The Narragansett Electric Company

Financial Statements

For the years ended March 31, 2014 and 2013

THE NARRAGANSETT ELECTRIC COMPANY

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Independent Auditor's Report

To the Shareholder and Board of Directors
of The Narragansett Electric Company

We have audited the accompanying financial statements of The Narragansett Electric Company (the "Company"), which comprise the balance sheets as of March 31, 2014 and 2013, and the related statements of income, comprehensive income, cash flows, capitalization, and changes in shareholders' equity for the years then ended.

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of the 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 financial statements that are free from material misstatement, whether due to fraud or error.

Auditor's Responsibility

Our responsibility is to express an opinion on the 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 financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on our judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, we consider internal control relevant to the Company's preparation and fair presentation of the 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 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 financial statements referred to above present fairly, in all material respects, the financial position of The Narragansett Electric Company at March 31, 2014 and 2013, 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.

PricewaterhouseCoopers LLP

July 18, 2014

PricewaterhouseCoopers LLP, 300 Madison Avenue, New York, NY 10017
T: (646) 471 3000, F: (646) 471 8320, www.pwc.com/us

THE NARRAGANSETT ELECTRIC COMPANY
STATEMENTS OF INCOME
(in thousands of dollars)

	Years Ended March 31,	
	2014	**2013**
Operating revenues:		
Electric services	**$ 964,035**	$ 813,925
Gas distribution	**455,736**	398,656
Total operating revenues	**1,419,771**	1,212,581
Operating expenses:		
Purchased electricity	**420,073**	341,181
Purchased gas	**247,982**	203,012
Contract termination charges and nuclear shutdown	**10,314**	7,383
Operations and maintenance	**393,740**	356,606
Depreciation and amortization	**85,048**	79,377
Other taxes	**106,351**	89,914
Total operating expenses	**1,263,508**	1,077,473
Operating income	**156,263**	135,108
Other income and (deductions):		
Interest on long-term debt	**(44,370)**	(36,138)
Other interest, including affiliate interest	**(1,430)**	(2,940)
Other income (deductions), net	**7,359**	(2,166)
Total other deductions, net	**(38,441)**	(41,244)
Income before income taxes	**117,822**	93,864
Income tax expense	**39,259**	33,168
Net income	**$ 78,563**	$ 60,696

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

THE NARRAGANSETT ELECTRIC COMPANY
STATEMENTS OF COMPREHENSIVE INCOME
(in thousands of dollars)

	Years Ended March 31,			
	2014		2013	
Net income	**$**	**78,563**	$	60,696
Other comprehensive income:				
Unrealized gains on securities, net of $148 and $111 tax expense		**275**		207
Changes in pension and other postretirement obligations, net of $6 and $2,731 tax expense		**12**		7,850
Adjustment for pension tracker, net of $ - and $54,481 tax expense		**-**		90,588
Reclassification of losses into net income, net of $140 and $191 tax benefit		**260**		354
Total other comprehensive income		**547**		98,999
Comprehensive income	**$**	**79,110**	$	159,695

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

THE NARRAGANSETT ELECTRIC COMPANY
STATEMENTS OF CASH FLOWS
(in thousands of dollars)

	Years Ended March 31,	
	2014	2013
Operating activities:		
Net income	**$ 78,563**	$ 60,696
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	**85,048**	79,377
Regulatory amortizations	**706**	5,737
Provision for deferred income taxes	**49,690**	81,938
Bad debt expense	**27,582**	16,648
Allowance for equity funds used during construction	**(2,536)**	488
Amortization of debt discount and issuance costs	**273**	224
Net pension and other postretirement expense (contributions)	**1,051**	(11,394)
Net environmental remediation payments	**(8,042)**	(1,930)
Share based compensation	**1,375**	-
Changes in operating assets and liabilities:		
Accounts receivable, net, and unbilled revenues	**(64,084)**	(56,548)
Accounts receivable from/payable to affiliates, net	**-**	(241)
Inventory	**6,480**	3,150
Regulatory assets and liabilities, net	**(25,950)**	(60,929)
Accounts payable and other liabilities	**(27,531)**	51,200
Other, net	**47,580**	(16,658)
Net cash provided by operating activities	**170,205**	151,758
Investing activities:		
Capital expenditures	**(224,461)**	(235,100)
Changes in restricted cash	**(5,211)**	32,298
Affiliated money pool investing and receivables/payables, net	**(153,189)**	-
Cost of removal	**(13,026)**	(17,360)
Other	**847**	343
Net cash used in investing activities	**(395,040)**	(219,819)
Financing activities:		
Dividends paid on preferred stock	**(110)**	(110)
Payments on long-term debt	**(1,375)**	(1,375)
Proceeds from long-term debt	**-**	250,000
Affiliated money pool borrowing and receivables/payables, net	**(22,048)**	(170,975)
Advance from affiliate	**250,000**	-
Payment of debt issuance costs	**-**	(1,875)
Net cash provided by financing activities	**226,467**	75,665
Net increase in cash and cash equivalents	**1,632**	7,604
Cash and cash equivalents, beginning of year	**10,905**	3,301
Cash and cash equivalents, end of year	**$ 12,537**	$ 10,905
Supplemental disclosures:		
Interest paid	$ (43,908)	$ (35,968)
Income taxes refunded	25,234	26,091
Significant non-cash items:		
Capital-related accruals included in accounts payable	22,865	8,515
Share based compensation	1,375	-

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

THE NARRAGANSETT ELECTRIC COMPANY
BALANCE SHEETS
(in thousands of dollars)

	March 31,	
	2014	2013
ASSETS		
Current assets:		
Cash and cash equivalents	**$ 12,537**	$ 10,905
Restricted cash and special deposits	**29,883**	24,526
Accounts receivable	**239,924**	201,702
Allowance for doubtful accounts	**(30,202)**	(27,115)
Unbilled revenues	**61,640**	60,273
Accounts receivable from affiliates	**21,364**	65,802
Intercompany money pool	**156,863**	-
Inventory	**17,626**	24,106
Regulatory assets	**105,013**	37,565
Derivative contracts	**6,243**	4,527
Current portion of deferred income tax assets, net	**32,853**	6,521
Prepaid taxes	**22,315**	75,134
Other	**14,100**	5,117
Total current assets	**690,159**	489,063
Property, plant, and equipment, net	**2,137,340**	1,986,075
Other non-current assets:		
Regulatory assets	**445,410**	485,018
Goodwill	**724,810**	724,810
Derivative contracts	**238**	1,885
Other	**12,636**	10,228
Total other non-current assets	**1,183,094**	1,221,941
Total assets	**$ 4,010,593**	$ 3,697,079

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

THE NARRAGANSETT ELECTRIC COMPANY
BALANCE SHEETS
(in thousands of dollars)

	March 31, 2014	March 31, 2013
LIABILITIES AND CAPITALIZATION		
Current liabilities:		
Accounts payable	**$ 123,538**	$ 132,985
Accounts payable to affiliates	**25,038**	30,970
Intercompany money pool	**-**	56,880
Advance from affiliate	**250,000**	-
Current portion of long-term debt	**1,375**	1,375
Taxes accrued	**14,088**	11,053
Interest accrued	**5,512**	6,310
Customer deposits	**8,557**	8,364
Regulatory liabilities	**77,884**	56,381
Derivative contracts	**10,372**	3,459
Other	**38,710**	21,434
Total current liabilities	**555,074**	329,211
Other non-current liabilities:		
Regulatory liabilities	**209,632**	197,433
Deferred income tax liabilities, net	**466,650**	411,105
Postretirement benefits	**126,058**	146,541
Environmental remediation costs	**130,550**	136,714
Derivative contracts	**416**	12
Other	**26,256**	59,330
Total non-current liabilities	**959,562**	951,135
Commitments and contingencies (Note 12)		
Capitalization:		
Shareholders' equity	**1,648,718**	1,568,343
Long-term debt	**847,239**	848,390
Total capitalization	**2,495,957**	2,416,733
Total liabilities and capitalization	**$ 4,010,593**	$ 3,697,079

