National Grid USA

Annual Report
Fiscal year ended March 31, 2008

REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

Report of Independent Auditors

To the Stockholder and Board of Directors of
National Grid USA:

In our opinion, the accompanying consolidated balance sheets and statements of capitalization and the related consolidated statements of income, of comprehensive income, of retained earnings and of cash flows present fairly, in all material respects, the financial position of National Grid USA and its subsidiaries (the "Company") at March 31, 2008 and 2007, 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 audit in accordance with generally accepted auditing standards as established by the Auditing Standards Board (United States) and in accordance with the standards of Public Company Accounting Oversight Board (United States). 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.

As described in Note A to the financial statements, the Company changed the manner in which it accounts for income taxes effective April 1, 2007 in accordance with Financial Interpretation 48, *Accounting for Uncertainty in Income* Taxes and the manner in which it accounts for pension and postretirement benefit plans effective March 31, 2007 in accordance with Financial Accounting and Standards Board Statement No. 158, *Employers' Accounting for Defined Benefit Pension and Other Postretirement Plans*.

PricewaterhouseCoopers LLP

August 22, 2008

NATIONAL GRID USA AND SUBSIDIARY COMPANIES

Consolidated Statements of Income

(In millions of dollars)

	For the years ended March 31, 2008	2007
Operating revenues		
Electric	**$ 7,609.6**	$ 6,944.4
Gas	**5,694.6**	1,218.0
Energy services and investments	**95.2**	-
Total operating revenues	**13,399.4**	8,162.4
Operating expenses		
Purchased energy		
Electricity purchased	**3,492.8**	3,483.9
Gas purchased	**3,804.9**	814.9
Contract termination charges and nuclear shutdown charges	**40.0**	63.8
Other operation and maintenance	**2,801.3**	1,691.6
Depreciation, depletion and amortization	**642.5**	411.0
Amortization of regulatory assets, stranded costs and rate plan deferrals	**531.9**	455.6
Other taxes	**630.6**	342.7
Income taxes	**354.8**	188.0
Total operating expenses	**12,298.8**	7,451.5
Operating income	**1,100.6**	710.9
Other income (deductions)	**24.1**	28.4
Operating and other deductions	**1,124.7**	739.3
Interest expense:		
Interest on long-term debt	**328.7**	138.6
Other interest, including affiliate interest	**176.4**	138.8
Total interest expense, net	**505.1**	277.4
Net income from continuing operations	**619.6**	461.9
Discontinued operations:		
Income from discontinued operations, net of tax expense of $21.7 million and $10.6 million	**27.8**	11.7
Gain (loss) on sale of discontinued businesses, net of tax	**15.2**	(120.2)
Net income (loss) from discontinued operations	**43.0**	(108.5)
Net income	**$ 662.6**	$ 353.4

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

NATIONAL GRID USA AND SUBSIDIARY COMPANIES
Consolidated Statements of Comprehensive Income
(In millions of dollars)

	For the years ended March 31, 2008	2007
Net income	**$ 662.6**	$ 353.4
Other comprehensive (loss) income, net of taxes:		
Unrealized (gains) losses on investments	**(13.6)**	6.0
Unrealized gain/(loss) on hedges	**14.2**	(17.5)
Change in additional minimum pension liability	**-**	(6.3)
Change in pension and other post-retirement obligations	**(100.5)**	-
Reclassification adjustment for gains (losses) included in net income	**17.8**	18.5
Total other comprehensive (loss) income	**(82.1)**	0.7
Comprehensive income	**$ 580.5**	$ 354.1
Adjustment to initially apply SFAS No. 158	**-**	(398.1)
Change in accumulated other comprehensive income (loss)	**$ 580.5**	$ (397.4)
Related tax expense (benefit):		
Unrealized (losses) gains on investments	**$ (9.1)**	$ 4.0
Unrealized gain (loss) on hedges	**9.5**	(11.7)
Change in pension and other post-retirement obligations	**(67.0)**	-
Change in additional minimum pension liability	-	(4.2)
Reclassification adjustment for gains (losses) included in net income	**11.8**	12.3
Total tax expense (benefit)	**$ (54.8)**	$ 0.4

NATIONAL GRID USA AND SUBSIDIARY COMPANIES
Consolidated Statements of Retained Earnings
(In millions of dollars)

	For the years ended March 31, 2008	2007
Retained earnings at beginning of period	**$ 1,550.0**	$ 1,484.6
Adoption of new accounting standard FIN 48	**(8.4)**	-
Adjusted balance at beginning of period	**1,541.6**	1,484.6
Net income	**662.6**	353.4
Dividends on preferred stock	**(1.9)**	(2.1)
Dividends on common stock	**-**	(286.1)
Return of capital to parent company	**(327.7)**	-
Other	**(0.4)**	0.2
Retained earnings at end of period	**$ 1,874.2**	$ 1,550.0

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

NATIONAL GRID USA AND SUBSIDIARY COMPANIES
Consolidated Balance Sheets
(In millions of dollars)

ASSETS	March 31, **2008**	2007
Assets:		
Property plant and equipment, net	**17,410.2**	9,689.2
Goodwill	**7,326.5**	3,338.8
Other property and investments	**504.2**	316.3
Current assets:		
Cash and cash equivalents	**1,169.9**	281.9
Restricted cash	**19.2**	63.1
Accounts receivable (less reserves of $305.5 and $165.2, respectively, including $64.1 million and $10.4 million from affiliates respectively)	**2,173.5**	1,066.6
Unbilled revenue	**941.2**	351.0
Inventories, at average cost:		
Gas in storage	**336.5**	20.9
Other	**389.3**	59.7
Derivative contracts	**171.0**	7.9
Current portion of accumulated deferred income taxes	**188.5**	176.2
Current portion of regulatory assets	**204.9**	304.0
Assets of discontinued operations	**3,025.4**	305.1
Other	**392.0**	161.8
Total current assets	**9,011.4**	2,798.2
Other non-current assets:		
Regulatory assets	**5,968.3**	5,101.4
Derivative contracts	**128.6**	-
Intangible assets, net of amortization	**230.9**	-
Other	**276.1**	67.7
Total other non-current assets	**6,603.9**	5,169.1
Total assets	**$ 40,856.2**	$ 21,311.6

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

NATIONAL GRID USA AND SUBSIDIARY COMPANIES
Consolidated Balance Sheets
(In millions of dollars)

CAPITALIZATION AND LIABILITIES	**March 31, 2008**	**2007**
Capitalization:		
Common stockholder's equity:		
Common stock ($.10 par value)	**$ -**	$ -
Authorized - 3000 shares		
Issued and outstanding -1000 shares		
Additional paid-in capital	**14,043.4**	7,599.0
Retained earnings	**1,874.2**	1,550.0
Accumulated other comprehensive income (loss)	**(483.8)**	(401.7)
Total common stockholder's equity	**15,433.8**	8,747.3
Minority interest in subsidiaries	**19.3**	16.4
Cumulative preferred stock, par value $ 100 per share	**34.8**	52.3
Long-term debt	**5,391.2**	1,968.5
Long-term debt to affiliates	**1,200.0**	1,200.0
Total capitalization	**22,079.1**	11,984.5
Current liabilities:		
Accounts payable	**1,917.1**	698.4
Customers' deposits	**107.6**	51.3
Accrued interest	**199.8**	75.1
Accrued taxes	**301.1**	33.2
Short-term debt due to affiliates	**1,136.4**	1,028.9
Current portion of long-term debt	**992.6**	218.9
Commercial paper	**1,115.0**	-
Notes payable - Other	**298.0**	-
Current portion of accrued Yankee nuclear plant costs	**23.2**	28.5
Liabilities of discontinued operations	**1,860.8**	34.9
Current regulatory liabilities	**322.8**	129.3
Other, including derivative contracts	**261.3**	458.8
Total current liabilities	**8,535.7**	2,757.3
Other non-current liabilities:		
Accumulated deferred income taxes	**2,443.3**	2,050.2
Derivates and swap contracts	**150.6**	254.7
Accrued employee pension and other benefits and other reserves	**2,864.7**	1,570.7
Environmental remediation costs	**1,282.9**	582.8
Regulatory liabilities, miscellaneous	**1,159.2**	846.6
Regulatory liabilities - removal costs recovered	**1,305.9**	642.2
Regulatory liabilities derivative accounts	**128.1**	2.3
Other	**906.7**	620.3
Total non-current liabilities	**10,241.4**	6,569.8
Total capitalization and liabilities	**$ 40,856.2**	$ 21,311.6

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

NATIONAL GRID USA AND SUBSIDIARY COMPANIES
Consolidated Statements of Cash Flows
(In millions of dollars)

	For the years ended March 31,	
Operating activities:	**2008**	2007
Net income	**$ 662.6**	$ 353.4
Adjustments to reconcile net income to net cash provided by operating activities:		
Net (income) loss from discontinued operations	**(43.0)**	108.5
Depreciation and amortization	**642.5**	411.0
Amortization of stranded costs and rate plan deferrals	**531.9**	455.6
Income from equity investments	**(8.6)**	-
Dividends from equity investments	**7.5**	-
Merger related and other non-cash charges	**(47.5)**	(28.3)
Provision for deferred federal and state income taxes and investment tax credits	**(76.6)**	108.6
Changes in operating assets and liabilities:		
Accounts receivable, net	**(803.9)**	(19.1)
Materials and supplies	**357.7**	27.4
Prepaids and other current assets	**(64.4)**	(59.1)
Accounts payable and accrued expenses	**199.8**	(10.6)
Pension and postretirement regulatory assets	**(271.8)**	(117.7)
Purchased power obligations	**5.8**	(0.2)
Other, net	**61.9**	(78.4)
Net cash provided by operating activities	**1,153.9**	1,151.2
Investing activities:		
Plant expenditures	**(1,105.6)**	(787.2)
Acquisitions	**(7,545.1)**	(496.7)
Net proceeds from sale of subsidary and assets	**313.8**	1.9
Change in restricted cash	**43.9**	17.2
Other, net	**40.9**	64.8
Net cash used in investing activities	**(8,252.1)**	(1,200.0)
Financing activities:		
Dividends paid on common and preferred stock	**(43.6)**	(288.2)
Dividends paid on common stock of minority interests	**(2.1)**	(2.2)
Return of capital to parent company	**(327.7)**	-
Capital contribution from parent for acquisitions	**7,545.1**	500.0
Payment of long-term debt	**-**	(317.3)
Proceeds from long-term debt	**147.3**	-
Redemption of preferred stock	**(18.0)**	-
Buyback of minority interest common stock	**(1.3)**	(1.7)
Buyback of common stock	**(1,075.5)**	-
Net change in short-term debt to affiliates	**107.5**	384.7
Net change in short-term debt	**1,130.6**	-
Capital contribution to discontinued operations	**-**	(158.8)
Net cash provided by financing activities	**7,462.4**	116.6
Net increase in cash and cash equivalents	**364.2**	67.9
Cash flow from discontinued operations - Operating Activities	**(2.0)**	18.2
Cash flow from discontinued operations - Investing Activities	**(20.1)**	(176.9)
Cash flow from discontinued operations - Financing Activities	**(9.5)**	158.8
Cash transferred from KeySpan	**555.4**	-
Cash and cash equivalents, beginning of period	**281.9**	214.0
Cash and cash equivalents, at end of period	**1,169.9**	281.9
Supplemental disclosures of cash flow information:		
Interest paid	**458.3**	255.2
Taxes paid	**413.1**	252.8

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

NATIONAL GRID USA AND SUBSIDIARY COMPANIES

Consolidated Statement of Capitalization

(in millions of dollars)

	March 31, 2008	March 31, 2007	March 31, 2008	March 31, 2007
Common Shareholders' Equity	**Shares Issued**		**Amounts**	
Common stock, $0.01 par value	1,000	1,000	$ -	$ -
Additional Paid in Capital			14,043.4	7,599.0
Retained earnings			1,874.2	1,550.0
Accumulated other comprehensive loss			(483.8)	(401.7)
Total Common Shareholders' Equity			15,433.8	8,747.3
Minority Interest in Subsidiaries			19.3	16.4
Cumulative Preferred Stock, $100 and $50 par value	944	1,000	34.8	52.3
Long - Term Debt	**Interest Rate**		**Amounts**	
Medium and Long - Term Debt	3.55% - 5.51%	-	159.1	-
	4.65% - 9.75%	7.30% -9.41%	3,456.3	861.9
Total Medium and Long-Term Debt			3,615.4	861.9
Gas Facilities Revenue Bonds	Variable	-	230.0	-
	4.70% - 6.95%	-	410.5	-
Total Gas Facilities Revenue Bonds			640.5	-
Promissory Notes to LIPA				
Pollution Control Revenue Bonds	5.15%	-	108.0	-
Electric Facility Revenue Bonds	5.30%	-	47.4	-
Total Promissory Notes to LIPA			155.4	-
Industrial Development Bonds	5.25%	-	128.3	-
First Mortgage Bonds	5.72% - 10.25%	5.72% - 10.25%	205.1	171.7
State Authority Financing Bonds	Variable	Variable	1,219.9	1,155.5
Committed Facilities	Variable	-	382.5	-
Inter-Company Notes	5.52%	5.52%	1,200.0	1,200.0
Subtotal			7,547.1	3,389.1
Fair value adjustment and unamortized interest rate hedge			36.7	(1.7)
Less: current maturities			992.6	218.9
Total Long - Term Debt			6,591.2	3,168.5
Total Capitalization			$ 22,079.1	$ 11,984.5

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

NATIONAL GRID USA AND SUBSIDIARY COMPANIES
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

NOTE A - SIGNIFICANT ACCOUNTING POLICIES

1. Nature of Operations

National Grid USA (referred to in the Notes to the Consolidated Financial Statements as the Company, NGUSA, we, us, and our) is a public utility holding company with regulated subsidiaries engaged in the transmission, distribution, and sale of both electricity and natural gas. The Company is a wholly owned subsidiary of National Grid plc (the Parent).

On August 24, 2007, the Company acquired KeySpan Corporation (KeySpan and the KeySpan Acquisition) including its subsidiaries and its service companies (see Note L –Acquisitions). The Company's electricity and gas distribution subsidiaries now serve over six million customers in New York State, Massachusetts, Rhode Island and New Hampshire. The Company's New England subsidiaries include: New England Power Company (NEP), The Narragansett Electric Company (Narragansett), Massachusetts Electric Company (Mass Electric), Nantucket Electric Company (Nantucket Electric), Granite State Electric Company (Granite State), New England Hydro-Transmission Electric Company, Inc., New England Hydro-Transmission Corporation, New England Hydro Finance Company, Inc., Boston Gas Company, Colonial Gas Company, Essex Gas Company and EnergyNorth Natural Gas Inc., collectively referred to as KeySpan Energy Delivery New England (KEDNE). The Company's New York subsidiaries include: Niagara Mohawk Power Corporation (Niagara Mohawk), KeySpan Energy Delivery New York (KEDNY) and KeySpan Energy Delivery Long Island (KEDLI).

Additionally, Company subsidiaries operate the electric transmission and distribution system owned by the Long Island Lightning Company (LIPA), in Nassau and Suffolk Counties in Long Island. The Company also owns and provides capacity to and produces energy for LIPA from our generating facilities located on Long Island and manages fuel supplies for LIPA to fuel our Long Island generating facilities. These services are provided in accordance with existing long-term service contracts having remaining terms that range from one to six years and power purchase agreements having remaining terms that range from six to 20 years. On February 1, 2006, KeySpan and LIPA agreed to extend, amend and restate these contractual arrangements. (See Note N, "2006 LIPA Settlement" for a further discussion of these agreements.)

Company subsidiaries also own or lease and operate the 2,200 MW Ravenswood Facility located in Queens, New York, and the 250 MW combined-cycle Ravenswood Expansion. Collectively the Ravenswood Facility and Ravenswood Expansion are referred to as the "Ravenswood Generating Station." To finance the purchase and/or construction of the Ravenswood Generating Station, KeySpan entered into a leasing arrangement for each facility. (See Note C, "Commitments and Contingencies" for further details on the leasing arrangements.)

The NYPSC required the divestiture of the Ravenswood Generating Station as a condition for their approval of the KeySpan Acquisition. Accordingly, the Ravenswood Generating Station is reflected as discontinued operations on the Consolidated Statement of Income, Consolidated Balance Sheet and Consolidated Statement of Cash Flows. The Company has unregulated subsidiaries engaged in the construction, leasing, and ownership of telecommunications infrastructure, and in engineering and consulting services that are also classified as discontinued operations (see Note M, "Discontinued Operations").

The Company's other operating subsidiaries are primarily involved in gas production and development, underground gas storage, liquefied natural gas storage, retail electric marketing, service and maintenance of energy systems, and the development of natural gas pipelines and other energy-related projects. Additionally, the Company has an equity ownership interest in two hydro-transmission electric companies as well as a minority ownership interest in three regional nuclear generating companies that own generating facilities that have been decommissioned.

2. Basis of Presentation

The Company's accounting policies conform to generally accepted accounting principles in the United States of America (US GAAP), including accounting principles for rate-regulated entities with respect to the Company's subsidiaries engaged in the transmission and distribution of gas and electricity (regulated subsidiaries), and are in accordance with the accounting requirements and ratemaking practices of the regulatory authorities having jurisdiction (see Item 4 "Regulation").

The consolidated financial statements include the accounts of the Company and all of its wholly-owned subsidiaries and entities for which the Company has control. Investments in which the Company can exercise significant influence over the operations of the investee (generally where the Company owns 20% of the investee but not in excess of 50%) are accounted for under the equity method of accounting. All intercompany transactions and balances between consolidated subsidiaries have been eliminated in consolidation.

The results of operations for companies acquired or disposed of are included in the consolidated financial statements from the effective date of acquisition or up to date of disposal.

