# National Grid North America Inc. and Subsidiaries

Consolidated Financial Statements

For the years ended March 31, 2019 and 2018

**NATIONAL GRID NORTH AMERICA INC. AND SUBSIDIARIES**

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# INDEPENDENT AUDITORS' REPORT

To the Board of Directors of
National Grid North America Inc. and Subsidiaries

We have audited the accompanying consolidated financial statements of National Grid North America Inc. and Subsidiaries (the "Company"), which comprise the consolidated balance sheets and statements of capitalization as of March 31, 2019 and 2018, and the related consolidated statements of operations and comprehensive income, cash flows, and changes in shareholders' equity for each of the years then ended, and the related notes to the consolidated financial statements.

## Management's Responsibility for the Consolidated Financial Statements

Management is responsible for the preparation and fair presentation of these consolidated financial statements in accordance with accounting principles generally accepted in the United States of America; this includes the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of consolidated financial statements that are free from material misstatement, whether due to fraud or error.

## Auditors' Responsibility

Our responsibility is to express an opinion on these consolidated financial statements based on our audits. We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the consolidated financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the consolidated financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the consolidated financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the Company's preparation and fair presentation of the consolidated financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Company's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the consolidated financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

## Opinion

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of National Grid North America Inc. and Subsidiaries as of March 31, 2019 and 2018, and the results of its operations and its cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

Deloitte + Touche LLP

August 16, 2019

**NATIONAL GRID NORTH AMERICA INC. AND SUBSIDIARIES**
**CONSOLIDATED STATEMENTS OF OPERATIONS AND COMPREHENSIVE INCOME**
*(in millions of dollars)*

| | Years Ended March 31, | |
|---|---|---|
| | **2019** | 2018 |
| **Operating revenues** | **$ 12,815** | 12,173 |
| **Operating expenses:** | | |
| Purchased electricity | **1,914** | 1,737 |
| Purchased gas | **2,276** | 2,035 |
| Operations and maintenance | **4,661** | 4,443 |
| Depreciation | **1,173** | 1,082 |
| Other taxes | **1,251** | 1,203 |
| Total operating expenses | **11,275** | 10,500 |
| **Operating income** | **1,540** | 1,673 |
| **Other income and (deductions):** | | |
| Interest on long-term debt | **(582)** | (517) |
| Other interest, including affiliate interest | **(185)** | (176) |
| Income from equity investments | **51** | 39 |
| Loss on sale of assets | **-** | (45) |
| Other income (deductions), net | **40** | (8) |
| Total other deductions, net | **(676)** | (707) |
| **Income before income taxes** | **864** | 966 |
| **Income tax expense** | **198** | 440 |
| **Income from continuing operations** | **666** | 526 |
| Income from discontinued operations, net of taxes | **6** | 27 |
| **Net income** | **672** | 553 |
| Net income attributable to non-controlling interest | **(2)** | (2) |
| **Net income attributable to common shares** | **$ 670** | $ 551 |
| **Other comprehensive income (loss), net of taxes:** | | |
| Unrealized gains on securities, net of $0 and $(2) taxes in 2019 and 2018, respectively | **1** | 2 |
| Change in pension and other postretirement obligations, net of $0 and $(58) taxes in 2019 and 2018, respectively | **20** | 111 |
| Unrealized (losses) gains on hedges, net of $11 and $(3) taxes in 2019 and 2018, respectively | **(28)** | 10 |
| Reclassification to regulatory asset, net of $0 and $(168) taxes in 2019 and 2018, respectively | **-** | 429 |
| **Total other comprehensive (loss) income** | **(7)** | 552 |
| **Comprehensive income** | **$ 665** | $ 1,105 |
| Less: comprehensive income attributable to non-controlling interest | **(2)** | (2) |
| **Comprehensive income attributable to common shares** | **$ 663** | $ 1,103 |

The accompanying notes are an integral part of these consolidated financial statements.

## NATIONAL GRID NORTH AMERICA INC. AND SUBSIDIARIES
## CONSOLIDATED STATEMENTS OF CASH FLOWS
*(in millions of dollars)*

| | Years Ended March 31, | |
|---|---|---|
| | **2019** | 2018 |
| **Operating activities:** | | |
| Net income | **$ 672** | $ 553 |
| Adjustments to reconcile net income to net cash provided by operating activities: | | |
| Depreciation | **1,173** | 1,082 |
| Regulatory amortizations | **22** | 80 |
| Deferred income tax | **246** | 400 |
| Bad debt expense | **188** | 136 |
| Income from equity and financial investments, net of dividends received | **(38)** | (32) |
| Loss on sale of assets | **-** | 45 |
| Allowance for equity funds used during construction | **(62)** | (27) |
| Amortization of debt discount and issuance costs | **25** | 20 |
| Stock-based compensation | **19** | 19 |
| Pension and postretirement benefit expenses, net | **235** | 399 |
| Pension and postretirement benefit contributions | **(294)** | (411) |
| Environmental remediation payments | **(50)** | (80) |
| Changes in operating assets and liabilities: | | |
| Accounts receivable and unbilled revenues | **(49)** | (565) |
| Inventory | **(21)** | 13 |
| Regulatory assets and liabilities, net | **345** | 254 |
| Derivative instruments | **(81)** | (79) |
| Prepaid and accrued taxes | **(105)** | 213 |
| Accounts payable and other liabilities | **1** | 256 |
| Renewable energy certificate obligations, net | **22** | 46 |
| Other, net | **80** | (47) |
| Net cash provided by operating activities | **2,328** | 2,275 |
| **Investing activities:** | | |
| Capital expenditures | **(3,113)** | (3,285) |
| Proceeds from sale of assets | **-** | 172 |
| Cost of removal | **(245)** | (238) |
| Contributions in equity and financial investments | **(163)** | (122) |
| Purchases of financial investments | **(88)** | - |
| Proceeds from sales of financial investments | **89** | - |
| Other | **(17)** | - |
| Net cash used in investing activities | **(3,537)** | (3,473) |
| **Financing activities:** | | |
| Payments on long-term debt | **(2,573)** | (3,253) |
| Proceeds from long-term debt | **3,191** | 4,158 |
| Payment of debt issuance costs | **(26)** | (16) |
| Commercial paper issued | **8,032** | - |
| Commercial paper paid | **(7,178)** | (692) |
| Advance from affiliate | **-** | (653) |
| Equity infusion from Parent | **-** | 1,291 |
| Payments on sale/leaseback arrangement | **(27)** | (41) |
| Other | **3** | - |
| Net cash provided by financing activities | **1,422** | 794 |
| Net increase (decrease) in cash, cash equivalents, restricted cash and special deposits | **213** | (404) |
| Net cashflow from discontinued operations - operating | **(1)** | 29 |
| Cash, cash equivalents, restricted cash and special deposits, beginning of year | **453** | 828 |
| Cash, cash equivalents, restricted cash and special deposits, end of year | **$ 665** | $ 453 |
| **Supplemental disclosures:** | | |
| Interest paid | **$ (639)** | $ (614) |
| Income taxes refunded | **45** | 62 |
| **Significant non-cash items:** | | |
| Capital-related accruals included in accounts payable | **299** | 157 |
| Reclassification to regulatory asset | **-** | 597 |

The accompanying notes are an integral part of these consolidated financial statements.

**NATIONAL GRID NORTH AMERICA INC. AND SUBSIDIARIES**
**CONSOLIDATED BALANCE SHEETS**
*(in millions of dollars)*

| | March 31, | |
|---|---|---|
| | **2019** | 2018 |
| **ASSETS** | | |
| **Current assets:** | | |
| Cash and cash equivalents | **$ 547** | $ 380 |
| Restricted cash and special deposits | **118** | 73 |
| Accounts receivable | **2,530** | 2,613 |
| Allowance for doubtful accounts | **(445)** | (411) |
| Unbilled revenues | **556** | 578 |
| Inventory | **394** | 356 |
| Regulatory assets | **359** | 535 |
| Derivative instruments | **33** | 24 |
| Accrued tax benefits and prepaid taxes | **350** | 260 |
| Other | **131** | 140 |
| Total current assets | **4,573** | 4,548 |
| **Equity investments** | **406** | 302 |
| **Property, plant and equipment, net** | **34,299** | 31,874 |
| **Other non-current assets:** | | |
| Regulatory assets | **5,136** | 5,192 |
| Goodwill | **7,129** | 7,129 |
| Derivative instruments | **28** | 158 |
| Postretirement benefits asset | **382** | 359 |
| Financial investments | **760** | 671 |
| Other | **170** | 266 |
| Total other non-current assets | **13,605** | 13,775 |
| **Total assets** | **$ 52,883** | $ 50,499 |

The accompanying notes are an integral part of these consolidated financial statements.

**NATIONAL GRID NORTH AMERICA INC. AND SUBSIDIARIES**
**CONSOLIDATED BALANCE SHEETS**
*(in millions of dollars)*

| | March 31, | |
|---|---|---|
| | **2019** | 2018 |
| **LIABILITIES AND CAPITALIZATION** | | |
| **Current liabilities:** | | |
| Accounts payable | **$ 1,742** | $ 1,573 |
| Accounts payable to affiliates | **35** | 36 |
| Commercial paper | **1,144** | 290 |
| Current portion of long-term debt | **1,280** | 2,602 |
| Taxes accrued | **124** | 132 |
| Customer deposits | **106** | 111 |
| Interest accrued | **192** | 159 |
| Regulatory liabilities | **1,065** | 1,039 |
| Derivative instruments | **71** | 90 |
| Renewable energy certificate obligations | **221** | 189 |
| Payroll and benefits accruals | **339** | 334 |
| Other | **391** | 405 |
| Total current liabilities | **6,710** | 6,960 |
| **Other non-current liabilities:** | | |
| Regulatory liabilities | **6,276** | 6,189 |
| Asset retirement obligations | **99** | 95 |
| Deferred income tax liabilities, net | **3,402** | 3,167 |
| Postretirement benefits | **1,837** | 1,932 |
| Environmental remediation costs | **1,902** | 1,874 |
| Derivative instruments | **125** | 79 |
| Other | **792** | 861 |
| Total other non-current liabilities | **14,433** | 14,197 |
| **Commitments and contingencies (Note 15)** | | |
| **Capitalization:** | | |
| Common and preferred stock | **9,616** | 9,597 |
| Retained earnings | **5,451** | 4,761 |
| Accumulated other comprehensive loss | **(132)** | (104) |
| Common and preferred equity | **14,935** | 14,254 |
| Non-controlling interest | **25** | 23 |
| Total shareholders' equity | **14,960** | 14,277 |
| Long-term debt | **16,780** | 15,065 |
| **Total capitalization** | **31,740** | 29,342 |
| **Total liabilities and capitalization** | **$ 52,883** | $ 50,499 |

The accompanying notes are an integral part of these consolidated financial statements.

**NATIONAL GRID NORTH AMERICA INC. AND SUBSIDIARIES**
**CONSOLIDATED STATEMENTS OF CAPITALIZATION**
*(in millions of dollars)*

| | | | March 31, | |
|---|---|---|---|---|
| | | | **2019** | 2018 |
| **Common and preferred equity** | | | **$ 14,935** | $ 14,254 |
| **Non-controlling interest** | | | **25** | 23 |
| **Long-term debt:** | Interest Rate | Maturity Date | | |
| European Medium Term Note | Variable | August 2019 - June 2028 | **3,542** | 4,613 |
| Convertible Bond | Variable | November 2020 | **521** | 561 |
| Export Credit Agreements | Variable | December 2025 - March 2027 | **449** | 129 |
| Notes Payable[1] | 2.72% - 9.75% | August 2019 - March 2049 | **11,540** | 9,710 |
| First Mortgage Bonds | 6.82% - 9.63% | May 2020 - April 2028 | **105** | 121 |
| State Authority Financing Bonds | 3.23% - 3.48% | December 2023 - July 2029 | **424** | 429 |
| State Authority Financing Bonds | Variable | November 2020 - August 2042 | **410** | 410 |
| Intercompany Notes | Variable | July 2019 - July 2027 | **1,172** | 1,788 |
| Total debt | | | **18,163** | 17,761 |
| Unamortized debt discount | | | **(40)** | (40) |
| Unamortized debt issuance costs | | | **(63)** | (54) |
| Current portion of long-term debt | | | **(1,280)** | (2,602) |
| Long-term debt | | | **16,780** | 15,065 |
| **Total capitalization** | | | **$ 31,740** | $ 29,342 |

[1] See Note 12, "Capitalization" under "Notes Payable" for additional details.

The accompanying notes are an integral part of these consolidated financial statements.

# NATIONAL GRID NORTH AMERICA INC. AND SUBSIDIARIES
## CONSOLIDATED STATEMENTS OF CHANGES IN SHAREHOLDERS' EQUITY
*(in millions of dollars)*

| | Common Stock | Cumulative Preferred Stock | Additional Paid-in Capital | Accumulated Other Comprehensive Income (Loss): Unrealized Gain (Loss) on Available-For-Sale Securities | Pension and Other Postretirement Benefits | Equity Investments | Hedging Activity | Foreign Currency Translation | Total Accumulated Other Comprehensive Income (Loss) | Retained Earnings | Non-controlling Interest | Total |
|---|---|---|---|---|---|---|---|---|---|---|---|---|
| **Balance as of March 31, 2017** | **$ -** | **$ 35** | **$ 8,252** | **$ 12** | **$ (562)** | **$ -** | **$ 33** | **$ (139)** | **$ (656)** | **$ 4,206** | **$ 21** | **$ 11,858** |
| Net income | - | - | - | - | - | - | - | - | - | 551 | 2 | 553 |
| Other comprehensive income: | | | | | | | | | | | | |
| Unrealized gains on securities, net of $2 tax expense | - | - | - | 2 | - | - | - | - | 2 | - | - | 2 |
| Change in pension and other postretirement obligations, net of $58 tax expense | - | - | - | - | 111 | - | - | - | 111 | - | - | 111 |
| Reclassification to regulatory asset, net of $168 tax expense | - | - | - | - | 429 | - | - | - | 429 | - | - | 429 |
| Unrealized gains on hedges, net of $3 tax expense | - | - | - | - | - | - | 10 | - | 10 | - | - | 10 |
| Total comprehensive income | | | | | | | | | | | | 1,105 |
| Issuance of common stock | - | - | 1,291 | - | - | - | - | - | - | - | - | 1,291 |
| Stock-based compensation | - | - | 19 | - | - | - | - | - | - | 4 | - | 23 |
| **Balance as of March 31, 2018** | **$ -** | **$ 35** | **$ 9,562** | **$ 14** | **$ (22)** | **$ -** | **$ 43** | **$ (139)** | **$ (104)** | **$ 4,761** | **$ 23** | **$ 14,277** |
| Net income | - | - | - | - | - | | - | - | - | 670 | 2 | 672 |
| Other comprehensive income (loss): | | | | | | | | | | | | |
| Unrealized gains on securities, net of $0 tax expense | - | - | - | 1 | - | - | - | - | 1 | - | - | 1 |
| Change in pension and other postretirement obligations, net of $0 tax expense | - | - | - | - | 20 | - | - | - | 20 | - | - | 20 |
| Unrealized losses on hedges, net of $11 tax benefit | - | - | - | - | - | - | (28) | - | (28) | - | - | (28) |
| Total comprehensive income | | | | | | | | | - | | | 665 |
| | | | | | | | | | - | | | |
| Impact of adoption of the recognition and measurement of financial assets and liabilities standard | - | - | - | (8) | - | - | (13) | - | (21) | 20 | - | (1) |
| Stock-based compensation | - | - | 19 | - | - | - | - | - | - | - | - | 19 |
| **Balance as of March 31, 2019** | **$ -** | **$ 35** | **$ 9,581** | **$ 7** | **$ (2)** | **$ -** | **$ 2** | **$ (139)** | **$ (132)** | **$ 5,451** | **$ 25** | **$ 14,960** |

The Company had 196 shares of common stock authorized, issued and outstanding, with a par value of $0.10 per share at March 31, 2019 and 2018, and 372,641 shares of cumulative preferred stock authorized, issued and outstanding, with par values of $100 and $50 per share at March 31, 2019 and 2018.

The accompanying notes are an integral part of these consolidated financial statements.

## NATIONAL GRID NORTH AMERICA INC. AND SUBSIDIARIES
## NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

### 1. NATURE OF OPERATIONS AND BASIS OF PRESENTATION

National Grid North America Inc. ("NGNA" or "the Company") is a Delaware corporation that was created on May 16, 2001 to finance acquisitions in the United States ("U.S."). The Company is an indirect wholly-owned subsidiary of National Grid plc (the "Parent"), a public limited company incorporated under the laws of England and Wales. It is the intermediate holding company of National Grid USA ("NGUSA") and acts as a funding company on behalf of the Parent for certain subsidiaries' borrowings.

NGUSA has two major lines of business, "Gas Distribution" and "Electric Services," and operates various energy services and investment companies. The Company's Gas Distribution business consists of six gas distribution subsidiaries which provide gas distribution services to customers in the areas of central, northern, and eastern New York, the New York City boroughs of Brooklyn, Queens, and Staten Island, and the Long Island Counties of Nassau and Suffolk, as well as the states of Massachusetts and Rhode Island. The Company's Electric Services business primarily consists of five electric distribution subsidiaries which provide electric services to customers in the areas of eastern, central, northern, and western New York, as well as the states of Massachusetts and Rhode Island and operate electric transmission facilities in Massachusetts, New Hampshire, Rhode Island, Maine, and Vermont.

The Company's wholly-owned New England subsidiaries include: New England Power Company ("NEP"), The Narragansett Electric Company ("Narragansett"), Massachusetts Electric Company ("Massachusetts Electric"), Nantucket Electric Company ("Nantucket"), Boston Gas Company ("Boston Gas"), and Colonial Gas Company ("Colonial Gas"). The Company's wholly-owned New York subsidiaries include: Niagara Mohawk Power Corporation ("Niagara Mohawk"), National Grid Generation, LLC ("Genco"), The Brooklyn Union Gas Company ("Brooklyn Union"), and KeySpan Gas East Corporation ("KeySpan Gas East").

Genco provides energy services and supply capacity to and produces energy for the use of customers of the Long Island Power Authority ("LIPA") on Long Island, New York. The services provided to LIPA through the Power Supply Agreement ("PSA"), which was amended and restated for a maximum term of 15 years in May 2013, provide LIPA with electric generating capacity, energy conversion, and ancillary services from the Company's Long Island generating units.

Prior to December 31, 2013, the Company also provided operation, maintenance and construction services, and significant administrative services relating to the Long Island electric transmission and distribution system owned by LIPA. These activities, primarily settlement of legacy contingencies, are reflected as discontinued operations in the accompanying consolidated financial statements for the years ended March 31, 2019 and 2018.

The Company's energy investments business consists of development investments such as natural gas pipelines, as well as certain other domestic energy-related investments. The Company has a wholly-owned subsidiary, National Grid LNG LLC, which is engaged in the business of receiving, storing, and redelivering liquefied natural gas ("LNG") in liquid and gaseous states, through facilities located in Providence, Rhode Island. The Company also owns a 53.7% interest in two hydro-transmission electric companies which are consolidated into these financial statements.

The Company uses the equity method of accounting for its investments in affiliates when it has the ability to exercise significant influence over the operating and financial policies, but does not control the affiliates. The Company's share of the earnings or losses of such affiliates is included as income from equity investments in the accompanying consolidated statements of operations and comprehensive income.

The accompanying consolidated financial statements are prepared in accordance with accounting principles generally accepted in the United States of America ("U.S. GAAP"), including the accounting principles for rate-regulated entities as applicable. The consolidated financial statements reflect the ratemaking practices of the applicable regulatory authorities.

The consolidated financial statements include the accounts of the Company and its wholly-owned subsidiaries. Non-controlling interests of majority-owned subsidiaries are calculated based upon the respective non-controlling interest ownership percentages. All intercompany transactions have been eliminated in consolidation.

Under its holding company structure, the Company does not have significant independent operations or source of income of its own and conducts most of its operations through its subsidiaries. As a result, the Company depends on the earnings and cash flow of, and dividends or distributions from, its subsidiaries to provide the funds necessary to meet its debt and contractual obligations. Furthermore, a substantial portion of the Company's consolidated assets, earnings, and cash flow is derived from the operations of its regulated utility subsidiaries, whose legal authority to pay dividends or make other distributions to the Company is subject to regulation by state regulatory authorities.

The Company has evaluated subsequent events and transactions through August 16, 2019, the date of issuance of these consolidated financial statements, and concluded that there were no events or transactions that require adjustment to, or disclosure in, the consolidated financial statements as of and for the year ended March 31, 2019, except as described in Note 19, "Subsequent Events."

## 2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

### Use of Estimates

In preparing consolidated financial statements that conform to U.S. GAAP, the Company must make estimates and assumptions that affect the reported amounts of assets, liabilities, revenues, and expenses, and the disclosure of contingent assets and liabilities included in the consolidated financial statements. Actual results could differ from those estimates.

### Regulatory Accounting

The Federal Energy Regulatory Commission ("FERC"), the New York Public Service Commission ("NYPSC"), the Massachusetts Department of Public Utilities ("DPU"), and the Rhode Island Public Utilities Commission ("RIPUC") regulate the rates the Company's regulated subsidiaries charge their customers in the applicable states. In certain cases, the rate actions of the FERC, NYPSC, DPU and RIPUC can result in accounting that differs from non-regulated companies. In these cases, the subsidiaries defer costs (as regulatory assets) or recognize obligations (as regulatory liabilities) if it is probable that such amounts will be recovered from, or refunded to, customers through future rates. In accordance with Accounting Standards Codification ("ASC") 980, "Regulated Operations," regulatory assets and liabilities are reflected on the consolidated balance sheets consistent with the treatment of the related costs in the ratemaking process.

### Revenue Recognition

Revenues are recognized for energy service provided on a monthly billing cycle basis. Revenues are recognized for sales of capacity and energy to LIPA under terms of the amended and restated ("A&R") PSA, with rates approved by the FERC. See Note 15, "Commitments and Contingencies" under "Electric Services and LIPA Agreements," for additional information on the A&R PSA. The Company records unbilled revenues for the estimated amount of services rendered from the time meters were last read to the end of the accounting period (see Note 4, "Revenue" for additional details).

### Other Taxes

The Company's subsidiaries collect taxes and fees from customers such as sales taxes, other taxes, surcharges, and fees that are levied by state or local governments on the sale or distribution of gas and electricity. The Company accounts for taxes that are imposed on customers (such as sales taxes) on a net basis (excluded from revenues), while taxes imposed on the Company, such as excise taxes, are recognized on a gross basis. Excise taxes collected and paid for the years ended March 31, 2019 and 2018 were $115 million and $112 million, respectively.

The state of New York imposes a franchise tax that is computed as the higher of a tax based on income or a tax based on capital. To the extent the Company's New York state ("NYS") tax based on capital is in excess of the state tax based on income, the Company reports such excess in other taxes and taxes accrued in the accompanying consolidated financial statements.

**Income Taxes**

Federal and state income taxes have been computed utilizing the asset and liability approach that requires the recognition of deferred tax assets and liabilities for the tax consequences of temporary differences by applying enacted statutory tax rates applicable to future years to differences between the carrying amounts and the tax basis of existing assets and liabilities. Deferred income taxes also reflect the tax effect of net operating losses, capital losses, and general business credit carryforwards. The Company assesses the available positive and negative evidence to estimate whether sufficient future taxable income of the appropriate tax character will be generated to realize the benefits of existing deferred tax assets. When the evaluation of the evidence indicates that the Company will not be able to realize the benefits of existing deferred tax assets, a valuation allowance is recorded to reduce existing deferred tax assets to the net realizable amount.