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

THE NARRAGANSETT ELECTRIC COMPANY
STATEMENTS OF CAPITALIZATION
(in thousands of dollars)

			March 31,	
			2014	2013
Total shareholders' equity			**$ 1,648,718**	$ 1,568,343
Long-term debt:	Interest Rate	Maturity Date		
Unsecured notes:				
Senior Note	4.53%	March 15, 2020	**250,000**	250,000
Senior Note	5.64%	March 15, 2040	**300,000**	300,000
Senior Note	4.17%	December 10, 2042	**250,000**	250,000
			800,000	800,000
First Mortgage Bonds ("FMB"):				
FMB Series S	6.82%	April 1, 2018	**14,464**	14,464
FMB Series N	9.63%	May 30, 2020	**10,000**	10,000
FMB Series O	8.46%	September 30, 2022	**12,500**	12,500
FMB Series P	8.09%	September 30, 2022	**5,625**	6,250
FMB Series R	7.50%	December 15, 2025	**9,000**	9,750
Unamortized debt discounts			**(2,975)**	(3,199)
Total debt			**848,614**	849,765
Current portion of long-term debt			**1,375**	1,375
Long-term debt			**847,239**	848,390
Total capitalization			**$ 2,495,957**	$ 2,416,733

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

THE NARRAGANSETT ELECTRIC COMPANY
STATEMENTS OF CHANGES IN SHAREHOLDERS' EQUITY
(in thousands of dollars)

				Accumulated Other Comprehensive Income (Loss)					
	Common Stock	Cumulative Preferred Stock	Additional Paid-in Capital	Unrealized Gain (Loss) on Available-for-Sale Securities	Hedging Activities	Pension and Postretirement Benefits	Total Accumulated Other Comprehensive Income (Loss)	Retained Earnings	Total
Balance as of March 31, 2012	**$ 56,624**	**$ 2,454**	**$ 1,353,559**	**$ 584**	**(5,608)**	**$ (98,429)**	**$ (103,453)**	**$ 99,574**	**$ 1,408,758**
Net income	-	-	-	-	-	-	-	60,696	60,696
Other comprehensive income (loss):									
Unrealized gains on securities, net of $111 tax expense	-	-	-	207	-	-	207	-	207
Changes in pension and other postretirement obligations, net of $2,731 tax expense	-	-	-	-	-	7,850	7,850	-	7,850
Adjustment for pension tracker, net of $54,481 tax expense	-	-	-	-	-	90,588	90,588	-	90,588
Reclassification of (gains) losses into net income, net of $191 tax benefit	-	-	-	(107)	461	-	354	-	354
Total comprehensive income									159,695
Dividends on preferred stock	-	-	-	-	-	-	-	(110)	(110)
Balance as of March 31, 2013	**$ 56,624**	**2,454**	**1,353,559**	**684**	**(5,147)**	**9**	**(4,454)**	**160,160**	**1,568,343**
Net income	-	-	-	-	-	-	-	78,563	78,563
Other comprehensive income (loss):									
Unrealized gains on securities, net of $148 tax expense	-	-	-	275	-	-	275	-	275
Changes in pension and other postretirement obligations, net of $6 tax expense	-	-	-	-	-	12	12	-	12
Reclassification of (gains) losses into net income, net of $140 tax benefit	-	-	-	(227)	487	-	260	-	260
Total comprehensive income									79,110
Share based compensation	-	-	1,375	-	-	-	-	-	1,375
Dividends on preferred stock	-	-	-	-	-	-	-	(110)	(110)
Balance as of March 31, 2014	**$ 56,624**	**$ 2,454**	**$ 1,354,934**	**$ 732**	**$ (4,660)**	**$ 21**	**$ (3,907)**	**$ 238,613**	**$ 1,648,718**

The Company had 1,132,487 of common stock authorized, issued and outstanding, with a par value of $50 per share and 49,089 of cumulative preferred stock authorized, issued and outstanding, with a par value of $50 per share at March 31, 2014 and 2013.

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

THE NARRAGANSETT ELECTRIC COMPANY
NOTES TO THE FINANCIAL STATEMENTS

1. NATURE OF OPERATIONS AND BASIS OF PRESENTATION

The Narragansett Electric Company ("the Company") is a retail distribution company providing electric service to approximately 493,000 customers and gas service to approximately 260,000 customers in 38 cities and towns in Rhode Island. The Company's service area covers substantially all of Rhode Island.

The Company is a wholly-owned subsidiary of National Grid USA ("NGUSA" or "Parent"), a public utility holding company with regulated subsidiaries engaged in the generation of electricity and the transmission, distribution, and sale of both natural gas and electricity. NGUSA is a direct wholly-owned subsidiary of National Grid North America Inc. ("NGNA") and an indirect wholly-owned subsidiary of National Grid plc, a public limited company incorporated under the laws of England and Wales.

The accompanying 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. The financial statements reflect the ratemaking practices of the applicable regulatory authorities.

Management recorded out-of-period adjustments during the current fiscal year that resulted in net reductions of net income of $1.4 million. The adjustments primarily related to correction of operations and maintenance expense and stock compensation expense. Management concluded that the impact of recording these adjustments was not material to the current fiscal year or any prior period.

The Company has evaluated subsequent events and transactions through July 18, 2014, the date of issuance of these financial statements, and concluded that there were no events or transactions that require adjustment to or disclosure in the financial statements as of and for the year ended March 31, 2014.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Use of Estimates

In preparing 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 financial statements. Actual results could differ from those estimates.

Regulatory Accounting

The Federal Energy Regulatory Commission ("FERC"), the Rhode Island Public Utilities Commission ("RIPUC") and the Rhode Island Division of Public Utilities and Carriers ("Division") regulate the rates the Company charges its customers. In certain cases, the rate actions of the FERC and RIPUC can result in accounting that differs from non-regulated companies. In these cases, the Company defers costs (as regulatory assets) or recognizes obligations (as regulatory liabilities) if it is probable that such amounts will be recovered from or refunded to customers through future rates. Regulatory assets and liabilities are amortized to the statements of income 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. 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.

As approved by the RIPUC, the Company is allowed to pass through commodity-related costs to customers and also bills for other approved rate adjustment mechanisms. In addition, the Company has a revenue decoupling mechanism which requires the Company to adjust its base rates annually to reflect the over or under recovery of the Company's targeted base distribution revenues from the prior fiscal year.

Other Taxes

The Company collects 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).

The Company's policy is to accrue for property taxes on a calendar year basis, taking into account the assessment period. The Company had accrued for property taxes of $12.5 million and $10.5 million at March 31, 2014 and 2013, respectively.

Income Taxes

Federal 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 income taxes also reflect the tax effect of net operating losses, capital losses and general business credit carryforwards.

The effects of tax positions are recognized in the 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 company determines its current and deferred taxes based on the separate return method. The Company settles its current tax liability or benefit each year with NGNA pursuant to a tax sharing arrangement between NGNA and its subsidiaries. Tax benefits attributable to the tax attributes of other group companies and allocated by NGNA are treated as capital contributions.

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 primarily consists of deposits held by ISO New England, Inc. ("ISO-NE"). Special deposits primarily include collateral paid to the Company's counterparties for outstanding derivative contracts, health insurance and worker's compensation. The Company had restricted cash of $25.3 million and $20.1 million and special deposits of $4.6 million and $4.4 million at March 31, 2014 and 2013, respectively.

Accounts Receivable and Allowance for Doubtful Accounts

The Company recognizes an allowance for doubtful accounts to record accounts receivable at estimated net realizable value. During the year ended March 31, 2014, the Company enhanced its estimation methodology. 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. In prior years, the estimate placed a higher emphasis on a write off history. Management believes the more fulsome analysis of all information disclosed above results in an improved estimate

and the updated approach resulted in an increase of approximately $1.8 million in the reserve. 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.

