Nantucket Electric Company

Financial Statements

For the year ended March 31, 2010

Nantucket Electric Company

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PRICEWATERHOUSECOOPERS

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Report of Independent Auditors

To the Stockholder and Board of Directors of
Nantucket Electric Company:

In our opinion, the accompanying balance sheets and related statements of income, of comprehensive income, of retained earnings, of capitalization and of cash flows present fairly, in all material respects, the financial position of Nantucket Electric Company (the "Company") at March 31, 2010 and 2009, and the results of their operations and their cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits. We conducted our audits of these statements 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 financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

Nantucket Electric Company engages in significant transactions with Massachusetts Electric Company.

PricewaterhouseCoopers LLP

July 29, 2010

Nantucket Electric Company

BALANCE SHEETS

(in thousands of dollars)		**March 31, 2010**		March 31, 2009
ASSETS				
Current assets:				
Cash and cash equivalents	**$**	**74**	$	41
Restricted cash		**55**		55
Accounts receivable:				
Customers		**5,129**		4,604
Money pool		**2,875**		1,175
Affiliates, net		**3,110**		124
Allowance for uncollectible customer accounts		**(91)**		(82)
Unbilled revenues		**874**		1,504
Materials and supplies, at average cost		**161**		161
Deferred federal and state income taxes		**2,768**		2,639
Prepaid and other current assets		**5,590**		194
Total current assets		**20,545**		10,415
Other investments		**672**		531
Property, plant and equipment				
Property, plant and equipment, at original cost		**103,776**		102,057
Less accumulated depreciation		**(32,080)**		(29,098)
Net property, plant and equipment		**71,696**		72,959
Deferred charges:				
Regulatory assets		**7,357**		5,786
Goodwill		**15,706**		15,706
Deferred charges and other assets		**1,405**		1,185
Total deferred charges		**24,468**		22,677
Total assets	**$**	**117,381**	$	106,582

The accompanying notes are an integral part of these financial statements

Nantucket Electric Company

BALANCE SHEETS

(in thousands of dollars)	**March 31, 2010**	March 31, 2009
LIABILITIES AND CAPITALIZATION		
Current liabilities:		
Long-term debt due within one year	**$ 230**	$ 210
Accounts payable:		
Non-affiliates	**1,070**	1,501
Accrued interest and taxes	**101**	642
Other accrued expenses	**11,599**	10,905
Customer deposits	**53**	80
Total current liabilities	**13,053**	13,338
Deferred credits and other liabilities:		
Regulatory liabilities:		
Cost of removal	**1,315**	1,248
Regulatory liabilities	**733**	747
Deferred federal and state income taxes	**11,499**	5,677
Accrued pension and other postretirement benefits	**3,166**	3,368
Other reserves and deferred credits	**2,583**	68
Total deferred credits and other liabilities	**19,296**	11,108
Capitalization:		
Common stock, par value $1 per share, authorized 1,200 shares and 1 share outstanding	**-**	-
Additional paid-in capital	**22,475**	22,475
Retained earnings	**9,802**	8,186
Accumulated other comprehensive losses	**(24)**	(1,527)
Total common stockholders' equity	**32,253**	29,134
Long-term debt	**52,779**	53,002
Total capitalization	**85,032**	82,136
Total liabilities and capitalization	**$ 117,381**	$ 106,582

The accompanying notes are an integral part of these financial statements

Nantucket Electric Company

STATEMENTS OF INCOME

(in thousands of dollars)	For the Years Ended March 31, 2010	2009
Operating revenue	**$ 24,997**	$ 27,904
Operating expenses:		
Purchased electric energy:		
Non-affiliates	**11,348**	15,989
Contract termination charges from affiliate	**106**	277
Other operations and maintenance	**5,498**	4,134
Depreciation	**3,647**	3,621
Taxes, other than income taxes	**524**	565
Total operating expenses	**21,123**	24,586
Operating income	**3,874**	3,318
Other income (deductions):		
Interest on long-term debt	**(811)**	(969)
Other interest	**(175)**	(262)
Other income, net	**124**	250
Total other deductions	**(862)**	(981)
Income taxes expenses (benefits):		
Current income tax expense (benefit)	**(3,326)**	58
Deferred income tax expense and investment tax credit, net	**4,722**	830
Total income taxes	**1,396**	888
Net income	**$ 1,616**	$ 1,449

The accompanying notes are an integral part of these financial statements

Nantucket Electric Company

STATEMENTS OF COMPREHENSIVE INCOME

	For the Years Ended March 31,	
(n thousands of dollars)	**2010**	2009
Net income	**$ 1,616**	$ 1,449
Other comprehensive income (loss), net of taxes:		
Unrealized gains (losses) on securities	**67**	(43)
Change in pension and other postretirement obligations	**765**	(693)
Reclassification adjustment for (losses) gains included in net income	**(10)**	2
Total other comprehensive income (losses)	**822**	(734)
Comprehensive income	**$ 2,438**	$ 715
Related tax (expense) benefit:		
Unrealized (loss) gain on securities	**$ (45)**	$ 27
Change in pension and other postretirement obligations	**(510)**	448
Reclassification adjustment for gains (losses) included in net income	**7**	(1)
Total tax (expense) benefit	**$ (548)**	$ 474

STATEMENTS OF RETAINING EARNINGS

	For the Years Ended March 31,	
(in thousands of dollars)	**2010**	2009
Retained earnings at beginning of year	**$ 8,186**	$ 6,737
Net income	**1,616**	1,449
Retained earning at end of year	**$ 9,802**	$ 8,186

