six Kyoto gases, using the operational control approach for emissions accounting.

Our total Scope 1 and Scope 2 greenhouse gas emissions (excluding electricity transmission and distribution line losses) for 2013/14 were around 7.4 million tonnes carbon dioxide equivalent (Scope 1 was 7.2 and Scope 2 was 0.2). This is equivalent to an intensity of 501 tonnes carbon dioxide equivalent per £million of revenue for 2013/14.

These Scope 1 and 2 emissions are independently assured against the international standard ISO 14064-3 Greenhouse Gas assurance protocol. A copy of this statement of assurance is available on our website.

The 2013/14 emissions quantity represents a 62% reduction from our 1990 baseline and a 9% reduction from our 2012/13 emissions. Although our outturn is better than our 2020 target, we will need to innovate if we are to meet the target for 2050.

In the UK we have experienced a mild year, which has been beneficial to the overall emissions of many of our business units. In the UK activities at Grain LNG have led to a 60% reduction of energy consumption of on-site nitrogen production. Our Electricity Transmission business has reduced SF<sub>6</sub>

We have remained focused on greenhouse gas emissions reduction programmes to achieve our corporate commitment targets of 45% and 80% reduction in Scope 1 and 2 emissions by 2020 and 2050 respectively from our 1990 baseline.

leak rates to 1.2% in 2013/14 compared with 1.7% in the previous year and our Property function has delivered a 2% year-on-year reduction in electricity-related emissions across occupied sites.

In the US we have completed power plant turbine efficiency upgrades in Long Island and continued to focus on efficiency-related maintenance programmes. This has contributed towards outperforming our LIPA contractual efficiency target. Our US and UK Gas Distribution businesses have continued to deliver significant reductions in emissions in line with forecasts.



**Table of Contents**



**12 National Grid Annual Report and Accounts 2013/14**

**Operating environment**

*Recent signs of economic growth have had a positive effect on consumer confidence, but the long downturn and its impact on wages have led to widespread concerns over energy bills. Affordability remains a primary concern of consumers and regulators.*

**Economic environment**

Our UK price controls and US rate plans are agreed against the backdrop of the broader macroeconomic environment.

In the UK, economic growth is projected to continue to increase at a moderate pace in 2014, while the RPI measure of inflation is expected to remain subdued. Monetary policymakers have indicated that interest rates are expected to remain low during 2014, despite significant reductions in unemployment.

In the US, employment and GDP growth continue to improve steadily. The US Congress has reached a two year budget deal, which should ease some concerns in market conditions. Market indicators in areas such as housing and construction are returning to pre-2008 levels.

**Market driver**

**Impact**

**Changing energy mix**

**Cost and environmental pressures affecting traditional electricity generation**

Older gas-fired power stations in the UK and many coal-fired power stations in the US are closing or being mothballed due to changes in environmental regulations.

In the UK, fuel prices are affecting the economic viability of fossil fuel-fired electricity generation. Further decline in traditional electricity generation is likely if the UK's carbon reduction targets are to be met. The US is seeing renewed demand for gas, as the increasing availability of shale gas has lowered prices.

**Long-term certainty needed to secure investment**

Current uncertainty in the UK market has led some developers to delay investing in new generation capacity. An agreement on long-term prices for low carbon generation under Electricity Market Reform (EMR) could provide additional certainty for these developers.

**Changing UK energy sources**

The locations where gas comes into the UK are changing, with forecast reductions in North Sea production and increased reliance on imported gas. New low carbon generation may not be located in the same place or have the same characteristics as existing plant.

**This means changes to our network will be needed**

Changes to the energy mix and location of supply and demand centres will create pressures on our networks, potentially requiring further investment.

**Shale gas production is transforming supply and demand**

In the US, shale gas production will mean lower-priced gas over the long term, changing supply and demand patterns.

**We may need to invest in additional network capacity**

As more generation plants convert to lower priced natural gas, we may need to invest in additional gas network capacity. Changes in generation could also mean modifications to the electricity transmission network.

## Energy policy

### **Sustainability, security of supply and affordability underpin EU policy**

In a difficult economic and financial context, the EU energy policy is underpinned by the three cornerstones of sustainability, security of supply and affordability. The European Commission published its 2030 Climate Change and Energy framework in 2014, featuring a continued ambition in terms of greenhouse gas reduction targets and energy policy objectives.

Negotiations for a new international agreement on climate change continued at the nineteenth session of the Conference of the Parties (COP19) in 2013, and nations are looking to the Paris worldwide conference in 2015 as the next opportunity to work out a new climate change deal.

### **Policy decisions can affect our investment needs and compliance obligations**

Energy policy decisions by governments, government authorities and others have a direct impact on our business, influencing the emerging challenges and opportunities. They can affect the amount and location of investment required in our networks and the way we operate. They can also change our compliance obligations.

### **This requires more market integration, interconnection and renewable generation**

Greater levels of market integration, interconnection and renewable generation are fundamental to achieving the EU's policy objectives. While European developments present challenges, the significant level of investment required may create opportunities for growth. For example, potential future interconnector opportunities include connections between the UK and Belgium, Norway, France, Ireland, Denmark and Iceland.

**Table of Contents**

<b>Strategic Report</b>	<b>Corporate Governance</b>	<b>Financial Statements</b>	<b>Additional Information</b>	<b>13</b>
-------------------------	-----------------------------	-----------------------------	-------------------------------	-----------

Market driver	Impact
<p><b>UK policy changes are in place to attract investment</b></p> <p>In the UK, energy policy continues to evolve from the Climate Change Act 2008, which commits the UK Government to reducing UK greenhouse gas emissions to at least 80% lower than a 1990 baseline by 2050. The Energy Act 2013 implements the main aspects of Electricity Market Reform (EMR), and puts in place measures to attract the investment needed to replace current generating capacity and upgrade the grid by 2020, and to cope with a rising demand for electricity.</p>	<p><b>National Grid has been asked to play a key delivery role</b></p> <p>In the UK, National Grid has been asked to play a major role as the delivery body for EMR, to be conferred on National Grid by Government in secondary legislation.</p>
<p><b>US policy is evolving to meet environmental and energy diversity goals</b></p> <p>In the US, many federal level developments have been through federal agency regulations and Presidential executive orders. At a state level, energy policy continues to evolve in the northeastern US, driven by interest in promoting energy efficiency, maintaining reliability and deploying renewable technologies that help meet environmental and energy diversity goals.</p>	<p><b>Options for increased renewable and distributed generation are being explored</b></p> <p>In the US, the impact on natural gas dependency has resulted in an evaluation of the best way of increasing fuel diversity through renewable and distributed generation resources. We continue to support movement towards a clean energy economy; and support additional measures to increase America's energy productivity.</p>

## Regulation

### **Infrastructure investment needs must be balanced with affordability**

Regulators acknowledge that there is a significant need for infrastructure investment. However, affordability continues to be a primary concern.

Cast iron gas mains still in use can be more than 100 years old, becoming riskier to use and contributing to greenhouse gas emissions through leaks. Severe weather in recent years has also highlighted the potential need for additional investment in network resilience. Regulators and policymakers are beginning to ask utilities to put plans in place to strengthen their networks' ability to withstand the effects of severe weather.

### **UK regulators want greater efficiency and innovation**

In the UK, the regulatory focus during the year has been on the new RIIO price controls which give greater focus to incentives and innovation than the previous regulatory regime.

The projected increase in offshore wind generation and interconnection has created a debate on the regulatory approach to electricity transmission investment – a debate we continue to be fully engaged in.

### **We must accommodate customers' cost concerns and also provide safe, up-to-date systems**

We must accommodate our customers' affordability concerns while fulfilling our obligations to provide safe and reliable services and upgrading our systems. Investment is required for new connections, to meet the challenges of changing supply and demand patterns, and to replace ageing infrastructure in the UK and US.

### **This is driving them to favour more market competition**

In the UK, competition is already in place for offshore development and Ofgem has stated its intent to retain the option of using greater competition for certain large onshore projects.

For more information about network efficiency and innovation, see pages 30, 31 and 33.

**US policymakers are focused on grid modernization**

In the US, we are actively involved in the New York Energy Highway initiative to examine new ways of delivering infrastructure in the state. In Massachusetts, we are working with regulators and policymakers on a new grid modernisation policy. This is ongoing but is likely to affect our investments in smart grid and metering, and cost recovery of electric infrastructure investments.

**This will present opportunities to address customers' needs more effectively**

In the US, developments like the New York Energy Highway initiative, the Reforming Energy Vision initiative announced by the Governor of New York, the Massachusetts Grid Modernization regulatory proceeding and our Connect21 dialogue with stakeholders, will help present new opportunities to respond to customers' needs and build the necessary infrastructure to address them.

**Innovation and technology**

**Technology developments have the potential to reshape our market**

There is continued significant technological development in the energy sector as new technologies take shape and approach commercial viability.


HVDC technology could play an important part in the development of a more integrated electricity grid, particularly the extension of offshore links.

**This influences demand and helps us to manage supply**

While carbon-based generation is likely to remain a significant part of the global energy mix, carbon capture and storage technologies may become critical to governments achieving their climate change targets. Technologies such as energy storage, electric transportation and distributed generation all have the potential to affect our networks significantly. New consumer products, such as alternative fuelled vehicles and distributed generation, will increase demand and require new infrastructure.

Smart grids will change the way loads are balanced across the distribution network, allowing our customers to make smarter energy choices and increasing network flexibility. Our infrastructure needs the flexibility to respond innovatively to emerging developments, potentially by being managed differently rather than by creating new infrastructure to meet supply and demand changes.

**Table of Contents**





**14 National Grid Annual Report and Accounts 2013/14**

**Our vision and strategy**


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

**Table of Contents**

					
	<b>Strategic Report</b>	<b>Corporate Governance</b>	<b>Financial Statements</b>	<b>Additional Information</b>	<b>15</b>



**Table of Contents**



**16 National Grid Annual Report and Accounts 2013/14**

**What we do**

Electricity

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

**Table of Contents**

<b>Strategic Report</b>	<b>Corporate Governance</b>	<b>Financial Statements</b>	<b>Additional Information</b>	<b>17</b>
-------------------------	-----------------------------	-----------------------------	-------------------------------	-----------

<p><b>System operator</b></p> <p>As system operator (SO) for England and Wales, we coordinate and direct electricity flows onto and over the transmission system, balancing generation supply and user demand. Where necessary, we pay sources of supply and demand to increase or decrease their generation or usage.</p>	<p>We have the same role for the two high voltage electricity transmission networks in Scotland and we have been appointed as system operator for the offshore electricity transmission regime.</p> <p>Our charges for SO services in the UK are subject to a price control approved by Ofgem. System users pay us for connection, for using the system and balancing services.</p>	<p>As electricity transmission system operator, our price control includes incentives to minimise the costs and associated risks of balancing the system through buying and selling energy, as well as procuring balancing services from industry participants.</p> <p>In the US, similar services are provided by independent system operators.</p>
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**Table of Contents**



**18 National Grid Annual Report and Accounts 2013/14**

**What we do**

**Gas**

*The gas industry connects producers, processors, storage, transmission and distribution network operators, as well as suppliers to industrial, commercial and domestic users.*

**Table of Contents**

<b>Strategic Report</b>	<b>Corporate Governance</b>	<b>Financial Statements</b>	<b>Additional Information</b>	<b>19</b>
-------------------------	-----------------------------	-----------------------------	-------------------------------	-----------

**System operator**

As system operator we are responsible for the high pressure gas National Transmission System (NTS) in Great Britain. We have responsibility for the residual balancing activities on the NTS and for keeping the physical system within safe operating limits.

Our price control, set by Ofgem, includes incentives that aim to maintain and improve our daily operational efficiency and are subject to renegotiation at set intervals.

**Table of Contents**



20 National Grid Annual Report and Accounts 2013/14

**How we make  
money from  
our regulated  
assets**

*Our transmission and distribution businesses operate as regulated monopolies. Regulators safeguard customers' interests by setting the level of charges we are allowed to pass on, so that we provide value for money while maintaining safe and reliable networks, and deliver good customer service.*

In the UK we have one regulator for our businesses, Ofgem. In the US, different services and locations are regulated by different bodies. For the areas in which we operate, these are the relevant state regulators and FERC.

**Investment in network assets** in the UK we are given a cost allowance to make necessary investments in the networks. These investment costs allowed by the regulator are linked to the outputs delivered by the networks.

**Financial review**

pages 06 – 09

Each of our regulatory agreements can include differences in structure, terms and values, which we summarise below. You can find more details about regulatory agreements on pages 160 to 165.

**Performance against incentives** our regulatory agreements, mainly in the UK, include incentives that are designed to encourage specific actions, such as reducing greenhouse gas emissions.

**UK regulation**

pages 160 – 162

The value of our regulated assets is calculated based on the terms of our regulatory agreements. In the UK, the value of regulated assets is also indexed for inflation.

Outperforming against incentive targets can increase our allowed revenues in the current year or a future year. Failing to achieve certain minimum targets may lead to a reduction in our allowed revenue.

**US regulation**

pages 162 – 165

Our regulatory agreements also determine the amount we are allowed to charge customers, commonly referred to as our allowed revenues. Allowed revenue is calculated based on a number of factors:

**Depreciation of regulated assets**

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

**Return on equity and cost of debt**

regulated assets are funded through debt or equity. Regulatory agreements set this ratio. The equity portion earns a return on equity. This represents the profit we can earn on our investment in regulated assets. The debt portion earns an allowance based on the cost of debt (interest costs).

Some regulatory agreements allow us to charge customers based on the interest we pay; others use an external benchmark interest rate to incentivise us to raise debt efficiently. The benchmark interest method also provides an opportunity to outperform our regulatory allowance.

**Cost of service** in establishing our regulatory agreements, our regulators consider what costs

A further incentive mechanism enables customers and shareholders to share the difference between allowed and actual costs via adjustments to revenue.

**Commodity costs** in the US, we supply gas and electricity to customers who have chosen us as their supplier. Most of our regulatory agreements include mechanisms known as trackers that allow us to recover the costs we incur when we buy gas and electricity.

**Deferrals** the costs we incur may not be included in the calculation of allowed revenue in the same year. Instead, these are deferred for regulatory purposes and we can normally recover them in future years. See pages 08 and 09 of the Financial review.

For example, in the US we incur costs restoring power to customers immediately after a major storm. However, these costs will generally be included in allowed revenue over a number of years and may not start until the relevant regulator has approved a request. This can be some time after the storm and may not cover all the costs.

**Timing** our regulated revenue entitlements are set based on our regulatory price controls. We use forecast energy volumes that we expect to deliver to set the billing tariff. Where there is a difference between the actual and estimated energy volumes, the amount of revenue we collect will be different. Differences arising from volume and revenue entitlement changes are typically collectable in the following year for the US. For information about timing in the

an efficiently run company would incur to operate and maintain our networks. They vary and examples can include costs relating to employees, office rental, IT systems and taxes.

UK, see pages 08 and 09.

The regulators have different approaches to determining what is considered an efficient or prudent cost and this may be different to the actual costs we incur.

**Table of Contents**

<b>Strategic Report</b>	<b>Corporate Governance</b>	<b>Financial Statements</b>	<b>Additional Information</b>	<b>21</b>
-------------------------	-----------------------------	-----------------------------	-------------------------------	-----------

**How our strategy**

creates value

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

**Customer and community value**

Our business model – a virtuous circle of growth

**Safety and reliability** we aim to provide reliable networks safely, which is essential to safeguard our customers, employees and the communities in which we operate.

**Affordability** we aim to provide services in a cost-efficient way, which helps to reduce the impact on customer bills.

**Customer service** providing essential services that meet the needs of our customers and communities is a crucial part of the value they expect from us.

**Sustainability** we aim to protect the environment and preserve resources for current and future generations.

**Emergency services** we provide telephone call centres, coordinate the response to gas emergencies, and respond



to severe weather events.

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

### Shareholder value

**Regulatory frameworks** operating within sound regulatory frameworks provides stability. Ensuring these frameworks maintain a balance between risk and return underpins our investment proposition.

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

**Efficient operations** efficient capital and operational expenditure allows us to deliver network services at a lower cost and reduces working capital requirements.

**Maximising incentives** positive performance under incentive mechanisms, and delivery of the outputs our customers and regulatory stakeholders require, helps us to make the most of our allowed returns.

**Funding and cash flow management** securing low cost funding and carefully managing our cash flows are essential to maintaining strong returns for our investors.

**Customers and communities** our focus on safety and reliability, as well as efficient investment in our networks, means that we are able to provide our customers and the communities in which we operate with the highest quality service we can. This makes sure they are able to access vital and reliable services whenever they need, wherever we operate.

**Reinvestment in our business** to continue generating reasonable returns for our shareholders and revenue growth, we reinvest efficiently in our regulated assets. This is critical to the sustainability of our business. By challenging our investment decisions, we continue to deliver reliable, cost-effective networks that benefit our customers.

**Revenue** the majority of our revenue is set in accordance with our regulatory agreements. This allows us a level of certainty over future revenues if we continue to meet safety and reliability targets, as well as the efficiency and innovation targets included in the new RIIO licence agreements in our UK regulated businesses.

**Cash flow** our ability to convert revenue to cash is an important factor in the ongoing reinvestment in our business and our ability to provide sustainable value growth for our shareholders. Our focus on efficient development of our networks is important in maximising free cash flow.

**Disciplined investment** we can achieve future revenue and earnings growth by increasing our regulatory asset value and rate base in line with regulatory capital allowances. Investment in non-regulated assets helps us to use and enhance our core capabilities with the aim of delivering attractive returns.

**Table of Contents**

**22 National Grid Annual Report and Accounts 2013/14**

**Internal control  
and risk  
management**

National Grid is exposed to a variety of uncertainties that could have a material adverse effect on:

the Company's financial condition;

our operational results;

our reputation; and

the value and liquidity of our shares.

The Board is committed to protecting and enhancing our reputation and assets, while safeguarding the interests of our shareholders. It has overall responsibility for the Company's system of risk management and internal control.

Below, we describe the main arrangements put in place so that the Board can carry out this responsibility and so that its members can be assured of the integrity of the Company's risk management and internal

Our Board also sets and monitors risk appetite annually. We have a framework that differentiates our appetite for risk by categories. At the annual review meeting, the Board compares the decisions the Company has taken to the appetite level in each category. It then considers the appropriate appetite levels to set for the year ahead.

**Our principal risks**

Accepting that it is not possible to identify, anticipate or eliminate every risk that may arise and that risk is an inherent part of doing business, our risk management process aims to provide reasonable assurance that we understand and manage the main uncertainties that we face in delivering our objectives.

This includes consideration of inherent risks, which exist because of the nature of day-to-day operations in our industry. An overview of the key inherent risks we face is provided on pages 167 to 169. Examples

control systems, financial information and financial controls.

include:

### Risk management approach

Our Company-wide corporate risk management process provides a framework through which we can consistently identify, assess, prioritise, manage and report risks. It is designed to support delivery of our strategic and business objectives described on pages 14 and 15.

The risks we identify are collated in risk registers and are reported at functional and regional levels of the Company. These registers include an assessment of how likely it is that each risk will materialise.

They highlight the potential worst case credible financial and reputational impact of the risk and details of mitigation activities. The risk registers also describe the adequacy of our existing risk controls. The main risks for our UK and US businesses are summarised and are reviewed, reported and discussed regularly by our senior leadership team.

In addition, we also record the main strategic risks for the Company which are developed through discussions with the Executive leadership team. These risks are reported and discussed with the Executive Committee and Audit Committee every six months and by the Chief Executive through quarterly performance reports.

During 2013/14 the Board reviewed the main elements of our risk management process. This included validating the risks

aspects of the work we do could potentially harm employees, contractors, members of the public or the environment;

we may suffer a major network failure or interruption, or may not be able to carry out critical non-network operations due to the failure of technology supporting our business-critical processes;

changes in foreign currency rates, interest rates or commodity prices could materially impact earnings or our financial condition;

an inability to access capital markets at commercially acceptable interest rates could affect how we maintain and grow our businesses; and

customers and counterparties may not perform their obligations.

included in our corporate risk profile and consideration of how we treat special categories of risks, such as potential extreme catastrophic events and emerging risks (uncertainties that are still developing). The results of the Board review are being incorporated into the ongoing work of the Corporate Risk team.

**Table of Contents**

<b>Strategic Report</b>	<b>Corporate Governance</b>	<b>Financial Statements</b>	<b>Additional Information</b>	<b>23</b>
-------------------------	-----------------------------	-----------------------------	-------------------------------	-----------

**Principal risks**

Our corporate risk profile contains the principal risks that the Board considers to be the main ones currently faced by the Company. An overview of these risks is provided below, together with examples of the relevant controls and mitigating actions we are taking.

Strategic objective	Risk description	Example of mitigations
<b>Deliver growth</b>	<p>Failure to identify the right opportunities to execute our strategic ambition.</p> <p>Failure to sufficiently grow our core business and have viable options for new business over the longer term would negatively affect the Group’s credibility and jeopardise the achievement of intended financial returns.</p> <p>Our ability to achieve our ambition for growth is subject to a wide range of external uncertainties, including the availability of potential investment targets and attractive financing; and internal uncertainties, such as the performance of our operating businesses and our business planning model assumptions.</p>	<p>We regularly monitor and analyse market conditions, competitors and their potential strategies, as well as the performance of our Group portfolio. We are also looking to access new sources of finance and capabilities through partnering.</p> <p>We have internal processes for reviewing and approving investments in new businesses, disposals of existing ones and organic growth investment opportunities. These processes are reviewed regularly to make sure our approach supports our short- and long-term strategies. We undertake due diligence exercises on investment or partnering opportunities and carry out post-investment reviews to make sure we learn lessons for the future.</p>

<p><b>Engage externally</b></p>	<p>Inability to influence future energy policy.</p> <p>Policy decisions by regulators, governments and others directly affect our business. We must engage widely in the energy policy debate, making sure our position and perspective help to shape future policy direction.</p>	<p>In the UK, we are working closely with DECC on Electricity Market Reform (EMR) plans. We have also restructured our business so we are prepared for our new role under EMR and to make sure we are well positioned to deliver value under RII0. The Board is also continuing to monitor the increasing public debate around the cost, availability, security and sustainability of UK energy supplies.</p> <p>In the US, we have begun to engage our external stakeholders about the role of the utility company of the future, under the banner of Connect21. We believe this conversation will help shape the regulatory and fiscal regime in the US in the future. We are maintaining our jurisdictional focus and we will continue to file new rate cases so our businesses can earn a fair and reasonable rate of return. Our rate filings include structural changes where appropriate, such as revenue decoupling mechanisms, capital trackers, commodity-related bad debt true-ups and pension and other post-employment benefit true-ups, as described on pages 162 to 165.</p>
<p><b>Engage our people</b></p>	<p>Inability to secure the business capacity, appropriate leadership capability and employee engagement levels required to deliver our vision and strategy.</p> <p>It is through the high-quality work of our employees that we will achieve our vision, respond to the changing needs of our stakeholders and create a competitive advantage. Obtaining and fostering an engaged and talented team that has the knowledge, training, skills and experience to deliver on our strategic objectives is vital to our success. We must attract,</p>	<p>We have identified the core capabilities that align with our strategic ambition and continue to develop our Academy to help develop the right skills for the future (see page 40).</p> <p>We are involved in a number of initiatives to help secure the future engineering talent required (see page 40).</p> <p>We continue to develop our succession plans for key roles, including leadership.</p> <p>We have described on page 41 some of the ways we seek to engage employees,</p>

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integrate and retain the talent we need at all levels of the business.

including how we promote inclusion and diversity.

We monitor employee engagement and formally solicit employee opinions via a Company-wide employee survey annually.



**Table of Contents**



24 National Grid Annual Report and Accounts 2013/14

**Internal control and  
risk management**

continued

Strategic objective	Risk description	Example of mitigations
<p><b>Deliver operational excellence</b></p>	<p>Failure to achieve levels of financial performance required to meet regulatory requirements.</p> <p>The Group operates under a number of regulatory regimes and we must maintain the performance levels required. Failure to achieve the agreed returns could damage our reputation and threaten future growth opportunities and regulatory arrangements.</p>	<p>We have a US strategy focused on safety and reliability, customer responsiveness, stewardship and cost competitiveness. Performance measures are tracked and reported monthly. US jurisdictional presidents continue to develop strong relationships with local regulators and communities. A process excellence initiative was launched to deliver sustainable and innovative performance improvements with initial focus on six core end-to-end processes.</p> <p>The UK operating model implemented in 2013 to support our performance under RIIO is now established and we continue to roll out our performance excellence framework across</p>

		<p>the business.</p> <p>We monitor network reliability and customer satisfaction as KPIs, as described on page 10.</p>
	<p>Failure to deliver appropriate information systems and data integrity.</p> <p>The Company is increasingly reliant on technology to support and maintain our business-critical processes. We must be able to rely on the performance of these systems and the underlying data to demonstrate the value of our business to our shareholders, and to meet our obligations under our regulatory agreements, and comply with agreements with bond holders and other providers of finance.</p>	<p>In November 2012, our new US back office system went live. A business improvement team has been established to ensure that a comprehensive and integrated approach is applied to the execution of system changes (such as enablement of the LIPA MSA transition) and enhancements to drive business value (such as payroll, supply chain and finance process improvements).</p> <p>We are undertaking a programme to strengthen identified weaknesses in US controls over financial reporting.</p> <p>We are implementing a global information management framework focusing on data integrity and security.</p> <p>We have completed a data assurance programme, and we are developing actions to improve our data quality and integrity processes based on the results.</p>
	<p>We experience a catastrophic/major cyber security breach.</p> <p>Due to the nature of our business we recognise that our critical national infrastructure systems may be a potential target for cyber threats. We must protect our business assets and infrastructure and be prepared for any malicious attack.</p>	<p>We use industry best practices as part of our cyber security policies, processes and technologies.</p> <p>We continually invest in cyber strategies that are commensurate with the changing nature of the security landscape. This includes collaborative working with DECC and the Centre for Protection of National Infrastructure (CPNI) on key cyber risks and development of an enhanced critical national infrastructure (CNI) security strategy and our involvement in the US with developing the National Institute of Standards and Technology (NIST) Cyberspace Security</p>

Framework.

Failure to prevent a significant process safety event.

We have established safety and occupational health plans, programmes and procedures that are aimed at continuous improvements in safety performance.

The nature of our day-to-day operations is such that safety incidents can occur. The safety of our employees, contractors, suppliers, and the communities in which we operate is critical. We must operate within local laws and regulations relating to health, safety and the environment.

We supplement Company-wide initiatives with specific regional safety programmes. These are aimed at addressing specific areas so that safety is at the forefront of every employee's mind. We also benchmark against other industry groups to seek and implement best practice.

We continue to focus on process safety, aimed at preventing major incidents. A baseline assessment has been completed and a 10 year plan is under development.

We monitor employee IFR as a KPI as described on page 10.

**Table of Contents**

<b>Strategic Report</b>	<b>Corporate Governance</b>	<b>Financial Statements</b>	<b>Additional Information</b>	<b>25</b>
-------------------------	-----------------------------	-----------------------------	-------------------------------	-----------

**Our internal control process**

We have a number of processes to support our internal control environment. These processes are managed by dedicated specialist teams, as described in the box on the right. Oversight of these activities is provided through regular review and reporting to the appropriate Board committees as outlined in the Corporate Governance section on pages 44 to 57.

These reviews are supplemented by quarterly performance reviews, attended by the Chief Executive and Finance Director which consider historical results and expected future performance and involve senior management from both operational and financial areas of the business.

Each month the Finance Director presents a consolidated financial report to the Board.

**Reviewing the effectiveness of our internal control**

Each year the Board reviews the effectiveness of our internal control process, including financial reporting, to make sure it remains robust. The latest review covered the financial year to 31 March 2014 and the period to the approval of this Annual Report and Accounts. It included:

As part of our assessment of financial controls, we have identified a number of weaknesses in our US financial control framework. Plans are in place to remediate these. For more information, including our opinion on internal control over financial reporting, see page 170.

the Certificate of Assurance for noting following approval by the Audit Committee to provide overall assurance around the effectiveness of National Grid's risk management and internal controls systems;

**Our internal control environment**

Our specialist teams that manage the processes supporting our internal control environment are described below.

where appropriate, assurance from our committees, with particular reference to the reports received from the Audit, and Safety, Environment and Health Committees on reviews undertaken at their meetings; and

assurances about the certifications required under Sarbanes-Oxley as a result of our US reporting obligations.

Our risk management and internal control processes comply with the Turnbull guidance on internal control and the requirements of the UK Corporate Governance Code. They are also the basis of our compliance with obligations set by the Sarbanes-Oxley Act 2002 and other internal assurance activities.

### Internal control over financial reporting

We have specific internal mechanisms to govern the financial reporting process and the preparation of the Annual Report and Accounts. Our financial controls guidance sets out the fundamentals of internal control over financial reporting, which are applied across the Company.

Our financial processes include a range of system, transactional and management oversight controls. In addition, our businesses prepare detailed monthly management reports that include analysis of their results along with comparisons to relevant budgets, forecasts and prior year results. These are presented to and reviewed by senior management within our Finance function.

### Risk management:

works with the Board to determine risk appetite and establish and implement risk management policies;

is responsible for the independent review and challenge of risk information throughout the business, compilation and analysis of risk profiles and monitoring risk management processes within the Company; and

regularly reports on risks to the regional level and Board level oversight committees.

### Ethics and compliance management:

maintains our standards of ethical business conduct;

promotes ethical behaviour and monitors compliance with external legal and regulatory requirements; and

operates our whistle-blower helplines and supports activities to prevent and detect bribery.

### Corporate audit:

develops and executes a risk-based audit plan; and

provides independent, objective assurance to the Audit Committee, SEH Committee and the Executive Committee on the extent to which control and governance frameworks are operating effectively.

### Safety, environment and health:

develops policy recommendations for the Board;

monitors safety, environment and health performance; and

works with process owners to deliver our safety, environment and health objectives.

**Internal controls:**

works with process owners to identify, document and test the design and operation of internal control over financial reporting; and

helps refine and improve controls where required.

**Table of Contents**



**26 National Grid Annual Report and Accounts 2013/14**

**How executive remuneration aligns to Company strategy**

The Remuneration Committee determines remuneration policy and practices through which we aim to promote the success of the Company by attracting, motivating and retaining high-calibre Executive Directors and other senior employees to deliver value for our shareholders, customers and the communities in which we operate.

**Our strategy**

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

The Committee believes that the changes will further enhance the long-term alignment between executive remuneration and the delivery of the corporate strategy.

The information set out below describes current rather than future policy.

**Alignment to strategy**

**Annual Performance Plan (APP)**

Our APP aims to incentivise and reward the achievement of annual financial and strategic business measures, and the delivery of annual individual objectives. Performance metrics, including corporate financial measures and individual objectives, are agreed at the start of each performance year and are aligned with the strategic business priorities for that year.

The table below shows the financial measures and their relative weightings that were included within the APP for the Executive Directors for 2013/14:

**Our vision and strategy**

pages 14 15

**Remuneration Report**

pages 58 73

our investors.

## Our strategic objectives

### Deliver operational excellence

**Andrew  
Bonfield**

and

### Engage our people

**Steve  
Holliday**      **Tom  
King**      **Nick  
Winser**

### Stimulate innovation

Adjusted EPS	24%	24%	24%
Cash flow (Group or regional)	38%	28%	43%

### Engage externally

UK RoE	14%	n/a	33%
US RoE	14%	24%	n/a

### Embed sustainability

US capital plan delivery			
	10%	24%	n/a

### Drive growth

Financial measures together represent 70% of the APP.

The Remuneration Committee aligns the remuneration policy to our Company strategy and main business objectives. Performance-based incentives are earned through achieving demanding targets for short-term business and individual performance, as well as creating long-term value for our shareholders, customers

Individual performance objectives in the APP reflect 30% of the plan and are defined in terms of target and stretch performance requirements. The performance objectives change each year, depending upon business priorities. Examples of individual objectives include those relating to safety, stakeholder relations, employee engagement and capability, and the development of Group and financial strategy.

In order to provide balance for all our stakeholders, at the end of the year the Remuneration Committee has discretion to reduce APP awards to take account of any safety, customer, service-related, environmental or



and the communities in which we operate. governance issues that may have occurred.

## Remuneration Committee review

### of remuneration

During the year, the Remuneration Committee undertook a detailed review of the remuneration arrangements for Executive Directors, with the aim of achieving further alignment between executive reward and long-term shareholder value.

As a result of this review, the Committee is proposing some significant changes to the arrangements for the 2014/15 financial year, and these are set out in detail on pages 58 to 73. Shareholders are being asked to approve these changes at the AGM on 28 July 2014.

**Table of Contents**

<b>Strategic Report</b>	<b>Corporate Governance</b>	<b>Financial Statements</b>	<b>Additional Information</b>	<b>27</b>
-------------------------	-----------------------------	-----------------------------	-------------------------------	-----------

**Long Term Performance Plan (LTPP)**

Our LTPP aims to drive long-term performance, aligning Executive Director incentives to key strategic objectives and shareholder interests. Performance measures set are considered to either drive or measure long-term value within the business, aligning executive reward with long-term sustainable performance.

The table below shows the performance measures and the relative weightings of these that were included within the LTPP awards made to the Executive Directors during 2013/14:

Performance measure	Weighting	Definitions and performance period
<b>Adjusted earnings per share (EPS)</b>	50%	<p>Threshold performance where EPS growth exceeds RPI growth by three percentage points</p> <p>Stretch performance where EPS growth exceeds RPI growth by eight percentage points or more</p>

		Performance period	three years
<b>Relative total shareholder return (TSR)</b>	25%	Threshold performance	where TSR is at the median of the FTSE 100
		Stretch performance	where TSR performance is 7.5 percentage points or more above that of the median of the FTSE 100
		Performance period	three years
<b>UK and US RoE</b>	25%	Threshold performance	where allowed regulatory returns are achieved (UK) or under-performed by one percentage point (US)
		Stretch performance	where allowed regulatory returns are out-performed by at least two percentage points (UK) or at least one percentage point (US)
		Performance period	four years

If the Remuneration Committee considers the underlying performance of the Company does not justify the vesting of LTTP awards, even if some or all of the performance measures are satisfied in whole or in part, it can declare that some or all of the awards lapse.

For full details about our remuneration policy and how it is implemented, please see the Remuneration Report on pages 58 to 73.



**Table of Contents**

**Table of Contents**

<b>Strategic Report</b>	<b>Corporate Governance</b>	<b>Financial Statements</b>	<b>Additional Information</b>	<b>29</b>
-------------------------	-----------------------------	-----------------------------	-------------------------------	-----------

**Principal operations**

Overview of our UK RIIO-regulated businesses during 2013/14

Over the past year there have been significant regulatory changes in the UK, most notably the introduction of RIIO and its associated incentives.

The RIIO regulatory framework, which began on 1 April 2013, incentivises us to operate efficiently. It also provides opportunities in terms of specific incentives to engage and serve our customers and stakeholders well.

There have been significant Government and regulatory policy changes affecting our business, including the introduction of EMR and the evolution of the system operator role in the long-term planning of the network. Also, with a likely tightening of the margin between electricity supply and demand in the mid to late part of the decade, additional tools have been developed to help us balance the electricity transmission system.

costs. Following the severe wet weather over Christmas 2013 we have been working on future potential network resilience issues. For details about our reliability performance see page 10.

Renegotiating our key contracts and introduced new contractor relationships so we can deliver our RIIO outputs efficiently and provide clarity on the accountability for safety between ourselves and our contractors.

Continuing to focus on delivering excellent levels of service. 2013/14 has been the first year in which we have had incentives for customer and stakeholder satisfaction for our regulated businesses. Ofgem set a baseline target of 6.9 for customer and stakeholder satisfaction for our regulated transmission businesses with scoring ranging from 1 very dissatisfied to 10 very satisfied. We have performed well in our customer surveys, scoring 7.2 for our Gas Transmission business and 7.4 for our Electricity Transmission business. The stakeholder surveys are newly introduced but early indications are that both transmission businesses are in line to achieve good results for stakeholder

The planning process for obtaining consent for major infrastructure projects has also changed, requiring significant consultation before an application to the Planning Inspectorate. Our Kings Lynn B connection project was the first to go through the new process and was granted consent by the Secretary of State in December 2013.

### Progress during 2013/14

Our activities and achievements in the UK during 2013/14 have included:

Achieving an employee injury frequency rate of 0.06, meeting our target of world-class performance. Initiatives during 2013/14 included a visible safety leadership programme with a renewed focus on behavioural safety and excellent role modelling, as well as introducing best practice incident analysis tools and systems from the US into our UK business so we can improve how we learn from incidents.

Making significant progress on the implementation of our new UK operating model by concluding the managerial and staff appointment process in our Transmission business.

Working with trade unions to agree revisions to pay and terms and conditions for employees. We have also agreed changes to our UK pension arrangements for all employees who have defined benefit (DB) or defined contribution (DC) schemes. These changes aim to make sure our total reward package remains both competitive in the market and sustainable under RIIO.

Working on the 2013 triennial valuations of our two DB pension plans (for further information see note 29 under Notes to the consolidated financial statements ).

satisfaction.

Under RIIO our gas distribution customer satisfaction results are now reported on an annual basis, rather than quarterly, which was how we reported them under our previous price control. We will publish the results on our website in the summer as part of our commitment to our stakeholders, and in our Annual Report and Accounts for 2014/15.

Extensive involvement in the development of new network codes to underpin the European internal energy market.

Focusing on changing our ways of working supporting the development of our global performance excellence framework with targeted roll-out in the UK. Our approach has been to build up the capability requirements through early adopters before starting the full-scale roll-out over the coming months.

### Principal risks

Our regional risk profile describes the main risks our UK business faces. Below, we provide an overview of some of the risk themes we are managing:

the risk of changes to the complex political and regulatory agenda for UK and European energy policy development and their potential implications for our business;

challenges associated with making sure the data required to deliver business processes and regulatory requirements is complete, accurate and consistent;

the impact of changes in our business structure and processes on our ability to continue to perform under RIIO; and

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Maintaining resilient networks during the wettest winter on record. Our networks withstood the winter storms well, when some electricity distribution networks had significant issues. We have installed extra flood protection at critical UK sites, helping maintain reliability and reduce

continued management of safety, security and network resilience.



**Table of Contents**



**30 National Grid Annual Report and Accounts 2013/14**

**Principal operations**

continued

**UK Electricity Transmission**

**What we do**

We own the electricity transmission system in England and Wales. Our networks comprise approximately 7,200 kilometres (4,470 miles) of overhead line, 1,400 kilometres (870 miles) of underground cable and 335 substations.

We are also the national electricity transmission system operator, responsible for both the England and Wales transmission system, and the two high voltage transmission networks in Scotland, which we do not own.

Day-to-day operation of the system involves the continuous real-time matching of demand and generation output. We are also designated as system operator for the new offshore electricity transmission regime.

activities, increasing the potential for access to the transmission system.

We improved our asset maintenance policy, which will provide greater efficiency for our maintenance programme. We are implementing the policy throughout 2014 to minimise disruption to customers and planned work.

We worked closely with DECC and Ofgem to help inform and manage security of supply through a period of significant change in the UK energy market.

We have carried out analysis to help inform the Government's decisions on energy policy as well as administering key parts of the enduring regime.

We have developed two new balancing services that could be used to provide additional reserves to support the operation of the electricity transmission system if margins continue to tighten towards the middle of this decade. These new services, known as the Demand Side Balancing

**30%**

**UK Electricity Transmission adjusted operating profit of Group total**

### Where we are heading

Although demand for electricity is generally increasing around the world, in the UK it is expected to remain broadly flat over the next five to 10 years.

Changes in the sources and characteristics of generation connecting to our network mean we need to develop the way we balance and operate our network to accommodate these sources, including wind, new and large-scale nuclear generation, and many embedded sources that are connected to local networks and not our transmission grid.

Industry forecasts indicate there will be a tightening of the margin between the available supply of electricity and the demand for it over the next few years. We have a central role in developing the reform of the electricity market, which is designed to incentivise new generation to be built. We have also developed two new balancing services allowing the market to provide us with additional tools to balance the network if required.

Over the last 12 months some generators have delayed their connection dates to the network and this means our future investment profile for electricity transmission is flatter than in previous years. But we are ready to respond to connection dates when we need to. We will continue to renew our network to deliver the network reliability our customers require as efficiently as possible.

Reserve and the Supplemental Balancing Reserve, were approved by Ofgem in December 2013, and the associated funding arrangements approved in April 2014. We will tender for these services if they are needed for the forthcoming winters.

### Priorities for the year ahead

Work with our contract partners to continue improving safety performance.

Engage with customers and stakeholders while we progress our major infrastructure projects through the planning process.

Continue the roll-out of our new performance excellence way of working across Electricity Transmission.

Develop new, innovative ways to deliver the network reliability our customers require, at minimum cost.