Inventory

Inventory is comprised of materials and supplies as well as gas in storage. Materials and supplies are stated at the lower of weighted average cost or market value and are expensed or capitalized as used. The Company's policy is to write-off obsolete inventory; there were no material write-offs of obsolete inventory for the years ended March 31, 2014 or 2013.

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 RIPUC.

The Company had materials and supplies of $10.8 million and $9.5 million and gas in storage of $6.4 million and $14.6 million at March 31, 2014 and 2013, respectively.

Derivatives

Commodity Derivative Instruments – Regulated Accounting

The Company uses derivative instruments for commodity price risk management. All derivative instruments are recorded in the accompanying 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. Therefore, gains or losses on the settlement of these contracts are initially deferred and then refunded to, or collected from customers consistent with regulatory requirements.

Certain non-trading contracts for the physical purchase of natural gas qualify for the normal purchase normal sale exception and are accounted for upon settlement. If the Company were to determine that a contract for which it elected the normal purchase normal sale exception, no longer qualifies, the Company would recognize the fair value of the contract in accordance with 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, and to record and present the fair value of the derivative on a gross basis, with related cash collateral recorded as special deposits in the accompanying balance sheets.

Commodity Derivative Instruments – Non-Regulated Accounting

The Company also uses derivative instruments related to storage optimization, such as gas purchase contracts and swaps, to reduce the cash flow variability associated with forecasted purchases and sales of various energy-related commodities which do not receive regulatory recovery. All such derivative instruments are accounted for at fair value in the accompanying balance sheets with all changes in fair value reported in the statements of income.

Renewable Energy Certificates

Renewable Energy Certificates ("RECs") are used to measure compliance with renewable energy standards and are held primarily for consumption. At March 31, 2014 and 2013 the Company recorded purchased RECs of $12.1 million and $3.1 within other current assets and a compliance liability based on retail electricity sales of $23.3 million and $15.9 million within other current liabilities in the accompanying balance sheets.

Fair Value Measurements

The Company measures derivatives and available-for-sale securities 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; and
- 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.

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 RIPUC. The average composite rates and average service lives for the years ended March 31, 2014 and 2013 are as follows:

	Electric		Gas	
	Years Ended March 31,		Years Ended March 31,	
	2014	2013	**2014**	2013
Composite rates	**3.1%**	3.1%	**3.2%**	3.2%
Average service lives	**44 years**	44 years	**43 years**	43 years

Depreciation expense includes a component for estimated future 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 had cumulative costs of removal recovered in excess of costs incurred of $171.5 million and $160.1 million at March 31, 2014 and 2013, respectively.

Allowance for Funds Used During Construction

In accordance with applicable accounting guidance, the Company records AFUDC, which represents the debt and equity costs of financing the construction of new property, plant and equipment. AFUDC equity is reported in the statements of income as non-cash income in other income (deductions), net and AFUDC debt 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 and corresponding depreciation expense. The Company recorded AFUDC related to equity of $2.5 million and $0.5 million and AFUDC related to debt of $1.8 million and $0.5 million for the years ended March

31, 2014 and 2013, respectively. The average AFUDC rates for the years ended March 31, 2014 and 2013 were 5.9% and 2.6% respectively.

Goodwill

The Company tests goodwill for impairment annually on January 31, and when events occur or circumstances change that would more likely than not reduce the fair value of the Company below its carrying amount. Goodwill is tested for impairment using a two-step approach. The first step compares the estimated fair value of the Company with its carrying value, including goodwill. If the estimated fair value exceeds the carrying value, then goodwill is considered not impaired. If the carrying value exceeds the estimated fair value, then a second step is performed to determine the implied fair value of goodwill. If the carrying value of goodwill exceeds its implied fair value, then an impairment charge equal to the difference is recorded.

The fair value of the Company was calculated in the annual goodwill impairment test for the year ended March 31, 2014 utilizing both income and market approaches.

- To estimate fair value utilizing the income approach, the Company used a discounted cash flow methodology incorporating its most recent business plan forecasts together with a projected terminal year calculation. Key assumptions used in the income approach were: (a) expected cash flows for the period from April 1, 2014 to March 31, 2019; (b) a discount rate of 5.5%, which was based on the Company's best estimate of its after-tax weighted-average cost of capital; and (c) a terminal growth rate of 2.25%, based on the Company's expected long-term average growth rate in line with estimated long-term U.S. economic inflation.

- To estimate fair value utilizing the market approach, the Company followed a market comparable methodology. Specifically, the Company applied a valuation multiple of earnings before interest, taxes, depreciation and amortization ("EBITDA"), derived from data of publicly-traded benchmark companies, to business operating data. Benchmark companies were selected based on comparability of the underlying business and economics. Key assumptions used in the market approach included the selection of appropriate benchmark companies and the selection of an EBITDA multiple of 10.0, which the Company believes is appropriate based on comparison of its business with the benchmark companies.

The Company determined the fair value of the business using 50% weighting for each valuation methodology, as it believes that each methodology provides equally valuable information. Based on the resulting fair value from the annual analyses, the Company determined that no adjustment of the goodwill carrying value was required at March 31, 2014 or 2013.

Available-For-Sale Securities

The Company holds available-for-sale securities that include equities, municipal bonds and corporate bonds. These investments are recorded at fair value and are included in other non-current assets in the accompanying balance sheets. Changes in the fair value of these assets are recorded within other comprehensive income.

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 distribution 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 following table represents the changes in the Company's asset retirement obligations:

	Years Ended March 31,	
	2014	2013
	(in thousands of dollars)	
Balance as of the beginning of the year	**$ 3,441**	$ 3,660
Accretion expense	**211**	204
Liabilities settled	**(501)**	(423)
Balance as of the end of the year	**$ 3,151**	$ 3,441

Accretion expense is deferred as part of the Company's asset retirement obligation regulatory asset as management believes it is probable that such amounts will be collected in future rates.

Employee Benefits

The Company participates with other subsidiaries in defined benefit pension plans ("Pension Plans") and postretirement benefit other than pension ("PBOP") plans for its employees, administered by NGUSA. The Company recognizes its portion of the Pension Plans' and PBOP plan's funded status in the balance sheets as a net liability or asset. The cost of providing these plans is recovered through rates; therefore, the net funded status is offset by a regulatory asset or liability. The Pension Plans' and PBOP plan's assets are commingled and cannot be allocated to an individual company. 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 Adopted in Fiscal Year 2014

Offsetting Assets and Liabilities

In December 2011 and January 2013, the Financial Accounting Standards Board ("FASB") issued amendments to address and clarify the scope of the disclosures related to offsetting assets and liabilities. Under the amendments, reporting entities are required to disclose both gross and net information about instruments and transactions eligible for offset in the statement of financial position and instruments and transactions subject to an agreement similar to a master netting agreement, such as for derivatives. The instruments and activities subject to these disclosures are recognized derivatives, repurchase and reverse repurchase agreements, and securities lending transactions. The Company adopted this guidance effective April 1, 2013, which only impacted its disclosures.

Presentation of an Unrecognized Tax Benefit When a Net Operating Loss Carryforward, a Similar Tax Loss, or a Tax Credit Carryforward Exists

In July 2013, the FASB issued amendments to address diversity in practice related to the presentation of unrecognized tax benefits in certain situations. The amendments require a liability related to an unrecognized tax benefit to be presented on a net basis with its associated deferred tax asset when utilization of such deferred tax assets is required or expected in the event the uncertain tax position is disallowed. Otherwise, the unrecognized tax benefit will be presented as a liability and will not be netted against deferred tax assets. The Company early adopted this guidance effective April 1, 2013 with no material impact on its financial position, results of operations or cash flows.

Accounting Guidance Not Yet Adopted

Reclassifications From Accumulated Other Comprehensive Income

In February 2013, the FASB issued amendments to improve the reporting of reclassifications out of accumulated other comprehensive income ("AOCI"). The amendments require an entity to provide information either on the face of the financial statements or in a single footnote on significant amounts reclassified out of AOCI and the related income statement line items to the extent an amount is reclassified in its entirety to net income. For significant items not reclassified to net income in their entirety, an entity is required to cross-reference to other disclosures that provide additional information. For non-public entities, the amendments are effective prospectively for reporting periods beginning after December 15, 2013. Early adoption is permitted. The Company will adopt this guidance effective April 1, 2014, which will only impact its disclosures.