The accompanying notes are an integral part of these financial statements

Nantucket Electric Company

STATEMENTS OF CASH FLOWS

(in thousands of dollars)	For the Years Ended March 31, 2010	2009
Operating activities:		
Net income	**$ 1,616**	$ 1,449
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation	**3,647**	3,621
Deferred income taxes and investment tax credit, net	**4,722**	830
Allowance for funds used during constructions	**(3)**	-
Changes in assets and liabilities:		
Accounts receivable, net and unbilled revenue	**114**	(985)
Accounts receivable - affiliates, net	**(2,986)**	15
Accounts payable	**(440)**	(200)
Materials and supplies	**-**	57
Other current liabilities	**(2,701)**	1,987
Accrued pension and other post-retirement benefits	**(119)**	(165)
Other, net	**539**	210
Net cash provided by operating activities	**4,389**	6,819
Investing activities:		
Plant expenditures, excluding allowance for funds used during construction	**(2,132)**	(2,496)
Change in account receivable - money pool	**(1,700)**	(1,175)
Other	**(314)**	163
Net cash used in investing activities	**(4,146)**	(3,508)
Financing activities:		
Reductions in long-term debt	**(210)**	(195)
Changes in intercompany short-term debt and money pool, net	**-**	(3,375)
Net cash used in financing activities	**(210)**	(3,570)
Net increase (decrease) in cash and cash equivalents	**33**	(259)
Cash and cash equivalents at beginning of year	**41**	300
Cash and cash equivalents at end of year	**$ 74**	$ 41
Supplementary information:		
Interest paid less amounts capitalized	**$ 871**	$ 1,098
Federal income taxes refunded from Parent	**$ -**	$ (502)
Capital-related accruals included in Accounts payable	**$ 9**	$ -

The accompanying notes are an integral part of these financial statements

STATEMENTS OF CAPITALIZATION

(In thousands, except number of shares)	March 31			
	2010	2009	**2010**	2009
Common stockholders' equity	**Shares Issued**		**Amounts**	
Common stock, $1.00 par value	**1**	1	**$ -**	$ -
Additional paid-in capital			**22,475**	22,475
Retained earnings			**9,802**	8,186
Accumulated other comprehensive loss			**(24)**	(1,527)
Total common stockholder' equity			**$ 32,253**	$ 29,134

Long-term debt	Interest rates (%)	Maturity Date	Amounts	
State authority financing bonds				
2016 Series 1996 MIFA Tax exempt	Variable	March 1, 2016	**$ 1,755**	$ 1,965
2004 $10 Million MIFA Tax exempt	Variable	March 1, 2039	**10,000**	10,000
2005 $28 Million MIFA Tax exempt	Variable	December 1, 2040	**28,000**	28,000
2007 $13.3 Million 1996 MDFA Tax exempt	Variable	August 1, 2042	**13,300**	13,300
Unamortized discounts			**(46)**	(53)
Total long-term debt			**53,009**	53,212
Long-term debt due within a year			**230**	210
Total long-term debt, excluding current portion			**52,779**	53,002
Total capitalization			**$ 85,032**	$ 82,136

The accompanying notes are an integral part of these financial statements

Nantucket Electric Company

Notes to the Financial Statements

NOTE 1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

A. Organization and Purpose

Nantucket Electric Company (the Company, we, us and our) is an electric retail distribution company providing electric service to approximately 13,000 customers on Nantucket Island. The Company is a wholly-owned subsidiary of National Grid USA (NGUSA), a public utility holding company with regulated subsidiaries engaged in the generation, transmission, distribution and sale of both natural gas and electricity in New England and New York State. NGUSA is a wholly-owned subsidiary of National Grid plc, a public limited company incorporated under the laws of England and Wales. The properties of the Company consist principally of substations and distribution lines, including two undersea electric cables, which connect Nantucket Island to the mainland electric grid.

B. Basis of Presentation

The Company's accounting policies conform to general accepted accounting principles in the United States of America (GAAP), including the accounting principles for rate-regulated entities, (See Note 2 Rates and Regulatory) and are in accordance with the accounting requirements and ratemaking practices of the applicable regulatory authorities.

The accounts of the Company are maintained in accordance with the Uniform System of Accounts prescribed by regulatory bodies having jurisdiction.

The preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets, liabilities and disclosure of contingent liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

The Company has evaluated events or transactions that occurred after March 31, 2010 through July 29, 2010 for potential recognition or disclosure in the financial statements. There were no subsequent events, other than regulated matter included in Note2 that needed to be recognized.

C. Accounting for the Effects of Rate Regulation

The Federal Energy Regulatory Commission (FERC) has jurisdiction over certain of the Company's activities, including (i) regulating certain transactions among our affiliates; (ii) governing the issuance, acquisition and disposition of securities and assets; and (iii) approving certain utility mergers and acquisitions (See Note 2- Rates and Regulatory). The Company is also subject to the regulations of the Massachusetts Department of Public Utilities (DPU) in addition to FERC.

D. Revenue Recognition

Revenues are based on billing rates authorized by the DPU. The Company follows the policy of accruing the estimated amount of revenues for electricity but not yet billed (unbilled revenues), to match costs and revenues more closely. The unbilled revenues at March 31, 2010 and 2009 were approximately $0.9 million and $1.5 million, respectively. The Company records revenues in an amount management believes to be recoverable pursuant to provisions of approved tariffs, settlement agreements and state legislation. The Company defers for future recovery from or refunds to electric customers the difference between revenue and expenses from energy conservation programs, standard offer/default service, transmission service, and contract termination charges (CTC).

E. Property, Plant and Equipment

The cost of additions to property, plant and equipment and replacements of retirement units of property are capitalized. Costs include direct material, labor, overhead and the Allowance for Funds Used during Construction (AFUDC). Replacement of minor items of utility plant and the cost of current repairs and maintenance are charged to expense. Whenever utility plant is retired, its original cost, together with the cost of removal, less salvage, is charged to accumulated depreciation.

