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2 March 2010

Email: [codereview@frc.org.uk](mailto:codereview@frc.org.uk)

Dear Mr Hodge,

**Financial Reporting Council (“FRC”) Consultation on the Revised UK Corporate Governance Code (the “Code”)**

National Grid (the “Company”) is pleased to comment on this consultation, having also commented in 2009 on both the first and second consultations of the review of the effectiveness of the Combined Code.

At the outset we would like to emphasise our support for the FRC’s approach that the ‘comply or explain’ mechanism is retained as there is clear evidence in recent years that this flexible framework has led to meaningful governance by UK listed companies. We understand and support the underlying reasons for making the changes proposed and believe that most companies should be able to implement the new proposals without undue cost or difficulty.

Chairman’s preface and ‘Comply or Explain’

We are pleased that Sir Christopher Hogg acknowledges that the Code is ‘a guide only’ and ‘cannot guarantee effective board behaviour’. It is not always appropriate for some companies to comply with every aspect of the Code due to their individual circumstances and therefore this acknowledgement is received positively as more companies should feel that they can explain as opposed to comply.

We support Sir Christopher’s hope ‘that chairmen will choose to report personally in their annual statements how the principles [.....] relating to the role and effectiveness of the board have been applied’. However, as you will be aware from our Chairman Sir John Parker’s letter to you dated 13<sup>th</sup> May 2009, this could have been embedded in the provisions themselves or by means of a clearer requirement that chairmen will or are expected to report personally in their annual statements.

Section A: Leadership

We support the changes to this section of the Code. As an organisation, we believe we have always taken extremely seriously the culture and effectiveness of the Board and have tried to ensure constructive challenge and active participation in strategy discussions by all the non-executive directors. We believe the proposed changes will encourage a greater focus by more companies on board effectiveness and boardroom behaviours.

## Section B: Effectiveness

It is our view that our Chairman, along with the other members of our Nominations Committee, has always sought to ensure that the Board has an appropriate balance of skills, experience, independence and knowledge of the Company to discharge its duties and responsibilities effectively as required under the Code changes.

We are also pleased that that there is no minimum recommended time commitment from Directors proposed in the Code changes; the new words 'All Directors must be able to allocate sufficient time to the company to perform their responsibilities effectively' is sufficient to enable proper consideration of the issue.

## Section C: Accountability

As our Board already has overall and clear responsibility for risk management (and has had committees that look at different aspects of the Company's risk profile in place for many years) and setting the Company's risk appetite and tolerance, we are very happy this has been introduced as a main principle.

## Section D: Remuneration (and Schedule A)

As regards provisions on the design of performance-related remuneration for Executive Directors, the changes already reflect what many companies already have in place to align their interests with those of shareholders and to promote the long-term success of the company. Our Remuneration Committee considers risk, internal control and related matters when determining performance-related remuneration and it already includes non-financial performance metrics such as those linked to safety and environment in this process.

## Section E: Communication

We anticipate responding to the separate but related January 2010 'Consultation on a Stewardship Code for Institutional Investors'. We understand that Section E of the Code may be reinstated if sufficient progress is not made on that consultation. However, the FRC requested views on whether the proposed Stewardship Code for institutional investors can be operated effectively. It is difficult to see any adverse impact where companies and their major shareholders markedly increase the extent and quality of their communication, and that investors be encouraged by this to adopt a longer-term perspective in their decisions. Furthermore our view is that it is a good thing that investors be required to report governance on a 'comply or explain' mechanism. Dialogue should be ongoing and not a 'box-ticking exercise' by investors and should not be routine in nature for companies (i.e. reactive in nature to specific events), as is often the case. We acknowledge difficulties are likely to arise in relation to companies subject to the Disclosure and Transparency Rules in relation to the disclosure of potentially price-sensitive information. Overall though it is likely that more effective engagement should improve the governance and performance of companies, assist with the efficient operation of capital markets and increase confidence in business.