3. REGULATORY ASSETS AND LIABILITIES

The Company records regulatory assets and liabilities that result from the ratemaking process. The following table presents the regulatory assets and regulatory liabilities recorded in the accompanying balance sheets.

	March31,	
	2014	2013
	(in thousands of dollars)	
Regulatory assets		
Current:		
Derivative contracts	**$ 10,210**	$ 3,113
Gas cost adjustment	**42,453**	-
Rate adjustment mechanisms	**31,026**	6,626
Renewable energy certificates	**11,155**	12,698
Revenue decoupling mechanism	**-**	5,565
Storm costs	**7,300**	4,800
Other	**2,869**	4,763
Total	**105,013**	37,565
Non-current:		
Derivative contracts	**416**	12
Environmental response costs	**138,000**	140,923
Postretirement benefits	**212,577**	236,752
Regulatory deferred tax asset	**14,406**	14,137
Storm costs	**69,038**	78,470
Other	**10,973**	14,724
Total	**445,410**	485,018
Regulatory liabilities		
Current:		
Derivative contracts	**5,662**	4,511
Energy efficiency	**34,014**	28,555
Gas cost adjustment	**-**	545
Rate adjustment mechanisms	**21,327**	22,770
Revenue decoupling mechanism	**16,881**	-
Total	**77,884**	56,381
Non-current:		
Cost of removal	**171,491**	160,128
Derivative contracts	**2,470**	1,885
Postretirement benefits	**19,267**	20,540
Refund of customer credit	**8,758**	8,364
Other	**7,646**	6,516
Total	**209,632**	197,433
Net regulatory assets	**$ 262,907**	$ 268,769

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 contracts (assets and liabilities): Gains or losses resulting from commodity derivatives are typically required to be refunded to, or recovered from, customers through the gas cost adjustment. Accordingly, the Company evaluates open derivative contracts to determine if they are probable of recovery, or refund, through future rates charged to customers and qualify for regulatory deferral. Derivative contracts that qualify for regulatory deferral 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 ("EE"): This amount represents the difference between revenue billed to customers through its EE Charge and the costs of the Company's EE programs as approved by the RIPUC.

Environmental response costs: This regulatory asset represents deferred costs associated with the Company's share of the estimated costs to investigate and perform certain remediation activities at sites with which it may be associated. The Company's rate plans provide for specific rate allowances for these costs at a level of $4.4 million per year, with variances deferred for future recovery or return to customers. The Company believes future costs, beyond the expiration of current rate plans, will continue to be recovered through rates.

Gas cost 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 the RIPUC. These amounts will be refunded to, or recovered from, customers over the next year.

Postretirement benefits: This amount primarily represents the excess costs of the Company's pension and PBOP plans over amounts received in rates that are deferred as a regulatory asset to be recovered in future periods and the non-cash accrual of net actuarial gains and losses.

Rate adjustment mechanisms: The Company is subject to a number of 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 RIPUC. Rate adjustment mechanisms include the Renewable Energy Standard Charge, a charge designed to cover our compliance costs associated with state renewable portfolio standards and Low Income Energy Assistance Program, a federally funded, state administered program providing funding to assist low income customers in paying their heating bills.

Refund of customer credit: This regulatory liability primarily represents interest on retained funds for the E-183 Line undergrounding project as per the Customer Credit Adjustment Provision approved by RIPUC Docket No. 3617.

Regulatory deferred tax asset: This amount represents unrecovered federal deferred taxes of the Company primarily as a result of regulatory flowthrough accounting treatment, and tax rate changes. The income tax benefits or charges for certain plant related timing differences, such as equity AFUDC, are immediately flowed through to, or collected from, customers. The amortization of the related regulatory deferred tax asset, for these items, follows the book life of the underlying plant asset. The Company also has a recovery of historic unfunded deferred tax balances that are currently amortizing into rates at a stated annual revenue requirement under the current rate plan.

Renewable energy certificates: Represents deferred costs associated with the Company's compliance obligation with Rhode Island's 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 RIPUC, the Company has a RDM which allows for annual adjustment to the Company's delivery rates as a result of the reconciliation between allowed revenue per customer and actual revenue per customer. Any difference between the allowed revenue per customer and the actual revenue per customer is recorded as a regulatory asset or regulatory liability.

Storm costs: This regulatory asset represents the incremental costs to restore power to customers resulting from major storms. The Company's most recent settlement with the RIPUC included storm fund recovery at a level of $4.8 million per year through December 31, 2013, and then to $7.3 million per year effective January 1, 2014. This level of recovery will remain in place at least through January 31, 2018 and will be subject to RIPUC review at that time.

The Company records carrying charges on regulatory balances related to rate adjustment mechanisms, storm costs, postretirement benefits, and environmental costs 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.

4. RATE MATTERS

General Rate Case

On December 20, 2012, the RIPUC approved a settlement agreement among the Division, the Department of the Navy, and the Company, which provided for an increase in electric base distribution revenue of $21.5 million and an increase in gas base distribution revenue of $11.3 million based on a 9.5% allowed return on equity ("ROE") and a common equity ratio of approximately 49.1%, effective February 1, 2013. The settlement also included reinstatement of base rate recovery of storm fund contributions and implementation of a Pension Adjustment Mechanism for pension and PBOP expenses for the electric business identical to the mechanism in place for the gas business.

New England East-West Solution ("NEEWS") Project

In September 2008, the Company, its affiliate, New England Power ("NEP"), and Northeast Utilities jointly filed an application with the FERC to recover financial incentives for the NEEWS, pursuant to the FERC's Transmission Pricing Policy Order, Order No. 679. NEEWS consists of a series of inter-related transmission upgrades identified in the New England Regional System Plan and is being undertaken to address a number of reliability problems in Connecticut, Massachusetts, and Rhode Island. The Company's share of the NEEWS-related transmission investment is approximately $575 million. The Company is fully reimbursed for its transmission revenue requirements on a monthly basis by NEP through NEP's Tariff No. 1. Effective as of November 18, 2008, the FERC granted for NEEWS (1) an incentive ROE of 12.89% (125 basis points above the approved base ROE of 11.64%), (2) 100% construction work in progress in rate base, and (3) recovery of plant abandoned for reasons beyond the companies' control. On June 19, 2014, the FERC issued an order that all ROE incentives, such as the NEEWS incentive ROE, be capped at 11.74% subject to further limited proceedings to determine growth rates. It is currently unclear how the FERC's order will affect the ROE for NEEWS.

5. PROPERTY, PLANT AND EQUIPMENT

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

	March 31,	
	2014	2013
	(in thousands of dollars)	
Plant and machinery	**$ 2,695,582**	$ 2,482,843
Land and buildings	**114,485**	106,694
Assets in construction	**148,380**	180,879
Software and other intangibles	**30,144**	30,058
Property held for future use	**15,016**	15,016
Total property, plant and equipment	**3,003,607**	2,815,490
Accumulated depreciation and amortization	**(866,267)**	(829,415)
Property, plant and equipment, net	**$ 2,137,340**	$ 1,986,075

6. DERIVATIVE CONTRACTS

The Company utilizes derivative instruments, such as gas future contracts, gas swap contracts and gas purchase contracts, to manage commodity price risk associated with its natural gas purchases. The Company's risk management strategy is to reduce fluctuations in firm gas sales prices to its customers.

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 to, and only in terms and volumes consistent with its core business.