Upon acquisition, KeySpan aligned certain of its accounting policies with National Grid's policies. Specifically and most importantly, KeySpan adjusted certain assumptions underlying the calculations for its pension and other postretirement reserves to align those assumptions with National Grid's pension and postretirement reserve assumptions where appropriate. Additionally, KeySpan adjusted certain assumptions underlying the calculations for its environmental reserve to align those assumptions with National Grid's environmental reserve assumptions where appropriate. (See Note L "Acquisitions" for additional details on the accounting policy changes.)

3. Use of Estimates

The preparation of financial statements in conformity with US GAAP requires management to make estimates that affect the reported amounts of assets and liabilities and the disclosures of contingent assets and liabilities as of the date of the balance sheets, and revenues and expenses for the period. These estimates may differ from actual amounts if future circumstances cause a change in the assumptions used to calculate these estimates.

For the fiscal year ended March 31, 2008, the Company revised certain assumptions used to determine the reported amount of derivative liabilities. The revision was primarily due to changes in market price forecasts. The changes had the effect of reducing the derivative liability by approximately $50.3 million. The changes had no effect on the Consolidated Statements of Income for the period ending March 31, 2008 as the corresponding regulatory asset was adjusted by the same amount. See note B – "Rate and Regulatory."

4. Regulation

The Federal Energy Regulatory Commission (FERC) has jurisdiction over certain of our holding company activities, including (i) regulating certain transactions among our affiliates within our holding company system; (ii) governing the issuance, acquisition and disposition of securities and assets by certain of our public utility subsidiaries; and (iii) approving certain utility mergers and acquisitions.

Moreover, our affiliate transactions also remain subject to certain regulations of the New York Sate Public Service Commission (NYPSC), the Massachusetts Department of Public Utilities (MADPU), the New Hampshire Public Utility Commission (NHPUC) and the Rhode Island Public Utility Commission (RIPUC) in addition to FERC.

Under our holding company structure, we have no independent operations or source of income of our own and conduct all of our operations through our subsidiaries and, as a result, we depend on the earnings and cash flow of, and dividends or distributions from, our subsidiaries to provide the funds necessary to meet our debt and contractual obligations. Furthermore, a substantial portion of our consolidated assets, earnings and cash flow is derived from the operations of our regulated utility subsidiaries, whose legal authority to pay dividends or make other distributions to us is subject to regulation by state regulatory authorities, (See Note B – "Rate and Regulatory").

5. Goodwill

National Grid plc's acquisitions of the Company's subsidiaries, including the acquisitions by the Company of Eastern Utilities Associates (EUA), Niagara Mohawk, the Rhode Island gas assets of New England Gas Company and KeySpan (see Note L – "Acquisitions"), were accounted for by the purchase method, the application of which includes the recognition of goodwill. Goodwill was approximately $7.3 billion and $3.3 billion at March 31, 2008 and 2007, respectively. In accordance with the Financial Accounting Standards Board (FASB) Statement of Financial Accounting Standards (SFAS) No. 142, "Goodwill and Other Intangible Assets," the Company reviews its goodwill annually for impairment and whenever indicators of impairment are present. The Company utilized a discounted cash flow approach incorporating its most recent business plan forecasts in the performance of the annual goodwill impairment test. The result of the annual analysis determined that no impairment adjustment to goodwill carrying value was required.

During fiscal year 2008, goodwill increased by approximately $4.0 billion, primarily related to the KeySpan Acquisition. Additionally, the Company recorded an adjustment to goodwill during the current fiscal year of $49.5 million upon adoption of Financial Accounting Standards Board (FASB) Interpretation No. 48 (FIN 48), "Accounting for Uncertainty in Income Taxes – an interpretation of FASB Statement No. 109,", related to the pre-merger period in fiscal year 2008. See Note G – "Income Taxes". During fiscal year 2007, goodwill increased by approximately $262 million. This amount primarily related to (i) an increase to Narragansett goodwill of $236 million due to the acquisition of the Rhode Island gas assets from Southern Union Company and

(ii) an increase to Niagara Mohawk of $26 million due to an adjustment related to a tax contingency.

6. Revenue Recognition

Electric and Gas Utility Services: The Company's regulated subsidiaries charge customers for electric and gas service in accordance with rates approved by FERC and the applicable state regulatory commissions.

The Company's distribution subsidiaries follow the policy of accruing the estimated amount of base rate revenues for electricity and gas delivered but not yet billed (unbilled revenues), to match costs and revenues. The unbilled revenue included in accounts receivable at March 31, 2008 and 2007 was approximately $941.2 million and $351 million, respectively. The distribution subsidiaries record revenues in amounts management believes to be recoverable pursuant to provisions of approved settlement agreements and state legislation. The distribution subsidiaries normalize the difference between revenue and expenses from energy conservation programs, commodity purchases, transmission service and contract termination charges.

KEDNY, KEDLI, Niagara Mohawk and Narragansett gas utility tariffs contain weather normalization adjustments that largely offset shortfalls or excesses of firm net revenues (revenues less gas costs and revenue taxes) during a heating season due to variations from normal weather. Revenues are adjusted each month the clause is in effect. Gas utility rate structures for the other gas distribution subsidiaries contain no weather normalization feature; therefore their net revenues are subject to weather related demand fluctuations. As a result, fluctuations from normal weather may have a significant positive or negative effect on the results of these operations. To mitigate the effect of fluctuations from normal weather on our financial position and cash flows, we may enter into weather related derivative instruments from time to time. (See Note E, "Derivative Contracts and Hedging Activities" for additional information on these derivatives.)

LIPA Agreements**:** In 1998, KeySpan and LIPA entered into three major long-term service agreements that (i) provide to LIPA all operation, maintenance and construction services and significant administrative services relating to the Long Island electric transmission and distribution (T&D) System pursuant to the Management Services Agreement (the "1998 MSA"); (ii) supply LIPA with electric generating capacity, energy conversion and ancillary services from our Long Island generating units pursuant to the Power Supply Agreement (the "1998 PSA"); and (iii) manage all aspects of the fuel supply for our Long Island generating facilities, as well as all aspects of the capacity and energy owned by or under contract to LIPA pursuant to the Energy Management Agreement (the "1998 EMA"). The 1998 MSA, 1998 PSA and 1998 EMA all are collectively referred to as the "1998 LIPA Agreements".

On February 1, 2006, KeySpan and LIPA entered into (i) an amended and restated Management Services Agreement (the "2006 MSA"), pursuant to which KeySpan will continue to operate and maintain the electric T&D System owned by LIPA on Long Island; (ii) a new Option and Purchase and Sale Agreement (the "2006 Option Agreement"), to replace the Generation Purchase Rights Agreement (as amended, the "GPRA"), pursuant to which LIPA had the option, through December 15, 2005, to effectively acquire substantially all of the electric generating facilities owned by KeySpan on Long Island; and (iii) a Settlement Agreement (the "2006 Settlement Agreement") resolving outstanding issues between the parties regarding the 1998

LIPA Agreements. The 2006 MSA, the 2006 Option Agreement and the 2006 Settlement Agreement are collectively referred to herein as the "2006 LIPA Agreements." The applicable rate components of each of the 2006 LIPA agreements became effective retroactive to January 1, 2006 upon receipt of all the required governmental approvals in 2007. (See Note N, "2006 LIPA Settlement "for additional details on these agreements).

The Company's compensation for managing the electric transmission and distribution system owned by LIPA under the 2006 MSA consists of two components: a minimum compensation component of $224 million per year and a variable component based on electric sales. The $224 million component will remain unchanged for three years and then increase annually by 1.7%, plus inflation. The variable component, which will comprise no more than 20% of KeySpan's compensation, is based on electric sales on Long Island exceeding a base amount of 16,558 gigawatt hours, increasing by 1.7% in each year. Above that level, the Company will receive approximately 1.34 cents per kilowatt hour for the first contract year, 1.29 cents per kilowatt hour in the second contract year (plus an annual inflation adjustment), 1.24 cents per kilowatt hour in the third contract year (plus an annual inflation adjustment), with the per kilowatt hour rate thereafter adjusted annually by inflation.

In addition, the Company sells to LIPA under the 1998 PSA all of the capacity and, to the extent requested, energy conversion services from its existing Long Island based oil and gas-fired generating plants. Sales of capacity and energy conversion services are made under rates approved by the FERC. Rates charged to LIPA include a fixed and variable component. The variable component is billed to LIPA on a monthly per megawatt hour basis and is dependent on the number of megawatt hours dispatched. The 1998 PSA provides incentives and penalties that can total $4 million annually for the maintenance of the output capability and the efficiency of the generating facilities.

Pursuant to the 1998 EMA, the Company (i) procures and manages fuel supplies for LIPA to fuel KeySpan's Long Island based generating facilities acquired from LILCO in 1998; (ii) performs off-system capacity and energy purchases on a least-cost basis to meet LIPA's needs; and (iii) makes off-system sales of output from the Long Island based generating facilities and other power supplies either owned or under contract to LIPA. In exchange for these services we earn an annual fee of $1.5 million. LIPA is entitled to two-thirds of the profit from any off-system energy sales arranged by us. In addition, the 1998 EMA provides incentives and penalties that can total $5 million annually for performance related to fuel purchases and off-system power purchases. The original term for the fuel supply service described in (i) is 15 years, expiring May 28, 2013 and the original term for the off-system purchases and sales services described in (ii) and (iii), collectively, "Power Supply Management Services" was eight years, expiring May 28, 2006. The term for the Power Supply Management Services has been extended several times, most recently in 2007 when the parties amended the EMA to extend the term for such services until December 31, 2009, provided that LIPA shall have the right to terminate the Power Supply Management Services at any time upon 60 days prior notice.

In October 2007, LIPA issued a Request for Proposal (RFP) to provide Power Supply Management Services commencing in October 2009. National Grid submitted a bid in response to the RFP. On June 26, 2008, LIPA announced that it had selected another bidder to provide these serves effective October 1, 2009. The Company will continue to supply fuel procurement services under the EMA. The loss of the Power Supply Management Services is not expected to have a material impact to the Company's results of operations or cash flows.

7. Property, Plant and Equipment

Property, plant and equipment is stated at original cost for property acquired prior to the KeySpan Acquisition. Property, plant and equipment related to KeySpan and its subsidiaries is stated at original cost less accumulated depreciation up to the date of acquisition. Accumulated depreciation for KeySpan and its subsidiaries reflects additions to the reserve balance from the date KeySpan was acquired. The cost of additions to utility plant and replacements of retired units of property are capitalized. Costs include direct material, labor, overhead and allowance for funds used during construction (AFUDC) (see Item 8 "AFUDC" below). 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.

	At March 31,	
(in millions of dollars)	**2008**	2007
Property Plant and Equipment		
Electric plant	**$ 12,853.8**	$ 11,519.0
Gas plant	**8,195.2**	2,145.4
Common and other plant	**720.5**	358.1
Construction work-in-process	**527.6**	259.8
Total utility plant	**22,297.1**	14,282.3
Less: accumulated depreciation and amortization	**(4,924.0)**	(4,593.1)
Net property plant and equipment	**17,373.1**	9,689.2
Gas production	**39.1**	-
Less: depletion	**(2.0)**	-
Net gas production plant	**37.1**	-
Total Plant	**$ 17,410.2**	$ 9,689.2

8. AFUDC

The Company capitalizes AFUDC as part of construction costs in amounts equivalent to the cost of funds devoted to plant under construction for its regulated businesses. AFUDC represents the composite interest and equity costs of capital funds used to finance that portion of construction costs not yet eligible for inclusion in rate base. AFUDC is capitalized in "Utility plant" with offsetting cash credits to "Other interest" and non-cash credits to "Other income (deductions), net." This method is in accordance with established rate-making practices under which our utility subsidiaries are permitted to earn a return on, and the recovery of, prudently incurred capital costs through their ultimate inclusion in rate base and in the provision for depreciation. AFUDC rates vary by Company and regulatory jurisdiction.

Capitalized interest for the year ended 2008 and 2007 was $9.1 million and $11.8 million respectively and is reflected as a reduction to interest expense.

9. Depreciation and Amortization

Depreciation expense is determined using the straight-line method. The depreciation rates for the Company's gas and electric subsidiaries are based on periodic studies of the estimated useful lives of the assets and the estimated cost to remove them net of salvage value. The Company's gas and electric subsidiaries use composite depreciation rates that are approved by the respective federal and state utility commissions. The provision for depreciation as a percentage of weighted average depreciable property (excluding construction work-in-progress) was 3.20 percent and 3.03 percent for the fiscal years ended March 31, 2008 and 2007, respectively.

Regulatory assets, including those covered by contract termination charges, are amortized in accordance with the provisions of the regulated subsidiaries' rate settlement agreements and, therefore, are not necessarily amortized on a straight-line basis. NEP and Niagara Mohawk had deferred certain costs related to deregulation, including purchased power contract buyouts, and losses on the sale of generation assets as a regulatory asset (See Note B – "Rates and Regulatory"). Niagara Mohawk's costs are being amortized unevenly over ten years with larger amounts being amortized in the latter years, consistent with projected recovery through rates.

We also had $1.2 billion of other property at March 31, 2008, consisting of $527.6 million of construction work in progress with the remaining assets held by our corporate service subsidiary and our non regulated subsidiaries. These assets consist largely of land, buildings, office equipment, furniture, vehicles, computer and telecommunications equipment and systems. These assets have depreciable lives ranging from 3 to 40 years. We allocate the carrying cost of corporate service assets to our operating subsidiaries.

10. Cash Equivalents
The Company classifies short-term investments with an original maturity of three months or less as cash equivalents.

11. Restricted Cash
Restricted cash consists of margin accounts for commodity and interest rate hedging activity, health care claims deposits, New York State Department of Conservation securitization for certain site cleanup, and workers' compensation premium deposits.

12. Federal and State Income Taxes
Federal and State income taxes are recorded under the provisions of SFAS No. 109 "Accounting for 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. Effective April 1, 2007, the Company implemented FASB issued FIN 48 "Accounting for Uncertainty in Income Taxes – an interpretation of FASB No. 109" which applies to all income tax positions reflected on the Company's Consolidated Balance Sheet that have been included in previous tax returns or are expected to be included in future tax returns. FIN 48 addresses the methodology to be used prospectively in recognizing related interest and penalties. See Note G – "Income Taxes" for the impact of the adoption of FIN 48.

13. Derivatives
From time to time, we employ derivative instruments to hedge a portion of our exposure to commodity price risk, interest rate risk and weather fluctuations. Prior to January 1, 2008, KeySpan employed derivative financial instruments to hedge cash flow variability associated with a portion of its peak electric energy sales. Whenever hedge positions are in effect, we are exposed to credit risk in the event of nonperformance by counter-parties to derivative contracts, as well as nonperformance by the counter-parties of the transactions against which they are

hedged. We believe that the credit risk related to the futures, options and swap instruments is no greater than that associated with the primary commodity contracts which they hedge.

Financially-Settled Commodity Derivative Instruments. We employ derivative financial instruments, such as futures, options and swaps, for the purpose of hedging the cash flow variability associated with forecasted purchases and sales of various energy-related commodities. All such derivative instruments are accounted for pursuant to the requirements of SFAS 133 "Accounting for Derivative Instruments and Hedging Activities," as amended by SFAS 149, "Amendment of Statement 133 Derivative Instruments and Hedging Activities" (collectively, SFAS 133). With respect to those commodity derivative instruments that are designated and accounted for as cash flow hedges, the effective portion of periodic changes in the fair market value of cash flow hedges is recorded as accumulated other comprehensive income on the Consolidated Balance Sheet, while the ineffective portion of such changes in fair value is recognized in earnings. Unrealized gains and losses (on such cash flow hedges) that are recorded as accumulated other comprehensive income are subsequently reclassified into earnings concurrent when hedged transactions impact earnings. With respect to those commodity derivative instruments that are not designated as hedging instruments, such derivatives are accounted for on the Consolidated Balance Sheet at fair value, with all changes in fair value reported in earnings.

Firm Gas Sales Derivatives Instruments – Regulated Utilities. We use derivative financial instruments to reduce cash flow variability associated with the purchase price for a portion of future natural gas purchases associated with our gas distribution operations. Our strategy is to minimize fluctuations in firm gas sales prices to our regulated firm gas sales customers in our service territories. The accounting for these derivative instruments is subject to SFAS 71, "Accounting for Certain Types of Regulation". Therefore, the fair value of these derivatives is recorded as current or deferred assets and liabilities, with offsetting positions recorded as regulatory assets and regulatory liabilities on the Consolidated Balance Sheet. Gains or losses on the settlement of these contracts are initially deferred and then refunded to or collected from our firm gas sales customers consistent with regulatory requirements.

Physically-Settled Commodity Derivative Instruments. Certain of our contracts for the physical purchase of natural gas and certain power supply contracts were assessed as no longer being exempt from the requirements of SFAS 133 as normal purchases. As such, these contracts are recorded on the Consolidated Balance Sheet at fair market value. However, since such contracts were executed for regulated utility customers, and pursuant to the requirements of SFAS 71, changes in the fair market value of these contracts are recorded as a regulatory asset or regulatory liability on the Consolidated Balance Sheet.

Weather Derivatives. The utility tariffs associated with certain of our gas distribution operations do not contain weather normalization adjustments. As a result, fluctuations from normal weather may have a significant positive or negative effect on the results of these operations. To mitigate the effect of fluctuations from normal weather on our financial position and cash flows, we may enter into derivative instruments from time to time. Based on the terms of the contracts, we account for these instruments pursuant to the requirements of Emerging Issues Task Force ("EITF") 99-2 "Accounting for Weather Derivatives." In this regard, we account for weather derivatives using the "intrinsic value method" as set forth in such guidance.