The effects of tax positions are recognized in the consolidated financial statements when it is more likely than not that the position taken, or expected to be taken, in a tax return will be sustained upon examination by taxing authorities based on the technical merits of the position. The financial effect of changes in tax laws or rates is accounted for in the period of enactment. Deferred investment tax credits are amortized over the useful life of the underlying property.

NGNA files consolidated federal tax returns including all of the activities of its subsidiaries. Each subsidiary determines its tax provision based on the separate return method, modified by a benefits-for-loss allocation pursuant to a tax sharing agreement between NGNA and its subsidiaries. The benefit of consolidated tax losses and credits are allocated to the NGNA subsidiaries giving rise to such benefits in determining each subsidiary's tax expense in the year that the loss or credit arises. In a year that a consolidated loss or credit carryforward is utilized, the tax benefit utilized in consolidation is paid proportionately to the subsidiaries that gave rise to the benefit regardless of whether that subsidiary would have utilized the benefit. The tax sharing agreement also requires NGNA to allocate its parent tax losses, excluding deductions from acquisition indebtedness, to each subsidiary in the consolidated federal tax return with taxable income. The allocation of NGNA's parent tax losses to its subsidiaries is accounted for as a capital contribution and is performed in conjunction with the annual intercompany cash settlement process following the filing of the federal tax return.

**Cash and Cash Equivalents**

Cash equivalents consist of short-term, highly liquid investments with original maturities of three months or less. Cash and cash equivalents are carried at cost which approximates fair value.

**Restricted Cash and Special Deposits**

Restricted cash consists of margin calls to the New York Mercantile Exchange ("NYMEX") and collateral paid to the Company's counterparties for outstanding commodity and financial derivative instruments. Special deposits primarily consist of health care deposits, a release of property account for mortgaged property under a mortgage trust indenture, and a reserve for potential environmental violations. The Company had restricted cash of $76 million and $22 million and special deposits of $42 million and $51 million at March 31, 2019 and 2018, respectively.

The following table reconciles cash, cash equivalents, restricted cash and special deposits as reported on the consolidated balance sheets, to the cash, cash equivalents, restricted cash, and special deposits as reported in the accompanying consolidated statements of cash flows:

| | Years Ended March 31, | |
|---|---|---|
| | **2019** | 2018 |
| | *(in millions of dollars)* | |
| Cash and cash equivalents as reported on the consolidated balance sheets | **$ 547** | $ 380 |
| Restricted cash and special deposits as reported on the consolidated balance sheets | **118** | 73 |
| Cash, cash equivalents, restricted cash and special deposits reported in the consolidated statement of cash flows | **$ 665** | $ 453 |

**Accounts Receivable and Allowance for Doubtful Accounts**

The Company recognizes an allowance for doubtful accounts to record accounts receivable at estimated net realizable value. The allowance is determined based on a variety of factors including, for each type of receivable, applying an estimated reserve percentage to each aging category, taking into account historical collection and write-off experience, and management's assessment of collectability from individual customers, as appropriate. The collectability of receivables is continuously assessed and, if circumstances change, the allowance is adjusted accordingly. Receivable balances are written off against the allowance for doubtful accounts when the accounts are disconnected and/or terminated and the balances are deemed to be uncollectible. The Company recorded bad debt expense of $188 million and $136 million for the years ended March 31, 2019 and 2018, respectively, within operations and maintenance in the accompanying consolidated statements of operations and comprehensive income.

**Inventory**

Inventory is composed of materials and supplies, emission credits, renewable energy certificates (“RECs”), and gas in storage.

Materials and supplies are stated at weighted average cost, which represents net realizable value, and are expensed or capitalized as used. There were no significant write-offs of obsolete inventory for the years ended March 31, 2019 or 2018.

Emission credits are comprised of sulfur dioxide, nitrogen oxide (“NOx”), and carbon dioxide credits. Emission credits are valued at the lower of weighted average cost or net realizable value and are held primarily for consumption or may be sold to third-party purchasers. RECs are stated at cost and used to measure compliance with renewable energy standards. RECs are held primarily for consumption.

Gas in storage is stated at weighted average cost and the related cost is recognized when delivered to customers. Existing rate orders allow the Company to pass directly through to customers the cost of gas purchased, along with any applicable authorized delivery surcharge adjustments. Gas costs passed through to customers are subject to regulatory approvals and are reported periodically to the applicable state regulators.

The Company had materials and supplies of $159 million and $162 million, emission credits of $11 million and $4 million, purchased RECs of $100 million and $90 million, and gas in storage of $124 million and $100 million at March 31, 2019 and 2018, respectively.

**Derivative Instruments**

The Company uses derivative instruments to manage commodity price, interest rate, and foreign currency rate risk. All derivative instruments, except those that qualify for the normal purchase normal sale exception, are recorded on the consolidated balance sheets at their fair value. All commodity costs, including the impact of derivative instruments, are passed on to customers through the Company’s commodity rate adjustment mechanisms. Regulatory assets or regulatory

liabilities are recorded to defer the recognition of unrealized losses or gains on derivative instruments, respectively. The gains or losses on the settlement of these contracts are recognized as purchased electricity and purchased gas in the accompanying consolidated statements of operations and comprehensive income and then refunded to, or collected from, customers consistent with regulatory requirements. Qualifying derivative instruments may be designated as either cash flow hedges or fair value hedges.

The effective portion of the change in fair value of a cash flow hedge is recorded in accumulated other comprehensive income ("AOCI"), net of related tax effects, and the ineffective portion is reported in earnings. Amounts in AOCI are reclassified into earnings in the same period or periods during which the hedged item affects earnings. The effective portion of the change in the fair value of a fair value hedge is offset in the accompanying consolidated statements of operations and comprehensive income by changes in the hedged item. If the hedge relationship is terminated, the fair value adjustment to the hedged item continues to be reported as part of the basis of the item and is amortized to the accompanying consolidated statements of operations and comprehensive income as a yield adjustment over the remainder of the hedging period. For the years ended March 31, 2019 and 2018, the Company recorded ineffectiveness related to cash flow hedges of a $2 million gain and zero, respectively within other income (deductions), net in the accompanying consolidated statements of operations and comprehensive income.

The Company has certain non-trading instruments for the physical purchase of electricity that qualify for the normal purchase normal sale exception and are accounted for upon settlement. If the Company were to determine that a contract no longer qualifies for the normal purchase normal sale exception, then the Company would recognize the fair value of the contract and account for the gains and losses using the regulatory accounting described above.

The Company's accounting policy is to not offset fair value amounts recognized for derivative instruments and related cash collateral receivable or payable with the same counterparty under a master netting agreement, but rather to record and present the fair value of the derivative instrument on a gross basis, with related cash collateral recorded within restricted cash and special deposits on the consolidated balance sheets.

**Variable Interest Entities**

A variable interest entity ("VIE") is an entity that does not have a sufficient equity investment at risk to permit it to finance its activities without additional subordinated financial support, or whose equity investors lack the obligation to absorb losses, the right to receive residual returns, or the right to make decisions about the entity's activities. The primary beneficiary is the business enterprise that has the power to direct the activities of the VIE that most significantly impact the VIE's economic performance and either absorbs a significant amount of the VIE's losses or has the right to receive the benefits that could be significant to the VIE. The primary beneficiary holds a controlling financial interest in an entity and is required to consolidate the VIE.

The Company determines whether they are the primary beneficiary of a VIE by evaluating the purpose and design of the entity, the nature of the VIE's risks and the risks that the Company absorbs, who has the power to direct the activities of the VIE that most significantly impact the economic performance of the VIE, and who has the obligation to absorb losses or receive benefits that could be significant to the VIE.

The Company has non-controlling interests in Yankee Atomic (34.5%), Connecticut Yankee (19.5%), and Maine Yankee (24%) (the "Yankees") which own nuclear generating facilities that are permanently retired and are being decommissioned. Additionally, the Company has a 50% interest in Generation Ventures and Sunrun Neptune Investor 2016 LLC ("Sunrun").

**Power Purchase Agreements**

Certain of the Company's subsidiaries enter into power purchase agreements ("PPAs") to procure electricity to serve their electric service customers. The Company evaluates whether such agreements are leases, derivative instruments, or executory contracts and performs an assessment under the guidance for VIE, included in Topic 810, "Consolidations." PPAs that do not qualify as leases or derivative instruments are accounted for as executory contracts and are, therefore, recognized as the electricity is purchased. In making its determination of the accounting for PPAs, the Company considers many factors,

including: the source of the electricity; the level of output from any specified facility that the Company is taking under the contract; the involvement, if any, that the Company has in operating the specified facility; and the pricing mechanisms in the contract.

**Natural Gas Long-Term Arrangements**

Certain of the Company's subsidiaries enter into long-term gas contracts to procure gas to serve their gas customers. Those contracts include Asset Management Agreements, Baseload, and Peaking gas contracts. Similar to the PPAs noted above, the Company evaluates whether such agreements are leases, derivative instruments, or executory contracts and performs an assessment under the guidance for VIE included in Topic 810, "Consolidations," and applies the appropriate accounting treatment.

**Fair Value Measurements**

The Company measures derivative instruments, securities, pension and postretirement benefit other than pension plan ("PBOP") assets, and financial assets for which it has elected the fair value option at fair value. Fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. The following is the fair value hierarchy that prioritizes the inputs to valuation techniques used to measure fair value:

- Level 1: quoted prices (unadjusted) in active markets for identical assets or liabilities that a company has the ability to access as of the reporting date;
- Level 2: inputs other than quoted prices included within Level 1 that are directly observable for the asset or liability or indirectly observable through corroboration with observable market data;
- Level 3: unobservable inputs, such as internally-developed forward curves and pricing models for the asset or liability due to little or no market activity for the asset or liability with low correlation to observable market inputs; and
- Not categorized: certain investments are not categorized within the fair value hierarchy. These investments are typically in commingled funds or limited partnerships that are not publicly traded and have ongoing subscription and redemption activity. As a practical expedient, the fair value of these investments is the Net Asset Value ("NAV") per fund share, derived from the underlying securities' quoted prices in active markets.

The asset or liability's fair value measurement level within the fair value hierarchy is based on the lowest level of any input that is significant to the fair value measurement. The Company uses valuation techniques that maximize the use of observable inputs and minimize the use of unobservable inputs.

**Property, Plant and Equipment**

Property, plant and equipment is stated at original cost. The cost of repairs and maintenance is charged to expense and the cost of renewals and betterments that extend the useful life of property, plant and equipment is capitalized. The capitalized cost of additions to property, plant and equipment includes costs such as direct material, labor and benefits, and an allowance for funds used during construction ("AFUDC").

Depreciation is computed over the estimated useful life of the asset using the composite straight-line method. Depreciation studies are conducted periodically to update the composite rates and are approved by the state authorities. The average composite rates for the years ended March 31, 2019 and 2018 are as follows:

| | Composite Rates | |
| --- | --- | --- |
| | Years Ended March 31, | |
| | **2019** | 2018 |
| Electric | **2.9%** | 2.6% |
| Gas | **2.8%** | 2.9% |
| Common | **8.7%** | 8.5% |

Depreciation expense, for regulated subsidiaries, includes a component for the estimated cost of removal, which is recovered through rates charged to customers. Any difference in cumulative costs recovered and costs incurred is recognized as a regulatory liability. When property, plant and equipment is retired, the original cost, less salvage, is charged to accumulated depreciation, and the related cost of removal is removed from the associated regulatory liability. The Company recognized a regulatory liability for the amount that was in excess of costs incurred of $1.7 billion at both March 31, 2019 and 2018.

*Allowance for Funds Used During Construction*

The Company records AFUDC, which represents the debt and equity costs of financing the construction of new property, plant and equipment. The equity component of AFUDC is reported in the accompanying consolidated statements of operations and comprehensive income as non-cash income in other income (deductions), net. The debt component of AFUDC is reported as a non-cash offset to other interest, including affiliate interest. After construction is completed, the Company is permitted to recover these costs through their inclusion in rate base. The Company recorded AFUDC related to equity of $62 million and $27 million and AFUDC related to debt of $34 million and $20 million for the years ended March 31, 2019 and 2018, respectively. The average AFUDC rates for the years ended March 31, 2019 and 2018 were 6.1% and 4.1%, respectively.

*Impairment of Long-Lived Assets*

The Company tests the impairment of long-lived assets when events or changes in circumstances indicate that the carrying amount of the asset may not be recoverable. The recoverability of an asset is determined by comparing its carrying value to the estimated undiscounted cash flows that the asset is expected to generate. If the comparison indicates that the carrying value is not recoverable, an impairment loss is recognized for the excess of the carrying value over the estimated fair value. For the years ended March 31, 2019 and 2018, there were no impairment losses recognized for long-lived assets.

**Goodwill**

The Company tests goodwill for impairment annually on January 1, and when events occur, or circumstances change that would more likely than not reduce the fair value of each of the Company's respective reporting units below the carrying amount. The Company tests its goodwill based upon four identified reporting units, aligned with its jurisdictional operational model. The Company has early adopted Accounting Standards Update ("ASU") No. 2017-04, "Intangibles—Goodwill and Other (Topic 350): Simplifying the Test for Goodwill Impairment," which eliminates step two from the two-step goodwill impairment test. The one-step approach requires a recoverability test performed based on the comparison of the Company's estimated fair value for each reporting unit with the carrying value, including goodwill. If the estimated fair value exceeds the carrying value, then goodwill is not considered impaired. If the carrying value exceeds the estimated fair value, the Company is required to recognize an impairment charge for such excess, limited to the allocated amount of goodwill.

Historically, the fair value of each reporting unit was calculated for the annual goodwill impairment test utilizing both income and market approaches. For the year ended March 31, 2019, the fair value of the Company was calculated utilizing solely the income approach. The Company believes that this approach provides the most reliable information about the Company's estimated fair value. Key assumptions in the income approach include the discount rate of 5.3% (2018: 5.3%) and the terminal growth rate of 2.2% (2018: 2.3%). Based on the resulting fair values from the annual analyses, the relative headroom in the four reporting units ranged from 25% to 82% for 2019 and 20% to 55% for 2018, and, as a result, the Company determined that no adjustment to the goodwill carrying value was required at March 31, 2019 or 2018.

**Financial Investments**

Financial investments are primarily comprised of securities and funds designated for Supplemental Executive Retirement Plans. Other financial investments are subsequently measured at fair value through profit and loss and are primarily comprised of money market funds, insurance company fund investments, and corporate venture capital investments held by National Grid Partners ("NGP").

The Company holds securities that include equities, municipal bonds, and corporate bonds. These investments are recorded at fair value. Changes in the fair value of these assets are recorded within other comprehensive income.

Both the Company's securities and NGP investments are recorded at fair value and included in the tables in Note 10, "Fair Value Measurements."

The Company also has corporate assets representing funds designated for Supplemental Executive Retirement Plans. These funds are invested in corporate owned life insurance policies and securities primarily consisting of equity investments and investments in municipal and corporate bonds. The corporate owned life insurance investments are measured at cash surrender value, not recorded at fair value, with increases and decreases in the value of these assets recorded in the accompanying consolidated statements of operations and comprehensive income.

The following table presents the financial investments recorded on the consolidated balance sheets:

| | March 31, | |
|---|---|---|
| | **2019** | 2018 |
| | *(in millions of dollars)* | |
| Securities | **$ 400** | $ 386 |
| Supplemental Executive Retirement Plans | **288** | 281 |
| Other | **72** | 4 |
| Total | **$ 760** | $ 671 |

On February 13, 2018, the Company obtained board approval to sell its investment in Dominion Midstream Partners, LP ("DM"). The Company completed the sale of its investment in DM to Deutsche Bank for proceeds of $172 million, which settled February 21, 2018. The transaction resulted in a loss on sale of assets of $45 million in the year ended March 31, 2018. The Company's investment in DM was previously included within financial investments on the consolidated balance sheet.

**Asset Retirement Obligations**

Asset retirement obligations are recognized for legal obligations associated with the retirement of property, plant and equipment, primarily associated with the Company's gas distribution and electric generation facilities. Asset retirement obligations are recorded at fair value in the period in which the obligation is incurred, if the fair value can be reasonably estimated. In the period in which new asset retirement obligations, or changes to the timing or amount of existing retirement obligations are recorded, the associated asset retirement costs are capitalized as part of the carrying amount of the related long-lived asset. In each subsequent period the asset retirement obligation is accreted to its present value. The Company applies regulatory accounting guidance and both the depreciation and accretion costs associated with asset retirement obligation are recorded as increases to regulatory assets on the consolidated balance sheets. These regulatory assets represent timing differences between the recognition of costs in accordance with U.S. GAAP and costs recovered through the ratemaking process.

**Employee Benefits**

The Company has defined benefit pension plans and postretirement benefit other than pension plans for its employees. The Company recognizes all pension and PBOP plans' funded status on the consolidated balance sheets as a net liability or asset with an offsetting adjustment to accumulated other comprehensive income ("AOCI") in shareholders' equity. If the cost of providing these plans is recovered in rates through the Company's regulated subsidiaries, the net funded status is offset by a regulatory asset or liability. The Company measures and records its pension and PBOP funded status at the year-end date. Pension and PBOP plan assets are measured at fair value, using the year-end market value of those assets.

## New and Recent Accounting Guidance

### Accounting Guidance Recently Adopted

*Pension and Postretirement Benefits*

In March 2017, the Financial Accounting Standards Board ("FASB") issued Accounting Standards Update ("ASU") No. 2017-07, "Compensation—Retirement Benefits (Topic 715): Improving the Presentation of Net Periodic Pension Cost and Net Periodic Postretirement Benefit Cost," which changes certain presentation and disclosure requirements for employers that sponsor defined benefit pension and other postretirement benefit plans. The ASU requires the service cost component of the net benefit cost to be classified within the same line item as other compensation in operating income in an entity's statement of operations and the other components of net benefit cost to be classified outside of operating income on a retrospective basis. In addition, as prescribed by the ASU, only the service cost component will be eligible for capitalization when applicable, on a prospective basis.

The Company adopted this new guidance on April 1, 2018. As a result of the retrospective adoption of ASU No. 2017-07 for the year ended March 31, 2018, the Company reclassified $90 million related to the other components of net benefit cost that were previously presented within operations and maintenance to other income (deductions), net in the consolidated statement of operations and comprehensive income. The application of the new guidance did not have a material impact on the Company's results of cash flows and financial position.

*Statement of Cash Flows*

In November 2016, the FASB issued ASU No. 2016-18, "Statement of Cash Flows (Topic 230): Restricted Cash," which requires entities to show the changes in the total of cash, cash equivalents, restricted cash, and restricted cash equivalents in the consolidated statements of cash flows. The Company has adopted the new guidance in the current fiscal year and applied it retrospectively for the year ended March 31, 2018. Cash and restricted cash are presented on a combined basis in the Company's consolidated statements of cash flows. As a result of implementing the new accounting guidance for the statement of cash flows, the reclassification of the change in restricted cash balances, which was previously classified as investing activities, resulted in a decrease of $13 million in the total change in cash, cash equivalents, restricted cash and special deposits for the year ended March 31, 2018.

In August 2016, the FASB issued ASU No. 2016-15, "Statement of Cash Flows (Topic 230): Classification of Certain Cash Receipts and Cash Payments," which provides guidance about the classification of certain cash receipts and payments within the consolidated statements of cash flows, including debt prepayment or extinguishment costs, contingent consideration payments made after a business combination, proceeds from the settlement of insurance claims and policies, and distributions received from equity method investments. The Company adopted the new guidance in the current fiscal year and applied it retrospectively for each prior period presented. The application of the new guidance did not have a material impact on the Company's presentation of its consolidated statements of cash flows.

*Income Taxes*

In October 2016, the FASB issued ASU No. 2016-16, "Income Taxes (Topic 740): IntraEntity Transfers of Assets Other Than Inventory," which eliminates the exception for all intra-entity sales of assets other than inventory. As a result, a reporting entity would recognize the tax expense from the sale of the asset in the seller's tax jurisdiction when the transfer occurs, even though the pre-tax effects of that transaction are eliminated in consolidation. The application of this guidance did not have a material impact on the results of operations, cash flows, or financial position of the Company.

*Revenue Recognition*

In May 2014, the FASB issued ASU No. 2014-09, "Revenue from Contracts with Customers (Topic 606)." The FASB further amended ASC 606 through various updates issued thereafter. The underlying principle of this ASU is that an entity will recognize revenue to depict the transfer of promised goods or services to customers in an amount that reflects the

consideration the entity expects to be entitled to, in exchange for those goods or services. The Company adopted the new guidance on April 1, 2018, using the modified retrospective method applied to contracts that were not completed as of April 1, 2018, and the Company did not recognize an adjustment to retained earnings for the cumulative effect of adopting the standard.

The adoption of ASC 606 did not have a material impact on the presentation of the Company's results of operations, cash flows, or financial position. The Company has added additional disclosures as required under ASC 606 (See Note 4, "Revenue" for additional details).

*Financial Instruments – Classification and Measurement*

In January 2016, the FASB issued ASU No. 2016-01, "Financial Instruments–Overall (Subtopic 825-10): Recognition and Measurement of Financial Assets and Financial Liabilities." The new guidance eliminates the available-for-sale and cost method classification for equity securities and requires that all equity investments, other than those accounted for using the equity method of accounting, be measured and recorded at fair value with any changes in fair value recognized through net income. However, for equity investments that do not have a readily determinable fair value an entity may choose to measure equity investments at cost minus impairment, if any, plus or minus changes resulting from observable price changes in orderly transactions for identical or similar investments. If any entity elects to use the measurement alternative for equity investments without readily determinable fair values, those investments must be qualitatively assessed for impairment at each reporting period and if impairment exists the investment is required to be measured at fair value. The guidance does not impact the classification or measurement of investments in debt securities. The guidance also amended certain disclosure requirements related to financial instruments. The Company adopted the guidance on April 1, 2018 using a modified retrospective transition approach with a cumulative effect adjustment to retained earnings which was reclassified from accumulated other comprehensive income for $21 million related to equity investments that were previously classified as available-for-sale.

*Business Combinations*

In January 2017, the FASB issued ASU No. 2017-01, "Business Combinations (Topic 805): Clarifying the Definition of a Business," which provides a screen to determine when a set of assets or activities is not a business. The screen requires that when substantially all of the fair value of the gross assets acquired or disposed of is concentrated in a single identifiable asset or a group of similar identifiable assets, the set is not a business. The guidance also provides a framework to assist in evaluating whether both an input and a substantive process, two of the three must-have elements of a business, are present. The application of the new guidance did not have material impact on the results of operations, financial position, and disclosures of the Company.

**Accounting Guidance Not Yet Adopted**

*Derivatives and Hedging*

In August 2017, the FASB issued ASU No. 2017-12, "Derivative and Hedging (Topic 815): Targeted Improvements to Accounting for Hedging Activities," which will be effective for the fiscal year ending March 31, 2020, with early adoption permitted. The amendments in this update expand and refine hedge accounting for both financial and nonfinancial risk components and align the recognition and presentation of the effects of the hedging instrument and the hedged item in the consolidated financial statements. This update also includes changes to certain targeted improvements to ease the application of current guidance related to the assessment of hedge effectiveness. The Company is currently assessing the application of the guidance to determine if it will have a material impact on the results of operations and financial position of the Company.