Volumes

Volumes of outstanding commodity derivative contracts measured in dekatherms are as follows:

	March 31,	
	2014	2013
	(in thousands)	
Physical contracts:		
Gas purchase contracts	**3,701**	786
Financial contracts:		
Gas swap contracts	**12,722**	14,343
Gas future contracts	**19,730**	16,830
Total	**36,153**	31,959

Amounts Recognized in the Accompanying Balance Sheets

	Asset Derivatives			Liability Derivatives	
	March 31,			March 31,	
	2014	2013		**2014**	2013
	(in thousands of dollars)			*(in thousands of dollars)*	
Current assets:			**Current liabilities:**		
Rate recoverable contracts:			Rate recoverable contracts:		
Gas swap contracts	**$ 2,982**	$ 3,211	Gas swap contracts	**$ 157**	$ 1,316
Gas future contracts	**2,679**	1,300	Gas future contracts	**145**	1,797
Gas purchase contracts	**-**	-	Gas purchase contracts	**9,908**	-
Contracts not subject to rate recovery:			Contracts not subject to rate recovery:		
Gas swap contracts	**207**	16	Gas swap contracts	**69**	309
Gas purchase contracts	**375**	-	Gas purchase contracts	**93**	37
	6,243	4,527		**10,372**	3,459
Non-current assets:			**Non-current liabilities:**		
Rate recoverable contracts:			Rate recoverable contracts:		
Gas swap contracts	**38**	274	Gas swap contracts	**50**	7
Gas future contracts	**200**	1,611	Gas future contracts	**366**	5
	238	1,885		**416**	12
Total	**$ 6,481**	$ 6,412	Total	**$ 10,788**	$ 3,471

The changes in fair value of the Company's rate recoverable contracts 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 statements of income. At March 31, 2014 and 2013 the Company recorded gains of $0.7 million and losses of $0.4 million within purchased gas in the accompanying statements of income for changes in fair value for contracts not subject to rate recovery.

Credit and Collateral

The Company is exposed to credit risk related to transactions entered for commodity price 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.

The credit policy for commodity transactions is managed and monitored by NGUSA's Executive Energy Risk Management Committee ("EERC"), 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, counterparty credit approval, as well as all valuation and control procedures. The EERC is chaired by the Global Tax and Treasury Director and reports to the Finance Committee. The EPRMC is chaired by the Vice President of U.S. Treasury and reports to the EERC.

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. The Company enters into enabling agreements that allow for payment netting with its counterparties, which reduce its exposure to counterparty risk by providing for the offset of amounts payable to the counterparty against amounts receivable from the counterparty. 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 derivative instruments and applicable payables and receivables, net of collateral and instruments that are subject to master netting agreements, was $2.1 million and $0.5 million as of March 31, 2014 and 2013, respectively.

The Company enters into commodity transactions on New York Mercantile Exchange ("NYMEX"). The NYMEX clearinghouses act as the counterparty to each trade. Transactions on the NYMEX must adhere to comprehensive collateral and margining requirements. As a result, transactions on NYMEX are significantly collateralized and have limited counterparty credit risk.

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 aggregate fair value of the Company's derivative instruments with credit-risk-related contingent features that are in a liability position at March 31, 2014 and 2013 was $0.5 million and $1.0 million, respectively. The Company had no collateral posted for these instruments at March 31, 2014 or 2013. If the Company's credit rating were to be downgraded by one or two levels, it would not be required to post any additional collateral. If the Company's credit rating were to be downgraded by three levels, it would be required to post $0.6 million and $1.1 million additional collateral to its counterparties at March 31, 2014 and 2013.

Offsetting Information for Derivatives Subject to Master Netting Arrangements

March 31, 2014
Gross Amounts Not Offset in the Balance Sheets
(in thousands of dollars)

ASSETS: Description	Gross amounts of recognized assets *A*	Gross amounts offset in the Balance Sheets *B*	Net amounts of assets presented in the Balance Sheets *C=A+B*	Financial instruments *Da*	Cash collateral received *Db*	Net amount *E=C-D*
Commodity Derivatives						
Gas swap contracts	$ 3,227	$ -	$ 3,227	-	$ 35	$ 3,192
Gas future contracts	2,879	-	2,879	-	2,879	-
Gas purchase contracts	375	-	375	-	-	375
Total	$ 6,481	$ -	$ 6,481	$ -	$ 2,914	$ 3,567

LIABILITIES: Description	Gross amounts of recognized liabilities *A*	Gross amounts offset in the Balance Sheets *B*	Net amounts of presented in the Balance Sheets *C=A+B*	Financial instruments *Da*	Cash collateral paid *Db*	Net amount *E=C-D*
Commodity Derivatives						
Gas swap contracts	$ (276)	$ -	$ (276)	$ -	$ (43)	$ (233)
Gas future contracts	(511)	-	(511)	-	(511)	-
Gas purchase contracts	(10,001)	-	(10,001)	-	-	(10,001)
Total	$ (10,788)	$ -	$ (10,788)	$ -	$ (554)	$ (10,234)

March 31, 2013
Gross Amounts Not Offset in the Balance Sheets
(in thousands of dollars)

ASSETS: Description	Gross amounts of recognized assets *A*	Gross amounts offset in the Balance Sheets *B*	Net amounts of assets presented in the Balance Sheets *C=A+B*	Financial instruments *Da*	Cash collateral received *Db*	Net amount *E=C-D*
Commodity Derivatives						
Gas swap contracts	$ 3,501	$ -	$ 3,501	$ -	$ 840	$ 2,661
Gas future contracts	2,911	-	2,911	-	2,911	-
Gas purchase contracts	-	-	-	-	-	-
Total	$ 6,412	$ -	$ 6,412	$ -	$ 3,751	$ 2,661

LIABILITIES: Description	Gross amounts of recognized liabilities *A*	Gross amounts offset in the Balance Sheets *B*	Net amounts of presented in the Balance Sheets *C=A+B*	Financial instruments *Da*	Cash collateral paid *Db*	Net amount *E=C-D*
Commodity Derivatives						
Gas swap contracts	$ (1,632)	$ -	$ (1,632)	$ -	$ -	$ (1,632)
Gas future contracts	(1,802)	-	(1,802)	-	(1,802)	-
Gas purchase contracts	(37)	-	(37)	-	-	(37)
Total	$ (3,471)	$ -	$ (3,471)	$ -	$ (1,802)	$ (1,669)

7. FAIR VALUE MEASUREMENTS

The following table presents assets and liabilities measured and recorded at fair value in the accompanying balance sheets on a recurring basis and their level within the fair value hierarchy as of March 31, 2014 and 2013:

	March 31, 2014			
	Level 1	**Level 2**	**Level 3**	**Total**
		(in thousands of dollars)		
Assets:				
Derivative contracts				
Gas swap contracts	$ -	$ 3,119	$ 108	$ 3,227
Gas future contracts	2,879	-	-	2,879
Gas purchase contracts	-	292	83	375
Available-for-sale securities	2,031	2,741	-	4,772
Total	4,910	6,152	191	11,253
Liabilities:				
Derivative contracts				
Gas swap contracts	-	276	-	276
Gas future contracts	511	-	-	511
Gas purchase contracts	-	13	9,988	10,001
Total	511	289	9,988	10,788
Net assets (liabilities)	$ 4,399	$ 5,863	$ (9,797)	$ 465

	March 31, 2013			
	Level 1	Level 2	Level 3	Total
		(in thousands of dollars)		
Assets:				
Derivative contracts				
Gas swap contracts	$ -	$ 3,501	$ -	$ 3,501
Gas future contracts	2,911	-	-	2,911
Available-for-sale securities	1,896	2,512	-	4,408
Total	4,807	6,013	-	10,820
Liabilities:				
Derivative contracts				
Gas swap contracts	-	1,632	-	1,632
Gas future contracts	1,802	-	-	1,802
Gas purchase contracts	-	37	-	37
Total	1,802	1,669	-	3,471
Net assets	$ 3,005	$ 4,344	$ -	$ 7,349

Derivative Contracts: The Company's Level 1 fair value derivative instruments consist of active exchange-based derivatives (e.g. natural gas futures traded on NYMEX) valued based on quoted prices (unadjusted) in active markets for identical assets or liabilities at the measurement date.