Build on the analysis results that informed the first EMR delivery plan and successfully implement and operate the Capacity Market and Contracts for Difference Feed-in Tariff regime, as part of the Government's EMR project. This will support a sustainable, affordable and secure electricity market into the future, in addition to the procurement of balancing services to support mid-decade capacity margins.

Shape development in the UK and EU energy industry by continuing the development of network codes to support the completion of a European Internal Energy Market in 2014.

### What we've achieved during 2013/14

We made significant progress with our network upgrade plans. We are pleased with our progress on the London Power Tunnels project and have now started site works on the first 600 kV subsea HVDC link in the world. Connecting Scotland and England, this link will support the export of low carbon Scottish generation.

In March 2014, the new Transmission National Control Centre in Warwick became operational. This will help our focus on the future complexities of network security, energy management and streamlining our operational and safety switching

**Table of Contents**

<b>Strategic Report</b>	<b>Corporate Governance</b>	<b>Financial Statements</b>	<b>Additional Information</b>	<b>31</b>
-------------------------	-----------------------------	-----------------------------	-------------------------------	-----------

**UK Gas Transmission**

**What we do**

We own and operate the gas national transmission system in Great Britain, with day-to-day responsibility for balancing demand. Our network comprises approximately 7,660 kilometres (4,760 miles) of high pressure pipe and 23 compressor stations.

**Where we are heading**

The UK's sources of gas are changing as gas from the UK continental shelf is being depleted, we are becoming increasingly reliant on imports from Europe and elsewhere. This also means that the traditional flow of gas from the North to the South is changing.

To ensure we continue delivering a safe, reliable and secure gas supply as we develop our asset replacement

**Priorities for the year ahead**

**11%**

Continue to improve safety performance by completing the roll-out of the visual safety leadership culture programme to every employee in our Gas Transmission business and implementing new safe control of operations working procedures.

Work with our customers and stakeholders to develop an enduring compressor replacement strategy that makes sure we comply with environmental legislation and meets as future system needs.

Complete the deployment of our new performance excellence way of working across all teams in our Gas Transmission business after the successful implementation at two of our compressor sites in 2013/14.

Support our customers in the transition to new commercial frameworks managing future capacity and connection arrangements to the gas transmission

**UK Gas Transmission  
adjusted operating  
profit of Group total**

programmes, we need to make sure we consider the future operational needs of the network.

We will continue to work closely with our customers and stakeholders to adapt our network and our services so we can meet their needs economically and efficiently.

system.

Shape developments in the UK and EU energy market by making sure that the new European codes governing the operation of the gas market in the UK are successfully introduced for our customers.

### What we ve achieved in 2013/14

We delivered our strongest-ever safety performance across all areas, achieving 12 months without a single lost time injury to either our employees or contractors and without experiencing any serious process safety incidents.

We delivered multiple innovation projects using the Network Innovation Allowance funding mechanism, including 3D models that allow for more efficient and cost-effective construction.

We have adapted our ways of working so we can meet the needs of our customers and stakeholders and deliver value under RIIO. For example, we used innovative techniques to protect a section of the pipeline that carries gas from the LNG importation terminal in west Wales, prior to the construction of a new road. This meant we were able to meet the timescales of the local authority building the road without disrupting gas supply to consumers.

We have delivered record levels of compressor availability in our network, peaking at 98%, after investing in our fleet of compressors in the summer of 2013 and by introducing improvements to our maintenance and repair methods.

**Table of Contents**

**Table of Contents**

<b>Strategic Report</b>	<b>Corporate Governance</b>	<b>Financial Statements</b>	<b>Additional Information</b>	<b>33</b>
-------------------------	-----------------------------	-----------------------------	-------------------------------	-----------

**Principal operations**

continued

**UK Gas Distribution**

We own and operate four of the eight regional gas distribution networks in Great Britain. Our networks comprise approximately 131,000 kilometres (81,000 miles) of gas distribution pipeline and we transport gas from the gas national transmission system to around 10.9 million consumers on behalf of 32 gas shippers.

A notable example of innovation during 2013/14 has been the use of a repair robot called CISBOT to fix a leaking 18 inch gas main in London. This was the first time in Great Britain that an 18 inch gas main has been fixed by robots. This kind of automation reduces traffic disruption and avoids the need to shut off the gas while doing the repair work, making life easier for people.

**UK Gas Distribution  
adjusted operating  
profit of Group total**

Gas consumption in our UK networks was 264 TWh in 2013/14 compared with 306 TWh in 2012/13. We manage the national gas emergency number (0800 111 999).

Working with Future Biogas we successfully commissioned the first commercial biogas-to-grid project in Doncaster. The biomethane injection is produced from a maize feedstock and is the first of 20 similar projects that we are committed to connect during 2014/15. This kind of project promotes the future role of gas in the transition to a low carbon economy and is also the first of 80 connections we expect to complete over the RIIO period.

This service, along with the enquiries lines, appliance repair helpline and meter enquiry service, handled nearly 2.5 million calls during 2013/14.

**Priorities for the year ahead**

## Where we are heading

We have articulated an ambition for 2017 to be the best gas distribution business in Britain. We are using modern technology and new, innovative techniques to develop gas networks that are fit for the future, safe and secure, keeping people warm.

Our regulator is able to make direct comparisons between the performance of our four gas distribution networks, and others. Customer expectations are increasing across all industries and we are responding by focusing more effort than ever before on providing a good-quality service at an affordable price to all our customers and stakeholders. We will do this by carrying out our works in the most efficient way possible.

## What we've achieved during 2013/14

We have improved our overall safety performance (see page 10). We have focused on reducing cable strikes with programmes like *dig before you dig* and seen a 14% reduction in cable strikes during 2013/14.

The number of customer complaints we received during 2013/14 was 13.3% less than the previous year. However, we know our customers want more and we are focusing our attention on improving even further, particularly the experience customers have when they want to connect to our network.

Last year we listened to what our stakeholders had to say through our consultation process and we made 29 commitments to improve in areas of stakeholder priority such as fuel poverty, vulnerability, gas safety including carbon monoxide awareness and new and innovative ways of working.

All our priorities support our Gas Distribution ambition and are above and beyond meeting our standards.

Achieve our safest year ever by improving the safety to members of the public, continuing to reduce cable strikes and making improvements that will help reduce the number of third-party encroachments.

Improve the experience our customers have with us and the way in which we engage with our stakeholders, including reducing complaints and rejuvenating our customer connections process.

Invest in our people to help them develop their skills and increase their capability, including a focus on the role of the supervisor and promoting accelerated development assignments.

Engage with our people by embedding performance excellence in the remainder of our Gas Distribution business and delivering on our enhanced engagement strategy.

Drive innovation so we can improve the services and value we provide to our customers by both maximising existing technology and identifying new opportunities for future development.

Improve the quality and availability of our data and management information so we can operate more efficiently in the future.



We have been simplifying and improving the way we work so that our employees can be as effective as possible and our customers get a service they value. We are doing this by looking for ways to streamline, innovate and improve everyday working practices with our business and our strategic partners who help us reach our goals.

**Table of Contents**

**Table of Contents**

<b>Strategic Report</b>	<b>Corporate Governance</b>	<b>Financial Statements</b>	<b>Additional Information</b>	<b>35</b>
-------------------------	-----------------------------	-----------------------------	-------------------------------	-----------

**Principal operations**

continued

**US Regulated business**

**What we do**

We own and operate electricity distribution networks in upstate New York, Massachusetts, and Rhode Island. Through these networks we serve approximately 3.4 million electricity consumers in New England and upstate New York.

Our US gas distribution networks provide services to around 3.6 million consumers across the northeastern US, located in service territories in upstate New York, New York City, Long Island, Massachusetts and Rhode Island. We added 31,145 new gas heating customers in these areas in 2013/14.

We own and operate an electricity transmission system of approximately 14,328 kilometres (8,903 miles) spanning upstate New York, Massachusetts, Rhode Island, New Hampshire and Vermont, operating 169 kilometres (105 miles) of underground cable and 521

Connect21 will help develop America's economic and environmental health in three very important ways:

**Drive economic growth:** invest in our networks in

ways that enhance state and local economies and

encourage innovation, while simultaneously reducing

the stress currently being exerted on our environment

and public health.

**Promote cleaner energy:** work with the industry to

find new ways to deliver cleaner energy, and more

**US Regulated business adjusted operating profit of Group total**

substations, with a further 12 planned.

importantly encourage consumers to use energy more

We also own and operate 50 fossil fuel-powered units on Long Island that together provide approximately 3,800 MW of power under contract to LIPA. A 15 year Power Supply Agreement (PSA) with LIPA was renewed in May 2013 for 3,634 MW of capacity, comprising eight dual fuel (gas/oil-fired) steam units at three sites, 11 dual fuel combustion turbine units, and 27 oil-fired combustion turbine/ diesel units. Under a separate contract with LIPA, four dual fuel combustion turbine units provide an additional 160 MW of capacity.

efficiently. We are already making progress on cleaner

sources of energy, such as natural gas. The amount of

energy generated by natural gas in the US is expected

to double between 1990 and 2040, making gas the

leading fuel for electricity generation.

**Advance innovative technologies:** harness existing

We are responsible for billing, customer service and supply services. We forecast, plan for and procure approximately 15 billion standard cubic metres of gas and 32 TWh of electricity annually across three states.

technologies to put energy information and usage

control in the hands of customers, which will help drive

improvements in our consumption behaviours.

### Where we are heading

We have introduced Connect21, our thinking on advancing America's natural gas and electricity infrastructure beyond its 20th century limitations, and creating a more customer-centric, resilient, agile, efficient and environmentally sound energy network.

Leverage technology to build smarter, more resilient

electric and natural gas networks that can withstand

the extreme weather.

Our approach is threefold:

**Build a resilient backbone** for our energy system

that can provide reliable, flexible electric and gas

service to all customers and integrate clean energy

### Principal risks

Our regional risk profile describes the main risks our US business faces. The current risk themes for the US are:

our ability to manage data and systems improvements required to deliver core business processes and

regulatory requirements;

wherever it is located on the grid.

our ability to recover costs through existing rate-

**Inform customers** about choices available to them

making mechanisms and to influence the development

to meet their energy needs and educate them on how

of the future US utility business model; and

to manage their use in the most cost-effective way.

safety performance and network reliability, security and resilience.

**Offer customised solutions** to customers who

want different levels of service.

### What we've achieved

Within each of our jurisdictions we have focused on Elevate 2015, our journey towards operational excellence. This focus has encompassed our end-to-end business processes, including:

delivery;

maintenance and operation of electric and gas

assets;

supply chain management;

meter to cash; and

emergency response.

Four main principles govern our business improvement strategy: safety and reliability; stewardship; customer responsiveness; and cost competitiveness.

**Table of Contents**



**36 National Grid Annual Report and Accounts 2013/14**

**Principal operations**

continued

**US Regulated business**

All jurisdictions have benefited from emergency response improvements. This has been a focus for the US business in response to the major storms we have experienced in recent years, such as Superstorm Sandy in 2012. Our Emergency Management Policy reinforces our commitment to our customers and the communities we serve. We strive to use effective emergency management principles and protocols that enhance our ability to provide safe and reliable energy services.

We have continued to strengthen resilience by assessing vulnerabilities throughout our system, flood-proofing critical equipment, readying more restoration crews, repair equipment and fuel supplies, reducing the risk of downed power lines from fallen trees and branches, and enhancing communications with our customers

reach our goal of zero injuries every day. Some of our initiatives during 2013/14 include the development and implementation of a safe motor vehicle operation policy, Smith System driver training, a soft tissue injury prevention programme, and slippery surface simulator training. Also, in a continued effort to promote safety awareness and improvement, we have shared incident reports and lessons learned briefings with all employees, on a daily basis.

**Network reliability:** we met all our reliability targets in Rhode Island and New York. In Massachusetts, we missed two of our electricity circuit level metrics and avoided a financial penalty due to earned offsets for good performance on our system metrics.

**National Grid teams maintain and repair the gas distribution networks across Rhode Island, where we deliver gas to 252,000 customers. The team in this picture is creating a solid base to reinstate the ground after some works on Rhode Island's gas network.**

and stakeholders. During 2013/14 we introduced some new tools and initiatives:

**Weather predictive tool:** allows us to use data from

past storm events to learn and predict future

potential damage, which will help our storm

response planning.

**Expanded contractor relationships:** expanding

contractor relationships that cover a wider

geographic area to increase flexibility and

responsiveness in any type of storm.

**Enhanced damage assessment:** by using

technology now available to us (mobile devices such

as tablets) we have introduced an enhanced

damage assessment process that helps us to gather

information from the field more quickly. Coupled with

data from existing outage reporting systems, this

allows us to determine where to send crews more

quickly and accurately. This, in turn, will help us to

**Customer satisfaction:** we use independent customer research studies and other measures to supplement the four J.D. Power and Associates customer satisfaction studies. We saw improvements in three of the four overall J.D. Power customer satisfaction quartile results see page 10 for details.

In terms of our achievements during 2013/14, here are some highlights from each of our jurisdictions:

#### Massachusetts

**Infrastructure investment:** we invested \$510 million to enhance the resilience, efficiency and safety of our infrastructure \$212 million in electric and \$298 million in natural gas.

**Energy efficiency:** we introduced Smart Energy Solutions , a programme rolled out to 15,000 customers. The programme uses grid modernisation solutions, including advanced meters and communications systems and offers our customers better data about their energy usage, which helps them to make more informed decisions.

**Gas expansion:** we installed 32 miles of new gas mains, replaced 162 miles of gas mains and added more than 9,700 new natural gas customers.

determine and execute restoration  
times faster for

customers and communities.

US enterprise resource planning system stabilisation continued, remedying the errors of poor implementation from the prior year. Over the course of the year, the US business made significant progress in the activities required to upgrade the system, with implementation expected in mid-2014. The focus is now on reducing the ongoing costs associated with the complex manual processes that are required to compensate for identified weaknesses in internal controls over financial reporting in the US. While these control weaknesses have not reduced the quality of financial statements produced, they have necessitated significant additional cost.

Overall, the business remains on track to successfully conclude the programme during 2014, with expected costs unchanged from the guidance provided last year.

**Safety:** we continue to make improvements on last year, including decreases in OSHA recordable incidents, road traffic collisions and lost time incidents. Still, we have much to accomplish to



**Table of Contents**

<b>Strategic Report</b>	<b>Corporate Governance</b>	<b>Financial Statements</b>	<b>Additional Information</b>	<b>37</b>
-------------------------	-----------------------------	-----------------------------	-------------------------------	-----------

**Economic development:** we installed 15 miles of new electric circuit in Cape Ann, and reconfigured existing circuits to release additional capacity (more than \$15 million investment).

electricity efficiency and more than \$44 million in benefits from natural gas efficiency).

**National Grid US field operations crew leader Mark Harris.**

**New York**

**Infrastructure investment:** we invested \$1,008 million to enhance the resilience, efficiency and safety of our infrastructure \$471 million in electric and \$537 million in natural gas. In partnership with the New York City Department of Environmental Protection, we launched the Newtown Creek Renewable Gas Demonstration project in Brooklyn. As part of our commitment to sustainable energy solutions, Newtown Creek is the first project in the US that directly injects renewable gas into a local distribution system by converting effluent from a wastewater treatment plant into biogas.

**FERC**

**Clean Line energy investment:** Clean Line Energy Partners is developing several long-haul HVDC transmission lines to connect the best renewable energy resources to communities. Five projects are currently in development which span across states in the Midwest and Southwest US. We are an equity partner in these projects and the first utility to invest with Clean Line.

**DeepWater Wind:** the 30 MW DeepWater Offshore Wind Farm, located off the coast of Block Island, Rhode Island is in development and could become the first offshore wind farm in the US.

**Energy efficiency:** we are working with 13 institutions and 50 public and private companies within the Buffalo Niagara Medical Campus to enhance power quality and reliability, as well as address other energy and transportation challenges related to the expansion and development of the campus.

We are designing and constructing the approximately 20 mile submarine transmission cable from Narragansett, Rhode Island to Block Island, Rhode Island. The transmission cable will allow the energy generated by the wind farm to access the mainland Rhode Island customers and connect Block Island Power Company (BIPCo), which will become a new wholesale

**Gas expansion:** we completed the largest oil to natural gas conversion on Long Island, saving the Northport VA Hospital nearly \$3 million a year, displacing 1.5 million gallons of oil annually, and reducing carbon emissions by more than 5,000 tonnes a year.

**Economic development:** we provided the State University of New York at Canton (SUNY Canton) with a \$750,000 Renewable Energy and Economic Development incentive to help with the completion of an on-campus wind turbine project.

### Rhode Island

**Infrastructure investment:** we are planning to build the underground infrastructure to provide electricity to newly created land parcels following relocation of route I-195 in Providence (\$3 million investment).

**Energy efficiency:** Rhode Island energy efficiency programmes will result in savings of more than 1.6 million MWh of electricity and 4.37 million Dth of natural gas over the lifetime of installed measures. The resulting reduction in carbon emissions is equivalent to taking more than 186,700 motor vehicles off the road for one year.

customer of National Grid, to the mainland electric system. While the wind farm will provide Rhode Island customers with a sustainable source of generation, the transmission cable will allow BIPCo to reduce its dependence on diesel generation which will result in significantly lower energy prices and emissions for the residents of Block Island.

### Priorities for the year ahead

Deliver a step change in safety to ensure zero injuries

each day.

Develop our people and build their capabilities for

today and the future.

Put the customer first to meet all our obligations by

working towards process excellence and successfully

completing our US Foundation Program (USFP).

Drive regulatory performance through each

jurisdiction and lead the delivery of future energy

networks.

**Gas expansion:** the Rhode Island Public Utilities Commission (RIPUC) approved a \$3 million gas expansion pilot programme to be included in the FY2014 Gas Infrastructure, Safety and Reliability (ISR) Plan.

**Economic development:** energy efficiency programmes resulted in more than 540 full-time equivalent jobs and should generate economic benefits of more than \$237 million over the life of the installed measures (with more than \$190 million from

**Table of Contents****38 National Grid Annual Report and Accounts 2013/14****Principal operations**

continued

**Other activities****Grain LNG**

Grain LNG is one of three LNG importation facilities in the UK. It was constructed in three phases, becoming operational in 2005, 2008 and 2010 respectively. It operates under long-term contracts with customers and provides importation services, storage and send out capacity on to the national transmission system. We are exploring with customers a number of developments to the Grain site to enhance its revenue earning capability.

**Interconnectors**

The England-France interconnector is a 2,000 MW HVDC link between the French and British transmission systems with ownership shared between National Grid and Réseau de Transport d'Electricité (RTE). The interconnector is approximately 70 kilometres (43 miles) in length, with 45 kilometres

**UK Property**

National Grid Property is responsible in the UK for the management, clean-up and disposal of surplus sites, most of which are former gas works. During 2013/14 we have sold 45 sites, exchanged on several high-profile land disposal agreements with JV partners and embarked on a new programme of holder demolitions. We have been embedding our estate management outsourcing agreement with Capita and our new tender framework for the clean-up of contaminated land is progressing well.

3%

**Other activities  
adjusted operating  
profit of Group  
total**

**Xoserve**

Xoserve delivers transactional services on behalf of all the major gas network transportation companies in Great Britain, including National Grid. Xoserve is jointly owned by National Grid, as majority shareholder, and the other gas distribution network companies.

(27 miles) of subsea cable. Following a significant valve replacement programme, the availability of the interconnector continues to show marked improvement and the 2013/14 average was at 83.84%. A substantial proportion of the flow continues to be in the import direction, from France to Great Britain.

BritNed is a joint venture between National Grid and TenneT, the Dutch transmission system operator. It built, and now owns and operates a 1,000 MW subsea electricity link between the UK and the Netherlands, which is approximately 260 kilometres (162 miles) in length. BritNed, which entered commercial operations on 1 April 2011, is a merchant interconnector that sells its capacity via a range of explicit and implicit auction products.

## Metering

National Grid Metering (NGM) provides installation and maintenance services to energy suppliers in the regulated market in Great Britain. It maintains an asset base of around 15 million domestic, industrial and commercial meters.

Through Ofgem's Review of Metering Arrangements, National Grid has been appointed National Metering Manager (NMM) to facilitate the transition to smart metering in the domestic sector. To support this, NGM has also undertaken a pricing consultation to define the tariff caps to apply to traditional domestic gas metering. This took effect on 1 April 2014 and will last until the end of the transition to smart metering.

## US non-regulated businesses

Some of our US businesses are not subject to state or federal rate-making authority. These include interests in some of our LNG road transportation, some gas transmission pipelines and certain commercial services relating to solar installations, fuel cells and other new technologies.

## Corporate activities

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

In addition, NGM has been further developing its contracts and services in the industrial and commercial market.

NGM has achieved its highest customer satisfaction scores for the last six years for both its Domestic and Industrial & Commercial businesses.

**Table of Contents**

**Table of Contents**



**40 National Grid Annual Report and Accounts 2013/14**

**People**

*If we are to achieve our strategic goals, we need to make sure our employees have the right skills and capabilities.*

During 2013/14 we have focused particularly on the areas that we believe can generate the most value for the Company through our people – both now and in the future.

real work experience and leadership training for qualified

graduates in engineering and business disciplines; and

This has involved a focus on future leaders, operational leaders, engineers and stakeholder relationship managers. In addition to increasing our capability across these groups we also need to make sure we have enough people in each group. We will also be developing plans to improve our succession planning for our operational leader, engineer and stakeholder relationship manager roles.

summer internships – providing six to eight week opportunities

for college students to gain work experience with us.

**Building skills and expertise**

As we continue working under RIIO in the UK and become increasingly focused on driving performance on both sides of the Atlantic, we have identified three main business capabilities we need to develop among our workforce to support us in achieving our strategic objectives: performance excellence; customer and stakeholder management; and contract management.

**Safeguarding the future**

In the UK, around 89,000 people are needed annually to meet demand in the UK’s engineering sector over the next decade, yet only around 51,000 are joining the profession each year.

To address this shortage, we are running or are involved with a number of programmes and initiatives aimed at encouraging young people to study STEM subjects. These include:



We believe that by focusing on these capabilities we will make sure we meet our customers' and stakeholders' expectations while building a systematic approach to improving performance.

To help us do this, we have brought all our learning and development resources together under our Academy.

To date, 110 of our senior leaders in the UK have attended our performance excellence senior leadership programme through our Academy and similar programmes have started in the US.

### Attracting the best people

We are involved in a number of initiatives to help attract new talent into our organisation and industry. In the UK, these include:

working with the energy sector towards delivering 11,000 new

apprenticeships and traineeships over the next three years through

the Energy & Efficiency Industrial Partnership;

developing our own people through Advanced Apprenticeships

and engineer training;

supporting power systems undergraduate bursaries through the

Power Academy; and

making sure our graduates continue their development throughout

School Power, which provides classroom resources,

including a dedicated website, to support the teaching of STEM

subjects;

work experience, offering year 10 students a week-long

residential course at our Eakring Academy (totalling 100 each

year); and

open house visits to our sites to give students and teachers an

insight into gas and electricity systems, as well as future energy

challenges.

We are leading a consortium of businesses to create an exhibition called 'That Could Be Me' at the Science Museum in London, which will provide insight into engineering as a career. It is due to launch in December 2014.

A further initiative, called 'Careers Lab', aims to help establish a coordinated approach towards businesses taking responsibility for the skills agenda. The pilot scheme, which began in January 2014, involves businesses and schools in the Midlands working together to progress careers advice programmes for young people.

In the US, overall engineering employment is expected to grow by 11% through to 2018, varying by speciality. By 2018, STEM occupations will account for about 1.1 million new jobs and 1.3 million replacement positions due to STEM

their career with us.

workers leaving the workforce.

Initiatives in the US include:

energy utility technology certificate programmes  
partnerships

with seven local community colleges to develop and  
prepare

students to become future electric line workers;

Troops to Energy Jobs a programme designed to  
help veterans

determine how their military skills and experience  
translate into the

skills we are looking for;

We are working with high schools and community colleges to build a curriculum that meets future workforce needs and supporting STEM education at K-12 levels. An example of this is the National Grid Engineering Pipeline Program a six year developmental journey designed to inspire young people to pursue an education and career in engineering. To date 164 young people have entered into the programme.

We also work closely with the National Centre for Energy Workforce Development on its energy industry fundamentals curriculum and competency models.

**Table of Contents**

<b>Strategic Report</b>	<b>Corporate Governance</b>	<b>Financial Statements</b>	<b>Additional Information</b>	<b>41</b>
-------------------------	-----------------------------	-----------------------------	-------------------------------	-----------

**Volunteering**

Our employees continue to support our local communities, sharing their time and expertise on a range of skills-based volunteering and fundraising activities. This year in the UK we continued supporting Special Olympics GB by sponsoring the National Summer Games, launched our first-ever employee chosen charity partnership with Macmillan Cancer Support and joined forces with two initiatives – Step up to Serve and TeachFirst.

In the US, our Power to Serve programme is evolving as we focus on volunteering efforts that make National Grid a great place to work, and our communities great places to live. Power to Serve supports our Elevate 2015 Stewardship principle and seeks to acknowledge existing community service, as well as to create new volunteer opportunities for employees.

**Health and wellbeing**

Our health and wellbeing programmes for 2013/14 have included encouraging employees to improve their levels of activity and quality of nutrition, as well as supporting employees' mental wellbeing and musculoskeletal conditions. With our major cancer charities (Macmillan Cancer Support in the UK and The American Cancer Society in the US) we have raised money and awareness. Our employee opinion survey results continue to show that employees have a growing awareness of our wellbeing programmes.

**Promoting an inclusive and diverse workforce**

## Edgar Filing: NATIONAL GRID PLC - Form 20-F

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

During 2013/14, Race for Opportunity and Opportunity Now each awarded us with their Gold standard and recognised us as one of the top 10 private sector employers in terms of their benchmark criteria. We were also once again selected as one of the Times Top 50 Employers for Women.

In the US, we have focused on boosting membership and awareness of our Employee Resource Groups, which have measurable goals that are in line with our vision and Elevate 2015 ambitions.

These groups aim to build awareness and understanding of inclusion and diversity throughout the organisation. Their activities include programmes designed to build skills that help manage differences.

The table below shows the breakdown by gender at different levels of the organisation. We have included information relating to subsidiary directors, as this is required by the Companies Act 2006 (Strategic Report and Directors Reports) Regulations 2013. We define senior management as those managers who are at levels Executive 1 and Executive 2, as well as those who are directors of subsidiaries or who have responsibility for planning, directing or controlling the activities of the Company, or a strategically significant part of the Company, and are employees of the Company.

### Financial year ended 31 March 2014

	Male	Female	Total	% male	% female
Our Board	9	4	13	69.2	30.8
Senior management	182	56	238	76.5	23.5
	18,387	5,522	23,909	76.9	23.1
Whole company					

## Human rights

National Grid does not have a specific policy relating to human rights, but respect for human rights is incorporated into our employment practices and our values, which include respecting others and valuing diversity.

Doing the Right Thing is our guide to ethical business conduct. The way in which we conduct ourselves allows us to build trust with the people we work with. We earn this trust by doing things in the right way, building our reputation as an ethical company that our stakeholders want to do business with, and that our employees want to work for.

Our procurement policies integrate sustainability into the way we do business throughout our supply chain, so that we create value, preserve natural resources and respect the interests of the communities we serve and from which we procure goods and services. Additionally, through our supplier code of conduct, we expect our suppliers to keep to all laws relating to their business, as well as the principles of the United Nations Global Compact, the United Nations Declaration of Human Rights and the International Labour Organization (ILO).

The Strategic Report was approved by the Board of Directors on 18 May 2014 and signed on its behalf by:

**Alison Kay**

Group General Counsel & Company Secretary  
18 May 2014

## Non-financial KPIs

pages 10 – 11

## Board diversity

page 56

## Table of Contents



**Table of Contents**

42	National Grid Annual Report and Accounts 2015
----	---

Corporate Governance	
Contents	
44	<a href="#"><u>Governance framework</u></a>
44	<a href="#"><u>Our Board</u></a>
44	<a href="#"><u>Board composition</u></a>
45	<a href="#"><u>Director induction and development</u></a>
45	<a href="#"><u>Investor engagement</u></a>
46	<a href="#"><u>Board and committee evaluation</u></a>
46	<a href="#"><u>Non-executive Director independence</u></a>
46	<a href="#"><u>Director performance</u></a>
48	<a href="#"><u>How our Board operates</u></a>
48	<a href="#"><u>Our Board and its committees</u></a>
49	<a href="#"><u>Audit Committee</u></a>
53	<a href="#"><u>Finance Committee</u></a>
54	<a href="#"><u>Safety, Environment and Health Committee</u></a>
55	<a href="#"><u>Nominations Committee</u></a>
56	<a href="#"><u>Board diversity and the Davies Review</u></a>
56	<a href="#"><u>Executive Committee</u></a>

**Chairman's foreword**

An effective Board is vital to the sound foundations of good corporate governance. Our Board has undergone a significant change over the last three years to refresh membership and replace long-serving Non-executive Directors. As part of this planned transition, this year we have welcomed Therese Esperdy and John Pettigrew to our Board and, following the AGM, Maria Richter will be stepping down from the Board. We will also be saying goodbye to Nick Winsor, who will not be standing for re-election to the Board at the AGM, but will continue in his role as President of ENTSO-E and Chairman of NGET and NGG until July 2015 when he will be leaving the Company.

57 Management committees

58 Remuneration Report


Through the progressive refresh of the Board we have successfully renewed the membership and key roles to bring a diverse range of skills and experience to our Board. I am pleased to report that the results of the Board evaluation this year were positive, showing that our regenerated Board is functioning well, although there is always room for improvement. See page 46 for examples of the actions we have identified for the coming year.

All our new Board members undertake a thorough induction programme to get them up to speed on our businesses. The induction programme is tailored to the new Director to take account of previous experience and their specific role on the Board. I am confident that the programmes designed for Therese and John, which are detailed on page 45, will provide a good basis to enable them both to make a valuable early contribution to our Board.

As a Board we continue to support constructive challenge, encourage robust debate and recognise the value of different thinking styles. During the year we held a development session for the Board on thinking styles , see page 45 for details.

It is my strong belief that our ongoing emphasis on a positive and collegiate boardroom environment is helping the dynamics of the relationship between our Executive and Non-executive Directors. Because of this, we are able to increase the individual contribution of Directors and use their diverse backgrounds and expertise in enriching the quality of boardroom debates and discussions.





The behaviours and dynamics of the Board will be an ongoing focus for us as we strive to continually improve our effectiveness and performance.

**Sir Peter Gershon**

Chairman

**Table of Contents**

Strategic Report	<b>Corporate Governance</b>	Financial Statements	Additional Information	43

**Our**

**Board**

**Table of Contents**



**44 National Grid Annual Report and Accounts 2013/14**

**Corporate**

**Governance**

continued

**Governance framework**

long-term success of the Company and deliver sustainable shareholder value.

**Compliance statement**

The Board considers that it complied in full with the provisions of the UK Corporate Governance Code 2012 (the Code) during the financial year being reported, see page 51 for our explanation in relation to external audit tendering.

The Board sets the risk appetite for the Company and takes the lead in areas such as safeguarding the reputation of the Company and financial policy, as well as making sure we maintain a sound system of internal control (see page 25).

The Board as a whole is responsible for making sure that there is satisfactory dialogue with shareholders. Further details of our investor engagement activities are set out opposite.

This report explains the main features of the Company's governance structure to give a greater understanding of how the main principles of the Code have been applied. The report also includes items required by the Disclosure and Transparency Rules. The index on page 57 sets out where to find each of the disclosures required in the Directors Report together with the Board's sign-off on the report.

The Board's full responsibilities are set out in the matters reserved for the Board, available on our website, together with other documentation relating to the Company's governance.

**Examples of Board focus during the year:**

### **Fair, balanced and understandable**

The Board received a paper on the governance arrangements that have been put in place to make sure that the Annual Report and Accounts meet the requirements of the Code.

The coordination and review of the Annual Report and Accounts follows a well-established and documented process, which is conducted in parallel with the formal audit process undertaken by the external auditors. The Board considered and endorsed the arrangements in place to enable it to confirm (see page 76) that the Annual Report and Accounts, taken as a whole, is fair, balanced and understandable.

### **Our Board**

Our Board is set out on the previous page, along with the age, committee membership, independence, and tenure of all members. Their full biographical details are set out on pages 171 to 173.

The Directors who were in place during the year are shown on page 48, together with details of Board meeting attendance. Committee membership during the year and attendance at meetings is set out in each of the individual committee reports later in this report. For further details about the Directors service contracts and letters of appointment, see page 65 of the Remuneration Report.

**Our Chairman** is responsible for the leadership and management of the Board and its governance. By promoting a culture of openness and debate, he facilitates the effective contribution of all Directors and helps maintain constructive relations between Executive and Non-executive

review of safety performance and initiatives following the previously reported fatality in April 2013;

half-day strategy session including discussions on technology developments and the differences between the UK, European and US markets, followed by further discussions about strategy at Board meetings;

risk workshop in support of the Board's oversight of corporate risk management;

updates on RIIO delivery and the UK business change programme;

US Foundation Program post systems implementation review and regular updates;

UK regulatory update, including future energy scenarios and EMR delivery plan;

update on the politics of UK energy, including the increased profile of the Company in the run-up to the next UK general election;

in-depth US operational update on topics central to the delivery of the US business strategy;

talent management update, including important elements of our strategy relating to people;

the results from the 2013 employee opinion survey and the associated action plan; and

progress against the actions arising from the 2012/13 Board and committee evaluation.

### **Examples of expected Board focus for next year:**

annual review of safety activities;

continued detailed review of strategy and financing;

risk appetite discussions;

Directors.

progress on the stabilisation of the new enterprise resource system and updates on the US Foundation Program;

**Our Chief Executive** is responsible for the executive leadership and day-to-day management of the Company, to ensure the delivery of the strategy agreed by the Board. Through his leadership of the Executive Committee, he demonstrates commitment to safety, operational and financial performance.

review of the business performance under RIIO;

outcome of the New York gas audit;

talent review and succession planning;

results and actions from the 2014 employee opinion survey; and

progress against the actions from the 2013/14 Board and committee evaluation.

**Our Senior Independent Director** acts as a sounding board for the Chairman and serves as an intermediary for the other Directors, as well as shareholders as required.

Independent of management, **our Non-executive Directors** bring diverse skills and experience, vital to constructive challenge and debate. Exclusively, they form the Audit, Nominations and Remuneration Committees, and have an important role in developing proposals on strategy.

### **Board composition**

The successful delivery of our strategy depends upon attracting and retaining the right talent. This starts with having a high-quality Board. Balance is an important requirement for the composition of the Board, not only in terms of the number of Executive and Non-executive Directors, but also in terms of the range of expertise and backgrounds.

### **Role of our Board**

Our Board is collectively responsible for the effective oversight of the Company and its businesses. It also determines the strategic direction and governance structure that will help achieve the

While traditional diversity criteria such as gender and ethnicity are important, we also value diversity of skills, experience and knowledge. You can read about our Board diversity policy in the Nominations Committee report on page 55.

**Table of Contents**

Strategic Report	<b>Corporate Governance</b>	Financial Statements	Additional Information	45
------------------	-----------------------------	----------------------	------------------------	----

The planned transition of the Board has continued over the year; Therese Esperdy joined as a Non-executive Director on 18 March 2014, John Pettigrew joined as an Executive Director on 1 April 2014, and Maria Richter will step down from the Board following the conclusion of the AGM in July. Nick Winser will also step down from the Board at this time.

**Director induction and development**

As our internal and external business environment changes, it is important to make sure that Directors skills and knowledge are refreshed and updated regularly. Our Chairman is responsible for the ongoing development of all Directors.

To strengthen the Directors knowledge and understanding of the Company, Board meetings regularly include updates and briefings on specific aspects of the Company s activities. In September, the Board received a presentation on accounting under RIIO and the introduction of new terminology in our external financial reporting.

Updates on corporate governance and regulatory matters are also provided at Board meetings, with

with timely and appropriate information on our strategy, performance, objectives, financing and other developments.

**Institutional investors**

We carry out a comprehensive engagement programme for institutional investors and research analysts, including meetings, presentations, webinars and attendance at investor conferences. The programme provides the opportunity for our current and potential investors to meet with executive and operational management.

In the past year, our engagement programme has focused on educating investors on how we intend to perform under the new RIIO price controls in the UK. In August we held a seminar in London to set out the details of the new regulatory regime. We explained how we have changed the way we operate to position us to deliver outperformance in the new regulatory environment.

We have also attended investor conferences across the UK and US, and held road shows in major investor centres across Europe, the US and Asia Pacific.

details of development and training opportunities for Directors available in our online document library.

Additionally, the Non-executive Directors are expected to visit at least one operational site annually. This provides the opportunity to meet local management teams and discuss aspects of the business with employees.

With the agreement of the Board, Executive Directors gain experience of other companies operations, governance frameworks and boardroom dynamics through non-executive appointments. The fees for these positions are retained by the individual. See page 65 for more details.

In February we held a thinking styles session supported by an external consultant. In advance of the session the Board completed questionnaires to assess its capability to think in diverse ways and the aggregated results were shared at the session. The session also covered the benefits of thinking styles for different types of discussion and ways in which the diverse capability that exists within the Board could be harnessed to maximise its effectiveness.

### **Directors induction programme**

Following Therese and John's appointment to the Board, the Chairman and Group General Counsel & Company Secretary have arranged a comprehensive induction programme. The programme has been tailored based on their experience and background and the requirements of their roles.

In addition to these engagement activities, we held our first stewardship meeting in May last year. The event had a governance theme and provided major investors with an insight into our decision-making processes, the work of our committees and the workings of the new regulatory regimes in the UK and US. The event also provided the opportunity for attendees to ask questions and meet members of the Board and for our newer Non-executive Directors to understand our shareholders' views and concerns. A copy of the presentation is available in the Investors section of our website.

As a result of its success last year, we are planning to hold a similar event this year.

Sir Peter also contacts our major shareholders following the release of our full-year results to offer them the opportunity to meet him, the Senior Independent Director, or any of our other Non-executive Directors, so they can discuss any issues they feel unable to raise with members of the executive team.

The Board receives regular feedback on investor perceptions and opinions about the Company. Specialist advisors, our brokers and the Director of Investor Relations provide updates on market sentiment. Each year, the Board also receives the results of an independent audit of investor perceptions.

### **Debt investors**

Over the last year representatives from our treasury team, together with other senior managers from across the business, have met with debt investors in Europe and the US to discuss topics such as the RIIO price controls.

For both Therese and John a one-to-one meeting was arranged with our external legal advisors to discuss the duties and requirements of being a listed company director. Therese's induction has also included one-to-one meetings with her fellow Directors and senior management in the UK. Over the coming months she will meet senior management in the US and undertake operational site visits.

Acknowledging John's in-depth understanding of the UK and US businesses, his induction has focused primarily on his role as a Director and the role of the Board in general.

### **Investor engagement**

We believe it is important to maintain effective channels of communication with our debt and equity institutional investors and individual shareholders. This helps us to understand their views about the Company and allows us to make sure they are provided

Additionally this year, an independent review of debt investor perceptions of the Company was conducted and the results were presented to the Finance Committee.

With the total debt issued during the year at £1.1 billion, it is important for us to explain to debt investors why this money is required and what protections are in place to safeguard their potential investment.

We also communicate with our debt investors through regular Company announcements and the debt investor section of our website. This contains bond prospectuses, credit ratings, materials relating to the retail bond issued in 2011 and subsidiary year-end reports. The website also contains information about our long-term debt maturity profile, so investors can see our future refinancing needs.



**Table of Contents**



**46 National Grid Annual Report and Accounts 2013/14**

**Corporate**

**Governance**

continued

**Individual shareholders**

Engagement with individual shareholders, who represent more than 95% of the total number of shareholders on our share register, is led by the Group General Counsel & Company Secretary. Shareholders are invited to learn more about the Company through the exhibits at our AGM and the shareholder networking programme.

The shareholder networking programme normally takes place twice a year and includes visits to UK operational sites and presentations by senior managers and employees over two days. If you are a UK resident shareholder and would like to take part, please apply online via the Investors section on our website.

**Annual General Meeting**

Our AGM will be held on Monday 28 July 2014 at The International Convention Centre in Birmingham and broadcast via our website. The Notice of Meeting for the 2014 AGM, available on

**Effectiveness of the Board** actions to improve Board effectiveness were proposed, for example: continue to improve the quality of Board papers; make sure in-depth items for Board consideration highlight the important issues to be discussed; and encourage reporting from management that incorporates more input from the Executive Directors.

**Responsibility: Chairman, Chief Executive and Group General Counsel & Company Secretary, as appropriate**

The actions from last year's externally conducted review were grouped into three themes mechanics, dynamics and specifics. Progress against the actions agreed by the Board has been monitored through the year and a commentary against each action is set out opposite.

An evaluation of committee performance was also conducted by the chairman of each of the Board committees, as well as the Executive Committee. Each committee concluded that it had operated

our website, sets out in full the resolutions for consideration by shareholders, together with explanatory notes and further information on the Directors standing for election and re-election.