*Leases*

In February 2016, the FASB issued ASU No. 2016-02 "Leases (Topic 842)" related to lease accounting. For the Company, the new standard is effective for the fiscal year ending March 31, 2020, and interim periods within. Under the new standard, a

lease is defined as a contract, or part of a contract, that conveys the right to control the use of identified assets for a period of time in exchange for consideration. Under the requirements of the new standard, lessees will need to recognize leases on the consolidated balance sheets as a right-of-use asset and a related lease liability, which will be equal to the present value of the estimated future lease payments. The right-of-use asset at inception will be based on the liability, subject to certain adjustments, such as initial direct costs. The new standard requires leases to be classified as either operating or financing which will impact the amount and classification of lease related expenses in the consolidated statements of operations and comprehensive income. Under the new standard, lessor accounting is largely unchanged. The new standard also has additional disclosure requirements.

Lessor accounting under the new guidance is consistent with the guidance under the old standard included in Topic 840, with updates to align with certain changes to the lessee model and the new revenue standard (Topic 606). Similar to current guidance, lessors will classify leases as operating, direct financing, or sales-type. The Company follows lessor accounting in respect of its A&R PSA and PPAs with LIPA. These were considered operating leases under the old standard, as well as the new standard. The standard will also require lessors to allocate (rather than recognize as currently required) certain variable payments to the lease and non-lease components when the changes in facts and circumstances on which the variable payment is based occur.

The new standard provides the Company with transition practical expedients including a package of three expedients that must be taken together and allows the Company to: not reassess whether existing contracts contain leases, carryforward the existing classification of any leases, and not reassess initial direct costs associated with existing leases. The Company has exercised its option to elect the package of practical expedients. The Company will make the election under the new standard to not reflect a right-of-use asset or related liability for leases with a term of twelve months or less. The Company has also elected the practical expedient to not reevaluate land easements existing at adoption if they were not previously accounted for as leases. The Company will not make the election to combine the lease components and the associated non-lease components of an arrangement and account for as a single lease component and will also not elect the expedient to use hindsight in determining the lease term for existing leases at the time of adoption.

The new standard permits lessors, as an accounting policy election, to not evaluate whether certain sales taxes and other similar taxes are lessor costs or lessee costs. Instead, those lessors will account for those costs as if they are lessee costs. The Company has made this accounting policy election. In addition, the new standard also allows lessors to exclude certain costs from variable payments, and therefore revenue, for lessor costs paid by lessees directly to third parties. The Company has also made this accounting policy election. In addition, the new standard also permits lessors, as an accounting policy election, to not separate lease and non-lease components if the non-lease components would otherwise be accounted for under Topic 606, the timing and pattern of both the lease and non-lease components is the same and the lease component would be accounted for as an operating lease under the new standard. The Company has not made this accounting policy election.

The Company will recognize and measure the cumulative effect of the new standard at the beginning of the earliest period presented using the modified retrospective approach. The Company determined the impact the ASU will have on its consolidated financial statements by reviewing its lease population and identifying lease data needed for the disclosure requirements. The Company will implement a new lease accounting system in fiscal year 2020, to ensure ongoing compliance with the ASU's requirements. The Company recognized approximately $769 million of operating lease liabilities as right-of-use assets on the consolidated balance sheets upon transition at April 1, 2019. Implementation of the new guidance will not materially impact the Company's results of operations or cash flows, as the Company does not expect significant changes to its pattern of expense recognition as a result of the new standard. The Company's operating leases are further discussed in Note 15, "Commitments and Contingencies."

*Intangibles - Goodwill and Other*

In August 2018, the FASB issued ASU No. 2018-15 "Intangibles – Goodwill and Other – Internal-Use Software (Subtopic 350-40), Customer's Accounting for Implementation Costs Incurred in a Cloud Computing Arrangement That Is a Service Contract" to help entities evaluate the accounting for fees paid by a customer. The amendment will align the requirements for capitalizing implementation costs incurred in a hosting arrangement that is a service contract with the requirements for capitalizing implementation costs incurred to develop or obtain internal-use software. For the Company, the requirements in

this update are effective for the fiscal year ending March 31, 2021 and interim periods within. The Company is currently assessing the application of the new guidance to determine if it will have a material impact on the presentation, results of operations, cash flows, and/or financial position of the Company.

*Financial Instruments*

In June 2016, the FASB issued ASU No. 2016-13 "Financial Instruments–Credit Losses (Topic 326): Measurement of Credit Losses on Financial Statements," which requires a financial asset (or a group of financial assets) measured at amortized cost basis to be presented at the net amount expected to be collected. The FASB further amended Topic 326 through additional updates issued thereafter. The allowance for credit losses is a valuation account that is deducted from the amortized cost basis of the financial asset(s) to present the net carrying value at the amount expected to be collected on the financial asset. Credit losses relating to available-for-sale debt securities should be recorded through an allowance for credit losses. For the Company, the requirements of the new standard will be effective for the fiscal year ending March 31, 2022, and interim periods within, with early adoption permitted from the fiscal year ending March 31, 2020 and interim periods within. The Company is currently assessing the application of the new guidance to determine if it will have a material impact on the presentation, results of operations, cash flows, and/or financial position of the Company.

*Tax*

In February 2018, the FASB issued ASU No. 2018-02, "Income Statement–Reporting Comprehensive Income (Topic 220): Reclassification of Certain Tax Effects from Accumulated Other Comprehensive Income," which allows a reclassification from accumulated other comprehensive income to retained earnings for stranded tax effects resulting from the Tax Cuts and Jobs Act of 2017 ("Tax Act"). The amendments eliminate the stranded tax effects resulting from the Tax Act and will improve the usefulness of information reported to financial statement users. For the Company, the requirements in this Update are effective for fiscal years ending March 31, 2020, including interim periods within those fiscal years. The Company is currently assessing the application of the new guidance to determine if it will have a material impact on the presentation, results of operations, cash flows, and/or financial position of the Company.

**Reclassifications**

Certain reclassifications have been made to the consolidated financial statements to conform the prior period's balances to the current period's presentation. These reclassifications had no effect on reported income, total assets, or stockholders' equity as previously reported.

## 3. WORK CONTINUATION PLAN

On June 25, 2018, Boston Gas and Colonial Gas (the "Massachusetts Gas Companies"), activated a work continuation plan after contractual agreements with two of their United Steelworkers unions expired and new agreements could not be reached. The United Steelworkers unions disagreed with proposed changes to employee health and retirement benefits. While the work continuation plan was in effect, internal management employees supplemented by external contractors filled the roles normally staffed by the United Steelworkers unions. As a result, the Massachusetts Gas Companies incurred approximately $448 million of costs, which are reflected in operations and maintenance expense in the accompanying consolidated statements of operations and comprehensive income for the year ended March 31, 2019. The Massachusetts Gas Companies reached new contractual agreements with two of their United Steelworkers unions, which were ratified on January 7, 2019.

## 4. REVENUE

The following table presents, for the year ended March 31, 2019, revenue from contracts with customers, as well as additional revenue from sources other than contracts with customers, disaggregated by major source:

| | Year Ended March 31, 2019 | |
|---|---|---|
| | *(in millions of dollars)* | |
| Revenue from Contracts with Customers: | | |
| Electric Transmission | $ | **1,236** |
| Electric Distribution | | **4,974** |
| Gas Distribution | | **5,729** |
| Off-System Sales | | **322** |
| Other Revenue from Contracts with Customers | | **59** |
| Total Revenue from Contracts with Customers | | **12,320** |
| Revenue from Regulatory Mechanisms | | **(10)** |
| Other Revenue | | **505** |
| Total Operating Revenues | **$** | **12,815** |

*Electric and Gas Distribution:* The Company's subsidiaries own and maintain electric and natural gas distribution networks. Distribution revenues are primarily from the sale of electricity, gas, and related services to retail customers. Distribution sales are regulated by the applicable state agencies, which are responsible for determining the prices and other terms of services as part of the ratemaking process. The arrangement where a utility provides a service to a customer in exchange for a price approved by a regulator is referred to as a tariff sales contract. Gas and electric distribution revenues are derived from the regulated sale and distribution of electricity and natural gas to residential, commercial, and industrial customers within the Company's service territory under the tariff rates. The tariff rates approved by the regulator are designed to recover the costs incurred by the Company for products and services provided along with a return on investment.

The performance obligation for distribution sales is to provide electricity and natural gas to the customers on demand. The electricity and natural gas supplied under the tariff represents a single performance obligation as it is a series of distinct goods or services that are substantially the same. The performance obligation is satisfied over time because the customer simultaneously receives and consumes the electricity or natural gas as the Company provides these services. The Company records revenues related to the distribution sales based upon the approved tariff rate and the volume delivered to the customers, which corresponds with the amount the Company has the right to invoice.

The distribution revenue also includes estimated unbilled amounts, which represent the estimated amounts due from customers for electricity and natural gas provided by the Company, but not yet billed. Unbilled revenues are determined based on estimated unbilled sales volumes for the respective customer classes and then applying the applicable tariff rate to those volumes. Actual amounts billed to customers, when the meter readings occur, may be different from the estimated amounts.

Certain customers have the option to obtain electricity or natural gas from other suppliers. In those circumstances revenue is only recognized for providing delivery of the commodity to the customer.

*Electric Transmission*: Transmission revenues are generated by NEP, Narragansett, Massachusetts Electric, Nantucket, and Niagara Mohawk. Such revenues are based on a formula rate that recovers actual costs plus a return on investment. Stranded cost recovery revenues are collected through a contract termination charge ("CTC"), which is billed to former wholesale customers of the Company in connection with the Company's divestiture of its electricity generation investments.

*Off-System Sales*: Represents direct sales of gas to participants in the wholesale natural gas marketplace, which occur after customers' demands are satisfied.

*Other Revenue from Contracts with Customers:* Includes contributions in aid of construction and pole rentals.

*Revenue from Regulatory Mechanisms:* The Company's regulated subsidiaries record revenues in accordance with accounting principles for rate-regulated operations that are arrangements between the regulated subsidiaries and their respective regulators, which are not accounted for as contracts with customers. These include various deferral mechanisms such as capital trackers, energy efficiency programs, storm deferral, and programs that qualify as Alternative Revenue Programs ("ARPs"). ARPs enable the regulated subsidiaries to adjust rates in the future, in response to past activities or completed events. The regulated subsidiaries' electric and gas distribution rates have revenue decoupling mechanisms ("RDM"), which allow for periodic adjustments to delivery rates as a result of the reconciliation between allowed revenue and billed revenue. The regulated subsidiaries also have other ARPs related to the achievement of certain objectives, demand side management initiatives, and certain other ratemaking mechanisms. ARPs are recognized with a corresponding offset to a regulatory asset or liability account when the specified events or conditions have been met, when the amounts are determinable, and when amounts are probable of recovery (or payment) through future rate adjustments.

*Other Revenue:* Includes lease income and other transactions that are not considered contracts with customers. The lease income primarily includes the electric generation revenue, which is derived from billings to LIPA for the electric generation capacity and, to the extent requested, energy from the Company's existing oil and gas-fired generating plants as discussed in Note 15, "Commitments and Contingencies" under "Electric Services and LIPA Agreements."

## 5. REGULATORY ASSETS AND LIABILITIES

The Company records regulatory assets and liabilities that result from the ratemaking process. Regulatory deferrals are recorded by legal entity and separate company results and positions can result in both assets and liabilities. The following table presents the regulatory assets and regulatory liabilities recorded on the consolidated balance sheets:

| | March 31, | |
|---|---|---|
| | **2019** | 2018 |
| | *(in millions of dollars)* | |
| **Regulatory assets** | | |
| Current: | | |
| Derivative instruments | **$ 15** | $ 67 |
| Gas costs adjustment | **105** | 184 |
| Rate adjustment mechanisms | **94** | 105 |
| Renewable energy certificates | **81** | 57 |
| Revenue decoupling mechanism | **42** | 97 |
| Other | **22** | 25 |
| Total | **359** | 535 |
| Non-current: | | |
| Environmental response costs | **2,249** | 2,283 |
| Net metering deferral | **166** | 108 |
| Postretirement benefits | **1,496** | 1,611 |
| Recovery of acquisition premium | **167** | 176 |
| Storm costs | **307** | 293 |
| Other | **751** | 721 |
| Total | **5,136** | 5,192 |
| **Regulatory liabilities** | | |
| Current: | | |
| Energy efficiency | **432** | 511 |
| Gas costs adjustment | **110** | 47 |
| Rate adjustment mechanisms | **99** | 195 |
| Revenue decoupling mechanism | **240** | 201 |
| Transmission service | **93** | 28 |
| Other | **91** | 57 |
| Total | **1,065** | 1,039 |
| Non-current: | | |
| Carrying charges | **243** | 264 |
| Cost of removal | **1,685** | 1,698 |
| Environmental response costs | **162** | 165 |
| Postretirement benefits | **233** | 250 |
| Regulatory tax liability, net | **2,835** | 2,836 |
| Other | **1,118** | 976 |
| Total | **6,276** | 6,189 |
| Net regulatory liabilities | **$ (1,846)** | $ (1,501) |

**Carrying charges:** The Company records carrying charges on regulatory balances for which cash expenditures have been made and are subject to recovery, or for which cash has been collected and is subject to refund. Carrying charges are not recorded on items for which expenditures have not yet been made.

**Cost of removal:** Represents cumulative amounts collected, but not yet spent, to dispose of property, plant and equipment. This liability is discharged as removal costs are incurred.

**Derivative instruments:** The Company evaluates open commodity derivative instruments for regulatory deferral by determining if they are probable of recovery from, or refund to, customers through future rates. Derivative instruments that qualify for recovery are recorded at fair value, with changes in fair value recorded as regulatory assets or regulatory liabilities in the period in which the change occurs.

**Energy efficiency**: Represents the difference between revenue billed to customers through the Company's energy efficiency charge and the costs of the Company's energy efficiency programs as approved by the state authorities.

**Environmental response costs:** The regulatory asset represents deferred costs associated with the Company's share of the estimated costs to investigate and perform certain remediation activities at former manufactured gas plant ("MGP") sites and related facilities. The Company believes future costs, beyond the expiration of current rate plans, will continue to be recovered through rates. The regulatory liability represents the excess of amounts received in rates over the Company's actual site investigation and remediation ("SIR") costs.

**Gas costs adjustment**: The Company is subject to rate adjustment mechanisms for commodity costs, whereby an asset or liability is recognized resulting from differences between actual revenues and the underlying cost being recovered or differences between actual revenues and targeted amounts, as approved by state regulators. These amounts will be refunded to, or recovered from, customers over the next year.

**Net metering deferral:** Net metering deferral reflects the recovery mechanism for costs associated with customer installed on-site generation facilities, including the costs of renewable generation credits. This surcharge provides the Company with a mechanism to recover such amounts.

**Postretirement benefits:** The regulatory asset balance represents the Company's, unamortized, non-cash accrual of net pension actuarial gains and losses in addition to actual costs associated with Company's pension plans in excess of amounts received in rates that are to be collected in future periods. The regulatory liability represents the Company's, unamortized, non-cash accrual of net PBOP actuarial gains and losses in addition to excess amounts received in rates over actual costs of the Company's PBOP plans that are to be passed back in future periods.

**Rate adjustment mechanisms**: In addition to commodity costs, the Company is subject to a number of additional rate adjustment mechanisms whereby an asset or liability is recognized resulting from differences between actual revenues and the underlying cost being recovered or differences between actual revenues and targeted amounts as approved by the applicable state regulatory bodies.

**Recovery of acquisition premium:** Represents the unrecovered amount (plus related taxes) by which the purchase price paid exceeded the net book value of Colonial Gas' assets in the 1998 acquisition of Colonial Gas by Eastern Enterprises, Inc. In exchange for certain rate concessions and the achievement of certain merger savings targets, the DPU has allowed Colonial Gas to recover the acquisition premium in rates through August 2039.

**Regulatory tax liability, net:** Represents over-recovered federal and state deferred taxes of the Company primarily as a result of regulatory flow through accounting treatment, income tax rate changes and excess federal deferred taxes as a result of the Tax Act.

**Renewable energy certificates:** Represents deferred costs associated with the Company's compliance obligation with the Rhode Island and Massachusetts Renewable Portfolio Standard ("RPS"). The RPS is legislation established to foster the development of new renewable energy sources. The regulatory asset will be recovered over the next year.

**Revenue decoupling mechanism**: As approved by the applicable state regulatory bodies, the Company has electric and gas RDMs which allow for an annual adjustment to the Company's delivery rates as a result of the reconciliation between allowed and actual billed revenues. Any difference is recorded as a regulatory asset or regulatory liability.

**Storm costs:** The Company is allowed to recover storm costs from retail delivery service customers. This balance reflects costs yet to be recovered. See Note 6, "Rate Matters," for additional information regarding the recovery of storm costs.

**Transmission service:** Massachusetts Electric and Nantucket (the "Massachusetts Electric Companies") and Narragansett arrange transmission service on behalf of their customers and bill the costs of those services to customers, pursuant to the Transmission Service Cost Adjustment Provision. Any over or under recoveries of these costs are passed on to customers receiving transmission service over the subsequent year.

## 6. RATE MATTERS

### Niagara Mohawk

*Electric and Gas Filing*

On April 28, 2017, Niagara Mohawk filed a proposal to reset electric and natural gas delivery prices beginning in April 2018. On January 19, 2018, Niagara Mohawk reached a settlement agreement with the NYPSC Staff and other parties to the case and filed a Joint Proposal for a three-year rate plan. The proposal reflects the new federal tax law changes and provides a cumulative revenue requirement increase of $241 million and $61 million for the electric and gas business, respectively, based on a 9.0% return on equity ("ROE") and 48% common equity ratio. On March 15, 2018, the NYPSC issued a final order approving the Joint Proposal and the new rates took effect on April 1, 2018.

As of March 31, 2018, resulting from the order, a new electric rate plan settlement credit of $45 million and a new gas rate plan settlement credit of $28 million were established. These credits are included in other non-current regulatory liabilities in the preceding table within Note 5, "Regulatory Assets and Liabilities." Niagara Mohawk applied $38 million of existing regulatory liabilities towards the creation of these credits. As authorized under the order, the Electric Rate Plan Settlement Deferral Credit balances are being amortized at the rate of $6 million per rate year to compensate the write-down of pre-Automated Meter Reading investments. The order authorizes Niagara Mohawk to fund $14 million in gas safety programs and compliance improvement programs form the Gas Rate Plan Settlement Deferral Credit balances. Further amortizations relating to meter investments, gas safety, or the settlement of other rate plan issues may be authorized in future proceedings.

*Tax Act*

On March 15, 2018, the FERC initiated multiple proceedings intended to adjust FERC-jurisdictional rates to reflect the corporate tax changes as a result of the passage of the Tax Act. Of the proceedings initiated relevant to the Company's regulated subsidiaries (Niagara Mohawk, NEP, Narragansett, and the Massachusetts Electric Companies) is the Notice of Inquiry ("NOI") seeking comments on the effects of the Tax Act on all FERC-jurisdiction rates and a Notice of Proposed Rulemaking ("NOPR") issued as a result of the NOI. In response to the FERC NOI, the Company made recommendations designed to mitigate the cash flow impacts of the expected refunds including providing flexibility regarding the methods used to refund accumulated deferred income tax ("ADIT") to customers and providing flexibility regarding the time period of the flow back. In the NOPR, the FERC proposed to give the flexibility the Company proposed. Comments on the NOPR were due on January 22, 2019. The Company is awaiting a final rule from the FERC.

In response to the Tax Act, the NYPSC issued an Order Instituting Proceeding under Case 17-M-0815 - Proceeding on Motion of the Commission on Changes in Law that May Affect Rates. This proceeding was instituted to solicit comments on the Tax Act's implications and places the utilities on notice of the NYPSC's intent to protect ratepayers' interest and to ensure that any cost reductions from the changes in federal income taxes are deferred for future ratepayer benefit.

On August 9, 2018, the NYPSC issued an order in its generic proceeding considering the impacts of federal tax reform. NYPSC Staff had advocated that all New York utilities implement a sur-credit by October 1 that would reflect the immediate effects

of the Tax Act and also return any deferred benefits to customers. In response, the Company's New York subsidiaries filed a proposal to (i) delay any sur-credit to January 1 to offset scheduled rate increases and (ii) retain any deferred benefits, including accumulated deferred federal income taxes ("ADFIT"), for future rate moderation.

The NYPSC's order effectively approved all aspects of Niagara Mohawk's proposal. The NYPSC agreed that Niagara Mohawk should be allowed to defer both the pass back of calendar year 2018 tax savings (to the extent not already returned in the new rate plan) and the amortization of excess ADFIT balances, and use the benefits as a rate moderator when base rates are next revised in 2020/2021. Specifically, the NYPSC directed that:

- for Niagara Mohawk, no sur-credit is required as the current rate plan already reflects the reduction of the tax rate to 21% and the termination of bonus depreciation. The NYPSC approved Niagara Mohawk's proposal to defer the tax benefit realized for the three-month period (January-March) prior to new rates, of $18 million for electric and $5 million for gas, to offset future rate increases or investments.

- Brooklyn Union and KeySpan Gas East (the "New York Gas Companies") implement a sur-credit to reflect the lower tax rate effective January 1, 2019 to offset planned rate increases and retain the calendar year 2018 deferred amounts for future rate mitigation and/or to offset investments. Deferring the tax benefits until January 1, 2019 results in a deferred balance of $40 million for Brooklyn Union and $31 million for KeySpan Gas East.

*Operations Staffing Audit*

In January 2014, the NYPSC initiated an operational audit to review internal staffing levels and use of contractors for the core utility functions at KeySpan Gas East and Brooklyn Union Gas Company (the "New York Gas Companies") and Niagara Mohawk. On June 26, 2014, the NYPSC selected a third party to conduct the audit. On February 21, 2017, the third party submitted its final report, which contained recommendations for all of the Company's New York utilities designed to improve the staffing and workforce management processes. The report contained 27 recommendations for the Company. The Company filed its implementation plan on March 23, 2017. On December 15, 2017, the NYPSC issued an order approving the Company's implementation plan without modification, with updates to be made every four months to the NYPSC on the status of implementation. On July 30, 2019, the NYPSC issued a letter closing out the audit, indicating that the Company had implemented all recommendations.

*New York Management Audit*

In 2018, the NYPSC initiated a comprehensive management and operations audit of the New York Gas Companies and Niagara Mohawk. New York law requires periodic management audits of all utilities at least once every five years. The Company last underwent a New York management audit in 2014/2015, when the NYPSC audited the Company's New York gas business. The audit is process oriented and forward looking, and presents opportunities to obtain feedback on how to improve service to customers and meet regulatory expectations. Areas of focus include the traditional audit areas of corporate governance, budgeting and finance, customer, work management, and long-term planning, as well as organization design, information systems, gas safety, and grid modernization. The final audit report is due in September 2019.

**The New York Gas Companies**

*Rate Case Filing*

On January 29, 2016, the New York Gas Companies filed to adjust their base gas rates, to be effective from January 1, 2017. The filing requested to increase gas delivery base revenues.

On September 7, 2016, the New York Gas Companies filed a Joint Proposal establishing a three-year rate plan beginning January 1, 2017 and ending December 31, 2019. The NYPSC issued an order approving the Joint Proposal on December 15, 2016 and the new rates went into effect beginning January 1, 2017.