The Company's Level 2 fair value derivative instruments consist of over-the-counter ("OTC") gas swaps and forward gas purchase contracts with pricing inputs obtained from the New York Mercantile Exchange and 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 forwards and gas purchase transactions, which are valued based on internally-developed models. 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. The internally developed forward curves have a high level of correlation with Platts Mark-to-Market curves and are reviewed by the middle office. The Company considers non-performance risk and liquidity risk in the valuation of derivative contracts categorized in Level 2 and Level 3.

Available-for-Sale Securities: Available-for-sale securities are included in other non-current assets in the accompanying 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).

Changes in Level 3 Derivatives

	Years Ended March 31, 2014	Years Ended March 31, 2013
	(in thousands of dollars)	
Balance as of the beginning of the year	**$ -**	$ -
Total gains or losses included in regulatory assets and liabilities	**(14,163)**	(347)
Settlements:		
included in earnings	**73**	85
included in regulatory assets and liabilities	**4,293**	262
Balance as of the end of the year	**$ (9,797)**	$ -
The amount of total gains or losses for the year included in net income attributed to the change in unrealized gains or losses related to non-regulatory assets and liabilities at year-end	**$ -**	$ -

A transfer into Level 3 represents existing assets or liabilities that were previously categorized at a higher level for which the inputs became unobservable during the year. A transfer out of Level 3 represents assets and liabilities that were previously classified as Level 3 for which the inputs became observable based on the criteria discussed previously for classification in Level 2. These transfers, which are recognized at the end of each period, result from changes in the observability of forward curves from the beginning to the end of each reporting period. There were no transfers between Level 1 and Level 2, and no transfers into or out of Level 3, during the years ended March 31, 2014 or 2013.

Quantitative Information About Level 3 Derivatives

Commodity	Level 3 Position	Fair Value as of March 31, 2014 Assets	(Liabilities)	Total	Valuation Technique(s)	Significant Unobservable Input	Range
		(thousands of dollars)					
Physical							
Gas	Gas Purchase Contract	$ -	$ (9,907)	$ (9,907)	Discounted Cash Flow	LNG Forward Curve	$3.5490 - $11.01/dth
Gas	Gas Purchase Contract	83	(81)	2	Discounted Cash Flow	Forward Curve	$2.534 - $4.544/dth
Financial							
Gas	Gas Swap Contract	108	-	108	Discounted Cash Flow	Forward Curve	($1.070) - ($0.610)/dth
	Total	$ 191	$ (9,988)	$ (9,797)			

The significant unobservable inputs listed above would have a direct impact on the fair values of the Level 3 instruments if they were adjusted. The significant unobservable inputs used in the fair value measurement of the Company’s gas purchase derivatives are forward liquefied natural gas commodity prices and gas forward curves. A relative change in commodity price at various locations underlying the open positions can result in significantly different fair value estimates.

Other Fair Value Measurements

The Company’s balance sheets reflect long-term debt at amortized cost. The fair value of the Company’s long-term debt was based on quoted market prices, where available or estimated using quoted market prices for similar debt. The fair value of this debt at March 31, 2014 and 2013 was $905.3 million and $964.6 million, respectively.

All other financial instruments in the accompanying balance sheets such as accounts receivable, accounts payable, and the intercompany money pool are stated at cost, which approximates fair value.

8. EMPLOYEE BENEFITS

The Company participates with other NGUSA subsidiaries in a qualified and non-qualified non-contributory defined benefit plan (the "Pension Plan") and PBOP plan (together with the Pension Plan (the "Plan")), covering substantially all employees.

The Pension Plan is a defined benefit plan which provides union employees, as well as non-union employees hired before January 1, 2011, with a retirement benefit. Supplemental nonqualified, non-contributory executive retirement programs provide additional defined pension benefits for certain executives. The PBOP Plan provides 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, 2014 and 2013, the Company made contributions of approximately $23.9 million and $45.3 million, respectively, to the Plan.

Plan assets are commingled and cannot be allocated to an individual company. The Plan's costs are first directly charged to the Company based on the Company's employees that participate in the Plan. Costs associated with affiliated service companies' employees are then allocated as part of the labor burden for work performed on the Company's behalf. The Company applies deferral accounting for pension and PBOP expenses associated with its regulated gas and electric operations. Any differences between actual pension costs and amounts used to establish rates are deferred and collected from or refunded to customers in subsequent periods. Pension and PBOP expense is included in operations and maintenance expense in the accompanying statements of income.

The NGUSA companies' pension and PBOP plans that the Company participates in have unfunded obligations at March 31, 2014 and 2013 as follows:

	March 31,	
	2014	2013
	(in thousands of dollars)	
Pension	**$ 402,928**	$ 471,000
PBOP	**302,360**	368,100
	$ 705,288	$ 839,100

The Company's net pension and PBOP expenses directly charged and allocated from affiliated service companies, net of capital, for the years ended March 31, 2014 and 2013 are as follows:

	March 31,	
	2014	2013
	(in thousands of dollars)	
Pension	**$ 20,503**	$ 23,135
PBOP	**7,392**	11,423
	$ 27,895	$ 34,558

Defined Contribution Plan

NGUSA has a defined contribution pension plan that covers substantially all employees. For the years ended March 31, 2014 and 2013, the Company recognized an expense in the accompanying statements of income of $2.5 million and $2.0 million, respectively, for matching contributions.

Other Benefits

During the year ended March 31, 2014, NGUSA improved its methodology for allocating to its subsidiaries the expense and liability for workers compensation, auto, and general insurance claims which have been incurred but not yet reported ("IBNR"). In prior years, such costs and liabilities were allocated to NGUSA's subsidiaries based on each subsidiary's pro-rata share of known outstanding case reserves. As of and for the year ended March 31, 2014, such IBNR amounts are allocated proportionally based on various factors including revenue, payroll, and number of fleet vehicles, as applicable to the related exposure source. Management believes this improved methodology provides a more accurate and appropriate allocation to each of its subsidiaries. The change in allocation methodology resulted in a decrease in income before taxes of approximately $3.8 million in the current fiscal year. At March 31, 2014 and 2013, the Company had accrued IBNR of $4.5 million and $4.4 million respectively.

9. CAPITALIZATION

Debt Authorizations

The Company had regulatory approval from the FERC to issue up to $400 million of short-term debt, which expired on November 30, 2013. Effective April 2014, the Company entered into an Equity Contribution Agreement with the Parent which provides the Company with the ability to call upon the Parent for contributions to the Company's capital, in an aggregate amount equal to the short-term borrowing limit until such time as regulatory approval for short-term borrowing is regained. The Company has not made use of this facility since its effective date. The Company had no short-term debt outstanding to third parties as of March 31, 2014 or 2013.

First Mortgage Bonds

At March 31, 2014, the Company had $51.6 million of First Mortgage Bonds ("FMB") outstanding. Substantially all of the assets used in the gas business of the Company are subject to the lien of the mortgage indentures under which these FMB have been issued. Interest rates on these FMB range from 6.82% to 9.63%. Maturities range on these FMB from April 2018 to December 2025. The FMB have annual sinking fund requirements totaling approximately $1.4 million.

The Company has a maximum 70% of debt-to-capitalization covenant. Furthermore, if at any time the Company's debt exceeds 60% of the total capitalization, each holder of bonds then outstanding shall receive effective as of the first date of such occurrence, a one time, and permanent 0.20% increase in the interest rate paid by the Company on its bonds. During the years ended March 31, 2014 and 2013, the Company was in compliance with this covenant. At March 31, 2014 and 2013 the Company's debt-to-capitalization ratio was 34% and 35%, respectively.

Current Maturities of Long-term Debt

(in thousands of dollars)		
Years Ended March 31,		
2015	$	1,375
2016		1,375
2017		1,375
2018		1,375
2019		15,839
Thereafter		830,250
Total	$	851,589

The Company is obligated to meet certain financial and non-financial covenants. During the years ended March 31, 2014 and 2013 the Company was in compliance with all such covenants.