### **Board and committee evaluation**

Following last year's external review, this year the Board felt it was appropriate to conduct an internal Board and committee evaluation.

The review of the Board was led by Sir Peter. Rather than using structured questionnaires, he asked a number of open questions at one-to-one interviews with each of the Directors in December and January.

The questions were designed to encourage broad discussions on the performance and effectiveness of the Board rather than to assess its procedures. The questions covered areas such as decision making, the quality of Board discussions, the degree of challenge from the Board members, the top concerns of each member and any topics they felt needed additional focus. The discussions also covered the balance between the Board and its committees and the effectiveness of the Board.

The feedback from these meetings formed the basis of the evaluation report from Sir Peter. The findings were presented by Sir Peter to the Nominations Committee in February and then to the Board meeting in March, along with a proposed action plan. The balance between the Board and its committees was felt to be appropriate and no changes in this area were identified. The Board agreed a number of actions for the forthcoming year, as set out below. Progress against these actions will be monitored throughout the year by the Board.

effectively throughout the year and agreed, where relevant, an action plan to further improve performance. Progress against the action plans will be monitored through the year by the respective committee and the Board.

### **Non-executive Director independence**

The independence of the Non-executive Directors is considered at least annually, along with their character, judgement, commitment and performance on the Board and relevant committees. The Board took into consideration the Code and indicators of potential non-independence, including length of service. A particularly rigorous review was conducted of Maria Richter as she has served for more than six years.

At year-end, all the Non-executive Directors, with the exception of the Chairman, have been determined by the Board to be independent. Tenure is just one indicator of potential non-independence and the experience and knowledge of Maria Richter, who has served on the Board for more than nine years, has been important in facilitating a structured handover and providing continuity during the search for Therese. Maria will not be standing for re-election at the 2014 AGM.

### **Director performance**

At a private meeting of the Non-executive Directors, Mark Williamson, as Senior Independent Director, led a review of Sir Peter's performance. The review noted that Sir Peter's commitments had changed during the year following his appointment as non-executive chairman of the Aircraft Carrier Alliance. The time commitment of the new role was carefully considered by the Board and was unanimously approved by the Board prior to Sir Peter accepting the position.

**Decision making** all important matters requiring approval are to be brought to the Board for early input before a decision is needed.

**Responsibility: Chairman and Chief Executive**

**Board discussions** greater clarity about the scope of Board discussions to be provided in advance and Board members to be encouraged to question if not clear.

**Responsibility: Chairman**

**Degree of challenge** the Executive Directors to speak to the Chairman about what would make them feel more comfortable to challenge and debate, both with the Non-executive Directors and with their fellow Executive Directors at Board meetings.

**Responsibility: Executive Directors**

**Board focus** a number of topics were identified that Directors felt needed additional focus by the Board at its meetings, for example cyber risk and the UK political landscape. Ways to improve the focus on each of these were discussed at the March Board meeting and specific actions were agreed and allocated to various Board members.

**Responsibility: various Board members**

The Non-executive Directors, with input from the Executive Directors, assessed his ability to fulfil his role as Chairman and the arrangements he has in place to fulfil his role, given he is also chairman of a FTSE 250 company. They concluded that Sir Peter's performance and contribution were first-class and that he demonstrated strong leadership.

The performance of each Director was raised by Sir Peter at his one-to-one meetings conducted for the Board and committee evaluation process.

Following recommendations from the Nominations Committee, the Board considers all Directors continue to be effective, committed to their roles and have sufficient time available to perform their duties. Therefore, in accordance with the Code, all Directors, with the exception of Maria Richter and Nick Winser who will be stepping down from the Board following the conclusion of the AGM, will seek election or re-election at the 2014 AGM as set out in the Notice of Meeting.

**Table of Contents**

Strategic Report	<b>Corporate Governance</b>	Financial Statements	Additional Information	47
------------------	-----------------------------	----------------------	------------------------	----

Area	Actions from last year's review	Commentary
<b>Mechanics</b>	<p>Chief Executive to meet with Executive Directors immediately after each Board meeting to discuss how the Board operated as a team and contributions from Directors, and reflect on any learning. Feedback from these meetings to be shared as appropriate with the Chairman.</p> <p><b>Responsibility: Chief Executive</b></p>	<p>This was implemented from January 2013 and will be continued as it has proved helpful in making sure that the right discussions are had at Board meetings.</p>
	<p>Review and build on the one page executive summary for non-standard papers introduced in July 2012 and consider its effectiveness in providing the Board with key information and clarity around requested contribution or action.</p> <p><b>Responsibility: Chairman and Chief Executive</b></p>	<p>An updated template summary sheet was introduced in September 2013. The revised template includes details of links to the risk register, financial impact and additional information on the lead presenter.</p>

All committees, except the Nominations Committee and Executive Committee, to get together immediately before or after their meetings to discuss papers, presenters contribution and any matters they wish to consider without management present.

This initiative has been implemented and meetings included on the forward business schedules as appropriate by each of the committees.

**Responsibility: Committee chairmen**

Thinking styles of candidates to the Board and Executive Committee to be taken into consideration once skills set and experience confirmed.

Diversity of thinking styles was a factor in the recruitment process for a successor to Maria Richter and in the appointment of John Pettigrew.

**Responsibility: Nominations Committee**

**Dynamics**

Schedule a development session for the Board which may include thinking styles, inclusive leadership and exploring positive challenge through questioning techniques.

A thinking styles session for the Board was held in February 2014. See page 45 for more information.

**Responsibility: Chairman and Group General Counsel & Company Secretary**

Review the following month's agenda and communicate to the Executive Directors the areas that presenters are to focus on.

The draft agenda for forthcoming Board meetings are noted by the Executive Committee. The Chairman also holds separate pre-Board meetings with the Chief Executive and the Group General Counsel & Company Secretary to discuss and review the business of the next meeting.

**Responsibility: Chairman and Chief Executive**

**Specifics**

Facilitate increased interaction between Non-executive Directors and high-potential employees during site visits and presentations at Board meetings.

High-potential employees have been invited to Board dinners in the UK and US. A schedule of proposed site visits has been provided to the Non-executive Directors.

**Responsibility: Executive Directors**

Appoint a taskforce to review gender diversity and employee turnover.

Following a detailed review in August 2013 by the Chairman and Chief Executive it was decided not to proceed with the taskforce at that time. Good progress continues to be made on gender diversity and employee turnover.

**Responsibility: Chief Executive**

Implement an inclusion and diversity scorecard and review progress with the Board.

The Executive Committee receives a quarterly inclusion and diversity scorecard and updates are provided to the Board. An inclusion and diversity session for the Board was held in April 2013.

**Responsibility: Executive Committee**

**Table of Contents**



**48 National Grid Annual Report and Accounts 2013/14**

**Corporate**

**Governance**

continued

**How our Board operates**

The Chairman sets the Board's agenda in line with its responsibilities and role as set out in the matters reserved for the Board, and the main challenges and opportunities facing the Company, making sure adequate time is available to discuss all items, including strategic issues.

To support discussion and decision making, Board and committee members receive papers sufficiently in advance of meetings so that they can prepare for and consider agenda items. Additionally, the Chairman holds a short meeting with the Non-executive Directors before and after each Board meeting to discuss the focus of the upcoming meeting and afterwards to share feedback and discuss any outstanding matters.

A one-page executive summary for non-standard papers provides information and clarity around

Instances of non-attendance during the year at Board and committee meetings were determined to be reasonable due to the individual circumstances.

Should any Director not be able to attend a Board or committee meeting, the Chairman and committee chairman are informed and the absent Director is requested to communicate opinions and comments on the matters to be considered.

**Our Board and its committees**

The Board delegates authority to its committees to carry out certain tasks on its behalf, so that it can operate efficiently and give the right level of attention and consideration to relevant matters.

The role and responsibilities of the committees are set out in their terms of reference, available on our website. The committee structure and delegation

the contribution or action required. Where appropriate, subject matter experts give presentations and provide the opportunity for Directors to ask questions.

and reporting lines are set out in the diagram below.

### Board membership and attendance

Board membership and attendance at meetings are set out below. Attendance is expressed as the number of meetings attended out of the number possible or applicable for the individual Director during the year to 31 March 2014. Committee membership during the year and attendance at meetings is set out in each of the individual committee reports later in this report.

In addition to the vertical lines of responsibility and reporting, the committees communicate and work together where required. For example, on some risk matters the Safety, Environment and Health (SEH) Committee collaborates with the Audit Committee. These lines of communication are shown in the diagram below.

Committee agendas and schedules of items to be discussed at future meetings are prepared in line with the terms of reference of each committee.

Name	Attendance
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Sir Peter Gershon	11 of 11
Steve Holliday	10 of 11
Andrew Bonfield	11 of 11
Tom King	11 of 11
John Pettigrew <sup>1</sup>	0 of 0
Nick Winser	10 of 11
Phillip Aiken	11 of 11
Nora Mead Brownell	10 of 11
Jonathan Dawson	11 of 11
Therese Esperdy <sup>2</sup>	1 of 1
Paul Golby	11 of 11
Ruth Kelly	11 of 11
Maria Richter	11 of 11
Mark Williamson	11 of 11

At committee meetings, items are discussed and, as appropriate, matters are endorsed, approved or recommended to the Board by the committee. The chairman of each committee provides the Board with a summary of the main decisions and discussion points so the non-committee members are kept up to date.

Below the Board committees are a number of management committees, including the Executive Committee.

The Executive Committee has responsibility for making management and operational decisions about the day-to-day running of the Company. Further information on some of the management committees, including the membership and operation of the Executive Committee, is set out on pages 56 and 57.

	3 of 4
Ken Harvey <sup>3</sup>	

Reports from each of the Board committees together with details of their activities during the year, are set out on the following pages.

George Rose <sup>3</sup>	4 of 4
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1. John Pettigrew was appointed to the Board with effect from 1 April 2014.

2. Therese Esperdy was appointed to the Board with effect from 18 March 2014.

3. George Rose and Ken Harvey stepped down from the Board with effect from 29 July 2013.

**Table of Contents**

Strategic Report	<b>Corporate Governance</b>	Financial Statements	Additional Information	49
------------------	-----------------------------	----------------------	------------------------	----

**Audit Committee**

**Significant issues**

Some of the significant issues the Audit Committee considered in relation to the financial statements during the year set out below are explained in more detail later in the report:

**Role**

Oversees the Company’s financial reporting, and internal controls and their effectiveness, together with the procedures for identifying, assessing and reporting risks. It also oversees the services provided by the external auditors and their remuneration.

- US financial controls program;
- LIPA MSA transition contract accounting;
- presentation of exceptional items; and
- fair, balanced and understandable assessment.

**Review of the year**

My first eight months as chairman have been busy but enjoyable. Last July we said goodbye to George Rose and this July Maria Richter will be stepping down from the Board. I would like to thank them both for their contribution to the Committee. In particular to George for his guidance and support during his handover to me.

As a committee we have held six meetings during the year, two of which were held in the US, providing all members with the

**Other matters reviewed**

Examples of other matters the Audit Committee reviewed:

- accounting for RIIO;
- the enhanced disclosures required by International Auditing Standard (UK and Ireland) 700;
- the Company’s refreshed approach to going concern following the publication of the Sharman Report;

opportunity to meet our US teams. Following last year's committee performance evaluation, we now also meet privately after some of our longer meetings. We use this time to review the meeting and discuss how we can evolve and make our meetings more effective.

The Committee's main focus has been the US finance function and ongoing improvement of the new enterprise resource system. The Committee has received regular reports throughout the year from the Finance Director and US Chief Financial Officer.

The UK finance team has provided valuable support to the US team and I visited the US with the Finance Director and Group Financial Controller in January to review progress and priorities for 2014. The work on stabilisation of the systems also coincided with the LIPA MSA transition. This was an important milestone in the overall US financial control program.

With the start of RIIO, the Committee received a paper from the UK finance team on the accounting implications of this new arrangement and its impact on the financial control environment. We also reviewed the disclosures within this Annual Report to ensure they provide a fair, balanced and understandable view in the context of current accounting standards.

Next year is also looking busy with an ongoing focus on the enterprise resource system and continual improvement in processes and controls around these systems.

the increased work involved to support the LIPA MSA transition;

the revised Certificate of Assurance process;

Sarbanes-Oxley Act 2002 testing and attestations;

external reporting obligations and the programme to improve the Company-wide framework;

a revised ethical business conduct process for Directors and executive members; and

a proposed revised approach to risk reporting.

### Committee membership and attendance

Committee membership during the year and attendance at meetings is set out below. Attendance is expressed as the number of meetings attended out of the number possible or applicable for the individual Director during the year to 31 March 2014. Biographical details and experience of Committee members are set out on pages 171 to 173.

Name	Attendance
Mark Williamson (chairman) <sup>1</sup>	6 of 6
Philip Aiken	5 of 6
Ruth Kelly	6 of 6
Maria Richter	6 of 6
George Rose <sup>2</sup>	2 of 2

**Mark Williamson**

Committee chairman

1. Chairman from July 2013.

2. George Rose stepped down from the Board with effect from 29 July 2013.

**Experience**

Mark Williamson took over as chairman of the Audit Committee following the 2013 AGM. The Board has determined that Mark:

has recent and relevant financial experience;

is a suitably qualified audit committee financial expert within the meaning of the SEC requirements; and

is independent within the meaning of the New York Stock Exchange listing rules.

**Table of Contents**



**50 National Grid Annual Report and Accounts 2013/14**

**Corporate**

**Governance**

continued

**Financial reporting**

The Committee monitors the integrity of the Company’s financial information and other formal documents relating to its financial performance. It makes appropriate recommendations to the Board before publication.

An important factor in the integrity of financial statements is making sure that suitable and compliant accounting policies are adopted and applied consistently on a year-on-year basis and across the Company. In this respect, the Committee also considered the estimates and judgements made by management when accounting for non-standard transactions, the treatment of exceptional items and in provision calculations.

These considerations are supported by input from other assurance providers such as the group controls, risk management and ethics and compliance teams, business separation compliance officer, internal (corporate) audit and the SEH

professionals, as well as to provide a new enterprise resource system to LIPA.

The Committee reviewed the accounting treatment of costs incurred as part of the transition and agreed that the judgements made by management were reasonable.

**Presentation of exceptional items:** at the half year and year end, the Committee discussed and challenged a detailed analysis of items to be classified as exceptional to make sure the items did not include income or costs relating to the underlying business.

In particular, the Committee considered the treatment of the provision at the half year for gas holder demolition, as well as LIPA MSA transition and pension costs (described above). The Committee agreed that the classification of these items is appropriate.

Committee, as well as our external auditors. In addition, the Committee also considers reports of the Disclosure Committee. See page 57 for more information.

The Committee reviews and approves the external audit plan annually (see Audit quality below) and, as part of this, considers the significant risks upon which the external auditors will focus their year-end audit. The independent auditors' report (pages 77 to 80) highlights these risks, some of which led to significant issues that the Committee discussed during the year. These were:

US financial controls program (including quality of reconciliation

process, US plant accounting and user access controls);

LIPA MSA transition contract accounting; and  
presentation of exceptional items.

Other risks, including the accuracy and valuation of treasury derivative transactions, and management override of internal control, were not considered in detail by the Committee during the year as nothing significant arose that warranted Committee attention.

Summarised below are the issues that attracted the most focus, and time, of the Committee in relation to the financial statements during the year.

**US financial controls program:** the primary focus of the Committee during the year has been the work to make sure of the integrity of the new financial system in the US. This included the measures taken to remediate US financial control deficiencies and those highlighted as a result of the

**Fair, balanced and understandable assessment:** the Committee has considered the requirement of the Code to ensure that the Annual Report and Accounts, taken as a whole, is fair, balanced and understandable .

In reaching this conclusion the Committee reviewed, among other things, the impact of the introduction of the RIIO price control regime in the UK on the Group's IFRS reported results, see pages 08 and 09 for more information.

### **Confidential reporting procedures and whistleblowing**

The integrity of the financial statements is further supported by the confidential reporting and whistleblowing procedures we have in place. The Committee reviews these procedures once a year to make sure that complaints are treated confidentially and that a proportionate, independent investigation is carried out in all cases.

### **Internal (Corporate) Audit**

The Corporate Audit function provides independent, objective assurance to the Audit, SEH and Executive Committees.

Audit work is delivered by a combination of internal resources – employees who typically have either a finance or operational business background – and external sources, where specific specialist skills are required.

The audit plan contains a mix of risk-based and cyclical reviews together with a small amount of work that is mandated, typically by US regulators.

implementation of the new enterprise resource system.

A number of focus areas are identified, such as financial, regulatory and asset management processes. Appropriate coverage is provided across each of these areas.

Over the course of the year, the Committee requested and reviewed a number of reports in order to understand the detail of the issues. These issues include the timeliness and quality of certain balance sheet account reconciliations, and the process and systems to ensure appropriate capitalisation of labour costs.

Inputs to the plan include risk registers, corporate priorities, external research of emerging risks and trends and discussions with senior management. A tool that captures all auditable areas, prior coverage and inherent process risk is also used to inform of audits that should be undertaken on a cyclical basis.

The Committee has also challenged and reviewed management's remediation plans and the design of compensating controls, including enhanced analytical reviews to make sure the Company maintains an effective internal control environment over financial reporting.

The plan is reviewed and approved by the Audit Committee in March each year, with focus given to not only the areas which are being covered but also those that are not, so we can make sure that the plan aligns with the Committee's view of risk.

Given the significance of this work, Mark Williamson visited the US and held detailed meetings with senior management in January 2014 to confirm remediation plans were progressing as expected.

Corporate Audit provides a twice-yearly report to the Audit Committee. The report summarises common control themes arising and progress with implementing management action plans, and also presents information on specific audits as appropriate.

**LIPA MSA transition contract accounting:** on 31 December 2013, our US business moved the MSA with LIPA to a third party. This transition was particularly complex. It involved many areas of our US business and required us to manage the transition of more than 2,000 employees, including more than 40 finance

Where specific control issues are identified, senior leaders are invited to attend the Audit Committee to provide a commentary around the actions they are taking to improve the control environment within their area of responsibility.

**Table of Contents**

Strategic Report	<b>Corporate Governance</b>	Financial Statements	Additional Information	51
------------------	-----------------------------	----------------------	------------------------	----

**External audit**

The Committee is responsible for overseeing relations with the external auditors, including the approval of fees, and makes recommendations to the Board on their appointment and reappointment. Details of total remuneration to auditors for the year, including audit services, audit-related services and other non-audit services, can be found in note 3 (e) of the consolidated financial statements on page 98.

**Auditor independence and objectivity**

The independence of the external auditors is essential to the provision of an objective opinion on the true and fair view presented in the financial statements.

Auditor independence and objectivity is safeguarded by a number of control measures, including limiting the nature and value of non-audit services performed by the external auditors, ensuring that employees of the external auditors who have worked on the audit in the past two years are not appointed to senior financial positions within the Company, and the rotation of the lead engagement partner at least every five years. The current lead engagement partner has held the position for four years.

**Audit quality**

To maintain audit quality and provide comfort on the integrity of financial reporting, the Committee reviews and challenges the proposed external audit plan to make sure that PwC has identified all key risks and developed robust audit procedures.

The Committee also considers PwC’s response to accounting, financial control and audit issues as they arise, and meets with them at least annually without management present, providing the external auditors with the opportunity to raise any matters in confidence.

**Auditor appointment**

An annual review is conducted by the Committee of the level and constitution of the external audit and non-audit fees and the effectiveness, independence and objectivity of the external auditors.

The annual review includes consideration of:

- the external audit process globally;
- the auditors’ performance;



**Non-audit services provided by the external auditors**

Non-audit services provided by the external auditors require approval by the Committee. Approval is given on the basis the service will not compromise independence and is a natural extension of the audit or if there are overriding business or efficiency reasons making the external auditors most suited to provide the service. Certain services are prohibited from being performed by the external auditors, as required under the SOX Act.

Total non-audit services provided by PwC during the year ended 31 March 2014 were £1.7 million (2013: £2.3 million), which comprised 15% (2013: 23%) of total audit and audit-related fees.

Total audit and audit-related fees include the statutory fee and fees paid to PwC for other services that the external auditors are required to perform, for example regulatory audits and SOX Act attestation. Non-audit fees represent all other services provided by PwC not included in the above.

Significant non-audit services provided by PwC in the year included the review of US pensions and other post-retirement benefits census data (£0.5 million) and tax compliance services in territories other than the US (£0.5 million).

PwC were engaged to review census data used in US pensions and other post-retirement benefit calculations and advise on enhancements to procedures and controls surrounding census data completeness and accuracy.

The Committee considered PwC best placed to provide this service given their in-depth understanding of our processes and control

the expertise of the firm and our relationship with them; and

the results of questionnaires completed by National Grid

employees engaged with the audit and members of the

Audit Committee.

Following this year's annual review, the Committee is satisfied with the effectiveness, independence and objectivity of the external auditors, and recommends to the Board their reappointment for a further year. A resolution to reappoint PwC and giving authority to the Directors to determine their remuneration will be submitted to shareholders at the 2014 AGM.

**Audit tender**

PwC have been the Company's external auditors since the merger with Lattice Group plc in 2002, having been the incumbent external auditors of both the merging parties and the audit contract has not been put out to tender since then. Their performance has been reviewed annually by the Committee since that time.

During the year the Committee spent time discussing a potential tender for the external audit, following the new requirement on audit tendering and rotation of auditors.

The Committee has also discussed the implications of the proposals by both the UK Competition Commission (implementing its decision to mandate tendering every 10 years) and the EU (requiring audit firm rotation at least every 20 years), and will implement them when they become final. These proposals have effectively superseded the comply-or-explain provision that underpins the

environment. In order to maintain the external auditors' independence and objectivity, the work was performed by a team independent of the audit team, management reviewed and considered PwC's findings and PwC did not make any decisions on behalf of management. Additionally, PwC had no input in respect of the production of financial information subsequently used by the audit team.

The Committee also considered that tax compliance services were most efficiently provided by the external auditors, as much of the information used in preparing computations and returns is derived from audited financial information. In order to maintain the external auditors' independence and objectivity, management reviewed and considered PwC's findings and PwC did not make any decisions on behalf of management.

Code. The Financial Reporting Council has decided to defer consideration of whether to make any changes to these sections of the Code until its next review, currently scheduled for 2016.

The Committee considered the additional disruption that both an audit tender and any change in audit firm would involve in light of the ongoing US financial controls program, and the services we currently receive from other firms that may be considered in a tender process.

The Committee concluded that a tender is not in the Company's interests at this time but agreed that this issue would be reviewed annually as part of the auditor appointment process. No representatives from PwC were present during the Committee's discussion of the options for a tender of the external audit.

There are no contractual obligations restricting our choice of external auditors and we have not entered into any auditor liability agreement.

**Table of Contents****52 National Grid Annual Report and Accounts 2013/14****Corporate****Governance**

continued

**Audit information**

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

**Internal control, risk and compliance**

We regularly consider the effectiveness of financial reporting, internal controls and compliance with applicable legal and internal requirements. We also review the procedures for the identification, assessment, mitigation and reporting of risks.

To continuously improve and remain at best practice levels, the risk management team reviews risk process standards, emerging trends and concepts being driven by the main consultancy firms and seeks to apply these as appropriate. The standards

**Going concern**

Having made enquiries and reviewed management's assessment of the going concern assumption, the Directors have a reasonable expectation that the Group has adequate resources to continue in operational existence for the next financial year and the foreseeable future. For this reason, the Directors are satisfied that, at the time of approving the financial statements, it is appropriate to continue to adopt the going concern basis in preparing the consolidated and individual financial statements of the Company.

**Management's assessment process**

In accordance with the draft recommendations of the updated Financial Reporting Council guidance on going concern and liquidity risk, we have reviewed and amended our going concern assessment process.

Our process is an extension of our business planning process, and is further supplemented by our annual

issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO) and the international risk standard ISO 31000 continue to inform the principles of our risk management process.

Specific improvements delivered during the year, and ongoing, were noted by the Committee at its meeting in September. These improvements include an enhanced approach for risk reporting to the Executive Committee, focusing on giving better visibility of mitigations and their impact on how risks are scored.

The scope of risk discussions has also been widened to incorporate specific consideration of our treatment of and preparedness for emerging risks (uncertainties on the horizon that are still developing and so may or may not evolve into threats or opportunities for us) and potential black swan type events (catastrophic events of extremely high impact and extremely low likelihood).

The Board has participated in an interactive risk workshop to reinforce awareness of our key risks so its views can be captured and incorporated into our risk management activities. The output of this session formed part of the risk information reviewed at the March Audit Committee meeting.

Details of our internal control and risk management systems, including over the financial reporting process can be found on pages 22 and 25 and page 170. Our risk factors are described in full on pages 167 to 169.

### **Compliance management**

The Global Ethics and Compliance team has continued to focus on promoting improved consistency of reporting on control frameworks

budget and other liquidity risk management controls. Our five year business plan and one year budget were reviewed and approved by the Board at its meetings in September 2013 and March 2014 respectively. The Finance Committee provides ongoing oversight of our liquidity policy, which requires us to maintain sufficient liquidity for a rolling 12 month period.

In light of our refreshed approach, we have reconsidered what the most appropriate foreseeable future period is. Given our business model, current regulatory clarity and other factors affecting our operating environment, and the robustness of our business planning process and scenario analysis, we have concluded the foreseeable future period is the five years ending 31 March 2018, in line with our business plan. This period is considered to be the foreseeable future as required for this going concern assessment only, and is in accordance with company law, accounting standards and the Listing Rules. We will reassess this period annually in light of developments in our operating environment, business model and strategic priorities.

Our business plan considers the significant solvency and liquidity risks involved in delivering our business model in light of our strategic priorities. The business plan models a number of upside and downside scenarios, derived from the risks and opportunities identified, and determines the impact these would have on our results and financial position over the five year period. In addition, we have reviewed and challenged a number of worst case scenarios and their possible remediation.

Our business model calls for significant capital investment to maintain and expand our network infrastructure. To deliver this, our business plan highlights that we will need to access capital markets to raise additional funds from time to time. We have a long and successful history in this regard; however, our business plan also models various KPIs used by lenders and credit rating agencies in assessing a company's credit worthiness.

across the compliance reporting process. The aim of this activity is to make sure any problem areas are transparent and that all parts of the business are applying a similar standard.

The Committee asked for a review of the key compliance areas that are subject to the reporting process. Currently, reporting focuses on legal compliance obligations only, and consideration is being given to whether all key areas are covered and what, if any, other areas should be included. The Committee also received the annual reports on the Company's anti-bribery procedures and whistleblowing procedures and reviewed their adequacy. It noted that no material instances of non-compliance had been identified.

These models indicate that we should continue to have access to capital markets at commercially acceptable interest rates throughout the five year period. To monitor and control risks around access to capital markets we have policies and procedures in place to help mitigate, as far as possible, any risk of a change in our credit ratings and other credit metrics.

More detail on our financial risks, including liquidity and solvency, is provided in note 30 to the consolidated financial statements. There have been no major changes to the Group's significant liquidity and solvency risks in the year.

**Table of Contents**

Strategic Report	<b>Corporate Governance</b>	Financial Statements	Additional Information	53
------------------	-----------------------------	----------------------	------------------------	----

**Finance Committee**

**Role**

Sets policy and grants authority for financing decisions, credit exposure, hedging and foreign exchange transactions, guarantees and indemnities subject to the risk appetite approved by the Board. It also approves other treasury, tax, pension funding and insurance strategies and, if appropriate, recommends them to the Board.

**Review of the year**

The Finance Committee was established in 2002 to focus on the Company’s debt book to make sure these matters were given

**Matters considered**

Examples of matters the Committee considered during the year include:

- long-term funding requirements;
- setting and reviewing treasury policies;
- treasury performance updates provided at each meeting;
- UK and US tax updates;
- activities of the Energy Procurement Risk Management Committee in the US;
- activities of the Incentive Risk Management Committee in the UK;
- credit rating agencies’ views on the Company;
- foreign exchange policy;
- pensions updates, in particular funding of the Company’s pension deficits; and
- insurance renewal strategy.

**Committee membership and attendance**

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the necessary attention.

Following a number of new Non-executive Directors joining the Board in 2012/13, a presentation on the work and remit of the Committee was given to the Board in April 2013.

The presentation focused on the risks inherent in the areas the Finance Committee covers namely, treasury activities, insurance, pensions and tax. The presentation aimed to help all Directors understand the role and responsibilities of the Committee.

During the year, external advisors have given presentations to the Committee on matters such as capital markets, the results of a debt investor survey and the current state of banks. Additionally, information was circulated between meetings to make sure the Committee was kept fully briefed.

This year, we continued to focus on funding plans to take into account international debt market conditions. The Committee received regular reports on treasury, tax, insurance, pensions and commodity activities to keep us advised of progress and we approved recommendations where appropriate.

In July, after seven years as chair of this Committee, I will be stepping down from the Board. I have been working closely with Therese to ensure a smooth handover of responsibilities. I have no doubt the Committee will continue to perform effectively and evolve under Therese's leadership.

Committee membership during the year and attendance at meetings is set out below. Attendance is expressed as the number of meetings attended out of the number possible or applicable for the individual Director during the year to 31 March 2014.

Name	Attendance
Maria Richter (chairman)	4 of 4
Steve Holliday	4 of 4
Andrew Bonfield	4 of 4
Jonathan Dawson	4 of 4
Therese Esperdy <sup>1</sup>	0 of 0
Ruth Kelly	4 of 4
Mark Williamson <sup>2</sup>	1 of 1

1. Therese Esperdy was appointed to the Committee with effect from 18 March 2014.
2. Mark Williamson stepped down following his appointment as chairman of the Audit Committee on 29 July 2013.

**Maria Richter**

Committee chairman



**Table of Contents**



**54 National Grid Annual Report and Accounts 2013/14**

**Corporate**

**Governance**

continued

**Safety, Environment and Health Committee**

**Role**

In relation to safety, environment and health, the Committee reviews the strategies, policies, initiatives, risk exposure, targets and performance of the Company and, where appropriate, of its suppliers and contractors. It monitors the resources we use for compliance and driving improvement in these areas. The Committee also reviews investigations into major incidents and subsequent measures taken.

**Review of the year**

**Matters considered**

Examples of matters the SEH Committee reviewed during the year include:

- ongoing monitoring of safety performance and significant incidents in both the US and UK;
- lessons learnt and steps taken following a contractor fatality in the US in April 2013;
- update on the UK and US safety and environment strategy, leadership and governance processes, looking at work done to coordinate approaches in the two regions. This includes the establishment of a Group-level safety, environment and health management committee which meets monthly and reports to the Executive Committee;
- Group-wide employee process safety culture survey results;
- audit of asbestos legislation compliance across the UK business;
- review of procedures for detecting gas mains in the US;
- consideration of the Company's risk appetite in the context of safety; and

In terms of safety, our focus over the past year has again been on process safety. This includes the progress made, following the introduction of the new safety management system, in managing major hazard assets across our businesses, as well as the work required for the Company to become an industry leader in this area.

climate change strategy, including performance against emissions targets and carbon budgets.

### Committee membership and attendance

Committee membership during the year and attendance at meetings is set out below. Attendance is expressed as the number of meetings attended out of the number possible or applicable for the individual Director during the year to 31 March 2014.

In particular, we have reviewed in depth the risks relating to our US LNG assets and the introduction of a new decision support tool for managing risks on gas transmission pipelines. We have also begun a review of the interfaces between our IT systems and safety processes.

Name	Attendance
Philip Aiken (chairman)	5 of 5
Andrew Bonfield <sup>1</sup>	0 of 0
Nora Mead Brownell	5 of 5
Paul Golby	5 of 5
Ken Harvey <sup>2</sup>	2 of 2

Following a fatality and other incidents involving contractors in the US gas distribution business, we spent time with senior local management considering what measures needed to be put in place to promote a culture of safety among both employees and contractors and prevent a reoccurrence.

In relation to environmental matters, we have continued to monitor the Company's strategy and approach to sustainability. In particular, we have looked at projects the Company is engaged in to reuse and recycle our resources such as overhead line conductors.

1. Andrew Bonfield was appointed to the Committee with effect from 27 March 2014.
2. Ken Harvey stepped down from the Board with effect from 29 July 2013.

We have also reviewed the Company's 2012 to 2016 Health and Wellbeing strategy. This includes a focus on mental wellbeing and how this affects not only employees' absence, but also their levels of performance and engagement at work and in their home life. The Company is working to identify business areas most susceptible to workplace pressure that may impact employees' mental wellbeing. We have started to provide training and information to reduce the stigma associated with mental illness as well as developing and

promoting access to health and wellbeing  
support and treatment for affected employees.

**Philip Aiken**

Committee chairman

**Table of Contents**

Strategic Report	<b>Corporate Governance</b>	Financial Statements	Additional Information	55
------------------	-----------------------------	----------------------	------------------------	----

**Nominations Committee**

**Role**

Responsible for considering the structure, size and composition of the Board and committees, and succession planning. It also identifies and proposes individuals to be Directors and executive management reporting directly to the Chief Executive, and establishes the criteria for any new position.

**Review of the year**

The Board is now in the final stages of its phased transition that commenced in 2011. Most recently we have welcomed Therese Esperdy and John Pettigrew to our Board and, following the AGM, Maria Richter will be stepping down from the Board. Nick Winser will also step down from the Board at this time, but will continue in his role as President of ENTSO-E and Chairman of NGET and NGG until July 2015 when he will be leaving the Company.

**Matters considered**

Examples of matters the Nominations Committee considered during the year include:

- Non-executive and Executive Director appointments, see page 56 for details of the processes; the successor as Senior Independent Director to Ken Harvey;
- Board and committee membership following changes to the composition of the Board;
- the executive succession planning process focusing on the identification, development and readiness of successors to the Executive Committee in particular; and
- review of the findings from the Board evaluation, see page 46 for more information, and discussion of the Committee's performance.

**Committee membership and attendance**

Committee membership during the year and attendance at meetings is set out below. Attendance is expressed as the number of meetings attended out of the number possible or applicable for the individual Director during the year to 31 March 2014.

<b>Name</b>	<b>Attendance</b>
Sir Peter Gershon (chairman)	6 of 6

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<p>Following the changes in Board membership, the composition of the committees was reviewed and updated to reflect the new balance of skills, knowledge and experience on the Board.</p>	<p>Philip Aiken</p>	<p>6 of 6</p>
	<p>Nora Mead Brownell</p>	<p>6 of 6</p>
	<p>Jonathan Dawson</p>	<p>6 of 6</p>
<p>Diversity of background, thinking styles and expertise have been important criteria in the transition of the Board. During the year the Committee reviewed our Board diversity policy. Progress against the policy was discussed and objectives to support the implementation of the policy were agreed, see page 56 for more details.</p>	<p>Therese Esperdy<sup>1</sup></p>	<p>1 of 1</p>
	<p>Paul Golby</p>	<p>6 of 6</p>
	<p>Ruth Kelly</p>	<p>6 of 6</p>
<p>The Committee agreed that the first objective should be to continue to meet, and aspire to exceed, the target of 25% of Board positions to be held by women by 2015. I look forward to reporting on our progress next year.</p>	<p>Maria Richter</p>	<p>6 of 6</p>
	<p>Mark Williamson</p>	<p>6 of 6</p>
	<p>Ken Harvey<sup>2</sup></p>	<p>1 of 1</p>
<p>Succession planning below Board level is also important.</p>	<p>George Rose<sup>2</sup></p>	<p>1 of 1</p>
<p>During the year the Committee with the Chief Executive reviewed the Executive Committee timeline and succession plans, rather than these being considered by the Board, to allow for a more open discussion. The presentation focused on succession cover to address the key risks and actions identified by an external assessment.</p>	<p>1. Therese Esperdy was appointed to the Committee with effect from 18 March 2014.</p> <p>2. George Rose and Ken Harvey stepped down from the Board with effect from 29 July 2013.</p>	

### **Sir Peter Gershon**

Committee chairman



**Table of Contents**



**56 National Grid Annual Report and Accounts 2013/14**

**Corporate**

**Governance**

continued

**Appointment processes**

**Non-executive Director**

The recruitment process undertaken for the appointment of Therese Esperdy was formal, rigorous and transparent. The Nominations Committee appointed Korn Ferry as the search consultancy, and the following process was undertaken:

a role profile was prepared against which potential candidates were considered;

Sir Peter Gershon interviewed an initial list of candidates, from which a shortlist of preferred candidates was selected;

Maria Richter, Mark Williamson, Steve Holliday and Andrew Bonfield interviewed the shortlist of candidates and provided feedback to the Committee;

the Committee considered these views in its deliberations before recommending a preferred candidate to the Board; and

we will only engage executive search firms who have signed up to the voluntary code of conduct on gender diversity;

where appropriate, we will assist with the development and support of initiatives that promote gender and other forms of diversity among our Board, executive and other senior management;

where appropriate, we will continue to adopt best practice in response to the Davies Review;

we will review our progress against the Board diversity policy annually;

we will report on our progress against the policy and our objectives in the Annual Report and Accounts along with details of initiatives to promote gender and other forms of diversity among our Board, Executive Committee and other senior management; and

we will continue to make key diversity data, both about the Board and our wider employee population, available in the Annual Report and Accounts.

the Board approved the appointment as recommended.

In addition to providing external search consultancy services to the Company, a subsidiary of Korn Ferry provides external coaching to senior managers in the US.

### **Executive Director**

John Pettigrew's appointment to the Board as an Executive Director had been envisaged for some time. His executive career with the Company has been guided to make sure that he has experience of multiple parts of the business. His readiness and suitability for appointment to the Board was assessed by an external consultant.

As part of the appointment process, John Pettigrew was interviewed individually by Sir Peter Gershon, Mark Williamson, Jonathan Dawson and Ruth Kelly. The feedback from these meetings was discussed by the Committee before agreeing to recommend John's appointment to the Board. The Board approved the recommendation to appoint John as an Executive Director. John's role has not changed following his appointment to the Board.

### **Board diversity and the Davies Review**

At National Grid, we believe that creating an inclusive and diverse culture supports the attraction and retention of talented people, improves effectiveness, delivers superior performance and enhances the success of the Company.

Our Board diversity policy promotes this and reaffirms our aspiration to meet and exceed the target of 25% of Board positions being held by women by 2015, as set out by Lord Davies.

Progress against the objectives and the policy will be reviewed annually and reported in the Annual Report and Accounts. The implementation of a successful diversity policy will need to be measured over a period of some years during which the size and shape of the Board may change to support the business.

### **Executive Committee**

Led by the Chief Executive, the Executive Committee oversees the safety, operational and financial performance of the Company. It is responsible for making day-to-day management and operational decisions it considers necessary to safeguard the interests of the Company and to further the strategy, business objectives and targets established by the Board. The Committee plays an important role in the development of our people and in driving a high-performance culture.

It approves expenditure and other financial commitments within its authority levels and discusses, formulates and approves proposals to be considered by the Board.

There are currently 10 members on the Committee. They have a broad range of skills and expertise, which are updated through training and development. Some members also hold external non-executive directorships, giving them valuable board experience.

On a quarterly basis the Committee receives an inclusion and diversity scorecard which sets out statistics from the business at all levels in the UK and US. Progress against our aspirational inclusion and diversity targets is reviewed on an annual basis.



We currently have 28% women on our Board, which will change to 25% on the departure of Maria Richter and Nick Winsler, and 20% women on our Executive Committee.

The number of women in senior management positions and throughout the organisation is set out on page 41 along with examples of the initiatives to promote and support inclusion and diversity throughout our Company.

During the year the Committee reviewed the Board diversity policy and progress made. It also discussed and agreed the following objectives to support the implementation of the policy:

the Board aspires to exceed the target of 25% of Board positions to be held by women by 2015;

all Board appointments will be made on merit, in the context of the skills and experience that are needed for the Board to be effective;

The Committee officially met 12 times this year, but the members interact much more regularly. Those members of the Committee who are not Directors all regularly attend Board and committee meetings for specific agenda items with Alison Kay, Group General Counsel & Company Secretary, being secretary to the Board and Nominations Committee. This means that knowledge is shared and every member is kept up to date with business activities and developments.

**Table of Contents**

Strategic Report	<b>Corporate Governance</b>	Financial Statements	Additional Information	57
------------------	-----------------------------	----------------------	------------------------	----

- 1 **Steve Holliday**, Committee chairman
- 2 **Andrew Bonfield**, Finance Director
- 3 **Stephanie Hazell**, Group Strategy & Corporate Development Director (joined the Committee in June 2013 to replace Alison Wood)
- 4 **Alison Kay**, Group General Counsel & Company Secretary (see page 173 for her biography)
- 5 **Tom King**, Executive Director, US
- 6 **David Lister**, Chief Information Officer
- 7 **George Mayhew**, Corporate Affairs Director
- 8 **John Pettigrew**, Executive Director, UK
- 9 **Mike Westcott**, Group Human Resources Director
- 10 **Nick Winsor**, Executive Director, UK

The Committee is chaired by the Finance Director and its members are the Group General Counsel & Company Secretary, the Global Tax and Treasury Director, the Group Financial Controller, the Director of Investor Relations, the Director of Corporate Audit and the Deputy Group General Counsel, with other attendees as appropriate.