AFUDC - The Company capitalizes AFUDC as part of construction costs. AFUDC represents an allowance for the cost of funds used to finance construction and, for the Company, includes a debt component and an equity component. AFUDC is capitalized in “Property, Plant and Equipment” with offsetting credits to “Other interest” for the debt component and “Other income (expense), net” for the equity component. This method is in accordance with an established FERC rate-making practice under which the Company is permitted to recover prudently incurred capital costs through their ultimate inclusion in rate base and in the provision for depreciation. The composite AFUDC rate was 2.5% and 2.8% for the years ended March 31, 2010 and 2009, respectively.

Depreciation - Depreciation is provided annually on a straight-line basis. The provisions for depreciation, as a percentage of weighted average depreciable property, and the weighted average service life, in years, for the years ended March 31, are presented in the table below:

	2010		2009	
	Provision	**Service Life**	Provision	Service Life
Asset Category:				
Electric	**3.6%**	**28**	3.7%	27

The increase in remaining service life was a result of a rate case filing detailed in Note 2.

F. Goodwill

In accordance with current accounting guidance for goodwill and other intangible assets, the Company tests goodwill for impairment on an annual basis and on an interim basis when certain events or circumstances exist. Goodwill impairment is determined by comparing the estimated fair value of a reporting unit with its respective book value. If the estimated fair value exceeds the book value, goodwill at the reporting unit level is not deemed to be impaired. If the estimated fair value is below book value, however, further analysis is required to determine the amount of the impairment. Additionally, if the forecasted returns utilized in the analysis are not achieved, an impairment of goodwill may result. For example, within our calculation of forecasted returns, we have made certain assumptions around the amount of pension and environmental costs to be recovered in future periods. Should we not benefit from improved rate relief in these areas, the result could be a reduction in fair value of the Company, which in turn could give rise to an impairment of goodwill.

The Company utilizes a discounted cash flow approach incorporating its most recent business plan forecasts together with a projected terminal year calculation in the performance of the annual goodwill impairment test. Critical assumptions used in the Company’s analysis include a discount rate of 6% and a terminal year growth rate of 3% based upon expected long-term average growth rates. Our forecasts assume long-term recovery and rate of returns that are in line with historical levels within the utility industry. The resulting fair value of the annual analysis determined that no adjustment of the goodwill carrying value was required.

G. Cash and Cash Equivalents
The Company classifies short-term investments with a maturity of 90 days or less at time of purchase as cash equivalents.

H. Income Taxes
Federal and state income taxes are recorded under the current accounting provision for the accounting and reporting of income taxes. 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 financial statement carrying amounts and the tax basis of existing assets and liabilities. Deferred investment tax credits are amortized over the useful life of the underlying property. Additionally, the Company follows the current accounting guidance relating to uncertainty in income taxes which applies to all income tax positions reflected on the Company's balance sheets that have been included in previous tax returns or are expected to be included in future tax returns. (See Note 6 – Income Taxes)

I. Comprehensive Income (Loss)
Comprehensive income (loss) is the change in the equity of a company, not including those changes that result from shareholder transactions. While the primary component of comprehensive income (loss) is reported net income or loss, the other components of comprehensive income (loss) consists of unrealized gains and losses associated with certain investments held as available for sales and changes in pension and other postretirement obligations.

J. Pension and Other Postretirement Plan Assets
On March 31, 2007, NGUSA adopted certain accounting guidance that requires employers to fully recognize all postretirement plans' funded status on the balance sheet as a net liability or asset and required an offsetting adjustment to regulatory assets upon implementation. Consistent with past practice and as required by the current accounting guidance, NGUSA values its pension and other postretirement assets using the year-end market value of those assets. Benefit obligations are also measured at year-end. (See Note 3 - Employee Benefits)

K. Fair Value Measurements
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 - exit price. The determination of fair value incorporates various factors required including not only the credits standing of the counterparties involved but also the impact of the Company's nonperformance risk on its liability. To increase consistency and comparability in fair value measurements, a fair value hierarchy was established that prioritizes the inputs to valuation techniques used to measure fair value into three levels. (See Note 7 – Fair Value Measurement) The following is a fair value hierarchy:

Level 1 — quoted prices (unadjusted) are available 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 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.

L. Inventory

Inventory is stated primarily at the lower of cost or market value under the average costs method. The Company's policy is to write-off obsolete inventory.

M. Recent Accounting Pronouncements

In May 2009, the Financial Accounting Standard Board (FASB) issued accounting guidance establishing the general standards of accounting for and disclosures of events that occur after the balance sheet date but before the financial statements are issued or are available to be issued. In particular, this FASB guidance requires enhanced disclosures about (a) events or transactions that may occur for potential recognition or disclosure in the financial statements in the period after the balance sheet date, (b) circumstances under which an entity should recognize such events, and (c) date through which an entity has evaluated subsequent events, including the basis for that date, and whether that date represents the date the financial statements were issued or available to be issued. This FASB guidance is effective for financial statements issued for interim and annual periods ending after June 15, 2009. The adoption of this guidance did not have an impact on the Company's financial statements.

In June 2009, the FASB issued an amendment to the accounting and disclosure requirements for transfers and servicing of financial assets and extinguishment of liabilities. The objective of the amendment is to improve the relevance, representational faithfulness, and comparability of the information that a reporting entity provides in its financial statements about a transfer of financial assets; and effects of a transfer on its financial position, financial performance and cash flows; and transferor's continuing involvement, if any, in transferred financial assets. The new provisions must be applied as of the beginning of each reporting entity's first annual reporting period that begins after November 15, 2009 and are to be applied to transfers occurring on or after the effective date.

In June 2009, FASB issued an amendment to the accounting and disclosure requirements for the consolidation of variable interest entities. The objective of the amendment is to improve financial reporting by enterprises involved with variable interest entities and to provide more relevant and reliable information to users of financial statements. The amendment requires an enterprise to perform an analysis to determine whether the enterprise's variable interest or interests give it a controlling financial interest in a variable interest entity. The new requirements shall be effective as of the beginning of each reporting entity's first annual reporting period that begins after November 15, 2009.