Dividend Restrictions

Pursuant to the preferred stock arrangement, as long as any preferred stock is outstanding, certain restrictions on payment of common stock dividends would come into effect if the common stock equity was, or by reason of payment of such dividends became, less than 25% of total capitalization. Common stock equity at March 31, 2014 and 2013 was approximately 66% and 65%, respectively, of total capitalization. Accordingly, the Company was not restricted as to the payment of common stock dividends under the foregoing provisions at March 31, 2014 or 2013.

Cumulative Preferred Stock

The Company has non-participating cumulative preferred stock outstanding which can be redeemed at the option of the Company. There are no mandatory redemption provisions on the Company's cumulative preferred stock. A summary of cumulative preferred stock is as follows:

	Shares Outstanding		Amount		
	March 31,		**March 31,**		Call
Series	**2014**	2013	**2014**	2013	Price
	(in thousands of dollars, except per share and number of shares data)				
$50 par value -					
4.50% Series	**49,089**	49,089	**$ 2,454**	$ 2,454	55.000

The Company did not redeem any preferred stock during the years ended March 31, 2014 or 2013. The annual dividend requirement for cumulative preferred stock was $0.1 million for the years ended March 31, 2014 and 2013.

10. INCOME TAXES

Components of Income Tax Expense

	Years Ended March 31,	
	2014	2013
	(in thousands of dollars)	
Current federal tax benefit	**$ (10,431)**	$ (48,770)
Deferred federal tax expense	**49,993**	82,387
Amortized investment tax credits, net [1]	**(303)**	(449)
Total deferred tax expense	**49,690**	81,938
Total income tax expense	**$ 39,259**	$ 33,168

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

Statutory Rate Reconciliation

The Company's effective tax rate for the years ended March 31, 2014 and 2013 is 33.3% and 35.3%, respectively. The following table presents a reconciliation of income tax expense at the federal statutory tax rate of 35% to the actual tax expense from continuing operations:

	Years Ended March 31,	
	2014	2013
	(in thousands of dollars)	
Computed tax at the statutory rate	**$ 41,023**	$ 32,854
Change in computed taxes resulting from:		
Allowance for equity funds used during construction	**(771)**	(128)
Investment tax credits	**(303)**	(449)
Other items, net	**(690)**	891
Total	**(1,764)**	314
Federal and state income taxes	**$ 39,259**	$ 33,168

The Company is included in the NGNA and subsidiaries consolidated federal income tax return. The Company has joint and several liability for any potential assessments against the consolidated group.

In September 2013, the Internal Revenue Service ("IRS") issued final regulations, effective for tax years beginning in 2014, that provide guidance on the appropriate tax treatment of costs incurred to acquire, produce or improve tangible property, as well as routine maintenance and repair costs. Proposed regulations were issued addressing the tax treatment of asset dispositions. The Company has evaluated tax accounting method changes that may be elected or required by the final regulations. At March 31, 2014, $3.4 million of deferred tax liabilities have been classified as current in the accompanying balance sheets, representing the cumulative adjustment expected to be reflected in income for tax purposes during the twelve months ending March 31, 2015.

Deferred Tax Components

	March 31,	
	2014	2013
	(in thousands of dollars)	
Deferred tax assets:		
Net operating losses	**$ 58,537**	$ 27,984
Pensions, PBOP and other employee benefits	**50,727**	62,031
Environmental reserve	**44,946**	47,211
Allowance for uncollectible accounts	**10,927**	9,468
Other items	**27**	3,463
Total deferred tax assets [1]	**165,164**	150,157
Deferred tax liabilities:		
Property related differences	**456,343**	404,360
Regulatory assets - pension and PBOP	**62,254**	61,247
Regulatory assets - environmental	**46,171**	47,602
Regulatory assets - storm costs	**27,113**	29,145
Other items	**6,570**	11,574
Total deferred tax liabilities	**598,451**	553,928
Net deferred income tax liabilities	**433,287**	403,771
Deferred investment tax credits	**510**	813
Net deferred income tax liabilities and investment tax credits	**433,797**	404,584
Current portion of deferred income tax assets, net	**32,853**	6,521
Deferred income tax liabilities, net	**$ 466,650**	$ 411,105

[1] There were no valuation allowances for deferred tax assets at March 31, 2014 or 2013.

The following table presents the amounts and expiration dates of operating losses as of March 31, 2014:

Expiration of net operating losses:	Federal
	(in thousands of dollars)
03/31/2029	$ 54,816
03/31/2030	13,689
03/31/2032	30,224
03/31/2033	50,227
03/31/2034	56,909

Unrecognized Tax Benefits

As of March 31, 2014 and 2013, the Company’s unrecognized tax benefits totaled $22.7 million and $22.3 million, respectively, none of which would affect the effective tax rate, if recognized. The unrecognized tax benefits are presented on a net basis with the associated deferred tax asset.

The following table presents changes to the Company's unrecognized tax benefits:

	Years Ended March 31,	
	2014	2013
	(in thousands of dollars)	
Balance as of the beginning of the year	**$ 22,271**	$ 19,811
Gross increases - tax positions in prior periods	**1,407**	313
Gross decreases - tax positions in prior periods	**(1,392)**	(536)
Gross increases - current period tax positions	**1,773**	3,422
Gross decreases - current period tax positions	**-**	(739)
Settlements with tax authorities	**(1,408)**	-
Balance as of the end of the year	**$ 22,651**	$ 22,271

As of March 31, 2014 and 2013, the Company has accrued for interest related to unrecognized tax benefits of zero and $0.5 million, respectively. During the years ended March 31, 2014 and 2013, the Company recorded interest income of $0.5 million and interest expense of $0.1 million, respectively. 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 statements of income. No tax penalties were recognized during the years ended March 31, 2014 or 2013.

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.

Federal income tax returns have been examined and all appeals and issues have been agreed with the IRS and the NGNA consolidated filing group through March 31, 2007.

During the year ended March 31, 2014 the IRS has concluded its examination of the NGNA consolidated filing group's corporate income tax returns for the years ended March 31, 2008 through March 31, 2009. These examinations were completed on March 31, 2014, with an agreement on the majority of income tax issues for the years referenced above, as well as an acknowledgment that certain discrete items remain disputed. NGNA is in the process of appealing these disputed issues with the IRS Office of Appeals. The Company does not anticipate a change in its unrecognized tax positions in the next twelve months as a result of the appeals. However, pursuant to the Company's tax sharing agreement, the audit or appeals may result in a change to allocated tax.

The years ended March 31, 2010 through March 31, 2014 remain subject to examination by the IRS.

11. 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.

The United States Environmental Protection Agency ("EPA"), the Massachusetts Department of Environmental Protection ("DEP"), and the Rhode Island Department of Environmental Management ("DEM") have alleged that the Company is a potentially responsible party under state or federal law for a number of sites at which hazardous waste is alleged to have been disposed. The Company's most significant liabilities relate to former Manufactured Gas Plant ("MGP") facilities formerly owned by the Blackstone Valley Gas and Electric Company and the Rhode Island gas distribution assets of New England Gas. The Company is currently investigating and remediating, as necessary, those MGP sites and certain other properties under agreements with the EPA, DEM and DEP. Expenditures incurred for the years ended March 31, 2014 and 2013 were $8.0 million and $1.9 million, respectively.

The Company estimated the remaining costs of environmental remediation activities were $130.6 million and $136.7 million at March 31, 2014 and 2013, respectively. These costs are expected to be incurred over the next 41 years, and these undiscounted amounts have been recorded as liabilities in the accompanying balance sheets. However, remediation costs for each site may be materially higher than estimated, depending upon changing technologies and regulatory standards, selected end use for each site, and actual environmental conditions encountered. The Company has recovered amounts from certain insurers and potentially responsible parties, and, where appropriate, the Company may seek additional recovery from other insurers and from other potentially responsible parties, but it is uncertain whether, and to what extent, such efforts will be successful.