The rate plan provided for a revenue increase of $384 million in the first year, an additional $61 million in the second year, and an additional $76 million in the third year, for a cumulative three-year increase of $1.3 billion, for the New York Gas Companies. In an effort to mitigate the potential bill impacts that the revenue increases would have on customers in the first year, the revenue increases are levelized over the three-year rate period. As such, for U.S. GAAP reporting, revenues are recognized equal to the amounts actually billed to customers during each period rather than per the provisions of the rate plan. The settlement is based upon a 9% ROE and 48% common equity ratio and includes an earnings sharing mechanism in which customers will share earnings when the New York Gas Companies' ROE is in excess of 9.5%.

Key provisions of the settlement include funding for removal of a specific mileage of leak prone pipe ("LPP") in each rate year. Additionally, recovery of proactive LPP replacement costs incurred in excess of this mileage are permitted and recovered through the Gas Safety and Reliability Surcharge. This also includes a positive revenue adjustment mechanism for unit cost savings versus those specific in rates.

The New York Gas Companies have capital tracker mechanisms that reconcile the New York Gas Companies' capital expenditures to the amounts permitted in rates. The Net Utility Plant and Depreciation Expense tracker is a downward only reconciliation that applies to the New York Gas Companies' aggregate total average net plant and depreciation expense combined. The reconciliation is summed at the end of rate year Three (December 31, 2019) to determine whether any underspend is owed to customers. Under the City/State Construction Reconciliation, the New York Gas Companies are authorized to defer 90% of the revenue requirement impact difference (excluding operations and maintenance expense) between actual and forecast city/state construction costs for future recovery from or return to customers.

The New York Gas Companies' RDM was also adjusted to include revenue-per-class RDMs for industrial and commercial customers not previously subject to the RDM.

Each rate year, the New York Gas Companies' will fully reconcile actual SIR expense to the Forecast Rate Allowance. Any under or over expenditures will be deferred for future refund to or recovery from customers (with the exception of the Citizens site). Brooklyn Union will continue to absorb 10% of the remaining investigation costs for the Citizens site. In the event that KeySpan Gas East incurs unanticipated expenses relating to SIR costs incremental to the forecast rate allowance, KeySpan Gas East may file a petition requesting that the NYPSC approve recovery of incremental costs through KeySpan Gas East's SIR Recovery Surcharge.

Brooklyn Union's environmental SIR expense has also been moved from a surcharge to base rates. Beginning in January 2018, to the extent that the difference between actual SIR expense and the Forecast Rate Allowance exceeds $25 million on a cumulative basis, Brooklyn Union will utilize its SIR Recovery Surcharge. The surcharge is designed to provide recovery for the differences between actual SIR expenses and the amounts allowed in rates and will be calculated annually and be limited to an amount no greater than 2% of Brooklyn Union's prior year aggregate revenues. Differences over this threshold will be deferred for future recovery.

On April 30, 2019, KeySpan Gas East and Brooklyn Union filed to increase revenues for the twelve months ending March 31, 2021 ("Rate Year"). The New York Gas Companies filed Corrections and Updates on July 3, 2019, which requested rate increases of $61.2 million for KeySpan Gas East and $195.5 million for Brooklyn Union. The filings propose to invest over $1.5 billion in the Rate Year to modernize the New York Gas Companies' gas infrastructure by replacing aging pipelines, implementing safety improvements, enhancing storm hardening and resiliency, and reducing methane emissions. The filings also include proposals to enhance gas safety and promote a sustainable and affordable path toward a low-carbon energy future. The New York Gas Companies included three additional years of data to facilitate the possibility of a multi-year rate settlement.

*Regulatory Proceedings*

On July 12, 2019, the NYPSC initiated a proceeding requiring the New York Gas Companies to demonstrate why a penalty action should not be commenced for more than 1,600 alleged gas safety violations. The alleged violations concern the NYPSC's investigation of improper operator qualification and related issues following a 2016 anonymous letter alleging a contractor

had facilitated employees cheating on operator qualification exams. The NYPSC also alleges violations for both employees and other contractors' workers whose qualifications had lapsed. The order directs the New York Gas Companies to respond within 45 days. The New York Gas Companies are assessing the allegation in the order. At this time, The New York Gas Companies are unable to determine the amount and probability of any potential penalty.

**The Massachusetts Electric Companies**

*Electric Rate Case Filing*

In November 2015, the Massachusetts Electric Companies, filed an application for new base distribution rates that become effective October 1, 2016. The DPU approved an overall increase in base distribution revenue of approximately $170 million based upon a 9.9% ROE and an overall capital structure of 50.69% equity, 49.22% long-term debt, and 0.09% preferred stock. This increase in revenue includes capital and solar assets placed in service after the last rate case test year of December 2008 and previously recovered through separate factors. The order also allows recovery over five years of the aggregate test-year balance of protected customer accounts receivable outstanding for more than 360 days of $41 million. As a result of the order the Massachusetts Electric Companies have recorded revenue of approximately $8 million for the year ended March 31, 2019 in relation to the recovery of protected accounts; the remaining $20 million of the protected receivables will be collected through 2021.

Storm recovery allowed in base rates increased from $4 million to $11 million per year. Deferred storm costs incurred through September 30, 2016 remain subject to carrying charges at the Weighted Average Cost of Capital. However, deferred storm costs incurred after October 1, 2016 will accrue carrying charges at the prime rate. Additionally, the DPU approved the extension of the recovery factor through August 2019 for costs associated with 16 storm events that took place between February 2010 and March 2013.

The order also allows for an increase in the annual capital costs for plant investment placed into service as part of the Massachusetts Electric Companies' Capital Investment Recovery Mechanism ("CIRM") from $170 million to $249 million and also allows for the inclusion of property taxes related to these incremental capital additions. The CIRM is a continuation of the Massachusetts Electric Companies' capital investment recovery mechanism initially part of its RDM, with an annual cap on capital investment of $249 million, which is a three-year calendar year historical average.

On November 15, 2018, the Massachusetts Electric Companies filed an application for new base distribution rates to become effective October 1, 2019. The requested net increase is $55 million based on a 10.5% ROE, with 53.49% equity, 46.43% long-term debt, and 0.08% preferred stock. The Massachusetts Electric Companies are requesting implementation of a five-year performance-based ratemaking ("PBR") plan, which would adjust base distribution revenue annually based on a pre-determined formula. If the PBR plan is approved, the Massachusetts Electric Companies will agree not to file a rate case for five-years and the CIRM will be discontinued after a transition period.

The Massachusetts Electric Companies also requested an increase in annual funding of the storm fund from $11 million to $19 million per year and an extension of the storm fund replenishment factor through November 2023. Evidentiary hearings were held in April and May 2019 and an order is expected in September 2019. The Massachusetts Electric Companies cannot predict the outcome of this request.

*Tax Act*

In February 2018, the DPU opened an investigation to examine the effect of the Tax Act on the rates of the investor-owned utilities in Massachusetts as of January 1, 2018 and directed the utilities to account for any revenues associated with the difference between the previous and current corporate income tax rates, and establish a regulatory liability for excess recovery in rates of ADIT. On May 1, 2018, the Massachusetts Electric Companies submitted their proposal for reducing electric rates prospectively, and for addressing ADIT. On June 29, 2018, the DPU approved the Massachusetts Electric Companies' proposal for reducing rates prospectively, and directed the Massachusetts Electric Companies to reduce rates effective July 1, 2018 and reduce their annual target revenue in its RDM by $26 million. On December 21, 2018, the DPU

issued an order requiring all utilities to begin crediting in rates the amortization of excess deferred federal income taxes, to the extent such amortization was not already included in base distribution rates, through the combination of factors associated with certain reconciling mechanisms and a separate factor for the amortization of the remaining amounts. The DPU approved the Massachusetts Electric Companies' compliance filing and proposed tariff allowing for the credit to customers of the amortization of the remaining amounts on January 28, 2019, and noted it would investigate the proposed refund of excess ADIT associated with the tax credit provision in D.P.U. 19-05, the Massachusetts Electric Companies' annual retail rate filing proceeding, and the excess ADIT associated with reconciling mechanisms in the individual dockets for those mechanisms. The DPU further noted it would investigate in the pending general rate case (D.P.U. 18-150), the Massachusetts Electric Companies' proposal to remove excess ADIT associated with any reconciling mechanism and the applicable amortization from those mechanisms and credit the remaining amounts through base distribution rates effective October 1, 2019.

In February 2019, the DPU issued an order finding that the Massachusetts utilities were not required to refund tax savings previously accrued from January 1, 2018 through June 30, 2018, as a result of the federal income tax rate reduction. The Massachusetts Electric Companies previously estimated that the total amount that would be subject to refund was approximately $14 million. On March 7, 2019, the Attorney General's ("AG") Office filed a motion for clarification and reconsideration, requesting that the DPU provide additional clarity regarding its February 2019 ruling, and to reconsider its determination to allow utilities to keep the federal tax savings accrued from January 1, 2018 through June 30, 2018. The Motion for Clarification and Reconsideration is still pending.

*Grid Modernization Plan*

On August 19, 2015, the Massachusetts Electric Companies filed their proposed grid modernization plan with the DPU, with four different proposed investment scenarios. On May 10, 2018, the DPU issued an order in this proceeding. The order approves $82 million in grid-facing investments over three years in: (1) Conservation Voltage Reduction and Volt VAR Optimization; (2) advanced distribution automation; (3) feeder monitors; (4) communications and information/operational technologies; and (5) advanced distribution management/distribution supervisory control and data acquisition. The DPU allowed recovery of both operation and maintenance expense and capital costs through a reconciling mechanism, and in the future will consider grid modernization plans in separate dockets (i.e., not through rate cases). The DPU did not approve any customer-facing (i.e., advanced metering infrastructure) investments; the DPU will address these in a further investigation to see if there are ways to achieve cost-effective deployment of advanced metering functionality ("AMF"). The DPU found there needs to be widespread adoption of dynamic pricing in order for AMF to be successful, and it needs to address how to facilitate this first. The DPU also refined its grid modernization objectives to place additional focus on improved access to the distribution system planning process.

**The Massachusetts Gas Companies**

*General Rate Case*

Effective October 1, 2018, the DPU approved a combined rate increase for the Massachusetts Gas Companies. The DPU authorized an allowed ROE of 9.5% and an equity ratio of 53%. In addition, the DPU approved funding the Gas Business Enablement program. The Gas Business Enablement program is being developed to consolidate and modernize the Massachusetts Gas Companies' systems and operating platforms to facilitate internal efficiencies and improve customers' experience. The DPU denied the Massachusetts Gas Companies' request to increase rates for certain post-test year capital investments, instead requiring the Massachusetts Gas Companies to include those investments in a subsequent base rate case. The Massachusetts Gas Companies filed a motion for reconsideration of certain aspects of the DPU decision. The motion for reconsideration is still pending. The Massachusetts Gas Companies cannot predict the outcome of this motion.

*Tax Act*

In February 2018, the DPU opened an investigation to examine the effect of the Tax Act on the rates of the investor-owned utilities in Massachusetts as of January 1, 2018, and directed the utilities to account for any revenues associated with the

difference between the previous and current corporate income tax rates, and establish a regulatory liability for excess recovery in rates of ADIT. The Massachusetts Gas Companies' filing was submitted to the DPU on May 1, 2018. In its June 29, 2018 order, the DPU allowed the Massachusetts Gas Companies to defer the effect of the tax reduction until new rates resulting from the then-pending rate case became effective on October 1, 2018, at which time the Massachusetts Gas Companies were directed to refund the three-month tax savings deferral to customers over one year, and the Massachusetts Gas Companies included this amount in their rate case compliance filing. On December 21, 2018, the DPU issued an order requiring all utilities to begin crediting in rates the amortization of excess deferred federal income taxes, to the extent such amortization was not already included in base distribution rates, through the combination of factors associated with certain reconciling mechanisms and a separate factor for the amortization of the remaining amounts. The Massachusetts Gas Companies included an estimate of amortization of excess deferred federal income taxes in their 2017 rate case, and the DPU required a filing by May 1, 2019 to update the balance of excess deferred federal income taxes and associated amortization. By order dated September 24, 2018 in D.P.U. 18-15-D ("Order 18-15-D"), the DPU approved the Massachusetts Gas Companies' methodology for calculating the amount of excess ADIT and proposed amortization periods for protected and unprotected amounts. On May 1, 2019, consistent with the DPU's directives in Order 18-15-D, the Massachusetts Gas Companies provided a final calculation of protected and unprotected excess ADIT amounts, and a final calculation of the amortization periods applicable to protected excess ADIT.

In February 2019, the DPU issued an order finding that the Massachusetts utilities were not required to refund tax savings previously accrued from January 1, 2018 through June 30, 2018 as a result of the federal income tax rate reduction. On March 7, 2019, the AG's office filed a motion for clarification and reconsideration requesting that the DPU provide additional clarity regarding its February 2019 ruling, and to reconsider its determination to allow utilities to keep the federal tax savings accrued from January 1, 2018 through June 30, 2018. The Massachusetts Gas Companies have recorded a combined $7 million regulatory liability pending the outcome of the AG's motion.

*Independent Statewide Pipeline Safety Audit*

On November 30, 2018, the DPU initiated an independent statewide pipeline safety audit of the natural gas distribution systems in Massachusetts and hired an independent auditor. The auditor is assessing the safety of the gas systems in the entire state and will be making recommendations for improvements that may impact the Massachusetts Gas Companies' operations and pipeline safety compliance requirements in the future. As part of Phase I of the audit, the Massachusetts Gas Companies submitted responses to information requests from the auditor and made a presentation to the auditor in January 2019. In May 2019 the independent auditor issued a Phase I Summary Report with 11 preliminary recommendations general to all the gas companies in Massachusetts and that include taking steps to improve emergency response plans, establishing programs and training for process safety hazard identification in the field, and addressing resource issues at the gas companies and in state government. Phase II of the audit will include field visits with each gas company, additional information requests and individual company recommendations. Phase II of the audit was expected/ to begin in the summer of 2019, but it has not yet begun. The Massachusetts Gas Companies do not anticipate that they will receive any penalties as a direct result of the audit, but the Massachusetts Gas Companies cannot predict the outcome of the audit at this time.

**NEP**

*Transmission ROE*

Transmission revenues are based on a formula rate that recovers NEP's actual costs plus a return on investment. Approximately 74% of NEP's transmission facilities are included under regional network service ("RNS") rates. NEP earns an additional 0.5% ROE incentive adder on RNS-related transmission facilities approved under the Regional Transmission Organization's ("RTO") Regional System Plan and placed in service on or before December 31, 2008. It also earns a 1.25% ROE incentive on its portion of New England East-West Solution ("NEEWS") (see the "New England East-West Solution" section).

NEP's transmission rates applicable to transmission service through October 15, 2014 reflected a base ROE of 11.14% applicable to NEP's transmission facilities, plus an additional 0.5% RTO participation adder applicable to transmission facilities included under the RNS rate. Starting on October 16, 2014, the FERC issued a series of orders as a result of NEP's four ROE

complaints (see the “FERC ROE Complaints” section in Note 15, “Commitments and Contingencies”), reducing NEP’s base ROE to 10.57%. The FERC also established a maximum ROE such that any incentives, taken together, may not exceed a cap of 11.74%.

On October 16, 2018, the FERC issued a Preliminary Order Directing Briefs on the four ROE complaints. The FERC proposes a new methodology for determining whether an existing ROE remains just and reasonable and also for determining a new ROE where an existing ROE is found to be unjust and reasonable. The FERC also proposes to set the base ROE in New England at 10.41% with a 13.08% cap on incentives. Briefs were submitted by the New England Transmission Operators (“NETOs”), Complainants, and FERC Trial Staff in early January of 2019. The FERC is under no deadline to act on the briefs and it is too early to determine when or how the FERC will decide on the briefs.

Although the order provided illustrative calculations, the FERC stated that these calculations are merely preliminary. The FERC's preliminary calculations are not binding, as changes to the methodology by the FERC are possible as a result of the parties' arguments and calculations in the briefing process. Until the FERC issues a final decision on each of these four complaints, there is significant uncertainty, and at this time, NEP cannot predict the impact to NEP’s current base ROE.

On March 21, 2019 the FERC announced a NOI on whether, and if so how, to revise its policies on determining the ROE used in setting rates charged by jurisdictional public utilities. NEP responded to the NOI on June 26, 2019 with reply comments due back on August 26, 2019.

*Stranded Cost Recovery*

Under the settlement agreements approved by state commissions and the FERC, NEP is permitted to recover stranded costs (those costs associated with its former generating investments (nuclear and non-nuclear) and related contractual commitments that were not recovered through the sale of those investments). NEP earns a ROE related to stranded cost recovery consisting of nuclear-related investments. In Massachusetts and Rhode Island, the current ROEs are 9.2% and 10.46%, respectively. NEP will recover its remaining non-nuclear stranded costs through 2020.

*Recovery of Transmission Costs*

In conformance with the terms of NEP’s Tariff No. 1, on November 17, 2014, NEP submitted a filing to the FERC under Section 205 of the Federal Power Act (“FPA”) proposing to reduce the ROE under its Tariff No. 1 formula rates so that they were consistent with those applied under the Independent System Operator New England (“ISO-NE”) Open Access Transmission Tariff pursuant to the FERC’s Opinion Nos. 531 and 531-A. Under the integrated facilities provisions of Tariff No. 1, NEP supports the cost of transmission facilities owned by its distribution affiliates, Massachusetts Electric and Narragansett, and makes these facilities available for open access transmission service on an integrated basis. The FERC rejected NEP’s filing on April 16, 2015, finding that it was inconsistent with the FERC’s clarifications issued in its Order on Rehearing in Opinion No. 531-B (see the “FERC ROE Complaints” section in Note 15, “Commitments and Contingencies”). On January 21, 2016, NEP re-filed proposed amendments to its Tariff No. 1 formula rates for integrated facilities to be consistent with Opinion No. 531-B among other proposed changes. On March 8, 2016, the FERC accepted the filing approving an effective date of October 16, 2014 for the ROE components. NEP has reduced its compensation to its distribution affiliates in accordance with the Order. On April 14, 2017, the U.S. Court of Appeals vacated the FERC’s Opinion Nos. 531, 531-A, and 531-B, and remanded the issue back to the FERC (refer to the “FERC ROE Complaints” section in Note 15, “Commitments and Contingencies”).

*Transmission Incentive Policy Inquiry*

On March 21, 2019 the FERC announced a NOI seeking comments on possible improvements to its electric transmission incentives policy to ensure that it appropriately encourages the development of the infrastructure needed to ensure grid reliability and reduce congestion to reduce the cost of power for consumers. The FERC believes it is prudent to seek comment on whether and how to improve FERC’s current transmission incentives policy. The NOI and the comments are meant to examine whether incentives should continue to be granted based on a project’s risks and challenges or should be based on

the benefits that a project provide. NEP responded to the NOI on June 26, 2019, with reply comments due back on August 26, 2019.

**Narragansett**

*General Rate Case*

Narragansett reached a settlement agreement with the Rhode Island Division of Public Utilities and Carriers ("Division") and several other intervening parties to increase distribution revenue for its electric and gas operations over the three-year period commencing September 1, 2018, which was approved by the RIPUC on August 24, 2018. This settlement is an agreement that was reached in response to the base distribution revenue increase requests that Narragansett filed with the RIPUC on November 27, 2017. Pursuant to the settlement, electric distribution revenue will increase by approximately $14 million, $11 million, and $4 million and gas distribution revenue will increase by approximately $6 million, $8 million, and $4 million annually, on September 1, 2018, September 1, 2019 and September 1, 2020, respectively. The settlement reflects an allowed ROE rate of 9.275% based on a common equity ratio of approximately 51%. Previously, Narragansett was entitled to earn an allowed ROE of 9.5%, with a common equity ratio of approximately 49.1%.

These revenue increases are intended to fund significant systems-related investments, including the replacement of several aging operational systems used in Narragansett's electric and gas businesses with newer integrated systems that will be shared by Narragansett and its electric and gas affiliates. The settlement identifies several additional metrics for tracking and reporting purposes only, some of which may become eligible for a financial performance incentive during the term of the multi-year rate plan. The increases set in place for the second and third years of the settlement may be reopened for recovery of the implementation of advanced metering and grid modernization costs.

*Tax Act*

The RIPUC opened a docket to address the change in the federal corporate income tax rate and other changes resulting from the Tax Act that was signed into law in December 2017. Specifically, the RIPUC requested Narragansett's proposal for how it planned to reduce rates associated with the income taxes recovered from customers on the equity component of the return on investment included in revenue taxed at the new lower income tax rate of 21% effective January 1, 2018, and how it planned to return to customers the reduction in its net deferred income tax liabilities resulting from the 14% decrease in the federal income tax rate from 35%. Effective September 1, 2018, Narragansett reduced its revenue requirement for the distribution electric and gas rates in effect for the impacts of the Tax Act as appropriate. On January 24, 2019, Narragansett filed with the RIPUC a settlement agreement among Narragansett, the Division, the Office of Energy Resources, and the State of Rhode Island Office of the Lieutenant Governor, pursuant to which approximately $5 million and $3 million will be provided to electric and gas customers, respectively, which reflect the benefits of Narragansett's reduced federal corporate income tax payment obligations for the period January 1, 2018 through August 31, 2018. The RIPUC approved the settlement agreement on May 17, 2019, as filed.

*Storm Contingency Fund*

On December 29, 2016, Narragansett filed with the RIPUC a petition to implement a Storm Fund Replenishment Factor ("SFRF") effective July 1, 2017 to collect approximately $84 million over a four-year period to be credited to Narragansett's Storm Contingency Fund ("Storm Fund") to restore the Storm Fund to a surplus position. In addition, Narragansett also requested to extend the annual $3 million of supplemental base distribution rate contributions beyond the current expiration date of January 31, 2019, to coincide with the four-year replenishment period. The Division, which is the primary intervener in Rhode Island on rate matters, filed testimony challenging the recovery of $11 million of the $84 million being sought through the SFRF. On June 21, 2017, the RIPUC unanimously approved Narragansett's request to collect the $84 million. On April 27, 2018, the RIPUC approved the Joint Proposal Settlement Agreement, which proposed a Storm Fund deficit balance reduction of $2 million, instead of $11 million as previously challenged. The SFRF is applicable to all retail electric delivery service customers effective July 1, 2017 for a four-year period. In addition, the RIPUC unanimously approved Narragansett's request to extend the annual $3 million of supplemental base distribution rate contributions to the Storm Fund, which the

RIPUC authorized in Narragansett's 2012 rate case, for an additional 26-month period beyond its current expiration to March 31, 2021.

## 7. EQUITY INVESTMENTS

The following table presents the equity investments recorded on the consolidated balance sheets:

| | March 31, | |
|---|---|---|
| | **2019** | 2018 |
| | *(in millions of dollars)* | |
| Millennium Pipeline Company LLC ("Millennium") | **$ 206** | $ 136 |
| Sunrun | **117** | 111 |
| New York Transco LLC ("NY Transco LLC") | **32** | 32 |
| Energy Impact Fund LP | **28** | 20 |
| Generation Ventures | **21** | 1 |
| Other | **2** | 2 |
| Total | **$ 406** | $ 302 |

The Company owns a 26.25% interest in Millennium, a company that owns a natural gas pipeline from southern New York to the Lower Hudson Valley.