In June 2009, the FASB issued the FASB Accounting Standards Codification (Codification). The Codification will become the single source for all authoritative GAAP recognized by the FASB to be applied for financial statements issued for periods ending after September 15, 2009. The Codification does not change GAAP and will not have an affect on our financial position, results of operations or liquidity. With the adoption of this new guidance, the Company has eliminated specific references in the notes to its financial statements and other documents and replaced them with more general topical references.

In January 2010, the FASB issued an amendment to the accounting guidance for fair value measurements that will provide for additional disclosures about (a) the different classes of assets and liabilities measured at fair value, (b) the valuation techniques and inputs used, (c) the activity in Level 3 fair value measurements, and (d) the transfers between Levels 1, 2, and 3. This FASB guidance is effective for financial statement issued for interim and annual periods beginning after December 15, 2009, except for the disclosures about purchases, sales, issuances, and settlements in the roll forward of activity in Level 3 fair value measurements. Those disclosures are effective for fiscal years beginning after December 15, 2010, and for interim periods within those fiscal years.

NOTE 2. RATES AND REGULATORY

The Company's accounting records are maintained in accordance with the Uniform System of Accounts prescribed by the FERC. The financial statements reflect the ratemaking policies and actions of the DPU in conformity with GAAP for rate-regulated enterprises.

The Company applies the current accounting guidance for rate-regulated enterprises. The guidance recognizes the ability of regulators, through the ratemaking process, to create future economic benefits and obligations affecting rate-regulated companies. Accordingly, the Company records these future economic benefits and obligations as regulatory assets and regulatory liabilities.

In the event the Company determines that its net regulatory assets are not probable of recovery, it would no longer apply the principles of the current accounting guidance for rate-regulated enterprises and would be required to record an after-tax, non-cash charge against income for any remaining regulatory assets and liabilities. The resulting charge would be material to the Company's reported financial condition and results of operations.

Management continues to believe that rates are based on the Company's incurred costs and investment levels and therefore should continue to apply the current accounting guidance for rate regulated enterprises.

Rate Matters:
Rates for services rendered by the Company are the same as those approved by the DPU for the Company's affiliate, Massachusetts Electric Company (Massachusetts Electric), a wholly-owned subsidiary of NGUSA, with the addition of a cable facilities surcharge to cover the costs associated with two 46 kilovolt submarine cables owned by the Company that deliver electricity from the mainland to the island of Nantucket. In March 2000, the DPU approved a long-term rate plan (Rate Plan) for the Company, which became effective on May 1, 2000. During the period from March 1, 2005 through December 31, 2009, the Rate Index Period, distribution rates were adjusted annually, based upon the movement of a distribution index rate (in cents per kilowatt-hour) of similarly unbundled distribution utilities in New England, New York, Pennsylvania and New Jersey. The Company implemented increases in distribution rates pursuant to this mechanism of 1.90% and 1.54% effective March 1, 2008, and 2009, respectively. The Rate Plan also included provisions for recovery of major storm costs and recovery or pass back to customers for exogenous costs.

On May 15, 2009, the Company, together with Massachusetts Electric, filed for an increase in base distribution rates effective January 1, 2010. The DPU issued its initial order on the Company's case on November 30, 2009. In that order the DPU approved, with modification, the revenue decoupling mechanism (RDM) proposed by the Company, as well as the reconciliation of commodity-related bad debt, pension and postretirement benefits other than pension (PBOP) costs to our actual costs. The reconciliation of pension and PBOP costs will occur outside of base rates through a separate factor. The RDM allows for annual adjustments to the Company's distribution rates as a result of incremental capital investment and the reconciliation between allowed revenue and billed revenue. As a result of the RDM, the Company's future revenues are not solely dependent on volumes of electricity delivered. In addition, the actual costs incurred for commodity related bad debt and pension and PBOPs are fully recoverable. The DPU issued a second order on April 13, 2010 which partially modified the initial order by approving an overall increase in base distribution revenue of approximately $42 million as compared to the revenue generated at the old rates, and increased the ratio of equity to debt in the capital structure to 49.99% for ratemaking purposes.

This rate order also allowed recovery of non-capitalized pension and PBOP costs to occur outside of base rates through a separate factor. Costs of the Company's pension and postretirement benefits plans over or under amounts reflected in rates are deferred to a regulatory asset to be recovered in a future period. As a result the Company reclassified "Accumulated Other Comprehensive Income" of $1.2 million and related "accumulated deferred income taxes" of $0.8 million to "regulatory assets" of $2 million.

In addition to the rates and tariffs put into effect following the rate case, the Company continues to be authorized to recover costs associated with the procurement of electricity for customers, all transmission costs, and costs charged by the Company's affiliate, New England Power Company (NEP) for stranded costs associated with NEP's former electric generation investments.

Other Regulatory Matters:
Pursuant to the 2008 Green Communities Act (GCA), the Massachusetts Legislature mandated large scale and innovative ideas for implementing renewable energy and alternative energy, as well as increased energy efficiency spending. The legislation established three-year energy efficiency plans that would cover calendar years 2010 through 2012 and result in increased energy efficiency spending increased energy efficiency spending compared to amounts spent in prior years. Statewide three-year electric plans were approved by the newly created Energy Efficiency Advisory Council on October 27, 2009. The Company's 2010 through 2012 energy efficiency plan (offered as a single combined program with Massachusetts Electric without allocation) were approved by the DPU on January 28, 2010, including the budget and cost recovery proposed by the Company. The proposed budget for the two electric companies in Massachusetts, exclusive of lost base revenue, that is, revenues reduced as a result of installed energy efficiency measures, for the calendar years 2010 through 2012 is $572.8 million. A performance incentive mechanism was also approved by the DPU. The sources used to fund our energy efficiency programs are recoverable from our ratepayers. The Company expected programs to ramp up over time.