Interest Rate Derivative Instruments. We continually assess the cost relationship between fixed and variable rate debt. Consistent with our objective to minimize our cost of capital, we periodically enter into hedging transactions that effectively convert the terms of underlying debt obligations from fixed to variable or variable to fixed. Payments made or received on these derivative contracts are recognized as an adjustment to interest expense as incurred. Hedging transactions that effectively convert the terms of underlying debt obligations from fixed to variable are designated and accounted for as fair-value hedges pursuant to the requirements of SFAS 133. Hedging transactions that effectively convert the terms of underlying debt obligations from variable to fixed are considered cash flow hedges.

14. Comprehensive Income

Comprehensive income 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 is reported as net income or loss, the other components of comprehensive income relate to changes in SFAS No. 158, "Employers' Accounting for Defined Benefit Pension and Postretirement Plans," deferred gains and losses associated with hedging activity, and unrealized gains and losses associated with certain investments held as available for sale (see Note D – "Accumulated Other Comprehensive Income (Loss)").

15. Recent Accounting Pronouncements

In March 2008, the Financial Accounting Standards Board (FASB) issued SFAS 161 "Disclosures about Derivative Instruments and Hedging Activities." This Statement amends and expands the disclosure requirements of SFAS 133 with the intent to provide users of financial statements with an enhanced understanding of (a) how and why an entity uses derivative instruments; (b) how derivative instruments and related hedged items are accounted for; and (c) how derivative instruments and related hedged items affect an entity's financial position, financial performance and cash flows. This Statement requires qualitative disclosures about objectives and strategies for using derivatives, quantitative disclosures about fair value amounts of and gains and losses of derivative instruments and disclosures about credit-risk-related contingent features in derivative agreements. This Statement shall be effective for financial statements issued for fiscal years and interim periods beginning after November 15, 2008. This Statement will have no impact on results of operations, financial position or cash flows, but will impact footnote disclosures.

In February 2007, the FASB issued SFAS 159 "The Fair Value Option for Financial Assets and Financial Liabilities." This statement permits entities to choose to measure many financial instruments and certain other items at fair value that are not currently required to be measured at fair value. The objective is to improve financial reporting by providing entities with the opportunity to mitigate volatility in reported earnings caused by measuring related assets and liabilities differently without having to apply complex hedge accounting provisions. This statement requires a business entity to report unrealized gains and losses on items for which the fair value option has been elected in earnings at each subsequent reporting date. An entity may decide whether to elect the fair value option for each eligible item on its election date, subject to certain requirements described in the statement. This statement shall be effective as of the beginning of each reporting entity's first fiscal year that begins after November 15, 2007. The Company has not elected the fair value method.

In December 2007, the FASB issued SFAS 141R "Business Combinations." The objective of SFAS 141R is to improve the relevance and comparability of the financial information that a reporting entity provides in its financial reports about a business combination and its effects. This Statement establishes principles and requirements for how the acquirer recognizes and measures the identifiable assets acquired, the liabilities assumed and any noncontrolling interest in the acquiree; recognizes and measures the goodwill acquired in business combination; and determines what information to disclose. This Statement shall be applied prospectively to business combinations for which the acquisition date is on or after the beginning of the first annual reporting period beginning on or after December 15, 2008. This Statement has no impact on the Company's current results of operations, cash flows or financial position.

In December 2007, the FASB issued SFAS 160 "Noncontrolling Interests in Consolidated Financial Statements – an amendment of Accounting Research Bulletin 51 "Consolidated Financial Statements." The objective of SFAS 160 is to improve the relevance, comparability and transparency of the financial information that a reporting entity provides in its consolidated financial statements by establishing accounting and reporting standards for the noncontrolling interest in a subsidiary and for the deconsolidation of a subsidiary. SFAS 160 shall be effective for fiscal years and interim periods within those fiscal years, beginning on or after December 15, 2008. The Company is currently reviewing the requirements of SFAS 160, and at this point in time cannot determine what impact, if any, SFAS 160 will have on its results of operations, cash flows or financial position.

On September 15, 2006, the FASB issued SFAS 157 "Fair Value Measurements." This statement defines fair value, establishes a framework for measuring fair value in generally accepted accounting principles and expands disclosures about fair value. SFAS 157 expands the disclosures about the use of fair value to measure assets and liabilities in interim and annual periods subsequent to initial recognition. The disclosures focus on the inputs used to measure fair value, the recurring fair value measurements using significant unobservable inputs and the effect of the measurement on earnings (or changes in net assets) for the period. The guidance in SFAS 157 also applies for derivatives and other financial instruments measured at fair value under Statement 133 "Accounting for Derivative Instruments and Hedging Activities" at initial recognition and in all subsequent periods. This Statement is effective for fiscal years beginning after November 15, 2007, and interim periods within those fiscal years. The Company is currently reviewing the requirements of SFAS 157, and at this point in time cannot determine what impact, if any, SFAS 157 will have on its results of operations or financial position. This Statement will have no impact on cash flow.

16. Reclassifications

Certain amounts from prior years have been reclassified on the accompanying consolidated financial statements to conform to the fiscal 2008 presentation.

In the fiscal year 2007 financial statements, the adoption of SFAS No. 158 was presented as activity during the fiscal year and therefore was included in comprehensive income (loss). However, it should have been reported as a direct reduction of accumulated other comprehensive income (loss) in the changes in equity accounts disclosed as an adjustment in the reporting period and excluded from comprehensive income (loss). The amount incorrectly recorded to comprehensive income (loss) was $398 million. The March 31, 2007 accumulated other comprehensive income (loss) balance reported in the fiscal year 2007 financial statements was properly stated. See Note D – "Accumulated Other Comprehensive Income (Loss)".

17. Other Property and Investments

Certain subsidiaries own as their principal assets, investments (including goodwill), representing ownership interests of 50% or less in energy-related businesses that are accounted for under the equity method. None of these current investments are publicly traded. Additionally, the Company has corporate assets recorded on the Consolidated Balance Sheet - other property and investments, representing funds designated for Supplemental Executive Retirement Plans. These funds are primarily invested in corporate owned life insurance policies. The Company records changes in the value of these assets in accordance with SFAS Technical Bulletin 85-4 "Accounting for the Purchase of Life Insurance." As such, increases and decreases in the value of these assets are recorded through earnings in the Consolidated Statement of Income - other income and (deductions) concurrent with the change in the value of the underlying assets.

18. Pension and Other Postretirement benefits

The Company adopted the provisions of SFAS 158 "Employers' Accounting for Defined Benefit Pensions and Other Postretirement Benefit Plans, an amendment of FASB Statements No. 87, 88, 106 and 132(R)" (SFAS 158) on March 31, 2007. SFAS 158 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 accumulated other comprehensive income in shareholders' equity upon implementation. As required by SFAS 158, the Company 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 F "Employee Benefits" for additional details on the Company's pension and other postretirement plans.)

NOTE B – RATE AND REGULATORY

The Company's regulated subsidiaries generally use the same accounting policies and practices for financial reporting purposes as non-regulated companies under US GAAP. However, actions by the FERC and the state utility commissions can result in accounting treatment that is different from that used by non-regulated companies. The Company applies the provisions of the SFAS No. 71, "Accounting for Certain Types of Regulation," which requires regulated entities, in appropriate circumstances, to establish regulatory assets or liabilities, and thereby defer the income statement impact of certain charges or revenues because they are expected to be collected or refunded through future customer billings.

In the event the Company determines, as a result of lower than expected revenues and (or) higher than expected costs, that its net regulatory assets are not probable of recovery, it can no longer apply the principles of SFAS No. 71. Management believes its rates are based on the Company's costs and investments and it should continue to apply the provisions of SFAS No. 71. The Company is earning a return on most of its regulatory assets under its rate agreement. If the Company could no longer apply SFAS No. 71, the resulting charge would be material to the Company's reported financial condition and results of operations.

The following table details the various categories of miscellaneous regulatory assets and liabilities:

At March 31 (in millions)	2008	2007
Regulatory assets included in accounts receivable:		
Rate adjustment mechanisms	**$ 106.8**	$ 12.7
Current portion of regulatory assets:		
Derivative and swap contracts	**76.3**	264.5
Purchase power obligations	**3.1**	10.9
Pension and post-retirement benefit plans other than pension cost	**39.6**	-
Yankee nuclear decommissioning costs and environmental response fund	**31.8**	28.6
Other	**54.1**	-
	204.9	304.0
Current portion of regulatory liabilities:		
Derivative and swap contracts	**(117.4)**	-
Rate adjustment mechanisms	**(140.2)**	(129.3)
Other	**(65.2)**	-
	(322.8)	(129.3)
Total net miscellaneous regulatory assets (liabilities) current	**(11.1)**	187.4
Regulatory assets:		
Stranded costs	**1,901.0**	2,273.2
Purchase power obligations	**116.4**	119.9
Derivative and swap contracts	**147.4**	254.7
Regulatory tax asset	**162.8**	139.8
Deferred environmental restoration costs	**1,500.2**	633.6
Pension and post-retirement benefit plans other than pension cost	**1,773.3**	1,248.7
Yankee nuclear decommissioning costs	**91.9**	117.4
Loss on reacquired debt	**61.5**	69.2
Long-term portion of standard offer under-recovery	**51.3**	49.9
Other	**162.5**	195.0
	5,968.3	**5,101.4**
Regulatory liabilities:		
Stranded costs and CTC related	**(131.2)**	(125.1)
Pension and post-retirement plans fair value deferred gain	**(385.7)**	(266.5)
Interest saving deferral	**(92.5)**	(92.5)
Environmental response fund and insurance recoveries	**(118.5)**	(91.3)
Storm costs reserve	**(44.1)**	(45.6)
Other	**(387.2)**	(225.6)
	(1,159.2)	(846.6)
Total net miscellaneous regulatory assets non-current	**4,809.1**	4,254.8
Net miscellaneous regulatory assets	**$ 4,798.0**	$ 4,439.9

Stranded costs:

Certain regulatory assets, referred to as stranded costs, resulted from major fundamental changes occurring in the public utility industry, most notably the divestiture of generation assets pursuant to deregulation. Under deregulation, the generation segment of the utility business was opened to competition in that consumers could choose their generation supplier. Public utilities continued to control the transmission and distribution of electricity and were encouraged to dispose of generation assets such as power plants. The net unrecovered costs from the sale of these generation assets, along with the costs to terminate, restate or amend existing purchase power contracts were deferred for recovery in rates over future periods. A large portion of these stranded costs are being recovered through a special rate being charged to customers. Similarly, the recovery of costs outside of customer rate recovery, but that nevertheless relate to the former generation business, are credited back to customers as well to offset stranded costs. This mechanism is called the Contract Termination Charge and (or) the Competitive Transition Charge (in both cases, these charges are called the CTC).

Management believes that future cash flows from charges for electric service under existing rate plans, including the CTC, will be sufficient to recover the Company's electric regulatory assets over the planned amortization period. This assumes that there will be no unforeseen reduction in demand and no bypass of the CTC or exit fees. In the event that revenues are lower than expected and (or) are higher than expected, the Company may determine that its net regulatory assets are not probable of recovery and that it can no longer apply the principles of SFAS No. 71. In that case, an after-tax, non-cash charge against income for any remaining unamortized regulatory assets and liabilities could be required. If the Company's subsidiaries could no longer apply SFAS No. 71, the resulting charge would be material to the Company's reported financial condition and results of operations.

Rate Agreements:

NEP

New England Regional Transmission Organization (RTO) and Rate Filing: On October 31, 2006, FERC issued an order establishing the return on common equity (ROE) for the New England Transmission Owners (NETOs), including NEP. In this order, FERC overturned the Administrative Law Judge's initial decision and approved, over the dissent of two Commissioners, the proposed 1.0 percent ROE adder for all new transmission investment approved through the regional system planning process as an incentive to build new transmission infrastructure. The resulting ROE varied depending on whether costs are recovered through Regional Network Service (RNS) rates or local network service (LNS) rates, and whether the costs are for existing or new facilities. For the locked-in period (February 2005 to October 2006), the resulting ROEs were 10.7 percent (including a 0.5 percent RTO participation adder) for recovery of existing transmission costs through RNS rates; 11.7 percent (including 0.5 percent and 1.0 percent adders) for new transmission costs recovered through RNS; and 10.2 percent (base ROE only) for LNS. For the prospective period beginning November 1, 2006, those ROEs increased to 11.4 percent, 12.4 percent and 10.9 percent respectively as a result of a FERC adjustment to reflect updated bond data. Overall, the ROEs approved by FERC represent an increase from NEP's last authorized ROE of 10.25 percent.

The NETOs and opposing parties to the NETOs requested rehearing of various aspects of the Commission's order. On March 24, 2008, FERC issued an order on rehearing increasing NEP's base ROE for all classes of transmission plant by 24 basis points retroactive to February 1, 2005. The Commission also limited the 1.0 percent ROE adder it had previously granted for new transmission investment approved under the regional system planning process so that it only applies to new transmission plant placed in service on or before December 31, 2008. The Commission's order also indicated that any future transmission investment incentives after 2008 must be sought through initiating an incentive proposal under Section 205 of the Federal Power Act pursuant to the Commission's Order No. 679 Transmission Pricing Policy.

Niagara Mohawk

Deferral Audit:

Under its Merger Rate Plan (MRP) Niagara Mohawk is authorized to recover actual amounts deferred under the plan for each two-year period, as well as deferrals projected to accrue over the subsequent two-year period that are in excess of a $100 million threshold. The deferrals are subject to regulatory review and approval. On July 29, 2005, Niagara Mohawk made its biannual deferral account recovery filing for balances in the deferral account as of June 30, 2005 plus projected deferrals. The Staff of the NYPSC (the Staff) filed testimony on August 2, 2006, proposing in excess of $200 million of initial adjustments to the deferral balance and projected deferrals. After replies from the Staff and Niagara Mohawk, an evidentiary hearing was held on October 5, 2006. Upon the conclusion of the evidentiary hearings, Niagara Mohawk and the Staff agreed to enter into non-binding mediation discussions before an administrative law judge from the NYPSC in an attempt to resolve some or all of the amounts remaining in dispute.

Through the mediation process, Niagara Mohawk, the Staff, and Multiple Intervenors (Parties), reached a resolution of the disputed issues presented in the deferral account case as well as other cases pending before the Commission regarding pension costs, the costs of enhanced inspections of the transmission and distribution system, and the sale of the Nine Mile Point nuclear generating facilities. A Stipulation of the Parties (Stipulation) setting forth the resolution of these issues was executed and filed with the Commission on March 23, 2007. A hearing on the Stipulation was held before the NYPSC's administrative law judge on May 17, 2007.

Under the Stipulation, Niagara Mohawk had agreed to a net reduction of the deferral account balance of approximately $127 million. This includes reclassifications from the deferral account to other balance sheet accounts of approximately $64 million. It also includes a reduction to the deferral account balance as of February 28, 2007 and decrease to earnings before income taxes of approximately $63 million.

Third CTC reset and Deferral Account Filings:

The biannual deferral account filing included in the third CTC reset was made on August 1, 2007 for deferral balances as of June 30, 2007 and projected deferrals through December 31, 2009. Any differences in the final deferral from balances authorized to be reflected in rates and the approved recovery level would be reflected in the next CTC reset filing and resulting rates to customers that take effect after 2009. A NYPSC order establishing the amount of deferral account recovery that will be reflected in the rates during 2008-2009 was approved on December 17, 2007 at $124 million per calendar year. This represents a reduction in rates charged to customers of $76 million per year from the $200 million per year previously being collected under rates approved in the second CTC reset proceeding.

On October 22, 2007, Niagara Mohawk made a compliance filing with the NYPSC regarding the implementation of the Follow-on Merger Credit associated with the KeySpan Acquisition. In its compliance filing, Niagara Mohawk calculated the share of the KeySpan Follow-on Merger savings allocable to Niagara Mohawk for the period from September 2007 through December 2011 to be approximately $40 million. Niagara Mohawk subsequently agreed, in its comments filed in the Third CTC Reset proceeding on October 31, 2007, to adjust rates submitted in its August 1, 2007 CTC Reset filing to reflect a proposal by the parties in that proceeding to accelerate the KeySpan Follow-on Merger Credit allocable to Niagara Mohawk's electric customers. This proposal was approved by the NYPSC in December 2007 and has resulted in a credit being applied for the benefit of electric customers over the next two years equal to the net present value of the KeySpan Follow-on Merger Credit that otherwise would have been credited to Niagara Mohawk electric customers over the four remaining years of the MRP. On May 29, 2008, however, the PSC issued its decision with respect to Niagara Mohawk's October 22, 2007 compliance filing rejecting Niagara Mohawk's proposed amount and requiring a Follow-on Merger Credit of $52 million for the August 24, 2007 through December 2011 period. Niagara Mohawk has submitted a letter to the NYPSC stating that it intends to seek rehearing of the order. The NYPSC has also issued a notice on June 25, 2008 seeking additional comment on two Follow-on Merger savings issues that were not addressed in the compliance filing. In the notice, the Commission asked for comments on a Staff position that Niagara Mohawk should be crediting an additional $35 million of synergy savings to electric and gas customers. Niagara Mohawk disagrees with the Staff position. On June 30, 2008, Niagara Mohawk filed a petition for rehearing of the May 29, 2008 order from the NYPSC.

Service Quality Penalties:
In connection with its Merger Rate Plan (MRP), Niagara Mohawk is subject to maintaining certain service quality standards. Service quality measures focus on eleven categories including safety targets related to gas operations, electric reliability measures related to outages, residential and business customer satisfaction, meter reads, customer call response times, and administration of the Low-Income Customer Assistance Program. If a prescribed standard is not satisfied, Niagara Mohawk may incur a penalty, with the penalty amount applied as a credit or refund to customers.