In 2017, the Company entered into an arrangement with San Francisco-based Sunrun, a leading U.S. provider of residential solar energy systems, for a 50% interest, and created National Grid Green Homes, Inc. as a subsidiary to provide investment.

Grid NY LLC, a direct wholly-owned subsidiary, was formed on October 10, 2014 to own a 28.261% equity interest in NY Transco LLC, a New York limited liability company, which was formed pursuant to the articles of organization filed on November 14, 2014 for the purpose of planning, construction, owning, operating, maintaining, and expanding transmission facilities in the state of New York. The Company has made multiple capital contributions since inception, totaling $32 million.

The Company also has a 9.4% interest in Energy Impact Fund LP, a strategic energy venture investment fund that has invested in 26 companies to date.

*Generation Ventures*

Genco owns a 50% interest in each of Island Park Energy Center LLC, LI Solar Generation LLC, LI Energy Storage System LLC, and Clean Energy Generation LLC. Genco makes contributions to these LLCs as needed to fund development activities and operations. Island Park Energy Center LLC was formed to develop, construct, own, and operate a proposed repowering of the E.F. Barrett steam and combustion turbine units, all located in Nassau County, New York. LI Solar Generation LLC is developing a 22.9 MW solar generation project in Calverton, New York based on a 2017 selection by LIPA for power contracts as part of a Request for Proposals ("RFP") process. Clean Energy Generation LLC was formed to jointly respond to RFPs in the State of New York related to generation, energy storage, and demand response resources with intent to develop, construct, own, and operate infrastructure assets if selected.

LI Energy Storage System LLC through its wholly-owned subsidiaries, East Hampton Storage Center LLC and Montauk Energy Storage Center LLC, were awarded contracts by LIPA as part of an RFP process. The award was for separate 5-megawatt hour ("mwh") and 40-mwh battery storage projects in East Hampton, New York and Montauk, New York. The entities own and operate the facilities and provide energy and storage services to LIPA through an executed 20-year PPA with LIPA. During the year ended March 31, 2019, the Company made $11 million in capital contributions to East Hampton Storage Center and $9

million to Montauk Energy Storage Center. The East Hampton Storage Center commenced commercial operations on August 1, 2018. The Montauk Energy Storage Center commenced commercial operations on February 1, 2019.

## 8. PROPERTY, PLANT AND EQUIPMENT

The following table summarizes property, plant and equipment at cost along with accumulated depreciation and amortization:

| | March 31, | |
|---|---|---|
| | **2019** | 2018 |
| | *(in millions of dollars)* | |
| Plant and machinery | **$ 38,510** | $ 35,762 |
| Land and buildings | **2,170** | 2,351 |
| Assets in construction | **2,707** | 2,215 |
| Software and other intangibles | **1,225** | 1,141 |
| Total property, plant and equipment | **44,612** | 41,469 |
| Accumulated depreciation and amortization | **(10,313)** | (9,595) |
| Property, plant and equipment, net | **$ 34,299** | $ 31,874 |

## 9. DERIVATIVE INSTRUMENTS AND HEDGING

The Company utilizes derivative instruments to manage commodity price, interest rate, and foreign currency rate risk associated with its natural gas and electricity purchases and its Euro commercial paper program. The Company's commodity risk management strategy is to reduce fluctuations in firm gas and electricity sales prices to its customers. The Company's interest rate risk management strategy is to minimize its cost of capital. The Company's currency rate risk management policy is to hedge the risk associated with its foreign currency borrowings by utilizing instruments to convert principal and interest payments into U.S. dollars.

The Company's financial exposures are monitored and managed as an integral part of the Company's overall financial risk management policy. The Company engages in risk management activities only in commodities and financial markets where it has an exposure, and only in terms and volumes consistent with its core business.

### Volumes

Volumes of outstanding commodity derivative instruments measured in dekatherms ("dths") and mwhs are as follows:

| | March 31, | |
|---|---|---|
| | **2019** | 2018 |
| | *(in millions)* | |
| Gas derivative contracts (dths) | **163** | 160 |
| Electric derivative contracts (mwhs) | **14** | 14 |

## Derivative Financial Instruments

The following tables reflect the gross and net amounts of the Company's derivative assets and liabilities at March 31, 2019 and 2018:

**March 31, 2019**
*(in millions of dollars)*

| ASSETS: | Gross amounts of recognized assets (liabilities) *A* | Gross amounts offset on the Consolidated Balance Sheet *B* | Net amounts of assets (liabilities) presented on the Consolidated Balance Sheet *C=A+B* | Gross amounts not offset on the Consolidated Balance Sheet *D* | Net amount *E=C-D* |
|---|---|---|---|---|---|
| **Current assets** | | | | | |
| Gas contracts | $ 7 | $ - | $ 7 | $ 1 | $ 6 |
| Electric contracts | 26 | - | 26 | 12 | 14 |
| **Other non-current assets** | | | | | |
| Gas contracts | 1 | - | 1 | - | 1 |
| Electric contracts | 12 | - | 12 | 2 | 10 |
| Cross-currency & interest rate swaps | 13 | - | 13 | 12 | 1 |
| Equity option contracts | 2 | - | 2 | - | 2 |
| Total | 61 | - | 61 | 27 | 34 |
| **LIABILITIES:** | | | | | |
| **Current liabilities** | | | | | |
| Gas contracts | (20) | - | (20) | (1) | (19) |
| Electric contracts | (15) | - | (15) | (12) | (3) |
| Cross-currency & interest rate swaps | (20) | - | (20) | (20) | - |
| Foreign exchange forward contracts | (16) | - | (16) | - | (16) |
| **Other non-current liabilities** | | | | | |
| Gas contracts | (2) | - | (2) | - | (2) |
| Electric contracts | (10) | - | (10) | (2) | (8) |
| Cross-currency & interest rate swaps | (111) | - | (111) | (54) | (57) |
| Equity option contracts | (2) | - | (2) | - | (2) |
| Total | (196) | - | (196) | (89) | (107) |
| **Net liabilities** | $ (135) | $ - | $ (135) | $ (62) | $ (73) |

**March 31, 2018**
*(in millions of dollars)*

| ASSETS: | Gross amounts of recognized assets (liabilities) A | Gross amounts offset on the Consolidated Balance Sheet B | Net amounts of assets (liabilities) presented on the Consolidated Balance Sheet C=A+B | Gross amounts not offset on the Consolidated Balance Sheet D | Net amount E=C-D |
|---|---|---|---|---|---|
| **Current assets** | | | | | |
| Gas contracts | $ 11 | $ - | $ 11 | $ - | $ 11 |
| Electric contracts | 9 | - | 9 | - | 9 |
| Cross-currency & interest rate swaps | 4 | - | 4 | 4 | - |
| **Other non-current assets** | | | | | |
| Electric contracts | 2 | - | 2 | - | 2 |
| Cross-currency & interest rate swaps | 154 | - | 154 | 82 | 72 |
| Equity option contracts | 2 | - | 2 | 2 | - |
| Total | 182 | - | 182 | 88 | 94 |
| **LIABILITIES:** | | | | | |
| **Current liabilities** | | | | | |
| Gas contracts | (12) | - | (12) | - | (12) |
| Electric contracts | (41) | - | (41) | - | (41) |
| Cross-currency & interest rate swaps | (37) | - | (37) | - | (37) |
| **Other non-current liabilities** | | | | | |
| Gas contracts | (7) | - | (7) | - | (7) |
| Electric contracts | (25) | - | (25) | (10) | (15) |
| Cross-currency & interest rate swaps | (45) | - | (45) | (11) | (34) |
| Equity option contracts | (2) | - | (2) | (2) | - |
| Total | (169) | - | (169) | (23) | (146) |
| **Net assets (liabilities)** | $ 13 | $ - | $ 13 | $ 65 | $ (52) |

The Company enters into enabling agreements that allow for payment netting with its counterparties, which reduces its exposure to counterparty risk by providing for the offset of amounts payable to the counterparty against amounts receivable from the counterparty.

The changes in fair value of the Company's rate recoverable contracts (commodity contracts only, hedge contracts are not rate recoverable) are offset by changes in regulatory assets and liabilities. As a result, the changes in fair value of those contracts had no impact in the accompanying consolidated statements of operations and comprehensive income. The majority of the Company's derivative instruments are subject to rate recovery as of March 31, 2019 and 2018.

## Credit and Collateral

The Company is exposed to credit risk related to transactions entered into for commodity price, interest rate and foreign currency rate risk management. Credit risk represents the risk of loss due to counterparty non-performance. Credit risk is managed by assessing each counterparty's credit profile and negotiating appropriate levels of collateral and credit support.

*Commodity Transactions*

The Company enters into commodity transactions on the NYMEX. The NYMEX clearing houses act as the counterparty to each trade. Transactions on the NYMEX must adhere to comprehensive collateral and margining requirements. As a result, transactions on the NYMEX are significantly collateralized and have limited counterparty credit risk.

The credit policy for commodity transactions is managed and monitored by the Finance Committee to the Parent's Board of Directors ("Finance Committee"), which is responsible for approving risk management policies and objectives for risk assessment, control and valuation, and the monitoring and reporting of risk exposures. NGUSA's Energy Procurement Risk Management Committee ("EPRMC") is responsible for approving transaction strategies, annual supply plans, and counterparty credit approval, as well as all valuation and control procedures. The EPRMC is chaired by the Vice President of U.S. Treasury and reports to both the NGUSA Board of Directors and the Finance Committee.

The EPRMC monitors counterparty credit exposure and appropriate measures are taken to bring such exposures below the limits, including, without limitation, netting agreements, and limitations on the type and tenor of trades. In instances where a counterparty's credit quality has declined, or credit exposure exceeds certain levels, the Company may limit its credit exposure by restricting new transactions with the counterparty, requiring additional collateral or credit support, and negotiating the early termination of certain agreements. Similarly, the Company may be required to post collateral to its counterparties.

The Company's credit exposure for all commodity derivative instruments and applicable payables and receivables, net of collateral, and instruments that are subject to master netting agreements, was a liability of zero and $55 million as of March 31, 2019 and 2018, respectively.

The aggregate fair value of the Company's commodity derivative instruments with credit-risk-related contingent features that were in a liability position at March 31, 2019 and 2018 was $6 million and $62 million, respectively. The Company had zero and $10 million collateral posted for these instruments at March 31, 2019 and 2018, respectively. At March 31, 2019, if the Company's credit rating were to be downgraded by one, two, or three levels, it would be required to post additional collateral to its counterparties of zero, zero, or $7 million, respectively. At March 31, 2018, if the Company's credit rating had been downgraded by one, two, or three levels, it would have been required to post additional collateral to its counterparties of $5 million, $14 million, or $55 million, respectively.

*Financing Transactions*

The credit policy for financing transactions is managed by a central treasury department under policies approved by the Finance Committee. In accordance with these treasury policies, counterparty credit exposure utilizations are monitored daily against the counterparty credit limits. Counterparty credit ratings and market conditions are reviewed continually with limits being revised and utilization adjusted, if appropriate. Management does not expect any significant losses from non-performance by these counterparties.

In relation to the Company's financial derivative instruments, the Company had $75 million and $12 million collateral posted for these instruments at March 31, 2019 and 2018, respectively. If the Company's credit rating were to be downgraded by one level it would not be required to post any additional collateral at March 31, 2019 and 2018. At March 31, 2019 and 2018, if the Company's credit rating were to be downgraded by two or three levels, it would be required to post additional collateral to its counterparties of $30 million and $14 million, respectively.

## 10. FAIR VALUE MEASUREMENTS

The following tables present assets and liabilities measured and recorded at fair value on the consolidated balance sheets on a recurring basis and their level within the fair value hierarchy as of March 31, 2019 and 2018:

| | March 31, 2019 | | | |
|---|---|---|---|---|
| | Level 1 | Level 2 | Level 3 | Total |
| | | *(in millions of dollars)* | | |
| **Assets:** | | | | |
| Derivative instruments | | | | |
| Gas contracts | $ - | $ 6 | $ 2 | $ 8 |
| Electric contracts | - | 38 | - | 38 |
| Cross-currency & interest rate swaps | - | 13 | - | 13 |
| Equity option contracts | - | 2 | - | 2 |
| Financial instruments | | | | |
| Securities | 237 | 163 | - | 400 |
| Other | - | - | 72 | 72 |
| Total | 237 | 222 | 74 | 533 |
| **Liabilities:** | | | | |
| Derivative instruments | | | | |
| Gas contracts | - | 18 | 4 | 22 |
| Electric contracts | - | 25 | - | 25 |
| Cross-currency & interest rate swaps | - | 131 | - | 131 |
| Foreign exchange forward contracts | - | 16 | - | 16 |
| Equity option contracts | - | - | 2 | 2 |
| Total | - | 190 | 6 | 196 |
| **Net assets** | $ 237 | $ 32 | $ 68 | $ 337 |

| | March 31, 2018 | | | |
|---|---|---|---|---|
| | Level 1 | Level 2 | Level 3 | Total |
| | | (in millions of dollars) | | |
| **Assets:** | | | | |
| Derivative instruments | | | | |
| Gas contracts | $ - | $ 1 | $ 10 | $ 11 |
| Electric contracts | - | 10 | 1 | 11 |
| Cross-currency & interest rate swaps | - | 158 | - | 158 |
| Equity option contracts | - | - | 2 | 2 |
| Securities | 231 | 155 | - | 386 |
| Total | 231 | 324 | 13 | 568 |
| **Liabilities:** | | | | |
| Derivative instruments | | | | |
| Gas contracts | - | 11 | 8 | 19 |
| Electric option contracts | - | 65 | 1 | 66 |
| Cross-currency & interest rate swaps | - | 82 | - | 82 |
| Equity option contracts | - | - | 2 | 2 |
| Total | - | 158 | 11 | 169 |
| **Net assets** | $ 231 | $ 166 | $ 2 | $ 399 |

**Derivative instruments**: The Company's Level 1 fair value derivative instruments primarily consist of quoted prices (unadjusted) in active markets for identical assets or liabilities that a company has the ability to access as of the reporting date. Derivative assets and liabilities utilizing Level 1 inputs include active exchange-based derivative instruments (e.g. natural gas futures traded on the NYMEX).

The Company's Level 2 fair value derivative instruments primarily consist of over-the-counter ("OTC") currency swap transactions, and gas swap contracts with pricing inputs obtained from the NYMEX and the Intercontinental Exchange ("ICE"), except in cases where the ICE publishes seasonal averages or where there were no transactions within the last seven days. The Company may utilize discounting based on quoted interest rate curves, including consideration of non-performance risk, and may include a liquidity reserve calculated based on bid/ask spread for the Company's Level 2 derivative instruments. Substantially all of these price curves are observable in the marketplace throughout at least 95% of the remaining contractual quantity, or they could be constructed from market observable curves with correlation coefficients of 95% or higher.

The Company's Level 3 fair value derivative instruments primarily consist of OTC gas option contracts and gas purchase contracts, which are valued based on internally-developed models. The Company also has equity options, which are designated as Level 3 derivatives as they are traded on illiquid markets. Industry-standard valuation techniques, such as the Black-Scholes pricing model, Monte Carlo simulation, and Financial Engineering Associates libraries are used for valuing such instruments. A derivative is designated Level 3 when it is valued based on a forward curve that is internally developed, extrapolated, or derived from market observable curves with correlation coefficients less than 95%, where optionality is present, or if non-economic assumptions are made.

**Securities:** Securities are included in financial investments on the consolidated balance sheets and primarily include equity and debt investments based on quoted market prices (Level 1) and municipal and corporate bonds based on quoted prices of similar traded assets in open markets (Level 2).

The Company's Level 3 investments include investments in associates relating to Sunrun, accounted for at fair value (as discussed in Note 15, "Commitments and Contingencies" under "Financial Guarantees") and further equity investments accounted for at fair value through profit and loss. These equity holdings are part of the Company's corporate venture capital portfolio held by NGP and comprise a series of small minority interest unquoted investments where prices or valuation inputs

are unobservable. These investments are new this year and as such the valuation is based on the latest transaction price, being the price the Company paid for the investments.

## 11. EMPLOYEE BENEFITS

The Company sponsors several qualified and non-qualified non-contributory defined benefit plans (the "Pension Plans") and PBOP plans (together with the Pension Plan (the "Plans")), covering substantially all employees.

All of the Company's regulated subsidiaries have regulatory recovery of these costs and therefore have recorded related regulatory assets (liabilities) on the consolidated balance sheets. The Company records amounts for its unregulated subsidiaries to AOCI on the consolidated balance sheets.

*Pension Plans*

The Pension Plans are defined benefit plans which provide union employees, as well as non-union employees hired before January 1, 2011, with a retirement benefit. Supplemental non-qualified, non-contributory executive retirement programs provide additional defined pension benefits for certain executives. During the years ended March 31, 2019 and 2018, the Company made contributions of approximately $278 million and $258 million, respectively, to the qualified pension plans. The Company expects to contribute $180 million to the qualified pension plans during the year ending March 31, 2020.

Benefit payments to pension plan participants for the years ended March 31, 2019 and 2018 were approximately $520 million and $492 million, respectively.

*PBOP Plans*

The PBOP plans provide health care and life insurance coverage to eligible retired employees. Eligibility is based on age and length of service requirements and, in most cases, retirees must contribute to the cost of their coverage. During the years ended March 31, 2019 and 2018, the Company made contributions of zero and approximately $138 million, respectively, to the PBOP plans. The Company does not expect to contribute to the PBOP plans during the year ending March 31, 2020.

Benefit payments to PBOP plan participants for the years ended March 31, 2019 and 2018 were approximately $184 million and $207 million, respectively.

### Defined Contribution Plans

The Company has two defined contribution pension plans that cover substantially all employees. For the years ended March 31, 2019 and 2018, the Company recognized an expense in the accompanying consolidated statements of operations and comprehensive income of $77 million and $67 million, respectively.

### Net Periodic Benefit Costs

The Company's net periodic benefit pension cost for the years ended March 31, 2019 and 2018 was $253 million and $277 million, respectively.

The Company's net periodic benefit PBOP cost for the years ended March 31, 2019 and 2018 was $33 million and $65 million, respectively.

**Amounts Recognized in AOCI and Regulatory Assets**

The following tables summarize other pre-tax changes in plan assets and benefit obligations recognized primarily in regulatory assets and AOCI for the years ended March 31, 2019 and 2018:

| | Pension Plans | | PBOP Plans | |
|---|---|---|---|---|
| | Years Ended March 31, | | Years Ended March 31, | |
| | **2019** | 2018 | **2019** | 2018 |
| | *(in millions of dollars)* | | | |
| Net actuarial loss (gain) | **$ 131** | $ 28 | **$ 22** | $ (137) |
| Prior service cost | **25** | - | **-** | - |
| Amortization of net actuarial loss | **(258)** | (276) | **(25)** | (40) |
| Amortization of prior service (cost) credit, net | **(7)** | (6) | **6** | 6 |
| Total | **$ (109)** | $ (254) | **$ 3** | $ (171) |
| | | | | |
| Included in regulatory assets | **$ (90)** | $ 415 | **$ 2** | $ (74) |
| Included in AOCI | **(19)** | (669) | **1** | (97) |
| Total | **$ (109)** | $ (254) | **$ 3** | $ (171) |

The Company's regulated subsidiaries have regulatory recovery of these obligations and therefore amounts are included in regulatory assets on the consolidated balance sheets. Costs of non-regulated subsidiaries are recorded as part of AOCI on the consolidated balance sheets.

**Amounts Recognized in AOCI and Regulatory Assets – not yet recognized as components of net actuarial loss**

The following tables summarize the Company's amounts in regulatory assets and AOCI on the consolidated balance sheets that have not yet been recognized as components of net actuarial loss at March 31, 2019 and 2018:

| | Pension Plans | | PBOP Plans | |
|---|---|---|---|---|
| | Years Ended March 31, | | Years Ended March 31, | |
| | **2019** | 2018 | **2019** | 2018 |
| | *(in millions of dollars)* | | | |
| Net actuarial loss | **$ 1,300** | $ 1,427 | **$ 69** | $ 72 |
| Prior service cost (credit) | **48** | 30 | **(4)** | (10) |
| Total | **$ 1,348** | $ 1,457 | **$ 65** | $ 62 |
| | | | | |
| Included in regulatory assets | **$ 1,180** | $ 1,270 | **$ 104** | $ 102 |
| Included in AOCI | **168** | 187 | **(39)** | (40) |
| Total | **$ 1,348** | $ 1,457 | **$ 65** | $ 62 |

The amount of net actuarial loss and prior service cost to be amortized from regulatory assets and AOCI during the year ending March 31, 2020 for the Pension Plans is $186 million and $8 million, respectively, and net actuarial loss and prior service benefit to be amortized from regulatory assets and AOCI during the year ending March 31, 2020 for the PBOP Plans is $18 million and $(4) million, respectively.

**Amounts Recognized on the Consolidated Balance Sheets**

The following table summarizes the portion of the funded status that is recognized on the Company's consolidated balance sheets at March 31, 2019 and 2018:

| | Pension Plans | | PBOP Plans | |
|---|---|---|---|---|
| | March 31, | | March 31, | |
| | **2019** | 2018 | **2019** | 2018 |
| | *(in millions of dollars)* | | | |
| Projected benefit obligation | **$ (9,098)** | $ (9,068) | **$ (4,478)** | $ (4,489) |
| Fair value of plan assets | **8,649** | 8,460 | **3,437** | 3,506 |
| Total | **$ (449)** | $ (608) | **$ (1,041)** | $ (983) |
| Non-current assets | **$ 365** | $ 341 | **$ 17** | $ 18 |
| Current liabilities | **(23)** | (23) | **(12)** | (11) |
| Non-current liabilities | **(791)** | (926) | **(1,046)** | (990) |
| Total | **$ (449)** | $ (608) | **$ (1,041)** | $ (983) |

The benefit obligation shown above is the projected benefit obligation for the Pension Plans and the accumulated projected benefit obligation ("APBO") for the PBOP Plans. The Pension Plans had APBO balances that exceeded the fair value of plan assets as of March 31, 2019 and 2018. The aggregate APBO balance for the Pension Plans was $8.7 billion as of both March 31, 2019 and 2018.

**Expected Benefit Payments**

Based on current assumptions, the Company expects to make the following benefit payments subsequent to March 31, 2019:

| *(in millions of dollars)*<br>Years Ending March 31, | Pension Plans | PBOP Plans |
|---|---|---|
| 2020 | $ 524 | $ 185 |
| 2021 | 524 | 193 |
| 2022 | 528 | 202 |
| 2023 | 534 | 211 |
| 2024 | 540 | 218 |
| 2025-2029 | 2,790 | 1,173 |
| Total | $ 5,440 | $ 2,182 |

**Assumptions Used for Employee Benefits Accounting**

| | Pension Plans | | PBOP Plans | |
|---|---|---|---|---|
| | Years Ended March 31, | | Years Ended March 31, | |
| | **2019** | 2018 | **2019** | 2018 |
| **Benefit Obligations:** | | | | |
| Discount rate | **4.10%** | 4.10% | **4.10%** | 4.10% |
| Rate of compensation increase | **3.50%** | 3.50% | **N/A** | N/A |
| Expected return on plan assets | **6.00% - 6.50%** | 6.00% - 6.25% | **6.00% - 7.25%** | 6.25% - 6.75% |
| **Net Periodic Benefit Costs:** | | | | |
| Discount rate | **4.10% - 4.50%** | 4.30% | **4.10%** | 4.30% |
| Rate of compensation increase | **3.50%** | 3.50% | **N/A** | N/A |
| Expected return on plan assets | **6.00% - 6.25%** | 6.25% - 6.50% | **6.25% - 6.75%** | 6.50% - 6.75% |

The Company selects its discount rate assumption based upon rates of return on highly rated corporate bond yields in the marketplace as of each measurement date. Specifically, the Company uses the Hewitt AA Above Median Curve along with the expected future cash flows from the Company retirement plans to determine the weighted average discount rate assumption.