The GCA allows electric utilities to invest in solar generation, provided, however, that such utility does not own or operate more than 50 megawatts (MW) of solar capacity after January 1, 2010. On April 23, 2009 the Company and Massachusetts Electric petitioned the DPU for approval to construct, own, and operate approximately 5 MW of solar generation on five separate properties owned by Massachusetts Electric and/or its affiliates in Dorchester, Everett, Haverhill, a location on the Sutton/Northbridge border, and Revere, Massachusetts. The estimated total capital cost of the projects is approximately $31 million. The DPU approved the proposal on October 23, 2009 with no material modifications. Pursuant to the terms of the DPU's approval, and following specific cost recovery filings with the DPU as each unit goes into service, the Company and Massachusetts Electric are allowed to recover the costs of each site with a return equal to the weighted average cost of capital approved in the DPU's most recent rate proceeding for the Company and Massachusetts Electric through an interim cost recovery mechanism continuing until their next distribution rate proceeding. Construction of the sites is expected to continue through the remainder of the year.

Other provisions of the GCA that will affect the Company include requirements to enter into long-term contracts with renewable electricity suppliers for no less than 3% of the utilities' load, the development of a smart grid pilot program, and net metering to allow customers to sell self-generated electricity back to the utilities. Utilities would be allowed to recover costs associated with these new requirements and have the opportunity to earn incentives for certain of these provisions. In addition, under the new law, the maximum level of service quality penalties has been increased from 2% to 2.5% of distribution revenues.

The Company and Massachusetts Electric also filed a proposed smart grid pilot program on April 1, 2009 which is also pending at the DPU. The direct expenditures of the proposed pilot program are estimated at approximately $56.4 million. If the program is approved, the provisions of the GCA allow for the recovery of the program costs through basic service rates.

The Company provided energy efficiency initiatives for its customers under its 2009 single combined program with Massachusetts Electric without allocation, with a budget approved by the DPU of $85.3 million. The Company and Massachusetts Electric obtain cost recovery through each company's systems benefit charge. In addition, the companies can earn performance incentives depending on whether certain set goals are met, and are also entitled to seek recovery of lost base revenues, that is, revenues reduced as a result of installed energy efficiency measures. Lost base revenues may be recovered from a set point in time until the companies' revenue decoupling proposal was approved by the DPU. The Company has requested recovery of lost base revenues in its 2010 Energy Efficiency Reconciliation Factor (EERF), which the DPU has approved for implementation subject to further investigation. The EERF is a separate charge to customers that covers energy efficiency plan costs not otherwise covered by other allowed regulatory cost recovery mechanisms.

On May 7, 2010, the Company and Massachusetts Electric announced that they had entered into a fifteen year Power Purchase Agreement (PPA) with Cape Wind Associates, LLC to purchase half of the power generated by the proposed four hundred and sixty-eight MW offshore wind project at an initial price of 20.7 cents per kilowatt hour beginning in 2013. Under the terms of the PPA the contract price would increase by 3.5% annually to account for inflation. On June 4, 2010, the Company and Massachusetts Electric submitted a filing with the DPU officially requesting its approval of the PPA and the cost recovery proposed in that filing. The DPU must approve the PPA before it can become effective. The Company's filing requesting approval of the PPA is pending before the DPU.

The components of regulatory assets (liabilities) at March 31, are as follows:

(in thousands of dollars)	**2010**	2009
Current regulatory assets in accounts receivable:		
Rate adjustment mechanisms	**$ 3,756**	$ 3,190
Current regulatory (liabilities) in other accrued expenses:		
Rate adjustment mechanisms	**(11,228)**	(10,504)
Total current regulatory liabilities, net	**(7,472)**	(7,314)
Non-current regulatory assets:		
Long-term portion of standard offer under-recovery	**2,238**	2,242
Unamortized losses on reacquired debt	**561**	630
Second cable deferral	**2,294**	2,929
Pension expenses	**2,264**	-
Other	**-**	(15)
Total non-current regulatory assets	**7,357**	5,786
Non-current regulatory liabilities:		
Regulatory tax liability	**(623)**	(624)
Postretirement benefits	**(48)**	(63)
Cost of removal	**(1,315)**	(1,248)
Other	**(62)**	(60)
Total non-current regulatory (liabilities)	**(2,048)**	(1,995)
Total non-current regulatory assets, net	**5,309**	3,791
Net regulatory liabilities	**$ (2,163)**	$ (3,523)

Cost of Removal and Asset Retirement Obligations:
The Company adheres to the accounting guidance related to asset retirement obligations associated with tangible long-lived assets. The Company does not have any material asset retirement obligations arising from legal obligations as defined under accounting guidance related to asset retirement obligations. However, under the Company's current and prior rate plans, it has collected through rates an implied cost of removal for its plant assets. This cost of removal collected from customers differs from the accounting guidance related to asset retirement obligations associated with tangible long-lived assets definition in that these collections are for costs to remove an asset when it is no longer deemed usable (i.e. broken or obsolete) and not necessarily from a legal obligation. These collections have been recorded as regulatory liability to reflect future use. The Company estimates it has collected over time approximately $1.3 million and $1.2 million for cost of removal and asset retirement obligations in excess of what the Company incurred through March 31, 2010 and 2009, respectively.

NOTE 3. EMPLOYEE BENEFITS

Summary
The Company participates in a non-contributory defined benefit pension plan and the PBOP plan (the Plans) covering substantially all employees. The Plans cover the Company and certain other NGUSA subsidiaries.

The pension plan is a non-contributory, tax-qualified defined benefit plan which provides all employees with a minimum retirement benefit. Under the pension plan, a participant's retirement benefit is computed using formulas based on percentages of highest average compensation computed over five consecutive years. The compensation covered by the pension plan includes salary, bonus and incentive share awards. Non-union employees hired after July 15, 2002 participate under a non-contributory defined benefit cash balance design.

Supplemental nonqualified, non-contributory executive retirement programs provide additional defined pension benefits for certain executives.

PBOPs 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.