The RIPUC has approved a settlement agreement that provides for rate recovery of remediation costs of former MGP sites and certain other hazardous waste sites located in Rhode Island. Under that agreement, qualified costs related to these sites are paid out of a special fund established as a regulatory liability in the accompanying balance sheets. Rate-recoverable contributions of approximately $3 million are added annually to the fund along with interest and any recoveries from insurance carriers and other third parties. Accordingly, as of March 31, 2014 and 2013, the Company has recorded environmental regulatory assets of $136.6 million and $140.9 million, respectively, and environmental regulatory liabilities of $2.4 million and $1.9 million, respectively.

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. Where the Company has regulatory recovery, it believes 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.

12. COMMITMENTS AND CONTINGENCIES

Purchase Commitments

The Company has several long-term contracts for the purchase of electric power. Substantially all of these contracts require power to be delivered before the Company is obligated to make payment. Additionally, the Company has entered into various contracts for electricity and gas delivery storage and supply services. Certain of these contracts require payment of annual demand charges. The Company is liable for these payments regardless of the level of services required from third parties. Such charges are currently recovered from customers as purchased electricity and purchased gas. The Company also has various capital commitments related to the construction of property, plant and equipment.

The Company's commitments under these long-term contracts for the years subsequent to March 31, 2014 are summarized in the table below:

(in thousands of dollars) Years Ending March 31,	Energy Purchases	Capital Expenditures
2015	$ 329,049	$ 72,256
2016	96,670	-
2017	35,807	-
2018	23,128	-
2019	9,668	-
Thereafter	41,587	-
Total	$ 535,909	$ 72,256

The Company purchases additional energy to meet load requirements from independent power producers, other utilities, energy merchants or the ISO-NE at market prices.

Long-Term Contracts for Renewable Energy

Town of Johnston Project

In June 2010, pursuant to 2009 Rhode Island legislation that required the Company to negotiate a contract for an electric generating project fueled by landfill gas from the Rhode Island Central Landfill, the Company entered into a contract with Rhode Island LFG Genco for the Town of Johnston Project, a combined cycle power plant with an average output of 32 megawatts ("MW"). The facility reached commercial operation on May 28, 2013 and is being accounted for as an operating lease.

Deepwater Agreement

The 2009 law also required the Company to solicit proposals for a small scale renewable energy generation project of up to eight wind turbines with an aggregate nameplate capacity of up to 30 MW to benefit the Town of New Shoreham. The renewable energy generation project also included a transmission cable to be constructed between Block Island and the mainland of Rhode Island. On June 30, 2010, the Company entered into a 20-year Amended Power Purchase Agreement ("PPA") with Deepwater Wind Block Island LLC, which was approved by the RIPUC in August 2010. The Company also negotiated a Transmission Facilities Purchase Agreement ("Facilities Purchase Agreement") with Deepwater Wind Block Island Transmission, LLC ("Deepwater") to purchase from Deepwater the permits, engineering, real estate, and other site development work for construction of the undersea transmission cable. On April 2, 2014, the Division issued its Consent Decision for the Company to execute the Facilities Purchase Agreement with Deepwater. The Company intends to make a filing with the FERC to recover the costs associated with the cable in transmission rates.

Annual Solicitations

- 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 ("Black Bear PPA"). The Black Bear 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.

Legal Matters

The Company is subject to various legal proceedings, primarily injury claims, arising out of the ordinary course of its business. 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.

13. RELATED PARTY TRANSACTIONS

Advance from Affiliate

In December 2008, the Company entered into an agreement with NGUSA whereby the Company can borrow up to $250 million from time to time for working capital needs. The advance is non-interest bearing. At March 31, 2014 and 2013, the Company had an outstanding advance from affiliate of $250 million and zero, respectively.

Accounts Receivable from and Accounts Payable to Affiliates

NGUSA and its affiliates provide various services to the Company, including executive and administrative, customer services, financial (including accounting, auditing, risk management, tax, and treasury/finance), human resources,

information technology, legal and strategic planning that are charged between the companies and charged to each company.

The Company records short-term payables to and receivables from certain of its affiliates in the ordinary course of business. The amounts payable to and receivable from its affiliates do not bear interest and are settled through the intercompany money pool. A summary of net outstanding accounts receivable from affiliates and accounts payable to affiliates balances is as follows:

	Accounts Receivable from Affiliates		**Accounts Payable to Affiliates**	
	March 31,		**March 31,**	
	2014	2013	**2014**	2013
	(in thousands of dollars)		*(in thousands of dollars)*	
Boston Gas Company	**$ 5,650**	$ 34,095	**$ -**	$ -
Colonial Gas Company	**1,133**	11,372	**-**	-
New England Power Company	**11,373**	19,269	**-**	-
Massachusetts Electric Company	**-**	-	**5,391**	158
Niagara Mohawk Power Company	**1,215**	466	**-**	-
NGUSA Service Company	**-**	-	**16,812**	27,942
Other	**1,993**	600	**2,835**	2,870
Total	**$ 21,364**	$ 65,802	**$ 25,038**	$ 30,970

Recovery of Transmission Costs

NEP operates the transmission facilities of its New England affiliates as a single integrated system and reimburses the Company for the cost of its transmission facilities in Rhode Island, including a return on those facilities under NEP's Tariff No. 1. In turn, these costs are allocated among transmission customers in New England in accordance with the ISO New England transmission tariff. The Company is compensated for its actual monthly transmission costs with its authorized ROE ranging from 11.14% to 12.64%. The amounts reimbursed to the Company by NEP for the years ended March 31, 2014 and 2013 were $100.7 million and $84.1 million, respectively, which are included within operations and maintenance expense in the accompanying statements of income.

Intercompany Money Pool

The settlement of the Company's various transactions with NGUSA and certain affiliates generally occurs via the intercompany money pool. The Company is a participant in the Regulated Money Pool and can both borrow and lend funds. Borrowings from the Regulated Money Pool bear interest in accordance with the terms of the intercompany money pool agreement. As the Company fully participates in the Regulated Money Pool rather than settling intercompany charges with cash, all changes in the intercompany money pool balance and accounts receivable and payable from affiliate balances, are reflected as investing or financing activities in the accompanying statements of cash flows. In addition, for the purpose of presentation in the statement of cash flows, it is assumed all amounts settled through intercompany money pool are constructive cash receipts and payments, and therefore are presented as such.

The Regulated Money Pool is funded by operating funds from participants. Collectively, NGUSA, and its subsidiary, KeySpan, have the ability to borrow up to $3 billion from National Grid plc for working capital needs including funding of the intercompany money pools, if necessary. The Company had short-term intercompany money pool investments of $156.9 million and borrowings of $56.9 million at March 31, 2014 and 2013, respectively. The average interest rates for the intercompany money pool were 0.7% and 0.6% for the years ended March 31, 2014 and 2013, respectively.

Service Company Charges

The affiliated service companies of NGUSA provide certain services to the Company at their cost. The service company costs are generally allocated to associated companies through a tiered approach. First and foremost, costs are directly charged to

the benefited company whenever practicable. Secondly, in cases where direct charging cannot be readily determined, costs are allocated using cost/causation principles linked to the relationship of that type of service, such as number of employees, number of customers/meters, capital expenditures, value of property owned, total transmission and distribution expenditures. Lastly, all other costs are allocated based on a general allocator determined using a 3-point formula based on net margin, net property, plant and equipment, and operations and maintenance expense.

Charges from the service companies of NGUSA to the Company for the years ended March 31, 2014 and 2013 were $197.1 million and $264.7 million, respectively.

Holding Company Charges

NGUSA received charges from National Grid Commercial Holdings Limited (an affiliated company in the U.K.) for certain corporate and administrative services provided by the corporate functions of National Grid plc to its U.S. subsidiaries. These charges, which are recorded on the books of NGUSA, have not been reflected on these financial statements. Were these amounts allocated to the Company, the estimated effect on net income would be $5.1 million before taxes, and $3.3 million after taxes, for each of the years ended March 31, 2014 and 2013.