The MRP includes provisions related to frequency and duration of outages that causes the annual $4.4 million penalty associated with these standards to be doubled under certain circumstances when penalties have been incurred in the current year and two of the last four years. In calendar year 2006, Niagara Mohawk incurred a $4.4 million penalty related to outage frequency, which it recorded in fiscal year 2007. Similar penalties were incurred in the two prior years. Based on this performance and consistent with the terms of the MRP, the NYPSC on November 7, 2007 doubled the 2006 penalty associated with outage frequency to $8.8 million per year. In September 2007, the Commission also modified the MRP, in the context of the KeySpan Acquisition proceeding, to add an additional incremental $4.4 million penalty exposure for each consecutive year Niagara Mohawk misses the target for a doubled penalty. This additional incremental penalty exposure resulted in a $13.2 million penalty for missing the outage frequency target for 2007.

Niagara Mohawk has recorded service quality penalty expenses of $14.2 million and $10.9 million for the twelve months ended March 31, 2008 and 2007, respectively.

Niagara Mohawk filed with the NYPSC on October 26, 2007 to implement an automated outage management system and to recalibrate its targets relating to the frequency and duration of outages. The recalibration is intended to allow for a transition to the new outage management system in a performance neutral manner.

Asset Condition and Capital Investment Plan:
On October 22, 2007, Niagara Mohawk filed with the NYPSC reports on its asset condition and capital investment plan for its electric transmission and distribution system. Niagara Mohawk's plan involves significant investment in capital improvements over the projections initially

included in its MRP. In the order approving the KeySpan Acquisition, the NYPSC found that the rate impacts associated with certain incremental investments during the remaining period of the MRP would be limited to 50 percent of the total rate impact as ultimately determined by the NYPSC.

On December 21, 2007, Niagara Mohawk filed with the NYPSC a Petition for Special Ratemaking seeking authorization to defer for later rate recovery 50 percent of the revenue requirement impact during calendar year 2008 of specified capital programs and operating expenses that are directly associated with these programs. The amount of the requested deferral is projected to be approximately $5.2 million in calendar year 2008. At a Commission meeting on July 16, 2008, the NYPSC agreed to adopt a staff recommendation finding that Niagara Mohawk's deferral request qualifies for deferral under the MRP. However, the Commission also agreed with the staff that the petition was premature and decided that Niagara Mohawk should supplement its petition with actual expense information once results for 2008 become known. Niagara Mohawk will be required to show in its supplemental filing that it will not over earn in 2008 after the deferrals are allowed, the expenditure on which the deferrals are based on incremental to what was reflected in the MRP forecast, such expenditures have been offset by all relevant cost savings and related benefits, and to the extent that actual expenditures for 2008 differ from amounts in the budgets that were previously filed with the Commission, that Niagara Mohawk identify and explain the basis for such differences. Niagara Mohawk plans to request deferral recovery of 50 percent or more of the annual revenue requirement associated with certain capital investments and associated operating expenses through the end of 2011 at a later date.

Financial Protections:
Niagara Mohawk made a filing on November 19, 2007 proposing certain financial protections for Niagara Mohawk as required by the NYPSC in the order approving the KeySpan Acquisition and made an additional filing with the NYPSC regarding these protections. The NYPSC adopted the protections in March 2008 which provide, among other things, for restrictions on the payment of common dividends if certain credit ratings are not maintained by Niagara Mohawk or National Grid plc; credits to Niagara Mohawk's deferral account of any incremental increase in interest expense due to a decline in Niagara Mohawk's bond rating; a prohibition with respect to certain types of cross-default provisions; and the implementation of a class of preferred stock having one share (the Golden Share), subordinate to any existing preferred stock, that would have voting rights which limit Niagara Mohawk's right to commence any voluntary bankruptcy, liquidation, receivership or similar proceeding without the consent of such share of stock. Niagara Mohawk committed to seek authority from the NYPSC to establish the Golden Share within six weeks of the NYPSC's approval of the petition of KEDNY and KEDLI for the establishment of each of their respective Golden Shares which was also required by the NYPSC.

On January 31, 2008, Moody's Investors Service said it has changed the outlook for National Grid plc and its subsidiaries, including Niagara Mohawk, to negative from stable following National Grid plc's announcement that it will increase its dividend for 2007-08 by 15 percent.

Rate Plan Filing:

Niagara Mohawk

Niagara Mohawk filed with the PSC on May 23, 2008 for a $95 million rate increase in natural gas delivery rates. This filing would represent the first delivery rate increase since 1996. The filing includes a revenue decoupling proposal, a gas marketing program, a new rate for low-income customers and expanded capital infrastructure investments. The proposed $95 million rate increase would include recovery of $11 million of costs associated with an energy efficiency program proposal filed recently. The filing further reflects an 11 percent return on equity and a 50 percent debt and 50 percent equity capital structure. A decision is expected by the NYPSC in May 2009 at which point new rates would become effective, if approved.

The Narragansett Electric Company

Electric segment: In September 2004, the Rhode Island Public Utility Commission approved a rate plan that reduced annual distribution rates effective November 1, 2004 by $10.2 million and froze them at that level through 2009. From 2005 through 2009, the Company will keep 100 percent of its earnings up to an allowed return on equity of 10.5 percent, plus $4.65 million (pre-tax), which represents its share of demonstrated savings under the rate plan. Earnings above that amount up to an 11.5 percent return on equity are to be shared equally between the Company and its customers, while earnings above an 11.5 percent return on equity will be allocated 75 percent to customers and 25 percent to the Company.

Gas segment: In fiscal year 2007 (August 2006), National Grid completed the acquisition of the Rhode Island gas assets of New England Gas Company. Pursuant to the Rhode Island Public Utility Commission order approving the acquisition, Narragansett and its parent agreed to honor the provisions of the former New England Gas Company Rate Settlement and committed to file a new rate plan with the Rhode Island Public Utility Commission. On April 1, 2008, Narragansett submitted its new rate plan which included, among other things, a requested $20 million increase in distribution rates, including a return on equity of 11.50 percent, and proposals for revenue decoupling, an accelerated capital investment and recovery mechanism, low income distribution rates and sharing of merger related savings between customers and Narragansett. The submission also included an alternative three year rate plan which replaces the initial $20 million rate increase with annual increases of $13.8 million in each of the three years of the plan and includes other capital investment commitments by the Company. A decision on the April 1st submission is expected in the third quarter of fiscal year 2009.

KeySpan

On August 22, 2007, the NYPSC unanimously voted to approve the KeySpan Acquisition by National Grid plc. The NYPSC issued an abbreviated order and a long-form order on August 23, 2007 and September 17, 2007, respectively, authorizing the KeySpan Acquisition subject to conditions and setting partial revenue requirements for KEDNY and KEDLI ("the Order"). In addition, KEDNY and KEDLI reached an agreement in principle with the Staff of the NYPSC and other parties related to gas rates for KEDNY and KEDLI and on October 10, 2007 the Gas Rates Joint Proposal ("the Rates JP") was filed with the NYPSC for approval. The Rates JP was approved at the NYPSC session on December 21, 2007. Below is a discussion of the more significant aspects of the Order and the Rates JP.

The Order

The Order sets out conditions for the KeySpan Acquisition, upon which the NYPSC's approval is based. These conditions, relate to, among other things, financial protections for customers; potential revenue adjustments that are based on safety, reliability and customer service performance measures; and requirements concerning the sale of the Ravenswood Generating Station. The Order also makes some revenue requirement determinations for KEDNY and KEDLI that are discussed more fully below.

The Order includes the following restrictions and/or requirements that KEDNY and KEDLI must adhere to.

1. Goodwill, or the amount National Grid plc pays for KeySpan Corporation (together with transaction costs) in excess of the book value of the assets and liabilities of the latter and its subsidiaries, will not be reflected on the regulatory books of KEDNY or KEDLI or in the determination of KEDNY and KEDLI's rates and the calculation of their respective earned returns.

2. KEDNY and KEDLI will each be able to pay dividends in any year, provided at least two nationally and internationally recognized rating agencies give it an investment grade credit rating. The maximum dividend in any year would be (a) income available for dividends in that year, plus (b) cumulative retained earnings, plus (c) certain paid in capital.

3. KEDNY and KEDLI will each be barred from paying dividends when (a) its least secure form of debt is at the lowest investment grade and at least one rating agency has issued an outstanding negative watch or review downgrade notices, or (b) National Grid plc's least secure form of debt is rated below investment grade by one or more rating agencies.

4. If KEDNY's and KEDLI's bond rating falls below A- or A3, as determined by two nationally recognized credit rating agencies, then any long-term debt issued by the relevant company during the period of such reduced credit rating will be priced as if it had been issued by an A-/A3 utility at the same issue date, and any difference will be credited to KEDNY's or KEDLI's customers. KEDNY's and KEDLI's earnings sharing calculations will then reflect the actual debt rates outstanding for the companies.

5. KEDNY's and KEDLI's debt ratios for any 12-month period ending at the end of a fiscal quarter will not exceed 56% and 58%, respectively. If these limits are exceeded, KEDNY and KEDLI would have a nine month period to reduce their debt balance accordingly, during which the dividends paid out as a percentage of total equity may not be increased. If the stated debt ratios are not met by the end of the nine month cure period, KEDNY and/or KEDLI may not pay any dividends until the debt limits are met.

6. No debt associated with the KeySpan Acquisition will be reflected as an obligation of KEDNY or KEDLI.

7. There will be a regulated money pool in which KEDNY and KEDLI may participate as borrowers and lenders. The regulated money pool will prohibit its utility participants from directly or indirectly loaning or transferring funds borrowed from the regulated money pool to any unregulated affiliate.

8. There will be no cross-default provisions for any affiliate of National Grid plc that affect KEDNY and KEDLI.

9. KEDNY and KEDLI will establish "golden shares" to prevent a bankruptcy of any National Grid plc affiliate from necessarily triggering a bankruptcy of KEDNY and KEDLI. The holder(s) of the golden shares will be determined by the NYPSC.

In addition to the above, KEDNY and KEDLI are subject to maintaining certain service quality and reliability performance standards. KEDNY's or KEDLI's failure to meet the stated performance targets for calendar years 2008 through 2012 may result in downward revenue adjustments. The safety and reliability performance measures focus primarily on (i) minimum requirements for main and service replacement; (ii) response time for gas leak investigations; and (iii) reduction in the number of gas leaks. Failure to meet the safety and reliability performance measures can result in downward revenue adjustments of up to $7.0 million and $6.2 million for KEDNY and KEDLI, respectively. The customer services performance measures focus primarily on (i) reducing the number of customer complaints and customer bill adjustments; (ii) customer survey satisfaction ratings; and (iii) response time associated with customer telephone inquires. Failure to meet the customer service performance measures can result in downward revenue adjustments of up to $11.7 million and $9.9 million for KEDNY and KEDLI, respectively.

National Grid plc is also required, as a condition to NYPSC approval, to sell the Ravenswood Generating Station within the next three years. KeySpan has announced that it has agreed to sell KeySpan Ravenswood, LLC to TransCanada and expects to complete the transaction during the summer of 2008. Additionally, National Grid plc took steps to assure that it is financially indifferent to the price of energy in the New York City electric energy market with respect to the electric output of the Ravenswood Generating Station by entering into a single contract on January 1, 2008 to sell all the Ravenswood Generating Station's energy for the period prior to the divestiture of the Ravenswood Generating Station. Capacity and ancillary services from the Ravenswood Generating Station will continue to be bid into the market. However, commencing with the New York Independent System Operator auction for 2008, capacity for the Ravenswood Generating Station must be bid at zero or an agreed to level based solely on the marginal cost to maintain the plant in service.

The Gas Rates Joint Proposal

As noted, KEDNY and KEDLI reached an agreement with the NYPSC and other parties related to gas rates for KEDNY and KEDLI. The discussion that follows summarizes some of the more significant aspects to the Rate JP.

Under the Rates JP, KEDNY's base delivery rates will be increased $5 million annually in rate year one (beginning January 1, 2008) through rate year five. However, the increase in base delivery rates will be deferred and used to offset future increases in special franchise taxes and environmental investigation and remediation costs. KEDLI's base delivery rates will be increased by $60 million on January 1, 2008. In rate years two through five, base delivery rates for KEDLI will be increased $10 million. However, the increase in KEDLI's base delivery rates will also be deferred and used to offset future increases in special franchise taxes and environmental investigation and remediation costs. In addition, for both KEDNY and KEDLI, certain gas related costs previously recovered in base delivery rates were transferred out of base delivery rates on January 1, 2008 and are currently being recovered through the gas adjustment clause. The calculation of the revenue requirement for each company reflects a 50% - 50% sharing of net synergy savings (synergy savings less costs to achieve those synergy savings) that are estimated to be generated as a result of the merger.

As part of the Rates JP, KEDNY returned to the New York Public Service Commission's Statement of Policy for Pensions and Other Postretirement Employee Benefits (OPEB) issued in September 1993. As a result, KEDNY will reconcile its actual pension and OPEB expense to the estimated pension and OPEB expense established in the Rates JP and defer or "true-up" the difference for future recovery from or refund to its gas sales customers. KEDNY recorded a regulatory liability of approximately $128 million to return to the Statement of Policy for Pensions and Other Postretirement Employee Benefits along with a direct charge to equity. The regulatory liability will be amortized over the next five years. KEDLI has followed the Statement of Policy for Pensions and Other Postretirement Employee Benefits since it was issued.

The Rates JP also allows KEDNY to true-up 90% of the difference between actual property and special franchise taxes to the estimated amounts established in the Rates JP. However, recovery of $22.5 million of previously deferred special franchise taxes was disallowed and expensed. KEDLI is currently following this procedure. KEDLI, however, was required to record a $62 million regulatory liability associated with a Nassau County property tax litigation matter. This amount was recorded as a direct charge to equity and the regulatory liability will be amortized over five years. Additionally, both companies are permitted to continue to true-up 100% of the difference between actual environmental site and investigation costs to the estimated amounts established in the Rates JP.

The revenue requirement for both companies provide for sharing of earnings above 10.5% calculated using an equity component of 45% with gas sales customers in the following manner. Earnings between 10.5% - 12.5% are shared 50% - 50% between gas sales customers and KEDNY and KEDLI. Earnings between 12.5% - 13.5% are shared 65% to gas sales customers and the remaining 35% to KEDNY and KEDLI. Earnings in excess of 13.5% are refunded to gas sales customers.

Additionally, certain "exogenous costs" that are outside the control of KEDNY and KEDLI, may be deferred for future recovery from or refund to gas sales customers. Exogenous costs are incremental effects on KEDNY's and KEDLI's revenue requirements due to any of the following: (i) externally imposed accounting changes; (ii) any change in Federal, state or local taxes; and (iii) any legislative, court or regulatory change

Also as part of the Rates JP, the temperature controlled monthly price cap that can be charged to large volume duel-fuel temperature controlled customers was changed to an annual price cap. In our large-volume heating and other interruptible (non-firm) markets, which include large apartment houses, government buildings and schools, gas service is provided under rates that are designed to compete with prices of alternative fuel, including No. 2 and No. 6 grade heating oil. These "dual-fuel" customers can consume either natural gas or fuel oil for heating purposes. Also, based on NYPSC regulations, gas sales to some of these customers may be interrupted when the temperature falls below 15 degrees to ensure system reliability to firm gas sales customers. Under the new mechanism, effective January 1, 2008, temperature controlled prices, including the minimum charge, are subject to an annual price cap based on the commercial heating rate paid by firm gas sale customers. The Company estimates that this pricing change, under certain circumstances, could reduce consolidated earnings by $12 million.

Other Matters
On February 23, 2008, EnergyNorth Natural Gas, Inc. d/b/a/ National Grid NH filed a request with the New Hampshire Public Utilities Commission to increase distribution rates by approximately $9.9 million for its approximately 84,000 New Hampshire natural gas customers. The requested increase reflects an overall rate of return of 9.26% based on an 11.5% return on common equity and a 50/50 imputed capital structure as stipulated in the Merger Settlement Agreement and approved in Docket DG 06-122.

Contemporaneous with the request for permanent rates, the Company also filed a request for temporary rates designed to produce a temporary rate increase of approximately $6.6 million in annual revenues to be effective with service rendered on and after August 24, 2008 and remain in effect until a determination of the Company's request for permanent rates. The EnergyNorth Merger Rate Agreement, which was approved by the Commission in Order No. 24,277 in Docket DG 06-107 as part of its authorization of the KeySpan Acquisition, contemplated that the Company would file for a temporary rate increase with rates to be effective one year after consummation of the merger (i.e., August 24, 2008). Any temporary rate increase approved by the Commission would be subject to reconciliation with the final rates established by the Commission retroactive to August 24.

NOTE C – COMMITMENTS AND CONTINGENCIES

The normal ongoing operations and historic activities of the Company are subject to various federal, state and local environmental laws and regulations. Like most other industrial companies, the Company's historic and current gas, electric transmission and distribution and electric generation businesses use or generate some hazardous and potentially hazardous wastes and by-products. 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.

Air. Our generating facilities are located within a Clean Air Act (CAA) ozone non-attainment and PM 2.5 (fine particulate matter) non-attainment area, and are likely to be subject to increasingly stringent NOx, SO2 and particulate emission limitations. While regulatory programs to implement such limitations are the subject of various federal legal proceedings, the Company is implementing strategies to achieve various improvements. These improvements also include measures to improve fuel efficiency and reduce CO2 emissions and are planned to be incurred over a five to six year period and are estimated to cost approximately $100 million. Such amounts are substantially recoverable through contractual provisions with LIPA.

Water. Additional capital expenditures associated with the compliance and renewal of the surface water discharge permits for our power plants will likely be required by the Department of Environmental Conservation (DEC). Such amounts, estimated to be approximately $60 million over the next ten years, are recoverable through contractual provisions with LIPA.