**Directors Report statutory and other disclosures (starting on page indicated)**

AGM page 46

Articles of Association page 176

Audit information page 52

Board of Directors page 43

## Management committees

To help make sure we allocate time and expertise in the right way, the Company has a number of management committees, which include the Disclosure Committee, Global Ethics and Compliance Committees and the Global Retirement Plan Committee. These management committees provide reports, where relevant, to the appointing committee in line with our governance framework on the responsibilities they have been delegated.

**Business model** page 14

**Change of control provisions** page 173

**Code of Ethics** page 177

## Disclosure Committee

The role of the Disclosure Committee is to assist the Chief Executive and the Finance Director in fulfilling their responsibility for overseeing the accuracy and timeliness of the disclosures made whether in connection with our presentations to analysts, financial reporting obligations or other material stock exchange announcements.

**Conflicts of interest** page 173

**Contractual and other arrangements**  
page 160

This year the Committee met to consider the announcements of the full- and half-year results and the interim management statements. It reported on the matters arising to the Audit Committee. In doing so it spent time considering the Company's disclosure obligations relating to RIIO, the implementation of the US financial systems and controls, the LIPA MSA transition and the Board's approach to the offer of the scrip dividend option. The Committee also reports the results of its evaluation of the effectiveness of the Company's disclosure controls to the Audit Committee.

**Directors indemnity** page 173

**Directors share interests** page 70

**Diversity** page 41

**Dividend** page 02

**Events after the reporting period** page 173

**Financial instruments** page 83

**Future developments** page 12

**Greenhouse gas emissions** page 11

**Human rights** page 41

**Important events affecting the  
Company during the year** page 06

**Internal control** page 22

**Material interests in shares** page 174

**People** page 40

**Political donations and expenditure**  
page 174

**Principal activities** page 12

**Research and development** page 174

**Risk management** page 22

**Share capital** page 174

The Directors' Report, prepared in accordance with the requirements of the Companies Act 2006 and the UK Listing Authority's Listing, and Disclosure and Transparency rules, comprising pages 06 to 73 and 160 to 187, was approved by the Board and signed on its behalf by:

**Alison Kay**

Group General Counsel & Company Secretary

Company number 4031152

18 May 2014

**Table of Contents**



**58 National Grid Annual Report and Accounts 2013/14**

**Remuneration**

**Report**

**Annual statement from the Remuneration Committee chairman**

I am delighted to present my first Directors Remuneration Report.

Following the introduction of a new UK regulatory framework in 2013 and the continued evolution of our US business, last summer the Committee initiated an extensive review of our executive remuneration strategy. Our objective was to assess whether the principles on which the current remuneration strategy is based continued to reflect our business drivers given recent changes. Our review concluded that a number of significant changes were appropriate. They are presented in this report for our shareholders' consideration and, I hope, approval at our 2014 AGM.

The key factor in our discussions was to enhance the alignment of interest between executives and

Stronger alignment with our business model and the long-term value drivers around a dividend-led total return. It is proposed to move to two key LTPP metrics – RoE (50% weighting) and value growth (50% weighting):

RoE is aimed at focusing management on driving profits within the business; and

value growth is viewed as a clearer indicator than EPS of the long-term growth of the business and the creation of shareholder value.

Extended holding periods for incentive awards. It is proposed that any APP award is paid half in cash and half in shares. The shares would be paid immediately and be subject to a minimum holding period of two years. LTPP performance metrics would be measured over a three year period and awards would then be subject to a minimum two year holding period.

shareholders over the longer term. National Grid is a long-term business, where decisions taken today can have significant impact on performance and profitability over several years. Therefore the Committee believes that the bulk of incentives to executives should be paid in shares and that it is essential for high levels of personal shareholdings to become mandatory, rather than simply guidelines.

Having reached provisional conclusions I wrote to a number of our larger shareholders to seek their views. In the light of the constructive responses we received, the Committee amended its proposals and these amendments are incorporated into the recommendations in this report.

The key components of our recommendations are:

A rebalancing of variable pay from the Annual Performance Plan (APP) to the Long Term Performance Plan (LTPP). It is proposed:

to reduce the APP maximum from 150% of salary to 125% of salary for the CEO and the other Executive Directors; and

to increase the LTPP maximum from 225% to 350% of salary for the CEO and from 200% to 300% of salary for the other Executive Directors.

Increased alignment with shareholders by requiring Executive Directors to retain a significantly higher number of shares earned. It is proposed:

for the CEO, the new requirement is a shareholding of 500% of pre-tax salary, equivalent

The Company's commitment to increasing the annual dividend by at least RPI for the foreseeable future would be reflected in LTPP awards. The Committee will have the explicit power to reduce LTPP vesting should the Company fail to honour the dividend commitment, irrespective of the level of vesting resulting from the performance against the LTPP targets set by the Committee.

The consequence of all these changes is to reduce near-term cash incentives (APP) and tilt the balance to longer-term awards and longer-term shareholding exposure, with a greater proportion of Executive Directors remuneration earned in shares. As a result, we are striking an important balance between long-term reward and increased financial risk to executives through very high levels of mandatory shareholdings. In setting the quantum of future LTPP awards we have taken account of the reduced APP opportunity and longer holding periods that we are proposing. However, I want to assure shareholders that the Committee's intention is that any increase in remuneration should arise from commensurate increases in long-term performance. We will therefore seek to ensure that targets set for the LTPP metrics contain appropriately demanding levels of performance to justify any increase in executive reward.

For the 2014 LTPP award we are proposing that maximum payout would require an average annual Group RoE of 12.5% and an average annual value growth of 12% over the three year performance period. The Committee considers these stretch targets, in the light of the business plan and recent performance, to be more challenging to management than those for LTPP set in the recent past. To achieve such a performance would require incremental Group pre-tax profits of over £250 million per annum, which in turn would imply achieved customer savings in the region of £100 – £200 million.

to over nine years post-tax salary; and

for the other Executive Directors, the new requirement is a shareholding of 400% of pre-tax salary.

We can also confirm that, had the proposed APP and LTPP targets been applicable for 2013/14, no higher level of incentive remuneration would have resulted than was actually achieved under the current arrangements.



**Table of Contents**

Strategic Report	<b>Corporate Governance</b>	Financial Statements	Additional Information	59
------------------	-----------------------------	----------------------	------------------------	----

In addition to the incentive plans review, the Committee reviewed future pension policy and the Executive Directors' salaries. Last year there were no salary increases for Executive Directors. For the year ahead the Committee has awarded a 2.5% salary increase to Andrew Bonfield, Steve Holliday and Tom King, in line with the wider Group salary review budget. Nick Winser will not receive a salary increase, due to the fact that he is to stand down from the Board at the AGM in July 2014.

John Pettigrew joined the Board on 1 April 2014 with a starting salary of £475,000 and will not receive a salary increase from 1 June 2014. His remuneration package is in line with the remuneration policy presented for approval in this report. In particular, his salary is below the Committee's assessment of the market rate for equivalent roles. Subject to his performance, the Committee's intention is to increase his salary towards market level by way of future phased increases in excess of those awarded to other Executive Directors.

**Directors remuneration policy**

The following tables provide details of the policy we intend to apply, subject to shareholder approval, for three years from the date of the 2014 AGM. Following approval it will be displayed on the Company's website.

There may be circumstances from time to time when the Committee will consider it appropriate to apply some judgement and exercise discretion in respect of the approved policy. This ability to apply discretion is highlighted where relevant in the policy, detailed on pages 60 to 66, and the use of discretion will always be in the spirit of the approved policy.

The Committee will honour any commitments made to Directors before the policy outlined in this report comes into effect.

**Our peer group**

Our 2013/14 performance is set out on page 68. Overall, against the APP performance metrics of adjusted EPS, operating profit, US capital delivery, UK and US RoE and individual objectives, performance was ahead of target. As a result, we have made awards to the Executive Directors of between 83% and 129% of salary.

Details of future targets and historical performance will be disclosed each year in respect of the LTPP, and details of historical performance will be disclosed each year in respect of the APP.

The Committee believes that our proposals to restructure incentive pay are appropriate for the Company and on behalf of the Committee I commend them to shareholders.

**Jonathan Dawson**

Committee chairman

The Committee benchmarks its remuneration policy against appropriate peer groups annually to ensure we remain competitive in the relevant markets. The primary focus for reward benchmarking is the FTSE 11-40 for UK-based Executive Directors and general industry and energy services companies with similar levels of revenue for US-based Executive Directors. These peer groups are considered appropriate for a large, complex, international and predominantly regulated business.

**Table of Contents**



**60 National Grid Annual Report and Accounts 2013/14**

**Remuneration**

**Report**

continued

Future policy table Executive Directors

<p><b>Salary high-calibre individuals,</b></p>	<p><b>Purpose and link to strategy: to attract, motivate and retain while not overpaying.</b></p>	
<p>Operation</p>	<p>Maximum levels</p>	<p>Performance metrics, weighting and time period applicable</p>
<p>Salaries are targeted broadly at mid-market level.</p>	<p>No prescribed maximum annual increase.</p>	<p>Not applicable.</p>

They are generally reviewed annually. Salary reviews take into account:	Any increases are generally aligned to salary increases received by other Company employees and to market movement. Increases in excess of this may be made at the Committee's discretion in circumstances such as a significant change in responsibility; progression in the role; and alignment to market level.	
business and individual contribution; the individual's skills and experience; scope of the role, including any changes in responsibility; and market data in the relevant comparator group.		

**Benefits**  
**Purpose and link to strategy: to provide competitive and cost-effective benefits to attract and retain high-calibre individuals.**

<b>Operation</b>	<b>Maximum levels</b>	<b>Performance metrics, weighting and time period applicable</b>
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Benefits provided include:  company car or a cash alternative (UK only); use of a driver when required; private medical insurance; life assurance; personal accident insurance; opportunity to purchase additional benefits under flexible benefits schemes available to all employees; and opportunity to participate in the following HM Revenue & Customs (UK) or Internal Revenue Service (US) tax advantaged all-employee	Benefits have no pre-determined maximum, as the cost of providing these varies from year to year.  Participation in tax approved all-employee share plans is subject to limits set by the relevant tax authorities from time to time.	Not applicable.
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share plans:

**Sharesave:** UK employees may make monthly contributions from net salary for a period of 3 or 5 years. The savings can be used to purchase shares at a discounted price, set at the launch of each plan period.

**Share Incentive Plan (SIP):** UK employees may use gross salary to purchase shares. These shares are placed in trust.

**Incentive Thrift Plans (401(k) plans):** US employees may participate in these tax-advantaged savings plans. They are DC pension plans in which employees can invest their own and Company contributions.

**Employee Stock Purchase Plan (ESPP) (423(b) plan):** eligible US employees may purchase ADSs on a monthly basis at a discounted price.

Other benefits may be offered at the discretion of the Committee.

**Table of Contents**

Strategic Report	<b>Corporate Governance</b>	Financial Statements	Additional Information	61
------------------	-----------------------------	----------------------	------------------------	----

Pension attraction	Purpose and link to strategy: to reward sustained contribution and assist and retention.		
Operation	Maximum levels	Performance metrics, weighting and time period applicable	
Pension for a new Executive Director will reflect whether they are internally promoted or externally appointed.	<b>UK DB:</b> a maximum pension on retirement, at age 60, of two thirds final capped pensionable pay or up to one thirtieth accrual. On death in service, a lump sum of four times pensionable pay and a two thirds dependant s pension is provided.	Not applicable.	
If internally promoted:			

<p>retention of existing DB benefits without enhancement, except for capping of pensionable pay increases following promotion to Board; or retention of existing UK DC benefits or equivalent cash in lieu; or retention of existing US DC benefits plus 401(k) plan match, provided through 401(k) plan and non-qualified plans.</p>	<p><b>UK DC:</b> annual contributions of 30% of salary. Life assurance provision of four times pensionable salary and a spouse's pension equal to one third of the Director's salary are provided on death in service.</p>
<p>If externally appointed:  UK DC benefits or equivalent cash in lieu; or US DC benefits plus 401(k) plan match.</p>	<p><b>US DB:</b> an Executive Supplemental Retirement Plan provides for an unreduced pension benefit at age 62 (at age 55 in Tom King's case). For retirements at age 62 with 35 years of service, the pension benefit would be approximately two thirds of pensionable pay. Upon death in service, the spouse would receive 50% of the pension benefit (100% if the participant died while an active employee after the age of 55).</p>
<p>Andrew Bonfield and John Pettigrew are treated in line with the above policy.</p>	<p><b>US DC:</b> 9% of base salary plus APP with additional 401(k) plan match of up to 4%.</p>
<p>Steve Holliday and Nick Winser are provided with final salary pension benefits. For service prior to 1 April 2013, pensionable pay is normally the base salary in the 12 months prior to leaving the Company. For service from 1 April 2013 increases to pensionable pay are capped at the lower of 3% or the increase in inflation. Their pension scheme rules allow for indexed prior salaries to be used for all members. They both participate in the unfunded scheme in respect of benefits in excess of the Lifetime Allowance.</p>	<p><b>US DC:</b> 9% of base salary plus APP with additional 401(k) plan match of up to 4%.</p>
<p>Tom King participates in a qualified pension plan and in an Executive Supplemental Retirement Plan. These plans are non-contributory, cash balance and final average pay plans. Tom's benefits include</p>	<p><b>US DC:</b> 9% of base salary plus APP with additional 401(k) plan match of up to 4%.</p>

compensation to buy out entitlements from his former employer that were lost on recruitment to National Grid. This includes a provision to allow an unreduced pension to be taken from age 55 if Tom is still in the employment of the Company at that time.

In line with market practice, pensionable pay for UK-based Executive Directors includes salary only and for US-based Executive Directors it includes salary and APP award.



**Table of Contents**



**62 National Grid Annual Report and Accounts 2013/14**

**Remuneration**

**Report**

continued

<p><b>Annual achievement of annual Performance Plan individual objectives.</b></p>	<p><b>Purpose and link to strategy: to incentivise and reward the financial and strategic business targets and the delivery of annual</b></p>	
<p><b>Operation</b></p>	<p><b>Maximum levels</b></p>	<p><b>Performance metrics, weighting and time period applicable</b></p>
<p>Performance metrics and targets are agreed at the start of each financial year. Performance metrics are aligned with strategic business priorities. Targets are set with reference to the budget. Awards are</p>	<p>From 2014/15, it is proposed that the maximum award will reduce from 150% of salary to 125% of salary.</p>	<p>A significant majority of the APP is based on performance against corporate financial measures, with the remainder based on performance against individual objectives. Individual</p>

<p>paid in June.</p> <p>For APP awards made in 2013/14, 50% of any award was deferred into shares in the Deferred Share Plan (DSP). The DSP has no performance conditions and vests after three years, subject to continued employment. These shares are subject to forfeiture for leavers in certain circumstances.</p>		<p>objectives are role specific.</p> <p>The Committee may use its discretion to set measures that it considers appropriate in each financial year and reduce the amount payable, taking account of significant safety or customer service standard incidents, environmental and governance issues.</p>
<p>For APP awards made in respect of years from 2014/15, it is proposed discontinuing the DSP. Instead 50% of awards will be paid in shares, which (after any sales to pay tax) must be retained until the shareholding requirement is met, and in any event for two years after receipt.</p>		<p>For 2013/14, the APP was structured so that payout at threshold, target and stretch performance levels were 6.67%, 40% and 100% respectively.</p>
<p>Awards are subject to clawback and malus provisions.</p>		<p>From 2014/15, it is proposed the payout levels will be amended so that payouts at threshold, target and stretch performance levels will be 0%, 50% and 100% respectively.</p>

<p><b>Long Term aligning Executive Performance Plan</b></p>	<p><b>Purpose and link to strategy: to drive long-term performance, Director incentives to key strategic objectives and shareholder interests.</b></p>
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<p>Operation</p>	<p>Maximum levels</p>	<p>Performance metrics, weighting and time period applicable</p>
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Awards of shares may be granted each year, with vesting subject to long-term performance conditions.

The performance metrics have been chosen as the Committee believes they reflect the creation of long-term value within the business. Targets are set each year with reference to the business plan.

Awards are subject to clawback and malus provisions. Notwithstanding the level of award achieved against the performance conditions, the Committee may use its discretion to reduce the amount vesting, and in particular will take account of compliance with the dividend policy.

From 2014, it is proposed that the maximum award for the CEO will increase from 225% of salary to 350% of salary and from 200% of salary to 300% of salary for the other Executive Directors.

For awards between 2011 and 2013 the performance measures and weightings were:

adjusted EPS (50%) measured over three years;  
 TSR relative to the FTSE 100 (25%) measured over three years; and  
 UK or US RoE relative to allowed regulatory returns (25%) measured over four years.

From 2014, it is proposed that the performance measures will be:

value growth and Group RoE (for the CEO and Finance Director); and  
 value growth, Group RoE and UK or US RoE (for the UK and US Executive Directors respectively).

LTPP table continued opposite

**Table of Contents**

Strategic Report	Corporate Governance	Financial Statements	Additional Information	63
------------------	----------------------	----------------------	------------------------	----

**Long Term Performance Plan continued** Purpose and link to strategy: to drive long-term performance, aligning Executive Director incentives to key strategic objectives and shareholder interests.

Operation Maximum levels Performance metrics, weighting and time period applicable

For awards granted from 2014, it is proposed that participants must retain vested shares (after any sales to pay tax) until the shareholding requirement is met, and in any event for a further two years after vesting.

All will be measured over a three year period.

The weightings of these measures may vary year to year, but would always remain such that the value growth metric would never fall below a 25% weighting and never rise above a 75% weighting.

Between 2011 and 2013, 25% of the award vested at threshold and 100% at stretch, with straight-line vesting in

between. From 2014, it is proposed that only 20% will vest at threshold.

**Future policy table Non-executive Directors (NEDs)**

**Fees for NEDs**

**Purpose and link to strategy: to attract NEDs who have a broad range of experience and skills to oversee the implementation of our strategy.**

**Operation**

**Maximum levels**

Performance metrics, weighting

and time period applicable

NED fees (excluding those of the Chairman) are set by the Executive Committee in conjunction with the Chairman; the Chairman's fees are set by the Committee.

There are no maximum fee levels.

Not applicable.

The benefits provided to the Chairman are not subject to a predetermined maximum cost, as the cost of providing these varies from year to year.

**Fee structure:**

Chairman fee;

basic fee, which differs for UK- and US-based NEDs;

committee membership fee;

<p>committee chair fee; and Senior Independent Director fee.</p>		
<p>Fees are reviewed every year and are benchmarked against those in companies of similar scale and complexity.</p>		
<p>NEDs do not participate in incentive or pension plans and, with the exception of the Chairman, are not eligible to receive benefits. The Chairman is covered by the Company's private medical and personal accident insurance plans and receives a fully expensed car or cash alternative to a car, with the use of a driver, when required.</p>		
<p>There is no provision for termination payments.</p>		

**Table of Contents**



**64 National Grid Annual Report and Accounts 2013/14**

**Remuneration**

**Report**

continued

**Shareholding requirement**

The requirement of Executive Directors to build up and hold a relatively high value of National Grid shares ensures they share a significant level of risk with shareholders and their interests are aligned.

From 2014/15 it is proposed that the existing shareholding guidelines for Executive Directors will be replaced by a firm requirement to build up and retain shares in the Company. The level of holding will increase from 200% of salary to 500% of salary for the CEO and from 125% of salary to 400% of salary for the other Executive Directors.

Unless the shareholding requirement is met, Executive Directors will not be permitted to sell shares, other than to pay tax or in exceptional circumstances.

The Company includes in its annual employee opinion survey questions on the appropriateness of the pay arrangements within the Company. It does not specifically invite employees to comment on the Directors' remuneration policy but any comments made by employees are noted.

**Policy on recruitment remuneration**

Salaries for new Executive Directors appointed to the Board will be set in accordance with the terms of the approved remuneration policy in force at the time of appointment, and in particular will take account of the appointee's skills and experience as well as the scope and market rate for the role.

Where appropriate, salaries may be set below market level initially, with the Committee retaining discretion to award increases in salary in excess of those of the wider workforce and inflation to bring salary to a market level over

### **Differences in remuneration policy for all employees**

The remuneration policy for the Executive Directors is designed with regard to the policy for employees across the Company as a whole. However, there are some differences in the structure of remuneration policy for the senior executives. In general, these differences arise from the development of remuneration arrangements that are market competitive for our various employee categories. They also reflect the fact that, in the case of the Executive Directors, a greater emphasis tends to be placed on performance-related pay in the market, in particular long-term performance-related pay.

All employees are entitled to base salary, benefits and pension. Many employees are eligible for an APP award based on Company and/or individual performance. Eligibility and the maximum opportunity available is based on market practice for the employee's job band. In addition, around 350 senior management employees are eligible to participate in the LTPP.

The Company has a number of all-employee share plans that provide employees with the opportunity to become, and to think like, a shareholder. These plans include Sharesave and the SIP in the UK and the 401(k) and 423(b) plans in the US. Further information is provided on page 60.

### **Consideration of remuneration policy elsewhere in the Company**

In setting the remuneration policy the Committee considers the remuneration packages offered to employees across the Company. As a point of principle, salaries, benefits, pensions and other elements of remuneration are benchmarked regularly to ensure they remain competitive in the markets in which we operate. In undertaking such benchmarking our aim is to be at mid-market level for all job bands, including those subject to union negotiation.

time, where this is justified by individual and Company performance.

Benefits consistent with those offered to other Executive Directors under the approved remuneration policy in force at the time of appointment will be offered, taking account of local market practice. The Committee may also agree that the Company will meet certain costs associated with the recruitment, for example legal fees, and the Committee may agree to meet certain relocation expenses or provide tax equalisation as appropriate.

Pensions for new Executive Directors appointed to the Board will be set in accordance with the terms of the approved remuneration policy in force at the time of appointment.

Ongoing incentive pay (APP and LTPP) for new Executive Directors will be in accordance with the approved remuneration policy in force at the time of appointment. This means the maximum APP award in any year would be 125% of salary and the maximum LTPP award would be 300% of salary (350% of salary for a new CEO).

For an externally appointed Executive Director, the Company may offer additional cash or share-based payments that it considers necessary to buy out current entitlements from the former employer that will be lost on recruitment to National Grid. Any such arrangements would reflect the delivery mechanisms, time horizons and levels of conditionality of the remuneration lost.

In order to facilitate buy out arrangements as described above, existing incentive arrangements will be used to the extent possible, although awards may also be granted outside of these



As would be expected, we have differences in pay and benefits across the business which reflect individual responsibility and there are elements of remuneration policy which apply to all, for example, flexible benefits and share plans.

When considering annual salary increases, the Committee reviews the proposals for salary increases for the employee population generally, as it does for any other changes to remuneration policy being considered. This will include a report on the status of negotiations with any trade union represented employees.

shareholder-approved schemes if necessary and as permitted under the Listing Rules.

For an internally appointed Executive Director, any outstanding variable pay element awarded in respect of the prior role will continue on its original terms.

Fees for a new Chairman or Non-executive Director will be set in line with the approved policy in force at the time of appointment.

**Table of Contents**

Strategic Report	Corporate Governance	Financial Statements	Additional Information	65
------------------	----------------------	----------------------	------------------------	----

**Service contracts and policy on payment for loss of office**

In line with our policy, all Executive Directors have service contracts which are terminable by either party with 12 months notice.

The contracts contain provisions for payment in lieu of notice, at the sole and absolute discretion of the Company. Such payments are limited to payment of salary only for the remainder of the notice period with the exception of Nick Winser. In Nick's case the value of benefits would also be paid. In the UK such payments would be phased on a monthly basis, over a period no greater than 12 months, and the Executive Director would be expected to mitigate any losses where employment is taken up during the notice period. In the US, for tax purposes the policy is to make any payment in lieu of notice as soon as reasonably practicable, and in any event within two and a half months of the later of 31 December and 31 March immediately following the notice date.

In the event of a UK Director being made redundant, statutory compensation would apply and the relevant pension plan rules may result in the early payment of an

**Dates of Directors service contracts/letters of appointment****Date of service contract/appointment****Executive Directors**

Andrew Bonfield	1 November 2010
Steve Holliday	1 April 2006
Tom King	11 July 2007
John Pettigrew	1 April 2014
Nick Winser	28 April 2003

**Non-executive Directors**

Philip Aiken	15 May 2008
Nora Mead Brownell	1 June 2012
Jonathan Dawson	4 March 2013
Therese Esperdy	18 March 2014
Sir Peter Gershon	1 August 2011
Paul Golby	1 February 2012
Ruth Kelly	1 October 2011
Maria Richter	1 October 2003
Mark Williamson	3 September 2012

**External appointments**

The Executive Directors may, with the approval of the Board, accept one external appointment as a non-executive director of another company and retain any fees received for the appointment. Experience as a board member of another company is considered to be beneficial personal development, that in turn is of value to the Company.

unreduced pension.

On termination of employment, no APP award would generally be payable and any DSP awards would generally lapse. However, the Committee has the discretion to deem an individual to be a good leaver, in which case an APP award would be payable on the termination date, based on performance during the financial year up to termination, and DSP awards would vest on the termination date. Examples of circumstances in which a Director would be treated as a good leaver include redundancy, retirement, illness, injury, disability and death. Any APP award would be prorated and would be subject to performance achieved against the objectives for that year.

On termination of employment, outstanding awards under the share plans will be treated in accordance with the relevant plan rules approved by shareholders. Share awards would normally lapse. Good leaver provisions apply at the Committee's discretion and in specified circumstances, including redundancy, retirement, illness, injury, disability and death, where awards will be released to the departing Executive Director or, in the case of death, to their estate. Long-term share plan awards held by good leavers may vest subject to performance measured at the normal vesting date and are prorated. Such awards would vest at the same time as for other participants.

The Chairman's appointment is subject to six months' notice by either party; for the other Non-executive Directors, notice is one month. No compensation is payable to Non-executive Directors if required to stand down.

Copies of Directors' service contracts and letters of appointment are available to view at the Company's registered office.

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**Table of Contents**



**66 National Grid Annual Report and Accounts 2013/14**

**Remuneration**

**Report**

continued

**Total remuneration opportunity**

The total remuneration for each of the Executive Directors that could result from the remuneration policy in 2014 under three different performance levels – below threshold (when only fixed pay is receivable), on target and maximum – is shown below.

1. Fixed pay – consists of salary, pension and benefits in kind as provided under the remuneration policy.
2. Salary is that to be paid in 2014/15, taking account of the increases that will be effective from 1 June 2014 shown on page 72.
3. Benefits in kind and pension are as shown in the single total figure of remuneration table for 2013/14 on page 67, except for John Pettigrew. For John, benefits in kind are assumed to be £18,300 and pension is assumed to be £320,000.
4. APP calculations are based on 125% of salary for the period 1 April 2014 to 31 March 2015.
5. LTPP calculations are based on awards with a face value of 350% of 1 June 2014 salary for Steve Holliday and 300% of 1 June 2014 salary for all other Executive Directors.
6. LTPP and APP payout is 50% for on target performance and the maximum is 100% for achieving stretch performance.
7. Tom King’s remuneration opportunity has been converted at \$1.62:£1.

**Statement of consideration of shareholder views**

The Committee considers all feedback received from shareholders throughout the year. While the Committee understands that not all shareholders' views will be the same, we consult with our larger shareholders on a regular basis to understand their expectations with regard to executive remuneration issues and any changes in shareholder views in this regard. In 2013/14 larger shareholders were consulted on the proposed changes to remuneration policy. Shareholders were supportive of the direction of change proposed, particularly increasing holding periods for awards and retention thresholds. Several responses suggested a number of small changes and where possible the Committee has reflected these changes in the proposals.

**Table of Contents**

Strategic Report	Corporate Governance	Financial Statements	Additional Information	67
------------------	----------------------	----------------------	------------------------	----

**Annual report on remuneration**

**Statement of implementation of remuneration policy in 2013/14**

**Role of Remuneration Committee**

The Committee is responsible for recommending to the Board the remuneration policy for Executive Directors and the other members of the Executive Committee and for setting the remuneration policy for the Chairman. The aim is to align remuneration policy to Company strategy and key business objectives and ensure it reflects our shareholders, customers and regulators interests.

**Members of the Committee**

All members of the Committee are independent. Committee membership during the year and attendance at meetings is set out below:

Member	Number of possible meetings during the year	Number of meetings attended
Jonathan Dawson – chairman from 29 July 2013	6	6
Nora Mead Brownell	6	5
Table of Contents		191

Paul Golby	6	6
Ken Harvey chairman until 29 July 2013	2	2
George Rose	2	2
Mark Williamson appointed on 29 July 2013	4	4

1. Ken Harvey and George Rose stepped down from the Board with effect from 29 July 2013.

**The Committee's activities during the year**

**Meeting Main areas of discussion**

April	Individual performance for the 2012/13 APP Framework for the 2013/14 APP 2013 Directors Remuneration Report Terms of reference and code of conduct for advisors to the Committee
May	Annual salary review for Executive Directors and Executive Committee 2012/13 APP outturns and confirmation of awards 2013 LTPP awards
July	2010 Performance Share Plan (PSP, the predecessor to the LTPP) final performance Appointment of new advisors to the Committee
November	New incentive plans (APP and LTPP) design Review of outcome from AGM
January	Shareholder consultation on new incentive plans



February Targets for LTPP and APP proposals  
Remuneration policy changes  
New format remuneration report

### Single total figure of remuneration – Executive Directors (audited information)

The following table shows a single total figure in respect of qualifying service for 2013/14, together with comparative figures for 2012/13:

	Salary		Benefits in kind		APP		PSP		Pension		Total	
	£ 000	£ 000	£ 000	£ 000	£ 000	£ 000	£ 000	£ 000	£ 000	£ 000	£ 000	£ 000
	2013/14	2012/13	2013/14	2012/13	2013/14	2012/13	2013/14	2012/13	2013/14	2012/13	2013/14	2012/13
Andrew Bonfield	712	709	55	54	790	677	1,418		214	213	3,189	1,653
Steve Holliday	1,000	996	35	31	1,169	846	2,179	670	418	627	4,801	3,170
Tom King	715	734	23	24	595	526	1,732	466	1,111	980	4,176	2,730
Nick Winser	546	543	12	11	704	500	1,177	335	212	148	2,651	1,537
Total	2,973	2,982	125	120	3,258	2,549	6,506	1,471	1,955	1,968	14,817	9,090

1. Base salaries were last increased on 1 June 2012. Tom King's annual salary was \$1,158,000 and was converted at \$1.62:£1 in 2013/14 and \$1.57:£1 in 2012/13.

2. Benefits in kind include private medical insurance, life assurance, either a fully expensed car or a cash alternative to a car and the use of a driver when required. For Andrew Bonfield, a cash allowance in lieu of additional pension contributions is included within pension rather than benefits in kind.

3. The APP value is the full award before the 50% mandatory deferral into the DSP.

4. During the year, the 2010 PSP award vested and entered a retention period, to be released in June 2014. The above value is based on the share price (744 pence) on the vesting date (1 July 2013). In the prior year the 2009 PSP award vested and entered a retention period, to be released in June 2013. The above valuation is based on the share price (681 pence) on the vesting date (2 July 2012).

5. The pension values for Steve Holliday and Nick Winser represent the additional benefit earned in the year (excluding inflation as measured by the consumer price index (CPI)), multiplied by a factor of 20, less the contributions they made.

6. The pension value for Tom King represents the additional benefit earned in the year multiplied by a factor of 20, plus the Company's contributions (£7,854) to the 401(k) plan.

7. Andrew Bonfield was a member of the DC pension plan during the year. The pension value represents 30% of salary via a combination of cash allowance in lieu of pension £185,120 (2012/13: £184,385) and Company pension contributions £28,480 (2012/13: £28,367). He opted out of the pension plan from 1 April 2014 and now receives the full cash allowance in lieu of pension of 30% of salary.

8. Pension figures in last year's report were based on the draft disclosure regulations. The 2012/13 figures in the above table are therefore amended from last year's report to reflect the final regulations.

**Table of Contents**

## 68 National Grid Annual Report and Accounts 2013/14

**Remuneration****Report**

continued

**Performance against targets for APP 2013/14 (audited information)**

APP awards are earned by reference to the financial year and paid in June. The APP awards earned in 2013/14 were:

Financial Metric	Target	Actual	Proportion of max achieved	Proportion of salary							
				Andrew Bonfield Max	Andrew Bonfield Actual	Steve Holliday Max	Steve Holliday Actual	Tom King Max	Tom King Actual	Nick Winser Max	Nick Winser Actual
Adjusted EPS (p/share)	51.0	54.3	100%	25%	25.00%	25%	25.00%	25%	25.00%	25%	25.00%
Group cash flow (£m)	(188)	195	100%	40%	40.00%	40%	40.00%				
UK cash flow (£m)	1,077 (62)	1,543 (85)	100% 29.5%					30%	8.85%	45%	45.00%

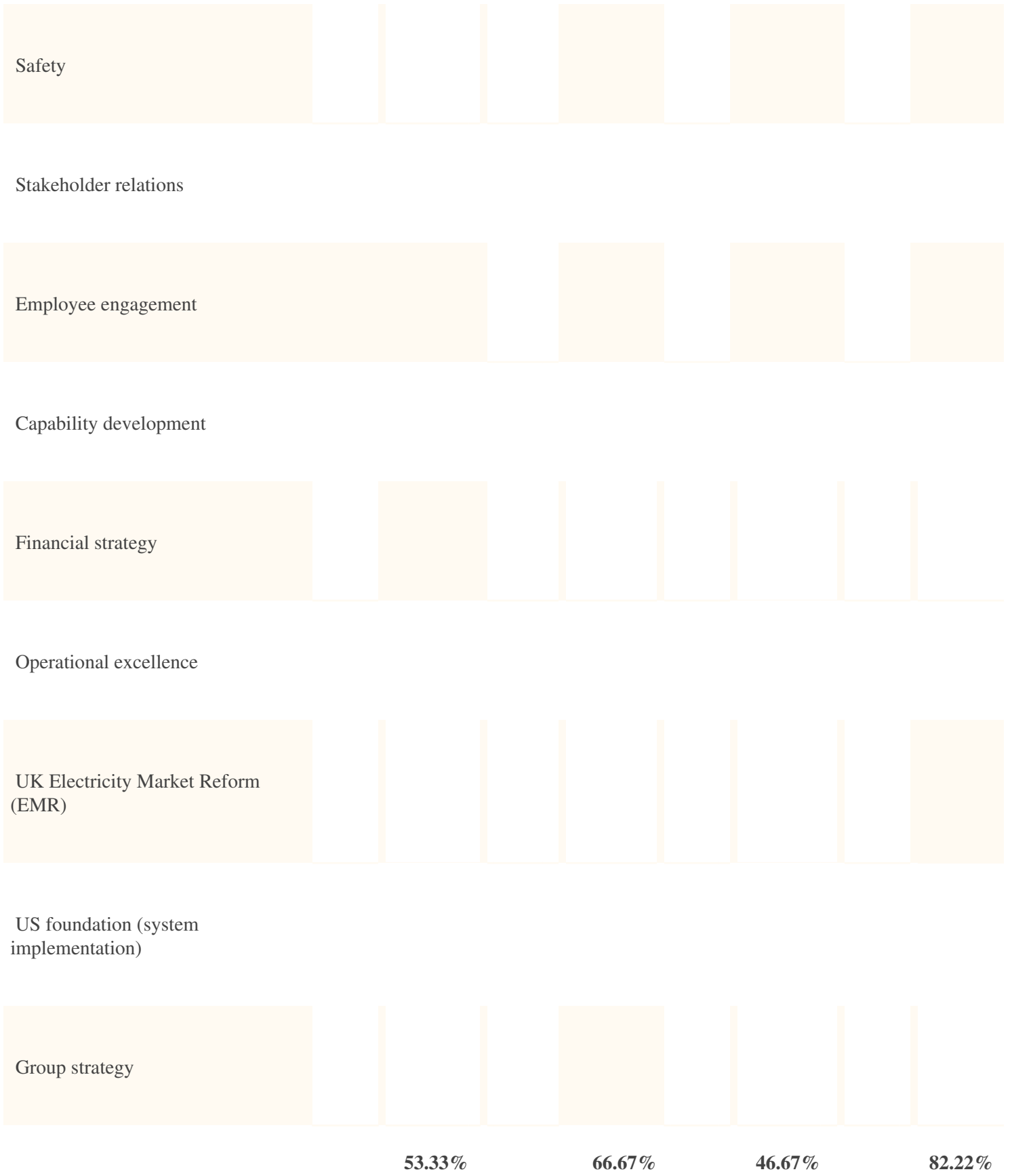
US cash flow (\$m)											
UK RoE (%)	12.4	12.7	62.46%	15%	9.38%	15%	9.38%			35%	21.88%
US RoE (%)	9.2	9.0	23.33%	15%	3.50%	15%	3.50%	25%	5.83%		
US capital plan delivery (£m)	1,192	1,219	90.3%	10%	9.03%	10%	9.03%	25%	22.58%		
Individual objectives	See below			45%	24.00%	45%	30.00%	45%	21.00%	45%	37.00%
<b>Totals</b>				150%	110.91%	150%	116.91%	150%	83.26%	150%	128.88%
<b>APP awarded</b>					<b>£789,679</b>		<b>£1,169,100</b>		<b>£595,155</b>		<b>£703,685</b>

1. In relation to the financial measures, threshold, target and stretch performance pays out at 6.67%, 40% and 100% respectively and on a straight-line basis in between threshold and target performance and target and stretch performance.
2. Adjusted EPS is amended for the impact of timing and actuarial assumptions on pensions and OPEBs.
3. Group cash flow excludes working capital movements and dividends, and is also amended for the impact of timing and certain LIPA transition costs.

### Individual objectives

The following table indicates the primary areas of focus of the individual performance objectives that the Executive Directors had for 2013/14. Threshold, target and stretch performance pays out at 0%, 50% and 100% respectively overall. Overall performance against these objectives is shown in the table:

	<b>Andrew Bonfield</b>	<b>Steve Holliday</b>	<b>Tom King</b>	<b>Nick Winser</b>
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**Proportion of maximum achieved****2013/14 PSP performance (audited information)**

The PSP value included in the 2013/14 single total figure relates to vesting of the conditional PSP award granted in 2010. Vesting was determined as at 30 June 2013 and was dependent on performance over the three years ending 31 March 2013 for the EPS measure and over the three years ending 30 June 2013 for the TSR measure. Transfer remains conditional upon continued service until 30 June 2014. The performance achieved against the performance targets was:

<b>Threshold</b>	<b>Maximum</b>	<b>Actual</b>	<b>Proportion of maximum achieved</b>
<b>Performance measure</b>	<b>100% vesting</b>		
TSR Ranked at median of the comparator group (FTSE 100)	7.5 percentage points or more above median	5.7 percentage points above median	83.3%
Adjusted EPS growth exceeds RPI increase by 3 percentage points	EPS growth exceeds RPI increase by 8 percentage points or more	Exceeded RPI by 6.5 percentage points	77.9%
<b>Total</b>			<b>80.6%</b>

1. The total proportion of maximum achieved is the weighted average of the proportion of maximum achieved for each performance measure. Each of the two measures had a 50% weighting.

**Table of Contents**

Strategic Report	<b>Corporate Governance</b>	Financial Statements	Additional Information
			69

**Total pension entitlements (audited information)**

The table below provides details of the Executive Directors' pension benefits:

	Total contributions to DC-type pension plan	Cash in lieu of contributions to DC-type pension plan	Increase in accrued pension over year, net of inflation at 31 March 2014	Transfer value of accrued benefits as at 31 March 2014	Normal date of retirement
	£ 000	£ 000	£ 000 pa	£ 000	date
Andrew Bonfield	28	185			17/08/2027
Steve Holliday			506 17	13,0137926	26/10/2016
Tom King	8		491 55 284 10	4,1126201 6,3417306	201/01/2027 06/09/2020

Nick  
Winser

1. The UK-based Executive Directors participate in FPS, a salary sacrifice arrangement for pension contributions. Contributions paid via salary sacrifice have been deducted from the figures in the table above.
2. For Steve Holliday, in addition to the pension above, there is an accrued lump sum entitlement of £125,000 as at 31 March 2014. There was no increase to the accumulated lump sum including and excluding inflation in the year to 31 March 2014. The transfer value information above includes the value of the lump sum. Steve paid contributions of £44,000 via FPS.
3. For Nick Winser, in addition to the pension above, there is an accrued lump sum entitlement of £313,000 as at 31 March 2014. The increase to the accumulated lump sum including inflation was £7,000 and excluding inflation was £nil in the year to 31 March 2014. The transfer value information above includes the value of the lump sum. Nick paid contributions of £33,000 via FPS.
4. For Tom King, the exchange rate as at 31 March 2014 was \$1.67:£1 and as at 31 March 2013 was \$1.52:£1. In addition to the transfer value quoted above, through participation in a 401(k) plan in the US, the Company made contributions worth £7,854 to a DC arrangement.
5. The increase in accrued pension figures for Steve Holliday and Nick Winser are net of inflation based on RPI for September 2013. The figures in the single figure table on page 67 are based on inflation using CPI for September 2012. If the same inflation measure was used for this table the relevant figures would be an increase in pension of £23,100 for Steve and £12,250 for Nick. Multiplying these figures by a factor of 20 and deducting member contributions correlates to the values in the single figure table. Tom King's pension figures do not allow for inflation as US pensions in payment or deferment do not increase in line with inflation. For Tom, multiplying the increase in accrued pension over the year, shown above (£55,150), by a factor of 20 and adding Company contributions to a DC-type pension plan, shown above, correlates to the value in the single figure table.
6. There are no additional benefits in the event of early retirement.