Pension Benefits:
The Company participates in the pension plans with certain other NGUSA subsidiaries. Pension plan assets are commingled and cannot be allocated to an individual company. Pension costs are allocated to the Company. At March 31, 2010 and 2009 the pension plans have a net underfunded obligation of $420.7 million and $469.8 million, respectively. The Company's net periodic pension cost for the years ended March 31, 2010 and 2009 were approximately $0.3 million and $0.2 million, respectively.

Defined Contribution Plan:
The Company has a defined contribution pension plan (employee savings fund plan) that covers substantially all employees. Employer matching contributions of approximately $0.1 million were expensed for each of the years ended March 31, 2010 and 2009, respectively.

Postretirement Benefits Other than Pension:
The Company participates in the PBOP plans with certain other NGUSA subsidiaries. PBOP costs are allocated to the Company. At March 31, 2010 and 2009 the PBOP plans have a net underfunded obligation of $477.3 million and $476.8 million, respectively. The Company's net period postretirement benefits cost for each of the years ended March 31, 2010 and 2009 were approximately $0.1 million, respectively.

Health Care Reform:
In March 2010, the Patient Protection and Affordable Care Act and the Health Care and Education Reconciliation Act of 2010 became law. These laws' included provisions which resulted in the repeal, with effect from 2012, of the deduction for federal income tax purposes of the portion of the cost of an employer's retiree prescription drug coverage for which the employer received a benefit under the Medicare Prescription Drug Improvement and Modernization Act of 2003. The consequential reduction in the deferred tax asset balance resulted in a net charge to the income statement is zero.

Special Termination Benefits (Voluntary Early Retirement Offer):
In connection with National Grid plc's acquisition of KeySpan, which was completed on August 24, 2007, National Grid plc and KeySpan offered certain non-union employees voluntary early retirement offer (VERO) packages in June 2007 in an effort to achieve necessary staff reduction through voluntary means. Of the 560 employees accepting the VERO, none of the Company's employees accepted. Employees enrolled in the early retirement program will retire by October 1, 2010. The Company's share of the cost of the VERO program was estimated to be $0.2 million, which has been expensed through March 31, 2010. For the years ended March 31, 2010 and 2009, the Company expensed $36 thousand and $82 thousand, respectively.

During the year ending March 31, 2010, an additional VERO package was offered to 38 union employees in connection with National Grid plc's acquisition of KeySpan to further the effort to achieve necessary staff reduction through voluntary means. Of the 38 eligible employees, 33 enrolled in the VERO and were all employees of one affiliates of the Company. Employees enrolled in the early retirement program retired in fiscal year 2010. The Company recorded $5 thousand of allocated costs associated with this VERO package.

NOTE 4. DEBT

Short-term:
The Company has regulatory approval from the FERC to issue up to $15 million of short-term debt. The Company had no short-term debt outstanding to third-parties at March 31, 2010 and 2009, respectively.

Long-term:
At March 31, 2010, the Company had approximately $53 million of tax exempt Electric Revenue Bonds in commercial paper mode with variable maturity dates from 2016 through 2042 and variable interest rates ranged from 0.70% to 1.85% during the year ended March 31, 2010. The bonds were issued by the Massachusetts Development Finance Agency in connection with the Company's financing of its first and second underground and submarine cable projects. Sinking fund payments of $0.2 million were made during the year ended March 31, 2010.

At March 31, 2010 and 2009, the Company had Standby Bond Purchase Agreement with banks totaling $58 million and $70 million, respectively, which were available to provide liquidity support for the bonds. The current agreement with banks that provide the Company's standby bond purchase facility expires on November 30, 2011. There were no borrowings under this facility at March 31, 2010.

The aggregate maturities of long-term debt for the five years subsequent to March 31, 2010 are approximately:

(in thousands of dollars)

Year	Amount
2011	$ 230
2012	250
2013	275
2014	305
2015	335
Thereafter	51,660
Total	$ 53,055

Massachusetts Electric unconditionally guarantees the full and prompt payment of the principal, premium, if any, and interest on certain tax exempt bonds issued by the Massachusetts Development Finance Agency in connection with the Company's financing of its first and second underground and submarine cable projects. Massachusetts Electric would be required to make any principal, interest or premium payments if the Company failed to pay. The carrying value of the debt guaranteed is approximately $53 million at March 31, 2010 and extends through 2042.

Nantucket Electric Company

Notes to Financial Statements

NOTE 5. PROPERTY, PLANT AND EQUIPMENT

The following table reflects the movements in our property, plant and equipment for the years ended March 31, 2010 and 2009:

(in thousands of dollars)	Plant and Machinery	Land and Buildings	CWIP	Total
Balance at March 31, 2008	$ 94,006	$ 4,331	$ 16	**$ 98,353**
Additions	-	-	4,674	**4,674**
Disposals	(826)	(144)	-	**(970)**
Reclassifications	4,182	76	(4,258)	**-**
Balance at March 31, 2009	$ 97,362	$ 4,263	$ 432	**$ 102,057**
Accumulated depreciation at March 31, 2009	(27,763)	(1,335)	-	**(29,098)**
Net book value at March 31, 2009	$ 69,599	$ 2,928	$ 432	**$ 72,959**
Balance at March 31, 2009	$ 97,362	$ 4,263	$ 432	**$ 102,057**
Additions	-	-	2,141	**2,141**
Disposals	(351)	(71)		**(422)**
Reclassifications	2,516	-	(2,516)	**-**
Balance at March 31, 2010	$ 99,527	$ 4,192	$ 57	**$ 103,776**
Accumulated depreciation at March 31, 2010	(30,733)	(1,347)	-	**(32,080)**
Net book value at March 31, 2010	$ 68,794	$ 2,845	$ 57	**$ 71,696**

NOTE 6. INCOME TAXES

The following is a summary of the components of federal and state income tax expense (benefits):