Land, Manufactured Gas Plants and Related Facilities. Federal and state environmental regulators, as well as private parties, have alleged that several of the Company's subsidiaries are potentially responsible parties under Superfund laws for the remediation of over 200 contaminated sites in New England, New York and Rhode Island. The Company's greatest potential Superfund liabilities relate to manufactured gas plant, or MGP, facilities formerly owned or operated by the Company's subsidiaries or their predecessors. MGP byproducts included fuel oils, hydrocarbons, coal tar, purifier waste and other waste products that may pose a risk to human health and the environment. The Company is investigating or remediating these sites, or both, as appropriate.

The Company uses the "Expected Value" method for measuring its environmental liabilities. The Expected Value method applies a weighting to potential future expenditures based on the probability of these costs being incurred. A liability is recognized for all potential costs based on this probability. Costs considered to be 100% probable of being incurred are recognized in full, with costs below a 100% probability recognized in proportion to their probability. As required by SFAS 141, KeySpan discounted its environmental reserves at the time of acquisition using an appropriate fair value methodology. Adjustments to the environmental reserves based on changing circumstances will be undiscounted. Environmental reserves recorded prior to the KeySpan Acquisition for non-KeySpan companies have not been discounted.

The Company's total reserve for estimated MGP related environmental activities is approximately $1.3 billion. The potential high end of the range at March 31, 2008 is presently estimated at approximately $1.9 billion on an undiscounted basis. Management believes that obligations imposed on the Company because of the environmental laws will not have a material adverse effect on its operations, financial condition or cash flows. Through various rate orders issued by the NYPSC, MADPU, NHPUC and Rhode Island PUC costs related to MGP environmental cleanup activities are recovered in rates charged to gas distribution customers. Accordingly, the Company has reflected a regulatory asset of $1.5 billion.

The Company is pursuing claims against other potentially responsible parties to recover investigation and remediation costs it believes are the obligations of those parties. The Company cannot predict the likelihood of success of such claims.

Non-Utility Sites: The Company is aware of three non-utility sites for which it may have or share environmental remediation or ongoing maintenance responsibility. The Company presently estimates the remaining cost of the environmental cleanup activities for these three non-utility sites will be approximately $23.2 million, which amount has been accrued as a reasonable estimate of probable costs for known sites however, remediation costs for each site may be materially higher than noted, depending upon changing technologies and regulatory standards, selected end use for each site, and actual environmental conditions encountered.

The Company believes that in the aggregate, the accrued liability for the sites and related facilities identified above are reasonable estimates of the probable cost for the investigation and remediation of these sites and facilities. As circumstances warrant, we periodically re-evaluate the accrued liabilities associated with MGP sites and related facilities. We may be required to investigate and, if necessary, remediate each site previously noted, or other currently unknown former sites and related facility sites, the cost of which is not presently determinable.

Decommissioning Nuclear Units:
NEP has minority interests in three nuclear generating companies: Yankee Atomic Electric Company (Yankee Atomic), Connecticut Yankee Atomic Power Company (Connecticut Yankee), and Maine Yankee Atomic Power Company (Maine Yankee) (together, the Yankees). These ownership interests are accounted for on the equity method. The Yankees operated nuclear generating units that have been permanently retired. Physical decommissioning of the units is complete. Spent nuclear fuel remains on each site, awaiting fulfillment by the U.S. Department of Energy (DOE) of its statutory obligation to remove it. In addition, groundwater monitoring is ongoing at each site. The three units are as follows:

	The Company's Investment at March 31, 2008			Date Retired	Future Estimated Billings to the Company	
Unit	*(percent)*	*(In millions)*			*(In millions)*	
Yankee Atomic	34.5	$	0.5	Feb-92	$	27.4
Connecticut Yankee	19.5	$	2.4	Dec-96	$	67.0
Maine Yankee	24	$	0.5	Aug-97	$	20.8

With respect to each of the units, NEP recorded a liability and a regulatory asset reflecting the estimated future decommissioning billings from the Yankees. In a 1993 decision, the FERC allowed Yankee Atomic to recover its undepreciated investment in the plant, including a return on that investment, as well as unfunded nuclear decommissioning costs and other costs. Maine Yankee and Connecticut Yankee recover their prudently incurred costs, including a return, in accordance with settlement agreements approved by the FERC in May 1999 and July 2000, respectively. The Yankees collect the approved costs from their purchasers, including NEP. NEP's share of the decommissioning costs is accounted for in "Purchased electric energy" on the income statement. Under settlement agreements, NEP is permitted to recover prudently incurred decommissioning costs through contract termination charges.

The Yankees are periodically required to file rate cases for FERC approval, which present the Yankees' estimated future decommissioning costs. The Yankees are currently collecting decommissioning and other costs under FERC Orders issued in their respective rate cases.

Future billings from the Yankees are based on cost estimates. These estimates include the projected costs of groundwater monitoring, security, liability and property insurance and other costs. They also include costs for interim spent fuel storage facilities, which the Yankees have constructed during litigation they brought to enforce the DOE's obligation to remove the fuel as required by the Nuclear Waste Policy Act of 1982. Following a trial at the U.S. Court of Federal Claims (Claims Court) to determine the level of damages, on October 6, 2006, the Claims Court awarded the three companies approximately $143 million for spent fuel storage costs that had been incurred through 2001 and 2002. The Yankees had requested $176 million. On December

4, 2006, the DOE filed a notice of appeal with the U. S. Court of Appeals for the Federal Circuit. Oral arguments were held on February 4, 2008. A decision is expected in 2008. If the order is upheld, the damages received by the Yankees, net of litigation expenses and taxes, will be applied to reduce the decommissioning and other costs collected from their purchasers. On December 14, 2007, the Yankees brought further litigation in the Claims Court to recover damages incurred subsequent to 2001 and 2002. DOE does not anticipate having a long term storage facility available to accommodate spent fuel for at least a decade. The decommissioning costs that are actually incurred by the Yankees may exceed the estimated amounts, perhaps substantially.

Connecticut Yankee rate filing, prudence challenge and other proceedings*:*
On July 1, 2004, Connecticut Yankee asked FERC for a rate increase to reflect increased costs for decommissioning, pensions and other employment benefits, increased security and insurance costs and other expenses. In aggregate, the increase requested amounted to approximately $396 million through 2010. NEP's share is included in the future estimated billings shown in the preceeding table. On November 16, 2006, FERC issued an Order approving a settlement reached by parties to the proceeding. Under the settlement, as a result of the operation of a budget incentive mechanism established in a prior rate settlement, NEP was not allowed to recover $1 million of its expenditures.

The settlement provides that Connecticut Yankee may resume payment of dividends to return equity to sponsors. After January 1, 2008, Connecticut Yankee will not be allowed to earn a return on equity greater than $10 million.

Nuclear Contingencies:
As of March 31, 2008 and 2007, the Company has a liability of $165 million and $158 million, respectively, in non-current liabilities for the disposal of nuclear fuel irradiated prior to 1983 at Niagara Mohawk's former nuclear facilities. In January 1983, the Nuclear Waste Policy Act of 1982 (the Nuclear Waste Act) established a cost of $.001 per kWh of net generation for current disposal of nuclear fuel and provides for a determination of the Company's liability to the DOE for the disposal of nuclear fuel irradiated prior to 1983. The Nuclear Waste Act also provides three payment options for liquidating such liability and the Company has elected to delay payment, with interest, until the year in which Constellation Energy Group Inc., which purchased the Niagara Mohawk's nuclear assets, initially plans to ship irradiated fuel to an approved DOE disposal facility. Progress in developing the DOE facility has been slow and it is anticipated that the DOE facility will not be ready to accept deliveries until at least 2010.

Long-Term Contracts for the Purchase of Electric Power:
The Company's subsidiaries have several types of 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. The Company's commitments under these long-term contracts, as of March 31, 2008, are summarized in the table below.

(In millions of dollars)		
Fiscal Years Ended March 31,		Estimated Payments
2009	$	2,347.3
2010		1,067.9
2011		368.7
2012		331.0
2013		234.9
Thereafter		2,268.9
Total	**$**	**6,618.7**

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

Gas Supply, Storage and Pipeline Commitments:
The Company's gas distribution subsidiaries have entered into various contracts for gas delivery, storage and supply services. Certain of these contracts require payment of annual demand charges in the aggregate amount of approximately $975 million. The Company and its gas distribution subsidiaries are liable for these payments regardless of the level of services required from third parties. Such charges are currently recovered from utility customers as gas costs.

Plant Expenditures:
The Company's utility plant expenditures are estimated to be approximately $1.4 billion in fiscal 2009. At March 31, 2008, substantial commitments had been made relative to future planned expenditures. Generally construction expenditure levels are consistent from year to year. However, the Company has undertaken a Reliability Enhancement Program to improve performance and reliability.

Legal Matters:
From time to time we are subject to various legal proceedings arising out of the ordinary course of our business. Except as described below, we do not consider any of such proceedings to be material to our business or likely to result in a material adverse effect on our results of operations, financial condition or cash flows.

From 1983 until 1998, NEP was the wholesale power supplier for Norwood, Massachusetts. In April 1998, Norwood began taking power from another supplier, although its contract term with NEP ran to 2008. Pursuant to a tariff amendment approved by the FERC in May 1998, NEP has charged Norwood a monthly contract termination charge (CTC) of $0.6 million, plus interest on unpaid balances at 18 percent per year. NEP and Norwood have been engaged in litigation at the FERC and in the Massachusetts state court, as follows.

On December 20, 2003, Norwood filed a complaint with FERC under Section 206 of the Federal Power Act, contending that FERC did not approve the application of NEP's 1998 amended CTC to Norwood, and that the CTC amount is too high in any event. The FERC held that it did approve the CTC and that the CTC amount is correctly calculated and the First Circuit upheld

FERC, and the US Supreme Court denied Norwood's petition for certiorari. However, FERC ruled on May 17, 2007 that the interest to be paid by Norwood on unpaid monthly CTC bills should be calculated at the prime rate from the beginning of the CTC and not at 18 percent, as provided in the tariff. NEP appealed this interest ruling to the First Circuit on the ground that it goes beyond FERC's authority to award retroactive relief under Section 206 of the Federal Power Act, and violates the filed rate doctrine. Oral argument was held in April 2008, and the parties await a decision. In 1998, NEP filed a collection action in Massachusetts Superior Court (Worcester County) to collect the CTC from Norwood. In June 2004, NEP obtained a judgment from the Superior Court based on amounts owed through January 31, 2001. The Massachusetts appellate courts sustained NEP's judgment against several challenges by Norwood. However, state court proceedings have been stayed pending the outcome of the FERC and First Circuit proceedings described above. At this point, the remaining issue to be decided by the First Circuit is NEP's challenge to FERC's determination of the amount of late payment interest owed to NEP. To date, Norwood has paid NEP $93.4 million, including its last payment of approximately $53.2 million made in January 2008.

Narragansett is in litigation with Constellation Energy Commodities Group (Constellation) in two cases. In the first case commenced on September 11, 2006 in the U.S. District Court for the District of Rhode Island, Constellation has alleged that certain power purchase agreements entitle it to additional compensation for capacity during calendar years 2006-2009, following the FERC-approved settlement in the forward capacity market. According to Constellation, the resolution of this claim "could adversely affect Constellation in amounts upwards of $150 million." In the second case commenced on April 14, 2008 in the U.S. District Court for the District of Massachusetts, Constellation has alleged that certain power purchase agreements entitle it to payments for a fuel adjustment factor during calendar years 2005-2009. The prospective portion of the fuel adjustment claim is subject to the effects of changing fuel prices. By Constellation's methodology for payment calculation, it is estimated that damages could exceed $200 million. Narragansett is exploring its options to resolve these matters. Regardless of the outcome, Narragansett is entitled to recover all purchased power costs from customers under current law and legal precedent, however any request to recover increased costs that may result from resolution of these matters would be subject to approval by the Rhode Island Public Utility Commission.

Since July 12, 2006, eight lawsuits have been filed which allege damages resulting from contamination associated with the historic operations of former manufactured gas plants located in Bay Shore. KeySpan has been conducting site investigations and remediations at these locations pursuant to Administrative Orders on Consent (ACO) with the New York State Department of Environmental Conservation (DEC). One of these lawsuits was settled on May 15, 2008 by purchasing a residential property. There is one lawsuit pending related to the former Clifton manufactured gas plant on Staten Island. KeySpan intends to contest each of the remaining proceedings vigorously.

On February 8, 2007, KeySpan received a Notice of Intent to File Suit from the Office of the Attorney General for the State of New York (AG) against KeySpan and four other companies in connection with the cleanup of historical contamination found in certain lands located in Greenpoint, Brooklyn and in an adjoining waterway. KeySpan has previously agreed to remediate portions of the properties referenced in this notice and will work cooperatively with the DEC and AG to address environmental conditions associated with the remainder of the properties. KeySpan has entered into an ACO for one of the land-based sites and is currently negotiating the terms of another ACO for the remaining land-based sites. To resolve issues associated with the waterway, KeySpan and the other four companies are currently negotiating the terms of a Consent Decree. At this time, we are unable to predict what effect, if any, the outcome of these proceedings will have on our financial condition, results of operation and cash flows.

In May 2007, KeySpan received a Civil Investigative Demand (CID) from the United States Department of Justice, Antitrust Division, requesting the production of documents and information relating to its investigation of competitive issues in the New York City electric energy capacity market prior to National Grid's acquisition of KeySpan. The CID is a request for information in the course of an investigation and does not constitute the commencement of legal proceedings, and no specific allegations have been made against KeySpan. In April 2008, KeySpan received a second CID in connection with this matter. KeySpan continues to believe that its activity in the capacity market is consistent with all applicable laws and regulations and will continue to fully cooperate with this investigation.

Lease Obligations*:*
The Company has various operating leases which include the lease of the Company's Brooklyn headquarters, a leveraged lease financing arrangement (as discussed below), as well as leases for other buildings, office equipment, vehicles and power operating equipment. Cash lease payments under these leases total approximately $170 million a year.

Sale/leaseback Transaction

The Company has a leveraged lease financing arrangement associated with the Ravenswood Expansion. In May 2004, the unit was acquired by a lessor from our subsidiary, KeySpan Ravenswood, LLC, and simultaneously leased back to that subsidiary. All the obligations of KeySpan Ravenswood, LLC have been unconditionally guaranteed by KeySpan. This lease transaction qualifies as an operating lease under SFAS 98 "Accounting for Leases: Sale/Leaseback Transactions Involving Real Estate; Sales-Type Leases of Real Estate; Definition of the Lease Term; an Initial Direct Costs of Direct Financing Leases, an amendment of FASB Statements No.13, 66, 91 and a rescission of FASB Statement No. 26 and Technical Bulletin No. 79-11." We have agreed to sell KeySpan Ravenswood, LLC to TransCanada Facility USA, Inc., a wholly owned subsidiary of TransCanada Corporation. The transaction provides for the restructuring and transfer of KeySpan's interest in the Ravenswood Expansion. TransCanada will prepay this sublease and provide back-to-back guarantees. However, KeySpan will remain responsible for the lease payments under this arrangement through the maturity of the lease – May 2040.

National Grid USA Service Company, Inc. entered into a lease dated January 7, 2008, in connection with an office building that will be newly constructed in Waltham, Massachusetts. The terms of the lease provide for a commencement date ("Commencement Date") to be set upon the substantial completion of the building, including all tenant improvements. The Commencement Date is currently projected to be May 15, 2009. The term of the lease expires twenty years and five months after the Commencement Date. The base rent under the lease increases every five years and will range between $10 million and $13 million annually.

Variable Interest Entity

We have an arrangement with an unaffiliated variable interest financing entity through which we lease a portion of the Ravenswood Facility. KeySpan acquired the Ravenswood Facility, in part, through the variable interest entity, from the Consolidated Edison Company of New York ("Consolidated Edison") on June 18, 1999 for approximately $597 million. In order to reduce the initial cash requirements, KeySpan entered into a lease agreement (the "Master Lease") with the variable interest entity that acquired a portion of the facility, i.e. the three steam generating units, directly from Consolidated Edison and leased it to a KeySpan subsidiary. The variable interest financing entity acquired the property for $425 million, financed with debt of $412.3 million (97% of capitalization) and equity of $12.7 million (3% of capitalization). KeySpan has no ownership interests in the units or the variable interest entity. KeySpan has guaranteed all payment and performance obligations of our subsidiary under the Master Lease. Monthly lease payments are substantially equal to the monthly interest expense on the debt securities.

The Master Lease had been consolidated on the Consolidated Balance Sheet based on KeySpan's current status as primary beneficiary as defined in Financial Accounting Standards Board Interpretation No. 46 (FIN 46), "Consolidation of Variable Interest Entities, an Interpretation of ARB No. 51." As part of the process to sell KeySpan Ravenswood, LLC, KeySpan terminated the Master Lease in June 2008 at a cost of $456 million. The operations of the Ravenswood Facility except for interest expense is classified as discontinued operations on the Consolidated Statement of Income, Consolidated Balance Sheet and Consolidated Statement of Cash Flows.

Financial Guarantees:

The Company has guaranteed the principal and interest payments on certain outstanding debt as discussed in Note H, "Long Term Debt". Additionally, KeySpan has issued financial guarantees in the normal course of business, on behalf of its and the Company's subsidiaries, to various third party creditors. At March 31, 2008, the following amounts would have to be paid by KeySpan in the event of non-payment by the primary obligor at the time payment is due:

Nature of Guarantee (In Millions of Dollars)		Amount of Exposure	Expiration Dates
Guarantees for Subsidiaries			
Medium-Term Notes - KEDLI	(i)	$ 400.0	2010
Industrial Development Revenue Bonds	(ii)	128.3	2027
Ravenswood - Master Lease	(iii)	425.0	2009
Ravenswood - Sale/leaseback	(iv)	431.0	2040
Surety Bonds	(v)	72.9	Revolving
Commodity Guarantees and Other	(vi)	27.7	2008 - 2009
Letters of Credit	(vii)	76.7	2008 - 2011
		$ 1,561.6	

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

(i) KeySpan has fully and unconditionally guaranteed $400 million to holders of Medium-Term Notes issued by KEDLI. These notes are due to be repaid February 1, 2010. KEDLI is required to comply with certain financial covenants under the debt agreements. The face value of these notes is included in long-term debt on the Consolidated Balance Sheet.