**Single total figure of remuneration – Non-executive Directors (audited information)**

The following table shows a single total figure in respect of qualifying service for 2013/14, together with comparative figures for 2012/13:

Fees	Other emoluments	Total
£ 000	£ 000	£ 000



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	2013/14	2012/13	<del>2013/14</del> 2013/14	2012/13
Philip Aiken	88	84	88	84
Nora Mead Brownell	88	73	88	73
Jonathan Dawson	84	6	84	6
Therese Esperdy	3		3	
Sir Peter Gershon	475	475	<del>1792</del> 492	492
Paul Golby	76	76	76	76
Ken Harvey	36	108	36	108
Ruth Kelly	76	76	76	76
Maria Richter	101	101	101	101
George Rose	30	91	30	91
Mark Williamson	99	44	99	44
<b>Total</b>	<b>1,156</b>	1,134	<b>1,173</b>	1,151

1. Sir Peter Gershon's other emoluments comprise private medical insurance, cash in lieu of a car and the use of a driver when required.

**Payments for loss of office or to past Directors (audited information)**

No payments were made in 2013/14 for these circumstances.

**Table of Contents**

## 70 National Grid Annual Report and Accounts 2013/14

**Remuneration****Report**

continued

**LTPP and DSP (conditional awards) granted during the financial year (audited information)**

<b>LTPP</b>	<b>Basis of award</b>	<b>Face value 000</b>	<b>Proportion vesting at threshold performance</b>	<b>Number of shares</b>	<b>Performance period end date</b>
Andrew Bonfield	200% of salary	£1,424	25%	194,798	June 2016 and June 2017
Steve Holliday	225% of salary	£2,250	25%	307,793	June 2016 and June 2017
Tom King	200% of salary	\$2,316	25%	41,225 (ADSs)	June 2016 and June 2017
Nick Winser	200% of salary	£1,092	25%	149,382	June 2016 and

1. The face value of the awards is calculated using the share price at the date of grant (27 June 2013) (£7.3101 per share and \$56.1784 per ADS).

DSP	Basis of award	Face value		Release date
		000	Number of shares	
Andrew Bonfield	50% of APP value	£339	45,706	13 June 2016
Steve Holliday	50% of APP value	£423	57,118	13 June 2016
Tom King	50% of APP value	\$413	7,119 (ADSs)	13 June 2016
Nick Winser	50% of APP value	£250	33,741	13 June 2016

The face value of the awards is calculated using the share price at the date of grant (13 June 2013) (£7.4092 per share and \$57.9720 ADS).

The award made in 2013/14 is 50% of the 2012/13 APP value.

#### Performance conditions for LTPP awards granted during the financial year

Performance measure	Weighting				Conditional share awards granted		201
	Andrew Bonfield	Steve Holliday	Tom King	Nick Winser	Threshold	25% vestingMaximum	
TR ranking	25%	25%	25%	25%	At median of comparator group (FTSE 100)	7.5 percentage points more above median	100% vesting
Adjusted EPS	50%	50%	50%	50%	EPS growth exceeds RPI increase by 3 percentage points	EPS growth exceeds RPI increase by 8 percentage points or more	100% vesting
ROE	12.5%	12.5%		25%	Equal to the average allowed regulatory return	2 percentage points or more above the allowed regulatory return	100% vesting

RoE	12.5%	12.5%	25%	1 percentage point below the allowed regulatory return	1 percentage point or above the allowed regulatory return
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**Conditions for DSP awards granted during the financial year**

DSP awards are subject only to continuous employment.

**Shareholder dilution**

Where shares may be issued or treasury shares reissued to satisfy incentives, the aggregate dilution resulting from executive share-based incentives will not exceed 5% in any 10 year period. Dilution resulting from all incentives, including all-employee incentives, will not exceed 7.99% in any 10 year period. The Committee reviews dilution against these limits regularly and under these limits the Company, as at 31 March 2014, had headroom of 4.01% and 7.99% respectively.

**Statement of Directors' shareholdings and share interests (audited information)**

Executive Directors are required to build up and hold a shareholding from vested share plan awards. Deferred share awards are not taken into account for these purposes until the end of the deferral period. Shares are valued for these purposes at the 31 March 2014 price, which was 68.74 pence per share (\$68.74 per ADS).

The following table shows how each Executive Director complies with the shareholding requirement and also the number of shares owned by Non-executive Directors, including connected persons. For Ken Harvey and George Rose, the shareholding is as at the date they stepped down from the Board. For all others it is 31 March 2014.

**Table of Contents**

Strategic Report	<b>Corporate Governance</b>	Financial Statements	Additional Information
			71

	Share ownership requirements (multiple of salary)	Number of shares required to hold	Number of shares outright (including connected persons)	Number of shares held as a multiple of current salary	Share ownership requirements met	Vested but unreleased share award subject to continuous employment (PSP 2010)	Conditional share awards subject to performance conditions (LTPP 2011, 2012 and 2013)	Conditional share award subject to continuous employment (DSP 2011, 2012 and 2013)
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Executive Directors								
Andrew Bonfield	125%	108,273	699	<1%	No	190,589	637,356	130,041
Steve Holliday	200%	243,309	752,031	618%	Yes	292,880	1,006,643	230,411
Tom King	125%	21,058	71,336	423%	Yes	46,556	131,378	32,381
	125%	83,029	355,413	535%	Yes	158,262	487,780	121,771
Nick Winsor								

**Non-executive  
Directors**

Philip Aiken	4,900	n/a	n/a
Nora Mead Brownell	5,000	n/a	n/a
Jonathan Dawson	24,000	n/a	n/a
Therese Esperdy		n/a	n/a
Sir Peter Gershon	75,771	n/a	n/a
Paul Golby	2,500	n/a	n/a
Ken Harvey	5,236	n/a	n/a
Ruth Kelly	800	n/a	n/a
Maria Richter	14,357	n/a	n/a
George Rose	6,792 4,726	n/a n/a	n/a n/a

Mark  
Williamson

1. The salary used to calculate the value of shareholding is the salary earned in the year.
2. Andrew Bonfield has not met the shareholding requirement as none of the share awards in the plans in which he has participated have been released yet.
3. Tom King's holdings and awards are shown as ADSs and each ADS represents five ordinary shares.
4. The release date for the PSP 2010 is 29 June 2014.
5. On 31 March 2014 Andrew Bonfield held 3,421 options granted under the Sharesave plan. These options were granted at a value of 445 pence per share, and they can be exercised at 445 pence per share between April 2016 and September 2016.
6. On 12 June 2013 Steve Holliday exercised two Share Match awards, totalling 37,475 shares. This comprised (i) an award of 16,092 options, expiring in June 2013, exercised for 100 pence in total, and (ii) an award of 21,383 options, expiring in May 2014, exercised for nil value. These shares are included in the table above ( Number of shares owned outright ). In addition, on 7 April 2014, he exercised a Sharesave option over 3,921 shares at the option price of 427.05 pence per share before expiration in September 2014.
7. For Andrew Bonfield, the number of conditional share awards subject to performance conditions is as follows: LTPP 2011: 229,463; LTPP 2012: 213,095; LTPP 2013: 194,798. The number of conditional share awards subject to continuous employment is as follows: DSP 2011: 29,184; DSP 2012: 55,150; DSP 2013: 45,706.
8. For Steve Holliday, the number of conditional share awards subject to performance conditions is as follows: LTPP 2011: 362,148; LTPP 2012: 336,702; LTPP 2013: 307,793. The number of conditional share awards subject to continuous employment is as follows: DSP 2011: 97,359; DSP 2012: 75,933; DSP 2013: 57,118.
9. For Tom King, the number of conditional awards over ADSs subject to performance conditions is as follows: LTPP 2011: 45,537; LTPP 2012: 44,616; LTPP 2013: 41,225. The number of conditional awards over ADSs subject to continuous employment is as follows: DSP 2011: 13,937; DSP 2012: 11,332; DSP 2013: 7,119.
10. For Nick Winser, the number of conditional share awards subject to performance conditions is as follows: LTPP 2011: 174,986; LTPP 2012: 163,412; LTPP 2013: 149,382. The number of conditional share awards subject to continuous employment is as follows: DSP 2011: 48,354; DSP 2012: 39,682; DSP 2013: 33,741.
- 11.

The normal vesting dates for the conditional share awards subject to performance conditions are 1 July 2014 and 1 July 2015; 1 July 2015 and 1 July 2016; and 1 July 2016 and 1 July 2017 for the LTPP 2011, LTPP 2012 and LTPP 2013 respectively. The normal vesting dates for the conditional share awards subject to continuous employment are 15 June 2014; 14 June 2015; and 13 June 2016 for the DSP 2011, DSP 2012 and DSP 2013 respectively.

12. Non-executive Directors do not have a shareholding requirement.

13. In April and May 2014 a further 30 shares were purchased on behalf of both Steve Holliday and Andrew Bonfield via the Share Incentive Plan (an HMRC approved all-employee share plan), thereby increasing their beneficial interests. There have been no other changes in Directors' shareholdings between 1 April 2014 and 18 May 2014.

### External appointments and retention of fees

The table below details the Executive Directors who served as non-executive directors in other companies during the year ended 31 March 2014:

	Company	Retained fees (£)
Andrew Bonfield	Kingfisher plc	81,200
Steve Holliday	Marks and Spencer Group plc	85,000
Nick Winser	Kier Group plc	53,700

### Relative importance of spend on pay

This chart shows the relative importance of spend on pay compared with other costs and disbursements (dividends, tax, net interest and capital expenditure). Given the capital-intensive nature of our business and the scale of our operations, these costs were chosen as the most relevant for comparison purposes. All amounts exclude exceptional items, remeasurements and stranded cost recoveries.





**Table of Contents**

## 72 National Grid Annual Report and Accounts 2013/14

**Remuneration****Report**

continued

**Performance graph and table**

This chart shows National Grid plc's five year annual total shareholder return (TSR) performance against the FTSE 100 index, of which National Grid is a constituent. It assumes dividends are reinvested. The TSR level shown at 31 March each year is the average of the closing daily TSR levels for the 30 day period up to and including that date.

**CEO's pay in the last five financial years**

Steve Holliday was the CEO throughout this five year period.

	2009/10	2010/11	2011/12	2012/13	2013/14
Total single figure £ '000	3,931	3,738	3,539	3,170	4,801
APP (proportion of maximum awarded)	95.33%	81.33%	68.67%	56.65%	77.94%
	100.00%	65.15%	49.50%	25.15%	76.20%

PSP (proportion of maximum vesting)

### Percentage change in CEO s remuneration

The table below shows how the percentage change in the CEO s salary, benefits and APP between 2013/14 and 2012/13 compares with the percentage change in the average of each of those components of remuneration for non-union employees in the UK. The Committee views this group as the most appropriate comparator group, as the CEO is UK-based and this group excludes employees represented by trade unions, whose pay and benefits are negotiated with each individual union.

	Salary			Taxable benefits			APP		
	£ 000	£ 000	Increase	£ 000	£ 000	Increase	£ 000	£ 000	Increase
	2013/14	2012/13		2013/14	2012/13		2013/14	2012/13	
Steve Holliday	1,000	996	0.4%	35	31	12.9%	1,169	846	38.2%
UK non-union employees (increase per employee)			2.9%			0.7%			10.6%

### Statement of implementation of remuneration policy in 2014/15

The remuneration policy will be implemented with effect from the 2014 AGM as follows:

#### Salary

	000		Increase
	From	From	
	1 June 2014	1 June 2013	
Andrew Bonfield	£729.8	£712	2.5%
Steve Holliday	£1,025 \$1,186.95	£1,000 \$1,158	2.5% 2.5%

Tom King

John Pettigrew	£475	£475	0%
----------------	------	------	----

APP measures for 2014/15

	<b>Weighting</b>
Adjusted EPS	35%
Group or UK or US RoE	35%
Individual objectives	30%

The APP targets are considered commercially sensitive and consequently will be disclosed after the end of the financial year in the 2014/15 annual report on remuneration.

**Table of Contents**

Strategic Report	Corporate Governance	Financial Statements	Additional Information	73
------------------	----------------------	----------------------	------------------------	----

## Performance measures for LTPP to be awarded in 2014

	Andrew Bonfield	Steve Holliday	Tom King	John Pettigrew	Threshold 20% vesting	Maximum 100% vesting
Group RoE	50%	50%	25%	25%	11.0%	12.5%
UK RoE				25%	Allowed return plus 1 percentage point	Allowed return plus 3.5 percentage points
US RoE			25%		90% of allowed return	105% of allowed return
Value growth	50%	50%	50%	50%	10.0%	12.0%

## NEDs' fees from 2014

	£ 000 From 1 June 2014	From 1 June 2013	Increase
Chairman	490	475	3.2%
Senior Independent Director	22	20	10.0%
Board fee (UK-based)	62	60	3.3%
Board fee (US-based)	74	72	2.8%

Committee membership fee	9	8	12.5%
Chair Audit Committee	17	15	13.3%
Chair Remuneration Committee	17	12.5	36.0%
Chair (other Board committees)	12.5	12.5	0%

1. Committee chair fees are in addition to the committee membership fee.

### Advisors to the Remuneration Committee

The Committee received advice until 31 July 2013 from independent remuneration consultants Towers Watson. From 1 August 2013 the Committee received advice from independent remuneration consultants New Bridge Street (NBS), a trading name of Aon Hewitt Ltd (part of Aon plc). NBS were selected as advisors by the Committee following a competitive tendering process.

Work undertaken by these advisors included updating the Committee on trends in compensation and governance matters and advising the Committee in connection with benchmarking of the total reward packages for the Executive Directors and other senior employees. NBS and Towers Watson are members of the Remuneration Consultants Group and have signed up to that group's Code of Conduct. Towers Watson also provides general remuneration, pension and benefits advice and services to the Company. The Committee is satisfied that any potential conflicts were appropriately managed. NBS does not provide any other advice or services to the Company. In the year to 31 March 2014 the Committee paid a total of £262,000 to NBS and Towers Watson, with fees being charged on a time incurred basis.

The Committee also received specialist advice from the following organisations:

Alithos Limited: provision of TSR calculations for the PSP and LTPP (£25,000 paid in 2013/14);  
 Linklaters LLP: advice relating to share schemes and to Directors' service contracts as well as providing other legal advice to the Company (£26,000 paid in 2013/14); and  
 KPMG LLP: advice relating to pension matters (£72,000 paid in 2013/14).

The Committee reviews the objectivity and independence of the advice it receives from its advisors each year. It is satisfied that they all provided credible and professional advice.

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The Committee considers the views of the Chairman on the performance and remuneration of the CEO; and of the CEO on the performance and remuneration of the other members of the Executive Committee. The Committee is also supported by the Group General Counsel & Company Secretary who acts as Secretary to the Committee, the Group HR Director, the Global Head of Reward and the Global Head of Pensions. No other advisors have provided significant services to the Committee in the year.

### Voting on 2012/13 Remuneration Report at 2013 AGM

	<b>For</b>	<b>Against</b>
Number of votes	2,201m	20m
Proportion of votes	99.1%	0.9%

1. The voting figures shown above refer to votes cast at the 2013 AGM. In addition, shareholders holding 147m shares abstained.

The Remuneration Report has been approved by the Board and signed on its behalf by:

**Jonathan Dawson**

Chairman of the Remuneration Committee

18 May 2014

**Table of Contents**

<b>74 National Grid Annual Report and Accounts 2013/14</b>	
<b>Financial Statements Contents</b>	
<b>Directors' statement and independent auditors report</b>	<b>Notes to the consolidated financial statements supplementary information</b>
76 <u>Statement of Directors' responsibilities</u>	132 Note 27 <u>Commitments and contingencies</u>
77 <u>Independent auditors' report</u>	133 Note 28 <u>Related party transactions</u>
81 <u>Report of Independent Registered Public Accounting Firm</u>	133 Note 29 <u>Actuarial information on pensions and other post-retirement benefits</u>
<b>Consolidated financial statements under IFRS</b>	137 Note 30 <u>Financial risk management</u>
<b>Basis of preparation</b>	145 Note 31 <u>Borrowing facilities</u>
82 <u>Basis of preparation</u>	146 Note 32 <u>Subsidiary undertakings, joint ventures and associates</u>
83 <u>Recent accounting developments</u>	147 Note 33 <u>Sensitivities on areas of estimation and uncertainty</u>
<b>Primary statements</b>	148 Note 34 <u>Additional disclosures in respect of guaranteed securities</u>
84 <u>Consolidated income statement</u>	<b>Company financial statements under UK GAAP</b>
86 <u>Consolidated statement of comprehensive income</u>	<b>Basis of preparation</b>
87 <u>Consolidated statement of changes in equity</u>	155 <u>Company accounting policies</u>
88 <u>Consolidated statement of financial position</u>	<b>Primary statement</b>
90 <u>Consolidated cash flow statement</u>	156 <u>Company balance sheet</u>
<b>Notes to the consolidated financial statements analysis of items in the primary statements</b>	<b>Notes to the Company financial statements</b>
92 Note 1 <u>Adoption of IAS 19 (revised) Employee benefits</u>	
93 Note 2 <u>Segmental analysis</u>	



97	Note 3	<u>Operating costs</u>	157	Note 1	<u>Fixed asset investments</u>
99	Note 4	<u>Exceptional items, revaluations and stranded cost recoveries</u>	157	Note 2	<u>Debtors</u>
101	Note 5	<u>Finance income and costs</u>	157	Note 3	<u>Creditors</u>
102	Note 6	<u>Taxation</u>	158	Note 4	<u>Derivative financial instruments</u>
107	Note 7	<u>Earnings per share</u>	158	Note 5	<u>Investments</u>
108	Note 8	<u>Dividends</u>	158	Note 6	<u>Borrowings</u>
109	Note 9	<u>Goodwill</u>	158	Note 7	<u>Called up share capital</u>
110	Note 10	<u>Other intangible assets</u>	159	Note 8	<u>Reserves</u>
111	Note 11	<u>Property, plant and equipment</u>	159	Note 9	<u>Reconciliation of movements in total shareholders funds</u>
112	Note 12	<u>Other non-current assets</u>	159	Note 10	<u>Parent Company guarantees</u>
113	Note 13	<u>Financial and other investments</u>	159	Note 11	<u>Audit fees</u>
114	Note 14	<u>Investments in joint ventures and associates</u>			
114	Note 15	<u>Derivative financial instruments</u>			
117	Note 16	<u>Inventories and current intangible assets</u>			
118	Note 17	<u>Trade and other receivables</u>			
119	Note 18	<u>Cash and cash equivalents</u>			
119	Note 19	<u>Borrowings</u>			
122	Note 20	<u>Trade and other payables</u>			
122	Note 21	<u>Other non-current liabilities</u>			
122	Note 22	<u>Pensions and other post-retirement benefits</u>			
126	Note 23	<u>Provisions</u>			
128	Note 24	<u>Share capital</u>			
129	Note 25	<u>Other equity reserves</u>			
130	Note 26	<u>Net debt</u>			

**Table of Contents**

Strategic Report	Corporate Governance	<b>Financial Statements</b>	Additional Information	75
------------------	----------------------	-----------------------------	------------------------	----

**Introduction to the financial statements**

We have continued to develop our presentational format to provide shareholders and users of these financial statements with additional information and guidance, and to make them easier to understand.

Throughout these financial statements we have included additional information boxes, providing helpful commentary on what the disclosures mean and why they are important to the understanding of our financial performance and position. Some of these boxes highlight *Our strategy in action*, drawing out the key elements of our business model (set out in the Strategic Report on pages 14 and 21), and showing how the disclosures reflect this strategy.

**Audit opinions**

We have two audit opinions on our financial statements, reflecting our dual listing on the London Stock Exchange and the New York Stock Exchange. Due to the different reporting requirements for each listing, our auditors are required to confirm compliance with each set of standards in a prescribed format. The IFRS audit opinion has changed this year, reflecting the change to auditing standards, which requires the auditors to provide more detail as to how they have planned and completed their audit, as well as their views on significant matters they have noted and that were discussed by the Audit Committee. There are also additional specific disclosure requirements due to our US listing which are included in the notes.

**Notes**

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

### **Unaudited commentary**

We have presented with the financial statements certain analysis previously included in the financial review section of the Strategic Report of our Annual Report. This approach provides a more understandable narrative, a logical flow of information and reduces duplication. We have created a combined financial review, including a commentary on items within the primary statements, on pages 84 to 91. Unless otherwise indicated, all analysis provided in the financial statements is on a statutory IFRS basis. All information in ruled boxes styled in the same manner as this one does not form part of the audited financial statements. This has been further highlighted by including the word **unaudited** at the start of each box header. Unaudited commentary boxes appear on pages 85 to 87, 89, 91, 96, 106, 108 and 121.

**Table of Contents**


## 76 National Grid Annual Report and Accounts 2013/14

**Statement of Directors****responsibilities**

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

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

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

The Directors are responsible for the maintenance and integrity of the Company's website. Legislation in the United Kingdom governing the preparation and dissemination of financial statements may differ from legislation in other jurisdictions.

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consolidated basis for that period.

Each of the Directors, whose names and functions are listed on page 43, confirms that:

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

select suitable accounting policies and then apply them consistently;

make judgements and estimates that are reasonable and prudent;

state that the consolidated financial statements comply with IFRS as issued by the IASB and IFRS adopted by the EU and, with regard to the Company financial statements, that applicable UK Accounting Standards have been followed, subject to any material departures disclosed and explained in the financial statements; and

prepare the consolidated financial statements and Company financial statements on a going concern basis unless it is inappropriate to presume that the Company, on a consolidated and individual basis, will continue in business, in which case there should be supporting assumptions or qualifications as necessary.

to the best of their knowledge, the consolidated financial statements and the Company financial statements, which have been prepared in accordance with IFRS as issued by the IASB and IFRS as adopted by the EU and UK GAAP respectively, give a true and fair view of the assets, liabilities, financial position and profit of the Company on a consolidated and individual basis;

to the best of their knowledge, the Strategic Report contained in the Annual Report and Accounts includes a fair review of the development and performance of the business and the position of the Company on a consolidated and individual basis, together with a description of the principal risks and uncertainties that it faces; and

they consider that the Annual Report and Accounts, taken as a whole, is fair, balanced and understandable and provides the information necessary for shareholders to assess the Company's performance, business model and strategy.

By order of the Board

**Alison Kay**

Group General Counsel & Company Secretary

18 May 2014

Company number: 4031152

**Table of Contents**

Strategic Report	Corporate Governance	<b>Financial Statements</b>	Additional Information	77

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**Table of Contents**

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78 National Grid Annual Report and Accounts 2013/14

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**Table of Contents**

Strategic Report	Corporate Governance	<b>Financial Statements</b>	Additional Information	79

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**Table of Contents**

--	--	--	--	--	--	--	--

80 National Grid Annual Report and Accounts 2013/14

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**Table of Contents**

Strategic Report	Corporate Governance	<b>Financial Statements</b>	Additional Information 81

**Report of Independent Registered**

**Public Accounting Firm**

to the Board of Directors and Shareholders of National Grid plc

**Audit opinion for Form 20-F**

In our opinion, the accompanying consolidated statements of financial position and the related consolidated income statements, consolidated statements of comprehensive income, consolidated cash flow statements and consolidated statements of changes in equity, present fairly, in all material respects, the financial position of National Grid plc and its subsidiaries at 31 March 2014 and 31 March 2013, and the results of their operations and their cash flows for each of the three years in the period ended 31 March 2014 in conformity with International Financial Reporting Standards as issued by the International Accounting Standards Board and in conformity with International Financial Reporting Standards as adopted by the European Union.

Also in our opinion, the Company maintained, in all material respects, effective internal control over financial reporting as of 31 March 2014, based on criteria established in Internal Control – Integrated Framework (1992) issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO). The Company’s management is responsible for these financial statements, for

A company’s internal control over financial reporting is a process designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles. A company’s internal control over financial reporting includes those policies and procedures that (i) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the company; (ii) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that receipts and expenditures of the company are being made only in accordance with authorisations of management and directors of the company; and (iii) provide reasonable assurance regarding prevention or timely detection of unauthorised acquisition, use, or disposition of the company’s assets that could have a material effect on the financial statements.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of

maintaining effective internal control over financial reporting and for its assessment of the effectiveness of internal control over financial reporting, included in the Additional Information section appearing on page 170 of the 2014 Annual Report and Accounts. As discussed in note 1, the Group changed the manner in which it accounts for employee benefits.

effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

**PricewaterhouseCoopers LLP**

London

United Kingdom

21 May 2014

Our responsibility is to express opinions on these financial statements and on the Company's internal control over financial reporting based on our integrated audits. We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audits to obtain reasonable assurance about whether the financial statements are free of material misstatement and whether effective internal control over financial reporting was maintained in all material respects. Our audits of the financial statements included examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. Our audit of internal control over financial reporting included obtaining an understanding of internal control over financial reporting, assessing the risk that a material weakness exists, and testing and evaluating the design and operating effectiveness of internal control based on the assessed risk. Our audits also included performing such other procedures as we considered necessary in the circumstances. We believe that our audits provide a reasonable basis for our opinions.

**Table of Contents****82 National Grid Annual Report and Accounts 2013/14**

**Basis of  
preparation**

Accounting policies describe our approach to recognising and measuring transactions and balances in the year. Accounting policies applicable across the financial statements are shown below. Accounting policies that are specific to a component of the financial statements have been incorporated into the relevant note.

This section also shows areas of judgement and key sources of estimation uncertainty in these financial statements. In addition, we summarise new EU endorsed accounting standards, amendments and interpretations and whether these are effective in 2014 or later years, explaining how significant changes are expected to affect our reported results.

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

**A. Basis of consolidation**

The consolidated financial statements incorporate the financial statements of the Company and its subsidiaries, together with a share of the results, assets and liabilities of jointly controlled entities (joint ventures) and associates using the equity method of accounting, where the investment is carried at cost plus post-acquisition changes in the share of net assets of the joint venture or associate, less any provision for impairment.

A subsidiary is defined as an entity controlled by the Company. Control is achieved where the Company has the power to affect the returns of an entity to which it is exposed or to which it has rights.

Losses in excess of the consolidated interest in joint ventures and associates are not recognised, except where the Company or its subsidiaries have made a commitment to make good those losses.

The Company has its primary listing on the London Stock Exchange and is also quoted on the New York Stock Exchange. These consolidated financial statements were approved for issue by the Board of Directors on 18 May 2014.

These consolidated financial statements have been prepared in accordance with International Accounting Standards (IAS) and International Financial Reporting Standards (IFRS) and related interpretations as issued by the International Accounting Standards Board (IASB) and IFRS as adopted by the EU. They are prepared on the basis of all IFRS accounting standards and interpretations that are mandatory for periods ending 31 March 2014 and in accordance with the Companies Act 2006 applicable to companies reporting under IFRS and Article 4 of the EU IAS Regulation. The 2013 and 2012 comparative financial information has also been prepared on this basis.

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

The consolidated financial statements have been prepared on a going concern basis following the assessment made by the Directors as set out on page 52.

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

The preparation of financial statements requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities,

Where necessary, adjustments are made to bring the accounting policies used in the individual financial statements of the Company, subsidiaries, joint ventures and associates into line with those used by the Company in its consolidated financial statements under IFRS. Intercompany transactions are eliminated.

The results of subsidiaries, joint ventures and associates acquired or disposed of during the year are included in the consolidated income statement from the effective date of acquisition or up to the effective date of disposal, as appropriate.

Acquisitions are accounted for using the acquisition method, where the purchase price is allocated to the identifiable assets acquired and liabilities assumed on a fair value basis and the remainder recognised as goodwill.

## **B. Foreign currencies**

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

Gains and losses arising on the retranslation of monetary assets and liabilities are included in the income statement, except where the adoption of hedge accounting requires inclusion in other comprehensive income note 15.

On consolidation, the assets and liabilities of operations that have a functional currency different from the Company's functional currency of pounds sterling, principally our US operations that have a

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disclosures of contingent assets and liabilities and the reported amounts of revenue and expenses during the reporting period (see accounting policy C).

functional currency of dollars, are translated at exchange rates prevailing at the reporting date. Income and expense items are translated at the weighted average exchange rates for the period where these do not differ materially from rates at the date of the transaction. Exchange differences arising are classified as equity and transferred to the consolidated translation reserve.

**Table of Contents**

Strategic Report	Corporate Governance	Financial Statements	Additional Information	83
------------------	----------------------	----------------------	------------------------	----

**Recent accounting****developments****C. Areas of judgement and key sources of estimation uncertainty**

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

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

the categorisation of certain items as exceptional items, remeasurements and stranded cost recoveries and the definition of adjusted earnings notes 4 and 7; and

energy purchase contracts classification as being for normal purchase, sale or usage note 27.

**New IFRS accounting standards and interpretations adopted in 2013/14**

During the year ended 31 March 2014, with the exception of IAS 19 (revised), and in respect of disclosures required by IFRS 13 Fair value measurements, the Company has not adopted any new IFRS, IAS or amendments issued by the IASB, or interpretations issued by the IFRS Interpretations Committee (IFRIC), which have had a material impact on the Company's consolidated financial statements. The impact of IAS 19 (revised) is set out in note 1. The additional disclosures required by IFRS 13 are included in note 30.

Other standards, interpretations and amendments issued by the IASB and IFRIC that have not had a material impact on the Company's consolidated results or assets and liabilities are:

IFRS 10 Consolidated financial statements ;

IFRS 11 Joint arrangements ;

IFRS 12 Disclosure of interests in other entities ;

amendments to IAS 27 Separate financial statements and IAS 28 Investments in associates and

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

- **Presentational formats:** we use the nature of expense method for our income statement and aggregate our statement of financial position to net assets and total equity. In the income statement, we present subtotals of total operating profit, profit before tax and profit from continuing operations, together with additional subtotals excluding exceptional items, remeasurements and stranded cost recoveries. Exceptional items, remeasurements and stranded cost recoveries are presented separately on the face of the income statement.
- **Customer contributions:** contributions received prior to 1 July 2009 towards capital expenditure are recorded as deferred income and amortised in line with the depreciation on the associated asset.
- **Financial instruments:** we normally opt to apply hedge accounting in most circumstances where this is permitted. For net investment hedges, we have chosen to use the spot rate method, rather than the alternative forward rate method.

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

impairment of goodwill note 9;

review of residual lives, carrying values and impairment charges for other intangible assets and property, plant and equipment notes 10 and 11;

estimation of liabilities for pensions and other post-retirement benefits notes 22 and 29;

valuation of financial instruments and derivatives notes 15 and 30;

joint ventures as a result of the adoption of the above standards;

amendments to IAS 1 Presentation of financial statements ; and

amendments to IFRS 7 Financial instruments: Disclosures .

### **New IFRS accounting standards and interpretations not yet adopted**

The Company enters into a significant number of transactions that fall within the scope of IFRS 9 Financial instruments . The IASB is completing IFRS 9 in phases and the Company is evaluating the impact of the standard as it develops. It is currently expected that the standard will be required to be adopted by the Company on 1 April 2018. We are currently assessing the likely impact of this standard on the Company s consolidated financial statements.

Other standards and interpretations or amendments thereto which have been issued, but are not yet effective, are not expected to have a material impact on the Company s consolidated financial statements.



revenue recognition and assessment of unbilled  
revenue note 2;

recoverability of deferred tax assets note 6; and

environmental and decommissioning provisions  
note 23.

In order to illustrate the impact that changes in  
assumptions could have on our results and financial  
position, we have included sensitivity analysis in  
note 33.

**Table of Contents**

## 84 National Grid Annual Report and Accounts 2013/14

**Consolidated****income statement**

for the years ended 31 March

	Notes	2014 £m	2014 £m	2013 (restated) <sup>1</sup> £m	2013 (restated) <sup>1</sup> £m	2012 (restated) <sup>1</sup> £m	2012 (restated) <sup>1</sup> £m
<b>Revenue</b>	2(a)		<b>14,809</b>		14,359		13,832
Operating costs	3		<b>(11,074)</b>		(10,610)		(10,297)
<b>Operating profit</b>							
Before exceptional items, remeasurements and stranded cost recoveries	2(b)	<b>3,664</b>		3,639		3,491	
Exceptional items, remeasurements and stranded cost recoveries	4	<b>71</b>		110		44	
<b>Total operating profit</b>	2(b)		<b>3,735</b>		3,749		3,535
<b>Finance income</b>	5		<b>36</b>		30		28

**Finance costs**

Before exceptional items and remeasurements	5	<b>(1,144)</b>	(1,154)	(1,118)
Exceptional items and remeasurements	4,5	<b>93</b>	68	(70)
<b>Total finance costs</b>	5	<b>(1,051)</b>	(1,086)	(1,188)
Share of post-tax results of joint ventures and associates	14	<b>28</b>	18	7

**Profit before tax**

Before exceptional items, remeasurements and stranded cost recoveries	2(b)	<b>2,584</b>	2,533	2,408
Exceptional items, remeasurements and stranded cost recoveries	4	<b>164</b>	178	(26)
<b>Total profit before tax</b>	2(b)	<b>2,748</b>	2,711	2,382

**Taxation**

Before exceptional items, remeasurements and stranded cost recoveries	6	<b>(581)</b>	(619)	(697)
Exceptional items, remeasurements and stranded cost recoveries	4,6	<b>297</b>	62	234
<b>Total taxation</b>	6	<b>(284)</b>	(557)	(463)

**Profit after tax**

Before exceptional items, remeasurements and stranded cost recoveries		<b>2,003</b>	1,914	1,711
Exceptional items, remeasurements and stranded cost recoveries	4	<b>461</b>	240	208
<b>Profit for the year</b>		<b>2,464</b>	2,154	1,919
<b>Attributable to:</b>				
Equity shareholders of the parent		<b>2,476</b>	2,153	1,917
Non-controlling interests		<b>(12)</b>	1	2
		<b>2,464</b>	2,154	1,919
<b>Earnings per share<sup>2</sup></b>				
Basic	7(a)	<b>66.4p</b>	57.8p	51.6p
Diluted	7(b)	<b>66.1p</b>	57.5p	51.3p

1. See note 1 on page 92.

2. Comparative amounts have been restated to reflect the impact of additional shares issued as scrip dividends.

**Table of Contents**

Strategic Report	Corporate Governance	Financial Statements	Additional Information	85
------------------	----------------------	----------------------	------------------------	----

**Unaudited commentary on the consolidated income statement**

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

**Adjusted earnings and EPS**

The following chart shows the five year trend in adjusted profit attributable to equity shareholders of the parent (adjusted earnings) and adjusted EPS.

**Revenue**

Revenue for the year ended 31 March 2014 increased by £450m to £14,809m. This increase was driven by higher revenues in our UK Electricity Transmission and UK Gas Distribution businesses, principally as a result of the new RIIO regulatory arrangements. Revenue in our US Regulated businesses was also higher, reflecting higher pass-through costs such as gas and electricity commodity costs, partially offset by the end of the Niagara Mohawk deferral revenue recoveries at 31 March 2013 and the impact of the weaker dollar.

**Operating costs**

Operating costs for the year ended 31 March 2014 of £11,074m were £464m higher than the prior year. This increase in costs was predominantly due to increases in pass-through costs in our UK and US Regulated

**Adjusted earnings and adjusted EPS<sup>1</sup>**

1. All comparatives restated for IAS 19 (revised). See note 1 on page 92. Adjusted earnings and adjusted EPS are attributable to equity shareholders of the parent.

The above earnings performance translated into adjusted EPS growth in 2013/14 of 2.6p (5%).

In accordance with IAS 33, all EPS and adjusted EPS amounts for comparative periods have been restated for shares issued via scrip dividends and the bonus element

businesses, together with higher depreciation and amortisation as a result of continued investment and increases in our controllable costs.

of the 2010 rights issue.

Exceptional items, remeasurements and stranded cost recoveries included in operating costs for the year ended 31 March 2014 were £39m lower than the prior year. Net exceptional gains included in 2013/14 of £55m primarily consisted of a net gain on the LIPA MSA transition in the US of £254m, a gain of £16m following the sale to a third party of a settlement award, restructuring costs of £136m and UK gas holder demolition costs of £79m. The 2013/14 results also included a gain of £16m on remeasurements of commodity contracts.

Our financial results are reported in sterling. Transactions for our US operations are denominated in dollars, so the related amounts that are reported in sterling depend on the dollar to sterling exchange rate. The weighted average dollar rate weakened to \$1.62:£1 in 2013/14 from \$1.57:£1 in 2012/13. Consequently, if 2012/13 results had been translated at 2013/14 exchange rates, revenue, adjusted operating profit and operating profit reported in sterling would have been £242m, £34m and £39m lower respectively.

There were no major storms affecting our operations in the year ended 31 March 2014. In 2012/13, two major storms in the US, Superstorm Sandy and Storm Nemo, increased operating costs by £136m.

The statement of financial position has been translated at an exchange rate of \$1.67:£1 at 31 March 2014 (\$1.52:£1 at 31 March 2013).

### **Net finance costs**

For the year ended 31 March 2014, net finance costs before exceptional items and remeasurements were £16m lower than 2012/13 at £1,108m, mainly due to the impact of the weaker dollar (£17m).

Finance costs for the year ended 31 March 2014 also included a gain of £93m on financial remeasurements relating to net gains and losses on derivative financial instruments.

### **Taxation**

The tax charge on profits before exceptional items, remeasurements and stranded cost recoveries was £38m lower than 2012/13. This was mainly due to a 1% decrease in the UK statutory corporation tax rate in the year and a change in the UK/US profit mix where higher UK profits were taxed at the lower UK tax rate. Our tax charge was also affected by changes in tax provisions in

respect of prior years.

Exceptional tax for 2013/14 included an exceptional deferred tax credit of £398m arising from a reduction in the UK corporation tax rate from 23% to 21% applicable from 1 April 2014 and a further reduction to 20% from 1 April 2015.

**This unaudited commentary does not form part of the financial statements.**

**Table of Contents**

## 86 National Grid Annual Report and Accounts 2013/14

**Consolidated statement****of comprehensive income**

for the years ended 31 March

	Notes	2014 £m	2013 (restated) <sup>1</sup> £m	2012 (restated) <sup>1</sup> £m
<b>Profit for the year</b>		<b>2,464</b>	2,154	1,919
<b>Other comprehensive income/(loss)</b>				
Items that will never be reclassified to profit or loss				
Remeasurements of net retirement benefit obligations	22	<b>485</b>	(714)	(1,140)
Tax on items that will never be reclassified to profit or loss	6	<b>(172)</b>	179	342
<b>Total items that will never be reclassified to profit or loss</b>		<b>313</b>	(535)	(798)
Items that may be reclassified subsequently to profit or loss				
Exchange adjustments		<b>(158)</b>	117	27
Net gains/(losses) in respect of cash flow hedges		<b>63</b>	(31)	(18)
Transferred to profit or loss in respect of cash flow hedges		<b>27</b>	73	19
Net gains on available-for-sale investments		<b>6</b>	20	16
Transferred to profit or loss on sale of available-for-sale investments		<b>(14)</b>	(10)	(9)
Tax on items that may be reclassified subsequently to profit or loss	6	<b>(2)</b>	(15)	



<b>Total items that may be reclassified subsequently to profit or loss</b>	<b>(78)</b>	154	35
<b>Other comprehensive income/(loss) for the year, net of tax</b>	<b>235</b>	(381)	(763)
<b>Total comprehensive income for the year</b>	<b>2,699</b>	1,773	1,156
<b>Attributable to:</b>			
Equity shareholders of the parent	<b>2,711</b>	1,772	1,154
Non-controlling interests	<b>(12)</b>	1	2
	<b>2,699</b>	1,773	1,156

1. See note 1 on page 92.

## Unaudited commentary on consolidated statement of comprehensive income

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

### Remeasurements of net retirement benefit obligations

We had a net gain after tax of £313m (2012/13: net cost of £535m) on our pension and other post-employment benefit schemes which is due to changes in key assumptions made in the valuation calculation and differences to actual outcomes during the year.

### Exchange adjustments

Adjustments are made when we translate the results and net assets of our companies operating outside the UK, as well as debt we have issued in foreign currencies. The net movement for the year resulted in a loss of £158m (2012/13: £117m gain).