Years Ended March 31, (in thousands of dollars)	**2010**	2009
Components of federal and state income taxes:		
Current tax expense (benefit):		
Federal	**$ (3,454)**	$ 18
State	**128**	40
Total current tax (benefit) expense	**(3,326)**	58
Deferred tax expense (benefit):		
Federal	**$ 3,847**	$ 725
Investment tax credits (1)	**(4)**	(5)
State	**879**	110
Total deferred tax expense	**4,722**	830
Total income tax expense	**$ 1,396**	$ 888

(1) Investment tax credits (ITC) are being deferred and amortized over the depreciable life of the property giving rise to the credits

Income tax expense for the years ended March 31, 2010 and 2009 varied from the amount computed by applying the statutory rate to income before income taxes. A reconciliation between the expected federal income tax expenses using the federal statutory rate of 35% to the Company's actual income tax expense for the fiscal years ended March 31, is presented in the following table:

(in thousands of dollars)	2010	2009
Computed tax	**$ 1,054**	$ 818
Increase (reduction) including those attributable to flow-through of certain tax adjustments:		
State income taxes, net of federal income tax benefit	**653**	97
Intercompany tax sharing	**(123)**	-
Medicare subsidy, included Patient Pretection & Affordable Care Act, net effect	**80**	(8)
Provision to return adjustment	**12**	3
Investment tax credit	**(4)**	(3)
Other items, net	**(276)**	(19)
Total	**342**	70
Federal and state income taxes	**$ 1,396**	$ 888

Significant components of the Company's net deferred tax assets and liabilities at March 31, are presented in the following table:

(in thousands of dollars)	2010	2009
Pension, OPEB and other employee benefits	**$ 1,445**	$ 965
Regulatory liabilities - other	**1,199**	3,104
Other items	**356**	284
Total deferred tax assets(1)	**3,000**	4,353
Property related differences	**(10,703)**	(4,980)
Regulatory assets - other	**-**	(2,343)
Regulatory assets - Pension and OPEB	**(862)**	-
Investment tax credit	**(6)**	(10)
Other items	**(160)**	(58)
Total deferred tax liabilities	**(11,731)**	(7,391)
Net accumulated deferred income tax liability	**(8,731)**	(3,038)
Current portion (net deferred tax asset)	**2,768**	2,639
Net accumulated deferred income tax liability (non-current)	**$ (11,499)**	$ (5,677)

(1)There were no valuation allowances for deferred tax assets at March 31, 2010 or 2009.

The Company is member of the National Grid Holdings Inc. (NGHI) and subsidiaries consolidated federal income tax return. The Company has joint and several liabilities for any potential assessments against the consolidated group. In December 2009, NGHI, the parent company of NGUSA, made an income tax accounting method change (in accordance with Internal Revenue Code Section 481(a)) to deduct routine repair and maintenance of network assets pursuant to Internal Revenue Code Section 162 and Treasury Regulation §1.162-4 in its consolidated federal income tax return for the tax year ended March 31, 2009 which resulted in a current tax benefit during the year ended March 31, 2010.

ASC 740 clarifies the accounting for uncertain tax positions. ASC 740-10-25-6 provides that the financial effects of a tax position shall initially be recognized when it is more likely than not, based on the technical merits, that the position will be sustained upon examination, assuming the position will be audited and the taxing authority has full knowledge of all relevant information.

With the application of ASC 740, as of March 31, 2010 and 2009, the Company's unrecognized tax benefits totaled $2.6 million and $0, respectively, none of which would affect the effective tax rate, if recognized. The unrecognized tax benefits are included in "Deferred Credits and Other Liabilities - other reserves and deferred credits" on the Balance Sheets.

The following table reconciles the changes to the Company's unrecognized tax benefits for the years ended March 31,:

Reconciliation of unrecognized tax benefits	**At March 31,**	
(in thousands of dollars)	**2010**	2009
Beginning balance	**$ -**	$ -
Gross increases related to current period	**2,569**	-
Ending balance	**$ 2,569**	$ -

As of March 31, 2010 and 2009, the Company has no accrued interest related to unrecognized tax benefits. The Company recognizes accrued interest related to unrecognized tax benefits in interest expense or interest income and related penalties, if applicable, in operating expenses. No interest or penalties were recognized during the years ended March 31, 2010 and 2009.

The Company is a member of a federal consolidated return with its parent, NGHI. Federal income tax returns have been examined and all appeals and issues have been agreed with the Internal Revenue Service (IRS) and the NGHI consolidated filing group through March 31, 2004.

The IRS is currently auditing the federal NGHI consolidated income tax returns, which included the Company, for March 31, 2005 through March 31, 2007. The Company expects to make a cash tax payment to the IRS within the next twelve months related to the 2005 to 2007 settlement. At that time, the Company does not expect to decrease its total gross unrecognized tax benefits. The years ended March 31, 2008 and 2009 remain subject to examination by the IRS.

On July 2, 2008 the State of Massachusetts changed the state filing requirements that eliminate the previous separate exporting filing rules and implement a unitary group filing requirement. The new combined reporting rules are effective for tax years beginning on or after January 1, 2009. This change does not have a material effect on the 2010 or 2009 financial statements.

The Company files a Public Service Corporation Franchise Tax Return with the State of Massachusetts. Massachusetts is not currently conducting an audit of the Company; however the tax returns for fiscal years ending March 31, 2007 through March 31, 2009 are open under statute of limitations.

NOTE 7. FAIR VALUE MEASUREMENTS

Available for sale securities are primarily equity investments based on quoted market prices and municipal bonds based on quoted prices of similarly traded assets in open markets.

The following table presents assets and liabilities measured and recorded at fair value on a recurring basis and their level within the fair value hierarchy as of March 31, 2010:

(in thousands of dollars)				
Available for sale securities	Level 1	Level 2	Level 3	Total
Assets	$ 254	$ 338	$ -	$ 592
Total net assets	$ 254	$ 338	$ -	$ 592

Long term debt is based on quoted market prices where available or calculated prices based on the remaining cash flows of the underlying bond discounted at the Company's incremental borrowing rate. The Company's Balance Sheet reflects the long term debt at carrying value; the fair value of this debt at March 31, 2010 is approximately $53.1 million.