(ii) KeySpan has fully and unconditionally guaranteed the payment obligations of its subsidiaries with regard to $128.3 million of Industrial Development Revenue Bonds issued through the Nassau County and Suffolk County Industrial Development Authorities for the construction of two electric-generation peaking plants on Long Island. The face value of these notes are included in long-term debt on the Consolidated Balance Sheet.

(iii) KeySpan has guaranteed all payment and performance obligations of KeySpan Ravenswood, LLC, the lessee under the Master Lease. The term of the lease had been extended to June 20, 2009. This guarantee has been terminated following the termination of the Master Lease in June 2008, other than with respect to certain continued indemnity obligations that are considered highly remote and likely immaterial.

(iv) KeySpan has guaranteed all payment and performance obligations of KeySpan Ravenswood, LLC, the lessee under the sale/leaseback transaction associated with the Ravenswood Expansion, including future decommissioning costs. The initial term of the lease is for 36 years. As noted previously, this lease qualifies as an operating lease and is not reflected on the Consolidated Balance Sheet. The cash consideration for KeySpan Ravenswood, LLC includes a prepayment from TransCanada to KeySpan of these payments on a present value basis. KeySpan's requirement to make these regular payments will continue after the sale of KeySpan Ravenswood, LLC. TransCanada will provide various guarantees to ensure that KeySpan does not have a continuing interest in the performance of the plant.

(v) KeySpan has agreed to indemnify the issuers of various surety and performance bonds associated with certain construction projects being performed by certain current and former subsidiaries. In the event that the subsidiaries fail to perform their obligations under contracts, the injured party may demand that the surety make payments or provide services under the bond. KeySpan would then be obligated to reimburse the surety for any expenses or cash outlays it incurs. Although KeySpan is not guaranteeing any new bonds for any of the former subsidiaries, KeySpan's indemnity obligation supports the contractual obligation of these former subsidiaries. KeySpan has also received from a former subsidiary an indemnity bond issued by a third party insurance company, the purpose of which is to reimburse KeySpan in an amount up to $80 million in the event it is required to perform under all other indemnity obligations previously incurred by KeySpan to support such company's bonded projects existing prior to divestiture. At March 31, 2008, the total cost to complete such remaining bonded projects is estimated to be approximately $16.0 million.

(vi) KeySpan has guaranteed commodity-related payments for certain subsidiaries. These guarantees are provided to third parties to facilitate physical and financial transactions involved in the purchase of natural gas, oil and other petroleum products for electric production and marketing activities. The guarantees cover actual purchases by these subsidiaries that are still outstanding as of March 31, 2008.

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

To date, KeySpan has not had a claim made against it for any of the above guarantees and we have no reason to believe that our subsidiaries or former subsidiaries will default on their current obligations. However, we cannot predict when or if any defaults may take place or the impact any such defaults may have on our consolidated results of operations, financial condition or cash flows.

The Company owns a 26.25% ownership interest in the Millennium Pipeline Company LLC ("Millennium"), the developer of the Millennium Pipeline project. The Millennium Pipeline project is anticipated to have the capacity to transport up to 525,000 DTH of natural gas a day from Corning, New York to Ramapo, New York, interconnecting with the pipeline systems of various other utilities in New York. Subject to the receipt of certain remaining permits and financing, Millennium expects that the first phase of the project will be in service by November 2008.

KeySpan has guaranteed $210 million of an $800 million Millennium Pipeline construction loan. The $210 million represents KeySpan's proportionate share of the $800 million loan based on KeySpan's 26.25% ownership interest in the Millennium Pipeline project. In addition, Consolidated Edison, KEDLI and Columbia Transmission have each entered into precedent agreements to purchase capacity on the pipeline. Upon and subject to the terms and conditions set forth in Precedent Agreements, KeySpan has agreed to guarantee the full and prompt payment of $15.8 million (the "Guaranteed Amount") of the contingent $60 million financial obligation that Millennium may incur for liquidated damages under the Precedent Agreements to Consolidated Edison and KEDLI. The liquidated damages are intended to reimburse Consolidated Edison and KEDLI for costs incurred to secure additional capacity if Millennium is unable to provide the contracted capacity. The $15.8 million guaranteed amount reflects KeySpan's proportionate share of the $60 million of financial security that is required to be provided to Consolidated Edison and KEDLI pursuant to the Precedent Agreements based on KeySpan's proportionate ownership interest in the Millennium Pipeline project. These guarantees have been accounted for in accordance with FIN 45 "Guarantor's Accounting and Disclosure Requirements for Guarantees, Including Indirect Guarantees of Indebtness of Others."

At March 31, 2008, the fair value of these guarantees was $2.7 million and is reflected as a component of equity investments, and other deferred credits and other liabilities on the Consolidated Balance Sheet.

NOTE D – ACCUMULATED OTHER COMPREHENSIVE INCOME (LOSS)

The following table details the components of accumulated other comprehensive income (loss) for the fiscal years ended March 31, 2008 and 2007:

(in millions)	Unrealized Gains (Losses) on investments	Postretirement Benefit Liabilities	Cash Flow Hedges	Total Accumulated Other Comprehensive Income (Loss)
March 31, 2006	$ 6.8	$ (6.4)	$ (4.8)	$ (4.3)
Other comprehensive income (loss), net of taxes:				
Unrealized gains (losses) on securities	6.0	-	-	6.0
Unrealized gains (losses) on hedges	-	-	(17.5)	(17.5)
Change in additional minimum pension liability	-	(6.3)	-	(6.3)
Adjustment for the adoption of SFAS No. 158	-	(398.1)	-	(398.1)
Relassification adjustment for gain (loss) included in net income	(3.5)	-	22.0	18.5
March 31, 2007	$ 9.3	$ (410.8)	$ (0.2)	$ (401.7)
Other comprehensive income (loss), net of taxes:				
Unrealized gains (losses) on investments	(13.6)	-	-	(13.6)
Unrealized gains (losses) on hedging			14.2	14.2
Change in pension and other postretirement provisions	-	(100.5)	-	(100.5)
Reclassification adjustment for gain included in net income	3.0	-	14.8	17.8
March 31, 2008	$ (1.3)	$ (511.3)	$ 28.8	$ (483.8)

NOTE E – DERIVATIVE CONTRACTS AND HEDGING ACTIVITIES

In the normal course of business, the Company's subsidiaries are party to derivative instruments, such as futures, options, swaps, and physical forwards that are principally used to manage commodity prices associated with their natural gas and electric operations. These financial exposures are monitored and managed as an integral part of the Company's overall Financial Risk Management Policy. Additionally, the Company continually assesses the cost relationship between fixed and variable rate debt. Consistent with its objective to minimize its cost of capital, the Company periodically enters into hedging transactions that effectively convert the terms of underlying debt obligations from fixed to variable or variable to fixed. The Company will generally engage in activities at risk only to the extent that those activities fall within commodities and financial markets to which it has a physical market exposure in terms and volumes consistent with its core business.

As discussed in greater detail below, certain derivative instruments employed by the Company are accounted for as cash-flow hedges or fair value hedges in the case of treasury related derivative instruments and receive hedge accounting treatment under SFAS 133.

The Company also employs derivative instruments that do not qualify for hedge accounting treatment. Most of these derivative instruments utilized by the Company are subject to SFAS 71 "Accounting for the Effects of Certain Types of Regulation" since the Company's rate agreements allow for the pass-through of the commodity costs of electricity and natural gas and the costs related to hedging activities.

Financial Derivatives – Receiving Hedge Accounting

Regulated Utilities

Derivative financial instruments are used to reduce the cash flow variability associated with the purchase price for a portion of future natural gas purchases associated with our gas distribution utilities. Our strategy is to minimize fluctuations in gas sales prices to our regulated firm gas sales customers in our New York and New England service territories.

Niagara Mohawk utilizes NYMEX gas futures contracts to accomplish the aforementioned strategy. At March 31, 2008 the fair value of these derivative instruments was $10 million. This balance is recorded in accumulated other comprehensive income and will be reclassified into earnings over the next twelve months. Narragansett also utilizes NYMEX gas futures contracts to reduce cash flow variability associated with natural gas purchases. At March 31, 2008 the fair value of its derivative instruments was $21 million. The maximum length of time over which Narragansett has hedged such cash flow variability is through March 2010. The estimated amount of gains associated with such derivative instruments that are recorded in accumulated other comprehensive income and that are expected to be reclassified into earnings over the next twelve months is $17.7 million. Ineffectiveness associated with these outstanding derivative financial instruments was immaterial for the year ended March 31, 2008.

Derivative financial instruments are used to reduce the cash flow variability associated with the purchase price for a portion of future electricity purchases associated with certain of our electric distribution subsidiaries. Our strategy is to minimize fluctuations in electric sales prices to our regulated firm electric sales customers in our upstate New York service territory.

Niagara Mohawk utilizes NYMEX electric futures contracts to hedge a portion of its electricity purchases. The maximum length of time over which Niagara Mohawk has hedged such cash flow variability is through December 2008. The fair value of these derivative instruments at March 31, 2008 was $10.3 million. The estimated amount of gains associated with such derivative instruments that are reported in accumulated other comprehensive income and that are expected to be reclassified into earnings over the next twelve months is $10.3 million. Ineffectiveness associated with these outstanding derivative financial instruments was immaterial for the year ended March 31, 2008.

On April 1, 2008, the Company electively discontinued its cash flow hedge accounting treatment for Niagara Mohawk and Narragansett NYMEX gas futures. On June 1, 2008, the Company electively discontinued its cash flow hedge accounting treatment for Niagara Mohawk NYMEX electric swap contracts. The accounting for these derivative instruments are subject to SFAS 71. Therefore, subsequent changes in the fair value of these derivatives will be recorded as regulatory assets and regulatory liabilities.

Other
Our Energy Investments subsidiary, Seneca-Upshur, utilizes OTC natural gas swaps to hedge the cash flow variability associated with the forecasted sales of a portion of its natural gas production. At March 31, 2008, Seneca-Upshur has hedge positions in place for approximately 70% of its estimated 2008 through 2009 gas production, net of gathering costs. We use market quoted forward prices to value these swap positions. The maximum length of time over which Seneca-Upshur has hedged such cash flow variability is through December 2009. The fair value of these derivative instruments at March 31, 2008 was a liability of $7.0 million. As required by SFAS 141, at the time of the KeySpan Acquisition all accumulated other comprehensive income balances were reclassified into equity. As a result, $5.1 million of losses are currently included in accumulated other comprehensive income and expected to be reclassified to earnings in the next twelve months. Ineffectiveness associated with these outstanding derivative financial instruments was immaterial for the period August 25, 2007 through March 31, 2008.

As of March 31, 2008, the above derivative financial instruments are designated as cash flow hedges under SFAS 133 and are not considered held for trading purposes as defined by current accounting literature. Accordingly, we carry the fair value of these derivative instruments on the Consolidated Balance Sheet as either a current or deferred asset or liability, as appropriate, and record the effective portion of unrealized gains or losses in accumulated other comprehensive income. Gains and losses are reclassified from accumulated other comprehensive income to the Consolidated Statement of Income in the period the hedged transaction affects earnings. Gains and losses on settled transactions are reflected as a component of revenue. Any hedge ineffectiveness that results from changes during the period in the price differentials between the index price of the derivative contract and the price of the purchase or sale for the cash flow that is being hedged is recorded directly to earnings.

Financial Derivatives – Not Receiving Hedge Accounting

Regulated Utilities
We use derivative financial instruments to reduce the cash flow variability associated with the purchase price for a portion of future natural gas purchases associated with our New York and Massachusetts gas service territories. Our strategy is to minimize fluctuations in gas sales prices to our regulated firm gas sales customers. At March 31, 2008 the fair value of these derivative instruments was $110.9 million.

Niagara Mohawk has eight indexed swap contracts, expiring in fiscal year 2009 (June 2008), which resulted from the Niagara Mohawk Rate Plan. These derivatives are not designated as hedging instruments and are covered by regulatory rulings that allow the gains and losses to be recorded as regulatory assets or regulatory liabilities. As of March 31, 2008 Niagara Mohawk had recorded liabilities at the present value of $51 million for these swap contracts and had recorded a corresponding swap contracts regulatory asset. The asset and liability are amortized over the remaining term of the swaps as nominal energy quantities are settled and they are adjusted as periodic reassessments are made of energy price forecasts. Niagara Mohawk will make these estimated payments of $51 million during fiscal year 2009. Niagara Mohawk uses NYMEX gas futures to hedge the gas commodity component of its indexed swap contracts. These instruments, as used, do not qualify for hedge accounting status under SFAS 133, but are recorded under SFAS 71. The fair value of these derivatives at March 31, 2008 was $10.7 million.

The accounting for the above derivative instruments is subject to SFAS 71. Therefore, the fair value of these derivatives is recorded as current or deferred assets and liabilities, with offsetting positions recorded as regulatory assets and regulatory liabilities on the Consolidated Balance Sheet. Gains or losses on the settlement of these contracts are initially deferred and then refunded to or collected from our customers consistent with regulatory requirements.

Other
The Company is required by the NYPSC to divest of the Ravenswood Generating Station. The Company is in the process of selling KeySpan Ravenswood, LLC, which owns the Ravenswood Generating Station. In addition, the NYPSC required the Company to enter into an energy agreement whereby it would no longer have a financial interest in the NYISO energy market clearing prices. In January 2008, KeySpan Ravenswood, LLC entered into a one-year energy tolling agreement with a single counterparty pursuant to the requirements of the NYPSC just mentioned. This agreement contains certain embedded derivatives that were determined to be clearly and closely related to the host contract and appropriately not valued. The Company has no other derivative positions associated with the Ravenswood Generating Station.

Based upon KeySpan's experience in the New York City electric capacity market and management's assessment that a financial opportunity existed related to this market, KeySpan entered into an International SWAP Dealers Association Master Agreement for a fixed for float unforced capacity financial swap (the "Swap Agreement") with Morgan Stanley Capital Group Inc. ("Morgan Stanley") on January 18, 2006 in an effort to enhance shareholder value. The Swap Agreement involves a financial transaction and was not intended to be an economic hedge on physical generation assets or a contract for the physical delivery of capacity or energy. However, the same market dynamics that impacted the physical generation business impacted the value of the financial Swap Agreement.

The Swap Agreement has a three year term that began on May 1, 2006. The notional quantity is 1,800,000kW (the "Notional Quantity") of In-City Unforced Capacity and the fixed price is $7.57/kW-month ("Fixed Price"), subject to adjustment upon the occurrence of certain events. Cash settlement occurs on a monthly basis based on the In-City Unforced Capacity price determined by the relevant NYISO Spot Demand Curve Auction Market ("Floating Price"). For each monthly settlement period, the price difference equals the Fixed Price minus the Floating Price. If such price difference is less than zero, Morgan Stanley will pay KeySpan an amount equal to the product of (a) the Notional Quantity and (b) the absolute value of such price difference. Conversely, if such price difference is greater than zero, KeySpan will pay Morgan Stanley an amount equal to the product of (a) the Notional Quantity and (b) the absolute value of such price difference.

At contract inception, the initial fair value of the Swap Agreement was fully reserved under the provision of EITF 02-3 "Issues Involved in Accounting for Derivative Contracts Held for Trading Purposes and Contracts Involved in Energy Trading and Risk Management Activities," due to KeySpan's assessment at that time that market prices for the underlying capacity were unobservable. Accordingly, no fair value was recorded at the inception of the contract.

In June 2006, stakeholders, including the NYPSC and the Consolidated Edison Company of New York, Inc. ("Con Ed"), complained to the NYISO that the summer 2006 In-City capacity market prices did not decline as some expected following the introduction of additional capacity into the market. After a stakeholder process, the NYISO proposed additional supplier mitigation measures to the FERC, but the NYISO's filing was rejected. FERC instead opened an investigation of the New York City capacity market. The purpose of FERC's investigation was to determine whether changes in the market are needed to attract and maintain necessary infrastructure without over compensating or under compensating suppliers. Subsequently, FERC ordered the NYISO to file comprehensive market reforms. On October 4, 2007, the NYISO proposed new mitigation measures to FERC involving mitigation of both suppliers and purchasers, with the intended effect of establishing both price caps and, during times of surplus, bid floors. Comments and alternative proposals were filed with FERC on November 19, 2007.

On March 7, 2008, the FERC approved the NYISO In-City capacity mitigation measures and revised the In-City capacity bid caps. The revised bid caps are expected to result in the SWAP Agreement floating price being set to equal the strike price, thereby eliminating all cash flow between the Company and Morgan Stanley for the remaining term of the Swap Agreement. As required by SFAS 141, the Company calculated the fair value of this derivative instrument to be a liability of $17.9 million at August 24, 2007 and such amount was recorded as a current liability. The Company does not anticipate any further cash settlements after payment of the $17.9 million, based on current and expected NYISO bid caps.

Physical Derivatives – Not Receiving Hedge Accounting

Regulated Utilities

As a result of a USGen bankruptcy settlement agreement (Bankruptcy Settlement), NEP resumed the performance and payment obligations under power supply contracts that had been transferred to USGen when the Company divested its generating business. The Company continues to record a derivative liability of approximately $94 million for the above-market portion of the power supply contracts with an equal offset to a corresponding regulatory asset. The performance and payment obligations will not affect the results of operations, as the Company will recover the above-market cost of the power supply contracts from customers through the contract termination charge. In accordance with the Bankruptcy Settlement, the Company received proceeds of approximately $196 million in June 2005 from USGen. That amount relates in part to the power supply contracts and the Company is crediting that amount to customers through a reduction in rates through December 31, 2009.