### Net gains/(losses) in respect of cash flow hedges

The value of derivatives held to hedge cash flows is impacted by changes in expected interest rates and exchange rates. The net gain for the year was £63m (2012/13: £31m loss).

**This unaudited commentary does not form part of the financial statements.**

**Table of Contents**

Strategic Report	Corporate Governance	Financial Statements	Additional Information	87
------------------	----------------------	----------------------	------------------------	----

**Consolidated statement****of changes in equity**

for the years ended 31 March

	Called up share capital £m	Share premium account £m	Retained earnings £m	Other equity reserves <sup>1</sup> £m	Total shareholders equity £m	Non- controlling interests £m	Total equity £m
Equity as at 1 April 2011 as previously reported	416	1,361	12,153	(4,870)	9,060	9	9,069
Impact of change in accounting policy <sup>2</sup>			(8)		(8)		(8)
Equity as at 1 April 2011 (restated)	416	1,361	12,145	(4,870)	9,052	9	9,061
Profit for the year <sup>2</sup>			1,917		1,917	2	1,919
Total other comprehensive (loss)/income for the year <sup>2</sup>			(798)	35	(763)		(763)
Total comprehensive income for the year <sup>2</sup>			1,119 (1,319)	35	1,154 (1,319)	2	1,156 (1,319)

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Equity dividends							
Scrip dividend related share issue <sup>3</sup>	6	(6)	313		313		313
Issue of treasury shares			13		13		13
Purchase of own shares			(4)		(4)		(4)
Other movements in non-controlling interests						(4)	(4)
Share-based payment			24		24		24
Tax on share-based payment			3		3		3
At 31 March 2012 (restated)	422	1,355	12,294	(4,835)	9,236	7	9,243
Profit for the year <sup>2</sup>			2,153		2,153	1	2,154
Total other comprehensive (loss)/income for the year <sup>2</sup>			(535)	154	(381)		(381)
Total comprehensive income for the year <sup>2</sup>			1,618	154	1,772	1	1,773
Equity dividends			(1,433)		(1,433)		(1,433)
Scrip dividend related share issue <sup>3</sup>	11	(11)	623		623		623
Issue of treasury shares			19		19		19
Purchase of own shares			(6)		(6)		(6)
Other movements in non-controlling interests						(3)	(3)
Share-based payment			20		20		20
Tax on share-based payment			(2)		(2)		(2)

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At 31 March 2013 (restated)	433	1,344	13,133	(4,681)	10,229	5	10,234
Profit for the year			2,476		2,476	(12)	2,464
Total other comprehensive income/(loss) for the year			313	(78)	235		235
Total comprehensive income/(loss) for the year			2,789	(78)	2,711	(12)	2,699
Equity dividends			(1,503)		(1,503)		(1,503)
Scrip dividend related share issue <sup>3</sup>	6	(8)	444		442		442
Issue of treasury shares			14		14		14
Purchase of own shares			(5)		(5)		(5)
Other movements in non-controlling interests			(4)		(4)	15	11
Share-based payment			20		20		20
Tax on share-based payment			7		7		7
<b>At 31 March 2014</b>	<b>439</b>	<b>1,336</b>	<b>14,895</b>	<b>(4,759)</b>	<b>11,911</b>	<b>8</b>	<b>11,919</b>

1. For further details of other equity reserves, see note 25 on page 129.

2. See note 1 on page 92.

3. Included within share premium account are costs associated with scrip dividends.

### Unaudited commentary on consolidated statement of changes in equity

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

#### Dividends

We paid a total of £1,503m dividends to shareholders in the year (2012/13: £1,433m) of which £444m (2012/13:

£623m) was settled via scrip issues. The Directors are proposing a final dividend of 27.54p, bringing the total dividend for the year to 42.03p, a 2.9% increase on 2012/13. The Directors intend to continue the dividend policy announced last year of increasing the annual dividend by at least the rate of RPI inflation for the foreseeable future.

**This unaudited commentary does not form part of the financial statements.**

**Table of Contents**

## 88 National Grid Annual Report and Accounts 2013/14

**Consolidated statement****of financial position**

as at 31 March

	Notes	2014 £m	2013 (restated) <sup>1</sup> £m
<b>Non-current assets</b>			
Goodwill	9	4,594	5,028
Other intangible assets	10	669	589
Property, plant and equipment	11	37,179	36,592
Other non-current assets	12	87	104
Pension assets	22	174	195
Financial and other investments	13	284	278
Investments in joint ventures and associates	14	351	371
Derivative financial assets	15	1,557	1,972
Total non-current assets		44,895	45,129
<b>Current assets</b>			
Inventories and current intangible assets	16	268	291
Trade and other receivables	17	2,855	2,910
Financial and other investments	13	3,599	5,431
Derivative financial assets	15	413	273
Cash and cash equivalents	18	354	671
Total current assets		7,489	9,576
<b>Total assets</b>		<b>52,384</b>	<b>54,705</b>

**Current liabilities**

Borrowings	19	<b>(3,511)</b>	(3,448)
Derivative financial liabilities	15	<b>(339)</b>	(407)
Trade and other payables	20	<b>(3,031)</b>	(3,051)
Current tax liabilities		<b>(168)</b>	(231)
Provisions	23	<b>(282)</b>	(308)
Total current liabilities		<b>(7,331)</b>	(7,445)

**Non-current liabilities**

Borrowings	19	<b>(22,439)</b>	(24,647)
Derivative financial liabilities	15	<b>(824)</b>	(1,274)
Other non-current liabilities	21	<b>(1,841)</b>	(1,884)
Deferred tax liabilities	6	<b>(4,082)</b>	(4,077)
Pensions and other post-retirement benefit obligations	22	<b>(2,585)</b>	(3,692)
Provisions	23	<b>(1,363)</b>	(1,452)
Total non-current liabilities		<b>(33,134)</b>	(37,026)

**Total liabilities** **(40,465)** (44,471)

**Net assets** **11,919** 10,234

**Equity**

Share capital	24	<b>439</b>	433
Share premium account		<b>1,336</b>	1,344
Retained earnings		<b>14,895</b>	13,133
Other equity reserves	25	<b>(4,759)</b>	(4,681)

**Shareholders equity** **11,911** 10,229

Non-controlling interests **8** 5

**Total equity** **11,919** 10,234

1. See note 1 on page 92.

The consolidated financial statements set out on pages 82 to 154 were approved by the Board of Directors on 18 May 2014 and were signed on its behalf by:

**Sir Peter Gershon** Chairman

**Andrew Bonfield** Finance Director

**Table of Contents**

Strategic Report	Corporate Governance	Financial Statements	Additional Information	89
------------------	----------------------	----------------------	------------------------	----

**Unaudited commentary on consolidated statement of financial position**

The consolidated statement of financial position sets out all the Group's assets and liabilities at the year end. As a capital-intensive business, we have significant amounts of physical assets and corresponding borrowings.

of £42m, more than offset by foreign exchange movements of £112m and utilisation of £288m in relation to all classes of provisions. Other non-current liabilities decreased by £43m principally due to foreign exchange movements of £47m.

**Goodwill and other intangible assets**

Goodwill and intangibles decreased by £354m to £5,263m as at 31 March 2014. This decrease primarily relates to foreign exchange movements of £472m and software amortisation of £127m, partially offset by software additions of £179m.

**Net debt**

Net debt is the aggregate of cash and cash equivalents, current financial and other investments, borrowings, and derivative financial assets and liabilities. See further analysis with the consolidated cash flow statement on page 90.

**Property, plant and equipment**

Property, plant and equipment increased by £587m to £37,179m as at 31 March 2014. This was principally due to capital expenditure of £3,262m on the renewal and extension of our regulated networks, offset by foreign exchange movements of £1,244m, and £1,299m of

**Net pension and other post-retirement obligations**

A summary of the total UK and US assets and liabilities and the overall net IAS 19 (revised) accounting deficit is shown below:

	UK	US	Total
	£m	£m	£m
<b>Net plan liability</b>			
As at 1 April 2013 (as restated)	(1,169)	(2,328)	(3,497)
Exchange movements		186	186
Current service cost	(96)	(129)	(225)
Net interest cost	(47)	(81)	(128)



depreciation in the year.	Curtailments and settlements		214	214
	LIPA			
	Curtailments and settlements	(30)	(12)	(42)
	other			
<b>Investments and other non-current assets</b>	<b>Actuarial (losses)/gains</b>			
	on plan assets	(98)	283	185
	on plan liabilities	452	(152)	300
	Employer contributions	235	361	596
Investments in joint ventures and associates, financial and other investments and other non-current assets have decreased by £31m to £722m. This is principally due to changes in the fair value of our US commodity contract assets and available-for-sale investments.	<b>As at 31 March 2014</b>	<b>(753)</b>	<b>(1,658)</b>	<b>(2,411)</b>
	<b>Represented by:</b>			
	Plan assets		174	174
	Plan liabilities	(753)	(1,832)	(2,585)
		<b>(753)</b>	<b>(1,658)</b>	<b>(2,411)</b>
<b>Inventories and current intangible assets, and trade and other receivables</b>				

Inventories and current intangible assets, and trade and other receivables have decreased by £78m to £3,123m at 31 March 2014. This decrease is principally due to foreign exchange movements of £195m, partially offset by an increase in trade and other receivables of £120m mostly due to colder weather in the US in February and March 2014 compared with 2013 resulting in increased billings for commodity costs and customer usage.

### Trade and other payables

Trade and other payables have decreased by £20m to £3,031m due to favourable foreign exchange movements of £150m, partially offset by higher payables in the UK due in part to changes in payment terms with new Gas Distribution strategic partners and increased activity on the Western Link project.

### Current tax liabilities

Current tax liabilities have decreased by £63m to £168m as at 31 March 2014. This is primarily due to higher tax payments made in 2013/14 although these were partially offset by a larger current year tax charge.

The principal movements in net obligations during the year include a curtailment gain of £214m following the LIPA MSA transition, net actuarial gains of £485m and employer contributions of £596m. Net actuarial gains include actuarial gains on plan liabilities of £542m arising as a consequence of an increase in the UK real discount rate and the nominal discount rate in the US. This is partially offset by actuarial losses of £283m arising from increases in life expectancy in the US. Actuarial (losses)/gains on plan assets reflects the asset allocations in the different plans. In both the UK and US, returns on equities were above the assumed rate; however, UK government securities had negative returns and corporate bonds were close to nil.

Further information on our pension and other post-retirement obligations can be found in notes 22 and 29 to the consolidated financial statements. Details of the restatements made for IAS 19 (revised) can be found in note 1.

### Off balance sheet items

There were no significant off balance sheet items other than the contractual obligations shown in note 30 (b) to the consolidated financial statements, and the commitments and contingencies discussed in note 27.

### **Deferred tax liabilities**

Deferred tax liabilities have increased by £5m to £4,082m as at 31 March 2014. This was primarily due to the impact of the £172m deferred tax charge on actuarial gains (a £179m tax credit in 2012/13) being offset by the impact of the reduction in the UK statutory tax rate for future periods, foreign exchange movements and the reduction in prior year charges.

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

**This unaudited commentary does not form part of the financial statements.**

### **Provisions and other non-current liabilities**

Provisions (both current and non-current) and other non-current liabilities decreased by £158m to £3,486m as at 31 March 2014.

Total provisions decreased by £115m in the year. The underlying movements include additions of £230m primarily relating to a provision for the demolition of certain gas holders in the UK of £79m, restructuring provisions of £86m and other provisions

**Table of Contents**


## 90 National Grid Annual Report and Accounts 2013/14

**Consolidated cash flow statement**

for the years ended 31 March

	Notes	2014 £m	2013 (restated) <sup>1</sup> £m	2012 (restated) <sup>1</sup> £m
<b>Cash flows from operating activities</b>				
Total operating profit	2(b)	<b>3,735</b>	3,749	3,535
<b>Adjustments for:</b>				
Exceptional items, remeasurements and stranded cost recoveries	4	<b>(71)</b>	(110)	(44)
Depreciation, amortisation and impairment		<b>1,417</b>	1,361	1,282
Share-based payment charge		<b>20</b>	20	24
Changes in working capital		<b>(59)</b>	(410)	146
Changes in provisions		<b>(150)</b>	(53)	(116)
Changes in pensions and other post-retirement benefit obligations		<b>(323)</b>	(408)	(382)
Cash flows relating to exceptional items		<b>(150)</b>	(112)	(205)
Cash flows relating to stranded cost recoveries				247
Cash generated from operations		<b>4,419</b>	4,037	4,487
Tax paid		<b>(400)</b>	(287)	(259)
<b>Net cash inflow from operating activities</b>		<b>4,019</b>	3,750	4,228
<b>Cash flows from investing activities</b>				
Acquisition of investments		<b>(4)</b>	(14)	(13)

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Proceeds from sale of investments in subsidiaries		183	365
Purchases of intangible assets	(179)	(175)	(203)
Purchases of property, plant and equipment	(2,944)	(3,214)	(3,147)
Disposals of property, plant and equipment	4	32	24
Dividends received from joint ventures	38	21	26
Interest received	35	29	24
Net movements in short-term financial investments	1,720	(2,992)	553
<b>Net cash flow used in investing activities</b>	<b>(1,330)</b>	<b>(6,130)</b>	<b>(2,371)</b>
<b>Cash flows from financing activities</b>			
Proceeds from issue of treasury shares	14	19	13
Purchase of own shares	(5)	(6)	(4)
Proceeds received from loans	1,134	5,062	1,809
Repayment of loans	(2,192)	(1,210)	(1,914)
Net movements in short-term borrowings and derivatives	37	452	(49)
Interest paid	(901)	(792)	(749)
Dividends paid to shareholders	(1,059)	(810)	(1,006)
<b>Net cash flow (used in)/from financing activities</b>	<b>(2,972)</b>	<b>2,715</b>	<b>(1,900)</b>
<b>Net (decrease)/increase in cash and cash equivalents</b>	26(a)	(283)	335
Exchange movements		(26)	14
Net cash and cash equivalents at start of year		648	299
<b>Net cash and cash equivalents at end of year<sup>2</sup></b>	18	<b>339</b>	<b>299</b>

1. See note 1 on page 92.

2. Net of bank overdrafts of £15m (2013: £23m; 2012: £33m).

**Table of Contents**

Strategic Report	Corporate Governance	<b>Financial Statements</b>	Additional Information	91
------------------	----------------------	-----------------------------	------------------------	----

**Unaudited commentary on consolidated cash flow statement**

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

receivables increased due to colder weather in the US in February and March 2014, cash outflows relating to exceptional items were £38m higher due to reorganisation in the UK and LIPA MSA transition costs in the US.

**Net capital expenditure**

Net capital expenditure in the year of £3,119m was £238m lower than the prior year. This was a result of lower spend in our UK regulated businesses, the impact of the weaker dollar, and reduced capital spend on the US enterprise resource system in 2013/14.

**Reconciliation of cash flow to net debt**

	2014 £m	2013 £m
Cash generated from operations	4,419	4,037
Net capital expenditure	(3,119)	(3,357)
Business net cash flow	1,300	680
Net interest paid	(866)	(763)
Tax paid	(400)	(287)
Net acquisitions and disposals	(4)	169
Dividends paid	(1,059)	(810)

**Net interest paid**

Net interest paid in 2013/14 was £866m, £103m higher than 2012/13, due to higher average net debt levels.

Other cash movements	47	34
Non-cash movements	1,221	(855)
<b>Decrease/(increase) in net debt</b>	<b>239</b>	<b>(1,832)</b>
Opening net debt	<b>(21,429)</b>	(19,597)
<b>Closing net debt</b>	<b>(21,190)</b>	(21,429)

**Tax paid**

Tax paid in the year to 31 March 2014 was £400m, £113m higher than prior year. This reflected higher tax payments in the UK on higher taxable profits.

**Cash generated from operations****Cash generated from operations**

£m

Cash flows from our operations are largely stable when viewed over the longer term. 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 intra-year 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 significant cash flow swings from year to year. Changes in volumes in the US, for example as a consequence of abnormally mild or extreme weather can affect cash flows, particularly in the winter months.

For the year ended 31 March 2014, cash flow from operations increased by £382m to £4,419m.

Adjusted operating profit before depreciation, amortisation and impairment was £81m higher year on year. Changes in working capital improved by £351m over the prior year, principally in the US due to the collection of receivables from LIPA relating to Superstorm Sandy. Partially offsetting this improvement,

**Net acquisitions and disposals**

There were no material acquisitions or disposals in the year. The year ended 31 March 2013 included proceeds received on the disposal of our gas and electricity businesses in New Hampshire in the US.

**Dividends paid**

Dividends paid in the year ended 31 March 2014 amounted to £1,059m. This was £249m higher than 2012/13, reflecting the 4% increase in the final dividend for the year ended 31 March 2013 paid in August 2013, together with a lower average scrip dividend take-up in the year. Given the relatively high scrip uptake for the dividend paid in August 2013, no scrip option was offered for the interim dividend paid in January 2014.

**Other cash movements**

Other cash flows principally arise from dividends from joint ventures and movements in treasury shares.

**Non-cash movements**

The non-cash movements are predominantly due to the change in foreign exchange arising on net debt

held in currencies other than sterling. In the year ended 31 March 2014, the dollar weakened from \$1.52 at 31 March 2013 to \$1.67 at 31 March 2014. This has caused a reduction in the sterling value of net debt.

Other non-cash movements are from changes in fair values of financial assets and liabilities and interest accretions and accruals.

### **Net debt**

#### **Net debt at 31 March**

£m

**This unaudited commentary does not form part of the financial statements.**

**Table of Contents**

## 92 National Grid Annual Report and Accounts 2013/14

**Notes to the consolidated****financial statements**

## analysis of items in the primary statements

**1. Adoption of IAS 19 (revised) Employee benefits**

This note sets out the impact that the required adoption of IAS 19 (revised) Employee benefits has had on our previously reported results. It provides details of the originally reported and the restated figures.

During the year, the Group adopted IAS 19 (revised) Employee benefits. The adoption constitutes a change in accounting policy and therefore the comparative information has been restated.

The standard requires past service costs to be recognised immediately in profit or loss and all actuarial gains and losses are recognised in other comprehensive income as they occur. The standard also replaces the interest cost on the DB obligation and the expected return on plan assets with a net interest cost based on the net DB asset or liability and the discount rate, measured at the beginning of the year. The impact on the Group for the years ended 31 March 2013 and 31 March 2012 is set out in the table below:

		Restatement for		As restated	
As previously reported		IAS 19 (revised)		31 March	31 March
31 March	31 March	31 March	31 March	31 March	31 March
	2012		2012	2013	



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	2013	£m	2013	£m	£m	2012
	£m		£m			£m
<b>Consolidated income statement</b>						
Operating costs	(10,605)	(10,293)	(5)	(4)	(10,610)	(10,297)
Total operating profit	3,754	3,539	(5)	(4)	3,749	3,535
Total finance income	1,252	1,301	(1,222)	(1,273)	30	28
Total finance costs	(2,104)	(2,288)	1,018	1,100	(1,086)	(1,188)
Total profit before tax	2,920	2,559	(209)	(177)	2,711	2,382
Total taxation	(624)	(521)	67	58	(557)	(463)
Profit for the year	2,296	2,038	(142)	(119)	2,154	1,919
<b>Consolidated statement of financial position</b>						
Deferred tax liabilities	(4,076)	(3,738)	(1)	2	(4,077)	(3,736)
Pensions and other post-retirement benefit obligations	(3,694)	(3,088)	2	(5)	(3,692)	(3,093)
Total non-current liabilities	(37,027)	(31,998)	1	(3)	(37,026)	(32,001)
Total liabilities	(44,472)	(38,089)	1	(3)	(44,471)	(38,092)
Retained earnings	13,132	12,297	1	(3)	13,133	12,294
Total equity	10,233	9,246	1	(3)	10,234	9,243
<b>Consolidated statement of other comprehensive income</b>						
Remeasurements of net retirement benefit obligations	(930)	(1,325)	216	185	(714)	(1,140)
Tax on items that will never be reclassified to	249	403	(70)	(61)	179	342

profit or loss							
Total comprehensive income for the year	1,769	1,151	4	5	<b>1,773</b>	<b>1,156</b>	
<b>Consolidated statement of changes in equity</b>							
Other comprehensive income	(527)	(887)	146	124	<b>(381)</b>	<b>(763)</b>	
Total comprehensive income for the year	1,769	1,151	4	5	<b>1,773</b>	<b>1,156</b>	
<b>Consolidated cash flow statement</b>							
Pensions and other post-retirement benefit obligations	(413)	(386)	5	4	<b>(408)</b>	<b>(382)</b>	
EPS basic	62.6p	55.6p	(4.8)p	(4.0)p	<b>57.8p</b>	<b>51.6p</b>	
EPS diluted	62.3p	55.4p	(4.8)p	(4.1)p	<b>57.5p</b>	<b>51.3p</b>	

The restated amounts for EPS in the above table reflect the impact of additional shares issued as scrip dividends. The effect of the change in accounting policy on the statement of cash flows was immaterial, with no impact on the cash position at any of the reporting dates.

We have revised our pension and other post-retirement benefit obligations disclosures in notes 22 and 29 to provide greater clarity by separately presenting our UK and US pension plans due to their different risk profiles.

**Table of Contents**

Strategic Report	Corporate Governance	<b>Financial Statements</b>	Additional Information	93
------------------	----------------------	-----------------------------	------------------------	----

**2. Segmental analysis**

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

**Our strategy in action**

We own a portfolio of businesses that range from cash generative developed assets with minimal investment requirements (such as National Grid Metering, included within Other activities) to businesses with high levels of investment and growth (such as UK Electricity Transmission).

We generate 95% of our revenue from our regulated businesses in the UK and US. We work with our regulators to obtain agreements that balance the risks we face with the opportunity to deliver reasonable returns for our investors. When investing in non-regulated businesses we aim to leverage our core capabilities to deliver higher returns for investors.

Our regulated businesses earn revenue for the transmission, distribution and generation services they have provided during the year. In any one year, the revenue recognised may differ from that allowed under our regulatory agreements and any such timing differences are adjusted through future prices. Our non-regulated businesses earn revenue in line with their contractual terms.

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Revenue primarily represents the sales value derived from the generation, transmission and distribution of energy, together with the sales value derived from the provision of other services to customers and, previously, recovery of US stranded costs during the year. It excludes value added (sales) tax and intra-group sales.

Revenue includes an assessment of unbilled energy and transportation services supplied to customers between the date of the last meter reading and the year end. This is estimated based on historical consumption and weather patterns.

Where revenue exceeds the maximum amount permitted by regulatory agreement and adjustments will be made to future prices to reflect this over-recovery, no liability is recognised, as such an adjustment relates to the provision of future services. Similarly no asset is recognised where a regulatory agreement permits adjustments to be made to future prices in respect of an under-recovery.

US stranded costs were various generation-related costs incurred prior to the divestiture of generation assets beginning in the late 1990s and costs of legacy contracts that are being recovered from customers. The recovery of stranded costs and other amounts allowed to be collected from customers under regulatory arrangements was recognised in the period in which these amounts were recoverable from customers. The recovery of stranded costs was substantially completed at 31 March 2012.

We present revenue and the results of the business analysed by operating segment, based on the information the Board of Directors uses internally for the purposes of evaluating the performance of operating segments and determining resource allocation between operating segments. The Board is National Grid's chief operating decision-making body (as defined by IFRS 8 Operating Segments) and assesses the performance of operations principally on the basis of operating profit before exceptional items, remeasurements and stranded cost recoveries (see note 4).

Following the commencement of new RIIO regulatory arrangements in the UK, we have changed the way in which we report our operational and financial performance. We have reviewed our segmental disclosure for the year ended 31 March 2014 with the separation of our UK Transmission segment into two new segments: UK Electricity Transmission and UK Gas Transmission. We have also moved the Great Britain-France electricity interconnector from UK Electricity Transmission to Other activities. The information given in this note for the years ended 31 March 2013 and 2012 has been restated to provide a like-for-like comparison.

**Table of Contents**


**94 National Grid Annual Report and Accounts 2013/14****Notes to the consolidated****financial statements continued****2. Segmental analysis continued**

The following table describes the main activities for each operating segment:

UK Electricity Transmission	High voltage electricity transmission networks in Great Britain.
UK Gas Transmission	The gas transmission network in Great Britain and UK LNG storage activities.
UK Gas Distribution	Four of the eight regional networks of Great Britain's gas distribution system.
US Regulated	Gas distribution networks, electricity distribution networks and high voltage electricity transmission networks in New York and New England (including EnergyNorth and Granite State up to the date they were sold on 3 July 2012) and electricity generation facilities in New York and Massachusetts.

Other activities primarily relate to non-regulated businesses and other commercial operations not included within the above segments, including: the Great Britain-France electricity interconnector; UK-based gas metering activities; UK property management; a UK LNG import terminal; US LNG operations; US unregulated transmission pipelines; together with corporate activities.

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Sales between operating segments are priced considering the regulatory and legal requirements to which the businesses are subject. The analysis of revenue by geographical area is on the basis of destination. There are no material sales between the UK and US geographical areas.

**(a) Revenue**

	2014			2013			2012		
	Total sales	Sales between segments	Sales to third parties	Total sales	Sales between segments	Sales to third parties	Total sales	Sales between segments	Sales to third parties
	£m	£m	£m	(restated) <sup>1</sup>	(restated) <sup>1</sup>	(restated) <sup>1</sup>	(restated) <sup>1</sup>	(restated) <sup>1</sup>	(restated) <sup>1</sup>
	£m	£m	£m	£m	£m	£m	£m	£m	£m
<b>Operating segments</b>									
<b>UK</b>									
Electricity Transmission	3,387	(14)	3,373	3,110	(15)	3,095	2,811	(16)	2,795
UK Gas Transmission	941	(104)	837	1,118	(89)	1,029	983	(8)	975
UK Gas Distribution	1,898	(49)	1,849	1,714	(47)	1,667	1,605	(52)	1,553
US Regulated	8,040		8,040	7,918		7,918	7,795		7,795
Other activities	736	(26)	710	678	(28)	650	744	(30)	714
	<b>15,002</b>	<b>(193)</b>	<b>14,809</b>	14,538	(179)	14,359	13,938	(106)	13,832
Total excluding stranded cost recoveries			<b>14,809</b>			14,359			13,553
Stranded cost recoveries									279
			<b>14,809</b>			14,359			13,832
<b>Geographical areas</b>									
UK			<b>6,759</b>			6,421			6,000
US			<b>8,050</b>			7,938			7,832

**14,809**

14,359

13,832

1. Restated to reflect the changes in operating segment presentation as described on page 93.

**Table of Contents**

Strategic Report	Corporate Governance	<b>Financial Statements</b>	Additional Information	95
------------------	----------------------	-----------------------------	------------------------	----

**2. Segmental analysis continued****(b) Operating profit**

A reconciliation of the operating segments' measure of profit to total profit before tax is provided below. Further details of the exceptional items, remeasurements and stranded cost recoveries are provided in note 4.

	Before exceptional items, remeasurements and stranded cost recoveries			After exceptional items, remeasurements and stranded cost recoveries		
	2013	2012		2013	2012	
	2014	(restated) <sup>1</sup>	(restated) <sup>1</sup>	2014	(restated) <sup>1</sup>	(restated) <sup>1</sup>
	£m	£m	£m	£m	£m	£m
<b>Operating segments</b>						
UK Electricity Transmission	<b>1,087</b>	1,049	876	<b>1,027</b>	1,020	876
UK Gas Transmission	<b>417</b>	531	453	<b>406</b>	517	453
UK Gas Distribution	<b>904</b>	794	763	<b>780</b>	763	739
US Regulated	<b>1,125</b>	1,254	1,192	<b>1,388</b>	1,438	1,156
Other activities	<b>131</b>	11	207	<b>134</b>	11	311
	<b>3,664</b>	3,639	3,491	<b>3,735</b>	3,749	3,535
<b>Geographical areas</b>						
UK	<b>2,723</b>	2,530	2,347	<b>2,531</b>	2,456	2,351
US	<b>941</b>	1,109	1,144	<b>1,204</b>	1,293	1,184
	<b>3,664</b>	3,639	3,491	<b>3,735</b>	3,749	3,535
<b>Reconciliation to profit before tax</b>						



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Operating profit	<b>3,664</b>	3,639	3,491	<b>3,735</b>	3,749	3,535
Finance income	<b>36</b>	30	28	<b>36</b>	30	28
Finance costs	<b>(1,144)</b>	(1,154)	(1,118)	<b>(1,051)</b>	(1,086)	(1,188)
Share of post-tax results of joint ventures and associates	<b>28</b>	18	7	<b>28</b>	18	7
<b>Profit before tax</b>	<b>2,584</b>	2,533	2,408	<b>2,748</b>	2,711	2,382

1. See note 1 on page 92. Also restated to reflect the changes in operating segment presentation as described on page 93.

**(c) Capital expenditure, depreciation and amortisation**

	Capital expenditure			Depreciation and amortisation		
		2013	2012		2013	2012
		(restated) <sup>1</sup>	(restated) <sup>1</sup>		(restated) <sup>1</sup>	(restated) <sup>1</sup>
	<b>2014</b>			<b>2014</b>		
	<b>£m</b>	£m	£m	<b>£m</b>	£m	£m
<b>Operating segments</b>						
UK Electricity Transmission	<b>1,381</b>	1,430	1,153	<b>(343)</b>	(323)	(281)
UK Gas Transmission	<b>181</b>	249	235	<b>(172)</b>	(162)	(146)
UK Gas Distribution	<b>480</b>	666	645	<b>(271)</b>	(261)	(251)
US Regulated	<b>1,219</b>	1,124	1,052	<b>(419)</b>	(430)	(411)
Other activities	<b>180</b>	217	290	<b>(211)</b>	(185)	(183)
	<b>3,441</b>	3,686	3,375	<b>(1,416)</b>	(1,361)	(1,272)
<b>Geographical areas</b>						
UK	<b>2,155</b>	2,471	2,217	<b>(938)</b>	(902)	(849)
US	<b>1,286</b>	1,215	1,158	<b>(478)</b>	(459)	(423)
	<b>3,441</b>	3,686	3,375	<b>(1,416)</b>	(1,361)	(1,272)
<b>By asset type</b>						
Property, plant and equipment	<b>3,262</b>	3,511	3,172	<b>(1,289)</b>	(1,260)	(1,193)
Non-current intangible assets	<b>179</b>	175	203	<b>(127)</b>	(101)	(79)
	<b>3,441</b>	3,686	3,375	<b>(1,416)</b>	(1,361)	(1,272)

1. Restated to reflect the changes in operating segment presentation as described on page 93.

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Total non-current assets other than derivative financial assets, financial and other investments, deferred tax assets and pension assets located in the UK and US were £24,531m and £18,349m respectively as at 31 March 2014 (31 March 2013: UK £23,344m, US £19,340m; 31 March 2012: UK £21,793m, US £17,666m).

**Table of Contents**

## 96 National Grid Annual Report and Accounts 2013/14

**Notes to the consolidated****financial statements** continued**Unaudited commentary on the results of our principal operations by segment**

We have summarised the results of our principal operating segments here by segment to provide direct reference to the results as disclosed in note 2. This analysis has been performed based on operating profit before exceptional items, remeasurements and stranded cost recoveries as set out in note 2 (b).

**UK Electricity Transmission**

For the year ended 31 March 2014, revenue in the UK Electricity Transmission segment increased by £277m, and adjusted operating profit increased by £38m.

**US Regulated**

Revenue in our US Regulated businesses was £122m higher at £8,040m, and adjusted operating profit fell by £129m to £1,125m.

The weaker dollar reduced operating profit in the year by £38m. Excluding the impact of foreign exchange, net regulated income fell by £52m, principally due to the end of deferral income recoveries for Niagara Mohawk at 31 March 2013. Timing differences added another £29m profit compared with prior year. Regulated controllable costs increased by £89m at constant currency as a result of inflation and wage increases, higher insurance costs post Superstorm Sandy, and cost true-ups identified during the implementation of new financial systems. Other operating costs (excluding major storms) increased by £61m at constant currency

Net regulated income after pass-through costs was £170m higher, reflecting increases in allowed revenues under the new RIIO regulatory framework. This was partially offset by under-recoveries of revenue in the year of £60m compared with over-recoveries of £29m in the prior year. Regulated controllable costs were £27m higher due to inflation, legal fees and one-off credits in the prior year. Depreciation and amortisation was £20m higher reflecting the continued capital investment programme (investment in the year was £1,381m). Other costs were £4m lower than prior year.

due to the higher cost of non-major storm remediation, higher property taxes and depreciation of the new US enterprise resource system.

There were no major storms affecting our operations in the year ended 31 March 2014. In 2012/13, two major storms in the US, Superstorm Sandy and Storm Nemo, reduced operating profit within US Regulated by £82m at constant currency.

### **UK Gas Transmission**

Revenue in the UK Gas Transmission segment decreased by £177m in 2013/14 to £941m and adjusted operating profit fell by £114m to £417m.

Our capital investment programme continues in the US, with a further £1,219m invested in 2013/14, including gas leak reduction programmes and gas growth and connection spend.

Net regulated income after pass-through costs was £80m lower, with lower permit income than prior year under the new RIIO arrangements. In addition, under-recoveries in the year of £21m compared with over-recoveries last year of £17m, gave rise to an adverse timing movement of £38m. Depreciation and amortisation was £10m higher due to investment, with £181m invested in the year. Partially offsetting these, other operating costs were £14m lower.

### **Other activities**

Revenue in Other activities increased by £58m to £736m in the year ended 31 March 2014. Adjusted operating profit was £120m higher at £131m.

### **UK Gas Distribution**

UK Gas Distribution revenue increased by £184m in the year to £1,898m, and adjusted operating profit increased to £904m from £794m in 2012/13.

There was no repeat of the major storm cost of £51m incurred in our insurance captive in the prior year due to Superstorm Sandy. Operating profit in the French interconnector was £62m higher as a result of strong auction revenues this year. In our other non-regulated businesses, adjusted operating profit was £7m higher due to improved results in our UK metering business and insurance captive, partially offset by higher costs associated with the stabilisation of the new US enterprise resource system.

Net regulated income after pass-through costs was £96m higher, reflecting increases in allowed revenues under the new RIIO regulatory framework. Timing differences added another £39m, with £29m over-recoveries in 2013/14, compared with a £10m under-recovery in the prior

Capital expenditure in our Other activities was £37m lower at £180m, principally reflecting reduced capital spend on the new US enterprise resource system.

year. Partially offsetting these, regulated controllable costs were £14m higher primarily due to inflation. Depreciation and amortisation was £10m higher reflecting the continued capital investment programme (investment in the year was £480m). Other costs were £1m higher than prior year.

**This unaudited commentary does not form part of the financial statements.**

**Table of Contents**

Strategic Report	Corporate Governance	Financial Statements	Additional Information	97
------------------	----------------------	----------------------	------------------------	----

**3. Operating costs**

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

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

	Before exceptional items, remeasurements and stranded cost recoveries			Exceptional items, remeasurements and stranded cost recoveries			Total		
	2014	2013	2012	2014	2013	2012	2014	2013	
	(restated) <sup>1</sup>	(restated) <sup>1</sup>	(restated) <sup>1</sup>	(restated) <sup>1</sup>	(restated) <sup>1</sup>	(restated) <sup>1</sup>	(restated) <sup>1</sup>	(restated) <sup>1</sup>	
	£m	£m	£m	£m	£m	£m	£m	£m	
Depreciation and amortisation	<b>1,416</b>	1,361	1,267			5	<b>1,416</b>	1,361	1,272
Payroll costs	<b>1,373</b>	1,434	1,381	<b>59</b>	22	82	<b>1,432</b>	1,456	1,463
Purchases of electricity	<b>1,513</b>	1,251	1,356	<b>(49)</b>	(111)	89	<b>1,464</b>	1,140	1,444
Purchases of gas	<b>1,722</b>	1,384	1,518	<b>33</b>	(69)	5	<b>1,755</b>	1,315	1,523

Rates and property taxes	<b>963</b>	969	955				<b>963</b>	969	955
Balancing Services Incentive Scheme	<b>872</b>	805	818				<b>872</b>	805	818
Payments to other UK network owners	<b>630</b>	487	407				<b>630</b>	487	407
Other	<b>2,656</b>	3,029	2,360	<b>(114)</b>	48	54	<b>2,542</b>	3,077	2,414
	<b>11,145</b>	10,720	10,062	<b>(71)</b>	(110)	235	<b>11,074</b>	10,610	10,297

Operating costs include:									
Inventory consumed							<b>422</b>	389	365
Operating leases							<b>115</b>	109	95
Research and development expenditure							<b>12</b>	15	15

. See note 1 on page 92.

#### a) Payroll costs

		2013	2014	2015
		(restated) <sup>1</sup>	(restated) <sup>1</sup>	(restated) <sup>1</sup>
	£m	£m	£m	£m
Wages and salaries <sup>2</sup>	<b>1,575</b>	1,596	1,560	1,560
Social Security costs	<b>126</b>	120	111	111
Pension costs (note 22)	<b>245</b>	231	231	231
Share-based payment	<b>20</b>	20	20	20
Severance costs (excluding pension costs)	<b>30</b>	16	30	30

Less: payroll costs capitalised	<b>1,996</b>	1,983	1,97
	<b>(564)</b>	(527)	(50)
	<b>1,432</b>	1,456	1,46

. See note 1 on page 92.

2. Included within wages and salaries are US other post-retirement benefit costs of £44m (2013: £43m; 2012: £60m). For further information refer to note 22 on page 122.

### b) Number of employees

	31 March 2014 Number	Monthly average 2014 Number	31 March 2013 Number <sup>1</sup>	Monthly average 2013 Number <sup>1</sup>	31 March 2012 Number <sup>1</sup>	Monthly average 2012 Number <sup>1</sup>
UK	<b>9,693</b>	<b>9,641</b>	9,990	9,816	9,696	9,76
US	<b>14,216</b>	<b>15,094</b>	15,438	15,555	15,843	16,08
	<b>23,909</b>	<b>24,735</b>	25,428	25,371	25,539	25,84

. Comparatives have been re-presented on a basis consistent with the current year classification.

The vast majority of employees in the US are either directly or indirectly employed in the transmission, distribution and generation of electricity or the distribution of gas, while those in the UK are either directly or indirectly employed in the transmission and distribution of gas or the transmission of electricity. At 31 March 2014, there were 2,044 (2013: 2,151; 2012: 2,357) employees in other operations, excluding shared services.



**Table of Contents**


## 98 National Grid Annual Report and Accounts 2013/14

**Notes to the consolidated****financial statements** continued**3. Operating costs** continued**(c) Key management compensation**

	<b>2014</b>	2013	2012
	<b>£m</b>	£m	£m
Short-term employee benefits	<b>9</b>	8	10
Post-employment benefits	<b>1</b>	3	6
Share-based payment	<b>5</b>	5	5
	<b>15</b>	16	21

Key management compensation relates to the Board of Directors, including the Executive Directors and Non-executive Directors for the years presented.

**(d) Directors' emoluments**

Details of Directors' emoluments are contained in the audited part of the Remuneration Report, which forms part of these financial statements.

**(e) Auditors' remuneration**

Auditors' remuneration is presented below in accordance with the requirements of the UK Companies Act 2006 and the principal accountant fees and services disclosure requirements of Item 16C of Form 20-F.

	2014	2013	2012
	£m	£m	£m
<b>Audit fees<sup>1</sup> payable to the parent Company's auditors and their associates in respect of:</b>			
Audit of the parent Company's individual and consolidated financial statements	0.9	1.1	1.1
The auditing of accounts of any associate of the Company	7.8	6.0	5.2
Other services supplied <sup>2</sup>	2.3	2.7	2.3
	<b>11.0</b>	9.8	8.6
<b>Total other services<sup>3</sup></b>			
<b>Tax fees<sup>4</sup></b>			
Tax compliance services	0.5	0.5	0.5
Tax advisory services	0.3	0.3	0.2
<b>All other fees<sup>5</sup></b>			
Other assurance services	0.1	0.1	0.3
Services relating to corporate finance transactions not covered above		0.3	0.2
Other non-audit services not covered above	0.8	1.1	2.6
	<b>1.7</b>	2.3	3.8
<b>Total auditors' remuneration</b>	<b>12.7</b>	12.1	12.4

1. Audit fees in each year represent fees for the audit of the Company's financial statements and regulatory reporting for the years ended 31 March 2014, 2013 and 2012, and the review of interim financial statements for the six month periods ended 30 September 2013, 2012 and 2011 respectively.

2. Other services supplied represent fees payable for services in relation to other statutory filings or engagements that are required to be carried out by the auditors. In particular, this includes fees for reports under section 404 of the US Public Company Accounting Reform and Investor Protection Act of 2002 (Sarbanes-Oxley) and audit reports on regulatory returns.

3. There were no audit related fees as described in Item 16C(b) of Form 20-F.

4. Tax fees include amounts charged for tax compliance, tax advice and tax planning. Total tax fees for the year ended 31 March 2014 were £0.8m (2013: £0.8m; 2012: £0.7m).