The expected rate of return for various passive asset classes is based both on analysis of historical rates of return and forward-looking analysis of risk premiums and yields. Current market conditions, such as inflation and interest rates, are evaluated in connection with the setting of the long-term assumptions. A small premium is added for active management of both equity and fixed income securities. The rates of return for each asset class are then weighted in accordance with the actual asset allocation, resulting in a long-term return on asset rate for each plan.

**Assumed Health Cost Trend Rate**

| | March 31, | |
|---|---|---|
| | **2019** | 2018 |
| Health care cost trend rate assumed for next year | | |
| Pre 65 | **7.25%** | 7.50% |
| Post 65 | **5.75%** | 5.75% |
| Prescription | **9.75%** | 10.25% |
| Rate to which the cost trend is assumed to decline (ultimate) | **4.50%** | 4.50% |
| Year that rate reaches ultimate trend | | |
| Pre 65 | **2028** | 2028 |
| Post 65 | **2026** | 2026 |
| Prescription | **2027** | 2027 |

**Plan Assets**

The Company manages the benefit plan investments to minimize the long-term cost of operating the Plans, with a reasonable level of risk. Risk tolerance is determined as a result of a periodic study which analyzes the Plans' liabilities and funded status and results in the determination of the allocation of assets across equity fixed income securities and other investments. Equity investments are broadly diversified across U.S. and non-U.S. stocks, as well as across growth, value, and small and large capitalization stocks. Likewise, the fixed income portfolio is broadly diversified across market segments. Approximately 10% of the total investment portfolio is approved for investments in private equity, real estate, and infrastructure with the objective of enhancing long-term returns while improving portfolio diversification. For the PBOP Plans, since the earnings on

a portion of the assets are taxable, those investments are managed to maximize after tax returns consistent with the broad asset class parameters established by the asset allocation study. Investment risk and return are reviewed by the Company's Investment Committee on a quarterly basis.

The Pension Plans are trusteed non-contributory defined benefit plan covering all eligible represented and non-represented employees of the Company. The PBOP Plans are both contributory and non-contributory, trusteed, employee life insurance and medical benefit plans sponsored by the Company. Life insurance and medical benefits are provided for eligible retirees, dependents, and surviving spouses of the Company.

The target asset allocations for the benefit plans as of March 31, 2019 and 2018 are as follows:

| | **Pension Plans** | | **Union PBOP Plans** | | **Non-Union PBOP Plans** | |
|---|---|---|---|---|---|---|
| | **March 31,** | | **March 31,** | | **March 31,** | |
| | **2019** | 2018 | **2019** | 2018 | **2019** | 2018 |
| U.S. equities | **20%** | 20% | **34%** | 34% | **45%** | 45% |
| Global equities (including U.S.) | **7%** | 7% | **12%** | 12% | **0%** | 0% |
| Global tactical asset allocation | **10%** | 10% | **17%** | 17% | **0%** | 0% |
| Non-U.S. equities | **10%** | 10% | **17%** | 17% | **25%** | 25% |
| Fixed income securities | **40%** | 40% | **20%** | 20% | **30%** | 30% |
| Private equity | **5%** | 5% | **0%** | 0% | **0%** | 0% |
| Real estate | **5%** | 5% | **0%** | 0% | **0%** | 0% |
| Infrastructure | **3%** | 3% | **0%** | 0% | **0%** | 0% |
| | **100%** | 100% | **100%** | 100% | **100%** | 100% |

**Fair Value Measurements**

The following tables provide the fair value measurement amounts for the pension and PBOP assets:

| | March 31, 2019 | | | | |
|---|---|---|---|---|---|
| | Level 1 | Level 2 | Level 3 | Not categorized | Total |
| | | | (in millions of dollars) | | |
| **Pension Assets:** | | | | | |
| Cash and cash equivalents | $ - | $ 43 | $ - | $ 100 | $ 143 |
| Accounts receivable | 252 | - | - | - | 252 |
| Accounts payable | (497) | - | - | - | (497) |
| Equity | 670 | - | - | 2,387 | 3,057 |
| Global tactical asset allocation | 239 | - | - | 659 | 898 |
| Fixed income securities | - | 2,515 | - | 1,268 | 3,783 |
| Preferred securities | - | 25 | - | - | 25 |
| Private equity | - | - | - | 576 | 576 |
| Real estate | - | - | - | 412 | 412 |
| Total | $ 664 | $ 2,583 | $ - | $ 5,402 | $ 8,649 |
| **PBOP Assets:** | | | | | |
| Cash and cash equivalents | $ 44 | $ - | $ - | $ 2 | $ 46 |
| Accounts receivable | 9 | - | - | - | 9 |
| Equity | 524 | - | - | 1,540 | 2,064 |
| Global tactical asset allocation | 229 | - | - | 410 | 639 |
| Fixed income securities | 3 | 675 | - | - | 678 |
| Private equity | - | - | - | 1 | 1 |
| Total | $ 809 | $ 675 | $ - | $ 1,953 | $ 3,437 |

| | March 31, 2018 | | | | |
|---|---|---|---|---|---|
| | Level 1 | Level 2 | Level 3 | Not categorized | Total |
| | | | *(in millions of dollars)* | | |
| **Pension Assets:** | | | | | |
| Cash and cash equivalents | $ 2 | $ 73 | $ - | $ 102 | $ 177 |
| Accounts receivable | 352 | - | - | - | 352 |
| Accounts payable | (567) | - | - | - | (567) |
| Equity | 1,068 | - | - | 2,344 | 3,412 |
| Global tactical asset allocation | - | - | - | 627 | 627 |
| Fixed income securities | - | 2,289 | - | 1,249 | 3,538 |
| Preferred securities | - | 26 | - | - | 26 |
| Private equity | - | - | - | 503 | 503 |
| Real estate | - | - | - | 392 | 392 |
| Total | $ 855 | $ 2,388 | $ - | $ 5,217 | $ 8,460 |
| **PBOP Assets:** | | | | | |
| Cash and cash equivalents | $ 40 | $ - | $ - | $ 1 | $ 41 |
| Accounts receivable | 6 | - | - | - | 6 |
| Equity | 714 | - | - | 1,556 | 2,270 |
| Global tactical asset allocation | 89 | - | - | 394 | 483 |
| Fixed income securities | 6 | 696 | - | - | 702 |
| Private equity | - | - | - | 4 | 4 |
| Total | $ 855 | $ 696 | $ - | $ 1,955 | $ 3,506 |

The methods used to fair value pension and PBOP assets are described below:

**Cash and cash equivalents**: Cash and cash equivalents that can be priced daily are classified as Level 1. Active reserve funds, reserve deposits, commercial paper, repurchase agreements, and commingled cash equivalents are classified as Level 2. Cash and cash equivalents invested in commingled money market investment funds, which have NAV pricing per fund share, are excluded from the fair value hierarchy.

**Accounts receivable and accounts payable:** Accounts receivable and accounts payable are classified as Level 1. Such amounts are short-term and settle within a few days of the measurement date.

**Equity and preferred securities:** Common stocks, preferred stocks, and real estate investment trusts are valued using the official close of the primary market on which the individual securities are traded. Equity securities are primarily comprised of securities issued by public companies in domestic and foreign markets plus investments in commingled funds, which are valued on a daily basis. If the Company can exchange shares of the publicly traded securities and the fair values are primarily sourced from the closing prices on stock exchanges where there is active trading, the securities are classified as Level 1 investments. Mutual funds with publicly quoted prices and active trading are classified as Level 1 investments. For investments in commingled funds that are not publicly traded and have ongoing subscription and redemption activity, the fair value of the investment is the NAV as a practical expedient per fund share, derived from the underlying securities' quoted prices in active markets. These investments are excluded from the fair value hierarchy.

**Global tactical asset allocation:** Assets held in global tactical asset allocation funds are managed by investment managers who use both top-down and bottom-up valuation methodologies to value asset classes, countries, industrial sectors, and individual securities in order to allocate and invest assets opportunistically. Mutual funds with publicly quoted prices and active trading are classified as Level 1 investments. For commingled funds that are not publicly traded and have ongoing subscription and redemption activity, the fair value of the investment is the NAV used as a practical expedient per fund share. These investments are excluded from the fair value hierarchy. Investments with redemption restrictions and that use NAV are excluded from the fair value hierarchy.

**Fixed income securities:** Fixed income securities (which include corporate debt securities, municipal fixed income securities, U.S. Government and Government agency securities including government mortgage backed securities, index linked government bonds, and state and local bonds), convertible securities, and investments in securities lending collateral (which include repurchase agreements, asset backed securities, floating rate notes and time deposits) are valued with an institutional bid valuation. A bid valuation is an estimated price a dealer would pay for a security (typically in an institutional round lot). Oftentimes, these evaluations are based on proprietary models which pricing vendors establish for these purposes. In some cases there may be manual sources when primary vendors do not supply prices. Fixed income investments are primarily comprised of fixed income securities and fixed income commingled funds. The prices for direct investments in fixed income securities are generated on a daily basis. Prices generated from less active trading with wider bid ask prices are classified as Level 2 investments. Mutual funds with publicly quoted prices and active trading are classified as Level 1 investments. For commingled funds that are not publicly traded and have ongoing subscription and redemption activity, the fair value of the investment is the NAV used as a practical expedient per fund share. These investments are excluded from the fair value hierarchy.

**Private equity and real estate:** Commingled equity funds, commingled special equity funds, limited partnerships, real estate, venture capital, and other investments are valued using evaluations (NAV used as a practical expedient per fund share) based on proprietary models, or based on the NAV used as a practical expedient. Investments in private equity and real estate funds are primarily invested in privately held real estate investment properties, trusts, and partnerships as well as equity and debt issued by public or private companies. The Company's interest in the fund or partnership is estimated based on the NAV used as a practical expedient. The Company's interest in these funds cannot be readily redeemed due to the inherent lack of liquidity and the primarily long-term nature of the underlying assets. Distribution is made through the liquidation of the underlying assets. The Company views these investments as part of a long-term investment strategy. These investments are valued by each investment manager based on the underlying assets. The funds utilize valuation techniques consistent with the market, income, and cost approaches to measure the fair value of certain real estate investments. The majority of the underlying assets are valued using significant unobservable inputs and often require significant management judgment or estimation based on the best available information. Market data includes observations of the trading multiples of public companies considered comparable to the private companies being valued. Investments in limited partnerships with redemption restrictions and that use NAV as a practical expedient are excluded from the fair value hierarchy.

While management believes its valuation methodologies are appropriate and consistent with other market participants, the use of different methodologies or assumptions to determine the NAV used as a practical expedient could result in a different fair value measurement at the reporting date.

## 12. CAPITALIZATION

The aggregate maturities of long-term debt for the years subsequent to March 31, 2019 are as follows:

| *(in millions of dollars)*<br>Years Ending March 31, | | |
|---|---|---|
| 2020 | $ | 1,280 |
| 2021 | | 1,064 |
| 2022 | | 883 |
| 2023 | | 1,305 |
| 2024 | | 682 |
| Thereafter | | 12,949 |
| Total | $ | 18,163 |

Sinking fund repayment requirements related to certain of the Company's First Mortgage Bonds ("FMB") for the years subsequent to March 31, 2019 are as follows:

| *(in millions of dollars)*<br>Years Ending March 31, | | |
|---|---|---|
| 2020 | $ | 1 |
| 2021 | | 1 |
| 2022 | | 1 |
| 2023 | | 1 |
| 2024 | | 1 |
| Thereafter | | 3 |
| Total | $ | 8 |

The Company's debt agreements and banking facilities contain covenants, including those relating to the periodic and timely provision of financial information by the issuing entity and financial covenants such as restrictions on the level of indebtedness. Failure to comply with these covenants, or to obtain waivers of those requirements, could in some cases trigger a right, at the lender's discretion, to require repayment of some of the Company's debt and may restrict the Company's ability to draw upon its facilities or access the capital markets. The Company's subsidiaries also have restrictions on the payment of dividends which relate to their debt to equity ratios. During the years ended March 31, 2019 and 2018, the Company was in compliance with all such covenants.

**Significant Debt Facilities**

*European Medium Term Note Program*

At March 31, 2019, the Company had a Euro Medium Term Note program (the "Program") under which it is able to issue debt instruments ("Instruments") up to a total of the equivalent of 8 billion Euros. Instruments issued under the Program are admitted to trading on the London Stock Exchange. The Program commenced in December 2007 and is renewed annually, with the latest renewal of the Program expiring in December 2019. If the Program was not renewed, it would have precluded the issuance of new notes under this Program, but it would not impact the outstanding debt balances and their maturity dates. Instruments carry certain affirmative and negative covenants, including a restriction on the Company's ability to mortgage, pledge, charge, or otherwise encumber its assets in order to secure, guarantee, or indemnify other listed or quoted debt obligations, as well as cross-acceleration in the event of breach by the Company or its principal subsidiaries of other listed or quoted debt obligations. At March 31, 2019 and 2018, the Company was in compliance with all covenants. At March 31, 2019 and 2018, $3.5 billion and $4.6 billion of these notes were issued and outstanding, respectively.

*Convertible Bond and Export Credit Agreements*

In September 2015, the Company issued a non-dilutive, cash-settled convertible bond which is valued at $521 million and $561 million at March 31, 2019 and 2018, respectively. At the same time, the Company purchased call options to offset the embedded option in the bond. The Company has Export Credit Agreements totaling $1,118 million, of which $449 million and $129 million were outstanding as of March 31, 2019 and 2018, respectively. The Company has procured this financing in relation to its share of investment in the North Sea Link interconnector and Interconnexion France-Angleterre 2 interconnector.

*Notes Payable*

In July 2017, Boston Gas issued $500 million of unsecured senior long-term debt at 3.15% for $499 million ($1 million discount) with a maturity date of August 1, 2027. In October 2017, Colonial Gas issued $150 million of unsecured senior long-term debt at 3.13% with a maturity date of October 5, 2027. In December 2017, NEP issued $400 million of unsecured senior long-term debt at 3.80% for $397 million ($3 million discount) with a maturity date of December 5, 2047. In March 2018, Brooklyn Union issued $650 million of unsecured senior long-term debt at 4.27% with a maturity date of March 15, 2048. In July 2018,

Narragansett issued $350 million of unsecured senior long-term debt at 3.92% with a maturity date of August 1, 2028. In December 2018, Niagara Mohawk issued $500 million of unsecured senior long-term debt at 4.28% with a maturity date of December 15, 2028. In March 2019, Brooklyn Union issued $550 million of unsecured long-term debt at 3.87% with a maturity date of March 4, 2029 and $450 million of unsecured long-term debt at 4.49% with a maturity date of March 4, 2049.

The following table represents the Company's note payables for the years ended March 31, 2019 and 2018:

| | Interest Rate | Maturity Date | March 31, 2019 | March 31, 2018 |
|---|---|---|---|---|
| | | | (in millions of dollars) | |
| *Brooklyn Union Unsecured Notes:* | | | | |
| Senior Note | 3.41% | March 10, 2026 | $ 500 | $ 500 |
| Senior Note | 3.87% | March 4, 2029 | 550 | - |
| Senior Note | 4.50% | March 10, 2046 | 500 | 500 |
| Senior Note | 4.27% | March 15, 2048 | 650 | 650 |
| Senior Note | 4.49% | March 4, 2049 | 450 | - |
| **Brooklyn Union Notes** | | | 2,650 | 1,650 |
| *KeySpan Gas East Unsecured Notes:* | | | | |
| Senior Note | 5.82% | April 1, 2041 | 500 | 500 |
| Senior Note | 2.74% | August 15, 2026 | 700 | 700 |
| **KeySpan Gas East Notes** | | | 1,200 | 1,200 |
| *Boston Gas Unsecured Notes:* | | | | |
| *Senior Note* | 4.49% | February 15, 2042 | 500 | 500 |
| *Senior Note* | 3.15% | August 1, 2027 | 500 | 500 |
| *Boston Gas MTN:* | | | | |
| MTN Series 1992 A | 8.33% | July 10, 2018 | - | 10 |
| MTN Series 1994 B | 6.93% | January 15, 2019 | - | 10 |
| MTN Series 1989 A | 8.97% | December 15, 2019 | 7 | 7 |
| MTN Series 1990 A | 9.75% | December 1, 2020 | 5 | 5 |
| MTN Series 1990 A | 9.05% | September 1, 2021 | 15 | 15 |
| MTN Series 1992 A | 8.33% | July 5, 2022 | 10 | 10 |
| MTN Series 1995 C | 6.95% | December 1, 2023 | 10 | 10 |
| MTN Series 1994 B | 6.98% | January 15, 2024 | 6 | 6 |
| MTN Series 1995 C | 6.95% | December 1, 2024 | 5 | 5 |
| MTN Series 1995 C | 7.25% | October 1, 2025 | 20 | 20 |
| MTN Series 1995 C | 7.25% | October 1, 2025 | 5 | 5 |
| **Boston Gas Notes** | | | 1,083 | 1,103 |
| *Colonial Gas Unsecured Notes:* | | | | |
| Senior Note-Series A | 3.30% | March 15, 2022 | 25 | 25 |
| Senior Note-Series A | 4.63% | March 15, 2042 | 25 | 25 |
| Senior Note-Series A | 3.13% | October 5, 2027 | 150 | 150 |
| **Colonial Gas Notes** | | | 200 | 200 |
| *NGUSA MTM* | 8.00% | November 15, 2030 | 250 | 250 |
| *NGUSA Unsecured Notes:* | | | | |
| Senior Note | 5.80% | April 1, 2035 | 307 | 307 |
| Senior Note | 5.88% | April 1, 2033 | 150 | 150 |
| **NGUSA Notes** | | | 707 | 707 |
| *Niagara Mohawk Unsecured Notes:* | | | | |
| Senior Note | 4.88% | August 15, 2019 | 750 | 750 |
| Senior Note | 2.72% | November 28, 2022 | 300 | 300 |
| Senior Note | 3.51% | October 1, 2024 | 500 | 500 |
| Senior Notes | 4.28% | December 15, 2028 | 500 | - |
| Senior Note | 4.28% | October 1, 2034 | 400 | 400 |
| Senior Note | 4.12% | November 28, 2042 | 400 | 400 |
| **Niagara Mohawk Notes** | | | 2,850 | 2,350 |
| *Narragansett Electric Unsecured Notes:* | | | | |
| Senior Note | 4.53% | March 15, 2020 | 250 | 250 |
| Senior Note | 3.92% | August 1, 2028 | 350 | - |
| Senior Note | 5.64% | March 15, 2040 | 300 | 300 |
| Senior Note | 4.17% | December 10, 2042 | 250 | 250 |
| **Narragansett Electric Notes** | | | 1,150 | 800 |
| *Massachusetts Electric Unsecured Notes:* | | | | |
| Senior Note | 5.90% | Novemeber 15, 2039 | 800 | 800 |
| Senior Note | 4.00% | August 15, 2046 | 500 | 500 |
| **Massachusetts Electric Notes:** | | | 1,300 | 1,300 |
| *New England Power Unsecured Notes:* | | | | |
| Senior Notes | 3.80% | December 5, 2047 | 400 | 400 |
| **Total** | | | $ 11,540 | $ 9,710 |

*First Mortgage Bonds*

The assets of Colonial Gas and Narragansett are subject to liens and other charges and are provided as collateral over borrowings of $75 million and $30 million, respectively, of non-callable FMB at March 31, 2019. These FMB indentures include, among other provisions, limitations on the issuance of long-term debt.

*State Authority Financing Bonds*

At March 31, 2019, the Company had outstanding $834 million of State Authority Financing Bonds, of which, approximately $490 million were issued through the New York State Energy Research and Development Authority ("NYSERDA") and the remaining $344 million were issued through various other state agencies.

At March 31, 2018, Niagara Mohawk had approximately $429 million of tax-exempt revenue bonds in a variable interest rate mode ("TE Bonds") issued by the NYSERDA. Niagara Mohawk pledged to the NYSERDA collateral, in the form of first mortgage bonds ("Pledged Bonds"), to secure the repayment of the NYSERDA TE bonds. The Pledged Bonds were issued under its 1937 Mortgage Trust Indenture, as amended and supplemented from time to time, that established a blanket lien (the "Indenture") (i.e. mortgage lien) on substantially all of Niagara Mohawk's operating properties.

In September and October 2018, Niagara Mohawk requested and received approval from the NYSERDA to convert the TE Bonds into a fixed rate mode which was fully completed on October 11, 2018. In connection with the mode conversion Niagara Mohawk i) cancelled the Insurance Policy, ii) replaced the Pledge Bonds with an unsecured note which eliminated the Pledge Bonds and effectively discharged the mortgage lien under the Indenture, and iii) made other modifications to NYSERDA TE Bonds transactional documents. The TE bonds were converted from a variable interest rate mode into a fixed rate interest mode ranging from 3.23% to 3.48%. These conversions were accounted for as extinguishments in accordance with ASC 470, "Debt." Prior to the conversion, the bonds bore interest at short-term interest rates ranging from 0.84% to 5.53% and 0.66% to 4.69% for the years ended March 31, 2019 and 2018, respectively.

Additionally, Genco has $41 million of 1999 Series A Pollution Control Revenue Bonds due October 1, 2028. The interest rate on the various variable rate series ranged from 0.94% to 3.72% during the year ended March 31, 2019 and 0.50% to 18.00% during the year ended March 31, 2018. Genco also has outstanding $25 million of variable rate 1997 Series A Electric Facilities Revenue Bonds due December 1, 2027 issued through the NYSERDA. The interest rate on the various variable rate series ranged from 1.00% to 1.95% during the year ended March 31, 2019 and 0.90% to 1.77% during the year ended March 31, 2018.

At March 31, 2019, NEP had outstanding $293 million of Pollution Control Revenue Bonds in tax-exempt commercial paper mode and Nantucket had $51 million of Electric Revenue Bonds in tax exempt commercial paper mode. The Electric Revenue Bonds were issued by the Massachusetts Development Finance Agency in connection with Nantucket's financing of its first and second underground and submarine cable projects.

*Intercompany Notes Payable*

NGNA's intercompany debt is in the form of intercompany loans from the Parent and other affiliated entities obtained to fund the acquisition of various entities. The intercompany loans are paid back by NGNA from the dividends it receives from NGUSA.

A summary of the Intercompany Notes Payable is as follows:

| Due to: | Interest Rate | Maturity Date | March 31, 2019 | 2018 |
|---|---|---|---|---|
| | | | (in millions of dollars) | |
| NatGrid TW1 Limited | 0.92% to 1.08% over LIBOR | July 2019 - July 2027 | **$ 1,172** | $ 1,172 |
| National Grid Twenty Five Limited | 2.30% over LIBOR | July 2018 | **-** | 616 |
| Total | | | **$ 1,172** | $ 1,788 |

*Standby Bond Purchase Agreement*

NEP and Nantucket have a Standby Bond Purchase Agreement, which expires on June 14, 2023. This agreement provides liquidity support for the $344 million long-term bonds in tax-exempt commercial paper mode. The Company has classified the debt as long-term due to its intent and ability to refinance the debt on a long-term basis in the event of a failure to remarket the bonds.