SFAS 133 establishes criteria that must be satisfied in order for option contracts, forward contracts with optionality features, or contracts that combine a forward contract and a purchase option contract to qualify for the normal purchases and sales exception. Certain contracts for the physical purchase of natural gas associated with our regulated gas utilities do not qualify for normal purchases under SFAS 133. Additionally, our regulated gas utilities have gas transportation service agreements with large generating facilities that contain embedded derivatives. At March 31, 2008, these derivatives had a net fair value of $40.3 million and are subject to SFAS 71 accounting treatment described earlier.

Other

The utility tariffs associated with certain of our gas utilities do not contain weather normalization adjustments. As a result, fluctuations from normal weather may have a significant positive or negative effect on the results of these operations.

The Company has heating-degree day put options to mitigate the effect of fluctuations from normal weather on KEDNE's financial position and cash flows for the 2007/2008 winter heating season – November 2007 through March 2008. These put options would have paid the Company $40,000 per heating degree day when the actual temperature was approximately 5% warmer than normal or below 4,141 heating degree days, based on the most recent 20-year average for normal weather. The maximum amount the Company would have received on these purchased put options was $16 million. The net premium cost for these options was $1.9 million and was amortized over the heating season. Since weather was colder than normal during the November 2007 through March 2008 heating season, these weather derivatives had no value.

We account for these derivatives pursuant to the requirements of EITF 99-2, "Accounting for Weather Derivatives." In this regard, such instruments are accounted for using the "intrinsic value method" as set forth in such guidance.

Treasury financial instruments

Financial derivative are used for hedging purposes in the management of exposure to interest rate risk enabling the Company to optimize the overall cost of accessing debt capital markets, and mitigating the market risk which would otherwise arise from the maturity of its treasury related assets and liabilities.

Treasury related derivative instruments may qualify as either fair value hedges or cash flow hedges. At present, the Company uses fair value hedges, consisting of interest rate and cross-currency swaps that are used to protect against changes in the fair value of fixed-rate, long-term financial instruments due to movements in market interest rates. For qualifying fair value hedges, all changes in the fair value of the derivative financial instrument and changes in the fair value of the item in relation to the risk being hedged are recognized in the income statement. If the hedge relationship is terminated, the fair value adjustment to the hedged item continues to be reported as part of the basis of the item and is amortized to the income statement as a yield adjustment over the remainder of the hedging period.

At March 31, 2008, $13.9 million of $541.5 million National Grid USA debt has been hedged. Net losses on the derivative financial instrument included in the income statement was $0.9 million and has been recorded as finance costs.

Credit and Collateral

Derivative contracts are primarily used to manage exposure to market risk arising from changes in commodity prices and interest rates. In the event of non-performance by a counterparty to a derivative contract, the desired impact may not be achieved. The risk of counterparty non-performance is generally considered a credit risk and is actively managed by assessing each counterparty credit profile and negotiating appropriate levels of collateral and credit support. In instances where the counterparties' credit quality has declined, or credit exposure exceeds certain levels, we may limit our credit exposure by restricting new transactions with counterparties, requiring additional collateral or credit support and negotiating the early termination of certain agreements. At March 31, 2008, the Company has received $19.2 million from its counterparties as collateral associated with outstanding derivative contracts. This amount has been recorded as restricted cash, with an offsetting position in current liabilities on the Consolidated Balance Sheet. Additionally, the Company has $4.3 million of collateral held by counterparties at March 31, 2008.

NOTE F - EMPLOYEE BENEFITS

Summary
The Company and its subsidiaries have defined benefit pension plans covering substantially all employees. The pension plans are non-contributory and tax qualified defined benefit plans which provide all employees with a minimum retirement benefit. Benefits are based on compensation and / or years of service.

The Company and its subsidiaries have defined benefit postretirement benefit plans other than pensions (PBOP) which provide health care and life insurance coverage to eligible retired employees. Eligibility is based on certain age and length of service requirement and, in most cases, retirees must contribute to the cost of their coverage.

Supplemental nonqualified, non-contributory executive retirement programs provide additional defined pension benefits for certain executives. A similar retirement program is provided to non-executive employees who have compensation or benefits in excess of the qualified plan limits.

The Company and its subsidiaries also offer employees a defined contribution plan. Plans are available to all eligible employees. Eligible employees contributing to the plans may receive certain employer contributions including matching contributions.

New York based pension and PBOP plans amortize prior service costs and gains and losses over a 10 year period calculated on a vintage year basis as required by the regulatory policy.

Funding Policy

On a tax-deductible basis, the company will contribute amounts collected in rates to the pension plans until 100 percent to 110 percent of the Pension Protection Act of 2006 (the PPA) funding target is reached. The Company will contribute no less than the minimum amounts required by PPA, even if such amounts exceed the amounts collected in rates.

The Company will contribute amounts to the PBOP plans that are in compliance with the regulatory requirements of the various regulated jurisdictions within which the company operates.

Plan Assets
The target asset allocations for the benefit plans at March 31 are:

	Pension Benefits		Non-Union PBOP		Union PBOP	
	2008	2007	**2008**	2007	**2008**	2007
U.S. equities	**42%**	37%	**46%**	33%	**49%**	50%
Global equities (including U.S.)	**3%**	5%	**1%**	0%	**0%**	0%
Global tactical asset allocation	**7%**	13%	**0%**	0%	**0%**	0%
Non-U.S. equities	**13%**	10%	**16%**	17%	**21%**	23%
Fixed income	**31%**	31%	**32%**	50%	**28%**	27%
Private equity and other	**4%**	4%	**5%**	0%	**2%**	0%
	100%	100%	**100%**	100%	**100%**	100%

The percentage of the fair value of total plan assets at March 31 is:

	Pension Benefits		Non-Union PBOP		Union PBOP	
	2008	2007	**2008**	2007	**2008**	2007
U.S. equities	**40%**	38%	**44%**	35%	**45%**	50%
Global equities (including U.S.)	**3%**	6%	**0%**	0%	**0%**	0%
Global tactical asset allocation	**7%**	12%	**0%**	0%	**0%**	0%
Non-U.S. equities	**14%**	11%	**18%**	18%	**19%**	24%
Fixed income	**31%**	30%	**31%**	47%	**34%**	26%
Private equity and other	**5%**	3%	**7%**	0%	**2%**	0%
	100%	100%	**100%**	100%	**100%**	100%

The Company manages benefit plan investments to minimize the long-term cost of operating the plans, with a reasonable level of risk. Risk tolerance is determined as a result of a periodic asset/liability study which analyzes plan liabilities and plan funded status and results in the determination of the allocation of assets across equity and fixed income securities, Equity investments are broadly diversified across U.S. and non-U.S. stocks, as well as across growth, value, and small and large capitalization stocks. Likewise, the fixed income portfolio is broadly diversified across the various fixed income market segments. Small investments are also held in private equity with the objective of enhancing long-term returns while improving portfolio diversification. For the PBOP plans, since the earnings on a portion of the assets are taxable, those investments are managed to maximize after tax returns consistent with the broad asset class parameters established by the asset allocation study. Investment risk and return are reviewed by the investment committee on a quarterly basis.

The estimated rate of return for various passive asset classes is based on both analysis of historical rates of return and forward looking analysis of risk premiums and yields. Current market conditions, such as inflation and interest rates, are evaluated in connection with the setting of the long-term assumption. A small premium is added for active management and rebalancing of both equity and fixed income. The rates of return for each asset class are then weighted in accordance with the plans' target asset allocation, and the resulting long-term return on asset rate is then applied to the market-related value of assets.

Assumptions Used for Benefits Accounting

The following weighted average assumptions were used to determine the pension and PBOP benefit obligations and net periodic benefit costs for the fiscal years ending March 31.

	Pension benefits			
	Benefit obligation		Net periodic benefit costs	
	2008	2007	**2008**	2007
Discount rate	**6.50%**	6.00%	**6.00% - 6.50%**	6.00%
Rate of compensation increase	**3.50%-4.0%**	3.90% - 4.30%	**3.50% - 5.00%**	3.90% - 4.30%
Expected long-term rate of return on assets	**n/a**	n/a	**8.00%**	8.00%

	PBOP			
	Benefit obligation		Net periodic benefit costs	
	2008	2007	**2008**	2007
Discount rate	**6.50%**	6.00%	**6.00% - 6.50%**	6.00%
Expected long-term rate of return on assets	**n/a**	n/a	**7.00% - 8.25%**	7.80%
Health care cost trend rate				
Initial - pre 65	**9.00%**	9.50%	**9.00% - 9.50%**	10.00%
Initial - post 65	**10.00%**	10.50%	**10.00% - 10.50%**	11.00%
Ultimate	**5.00%**	5.00%	**5.00%**	5.00%
Year ultimate rate reached - pre 65	**2014**	2012	**2012**	2011
Year ultimate rate reached - post 65	**2015**	2013	**2013**	2012

The expected contributions to the Company's pension and PBOP plans during fiscal year 2009 are expected to be $320.3 million and $253 million, respectively.

Pension Benefits

The Company's net periodic benefit cost for the fiscal years ended March 31, 2008 and 2007 included the following components:

(In millions)	**2008**	2007
Service Cost	**$ 93.2**	$ 55.3
Interest Cost	**276.1**	163.1
Expected return on plan assets	**(322.7)**	(174.5)
Amortization of prior service cost	**5.0**	4.9
Amortization of loss	**61.8**	58.3
Net periodic benefit costs before settlements and curtailments	**113.4**	107.1
Settlement and curtailment loss	**0.7**	25.6
Special termination benefits (VERO)	**50.3**	-
Net periodic benefit cost	**$ 164.4**	$ 132.7

The following table provides the changes in the pension plans' accumulated benefit obligation, funded status and the amounts recognized in the balance sheet at March 31:

(In millions)		**2008**		2007
Accumulated benefit obligation	**$**	**(5,027.6)**	$	(2,603.5)
Reconciliation of benefit obligation:				
Benefit obligation at beginning of period		**(2,897.2)**		(2,748.5)
Service cost		**(93.2)**		(55.4)
Interest cost		**(276.1)**		(163.1)
Actuarial gain (loss)		**163.4**		(87.0)
Benefits paid		**364.8**		156.7
Plan Amendments		**(8.4)**		-
Settlements		**(41.8)**		165.9
Acquisition		**(2,741.5)**		(165.9)
Benefit obligation at end of period		**(5,530.0)**		(2,897.2)
Fair value of plan assets at beginning of period		**2,494.8**		2,147.6
Actual return on plan assets		**(110.9)**		220.8
Company contributions		**437.8**		295.4
Benefits paid		**(364.8)**		(156.7)
Settlements		**(0.7)**		(165.9)
Acquisition		**2,621.2**		153.6
Fair value of plan assets at end of period		**5,077.4**		2,494.8
Funded status	**$**	**(452.6)**	$	(402.4)

On August 24, 2007, the Company acquired KeySpan. In connection with this acquisition, KeySpan's pension plans merged with the existing pension plan, resulting in an increase in the assets and benefit obligations of the plan in the amounts of $2.6 billion and $2.7 billion, respectively.

On August 24, 2006, the Company acquired the Rhode Island gas distribution assets of New England Gas Company from Southern Union Company. In connection with this acquisition, four small pension plans merged with the existing pension plan, resulting in an increase in the assets and benefit obligation of the plan in the amounts of $154 million and $166 million, respectively.

(In millions)		2008		2007
Amount recognized on the balance sheet consist of:				
Current pension liability		(19.1)		(9.0)
Non-current pension liability		(433.5)		(393.4)
Net amount recognized	**$**	**(452.6)**	$	(402.4)

(In millions)		2008			2007	
Amount recognized in regulatory assets and AOCI consist of:						
Net actuarial loss	**$**	**785.9**		$	586.1	
Prior service cost		**47.5**			43.9	
Net amount recognized	**$**	**833.4**	*****	$	630.0	*

* The above amounts are before adjustments for regulatory deferrals and deferred taxes

The estimated net actuarial loss and prior service cost for the defined benefit pension plans that will be amortized from accumulated other comprehensive income (loss) and regulatory assets into net periodic benefit cost during fiscal year 2009 are $58.9 million and $5.6 million, respectively.

The following pension benefit payments are expected to be paid:

(In millions)		Pension benefits
2009	$	358.6
2010	$	363.7
2011	$	368.0
2012	$	382.5
2013	$	401.6
2014-2018	$	2,096.6

Defined Contribution Plan

The Company also has several defined contribution pension plans primarily (section 401(k) employee savings fund plans) that cover substantially all employees. Employer matching contributions of approximately $27 million and $19 million were expensed in fiscal year 2008 and 2007, respectively.

Settlement Losses

The Company's pension plans have losses that have yet to be recognized in the income statement as a result of changes in the value of the projected benefit obligation and the plan assets due to experience different from that assumed and from changes in actuarial assumptions. Under SFAS No. 88, "Employers' Accounting for Settlements and Curtailments of Defined Benefit Pension Plans and for Termination Benefits," a company must recognize a portion of its loss immediately when payouts from a plan exceed a certain amount. During the fiscal year ended March 31, 2008, a pension settlement loss of $159,000 was recorded related to a nonqualified plan. It was not recoverable. Niagara Mohawk recognized a settlement loss of approximately $26 million during the fiscal year ended March 31, 2007 due to plan payouts that exceeded the threshold as prescribed in SFAS No. 88. During fiscal year 2007, Niagara Mohawk and the PSC staff reached an agreement that permits Niagara Mohawk to recover approximately 50 percent of the incurred pension settlement loss from rate payers.

Postretirement Benefits Other than Pensions

The Company's total net periodic benefit cost of PBOPs for the fiscal years ended March 31, 2008 and 2007 included the following components:

(In millions)		**2008**		2007
Service cost	**$**	**42.6**	$	28.2
Interest cost		**174.7**		121.5
Expected return on plan assets		**(101.7)**		(76.7)
Amortization of prior service cost		**13.3**		13.3
Amortization of net loss		**44.3**		43.9
Net periodic benefit cost before special termination benefits		**173.2**		130.2
Special termination benefits (VERO)		**1.4**		-
Net periodic benefit cost	**$**	**174.6**	$	130.2

The following table provides a reconciliation of the PBOP plans' funded status and the amounts recognized in the balance sheet at March 31:

(In millions)		**2008**		2007
Change in benefit obligation:				
Benefit obligation at beginning of period	**$**	**(2,216.0)**		(2,124.8)
Service cost		**(42.6)**		(28.2)
Interest cost		**(174.7)**		(121.5)
Actuarial loss		**19.0**		(6.9)
Benefits paid		**157.5**		118.3
Medicare subsidy		**(2.2)**		(5.4)
Plan amendments		**(0.2)**		-
Curtailment		**7.4**		-
Special termination benefits (VERO)		**(1.5)**		-
Acquisitions		**(1,286.9)**		(47.6)
Benefit obligation at end of period		**(3,540.2)**		(2,216.0)
Change in plan assets:				
Fair value of plan assets at beginning of period		**1,044.7**		988.2
Actual return on plan assets		**(32.8)**		100.9
Company contributions		**93.4**		53.2
Benefits paid		**(153.8)**		(110.6)
Acquisitions		**522.7**		13.0
Fair value of plan assets at end of period		**1,474.2**		1,044.7
Funded status	**$**	**(2,066.0)**	$	(1,171.3)

On August 24, 2007, the Company acquired KeySpan. In connection with this acquisition, the Company's assets and benefit obligations of the PBOP plan increased by $523 million and $1.3 billion, respectively.

On August 24, 2006, the Company acquired the Rhode Island gas distribution assets of New England Gas Company from Southern Union Company. In connection with this acquisition, the Company's assets and benefit obligation of the PBOP plan increased by $13 million and $48 million, respectively.

(In millions)		**2008**		2007
Amount recognized on the balance sheet consist of:				
PBOP liability	**$**	**(2,066.0)**	$	(1,171.3)
Net amount recognized	**$**	**(2,066.0)**	$	(1,171.3)

(In millions)		**2008**			2007	
Amount recognized in regulatory assets and AOCI consist of:						
Net actuarial loss	**$**	**585.9**		$	521.9	
Prior service cost		**93.3**			106.4	
Net amount recognized	**$**	**679.2**	*	$	628.3	*

* The above amounts are before adjustments for regulatory deferrals and deferred taxes.

The estimated net actuarial loss and prior service cost for the PBOP plans that will be amortized from regulatory assets into net periodic benefit cost during fiscal year 2009 are estimated to be $55.9 million and $13.3 million, respectively.

As a result of the Medicare Act of 2003, the Company receives a federal subsidy for sponsoring a retiree healthcare plan that provides a benefit that is actuarially equivalent to Medicare Part D.

The following PBOP benefit payments expected to be paid and subsidies expected to be received from the U.S. Federal Government, which reflect expected future services as appropriate are:

(In millions)		**Payments**		**Subsidies**
2009	$	190.2	$	10.7
2010	$	201.5	$	11.8
2011	$	212.4	$	12.8
2012	$	221.2	$	13.8
2013	$	228.0	$	14.9
2014-2018	$	1,241.7	$	82.1

The assumptions used in health care cost trends have a significant effect on the amounts reported. A one percent change in the assumed rates would have the following effects:

(in millions of dollars)		2008
Increase 1%		
Total of service cost plus interest cost	$	31.7
Postretirement benefit obligation	$	498.1
Decrease 1%		
Total of service cost plus interest cost	$	(26.0)
Postretirement benefit obligation	$	(423.8)

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; 560 employees enrolled in the VERO. Employees enrolled in the early retirement program will retire between October 1, 2007 and October 1, 2010. The cost of the VERO program is expected to be $147 million. The Company recorded $49 million of VERO costs for the fiscal year ended March 31, 2008, for program participants who retired as of April 1, 2008.