5. All other fees include amounts relating to the review of US pensions and other post-retirement benefits census data and sundry services, all of which have been subject to approval by the Audit

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Committee. Total other fees for the year ended 31 March 2014 were £0.9m (2013: £1.5m; 2012: £3.1m).

In addition, fees of £0.1m were incurred in 2014 in relation to the audits of the pension schemes of the Company (2013: £0.1m; 2012: £0.1m).

Subject to the Company's Articles of Association and the Companies Act 2006, the Audit Committee is solely and directly responsible for the approval of the appointment, reappointment, compensation and oversight of the Company's independent auditors. It is our policy that the Audit Committee must approve in advance all non-audit work to be performed by the independent auditors to ensure that the service will not compromise auditor independence. Certain services are prohibited from being performed by the external auditors under the Sarbanes-Oxley Act 2002.

**Table of Contents**

Strategic Report	Corporate Governance	<b>Financial Statements</b>	Additional Information	99
------------------	----------------------	-----------------------------	------------------------	----

**4. Exceptional items, remeasurements and stranded cost recoveries**

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

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

Items of income or expense that are considered by management for designation as exceptional items include such items as significant restructurings, write-downs or impairments of non-current assets, significant changes in environmental or decommissioning provisions, integration of acquired businesses, gains or losses on disposals of businesses or investments and debt redemption costs as a consequence of transactions such as significant disposals or issues of equity.

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Costs arising from restructuring programmes include redundancy costs. Redundancy costs are charged to the income statement in the year in which a commitment is made to incur the costs and the main features of the restructuring plan have been announced to affected employees.

Remeasurements comprise gains or losses recorded in the income statement arising from changes in the fair value of commodity contracts and of derivative financial instruments to the extent that hedge accounting is not achieved or is not effective. These fair values increase or decrease because of changes in commodity and financial indices and prices over which we have no control.

Stranded cost recoveries represent the recovery, through charges to electricity customers in upstate New York and New England, of historical generation-related costs, related to generation assets that are no longer owned by National Grid. Such costs have been recovered from customers as permitted by regulatory agreements, with substantially all having been recovered by 31 March 2012.

**Table of Contents****100 National Grid Annual Report and Accounts 2013/14****Notes to the consolidated****financial statements continued****4. Exceptional items, remeasurements and stranded cost recoveries continued**

	<b>2014</b>	2013	2012
	<b>£m</b>	£m	£m
<b>Included within operating profit</b>			
Exceptional items			
Restructuring costs <sup>1</sup>	<b>(136)</b>	(87)	(101)
Gas holder demolition costs <sup>2</sup>	<b>(79)</b>		
LIPA MSA transition <sup>3</sup>	<b>254</b>		(64)
Other <sup>4</sup>	<b>16</b>		1
Environmental charges			(55)
Net gain on disposal of businesses <sup>5</sup>		3	97
	<b>55</b>	(84)	(122)
Remeasurements – commodity contracts	<b>16</b>	180	(94)
Stranded cost recoveries <sup>7</sup>		14	260
	<b>71</b>	110	44
<b>Included within finance costs</b>			
Remeasurements – net gains/(losses) on derivative financial instruments <sup>8</sup>	<b>93</b>	68	(70)
	<b>93</b>	68	(70)

<b>Total included within profit before tax</b>	<b>164</b>	178	(26)
<b>Included within taxation</b>			
Exceptional credits/(charges) arising on items not included in profit before tax			
Deferred tax credit arising on the reduction in the UK corporation tax rate <sup>9</sup>	<b>398</b>	128	242
Deferred tax charge arising from an increase in US state income tax rates <sup>10</sup>	<b>(8)</b>		
Tax on exceptional items	<b>(57)</b>	31	54
Tax on remeasurements <sup>6,8</sup>	<b>(36)</b>	(92)	42
Tax on stranded cost recoveries		(5)	(104)
	<b>297</b>	62	234
<b>Total exceptional items, remeasurements and stranded cost recoveries after tax</b>	<b>461</b>	240	208
<b>Analysis of total exceptional items, remeasurements and stranded cost recoveries after tax</b>			
Exceptional items after tax	<b>388</b>	75	174
Remeasurements after tax	<b>73</b>	156	(122)
Stranded cost recoveries after tax		9	156
<b>Total</b>	<b>461</b>	240	208

1. Restructuring costs for the period of £136m related to the continued restructuring of our UK operations in preparedness to deliver RIIO, other transformation-related initiatives in the UK and US and an associated software impairment for licences that will no longer be used.

Restructuring costs for 2013 included: costs related to the restructuring of our UK operations of £66m in preparedness for delivering RIIO; costs for transformation-related initiatives in the UK and US of £31m; and a credit of £10m for the release of restructuring provisions in the UK recognised in prior years. For the year ended 31 March 2012, restructuring costs included: costs for the restructuring of our US operations of £58m, which included severance costs and pension and other post-retirement curtailment gains and losses; costs for transformation-related initiatives of £54m; and a credit of £11m for the release of restructuring provisions in the UK recognised in prior years.

2. A provision of £79m (2013: £nil) has been made for the demolition of certain non-operational gas holders in the UK.

3. A net gain of £254m (2013: £nil) has been recognised in the year ended 31 March 2014. This includes a pension curtailment and settlement gain of £214m for employees who transferred to a new employer following the cessation of the Management Services Agreement (MSA) with LIPA on 31 December 2013. There was also a gain of £142m following the extinguishment of debt obligations of £98m and a £56m cash payment to be received, in compensation for the Company forgiving a historic pension receivable and carrying charges. These gains were offset by transition costs and other provisions incurred to effect the transition. For the year ended 31 March 2012, an impairment charge of £64m was recognised, representing intangibles (originally recognised on the acquisition of KeySpan) related to our LIPA MSA contract. This amount was previously disclosed as impairment charges and related costs.

4. During the year ended 31 March 2014, £16m (2013: £nil) was received following the sale to a third party of a settlement award which arose as a result of a legal ruling in 2008. For the year ended 31 March 2012, an amortisation charge of £5m in relation to acquisition-related intangibles was offset by a release of £6m of unutilised provisions in our UK metering business.

5. For the year ended 31 March 2013, we recognised a gain of £3m on the disposal of two subsidiaries in New Hampshire. During the year ended 31 March 2012, we sold two other subsidiaries resulting in a gain on disposal of £72m. We also recognised gains of £25m in relation to disposals of businesses in prior years, representing the release of various unutilised provisions.

6. Remeasurements commodity contracts represent mark-to-market movements on certain physical and financial commodity contract obligations in the US. These contracts primarily relate to the forward purchase of energy for supply to customers, or to the economic hedging thereof, that are required to be measured at fair value and that do not qualify for hedge accounting. Under the existing rate plans in the US, commodity costs are recoverable from customers although the timing of recovery may differ from the pattern of costs incurred.

7. For the year ended 31 March 2013, stranded cost recoveries of £14m substantially represented the release of an unutilised provision recognised in a prior period. For the year ended 31 March 2012, stranded cost recoveries on a pre-tax basis consisted of revenue of £279m offset by operating costs of £19m. This represented the recovery of some of our historical investments in generating plants that were divested as part of the restructuring and wholesale power deregulation process in New England and New York during the 1990s.

8. Remeasurements net gains/(losses) on derivative financial instruments comprise gains/(losses) arising on derivative financial instruments reported in the income statement. These exclude gains and losses for which hedge accounting has been effective, which have been recognised directly in other comprehensive income or which are offset by adjustments to the carrying value of debt. The tax charge in the year includes a credit of £nil (2013: £1m; 2012: £1m) in respect of prior years.



9. The exceptional tax credit arises from reductions in the UK corporation tax rate, from 23% to 21% applicable from 1 April 2014, and a further reduction from 21% to 20% applicable from 1 April 2015. The rate reductions were enacted in the Finance Act 2013. Other UK tax legislation also reduced the UK corporation tax rate in the prior periods (2013: from 24% to 23%; 2012: from 26% to 24%). These reductions have resulted in a decrease in deferred tax liabilities.

10. The exceptional tax charge arises from a net increase in US state income tax rates. Effective from 1 April 2014, the state income tax rate for Massachusetts regulated utilities increased from 6.5% to 8% and, effective from 1 April 2016, the state income tax rate for New York will decrease from 7.1% to 6.5%.

**Table of Contents**

Strategic Report	Corporate Governance	<b>Financial Statements</b>	Additional Information	101
------------------	----------------------	-----------------------------	------------------------	-----

**5. Finance income and costs**

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

	2014	2013	2012
	£m	(restated) <sup>1</sup>	(restated) <sup>1</sup>
		£m	£m
<b>Finance income</b>			
Interest income on financial instruments			
Bank deposits and other financial assets	22	20	19
Gains on disposal of available-for-sale investments	14	10	9
<b>Finance income</b>	<b>36</b>	30	28
<b>Finance costs</b>			
Net interest on pensions and other post-retirement benefit obligations	(128)	(135)	(103)
Interest expense on financial liabilities held at amortised cost			
Bank loans and overdrafts	(61)	(65)	(84)
Other borrowings	(1,109)	(1,052)	(1,105)
Derivatives	79	51	122
Unwinding of discounts on provisions	(73)	(75)	(72)

Less: interest capitalised <sup>2</sup>	<b>148</b>	122	124
<b>Finance costs before exceptional items and remeasurements</b>	<b>(1,144)</b>	(1,154)	(1,118)
<b>Remeasurements</b>			
Net gains/(losses) on derivative financial instruments included in remeasurements <sup>3</sup> :			
Ineffectiveness on derivatives designated as:			
Fair value hedges <sup>4</sup>	<b>22</b>	17	9
Cash flow hedges	<b>4</b>	(7)	14
Net investment hedges	<b>38</b>	(26)	(15)
Net investment hedges undesignated forward rate risk	<b>(7)</b>	26	39
Derivatives not designated as hedges or ineligible for hedge accounting	<b>36</b>	58	(117)
<b>Exceptional items and remeasurements included within finance costs (note 4)</b>	<b>93</b>	68	(70)
<b>Finance costs</b>	<b>(1,051)</b>	(1,086)	(1,188)
<b>Net finance costs</b>	<b>(1,015)</b>	(1,056)	(1,160)

1. See note 1 on page 92.

2. Interest on funding attributable to assets in the course of construction was capitalised during the year at a rate of 4.5% (2013: 4.4%; 2012: 5.2%).

3. Includes a net foreign exchange gain on financing activities of £268m (2013: £32m loss; 2012: £280m gain) offset by foreign exchange gains and losses on derivative financial instruments measured at fair value.

4. Includes a net loss on instruments designated as fair value hedges of £183m (2013: £67m gain; 2012: £233m gain) offset by a net gain of £205m (2013: £50m loss; 2012: £224m loss) arising from fair value adjustments to the carrying value of debt.

**Table of Contents**


**102 National Grid Annual Report and Accounts 2013/14**

**Notes to the consolidated**

**financial statements** continued

**6. Taxation**

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

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

Current tax assets and liabilities are measured at the amounts expected to be recovered from or paid to the taxation authorities. The tax rates and tax laws used to compute the amounts are those that have been enacted or substantively enacted by the reporting date.

The calculation of the Group's total tax charge involves a degree of estimation and judgement, and management periodically evaluates positions taken in tax returns with respect to situations in which

applicable tax regulation is subject to interpretation and establishes provisions where appropriate on the basis of amounts expected to be paid to the tax authorities.

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

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

Deferred tax liabilities are recognised on taxable temporary differences arising on investments in subsidiaries and jointly controlled entities except where the Company is able to control the reversal of the temporary difference and it is probable that the temporary difference will not reverse in the foreseeable future.

Deferred tax is calculated at the tax rates that are expected to apply in the period when the liability is settled or the asset is realised, based on the tax rates and tax laws that have been enacted or substantively enacted by the reporting date.

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

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

**Table of Contents**

Strategic Report	Corporate Governance	<b>Financial Statements</b>	Additional Information	103
------------------	----------------------	-----------------------------	------------------------	-----

**6. Taxation continued****Tax charged/(credited) to the income statement**

	<b>2014</b>	2013 (restated) <sup>1</sup>	2012 (restated) <sup>1</sup>
	<b>£m</b>	£m	£m
Tax before exceptional items, remeasurements and stranded cost recoveries	<b>581</b>	619	697
Exceptional tax on items not included in profit before tax (note 4)	<b>(390)</b>	(128)	(242)
Tax on other exceptional items, remeasurements and stranded cost recoveries	<b>93</b>	66	8
Tax on total exceptional items, remeasurements and stranded cost recoveries (note 4)	<b>(297)</b>	(62)	(234)
<b>Total tax charge</b>	<b>284</b>	557	463

1. See note 1 on page 92.

**Taxation as a percentage of profit before tax**

	<b>2014</b>	2013 (restated) <sup>1</sup>	2012 (restated) <sup>1</sup>
	<b>%</b>	%	%
Before exceptional items, remeasurements and stranded cost recoveries	<b>22.5</b>	24.4	28.9

After exceptional items, remeasurements and stranded cost recoveries	<b>10.3</b>	20.5	19.4
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1. See note 1 on page 92.

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

		2013	
	<b>2014</b>	(restated) <sup>1</sup>	2012
	<b>£m</b>	£m	(restated) <sup>1</sup> £m
<b>Current tax</b>			
UK corporation tax at 23% (2013: 24%; 2012: 26%)	<b>355</b>	306	186
UK corporation tax adjustment in respect of prior years	<b>(9)</b>	(17)	(5)
	<b>346</b>	289	181
Overseas corporation tax	<b>54</b>	50	98
Overseas corporation tax adjustment in respect of prior years	<b>(88)</b>	(222)	(144)
	<b>(34)</b>	(172)	(46)
<b>Total current tax</b>	<b>312</b>	117	135
<b>Deferred tax</b>			
UK deferred tax	<b>(292)</b>	35	(12)
UK deferred tax adjustment in respect of prior years	<b>(3)</b>	(17)	(18)
	<b>(295)</b>	18	(30)
Overseas deferred tax	<b>276</b>	283	191
Overseas deferred tax adjustment in respect of prior years	<b>(9)</b>	139	167
	<b>267</b>	422	358
<b>Total deferred tax</b>	<b>(28)</b>	440	328
<b>Total tax charge</b>	<b>284</b>	557	463

1. See note 1 on page 92.

Adjustments in respect of prior years include the following amounts that relate to exceptional items, remeasurements and stranded cost recoveries: £nil (2013: £1m credit; 2012: £1m credit).



**Table of Contents**


## 104 National Grid Annual Report and Accounts 2013/14

**Notes to the consolidated****financial statements continued****6. Taxation continued****Tax charged/(credited) to other comprehensive income and equity**

	2014	2013	2012
	(restated) <sup>1</sup>	(restated) <sup>1</sup>	(restated) <sup>1</sup>
	£m	£m	£m
<b>Current tax</b>			
Share-based payment	(3)	1	(3)
Available-for-sale investments	(5)		
<b>Deferred tax</b>			
Available-for-sale investments	2	2	2
Cash flow hedges	5	13	(2)
Share-based payment	(4)	1	
Remeasurements of net retirement benefit obligations	172	(179)	(342)
	<b>167</b>	(162)	(345)
Total tax recognised in the statement of comprehensive income	<b>174</b>	(164)	(342)
Total tax relating to share-based payment recognised directly in equity	<b>(7)</b>	2	(3)
	<b>167</b>	(162)	(345)

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1. See note 1 on page 92.

The tax charge for the year after exceptional items, remeasurements and stranded cost recoveries is lower (2013: lower; 2012: lower) than the standard rate of corporation tax in the UK of 23% (2013: 24%; 2012: 26%).

	Before exceptional items, remeasurements and stranded cost recoveries 2014 £m	After exceptional items, remeasurements and stranded cost recoveries 2014 £m	Before exceptional items, remeasurements and stranded cost recoveries 2013 (restated) <sup>1</sup> £m	After exceptional items, remeasurements and stranded cost recoveries 2013 (restated) <sup>1</sup> £m	Before exceptional items, remeasurements and stranded cost recoveries 2012 (restated) <sup>1</sup> £m	After exceptional items, remeasurements and stranded cost recoveries 2012 (restated) <sup>1</sup> £m
Profit before exceptional items, remeasurements and stranded cost recoveries	2,584	2,584	2,533	2,533	2,408	2,408
Exceptional items, remeasurements and stranded cost recoveries		164		178		(16)
Profit before tax	2,584	2,748	2,533	2,711	2,408	2,392
Charge for corporation tax at rate of 23% (2013: 24%; 2012: 26%)	594	632	608	651	626	636
Effect of:	(109)	(109)	(116)	(117)	1	1

Adjustments in respect of prior periods						
Expenses not deductible for tax purposes	32	284	37	169	36	
Non-taxable income	(24)	(268)	(24)	(152)	(19)	(
Adjustment in respect of foreign tax rates	98	138	116	140	63	
Effect of tax-exempt income	(3)	(3)	2	2	1	
Deferred tax						
Effect of change in UK US tax rates		(390)		(128)		(2
Other	(7)		(4)	(8)	(11)	
<b>Total tax</b>	<b>581</b>	<b>284</b>	<b>619</b>	<b>557</b>	<b>697</b>	<b>4</b>
	%	%	%	%	%	
<b>Effective tax</b>	<b>22.5</b>	<b>10.3</b>	<b>24.4</b>	<b>20.5</b>	<b>28.9</b>	<b>19</b>

See note 1 on page 92.

### Factors that may affect future tax charges

The Finance Act 2013 (the Act) was substantively enacted on 2 July 2013. The Act further reduced the main rate of UK corporation tax to 20% with effect from 1 April 2014 and 20% from 1 April 2015.

The reduction in the UK corporation tax rate to 20% from 1 April 2015 has been enacted and deferred tax balances have been calculated at

Effective from 1 April 2014, the state income tax rate for Massachusetts regulated utilities increased from 6.5% to 8% and, effective from 1 April 2016, the state income tax rate for New York will decrease from 7.1% to 6.5%. Neither of these rate changes is expected to have a material impact on the Group's effective tax rate.



**Table of Contents**

Strategic Report	Corporate Governance	Financial Statements	Additional Information	105
------------------	----------------------	----------------------	------------------------	-----

**6. Taxation continued****Taxation included within the statement of financial position**

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

	Accelerated tax depreciation £m	Share- based payment £m	Pensions and other post- retirement benefits (restated) <sup>1</sup> £m	Financial instruments £m	Other net temporary differences £m	Total (restated) <sup>1</sup> £m
<b>Deferred tax (assets)/liabilities</b>						
Deferred tax assets at 31 March 2012	(1)	(18)	(1,173)	(98)	(702)	(1,992)
Deferred tax liabilities at 31 March 2012	5,484		128	9	109	5,730
At 1 April 2012 as previously reported	5,483	(18)	(1,045)	(89)	(593)	3,738
Impact of change in accounting policy <sup>1</sup>			(2)			(2)
At 1 April 2012 (restated)	5,483	(18)	(1,047)	(89)	(593)	3,736
Exchange adjustments	149		(47)	(1)	(32)	69
Charged/(credited) to income statement	329	2 1	65 (179)	68 15	(23)	441 (163)

Charged/(credited) to other comprehensive income and equity Other					(6)	(6)
At 31 March 2013 (restated)	5,961	(15)	(1,208)	(7)	(654)	4,077
Deferred tax assets at 31 March 2013	(2)	(15)	(1,362)	(16)	(777)	(2,172)
Deferred tax liabilities at 31 March 2013	5,963		154	9	123	6,249
At 1 April 2013	5,961	(15)	(1,208)	(7)	(654)	4,077
Exchange adjustments (Credited)/charged to income statement	(282)		78		59	(145)
(Credited)/charged to other comprehensive income and equity	(30)	(3)	141	(7)	(126)	(25)
		(4)	172	7		175
<b>At 31 March 2014</b>	<b>5,649</b>	<b>(22)</b>	<b>(817)</b>	<b>(7)</b>	<b>(721)</b>	<b>4,082</b>
Deferred tax assets at 31 March 2014	(1)	(22)	(960)	(13)	(796)	(1,792)
Deferred tax liabilities at 31 March 2014	5,650		143	6	75	5,874
	5,649	(22)	(817)	(7)	(721)	4,082

1. See note 1 on  
page 92.

Deferred tax assets and liabilities are only offset where there is a legally enforceable right of offset and there is an intention to settle the balances net. The deferred tax balances (after offset) for statement of financial position purposes consist solely of deferred tax liabilities of £4,082m (2013: £4,077m).

At the reporting date there were no material current deferred tax assets or liabilities (2013: £nil).

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Deferred tax assets in respect of capital losses, trading losses and non-trade deficits have not been recognised as their future recovery is uncertain or not currently anticipated. The deferred tax assets not recognised are as follows:

	<b>2014</b>	2013
	<b>£m</b>	£m
Capital losses	<b>274</b>	323
Non-trade deficits	<b>1</b>	1
Trading losses	<b>5</b>	11

The capital losses and non-trade deficits that arise in the UK are available to carry forward indefinitely. However, the capital losses can only be offset against specific types of future capital gains and non-trade deficits against specific future non-trade profits. The trading losses arising in the US have up to a 20 year carry forward time limit.

The aggregate amount of temporary differences associated with the unremitted earnings of overseas subsidiaries and joint ventures for which deferred tax liabilities have not been recognised at the reporting date is approximately £2,118m (2013: £1,817m). No liability is recognised in respect of the differences because the Company and its subsidiaries are in a position to control the timing of the reversal of the temporary differences and it is probable that such differences will not reverse in the foreseeable future. In addition, as a result of a change in UK tax legislation, which largely exempts overseas dividends received on or after 1 July 2009 from UK tax, the temporary differences are unlikely to lead to additional tax.

**Table of Contents**


**106 National Grid Annual Report and Accounts 2013/14****Notes to the consolidated****financial statements continued****Unaudited commentary on taxation****Tax transparency****Tax strategy**

National Grid manages its tax affairs in a proactive and responsible way in order to comply with all relevant legislation and minimise reputational risk. We have a good working relationship with all relevant tax authorities and actively engage with them in order to ensure that they are fully aware of our view of the tax implications of our business initiatives. Management responsibility and oversight for our tax strategy, which is approved by the Finance Committee, rests with the Finance Director and the Global Tax and Treasury Director who monitor our tax activities and report to the Finance Committee.

The UK tax charge for the year disclosed in the accounts in accordance with accounting standards and the UK corporation tax paid during the year will differ. For transparency we have included a reconciliation below of the tax charge per the income statement to the UK corporation tax paid in 2013/14.

The tax charge for the Group as reported in the income statement is £284m (2012/13: £557m). The UK tax charge is £51m (2012/13: £307m) and UK corporation tax paid was £329m (2012/13: £243m), with the principal differences between these two measures as follows:

	<b>Year ended 31 March</b>	
	<b>2014</b>	<b>2013</b>
<b>Reconciliation of UK total tax charge to UK corporation tax</b>		



	paid	£m	(restated) <sup>1</sup>
<b>Total UK tax contribution</b>			<b>£m</b>
National Grid has taken the decision to provide additional information in respect of its total UK tax contribution and first disclosed this in last year's annual report. This year we have again disclosed information in respect of our total UK tax contribution for consistency and to aid transparency in an area in which there has been increasing public interest. As was the case in the prior year, the total amount of taxes we pay and collect in the UK year on year is significantly more than just the corporation tax which we pay on our UK profits. Within the total, we again include significant other taxes paid such as business rates and taxes on employment together with employee taxes and other indirect taxes.	Total UK tax charge (current tax £346m (2013: £289m) and deferred tax £295m credit (2013: £18m charge))	<b>51</b>	307
	Adjustment for non-cash deferred tax credit/(charge)	<b>295</b>	(18)
	Adjustment for the current tax credit in respect of prior years	<b>9</b>	17
	UK current tax charge	<b>355</b>	306
	UK corporation tax instalment payments in respect of current year not payable until the following year	<b>(179)</b>	(155)
	UK corporation tax instalment payments in respect of prior years paid in current year	<b>153</b>	92
	UK corporation tax paid	<b>329</b>	243

1. All comparatives restated for IAS 19 (revised). See note 1 on page 92.

For 2013/14 our total tax contribution to the UK Exchequer was £1.4bn (2012/13: £1.2bn). Taxes borne in 2014 were £733m, an 8% increase on taxes borne in 2013 of £678m and primarily due to higher corporation tax payments in the current year. Our 2012/13 total tax contribution of £1.2bn resulted in National Grid being the 17th highest contributor of UK taxes based on the results of the Hundred Group's 2013 Total Tax Contribution Survey, a position commensurate with the size of our business and capitalisation relative to other contributors to the survey. In 2012 we were in 16th position. In 2013 we ranked 9th in respect of taxes borne.

#### **Tax losses**

We have total unrecognised deferred tax assets in respect of losses of £280m (2012/13: £335m) of which £274m (2012/13: £319m) are capital losses in the UK as set out on page 105. These losses arose as a result of the disposal of certain businesses or assets and may be available to offset against future capital gains in the UK.

#### **Development of future tax policy**

We believe that the continued development of a coherent and transparent tax policy in the UK is critical to help drive growth in the economy.

We continue to contribute to research into the structure of business taxation and its economic impact by contributing

Of course, National Grid's contribution to the UK economy is broader than just the taxes it pays over to and collects on behalf of HMRC.

The Hundred Group's 2013 Total Tax Contribution Survey ranks National Grid in 4th place in respect of UK capital expenditure on fixed assets and we also rank highly in respect of investment in research and development. National Grid's economic contribution also supports a significant number of UK jobs in our supply chain.

The most significant amounts making up the 2013/14 total tax contribution were as follows:

to the funding of the Oxford University Centre for Business Taxation at the Saïd Business School.

We are a member of a number of industry groups which participate in the development of future tax policy, including the Hundred Group, which represents the views of finance directors of FTSE 100 companies and several other large UK companies. Our Finance Director is Chairman of its Tax Committee. This helps to ensure that we are engaged at the earliest opportunity on taxation issues which affect our business. For example, in the current year we have engaged with and responded to a number of HMRC consultations, the subject matter of which has a direct impact on taxes borne or collected by our business, and reviewed numerous others with a potential impact.

**This unaudited commentary does not form part of the financial statements.**

#### **UK total tax contribution 2013/14**

**Table of Contents**

Strategic Report	Corporate Governance	<b>Financial Statements</b>	Additional Information	107
------------------	----------------------	-----------------------------	------------------------	-----

**7. Earnings per share (EPS)**

EPS is the amount of post-tax profit attributable to each ordinary share. Basic EPS is calculated on profit for the year attributable to equity shareholders divided by the weighted average number of shares in issue during the year. Diluted EPS shows what the impact would be if all outstanding share options were exercised and treated as ordinary shares at year end.

Adjusted EPS, excluding exceptional items, remeasurements and stranded cost recoveries, are provided to reflect the business performance subtotals used by the Company. For further details of exceptional items, remeasurements and stranded cost recoveries, see note 4.

**(a) Basic earnings per share**

	<b>Earnings 2014 £m</b>	<b>Earnings per share 2014 pence</b>	<b>Earnings 2013 (restated)<sup>1</sup> £m</b>	<b>Earnings per share 2013 (restated)<sup>1,2</sup> pence</b>	<b>Earnings 2012 (restated)<sup>1</sup> £m</b>	<b>Earnings per share 2012 (restated)<sup>1,2</sup> pence</b>
Adjusted earnings	<b>2,015</b>	<b>54.0</b>	1,913	51.4	1,709	46.0
Exceptional items after tax	<b>388</b>	<b>10.4</b>	75	2.0	174	4.7
Remeasurements after tax	<b>73</b>	<b>2.0</b>	156	4.2	(122)	(3.3)
Stranded cost recoveries after tax			9	0.2	156	4.2
<b>Earnings</b>	<b>2,476</b>	<b>66.4</b>	2,153	57.8	1,917	51.6

	<b>2014</b> millions	2013 millions	2012 millions
Weighted average number of shares basic	<b>3,729</b>	3,724	3,719

1. See note 1 on page 92.

2. Comparative amounts have been restated to reflect the impact of additional shares issued as scrip dividends.

**(b) Diluted earnings per share**

	<b>Earnings</b> <b>2014</b> £m	<b>Earnings</b> <b>per share</b> <b>2014</b> pence	Earnings 2013 (restated) <sup>1</sup> £m	Earnings per share 2013 (restated) <sup>1,2</sup> pence	Earnings 2012 (restated) <sup>1</sup> £m	Earnings per share 2012 (restated) <sup>1,2</sup> pence
Adjusted earnings	<b>2,015</b>	<b>53.8</b>	1,913	51.1	1,709	45.7
Exceptional items after tax	<b>388</b>	<b>10.4</b>	75	2.0	174	4.7
Remeasurements after tax	<b>73</b>	<b>1.9</b>	156	4.2	(122)	(3.3)
Stranded cost recoveries after tax			9	0.2	156	4.2
Earnings	<b>2,476</b>	<b>66.1</b>	2,153	57.5	1,917	51.3
		<b>2014</b> millions		2013 millions		2012 millions
Weighted average number of shares diluted <sup>2</sup>		<b>3,748</b>		3,742		3,738

1. See note 1 on page 92.

2. Comparative amounts have been restated to reflect the impact of additional shares issued as scrip dividends.

**(c) Reconciliation of basic to diluted average number of shares**

	<b>2014 millions</b>	2013 millions	2012 millions
Weighted average number of ordinary shares basic	<b>3,729</b>	3,724	3,719
Effect of dilutive potential ordinary shares employee share plans	<b>19</b>	18	19
Weighted average number of ordinary shares diluted	<b>3,748</b>	3,742	3,738

**Table of Contents**


**108 National Grid Annual Report and Accounts 2013/14****Notes to the consolidated****financial statements** continued**8. Dividends**

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

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

The following table shows the actual dividends paid to equity shareholders:

	2014			2013			2012		
	Pence per share	Total via scrip £m	Settled via scrip £m	Pence per share	Total via scrip £m	Settled via scrip £m	Pence per share	Total via scrip £m	Settled via scrip £m
Interim year ended 31 March 2014	<b>14.49</b>	<b>539</b>							

Final year ended 31 March 2013	<b>26.36</b>	<b>964</b>	<b>444</b>						
Interim year ended 31 March 2013				14.49	527	187			
Final year ended 31 March 2012				25.35	906	436			
Interim year ended 31 March 2012							13.93	497	34
Final year ended 31 March 2011							23.47	822	279
	<b>40.85</b>	<b>1,503</b>	<b>444</b>	39.84	1,433	623	37.40	1,319	313

The Directors are proposing a final dividend for the year ended 31 March 2014 of 27.54p per share that will absorb approximately £1,028m of shareholders' equity (assuming all amounts are settled in cash). It will be paid on 20 August 2014 to shareholders who are on the register of members at 6 June 2014 and a scrip dividend will be offered as an alternative, subject to shareholders' approval at the AGM.

### Unaudited commentary on dividends

Following the announcement of our new dividend policy in March 2013, we remain confident that our business is able to support a dividend rising at least in line with inflation for the foreseeable future, while continuing to invest as required in our regulated asset bases. The dividend cover chart opposite supports our decision.

With the exception of the 2013/14 interim dividend paid in January this year, a scrip option has been offered for all interim and final dividends in the last three years. The scrip take-up was as follows: 2012/13 final: 46%; 2012/13 interim: 35%; and 2011/12 final: 48%.

### Dividend cover

Times

**This unaudited commentary does not form part of the financial statements.**

**Table of Contents**

Strategic Report	Corporate Governance	<b>Financial Statements</b>	Additional Information	109
------------------	----------------------	-----------------------------	------------------------	-----

**9. Goodwill**

Goodwill represents the excess of what we paid to acquire businesses over the fair value of their net assets at the acquisition date. We assess whether goodwill is recoverable each year by performing an impairment review.

Goodwill is recognised as an asset and is not amortised, but is tested for impairment annually, or more frequently if events or changes in circumstances indicate a potential impairment. Any impairment is recognised immediately in the income statement and is not subsequently reversed.

Goodwill and fair value adjustments arising on the acquisition of a foreign entity are treated as assets and liabilities of the foreign entity and translated at the closing exchange rate.

**Impairment**

Goodwill is allocated to cash-generating units and this allocation is made to those cash-generating units that are expected to benefit from the business combination in which the goodwill arose.

Impairments of goodwill are calculated as the difference between the carrying value of the goodwill and the estimated recoverable amount of the cash-generating unit to which that goodwill has been allocated. Recoverable amount is defined as the higher of fair value less costs to sell and estimated value-in-use at the date the impairment review is undertaken.

Value-in-use represents the present value of expected future cash flows, discounted using a pre-tax discount rate that reflects current market assessments of the time value of money and the risks specific to the asset for which the estimates of future cash flows have not been adjusted.



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

	Total £m
Cost at 1 April 2012	4,776
Exchange adjustments	252
Cost at 31 March 2013	5,028
Additions	12
Exchange adjustments	(446)
Cost at 31 March 2014	4,594
<b>Net book value at 31 March 2014</b>	<b>4,594</b>
Net book value at 31 March 2013	5,028

The amounts disclosed above as at 31 March 2014 include balances relating to the following cash-generating units: New York £2,640m (2013: £2,898m); Massachusetts £987m (2013: £1,082m); Rhode Island £367m (2013: £403m); and Federal £600m (2013: £645m).

Additions during the year relate to a further investment in Clean Line Energy Partners LLC, a developer of long-distance, HVDC transmission projects in the US to move renewable energy to market. Under IFRS 10, this investment is now accounted for as a subsidiary rather than an equity investment. National Grid has a 37% interest, but has the option to increase this holding.

Goodwill is reviewed annually for impairment and the recoverability of goodwill at 31 March 2014 has been assessed by comparing the carrying amount of our operations described above (our cash-generating units) with the expected recoverable amount on a value-in-use basis. In each assessment, the value-in-use has been calculated based on five year plan projections that incorporate our best estimates of future cash flows, customer rates, costs, future prices and growth. Such projections reflect our current regulatory rate plans taking into account regulatory arrangements to allow for future rate plan filings and recovery of investment. Our plans have proved to be reliable guides in the past and the Directors believe the estimates are appropriate.

The future growth rate used to extrapolate projections beyond five years has been maintained at 2.25% (2013: 2.25%). The growth rate has been determined having regard to data on projected growth in US real gross domestic product (GDP). Based on our business place in the underlying US economy, it is appropriate for the terminal growth rate to be based upon the overall growth in real GDP and, given the nature of our operations, to extend over a long period of time. Cash flow projections have been discounted to reflect the time value of money, using an effective pre-tax discount rate of 9% (2013: 9%). The discount rate represents the estimated weighted average cost of capital of these operations.

While it is possible that a key assumption in the calculation could change, the Directors believe that no reasonably foreseeable change would result in an impairment of goodwill, in view of the long-term nature of the key assumptions and the margin by which the estimated fair value exceeds the carrying amount.

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**Table of Contents**


**110 National Grid Annual Report and Accounts 2013/14****Notes to the consolidated****financial statements** continued**10. Other intangible assets**

Other intangible assets includes software and acquisition-related assets (such as brand names and customer relationships), which are written down (amortised) over the period we expect to receive a benefit from the asset.

Identifiable intangible assets are recorded at cost less accumulated amortisation and any provision for impairment. Other intangible assets are tested for impairment only if there is an indication that the carrying value of the assets may have been impaired. Impairments of assets are calculated as the difference between the carrying value of the asset and the recoverable amount, if lower. Where such an asset does not generate cash flows that are independent from other assets, the recoverable amount of the cash-generating unit to which that asset belongs is estimated. Impairments are recognised in the income statement and are disclosed separately. Any assets which suffered impairment in a previous period are reviewed for possible reversal of the impairment at each reporting date.

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

On a business combination, as well as recording separable intangible assets possessed by the acquired entity at their fair value, identifiable intangible assets that arise from contractual or other legal rights are also included in the statement of financial position at their fair value. Acquisition-related intangible assets principally comprise customer relationships.

Other intangible assets are amortised on a straight-line basis over their estimated useful economic lives. Amortisation periods for categories of intangible assets are:

	Years
Software	3 to 10
Acquisition-related intangibles	10 to 25

	Software £m	Acquisition- related £m	Total £m
Cost at 1 April 2012	899	116	1,015
Exchange adjustments	20	6	26
Additions	175		175
Disposals	(26)		(26)
Reclassifications <sup>1</sup>	(37)		(37)
Cost at 31 March 2013	1,031	122	1,153
Exchange adjustments	(38)	(7)	(45)
Additions	179		179
Disposals	(16)	(115)	(131)
Reclassifications <sup>1</sup>	66		66
Cost at 31 March 2014	1,222		1,222
Accumulated amortisation at 1 April 2012	(353)	(116)	(469)
Exchange adjustments	(6)	(6)	(12)
Amortisation charge for the year	(101)		(101)
Disposals	9		9
Reclassifications <sup>1</sup>	9		9
Accumulated amortisation at 31 March 2013	(442)	(122)	(564)
Exchange adjustments	12	7	19
Amortisation charge for the year	(127)		(127)
Impairment charge	(5)		(5)
Disposals	12	115	127
Reclassifications <sup>1</sup>	(3)		(3)
Accumulated amortisation at 31 March 2014	(553)		(553)

<b>Net book value at 31 March 2014</b>	<b>669</b>	<b>669</b>
Net book value at 31 March 2013	589	589

1. Reclassifications represents amounts transferred (to)/from property, plant and equipment (see note 11 on page 112).

**Table of Contents**

Strategic Report	Corporate Governance	<b>Financial Statements</b>	Additional Information	111
------------------	----------------------	-----------------------------	------------------------	-----

**11. Property, plant and equipment**

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

**Our strategy in action**

We operate an energy networks business and therefore have a significant physical asset base. We continue to invest in our networks to maintain reliability, create new customer connections and ensure our networks are flexible and resilient. Our business plan envisages these additional investments will be funded through a mixture of cash generated from operations and the issue of new debt.

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

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

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

enhancements to, or replacement of, existing assets.

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

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

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

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

	Years
Freehold and leasehold buildings	up to 65
<b>Plant and machinery</b>	
Electricity transmission plant	15 to 60
Electricity distribution plant	15 to 60
Electricity generation plant	20 to 40
Interconnector plant	15 to 60
Gas plant mains, services and regulating equipment	30 to 100
Gas plant storage	15 to 21
Gas plant meters	10 to 33
Motor vehicles and office equipment	up to 10

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

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

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

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

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



**Table of Contents**

## 112 National Grid Annual Report and Accounts 2013/14

**Notes to the consolidated****financial statements continued****11. Property, plant and equipment continued**

	Land and buildings £m	Plant and machinery £m	Assets in the course of construction £m	Motor vehicles and office equipment £m	Total £m
Cost at 1 April 2012	2,013	42,699	2,975	770	48,457
Exchange adjustments	55	803	45	13	916
Additions	141	704	2,584	82	3,511
Disposals	(24)	(311)	(2)	(130)	(467)
Reclassifications <sup>1</sup>	140	1,471	(1,642)	68	37
Cost at 31 March 2013	2,325	45,366	3,960	803	52,454
Exchange adjustments	(99)	(1,471)	(82)	(28)	(1,680)
Additions	69	623	2,514	56	3,262
Disposals	(32)	(288)	(2)	(98)	(420)
Reclassifications <sup>1</sup>	(15)	2,195	(2,366)	120	(66)
Cost at 31 March 2014	2,248	46,425	4,024	853	53,550
Accumulated depreciation at 1 April 2012	(436)	(13,804)	(2)	(514)	(14,756)
Exchange adjustments	(11)	(216)		(9)	(236)
Depreciation charge for the year <sup>2</sup>	(75)	(1,085)		(121)	(1,281)
Disposals	23	299	2	96	420
Reclassifications <sup>1</sup>				(9)	(9)

Accumulated depreciation at 31 March 2013	(499)	(14,806)	(557)	(15,862)
Exchange adjustments	16	399	21	436
Depreciation charge for the year <sup>2</sup>	(84)	(1,112)	(103)	(1,299)
Impairment charge for the year	(1)			(1)
Disposals	25	234	93	352
Reclassifications <sup>1</sup>	107	(65)	(39)	3
Accumulated depreciation at 31 March 2014	(436)	(15,350)	(585)	(16,371)
<b>Net book value at 31 March 2014</b>	<b>1,812</b>	<b>31,075</b>	<b>4,024</b>	<b>268</b>
Net book value at 31 March 2013	1,826	30,560	3,960	246

1. Represents amounts transferred between categories and from/(to) other intangible assets (see note 10 on page 110).

2. Includes amounts in respect of capitalised depreciation of £10m (2013: £21m).

	<b>2014</b>	2013
	<b>£m</b>	£m
<b>Information in relation to property, plant and equipment</b>		
Capitalised interest included within cost	<b>1,409</b>	1,275
Net book value of assets held under finance leases (all relating to motor vehicles and office equipment)	<b>170</b>	188
Additions to assets held under finance leases (all relating to motor vehicles and office equipment)	<b>25</b>	48
<b>Contributions to cost of property, plant and equipment included within:</b>		
Trade and other payables	<b>44</b>	43
Non-current liabilities	<b>1,526</b>	1,492

## 12. Other non-current assets

Other non-current assets includes assets that do not fall into any other non-current asset category (such as goodwill or property, plant and equipment) and where the benefit to be received from the asset is not due to be received until after 31 March 2015.