*Committed Facility Agreements*

At March 31, 2019, NGUSA, NGNA, and the Parent have committed revolving credit facilities of $3.7 billion, of which $1.3 billion matures in June 2021, $2.2 billion matures in May 2022, and $0.2 billion matures in June 2024. These facilities have not been drawn against. NGUSA, NGNA, and the Parent can all draw on these facilities in a variety of currencies as needed, but the aggregate borrowings across the group cannot exceed the $3.7 billion limit. The terms of the facilities restrict the borrowing of all U.S. subsidiaries of the Company to $25 billion excluding intercompany indebtedness. Additionally, these facilities have a number of non-financial covenants which the Company is obliged to meet. At March 31, 2019 and 2018, NGUSA, NGNA, and the Parent were in compliance with all covenants.

*Commercial Paper and Revolving Credit Agreements*

At March 31, 2019, the Company had two commercial paper programs totaling $4 billion; a $2 billion U.S. commercial paper program and a $2 billion Euro commercial paper program. In support of these programs, the Company was a named borrower under the Parent's credit facilities with $3.7 billion available to the Company. These facilities support both the Parent's and the Company's commercial paper programs for ongoing working capital needs. At March 31, 2019 and 2018, there were $200 million and $290 million of borrowings outstanding on the U.S. commercial paper program and $944 million and zero outstanding on the Euro commercial paper program, respectively.

The credit facilities allow both the Parent and the Company to borrow in multi-currencies. The current annual commitment fees range from 0.09% to 0.28%. If for any reason the Company were not able to issue sufficient commercial paper or source funds from other sources, the facilities could be drawn upon to meet cash requirements. The facilities contain certain affirmative and negative operating covenants, including restrictions on the Company's utility subsidiaries' ability to mortgage, pledge, encumber, or otherwise subject their utility property to any lien, as well as financial covenants that require the Company and the Parent to limit the total indebtedness in U.S. and non-U.S. subsidiaries to pre-defined limits. Violation of these covenants could result in the termination of the facilities and the required repayment of amounts borrowed thereunder, as well as possible cross defaults under other debt agreements.

*Other Redemptions*

The following table indicates the Company's redemptions for the years ended March 31, 2019 and 2018:

| | Interest Rate | Maturity Date | Years Ended March 31, 2019 | 2018 |
|---|---|---|---|---|
| | | | (in millions of dollars) | |
| *Brooklyn Union GFRB:* | | | | |
| 1997 | Variable | December 1, 2020 | $ - | $ 125 |
| 2005B | Variable | June 1, 2025 | - | 55 |
| 1991D | Variable | July 1, 2026 | - | 50 |
| *Boston Gas MTN:* | | | | |
| MTN Series 1992 A | 8.33% | July 10, 2017 | - | 8 |
| MTN Series 1992 A | 8.33% | July 10, 2018 | **10** | - |
| MTN Series 1994 B | 6.93% | January 15, 2019 | **10** | - |
| *Narragansett Electric First Mortgage Bonds:* | | | | |
| FMB Series P & R | 7.5% - 8.09% | September 30, 2022 - December 15, 2025 | **1** | 1 |
| FMB Series S | 6.82% | April 1, 2018 | **15** | - |
| *New England Power Pollution Control Revenue Bonds:* | | | | |
| Massachusetts Development Finance Agency 1 | Variable | March 1, 2018 | - | 79 |
| *Niagara Mohawk State Authority Bonds:* | | | | |
| NMPC 1986 Series A | 3.42% | December 1, 2026 | **5** | - |
| *European Medium Term Note* | Variable | August 20, 2019 - June 15, 2028 | **1,916** | - |
| *Intercompany Notes Payable:* | | | | |
| National Grid North Twenty Five Limited | 2.30% over LIBOR | July 28, 2018 | **616** | - |
| Total | | | **$ 2,573** | $ 318 |

## Issuance of common stock

On June 12, 2017, the Company issued 16 shares of common stock to its direct parent, National Grid (US) Partner 1 Limited for $1.3 billion. The funds were used for general corporate purposes.

## 13. INCOME TAXES

### Components of Income Tax Expense

| | Years Ended March 31, 2019 | 2018 |
|---|---|---|
| | (in millions of dollars) | |
| Current tax expense (benefit): | | |
| Federal | **$ (21)** | $ 26 |
| State | **(27)** | 14 |
| Total current tax expense (benefit) | **(48)** | 40 |
| Deferred tax expense: | | |
| Federal | **185** | 359 |
| State | **63** | 45 |
| Total deferred tax expense | **248** | 404 |
| Amortized investment tax credits [1] | **(2)** | (4) |
| Total deferred tax expense | **246** | 400 |
| Total income tax expense | **$ 198** | $ 440 |

[1] Investment tax credits ("ITC") are accounted for using the deferral and gross up method of accounting and amortized over the depreciable life of the property giving rise to the credits.

**Statutory Rate Reconciliation**

The Company's effective tax rates for the years ended March 31, 2019 and 2018 are 23.0% and 45.5%, respectively. The following table presents a reconciliation of income tax expense at the federal statutory tax rate of 21% and 31.55%, respectively, to the actual tax expense:

| | Years Ended March 31, | |
|---|---|---|
| | **2019** | 2018 |
| | *(in millions of dollars)* | |
| Computed tax | **$ 181** | $ 305 |
| Change in computed taxes resulting from: | | |
| State income tax, net of federal benefit | **29** | 41 |
| Tax rate change | **23** | 128 |
| Other items, net | **(35)** | (34) |
| Total changes | **17** | 135 |
| Total income tax expense | **$ 198** | $ 440 |

The Company files a consolidated federal income tax return and Massachusetts and New York unitary state income tax returns. The Company has joint and several liability for any potential assessments against the consolidated group.

On December 22, 2017, the Tax Act was signed into law. The Tax Act includes significant changes to various federal tax provisions applicable to the Company, including provisions specific to regulated public utilities. The most significant changes include the reduction in the corporate federal income tax rate from 35% to 21% effective January 1, 2018, the elimination of bonus depreciation for certain property acquired or placed in service after September 27, 2017, and extension of the normalization requirements for ratemaking treatment of excess deferred taxes.

On August 3, 2018, the Internal Revenue Service ("IRS") and the U.S. Department of Treasury released proposed regulations associated with the bonus depreciation rules enacted as part of the Tax Act. The proposed regulations would enable utilities to claim additional bonus depreciation on property acquired and placed in service between September 28, 2017 and March 31, 2018. The Company adopted the guidance in the proposed regulations and claimed the additional six months of bonus depreciation on its fiscal year 2018 federal income tax return.

In accordance with ASC 740, "Income Taxes," the effects of changes in tax law are required to be recognized in the period of enactment, which for the Company was the period ended March 31, 2018. Since the Company's fiscal year end is March 31, the statutory rate applicable for the Company's fiscal year ended March 31, 2018 was a blended tax rate of 31.55%. For the fiscal year ended March 31, 2019, and future periods, the federal income tax rate is 21%. In addition, ASC 740 requires deferred income tax assets and liabilities to be measured at the enacted tax rate expected to apply when temporary differences are to be realized or settled. As a result, the Company remeasured its federal deferred income tax assets and liabilities using the newly enacted tax rate of 21%.

On December 22, 2017, the Securities and Exchange Commission issued Staff Accounting Bulletin ("SAB") 118, which provides guidance on accounting for the effects of the Tax Act. SAB 118 provides a measurement period that should not extend beyond one year from the Tax Act enactment date to complete the accounting under ASC 740, "Income Taxes." To the extent that a company's accounting for certain income tax effects of the Tax Act is incomplete, a company can determine a reasonable estimate for those effects and record a provisional estimate in the financial statements. As of March 31, 2019, any and all provisional amounts previously recorded in accordance with SAB 118 have been adjusted to reflect their final amounts.

As of March 31, 2018, the remeasurement amounted to a decrease in net deferred income tax liabilities of $2.1 billion, of which $100 million was recorded to deferred income tax expense and $2.2 billion was recorded as a regulatory liability for the refund of excess ADIT to the ratepayers. During the current period, the Company adjusted the remeasurement of the net

deferred income tax liabilities by $4 million, of which $23 million was recorded to deferred income tax expense and $27 million was recorded as a regulatory liability for excess ADIT. As of March 31, 2019, the regulatory liability for excess ADIT on a pre-tax basis prior to amortization amounted to $3.1 billion ($2.1 billion post-tax).

**Deferred Tax Components**

| | March 31, | |
|---|---|---|
| | **2019** | 2018 |
| | *(in millions of dollars)* | |
| **Deferred tax assets:** | | |
| Environmental remediation costs | **$ 618** | $ 564 |
| Net operating losses | **588** | 585 |
| Postretirement benefits and other employee benefits | **595** | 615 |
| Regulatory liabilities - other | **677** | 559 |
| Regulatory tax liability | **798** | 797 |
| Other items | **497** | 477 |
| Total deferred tax assets | **3,773** | 3,597 |
| **Deferred tax liabilities:** | | |
| Property related differences | **5,379** | 5,030 |
| Regulatory assets - environmental response costs | **601** | 605 |
| Regulatory assets - postretirement benefits | **336** | 372 |
| Regulatory assets - other | **501** | 442 |
| Other items | **320** | 283 |
| Total deferred tax liabilities | **7,137** | 6,732 |
| Net deferred income tax liabilities | **3,364** | 3,135 |
| Deferred investment tax credits | **38** | 32 |
| **Deferred income tax liabilities, net** | **$ 3,402** | $ 3,167 |

**Net Operating Losses**

The amounts and expiration dates of the Company's net operating losses carryforward as of March 31, 2019 are as follows:

| | Carryforward Amount | | Expiration Period |
|---|---|---|---|
| | *(in millions of dollars)* | | |
| **Federal** | $ 3,364 | | 2033-2038 |
| **New York** | 1,742 | [1] | 2035-2039 |
| **New York City** | 356 | [1] | 2035-2039 |
| **Massachusetts** | 57 | | 2035-2039 |

(1) The amount contains net operating losses that were incurred before the tax year ended March 31, 2015 that have been converted into a Prior Net Operating Loss Conversion subtraction that can be utilized beginning fiscal year 2017.

As a result of the accounting for uncertain tax positions, the amount of deferred tax assets reflected in the consolidated financial statements is less than the amount of the tax effect of the federal and state net operating losses carryforward reflected on the income tax returns.

The Company recognizes interest related to unrecognized tax benefits in other interest, including affiliate interest and related penalties, if applicable, in other income (deductions), net, in the accompanying consolidated statements of operations and comprehensive income. As of March 31, 2019 and 2018, the Company has accrued for interest related to unrecognized tax benefits of $72 million and $106 million, respectively. During the years ended March 31, 2019 and 2018, the Company recorded an interest benefit of $2 million and an interest expense of $16 million, respectively. No tax penalties were recognized during the years ended March 31, 2019 or 2018.

It is reasonably possible that other events will occur during the next twelve months that would cause the total amount of unrecognized tax benefits to increase or decrease. However, the Company does not believe any such increases or decreases would be material to its results of operations, financial position, or cash flows.

During the year ended March 31, 2019, the Company reached a settlement with the IRS for the tax years ended August 24, 2007, March 31, 2008, and March 31, 2009. As a result of the settlement, the Company recognized a tax benefit of $16 million through a release of previously established reserves for uncertain tax positions and expects to receive a refund of $162 million for the carryback of net operating losses. The IRS continues its examination of the next audit cycle which includes the income tax returns for the years ended March 31, 2010 through March 31, 2012. The examination is expected to conclude in the next fiscal year and result in a settlement agreement with the IRS. As a result of the settlement, the Company expects to recognize a tax benefit through a release of some of its previously established reserves for uncertain tax positions and does not expect to make a payment to the IRS due to the utilization of net operating losses. The Company, however, expects to make a payment of $30 million for the state tax consequences of the anticipated settlement with the IRS. The income tax returns for the years ended March 31, 2013 through March 31, 2019 remain subject to examination by the IRS.

During the year ended March 31, 2019, the Company reached a settlement with the state of New York in connection with its examination of KeySpan Corporation and Subsidiaries' income tax returns for the years ended December 31, 2003 through March 31, 2009. As a result of the settlement, the Company made a payment of $52 million, but recognized a tax and interest benefit of $17 million and $33 million, respectively, through the release of previously established tax reserves.

The state of New York is in the process of examining the Company's other New York State income tax returns. The following table presents the subsidiaries and years currently under examination. The income tax returns for the subsequent years through March 31, 2019 remain subject to examination by the state of New York.

| Companies | Years Under Examination |
|---|---|
| National Grid Engineering and Survey, Inc. | March 31, 2009 through March 31, 2012 |
| Niagara Mohawk | March 31, 2013 through March 31, 2015 |
| KeySpan Gas East | March 31, 2009 through March 31, 2012 |
| Brooklyn Union | March 31, 2009 through March 31, 2012 |
| Genco | March 31, 2013 through March 31, 2015 |
| KeySpan Energy Corporation | March 31, 2008 through March 31, 2014 |
| National Grid Development Holdings, Inc. | March 31, 2013 through March 31, 2015 |

The city of New York is in the process of examining the Company's New York City income tax returns. The following table presents the subsidiaries and years currently under examination. The income tax returns for the subsequent years through March 31, 2019 remain subject to examination by the city of New York.

| Companies | Years Under Examination |
|---|---|
| KeySpan Corporation and Subsidiaries | December 31, 2003 through March 31, 2009 |
| National Grid Services Inc. | March 31, 2012 through March 31, 2014 |

The state of Massachusetts is in the process of examining the Company's income tax returns for the years ended March 31, 2010 through March 31, 2012. The income tax returns for the years ended March 31, 2013 through March 31, 2019 remain subject to examination by the state of Massachusetts.

The following table indicates the earliest tax year subject to examination for each major jurisdiction:

| Jurisdiction | Tax Year |
|---|---|
| Federal | March 31, 2010 |
| Massachusetts | March 31, 2010 |
| New York | March 31, 2008 |

## 14. ENVIRONMENTAL MATTERS

The normal ongoing operations and historic activities of the Company are subject to various federal, state, and local environmental laws and regulations. Under federal and state Superfund laws, potential liability for the historic contamination of property may be imposed on responsible parties jointly and severally, without regard to fault, even if the activities were lawful when they occurred.

### Air

Genco’s generating facilities are subject to increasingly stringent emissions limitations under current and anticipated future requirements of the United States Environmental Protection Agency (“EPA”) and the NYS Department of Environmental Conservation (“DEC”). In addition to efforts to improve both ozone and particulate matter air quality, there has been an increased focus on greenhouse gas emissions in recent years. Genco’s previous investments in low NOx boiler combustion modifications, the use of natural gas firing systems at its steam electric generating stations, and the compliance flexibility available under cap and trade programs have enabled Genco to achieve its prior emission reductions in a cost-effective manner. These investments include the installation of enhanced NOx controls and efficiency improvement projects at certain of Genco’s Long Island based electric generating facilities. The total cost of these improvements was approximately $106 million, all of which have been placed in service as of the date of this report; a mechanism for recovery from LIPA of these investments has been established. Genco will continue to make investments for additional emissions reductions, as needed. Genco has developed a compliance strategy to address anticipated future requirements and is closely monitoring the regulatory developments to identify any necessary changes to its compliance strategy. At this time, Genco is unable to predict what effect, if any, these future requirements will have on its consolidated financial position, results of operations, and cash flows.

### Water

Additional capital expenditures associated with the renewal of the surface water discharge permits for Genco’s steam electric power plants have been required by the DEC pursuant to Section 316 of the Clean Water Act to mitigate the plants’ alleged cooling water system impacts to aquatic organisms. Final permits have been issued for Port Jefferson and Northport. Capital improvements have been completed at Port Jefferson and are in the design, procurement, and construction phase for Northport. The Company continues to engage in discussions with the DEC regarding the nature of capital upgrades or other mitigation measures necessary to reduce any impacts at E.F. Barrett. Total capital costs for these improvements at Northport and E.F. Barrett are estimated to be approximately $76 million. Costs associated with these capital improvements are reimbursable from LIPA under the PSA.

### Land, Manufactured Gas Plants and Related Facilities

Federal and state environmental regulators, as well as private parties, have alleged that several of the Company’s subsidiaries are potentially responsible parties under Superfund laws for the remediation of numerous contaminated sites in New York and New England. The Company’s greatest potential Superfund liabilities relate to MGP facilities formerly owned or operated

by its subsidiaries or their predecessors. MGP byproducts included fuel oils, hydrocarbons, coal tar, purifier waste, and other waste products which may pose a risk to human health and the environment.

Since July 12, 2006, several lawsuits have been filed which allege damages resulting from contamination associated with the historic operations of a former MGP located in Bay Shore, New York. The Company has been conducting remediation at this location pursuant to Administrative Order on Consent with the DEC. The Company intends to contest these proceedings vigorously.

At both March 31, 2019 and 2018, the Company's total reserve for estimated MGP-related environmental matters is $2.0 billion. The Company had a current portion of environmental remediation costs of $128 million and $108 million included in other current liabilities on the consolidated balance sheets at March 31, 2019 and 2018, respectively. Management believes that obligations imposed on the Company because of the environmental laws will not have a material adverse effect on its operations, financial position, or cash flows. Through various rate orders issued by the NYPSC, DPU, and RIPUC, costs related to MGP environmental cleanup activities are recovered in rates charged to gas distribution customers. Accordingly, the Company has reflected a net regulatory asset of $2.1 billion on the consolidated balance sheets at both March 31, 2019 and 2018. Expenditures incurred for the years ended March 31, 2019 and 2018 were approximately $50 million and $80 million, respectively. The Company is pursuing claims against other potentially responsible parties to recover investigation and remediation costs it believes are the obligations of those parties. The Company cannot predict the likelihood of success of such claims.

The Company believes that its ongoing operations, and its approach to addressing conditions at historic sites, are in substantial compliance with all applicable environmental laws, and that the obligations imposed on it because of the environmental laws will not have a material impact on its results of operations or financial position since, as noted above, environmental expenditures incurred by the Company are generally recoverable from customers.

## 15. COMMITMENTS AND CONTINGENCIES

### Operating Lease Obligations

The Company has various operating leases for buildings, office equipment, vehicles, and power operating equipment utilized by both the Company and its subsidiaries. Total rental expense for operating leases included in operations and maintenance expense in the accompanying consolidated statements of operations and comprehensive income was $89 million and $96 million for the years ended March 31, 2019 and 2018, respectively.

The future minimum lease payments for the years subsequent to March 31, 2019 are as follows:

| *(in millions of dollars)*<br>Years Ending March 31, | | |
|---|---|---|
| 2020 | $ | 133 |
| 2021 | | 120 |
| 2022 | | 103 |
| 2023 | | 88 |
| 2024 | | 70 |
| Thereafter | | 191 |
| Total | $ | 705 |

### Purchase Commitments

The Company's electric subsidiaries have several long-term contracts for the purchase of electric power. Substantially all of these contracts require power to be delivered before the subsidiaries are obligated to make payment. Additionally, the Company's gas distribution subsidiaries have entered into various contracts for gas delivery, storage, and supply services. Certain of these contracts require payment of annual demand charges, which are recoverable from customers. The

Company's gas distribution subsidiaries are liable for these payments regardless of the level of service required from third-parties.

The Company's commitments under these long-term contracts for the years subsequent to March 31, 2019 are summarized in the table below:

| *(in millions of dollars)*<br>Years Ending March 31, | | Energy Purchases |
|---|---|---|
| 2020 | $ | 1,636 |
| 2021 | | 999 |
| 2022 | | 789 |
| 2023 | | 687 |
| 2024 | | 562 |
| Thereafter | | 2,573 |
| Total | $ | 7,246 |

The Company's subsidiaries can purchase additional energy to meet load requirements from independent power producers, other utilities, energy merchants or on the open market through the New York Independent System Operator or the ISO-NE at market prices.

**Financial Guarantees**

The Company has guaranteed the principal and interest payments on certain outstanding debt of its subsidiaries. Additionally, the Company has issued financial guarantees in the normal course of business, on behalf of its subsidiaries, to various third-party creditors. At March 31, 2019, the following amounts would have to be paid by the Company in the event of non-payment by the primary obligor at the time payment is due:

| Guarantees for Subsidiaries: | | | Amount of Exposure<br>*(in millions of dollars)* | Expiration Dates |
|---|---|---|---|---|
| KeySpan Ravenswood LLC Lease | (i) | $ | 226 | May 2040 |
| Reservoir Woods | (ii) | | 142 | October 2029 |
| Surety Bonds | (iii) | | 187 | Revolving |
| Commodity Guarantees and Other | (iv) | | 122 | August 2025 - August 2042 |
| Letters of Credit | (v) | | 305 | September 2019 - December 2021 |
| NY Transco Parent Guaranty | (vi) | | 842 | None |
| National Grid Algonqin LLC | (vii) | | 100 | December 2021 |
| EDF Renewable Development, Inc. | (viii) | | 13 | None |
| Sunrun | (ix) | | 5 | None |
| | | $ | 1,942 | |

The following is a description of the Company's outstanding subsidiary guarantees:

(i) The Company had guaranteed all payment and performance obligations of a former subsidiary (KeySpan Ravenswood LLC) associated with a merchant electric generating facility leased by that subsidiary under a sale/leaseback arrangement. The subsidiary and the facility were sold in 2008. However, the original lease remains in place and the Company will continue to make the required payments under the lease through 2040.

The cash consideration from the buyer of the facility included the remaining lease payments on a net present value basis. At March 31, 2019, the Company's obligation related to the lease was $26 million and is reflected in other non-current liabilities on the consolidated balance sheets.

(ii) The Company has fully and unconditionally guaranteed $142 million in lease payments through 2029 related to the lease of office facilities by its service company at Reservoir Woods in Waltham, Massachusetts.

(iii) The Company has agreed to indemnify the issuers of various surety bonds associated with various construction requirements or projects of its subsidiaries. In the event that the Company or its subsidiaries fail to perform their obligations under contracts, the injured party may demand that the surety make payments or provide services under the bond. The Company would then be obligated to reimburse the surety for any expenses or cash outlays it incurs.

(iv) The Company has guaranteed commodity-related and operational payments for certain subsidiaries. These guarantees are provided to third-parties to facilitate physical and financial transactions supporting the purchase and transportation of natural gas, oil, and other petroleum products for gas and electric production and financing activities. The guarantees cover actual transactions by these subsidiaries that are still outstanding as of March 31, 2019.

(v) The Company has arranged for stand-by letters of credit to be issued to third-parties that have extended credit to certain subsidiaries. Certain vendors require the posting of letters of credit to guarantee subsidiary performance under the Company's contracts and to ensure payment to the Company's subsidiary subcontractors and vendors under those contracts. Certain of the Company's vendors also require letters of credit to ensure reimbursement for amounts they are disbursing on behalf of the Company's subsidiaries, such as to beneficiaries under the Company's self-funded insurance programs. Such letters of credit are generally issued by a bank or similar financial institution. The letters of credit commit the issuer to pay specified amounts to the holder of the letter of credit if the holder demonstrates that the Company has failed to perform specified actions. If this were to occur, the Company would be required to reimburse the issuer of the letter of credit.