NOTE 8. ACCUMULATED OTHER COMPREHENSIVE INCOME (LOSS)

(in thousands of dollars)	Unrealized Gain (Loss) on Available-for- Sale Securities	Post-retirement liability	Total Accumulated Other Comprehensive Income (Loss)
March 31, 2008 balance, net of tax	$ 3	$ (796)	$ (793)
Other comprehensive income (losses):			
Unrealized (losses) on securities	(43)	-	(43)
Change in pension and postretirement benefits	-	(693)	(693)
Reclassification adjustment for gains included in net income	2	-	2
March 31, 2009 balance, net of tax	$ (38)	$ (1,489)	$ (1,527)
Other comprehensive income (losses):			
Unrealized gains on securities	67	-	67
Change in pension and postretirement benefits	-	765	765
Reclassification adjustment for (losses) included in net income	(10)	-	(10)
Subtotal	$ 57	$ 765	$ 822
Adjustment to accumulated other comprehensive income:		681	681
March 31, 2010 balance, net of tax	$ 19	$ (43)	$ (24)

The adjustment to the accumulated other comprehensive income is the result of the new tracking mechanism that was implemented as part of the rate case filed on May 19, 2009.

NOTE 10. COMMITMENTS AND CONTINGENCIES

Plant Expenditures:
Generally construction expenditures are consistent from year to year. However, the Company has undertaken a Reliability Enhancement Program to improve performance and reliability.

Legal Proceedings:
The Company is subject to various legal proceedings arising out of the ordinary course of its business. The Company does not consider any of such proceedings to be material to its business or likely to result in a material adverse effect on its results of operations or financial condition.

Hazardous Waste:
The normal ongoing operations and historic activities of the Company are subject to various federal, state and local environmental laws and regulations. Like many other industrial companies, the Company generates hazardous waste. Under federal and state Superfund laws, potential liability for the historic contamination of property may be imposed on responsible parties jointly and severally, without fault, even if the activities were lawful when they occurred.

The Massachusetts Department of Environmental Protection has named the Company as a potentially responsible party for remediation of a site at which hazardous waste is alleged to have been disposed. The Company believes that obligations imposed on it because of the environmental laws will not have a material impact on its results of operations or financial position.

NOTE 11. RELATED PARTY TRANSACTIONS:

Accounts Receivable - Money Pool:
The Company participates with NGUSA and its affiliates in a system money pool. The money pool is administered by a NGUSA Service Company as the agent for the participants. Short-term borrowing needs are met first by available funds of the money pool. Borrowings from the money pool bear interest at the higher of (i) the monthly average rate for high-grade, 30-day commercial paper sold through dealers by major corporations as published in the Wall Street Journal, or (ii) the monthly average rate then available to money pool depositors from an eligible investment in readily marketable money market funds or the existing short-term investment accounts maintained by money pool depositors or the NGUSA Service Company during the period in question. In the event neither rate is one that is permissible for a transaction because of constraints imposed by the state regulatory commission having jurisdiction over a utility participating in the transaction, the rate is adjusted to a permissible rate as determined under the requirements of the state regulatory commission. Companies that invest in the money pool share the interest earned on a basis proportionate to their average monthly investment in the money pool. Funds may be withdrawn from or repaid to the money pool at any time without prior notice. The average interest rate for the money pool was 0.27% and 1.96% for the years ended March 31, 2010 and 2009, respectively. The Company had accounts receivable from the money pool of approximately $2.9 million and $1.2 million at March 31, 2010 and 2009, respectively.

Accounts Receivable from Affiliates:
Additionally, the Company engages in various transactions with NGUSA and its affiliates. Certain activities and costs, such as executive and administrative, financial (including accounting, auditing, risk management, tax and treasury/finance) human resources, information technology, legal and strategic planning are shared between the companies and allocated to each company appropriately. In addition, the Company has a tax sharing agreement with NGHI, a NGUSA affiliate, in filing consolidated tax returns. The Company had net accounts receivable from affiliates of approximately $3.1 million and $0.1 million at March 31, 2010 and 2009, respectively, for those services.

Service Company Charges:
The affiliated service companies of National Grid have furnished services to the Company at the cost of such services. These costs, including operating costs and capital expenditures, were approximately $1.9 million and $1.6 million for the years ended March 31, 2010 and 2009, respectively.

Nantucket Electric Company

Notes to Financial Statements

Related Party Reimbursement:
In accordance with the Credit and Operating Support Agreement dated March 26, 1996 between the Company and an NGUSA affiliate, Massachusetts Electric, will reimburse the Company an amount equal to the difference between the Company's actual net income for the year and the net income necessary for the Company to earn a ROE equivalent to Massachusetts Electric's DPU approved weighted average allowed ROE for the year, currently 10.35%. If the Company's actual ROE for the year exceeds the Company's allowed ROE, the Company reimburses to Massachusetts Electric the excess amount of the earnings. This reimbursement shall constitute an additional increase/decrease of revenue to the Company and an increase/decrease of expense to Massachusetts Electric. For the years ended March 31, 2010 and 2009, Massachusetts Electric reimbursed the Company approximately $3.3 million and $2.0 million, respectively.

Parent Company Charges:
For the year ended March 31, 2010, NGUSA received charges from National Grid Commercial Holdings Limited (an affiliated company in the UK) for certain corporate and administrative services provided by the corporate functions of National Grid plc to its US subsidiaries.

These charges, which are recorded on the books of NGUSA, have not been reflected on these financial statements. Were these amounts allocated to this subsidiary, the estimated effect on net income would be approximately $55 thousand before tax and $36 thousand after tax.