	<b>2014</b>	2013
	<b>£m</b>	£m
Commodity contract assets	<b>45</b>	47
Other receivables	<b>33</b>	51
Prepayments	<b>9</b>	6
	<b>87</b>	104



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values are determined by using valuation techniques that are consistent with techniques commonly used by the relevant market. The techniques use observable market data.

	2014	2013
	£m	£m
<b>Non-current</b>		
Available-for-sale investments	284	278
<b>Current</b>		
Available-for-sale investments	2,716	4,441
Loans and receivables	883	990
	<b>3,599</b>	5,431
<b>Total financial and other investments</b>	<b>3,883</b>	5,709
<b>Financial and other investments include the following:</b>		
Investments in short-term money funds	2,165	4,120
Managed investments in equity and bonds <sup>1</sup>	465	453
Bank deposits <sup>1</sup>	355	165
Cash surrender value of life insurance policies	140	145
Other investments	2	4
Restricted balances <sup>2</sup>	756	822
	<b>3,883</b>	5,709

Includes £296m (2013: £296m) of current investments which are held by insurance captives and

1. are therefore restricted.

2. Principally comprises collateral placed with counterparties with whom we have entered into a credit support annex to the ISDA Master Agreement £402m (2013: £507m), and assets held within security accounts, with charges in favour of the UK pension schemes Trustees of £234m (2013: £179m).

Available-for-sale investments are recorded at fair value. Due to their short maturities the carrying value of loans and receivables approximates their fair value. The maximum exposure to credit risk at the reporting date is the fair value of the financial investments. For further information on our credit risk, refer to note 30 (a). None of the financial investments are past due or impaired.

**Table of Contents****114 National Grid Annual Report and Accounts 2013/14****Notes to the consolidated****financial statements continued****14. Investments in joint ventures and associates**

Investments in joint ventures and associates represents businesses we do not control, but instead exercise joint control or significant influence.

A joint venture is an arrangement established to engage in economic activity, which the Company jointly controls with other parties and has rights to the net assets of the arrangement. An associate is an entity that is neither a subsidiary nor a joint venture, but over which the Company has significant influence.

	<b>2014</b>	2013
	<b>£m</b>	£m
Share of net assets at 1 April	<b>371</b>	341
Exchange adjustments	<b>(16)</b>	9
Additions	<b>4</b>	14
Share of post-tax results for the year	<b>28</b>	18
Dividends received	<b>(38)</b>	(21)
Other movements	<b>2</b>	10
<b>Share of net assets at 31 March</b>	<b>351</b>	371

A list of principal joint ventures and associates including the name, proportion of ownership and principal activity is provided in note 32.

The joint ventures and associates have no significant contingent liabilities to which the Group is exposed, and the Group has no significant contingent liabilities in relation to its interest in the joint ventures and associates.

Outstanding balances with joint ventures and associates are shown in note 28.

## 15. Derivative financial instruments

Derivatives are financial instruments that derive their value from the price of an underlying item such as interest rates, foreign exchange, credit spreads, commodities, equity or other indices. In accordance with Board approved policies, derivatives are transacted to manage our exposure to fluctuations in interest rate and foreign exchange rate on borrowings and other contractual cash flows. Specifically, we use derivatives to manage these risks from our financing portfolio to optimise the overall cost of accessing the debt capital markets. These derivatives are analysed below. We also use derivatives to manage our operational market risks from commodities. The commodity derivative contracts are detailed in note 30 (e).

Derivative financial instruments are initially recognised at fair value and subsequently remeasured at fair value at each reporting date. Changes in fair values are recorded in the period they arise, either in the income statement or other comprehensive income depending on the applicable accounting standards. Where the fair value of a derivative is positive it is carried as a derivative asset, and where negative as a derivative liability.

We calculate fair value of the financial derivatives by discounting all future cash flows using the market yield curve at the reporting date. The market yield curve for each currency is obtained from external sources for interest and foreign exchange rates. In the absence of sufficient market data, fair values would be based on the quoted market price of similar derivatives. Analysis of these derivatives and the various methods used to calculate their respective fair values is detailed below and in note 30.

For each class of derivative instrument type the fair value amounts are as follows:

	2014			2013		
	Assets £m	Liabilities £m	Total £m	Assets £m	Liabilities £m	Total £m
Interest rate swaps	861	(743)	118	1,282	(1,207)	75
Cross-currency interest rate swaps	1,025	(195)	830	900	(160)	740
Foreign exchange forward contracts	68	(12)	56	15	(63)	(48)
Forward rate agreements					(5)	(5)

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Inflation linked swaps	16	(213)	(197)	48	(246)	(198)
<b>Total</b>	<b>1,970</b>	<b>(1,163)</b>	<b>807</b>	2,245	(1,681)	564



**Table of Contents**

Strategic Report	Corporate Governance	<b>Financial Statements</b>	Additional Information	115
------------------	----------------------	-----------------------------	------------------------	-----

**15. Derivative financial instruments** continued

The maturity profile of derivative financial instruments is as follows:

	2014			2013		Total £m
	Assets £m	Liabilities £m	Total £m	Assets £m	Liabilities £m	
Less than 1 year	413	(339)	74	273	(407)	(134)
<b>Current</b>	<b>413</b>	<b>(339)</b>	<b>74</b>	273	(407)	(134)
In 1-2 years	54	(26)	28	42	(44)	(2)
In 2-3 years	73	(57)	16	75	(51)	24
In 3-4 years	71	(103)	(32)	119	(121)	(2)
In 4-5 years	244	(128)	116	84	(55)	29
More than 5 years	1,115	(510)	605	1,652	(1,003)	649
<b>Non-current</b>	<b>1,557</b>	<b>(824)</b>	<b>733</b>	1,972	(1,274)	698
	<b>1,970</b>	<b>(1,163)</b>	<b>807</b>	2,245	(1,681)	564

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

	2014	2013
	£m	£m

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Interest rate swaps	<b>(15,406)</b>	(16,603)
Cross-currency interest rate swaps	<b>(8,614)</b>	(9,641)
Foreign exchange forward contracts	<b>(4,698)</b>	(3,142)
Forward rate agreements		(2,443)
Inflation linked swaps	<b>(1,391)</b>	(1,390)
<b>Total</b>	<b>(30,109)</b>	(33,219)

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

Where possible, derivatives held as hedging instruments are formally designated as hedges as defined in IAS 39. Derivatives may qualify as hedges for accounting purposes if they are fair value hedges, cash flow hedges or net investment hedges. Our use of derivatives may entail a derivative transaction qualifying for one or more hedge type designations under IAS 39.

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

### Fair value hedges

Fair value hedges principally consist of interest rate and cross-currency swaps that are used to protect against changes in the fair value of fixed-rate, long-term financial instruments due to movements in market interest rates. For qualifying fair value hedges, all changes in the fair value of the derivative and changes in the fair value of the item in relation to the risk being hedged are recognised in the income statement to the extent the fair value hedge is effective. Adjustments made to the carrying amount of the hedged item for fair value hedges will be amortised over the remaining life, in line with the hedged item.

	<b>2014</b>	2013
	<b>£m</b>	£m
Cross-currency interest rate/interest rate swaps	<b>367</b>	732

**Fair value hedges****367**

732

**Cash flow hedges**

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

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

**Table of Contents**


**116 National Grid Annual Report and Accounts 2013/14****Notes to the consolidated****financial statements continued****15. Derivative financial instruments continued****Cash flow hedges continued**

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

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

	<b>2014</b>	2013
	<b>£m</b>	£m
Cross-currency interest rate/interest rate swaps	<b>224</b>	123
Foreign exchange forward contracts	<b>(11)</b>	1
Inflation linked swaps	<b>(32)</b>	(16)
<b>Cash flow hedges</b>	<b>181</b>	108

**Net investment hedges**

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Borrowings, cross-currency swaps and forward currency contracts are used in the management of the foreign exchange exposure arising from the investment in non-sterling denominated subsidiaries. Where these contracts qualify for hedge accounting they are designated as net investment hedges.

	<b>2014</b>	2013
	<b>£m</b>	£m
Cross-currency interest rate swaps	<b>342</b>	(56)
Foreign exchange forward contracts	<b>66</b>	(39)
<b>Net investment hedges</b>	<b>408</b>	(95)

The cross-currency swaps and forward foreign currency contracts are hedge accounted using the spot to spot method. The foreign exchange gain or loss on retranslation of the borrowings and the spot to spot movements on the cross-currency swaps and forward currency contracts are transferred to equity to offset gains or losses on translation of the net investment in the non-sterling denominated subsidiaries, with any ineffective portion recognised immediately in the income statement.

### **Derivatives not in a formal hedge relationship**

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

	<b>2014</b>	2013
	<b>£m</b>	£m
Cross-currency interest rate/interest rate swaps	<b>15</b>	16
Foreign exchange forward contracts	<b>1</b>	(10)
Forward rate agreements		(5)
Inflation linked swaps	<b>(165)</b>	(182)
<b>Derivatives not in a formal hedge relationship</b>	<b>(149)</b>	(181)

### **Discontinuation of hedge accounting**

Hedge accounting is discontinued when the hedging instrument expires or is sold, terminated, exercised or no longer qualifies for hedge accounting. At that time, any cumulative gains or losses relating to cash flow hedges recognised in equity are initially retained in equity and subsequently recognised in the income statement in the same periods in which the previously hedged item

affects net profit or loss. Amounts deferred in equity with respect to net investment hedges are subsequently recognised in the income statement in the event of the disposal of the overseas operations concerned. For fair value hedges, the cumulative adjustment recorded to the carrying value of the hedged item at the date hedge accounting is discontinued is amortised to the income statement using the effective interest method.

**Embedded derivatives**

No adjustment is made with respect to derivative clauses embedded in financial instruments or other contracts that are defined as closely related to those instruments or contracts. Consequently these embedded derivatives are not accounted for separately from the debt instrument. Where there are embedded derivatives in host contracts not closely related, the embedded derivative is separately accounted for as a derivative financial instrument.

**Table of Contents**

Strategic Report	Corporate Governance	<b>Financial Statements</b>	Additional Information	117
------------------	----------------------	-----------------------------	------------------------	-----

**16. Inventories and current intangible assets**

Inventories represent assets that we intend to use in order to generate revenue in the short term, either by selling the asset itself (for example fuel stocks) or by using it to fulfil a service to a customer or to maintain our network (consumables).

Inventories are stated at the lower of weighted average cost and net realisable value.

Where applicable, cost comprises direct materials and direct labour costs as well as those overheads that have been incurred in bringing the inventories to their present location and condition.

Emission allowances, principally relating to the emissions of carbon dioxide in the UK and sulphur and nitrous oxides in the US, are recorded as intangible assets within current assets and are initially recorded at cost and subsequently at the lower of cost and net realisable value. Where emission allowances are granted by relevant authorities, cost is deemed to be equal to the fair value at the date of allocation. Receipts of such grants are treated as deferred income, which is recognised in the income statement as the related charges for emissions are recognised or on impairment of the related intangible asset. A provision is recorded in respect of the obligation to deliver emission allowances and emission charges are recognised in the income statement in the period in which emissions are made.

	<b>2014</b>	2013
	<b>£m</b>	£m
Fuel stocks	<b>74</b>	114
Raw materials and consumables	<b>128</b>	156
Work in progress	<b>13</b>	13
Current intangible assets – emission allowances	<b>53</b>	8
	<b>268</b>	291

There is a provision for obsolescence of £29m against inventories as at 31 March 2014 (2013: £27m).



**Table of Contents****118 National Grid Annual Report and Accounts 2013/14****Notes to the consolidated****financial statements continued****17. Trade and other receivables**

Trade and other receivables are amounts which are due from our customers for services (and commodities in the US) we have provided. Other receivables also include prepayments made by us, for example, property lease rentals paid in advance.

Trade, loan and other receivables are initially recognised at fair value and subsequently measured at amortised cost, less any appropriate allowances for estimated irrecoverable amounts. A provision is established for irrecoverable amounts when there is objective evidence that amounts due under the original payment terms will not be collected.

	<b>2014</b>	2013
	<b>£m</b>	£m
Trade receivables	<b>1,602</b>	1,325
Prepayments and accrued income	<b>1,090</b>	1,421
Commodity contract assets	<b>42</b>	42
Current tax assets	<b>11</b>	
Other receivables	<b>110</b>	122

2,855 2,910

Trade receivables are non interest-bearing and generally have a 30-90 day term. Due to their short maturities, the fair value of trade and other receivables approximates their book value. Commodity contract assets are recorded at fair value. All other receivables are recorded at amortised cost.

#### **Provision for impairment of receivables**

	<b>2014</b>	2013
	<b>£m</b>	£m
At 1 April	<b>261</b>	270
Exchange adjustments	<b>(23)</b>	13
Charge for the year, net of recoveries	<b>105</b>	75
Uncollectible amounts written off against receivables	<b>(94)</b>	(97)
At 31 March	<b>249</b>	261

#### **Trade receivables past due but not impaired**

	<b>2014</b>	2013
	<b>£m</b>	£m
Up to 3 months past due	<b>212</b>	242
3 to 6 months past due	<b>69</b>	45
Over 6 months past due	<b>65</b>	4
	<b>346</b>	291

For further information on our wholesale and retail credit risk, refer to note 30 (a). For further information on our commodity risk, refer to note 30 (e).

**Table of Contents**

Strategic Report	Corporate Governance	<b>Financial Statements</b>	Additional Information	119
------------------	----------------------	-----------------------------	------------------------	-----

**18. Cash and cash equivalents**

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

Net cash and cash equivalents reflected in the cash flow statement are net of bank overdrafts, which are reported in borrowings. The carrying amounts of cash and cash equivalents and bank overdrafts approximate their fair values.

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

Net cash and cash equivalents held in currencies other than sterling have been converted into sterling at year-end exchange rates.

For further information on currency exposures, refer to note 30 (d).

	<b>2014</b>	2013
	<b>£m</b>	£m
Cash at bank	<b>75</b>	99
Short-term deposits	<b>279</b>	572
<b>Cash and cash equivalents excluding bank overdrafts</b>	<b>354</b>	671
Bank overdrafts	<b>(15)</b>	(23)
<b>Net cash and cash equivalents</b>	<b>339</b>	648

At 31 March 2014, £24m (2013: £21m) of cash and cash equivalents were restricted. This primarily relates to cash held in captive insurance companies.

## 19. Borrowings

We borrow money primarily in the form of bonds and bank loans. These are for a fixed term and may have fixed or floating interest rates or are linked to RPI. As indicated in note 15, we use derivatives to manage risks associated with interest rates and foreign exchange.

### Our strategy in action

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

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

The Finance Committee controls refinancing risk by limiting the amount of our debt maturities arising from borrowings in any one year which is demonstrated by our maturity profile.

	2014 £m	2013 £m
<b>Current</b>		
Bank loans	1,485	1,194
Bonds	1,730	1,761
Commercial paper	252	438
Finance leases	19	20
Other loans	10	12
Bank overdrafts	15	23
	<b>3,511</b>	<b>3,448</b>
<b>Non-current</b>		
Bank loans	1,414	1,863
Bonds	20,732	22,435
Finance leases	151	175

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Other loans	<b>142</b>	174
	<b>22,439</b>	24,647
<b>Total</b>	<b>25,950</b>	28,095

**Table of Contents**


**120 National Grid Annual Report and Accounts 2013/14****Notes to the consolidated****financial statements continued****19. Borrowings continued**

Total borrowings are repayable as follows:

	<b>2014</b>	2013
	<b>£m</b>	£m
Less than 1 year	<b>3,511</b>	3,448
In 1-2 years	<b>895</b>	1,872
In 2-3 years	<b>1,177</b>	860
In 3-4 years	<b>1,661</b>	1,255
In 4-5 years	<b>1,509</b>	1,420
<b>More than 5 years:</b>		
by instalments	<b>175</b>	71
other than by instalments	<b>17,022</b>	19,169
	<b>25,950</b>	28,095

The fair value of borrowings at 31 March 2014 was £28,131m (2013: £30,792m). Where market values were available, fair value of borrowings (Level 1) was £17,388m (2013: £20,543m). Where market values were not available, fair value of borrowings (Level 2) was £10,743m (2013: £10,249m), calculated by discounting cash flows at prevailing interest rates. The notional amount outstanding of the debt portfolio at 31 March 2014 was £25,539m (2013: £27,391m).

The assets of the Colonial Gas Company and the Niagara Mohawk Power Corporation and certain gas distribution assets of the Narragansett Electric Company are subject to liens and other charges

and are provided as collateral over borrowings totalling £438m at 31 March 2014 (2013: £512m).

Collateral is placed with or received from any counterparty where we have entered into a credit support annex to the ISDA Master Agreement once the current mark-to-market valuation of the trades between the parties exceeds an agreed threshold. Included in current bank loans is £843m (2013: £730m) in respect of cash received under collateral agreements. For further details of our borrowing facilities, refer to note 31. For further details of our bonds in issue, please refer to the debt investor section of our website.

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

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

#### Finance lease obligations

	<b>2014</b>	2013
	<b>£m</b>	£m
Gross finance lease liabilities are repayable as follows:		
Less than 1 year	<b>19</b>	20
1-5 years	<b>89</b>	109
More than 5 years	<b>100</b>	101
	<b>208</b>	230
Less: finance charges allocated to future periods	<b>(38)</b>	(35)
	<b>170</b>	195
The present value of finance lease liabilities is as follows:		
Less than 1 year	<b>19</b>	20
1-5 years	<b>70</b>	96
More than 5 years	<b>81</b>	79
	<b>170</b>	195

**Table of Contents**

Strategic Report	Corporate Governance	<b>Financial Statements</b>	Additional Information	121

**Unaudited commentary on borrowings**

As at 31 March 2014, total borrowings of £25,950m (2013: £28,095m) including bonds, bank loans, commercial paper, collateral, finance leases and other debt had decreased by £2,145m primarily representing maturity and redemption of debt during the year. We expect to repay £3,511m of our total borrowings in the next 12 months including commercial paper, collateral and interest, and we expect to be able to refinance this borrowing through the capital and money markets.

The maturity profile of long-term debt in our major entities is illustrated below:

**National Grid long-term debt maturity profile**

£m

1. Includes hybrid bonds at first callable date (euro: 2020; sterling: 2025). Actual maturity of these bonds is euro: 2076; sterling: 2073.

Further information on our bonds can be found in the debt investor section of our website.

**This unaudited commentary does not form part of the financial statements.**





**Table of Contents**


**122 National Grid Annual Report and Accounts 2013/14****Notes to the consolidated****financial statements** continued**20. Trade and other payables**

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

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

	<b>2014</b>	2013
	<b>£m</b>	£m
Trade payables	<b>1,942</b>	2,033
Deferred income	<b>224</b>	155
Commodity contract liabilities	<b>77</b>	69
Social security and other taxes	<b>146</b>	131
Other payables	<b>642</b>	663
	<b>3,031</b>	3,051

Due to their short maturities, the fair value of trade and other payables approximates their book value. Commodity contract liabilities are recorded at fair value. All other trade and other payables are recorded at amortised cost.

## 21. Other non-current liabilities

Other non-current liabilities includes deferred income which will not be recognised as income until after 31 March 2015. It also includes payables that are not due until after that date.

	<b>2014</b>	2013
	<b>£m</b>	£m
Deferred income	<b>1,605</b>	1,579
Commodity contract liabilities	<b>46</b>	70
Other payables	<b>190</b>	235
	<b>1,841</b>	1,884

Commodity contract liabilities are recorded at fair value. All other non-current liabilities are recorded at amortised cost. There is no material difference between the fair value and the carrying value of other non-current liabilities.

## 22. Pensions and other post-retirement benefits

Substantially all our employees are members of either DB or DC pension plans. The principal UK plans are the National Grid UK Pension Scheme, the National Grid Electricity Group of the Electricity Supply Pension Scheme and The National Grid YouPlan. In the US, we have a number of plans and also provide healthcare and life insurance benefits to eligible retired US employees.

The fair value of associated plan assets and present value of DB obligations are updated annually. For further details and the actuarial assumptions used to value the obligations, see note 29.

With the adoption of IAS 19 (revised), we have increased our disclosures by separately presenting our UK and US pension plans to show geographical split.

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

For DC plans, the Group pays contributions into separate funds on behalf of the employee and has no further obligations to employees. The risks associated with this type of plan are assumed by the member.

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

The cost of providing benefits in a DB plan is determined using the projected unit method, with actuarial valuations being carried out at each reporting date by a qualified actuary. This valuation method is an accrued benefits valuation method that makes allowance for projected earnings.

The Group's obligation in respect of DB pension plans is calculated separately for each plan by projecting the estimated amount of future benefit payments that employees have earned for their pensionable service in the current and prior periods. These future benefit payments are discounted to determine the present value of the liabilities and the fair value of plan assets and any unrecognised past service cost is then deducted. The discount rate used is the yield at the valuation date on high-quality corporate bonds.



**Amounts recognised in the statement of financial position**

	UK pensions			US pensions			US other post-retirement benefits		
	2014	2013	2012	2014	2013	2012	2014	2013	2012
	(restated) <sup>1</sup>	(restated) <sup>1</sup>	(restated) <sup>1</sup>	(restated) <sup>1</sup>	(restated) <sup>1</sup>	(restated) <sup>1</sup>	(restated) <sup>1</sup>	(restated) <sup>1</sup>	(restated) <sup>1</sup>
	£m	£m	£m	£m	£m	£m	£m	£m	£m
Present value of funded obligations	<b>(18,100)</b>	(18,495)	(16,719)	<b>(4,566)</b>	(4,915)	(4,424)	<b>(2,680)</b>	(3,020)	(2,630)
Fair value of plan assets	<b>17,409</b>	17,392	16,107	<b>4,229</b>	4,378	3,850	<b>1,620</b>	1,515	1,192
	<b>(691)</b>	(1,103)	(612)	<b>(337)</b>	(537)	(574)	<b>(1,060)</b>	(1,505)	(1,438)
Present value of unfunded obligations	<b>(62)</b>	(66)	(56)	<b>(186)</b>	(200)	(187)			
Other post-employment liabilities					(3)	(5)	<b>(75)</b>	(83)	(66)
Net defined benefit liability	<b>(753)</b>	(1,169)	(668)	<b>(523)</b>	(740)	(766)	<b>(1,135)</b>	(1,588)	(1,504)
<b>Represented by:</b>									
Liabilities	<b>(753)</b>	(1,169)	(668)	<b>(697)</b>	(935)	(921)	<b>(1,135)</b>	(1,588)	(1,504)
Assets				<b>174</b>	195	155			
	<b>(753)</b>	(1,169)	(668)	<b>(523)</b>	(740)	(766)	<b>(1,135)</b>	(1,588)	(1,504)

1. See note 1 on page 92.

**Table of Contents**


## 124 National Grid Annual Report and Accounts 2013/14

**Notes to the consolidated****financial statements** continued**22. Pensions and other post-retirement benefits** continued**Amounts recognised in the income statement and the statement of other comprehensive income**

	UK pensions			US pensions			US other post-retirement benefits		
	2014 £m	2013 (restated) <sup>1</sup> £m	2012 (restated) <sup>1</sup> £m	2014 £m	2013 (restated) <sup>1</sup> £m	2012 (restated) <sup>1</sup> £m	2014 £m	2013 (restated) <sup>1</sup> £m	2012 (restated) <sup>1</sup> £m
<b>Included within operating costs</b>									
Administration costs	6	6	6	5	4	5	1	2	1
<b>Included within payroll costs</b>									
Defined contribution scheme costs	19	16	13	21	23	25			
Defined benefit scheme costs									
Current service cost	96	90	84	85	87	75	44	43	37
Past service cost augmentations	15	2	2						

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Past service (credit)/cost redundancies	(19)	(7)	(6)		19			23
Past service credit plan amendments	(11)							
Special termination benefit cost redundancies	39	20	19					
	139	121	112	106	110	119	44	43
								60
<b>Included within exceptional items</b>								
LIPA MSA transition			(16)			(198)		
Net (gain)/loss on disposal of businesses			(6)	3			1	
			(6)	3		(198)	1	
<b>Included within finance income and costs</b>								
Net interest cost	47	31	1	27	34	26	54	70
								76
<b>Total included in income statement</b>	192	158	113	122	151	150	(99)	116
								137
Remeasurements of net retirement benefit obligations	354	(560)	(676)	81	(35)	(367)	50	(119)
Exchange adjustments				60	(37)	(2)	126	(75)
								(6)
<b>Total included in the statement of other comprehensive income</b>	354	(560)	(676)	141	(72)	(369)	176	(194)
								(103)



1. See note 1 on page 92.

### Reconciliation of the net defined benefit liability

	UK pensions			US pensions			US other post-retirement benefits		
	2014 £m	2013 (restated) <sup>1</sup> £m	2012 (restated) <sup>1</sup> £m	2014 £m	2013 (restated) <sup>1</sup> £m	2012 (restated) <sup>1</sup> £m	2014 £m	2013 (restated) <sup>1</sup> £m	2012 (restated) <sup>1</sup> £m
Opening net defined benefit liability	(1,169)	(668)	(90)	(740)	(766)	(484)	(1,588)	(1,504)	(1,452)
(Cost)/credit recognised in the income statement	(173)	(142)	(100)	(101)	(128)	(125)	99	(116)	(137)
Remeasurement effects recognised in the statement of other comprehensive income	354	(560)	(676)	141	(72)	(369)	176	(194)	(103)
Employer contributions	235	201	198	174	224	217	187	262	198
Other movements				3	2	(5)	(9)	(36)	(10)
<b>Closing net defined benefit liability</b>	<b>(753)</b>	<b>(1,169)</b>	<b>(668)</b>	<b>(523)</b>	<b>(740)</b>	<b>(766)</b>	<b>(1,135)</b>	<b>(1,588)</b>	<b>(1,504)</b>

1. See note 1 on page 92.

**Table of Contents**

Strategic Report	Corporate Governance	<b>Financial Statements</b>	Additional Information	125
------------------	----------------------	-----------------------------	------------------------	-----

**22. Pensions and other post-retirement benefits** continued

	UK pensions			US pensions			US other post-retirement benefits		
	2014 £m	2013 (restated) <sup>1</sup> £m	2012 (restated) <sup>1</sup> £m	2014 £m	2013 (restated) <sup>1</sup> £m	2012 (restated) <sup>1</sup> £m	2014 £m	2013 (restated) <sup>1</sup> £m	2012 (restated) <sup>1</sup> £m
<b>Changes in the present value of defined benefit obligations (including unfunded obligations)</b>									
Opening defined benefit obligations	<b>(18,561)</b>	(16,775)	(15,443)	<b>(5,115)</b>	(4,611)	(4,037)	<b>(3,020)</b>	(2,630)	(2,458)
Current service cost	<b>(96)</b>	(90)	(84)	<b>(85)</b>	(87)	(75)	<b>(44)</b>	(43)	(37)
Interest cost	<b>(780)</b>	(788)	(830)	<b>(221)</b>	(232)	(233)	<b>(123)</b>	(133)	(140)
Actuarial gains/(losses) experience	<b>16</b>	74	(112)	<b>(22)</b>	1	(13)	<b>47</b>	60	71
Actuarial losses demographic assumptions				<b>(129)</b>	5	(64)	<b>(154)</b>	(18)	(84)
Actuarial gains/(losses) financial assumptions	<b>436</b>	(1,765)	(1,062)	<b>57</b>	(245)	(422)	<b>49</b>	(218)	(70)

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Past service credit/(cost) redundancies	19	7	6	16	36	(19)	119	5	(23)
Special termination benefit cost redundancies	(39)	(20)	(13)						
Past service cost augmentations	(15)	(2)	(2)						
Past service credit plan amendments	11						19		
Transfers in Medicare subsidy received			1				(17)	(19)	(6)
Liabilities extinguished on settlements							60		
Employee contributions	(2)	(3)	(3)						
Benefits paid	849	801	767	291	269	268	117	123	127
Transferred to liabilities of businesses held for sale						3			2
Exchange adjustments				456	(251)	(19)	267	(147)	(12)
<b>Closing defined benefit obligations</b>	<b>(18,162)</b>	<b>(18,561)</b>	<b>(16,775)</b>	<b>(4,752)</b>	<b>(5,115)</b>	<b>(4,611)</b>	<b>(2,680)</b>	<b>(3,020)</b>	<b>(2,630)</b>
<b>Changes in the fair value of plan assets</b>									
Opening fair value of plan assets	17,392	16,107	15,353	4,378	3,850	3,550	1,515	1,192	1,066
Interest income	733	757	829	194	198	207	69	63	64
Return on assets (less)/greater than assumed	(98)	1,131	498	175	204	132	108	57	(14)
Administration costs	(6)	(6)	(6)	(5)	(4)	(5)	(1)	(2)	(1)
Transfers out	235	201	198	174	224	217	187	262	198

Employer contributions									
Employee contributions	<b>2</b>	<b>3</b>	<b>3</b>						
Benefits paid	<b>(849)</b>	<b>(801)</b>	<b>(767)</b>	<b>(291)</b>	<b>(269)</b>	<b>(268)</b>	<b>(117)</b>	<b>(123)</b>	<b>(127)</b>
Assets distributed in settlements and transfers					<b>(39)</b>			<b>(6)</b>	
Exchange adjustments				<b>(396)</b>	<b>214</b>	<b>17</b>	<b>(141)</b>	<b>72</b>	<b>6</b>
<b>Closing fair value of plan assets</b>	<b>17,409</b>	<b>17,392</b>	<b>16,107</b>	<b>4,229</b>	<b>4,378</b>	<b>3,850</b>	<b>1,620</b>	<b>1,515</b>	<b>1,192</b>
<b>Actual return on plan assets</b>	<b>635</b>	<b>1,888</b>	<b>1,327</b>	<b>369</b>	<b>402</b>	<b>339</b>	<b>177</b>	<b>120</b>	<b>50</b>
<b>Expected contributions to plans in the following year</b>	<b>182</b>	<b>181</b>	<b>129</b>	<b>118</b>	<b>183</b>	<b>224</b>	<b>109</b>	<b>196</b>	<b>248</b>

1. See note 1 on page 92.

**Table of Contents**


**126 National Grid Annual Report and Accounts 2013/14**

**Notes to the consolidated**

**financial statements continued**

**23. Provisions**

We make provisions when an obligation exists, resulting from a past event and it is probable that cash will be paid to settle it, but the exact amount of cash required can only be estimated.

The main estimates relate to environmental remediation and decommissioning costs for various sites we own or have owned and other provisions, including restructuring plans and lease contracts we have entered into that are now loss making.

**Our strategy in action**

We are committed to the protection and enhancement of the environment. However, we have acquired, owned and operated a number of businesses which have, during the course of their operations, created an environmental impact. Therefore we have a provision that reflects the expected cost to remediate these sites. Current operations will seldom result in new sites with significant expected costs being added to the provision.

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

Provision is made for decommissioning and environmental costs, based on future estimated expenditures, discounted to present values. An initial estimate of decommissioning and environmental costs attributable to property, plant and equipment is recorded as part of the original cost of the related property, plant and equipment.

Changes in the provision arising from revised estimates or discount rates or changes in the expected timing of expenditures that relate to property, plant and equipment are recorded as adjustments to their carrying value and depreciated prospectively over their remaining estimated useful economic lives; otherwise such changes are recognised in the income statement.

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

	Environmental	Decommissioning	Restructuring	Emissions	Other	Total
	£m	£m	£m	£m	£m	£m
At 1 April 2012	1,158	112	70	23	368	1,731
Exchange adjustments	45	5		1	14	65
Additions	92		31	1	83	207
Unused amounts reversed	(55)	(20)	(5)	(3)	(4)	(87)
Unwinding of discount	59				16	75
Utilised	(101)	(16)	(43)	(14)	(57)	(231)
At 31 March 2013	1,198	81	53	8	420	1,760
Exchange adjustments	(79)	(7)		(1)	(25)	(112)
Additions	11	84	86	7	42	230
Unused amounts reversed	(14)		(1)		(3)	(18)
Unwinding of discount	57				16	73
Utilised	(101)	(14)	(59)		(114)	(288)
<b>At 31 March 2014</b>	<b>1,072</b>	<b>144</b>	<b>79</b>	<b>14</b>	<b>336</b>	<b>1,645</b>
					<b>2014</b>	2013
					<b>£m</b>	£m
Current					<b>282</b>	308
Non-current					<b>1,363</b>	1,452
					<b>1,645</b>	1,760



**Table of Contents**

Strategic Report	Corporate Governance	<b>Financial Statements</b>	Additional Information	127
------------------	----------------------	-----------------------------	------------------------	-----

**23. Provisions continued****Environmental provision**

The environmental provision represents the estimated restoration and remediation costs relating to a number of sites owned and managed by subsidiary undertakings, together with certain US sites that National Grid no longer owns. The environmental provision is as follows:

	2014			2013		
	Discounted	Undiscounted	Real discount rate	Discounted	Undiscounted	Real discount rate
	£m	£m	rate	£m	£m	rate
UK sites <sup>1</sup>	286	367	2%	302	397	2%
US sites <sup>2</sup>	786	891	2%	896	1,014	2%
	1,072	1,258		1,198	1,411	



1. The remediation expenditure in the UK relates to old gas manufacturing sites and also to electricity transmission sites. Cash flows are expected to be incurred between 2014 and 2067. A number of uncertainties affect the calculation of the provision, including the impact of regulation, accuracy of the site surveys, unexpected contaminants, transportation costs, the impact of alternative technologies and changes in the discount rate. This provision incorporates our best estimate of the financial effect of these uncertainties, but future material changes in any of the assumptions could have a material impact on the calculation of the provision. The undiscounted amount is the undiscounted best estimate of the liability having regard to these uncertainties.

2. The remediation expenditure in the US is expected to be incurred between 2014 and 2059. The uncertainties regarding the calculation of this provision are similar to those considered in respect of UK sites. However, unlike the UK, with the exception of immaterial amounts of such costs, this expenditure is expected to be largely recoverable from ratepayers under the terms of various rate agreements in the US.

### **Decommissioning provision**

The decommissioning provision primarily represents both £55m (2013: £69m) of expenditure relating to asset retirement obligations expected to be incurred until 2058, and £72m (2013: £nil) of expenditure relating to the demolition of gas holders expected to be incurred until 2022. It also includes the net present value of the estimated expenditure (discounted at a real rate of 2%) expected to be incurred until 2038 in respect of the decommissioning of certain US nuclear generating units that National Grid no longer owns.

### **Restructuring provision**

The restructuring provision principally relates to business reorganisation costs in the UK and the US and is expected to be incurred until 2021.

### **Emissions provision**

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

### **Other provisions**

Included within other provisions at 31 March 2014 are amounts provided in respect of onerous lease commitments and rates payable on surplus properties of £117m (2013: £165m) with expenditure expected to be incurred until 2018.

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Other provisions also include £160m (2013: £174m) of estimated liabilities in respect of past events insured by insurance subsidiary undertakings, including employer liability claims. In accordance with insurance industry practice, these estimates are based on experience from previous years and there is, therefore, no identifiable payment date. It also includes £13m (2013: £13m) in respect of obligations associated with investments in joint ventures.

**Table of Contents**

## 128 National Grid Annual Report and Accounts 2013/14

**Notes to the consolidated****financial statements** continued**24. Share capital**

Ordinary share capital represents the total number of shares issued which are publicly traded. We also disclose the number of treasury shares the Company holds, which are shares that the Company has bought itself, predominantly to satisfy employee share option plan liabilities.

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

	Allotted, called up and fully paid	
	millions	£m
At 1 April 2012	3,701	422
Issued during the year in lieu of dividends <sup>1</sup>	94	11
At 31 March 2013	3,795	433

Issued during the year in lieu of dividends <sup>1</sup>	59	6
<b>At 31 March 2014</b>	<b>3,854</b>	<b>439</b>

1. The issue of shares in lieu of dividends is considered to be a bonus issue under the terms of the Companies Act 2006 and the nominal value of the shares is charged to the share premium account.

The share capital of the Company consists of ordinary shares of 11  $\frac{17}{43}$  pence nominal value each including ADSs. The ordinary and ADSs allow holders to receive dividends and vote at general meetings of the Company. The Company holds treasury shares but may not exercise any rights over these shares including the entitlement to vote or receive dividends. There are no restrictions on the transfer or sale of ordinary shares.

In line with the provisions of the Companies Act 2006, the Company has amended its Articles of Association and ceased to have authorised share capital.

### **Treasury shares**

At 31 March 2014, the Company held 124m (2013: 129m) of its own shares. The market value of these shares as at 31 March 2014 was £1,019m (2013: £989m).

The maximum number of shares held during the year was 129m ordinary shares (2013: 135m) representing approximately 3.4% (2013: 3.6%) of the ordinary shares in issue as at 31 March 2014 and having a nominal value of £15m (2013: £15m).

**Table of Contents**

Strategic Report	Corporate Governance	Financial Statements	Additional Information	129
------------------	----------------------	----------------------	------------------------	-----

**25. Other equity reserves**

Other equity reserves are different categories of equity as required by accounting standards and represent the impact of a number of our historical transactions.

Other equity reserves comprise the translation reserve (see accounting policy B), cash flow hedge reserve (see note 15), available-for-sale reserve (see note 13), the capital redemption reserve and the merger reserve. The merger reserve arose as a result of the application of merger accounting principles under the then prevailing UK GAAP, which under IFRS 1 was retained for mergers that occurred prior to the IFRS transition date. Under merger accounting principles, the difference between the carrying amount of the capital structure of the acquiring vehicle and that of the acquired business was treated as a merger difference and included within reserves.

As the amounts included in other equity reserves are not attributable to any of the other classes of equity presented, they have been disclosed as a separate classification of equity.

	Translation £m	Cash flow hedge £m	Available- for-sale £m	Capital redemption £m	Merger £m	Total £m
At 1 April 2011	319	(103)	60	19	(5,165)	(4,870)
Exchange adjustments	27					27
Net (losses)/gains taken to equity		(18)	16			(2)
Transferred to profit or loss		19	(9)			10
Tax		2	(2)			
At 31 March 2012	346	(100)	65	19	(5,165)	(4,835)

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Exchange adjustments	117					117
Net (losses)/gains taken to equity		(31)	20			(11)
Transferred to profit or loss		73	(10)			63
Tax		(13)	(2)			(15)
<b>At 31 March 2013</b>	<b>463</b>	<b>(71)</b>	<b>73</b>	<b>19</b>	<b>(5,165)</b>	<b>(4,681)</b>
Exchange adjustments	(158)					(158)
Net gains taken to equity		63	6			69
Transferred to profit or loss		27	(14)			13
Tax		(5)	3			(2)
<b>At 31 March 2014</b>	<b>305</b>	<b>14</b>	<b>68</b>	<b>19</b>	<b>(5,165)</b>	<b>(4,759)</b>

The merger reserve represents the difference between the carrying value of subsidiary undertaking investments and their respective capital structures following the Lattice demerger from BG Group plc and the 1999 Lattice refinancing of £5,745m and merger differences of £221m and £359m.

The cash flow hedge reserve on interest rate swap contracts will be continuously transferred to the income statement until the borrowings are repaid. The amount due to be released from reserves to the income statement next year is £17m (pre-tax) and the remainder released with the same maturity profile as borrowings due after more than one year.

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**Table of Contents**


**130 National Grid Annual Report and Accounts 2013/14**

**Notes to the consolidated**

**financial statements continued**

**26. Net debt**

Net debt represents the amount of borrowings and overdrafts, less cash, financial investments and related derivatives.

Funding and liquidity risk management is carried out by the treasury function under policies and guidelines approved by the Finance Committee of the Board. The Finance Committee is responsible for the regular review and monitoring of treasury activity and for the approval of specific transactions, the authority for which falls outside the delegation of authority to management.

The primary objective of the treasury function is to manage our funding and liquidity requirements. A secondary objective is to manage the associated financial risks, in the form of interest rate risk and foreign exchange risk, to within pre-authorised parameters. Details of the main risks arising from our financing and commodity hedging activities can be found in the risk factors discussion starting on page 167 and in note 30 to the consolidated financial statements on pages 137 to 144.

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

The movement in cash and cash equivalents is reconciled to movements in net debt.

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

	<b>2014</b>	2013	2012
	<b>£m</b>	£m	£m
(Decrease)/increase in cash and cash equivalents	<b>(283)</b>	335	(43)
(Decrease)/increase in financial investments	<b>(1,720)</b>	2,992	(553)
Decrease/(increase) in borrowings and related derivatives	<b>1,021</b>	(4,304)	154
Net interest paid on the components of net debt	<b>841</b>	756	721
Change in debt resulting from cash flows	<b>(141)</b>	(221)	279
Changes in fair value of financial assets and liabilities and exchange movements			