(vi) The Company has entered into a Parent Guaranty (the "Guaranty") dated November 14, 2014 for the benefit of NY Transco LLC, which Guaranty irrevocably and unconditionally guarantees all of Grid NY LLC's payment obligations under the New York Transco Limited Liability Company Agreement ("NY Transco LLC Agreement") dated November 14, 2014 entered into by and among Consolidated Edison Transmission, LLC, Grid NY LLC, Iberdrola USA Networks, NY Transco, LLC and Central Hudson Electric Transmission LLC. Grid NY LLC's payment obligations relate to, but are not limited to, funding project development of the initial projects, obtaining initial regulatory approvals and making capital contributions as set forth in the NY Transco LLC Agreement.

(vii) In connection with NGUSA's investment in the Access Northeast natural gas pipeline project, the Company has entered into a guarantee of the required capital contributions of NGA, an indirect wholly-owned subsidiary of the Company. The guarantee agreement, which is dated September 14, 2015, commits the Company to serve as a guarantor for up to $100 million of the capital contributions of NGA from the time of the effective date of the guarantee agreement through the earlier of (i) December 31, 2021, or (ii) the time at which NGA's capital commitments have been fully discharged. As of March 31, 2019, the Company has made $15 million of capital contributions to NGA.

(viii) The Company has entered into a Parent Guaranty dated February 23, 2017 under which the Company unconditionally and irrevocably guarantees to EDF Renewable Development, Inc., the timely payment of the purchase price related to the acquisition of the development rights for a 400 MW hydropower storage plant in accordance with and subject to the conditions and limitations set forth in the Purchase and Sale Agreement. The Company's aggregate liability with respect to such guaranteed obligations shall not exceed the purchase price which totals $13 million and is payable on certain milestones being achieved.

(ix) The Company entered into a guaranty as of December 22, 2016 in favor of Sunrun, unconditionally and irrevocably guaranteeing the timely payment when due of all of the Company's payment obligations to make "Capital Contributions" (as such term is defined in the LLC Agreement). The Company's aggregate liability with respect to such Guaranteed Obligations shall not exceed the Class A Capital Contribution Commitment (remaining commitment as of March 31, 2019 is $5 million).

As of the date of this report, the Company has not had a claim made against it for any of the above guarantees and has no reason to believe that the Company's subsidiaries or former subsidiaries will default on their current obligations. However, the Company cannot predict when, or if, any defaults may take place or the impact any such defaults may have on its consolidated results of operations, financial position, or cash flows.

**Long-term Contracts for Renewable Energy**

*Offshore Wind Energy Procurement*

On December 6, 2018, Narragansett entered into a 20-year PPA with DWW Rev I, LLC ("Revolution Wind"), for the purchase of the electricity and renewable energy credits generated by the offshore windfarm proposed by Revolution Wind, that will have a capacity of up to 408 MW. The anticipated commercial operations date for the windfarm is in January 2024. On May 28, 2019, at an open meeting, the RIPUC approved the contract without remuneration. The written order approving the agreement and that Narragansett will be able to recover the cost incurred under the agreement was issued by the RIPUC on June 7, 2019.

On July 31, 2018, the Massachusetts Electric Companies entered into two separate 20-year PPAs with Vineyard Wind LLC ("Vineyard Wind") for the purchase of 46.16% of the electricity and renewable energy credits generated by two offshore windfarms proposed by Vineyard Wind, with each individual windfarm having a capacity of up to 400 MW. The contracts with Vineyard Wind were entered into pursuant to Section 83C of the Green Communities Act. The anticipated commercial operations date for the first wind farm is in January 2022 with the second wind farm anticipated in January 2023, based on the terms of the contracts. On April 12, 2019 the DPU approved the contracts and the Massachusetts Electric Companies will be able to recover the costs incurred under the agreements.

*Clean Energy Procurement*

On June 13, 2018, the Massachusetts Electric Companies entered into two separate agreements for the transportation and purchase of electricity and the related environmental attributes from hydroelectric facilities located in the Canadian Province of Québec. The two agreements were entered into pursuant to Section 83D of the Green Communities Act. The first agreement is a 20-year PPA with H.Q. Energy Services Inc., ("H.Q. Energy"). for the purchase of approximately 498 mwhs of electricity, and related environmental attributes from a portfolio of hydroelectric facilities owned and operated by affiliates of H.Q Energy. The second agreement is a 20-year transmission service agreement ("TSA") with Central Maine Power Company ("CMP"). The TSA agreement provides for the transmission of the electricity supplied by H.Q. Energy, on a proposed new transmission line, that will run from the U.S. border to Lewiston Maine, where it will interconnect with ISO-NE. Both the TSA with CMP and the PPA with H.Q. Energy are contingent on the successful development and construction of the underlying transmission line by CMP. The anticipated commercial operations date of the transmission line is in December 2022, based on the contractual terms. The Section 83D contracts were approved by the DPU on June 25, 2019, and the Massachusetts Electric Companies will be able to recover the costs incurred under the agreements.

*Annual Solicitations*

The 2009 Rhode Island law also requires that, beginning on July 1, 2010, Narragansett conduct four annual solicitations for proposals from renewable energy developers and, provided commercially reasonable proposals have been received, enter into long-term contracts for the purchase of capacity, energy, and attributes from newly developed renewable energy resources. Narragansett's four solicitations have resulted in four PPAs that have been approved by the RIPUC:

- First Solicitation: On July 28, 2011, the RIPUC approved a 15-year PPA with Orbit Energy Rhode Island, LLC for a 3.2 MW anaerobic digester biogas project.
- Second Solicitation: On May 11, 2012, the RIPUC approved a 15-year PPA with Black Bear Development Holdings, LLC for a 3.9 MW run-of-river hydroelectric plant located in Orono, Maine. The facility reached commercial operation on November 22, 2013.
- Third Solicitation: On October 25, 2013, the RIPUC approved a 15-year PPA with Champlain Wind, LLC for a 48 MW land-based wind project located in Carroll Plantation and Kossuth Township, Maine. The PPA was terminated on January 23, 2017 because one of the required permits for the project was rejected. The impact of this termination is that Narragansett will need to backfill the MW capacity from that project to meet the 90 MW minimum long-term capacity requirements under the state statute.
- Fourth Solicitation: On October 29, 2015, the RIPUC approved a 15-year PPA with Copenhagen Wind Farm, LLC for an 80 MW land-based wind project located in Denmark, New York.

As approved by the RIPUC, Narragansett is allowed to pass through commodity-related / purchased power costs to customers. The cost of these contracts is accounted for as part of these costs.

*Aquidneck Island*

On January 21, 2019, Narragansett suspended gas service to approximately 7,100 gas customers on Aquidneck Island due to a gas transmission supply issue. The recovery effort took approximately nine days, with service restored to essentially all customers by January 30, 2019. On February 28, 2019, the RIPUC opened an investigation into the causes of the outage, in order to comport with the U.S. Senate's request to do so per Senate Resolution 188 passed on January 31, 2019. On June 4, 2019, the RIPUC issued a "Status Report on the Aquidneck Island Loss of Gas Investigation." In the report, the RIPUC noted that there may have been multiple contributing factors leading to the outage, and that a final report would be released before the upcoming heating season. The RIPUC also noted that following the release of the report, if it is found that Narragansett contributed to the incident through imprudent management decisions, a subsequent regulatory process would be initiated, through which fines or disallowed costs could be assessed. At this time, Narragansett is unable to predict or estimate any impact to earnings.

**Legal Matters**

The Company is subject to various legal proceedings arising out of the ordinary course of its business. During the year ended March 31, 2019, the Company recognized a benefit of $130 million, within operations and maintenance in the accompanying consolidated statements of operations and comprehensive income, related to legal settlements to recover costs associated with a U.S. systems implementation. Otherwise, the Company does not consider any of such proceedings to be material, individually or in the aggregate, to its business or likely to result in a material adverse effect on its results of operations, financial position, or cash flows.

*Colonial Gas Consent Solicitation*

On March 13, 2019, Colonial Gas commenced a consent solicitation, proposing certain amendments and modifications to its Second Amended and Restated First Mortgage Indenture dated as of June 15, 1992 as amended (the "Indenture"), relating to its issued and outstanding first mortgage bonds under the Indenture (the "Bonds"). Colonial Gas has received consent from the holders of the Bonds with respect to certain amendments to the Indenture ("Consent Solicitation"). The purposes of the amendments are to, among other things, (i) limit the assets covered by the lien of the Indenture to the legacy assets of Boston Gas prior to the intended legal merger of Colonial Gas and Boston Gas (the "Merger"), and any repairs, renewals, or replacements to such assets, (ii) limit certain other covenants in the Indenture to this same scope of assets, (iii) revise certain financial covenants therein, and (iv) add a governing law provision to the Indenture.

Boston Gas has requested authorization from the DPU to complete the Merger. If the proposed Merger is approved by the DPU, it is expected that Colonial Gas will merge with and into Boston Gas, and Boston Gas will be the surviving entity in accordance with Massachusetts law. As a result of the Merger, and by operation of the law, the facilities, properties and other

rights, assets, franchises, and liabilities of both companies will vest in Boston Gas as the successor by merger to Colonial Gas. Colonial Gas will cease to exist, and Boston Gas will be the sole surviving corporate entity. Provided the DPU approves the proposed Merger, no additional consents from the holders of the Bonds will be required to progress the Merger.

*FERC ROE Complaints*

Four separate complaints have been filed at the FERC by combinations of New England state attorneys general, state regulatory commissions, consumer advocates, consumer groups, municipal parties and other parties (collectively the "Complainants"). In each of the first three complaints, filed on October 1, 2011, December 27, 2012, and July 31, 2014, respectively, the Complainants challenged the NETO base ROE of 11.14% that had been utilized since 2005 and sought an order to reduce it prospectively from the date of the final FERC order and for the separate 15-month complaint periods. In the fourth complaint, filed April 29, 2016, the Complainants challenged the NETOs' base ROE of 10.57% and the maximum ROE for transmission incentive ("incentive cap") of 11.74%, asserting that these ROEs were unjust and unreasonable. NEP recorded a liability of $30 million included in other current liabilities on the consolidated balance sheets as of March 31, 2019 for the potential refund as a result of reduction of the base ROE.

In response to appeals of the FERC decision in the first complaint filed by the NETOs and the Complainants, the U.S. Court of Appeals for the D.C. Circuit issued a decision on April 14, 2017 vacating and remanding the FERC's decision. On October 16, 2018, the FERC issued an order on all four complaints describing how it intends to address the issues that were remanded by the U.S. Court of Appeals. The FERC proposed a new framework to determine whether an existing ROE is unjust and unreasonable and, if so, how to calculate a replacement ROE. The FERC stated that these calculations are merely preliminary. The potential financial impacts to NEP are unknown until the FERC issues a final order on the briefs and all appeals are resolved and does not provide a reasonable basis to change NEP's reserve.

*FERC 206 Proceeding on Rate Transparency*

On December 28, 2015, the FERC initiated a proceeding under Section 206 of the FPA. The FERC found that the ISO-NE Transmission, Markets, and Services Tariff is unjust, unreasonable, and unduly discriminatory or preferential. The FERC found that the ISO-NE's Tariff lacks adequate transparency and challenge procedures with regard to the formula rates for ISO-NE Participating Transmission Owners ("PTOs"). In addition, the FERC found that the ISO-NE PTOs', including NEP's, current RNS and LNS formula rates appear to be unjust, unreasonable, unduly discriminatory or preferential, or otherwise unlawful. The FERC explained that the formula rates appear to lack sufficient detail in order to determine how certain costs are derived and recovered in the formula rates. Accordingly, the FERC established hearing and settlement judge procedures to develop just and reasonable formula rate protocols to be included in the ISO-NE Tariff and to examine the justness and reasonableness of the RNS and LNS rates. On August 17, 2018, the parties filed a settlement package with a FERC judge that is close to revenue neutral. A small group of municipals and FERC Trial Staff submitted comments opposing the filed settlement. The settling parties filed an answer to the opposition in late September asking the FERC to approve the settlement as is, despite the protests. On May 22, 2019, the FERC rejected the Formula Rate 206 settlement in its entirely. Accordingly, the FERC remanded the matter to the Chief Administrative Law Judge ("ALJ") for hearing procedures. The Chief ALJ established Track III procedural time standards for this hearing, which require that the hearing be convened within 42 weeks and the initial decision issued within 63 weeks. On July 29, 2019, the Chief ALJ issued an order extending the Track III procedural time standards by 45 days and suspending discovery in order to allow the parties to focus on settlement. The Chief ALJ also designated a dispute resolution specialist to serve as settlement facilitator in the proceeding but any settlement discussions will have to proceed in parallel with hearing procedures. At this time, NEP is unable to predict whether and, if so, to what extent, there will be any impact to earnings as a result of the proceeding.

**Electric Services and LIPA Agreements**

On December 15, 2011, LIPA announced that it was not renewing the Management Service Agreement beyond its expiration on December 31, 2013. As of March 23, 2018 the parties have entered an agreement for the resolution of any outstanding matters under the MSA. Activity in the years ended March 31, 2019 and 2018 primarily relates to charges of certain contingencies, net of income taxes.

Effective May 28, 2013 (and most recently amended on April 1, 2018), Genco provides services to LIPA under an A&R PSA. Under the A&R PSA, Genco has a ROE of 9.75% and a capital structure of 50% debt and 50% equity. Genco's annual revenue requirement for the year ended March 31, 2019 was $458 million. The A&R PSA has a term of fifteen years, provided LIPA has the option to terminate the agreement as early as April 2025 on two years advance notice. Genco accounts for the A&R PSA as an operating lease under ASC 840.

The A&R PSA provides potential penalties to Genco if it does not maintain the output capability of the generating facilities, as measured by annual industry-standard tests of operating capability, plant availability, and efficiency. These penalties could total $4 million annually. Although the A&R PSA provides LIPA with all of the capacity from the generating facilities, LIPA has no obligation to purchase energy from the generating facilities and can purchase energy on a least-cost basis from all available sources consistent with existing transmission interconnection limitations of the transmission and distribution system. Genco must, therefore, operate its generating facilities in a manner such that Genco can remain competitive with other producers of energy. To date, Genco has dispatched to LIPA and LIPA has accepted the level of energy generated at the agreed to price per megawatt hour. Under the terms of the A&R PSA, LIPA is obligated to pay for capacity at rates that reflect recovery of an agreed level of the overall cost of maintaining and operating the generating facilities, including recovery of depreciation and return on its investment in plant. The capacity charge is approximately 95% of the annual revenue requirement and is adjusted each year using cost escalation and inflation factors applied to the prior year's capacity charge. A monthly variable maintenance charge is billed for each unit of energy actually acquired from the generating facilities. The billings to LIPA under the A&R PSA do not include a provision for fuel costs, as such fuel is owned by LIPA.

**Decommissioning Nuclear Units**

As of March 31, 2019 and 2018, Niagara Mohawk had a liability of $174 million and $170 million, respectively, recorded in other non-current liabilities on the consolidated balance sheets, for the disposal of nuclear fuel irradiated prior to 1983. The Nuclear Waste Policy Act of 1982 provides three payment options for liquidating such liability and Niagara Mohawk has elected to delay payment, with interest, until the year in which Constellation Energy Group Inc., which purchased Niagara Mohawk's nuclear assets, initially plans to ship irradiated fuel to an approved DOE disposal facility.

The 2010 Federal budget (which became effective October 1, 2009) eliminated almost all funding for the creation of the Yucca Mountain repository. A Blue Ribbon Commission ("BRC") on America's Nuclear Future, appointed by the U.S. Energy Secretary, released a report on January 26, 2012, detailing comprehensive recommendations for creating a safe, long-term solution for managing and disposing of the nation's spent nuclear fuel and high-level radioactive waste.

Despite insufficient funding and actions of the DOE to block its construction, the U.S. Court of Appeals for the D.C. Circuit directed the Nuclear Regulatory Commission ("NRC") to resume the Yucca Mountain licensing process. On November 18, 2013, the NRC ordered its staff to resume work on its Yucca Mountain safety report but scarce funding has precluded progress in the licensing process. On January 26, 2012 the BRC, which was charged with advising the DOE regarding alternatives to disposal at Yucca Mountain, issued a final report recommending that priority be given to removal of spent fuel from shutdown reactor sites. Private entities have initiated proposals, and submitted license applications to the NRC, to site consolidated interim storage facilities at two locations in the southwestern United States. It is impossible to predict when the DOE will fulfill its obligation to take possession of the Yankees' spent fuel. The decommissioning costs that are actually incurred by the Yankees may substantially exceed the estimated amounts.

**Other Contingencies**

At March 31, 2019 and 2018, the Company had accrued workers compensation, auto, and general insurance claims which have been incurred but not yet reported ("IBNR") of $82 million and $78 million, respectively. IBNR reserves have been established for claims and/or events that have transpired, but have not yet been reported to the Company for payment.

## 16. RELATED PARTY TRANSACTIONS

### Accounts Payable to Affiliates

The Company engages in various transactions with the Parent and its subsidiaries. Certain activities and costs, primarily executive and administrative and some human resources, legal, and strategic planning, are shared between the Company and its affiliates.

The Company records short-term receivables from, and payables to, certain of its affiliates in the ordinary course of business. A summary of outstanding accounts payable to affiliates is as follows:

| | March 31, | |
|---|---|---|
| | **2019** | 2018 |
| | *(in millions of dollars)* | |
| National Grid plc | **$ 25** | $ 23 |
| National Grid Holdings One plc | **8** | 9 |
| Other | **2** | 4 |
| Total | **$ 35** | $ 36 |

### Holding Company Charges

The Company received charges from National Grid Commercial Holdings Limited (an affiliated company in the United Kingdom) for certain corporate and administrative services provided by the corporate functions of the Parent to its U.S. subsidiaries. For the years ended March 31, 2019 and 2018, the effect on income before income taxes was $48 million.

## 17. PREFERRED STOCK

### Preferred stock of NGNA subsidiaries

The Company's subsidiaries have certain issues of non-participating preferred stock, some of which provide for redemption at the option of the Company. A summary of the preferred stock of NGNA subsidiaries at March 31, 2019 and 2018 is as follows:

| | | Shares Outstanding | | Amount | | |
|---|---|---|---|---|---|---|
| | | March 31, | | March 31, | | Call |
| Series | Company | **2019** | 2018 | **2019** | 2018 | **Price** |
| | | *(in millions of dollars, except per share and number of shares data)* | | | | |
| $100 par value - | | | | | | |
| 3.40% Series | Niagara Mohawk | **57,524** | 57,524 | **$ 6** | $ 6 | $ 103.500 |
| 3.60% Series | Niagara Mohawk | **137,152** | 137,152 | **14** | 14 | 104.850 |
| 3.90% Series | Niagara Mohawk | **95,171** | 95,171 | **9** | 9 | 106.000 |
| 4.44% Series | Massachusetts Electric | **22,585** | 22,585 | **2** | 2 | 104.068 |
| 6.00% Series | NEP | **11,117** | 11,117 | **1** | 1 | Non-callable |
| $50 par value - | | | | | | |
| 4.50% Series | Narragansett | **49,089** | 49,089 | **3** | 3 | 55.000 |
| Golden Shares - | | | | | | |
| | Niagara Mohawk and the New York Gas Companies | **3** | 3 | **-** | - | Non-callable |
| Total | | **372,641** | 372,641 | **$ 35** | $ 35 | |

In connection with the acquisition of KeySpan by NGUSA, each of the Company's New York subsidiaries became subject to a requirement to issue a class of preferred stock, having one share (the "Golden Share"), subordinate to any existing preferred

stock. The holder of the Golden Share would have voting rights that limit the Company's right to commence any voluntary bankruptcy, liquidation, receivership, or similar proceeding without the consent of the holder of the Golden Share. The NYPSC subsequently authorized the issuance of the Golden Share to a trustee, GSS Holdings, Inc. ("GSS"), who will hold the Golden Share subject to a Services and Indemnity Agreement requiring GSS to vote the Golden Share in the best interests of NYS. On July 8, 2011, the Company issued a total of 3 Golden Shares pertaining to Niagara Mohawk and the New York Gas Companies each with a par value of $1.

## 18. STOCK-BASED COMPENSATION

The Parent's Remuneration Committee determines remuneration policy and practices with the aim of attracting, motivating and retaining high caliber Executive Directors and other senior employees to deliver value for shareholders, high levels of customer service, and safety and reliability in an efficient and responsible manner. As such, the Remuneration Committee has established a Long-Term Performance Plan ("LTPP") which aims to drive long-term performance, aligning Executive Director incentives to shareholder interests. The LTPP replaces the previous Performance Share Plan which operated for awards between 2003 and 2010 inclusive. Both plans issue performance based restricted stock units which are granted in the Parent's common stock traded on the London Stock Exchange for U.K.-based directors and employees or the Parent's American Depository Receipts traded on the New York Stock Exchange for U.S.-based directors and employees. Both plans have a performance period of three years and have been approved by the Parent's Remuneration Committee.

As of March 31, 2019, the Parent had 3.7 billion of ordinary shares issued with 275,597,944 held as treasury shares. The aggregate dilution resulting from executive share-based incentives will not exceed 5% in any ten-year period for executive share-based incentives and will not exceed 10% in any ten-year period for all employee incentives. This is reviewed by the Remuneration Committee and, currently, the Parent has headroom of 3.91% and 7.83%, respectively.

The number of units within each award is subject to change depending upon the Parent's ability to meet the stated performance targets. Under the LTPP, performance conditions are split into two parts as follows: (1) 50% of the award is subject to average annual Value Growth over a period of three years and (2) 50% of the award is subject to average annual Parent ROE over a period of three years. Units under the plan generally vest at the end of the performance period.

The following table summarizes the stock-based compensation awards recognized by the Company for the years ended March 31, 2019 and 2018:

| | Units | Weighted Average Grant Date Fair Value |
|---|---|---|
| **Non-vested as of March 31, 2017** | 1,070,441 | $ 65.22 |
| Vested | 193,642 | 57.48 |
| Granted | 551,542 | 58.37 |
| Forfeited/Cancelled | 328,381 | 56.75 |
| **Non-vested as of March 31, 2018** | 1,099,960 | 57.72 |
| Vested | 442,966 | 50.67 |
| Granted | 622,375 | 54.04 |
| Forfeited/Cancelled | 2,091 | 52.71 |
| **Non-vested as of March 31, 2019** | 1,277,278 | $ 57.27 |

The total expense recognized for non-vested awards was $19 million and $17 million for the years ended March 31, 2019 and 2018, respectively, and non-vested awards vest over three years. The total tax benefit recorded was approximately $5 million and $6 million as of March 31, 2019 and 2018. Total expense expected to be recognized by the Parent in future periods for non-vested awards outstanding as of March 31, 2019 is $15 million, $13 million, and $3 million for the years ended March 31, 2020, 2021, and 2022, respectively.

## 19. SUBSEQUENT EVENTS

In March 2019, National Grid Ventures entered into an agreement to acquire 100% of Geronimo Energy, a clean energy developer based in Minneapolis in the U.S. for $100 million ($67 million paid upon closing with $33 million subject to holdback provisions) with potential further payments of up to $100 million subject to successful development of the project pipeline. Completion of the acquisition was dependent on the execution of a joint venture agreement with Washington State Investment Board and regulatory approvals being obtained. The acquisition was completed July 15, 2019, upon having satisfied all regulatory requirements and closing conditions.

In July 2019, Boston Gas issued $500 million of unsecured long-term debt at 3.00% with a maturity date of August 1, 2029.

On August 16, 2019, the Company received an equity contribution of $2.5 billion from the Parent, which is intended to be used to fund maturing commercial paper and operating company needs.