**Other areas on which FRC has specifically requested comment:**

a) New Provisions

As regards the 4 new provisions which will be subject to the 'comply or explain' requirement in the Listing Rules, the Company responds to each of these as follows:

- Director Development: In our view chairmen should have regular contact with each Board member which will often cover their contribution to the Board and areas identified for further knowledge building. All chairmen should have an annual meeting with each director to discuss in more detail the inputs and outputs of the company's Board and Committee evaluation survey and any resulting development needs. Whilst at present the outcome of these conversations may not be fully documented, the chairmen should be content to formalise this process.
- External Board evaluation: One area we have some concerns over is the proposed external facilitation at least every three years of the Board evaluation process. From our response to the second consultation, you will be aware that we do not believe it is appropriate to prescribe an externally facilitated review. What is not clear from the new provision is whether at least every three years the current process needs to be evaluated for effectiveness and facilitated to a degree by a third party or whether the third party needs to manage and run the process independently from the Company's personnel. We would therefore be grateful for some clarity here, since the latter option clearly leads to greater costs (we have been quoted up to £140,000 depending on the scope of services) and, potentially, little added value on our existing process. We continue to believe it is important to evaluate annually not just the effectiveness of the Board but also its Committees.
- Risk management: The Board of National Grid actively ensures it has a process in place to identify, evaluate and manage the significant risks and we have no concerns in this respect.
- Enhanced annual report disclosures: The Company's external auditors have already confirmed that the Company's annual report already includes an explanation of the Company's business model and overall financial strategy, thus there are no concerns with this new provision either.

b) Director Re-election

Regarding changes to existing provisions, the FRC has also asked for views on two options: the annual re-election of the chairman or the annual re-election of all directors. We are pleased the FRC has invited further comment on this area. We would prefer for there to be no change to our current practice. However, if this Code provision is endorsed in the final version and we decide it is appropriate to comply, then our preference is likely to be for the whole board to seek re-election annually. You will appreciate that many companies do have a significant number of members of the board (often as part of their compliance with the Code) and this will lead to many resolutions at the Annual General Meeting not necessarily to the benefit of shareholder debate. In our opinion and contrary to that of some institutional investors, we do not believe this makes Board members more accountable or that it will assist in improving communications between shareholders and the Board. Shareholders should be in a position to communicate freely with companies anyway on any area of concern without having to air them via such resolutions. Indeed, we suspect that annual re-election could

become routine anyway without a comply or explain requirement. We feel that our governance practices have always been rewarded by high levels of votes in favour of such resolutions and we do question the necessity of making voting on each Director a requirement.

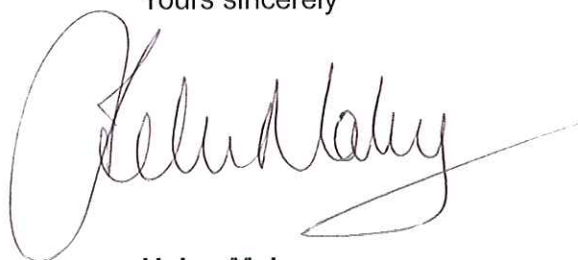
We do, however, welcome and support the view that a perceived lack of independence (in particular due to length of tenure) should not be considered an impediment for re-election where the individual brings clear skills, experience and knowledge to the Board, as noted by the deletion of the '9-year rule' if the Board as a whole stands for re-election. Many companies do find themselves in situations where the balance of experience and expertise over "independence" is important to ensure the non-executive directors offer 'constructive challenge' as required under the Code.

c) Use of Websites

The FRC also invited views on whether the requirements in the Code that certain information must be disclosed in the annual report should be amended to enable companies to take advantage of the flexibility allowed by being able to publish the corporate governance statement on their websites. We do not support this proposal. Our full annual report is already on the website and no other section of the document is split like this (noting the additional corporate social responsibility disclosures on our website are largely targeted at a different audience and are often numerical in nature). As a result this proposal could lead to confusion and potentially make web use a requirement which, if a shareholder has asked for all documents to be in paper format, would provide us with difficulties; as an organisation we endeavour to be inclusive to all our 1.1m shareholders.

We are pleased to respond to this consultation and look forward to the revised Code in April or May and note that the Code will likely apply to accounting periods beginning on or after 29 June 2010.

Yours sincerely

A handwritten signature in black ink, appearing to read 'Helen Mahy', with a long, sweeping underline that extends to the right.

**Helen Mahy**  
**Company Secretary and General Counsel**