NOTE G – INCOME TAXES

The following is a summary of the components of federal and state income tax and reconciliation between the amount of federal income tax expense reported in the Consolidated Statements of Income and the computed amount at the statutory level.

Total income taxes from continuing operations in the consolidated statements of income are as follows:

		For the year ended March 31,	
(In millions of dollars)		**2008**	2007
Income taxes charged to operations	**$**	**354.8**	188.0
Income taxes credited to "Other income/deductions"		**(10.0)**	(4.0)
Total income taxes	**$**	**344.8**	184.0

		For the year ended March 31,	
(In millions of dollars)		**2008**	2007
Current income taxes	**$**	**421.4**	75.5
Deferred income taxes		**(76.6)**	108.5
Total income taxes	**$**	**344.8**	184.0

(In millions of dollars)	For the year ended March 31, **2008**	2007
Federal income taxes	**$ 279.6**	$ 152.2
State income taxes	**65.2**	31.9
Total income taxes	**$ 344.8**	$ 184.0

The income tax amounts included in the Statement of Income differ from the amounts that result from applying the statutory federal income tax rate to income before income tax. The following is a reconciliation between reported income tax and tax computed at the statutory rate of 35%:

(In millions of dollars)	For the year ended March 31, **2008**	**Percent**	2007	Percent
Computed tax at statutory rate	**$ 342.9**	**35.0**	$ 226.1	35.0
Increases (reductions) in tax resulting from:				
State income tax, net of federal income tax benefit	**39.9**	**4.1**	19.3	3.0
Book/tax depreciation not normalized	**16.1**	**1.6**	13.5	2.1
Intercompany Tax Sharing Adjustment	**(17.5)**	**(1.8)**	(28.0)	(4.0)
Medicare Subsidy	**(13.5)**	**(1.4)**	(12.7)	(1.9)
Cost of removal	**(10.1)**	**(1.0)**	(6.9)	(1.1)
Amortization of ITC, net	**(6.2)**	**(0.6)**	(6.2)	(1.0)
Reserve changes and other adjustments from prior years	**(2.5)**	**(0.3)**	(24.9)	(4.2)
All other differences	**(4.3)**	**(0.4)**	3.8	0.6
Total income taxes	**$ 344.8**	**35.2**	$ 184.0	28.5

With regulatory approval, the subsidiaries have adopted comprehensive interperiod tax allocation (normalization) for temporary book/tax differences.

At March 31, 2008 and 2007, the significant components of Company's deferred tax assets and liabilities calculated under the provisions of SFAS No.109 "Accounting for Income Taxes" were as follows:

(In millions of dollars)	At March 31, **2008**	**2007**
Property related differences	**$ 2,790.3**	$ 1,428.0
Merger rate plan stranded costs	**687.1**	758.2
Property taxes	**60.4**	-
Investment Tax Credit	**47.2**	45.9
State income taxes	**8.1**	-
Employee benefits compensation	**(840.8)**	(405.1)
Reserves not currently deducted	**(215.6)**	(87.7)
Regulatory Assets	**(51.6)**	-
Environmental costs	**(39.8)**	(38.2)
Other items-net	**(190.5)**	172.9
Net deferred tax liability (asset)	**2,254.8**	1,874.0
Current deferred tax asset	**(188.5)**	(176.2)
Non-current deferred tax liability	**$ 2,443.3**	$ 2,050.2

The company has a deferred tax asset of approximately $90 million for losses incurred by NGUSA in the state of Massachusetts that are carried forward to offset future earnings of the Company. Valuation allowances have been established for the full amount of these loss carry forwards as the Company believes that the losses will not be utilized in the foreseeable future.

As of March 31, 2008, the Company has approximately $324 million of additional state net operating losses which will expire between 2011 and 2022.

In July 2006, the Financial Accounting Standards Board ("FASB") issued Financial Interpretation ("FIN") 48, "Accounting for Uncertainty in Income Taxes," which clarifies the accounting for uncertainty in income taxes recognized in the financial statements in accordance with Statement of Financial Accounting Standards ("SFAS") 109, "Accounting for Income Taxes." FIN 48 provides that a tax benefit from an uncertain tax position may be recognized when it is more likely than not that the position will be sustained upon examination, assuming the taxing authority has full knowledge of all relevant information and that any dispute with a taxing authority is resolved by the court of last resort. Income tax positions must meet a more-likely-than-not recognition threshold at the effective date to be recognized upon the adoption of FIN 48 and in subsequent periods. Recognized tax benefits are measured as the largest amount of tax benefit that is more likely than not to be realized upon settlement with the taxing authority, assuming the taxing authority has full knowledge of all relevant information.

The Company adopted the provisions of FIN 48 on April 1, 2007. As a result of the implementation of FIN 48, the Company recognized approximately a $92 million increase in the liability for unrecognized tax benefits, which was accounted for as a reduction in retained earnings of $10.2 million, an increase to deferred tax assets of $32.3 million, and an increase to goodwill of $49.5 million to reflect the measurement under the rules of FIN 48 of uncertain tax positions related to previous business combinations

Reconciliation of Unrecognized Tax Benefits (in millions)		
Beginning balance, upon adoption as of April 1, 2007	$	93.3
Gross increases (decreases) related to current period		23.8
Settlements with tax authorities		14.5
Acquisitions*		343.1
Ending balance at March 31, 2008	$	474.7

*On August 24, 2007, the Company acquired KeySpan. In connection with this acquisition, KeySpan's tax liabilities, including liabilities for unrecognized tax benefits, were assumed by the Company.

As of March 31, 2008, the Company's unrecognized tax benefits totaled $474.7 million, of which approximately $126.5 million would affect the effective tax rate, if recognized. Also included in the balance of unrecognized tax benefits at March 31, 2008 are tax positions for which the ultimate deductibility is highly certain but for which there is uncertainty about the timing of such deductibility. Because of the effect of deferred income tax accounting, other than for interest and penalties, the disallowance of the shorter deductibility period would not affect the effective income tax rate but would accelerate the payment of cash to the taxing authority to an earlier period.

Effective as of April 1, 2007, the Company recognizes interest accrued related to uncertain tax positions as interest income or interest expense and related penalties if applicable as operating expenses. Accrued interest and penalties are included within the related liability lines in the consolidated balance sheet as of March 31, 2008. In prior reporting periods, the Company recognized such accrued interest and penalties in income tax expense and taxes payable. The Company has accrued no penalties related to the uncertain tax benefits noted above. In total, the Company has accrued a liability for interest of $54.2 million and $106.5 million as of March 31, 2007 and March 31, 2008 respectively. During the fiscal year ended March 31, 2008, the Company accrued interest expense of $20.4 million.

As of March 31, 2008, the Internal Revenue Service (IRS) completed its audit of the Company, excluding the KeySpan acquired companies, for the fiscal years ending March 31, 2003 and March 31, 2004. Certain adjustments proposed by the IRS are being appealed to the IRS Office of Appeals but the Company does not expect resolution within the next twelve months. The IRS is currently auditing the federal consolidated income tax returns of the Company, excluding the KeySpan acquired companies, for March 31, 2005 through March 31, 2007.

The IRS has also commenced the examination of KeySpan's consolidated income tax returns for the years ended December 31, 2000 through 2006. At this time, we cannot predict the result of these audits.

New York State has recently completed its audit, without change, of National Grid USA Service Company's separate company returns for the fiscal years ending March 31, 2003 through March 31, 2005. New York State is also currently auditing the combined report for fiscal years ending March 31, 2003 through March 31, 2005 for Niagara Mohawk. In addition, the Massachusetts Department of Revenue is conducting a field audit of the Company's Combined Returns for March 31, 2003 thru March 31, 2005. The Company is also in the process of appealing adjustments made by the Massachusetts Department of Revenue in a previous audit of its Massachusetts Combined Returns for January 1, 2000 thru March 31, 2002.

The Company believes that it is not reasonably possible that the tax liability for unrecognized tax benefits will significantly increase or decrease by March 31, 2009. As described above, the Company is subject to examination in the US and various state jurisdictions. At this time, the Company cannot predict the result of these audits or expect resolution within the next twelve months. The Company's, excluding the KeySpan acquired companies, fiscal years ended prior to March 31, 2003 are no longer subject to examination by federal or state authorities in the major jurisdictions in which the Company operates. The following table indicates the earliest KeySpan tax year subject to examination for each major jurisdiction:

Jurisdiction	Tax Year
Federal	2000
New York State	2000
Massachusetts	2000
New Hampshire	2003

On July 3, 2008 the state of Massachusetts signed into law H.4904 "An Act Improving Tax Fairness and Business Competitiveness" that imposes a combined reporting regime that will be effective for the Company's tax year beginning April 1, 2009. The Company is currently evaluating the impact of this law change and at this time cannot determine the full impact that the new law may have on its financial statements.

On April 9, 2007, New York State enacted its 2007 - 2008 budget, which included amendments to the state income tax. Those amendments include a reduction in the corporate net income tax rate to 7.1% from 7.5%, and the adoption of a single sales factor for apportioning taxable income to New York State. Both amendments are effective January 1, 2007. The Company has evaluated the effects of the amendments and believes that the amendments will not have a material effect on its financial position, cash flows or results of operation.

NOTE H – LONG-TERM DEBT

Notes Payable**.** In 2006, KeySpan issued at KEDNY and KEDLI, respectively, $400 million and $100 million of Senior Unsecured Notes at 5.6% due November 29, 2016. Additionally, KEDLI has $400 million of 7.875% Medium-Term Notes due February 1, 2010, outstanding at March 31, 2008 which is guaranteed by KeySpan.

KeySpan also has $1.9 billion of medium and long term notes outstanding of which $950 million of these notes were associated with its acquisition of Eastern Enterprise and EnergyNorth Inc. These notes were issued in two series as follows: $700 million of 7.625% Notes due 2010 and $250 million of 8.00% Notes due 2030. KeySpan also has $160 million of 4.9% notes outstanding with a maturity date of May 2008 and $307.2 million of 5.8% notes outstanding with a maturity date of April 2035 issued pursuant to the MEDS Equity Units conversion in 2005. The remainder of KeySpan's debt of $483.0 million had interest rates ranging from 4.65% to 9.75%. KEDLI repaid $125 million of Medium-Term Notes at 6.90% at time of maturity, January 15, 2008.

Niagara Mohawk has a $600 million Senior Note with an interest rate of 7.75% due October 1, 2008. This note is currently callable with make-whole provisions.

Granite State had $15 million of long-term debt at March 31, 2008. This is made up of three $5 million notes. The first $5 million has an interest rate of 7.37% and has a maturity date of November 2023; the second $5 million has an interest rate of 7.94% and has a maturity date of July 2025; and the third $5 million has an interest rate of 7.3% and has a maturity date of June 2028. Granite State's long-term debt covenants provide for certain restrictive covenants and acceleration clauses. These covenants stipulate that note holders may declare the debt to be due and payable if total debt becomes greater than 70% of total capitalization. At March 31, 2008, the total long-term debt was 17% of total capitalization.

New England Hydro Finance had $41.2 million of 9.41% notes at March 31, 2008. These bonds have a monthly sinking fund requirement which totaled $5.7 million during fiscal year end March 31, 2008. The monthly sinking fund requirement will be $0.4 million until 2015. Debt covenants provide for certain restrictive covenants and acceleration clauses. These covenants stipulate that note holders may declare the debt to be due and payable if total debt becomes greater than 70% of total capitalization. At March 31, 2008, the total debt was 59% of total capitalization.

European Medium Term Note Program
At March 31, 2008, NGUSA had a Euro Medium Term Note program (the "Program") under which it is able to issue debt instruments ("Instruments") up to a total of the equivalent of 4 billion Euro. At March 31, 2008, $159.1 million of these notes were issued and outstanding, including the impact from the cross currency and interest rate swaps. Interest rates at March 31, 2008 ranged from 3.55% to 5.51%.

Instruments issued under the Program are admitted to trading on the London Stock Exchange. The Program commenced in December 2007 and is expected to be renewed annually for the foreseeable future. The funds raised under the Program may be used for general corporate purposes. Instruments may be issued in bearer form in any currency, with maturities ranging from one month to perpetuity. Instruments may not be offered, sold or delivered within the United States (US) or to a US person except in certain limited circumstances permitted by US regulations. Any fees associated with issuing Instruments under the Program are negotiated with the bank(s) managing the issuance at the time. Instruments issued under the Program rank pari passu with each other and with all other unsecured debt obligations of the Company, except to the extent that other debt obligations may be subordinated. Instruments carry certain positive and negative covenants, including a restriction on the Company's ability to mortgage, pledge, charge or otherwise encumber its assets in order to secure, guarantee or indemnify other listed or quoted debt obligations, as well as cross-acceleration in the event of breach by the Company or its principal subsidiaries of other listed or quoted debt obligations. At March 31, 2008, the Company was in compliance with all covenants.

Gas Facilities Revenue Bonds. KEDNY can issue tax-exempt bonds through the New York State Energy Research and Development Authority ("NYSERDA"). Whenever bonds are issued for new gas facilities projects, proceeds are deposited in trust and subsequently withdrawn to finance qualified expenditures. There are no sinking fund requirements on any of our Gas Facilities Revenue Bonds ("GFRBs"). At March 31, 2008, $640.5 million of GFRBs were outstanding $230 million of which are variable-rate auction bonds. The interest rate on the variable rate series due through July 1, 2026 is reset weekly and ranged from 3.00% to 6.27% for the period January 1, 2007 through March 31, 2008. The variable-rate auction bonds are currently in the auction rate mode and are backed by bond insurance. Credit rating agencies have recently downgraded the ratings of the bond insures. The resulting interest rate on the bonds revert to the maximum rate which depends on the current commercial paper rates and the senior unsecured rating of KEDNY or the bond insurer, whichever is greater. To date, the effect on interest expense has not been material.

Promissory Notes to LIPA. KeySpan and certain of its subsidiaries issued promissory notes to LIPA to support certain debt obligations assumed by LIPA in May 1998. At March 31, 2008, $155.4 million of these promissory notes remained outstanding with maturity dates between 2013 and 2025. Under these promissory notes, KeySpan is required to obtain letters of credit to secure its payment obligations if its long-term debt is not rated at least in the "A" range by at least two nationally recognized statistical rating agencies. At March 31, 2008, KeySpan was in compliance with this requirement.

Industrial Development Revenue Bonds. At March 31, 2008, KeySpan had outstanding $128.3 million of tax-exempt bonds with a 5.25% coupon maturing in June 2027 - $53.3 million dollars of these Industrial Development Revenue Bonds were issued in its behalf through the Nassau County Industrial Development Authority for the construction of the Glenwood Energy Center, an electric-generation peaking plant, and the balance of $75 million was issued in its behalf by the Suffolk County Industrial Development Authority for the Port Jefferson Energy Center an electric-generation peaking plant. KeySpan has guaranteed all payment obligations of these subsidiaries with regard to these bonds.

First Mortgage Bonds. Colonial Gas Company had outstanding $85 million of first mortgage bonds at March 31, 2008. These bonds are secured by gas utility property. The first mortgage bond indentures include, among other provisions, limitations on: (i) the issuance of long-term debt; (ii) engaging in additional lease obligations; and (iii) the payment of dividends from retained earnings. At March 31, 2008, these bonds remain outstanding and have interest rates ranging from 6.3% to 8.8% and maturities that range from 2008-2028. Colonial repaid $10 million of First Mortgage Bonds on their maturity date in March 2008.

Substantially all of the properties and franchise of Narragansett and Mass Electric are subject to the lien of mortgage indentures under which the First Mortgage Bonds have been issued. At March 31, 2008, Narragansett and Mass Electric had approximately $65 million and $55 million outstanding, respectively. During fiscal year end March 31, 2008, Narragansett redeemed $7 million and $3 million of 7.39% bonds due in 2027. During fiscal year end March 31, 2008 Mass Electric redeemed three series of bonds totaling $40 million with various rates and various end maturity dates. At March 31, 2008, Narragansett's bond interest rates range from 6.65% to 10.25% and maturities range from June 2008 to December 2025. These bonds have $1.6 million annual sinking fund requirements. Mass Electric's bond interest rates range from 5.72% to 6.66% and maturities range from June 2008 to November 2008.

State Authority Financing Bonds. Certain of KeySpan's electric generation subsidiaries can issue tax-exempt bonds through the NYSERDA. At March 31, 2008, $41.1 million of Authority Financing Notes 1999 Series A Pollution Control Revenue Bonds due October 1, 2028 were outstanding. The interest rate on these notes is reset based on an auction procedure. The interest rate ranged from 3% to 17.75% during the period January 1, 2007 through March 31, 2008, at which time the rate was 6.85%.

KeySpan also has outstanding $24.9 million variable rate 1997 Series A Electric Facilities Revenue Bonds due December 1, 2027. The interest rate on these bonds is reset weekly and ranged from 1.23% to 5.6% for the period January 1, 2007 through March 31, 2008, at which time the rate was 3.6%.

NEP had $410.3 million of Pollution Control Revenue Bonds at March 31, 2008 issued through Business Finance Authority of the State of New Hampshire, Massachusetts Industrial Finance Authority, and Connecticut Development Authority. The Pollution Control Revenue Bonds are in tax-exempt commercial paper mode at March 31, 2008. Interest rates ranged from 1.75% to 2.45%. There are no payments or sinking fund requirements due in 2009 through 2013. At March 31, 2008, NEP had lines of credit and standby bond purchase facilities with banks totaling $440 million, which is available to provide liquidity support for these bonds and for other corporate purposes. The agreement with banks that provide NEP's line of credit and standby bond purchase facility expires on November 29, 2009. There were no borrowings under these facilities at March 31, 2008.

Substantially all of Niagara Mohawk's operating properties are subject to mortgage liens securing its mortgage debt. At March 31, 2008, $650 million was outstanding. Several series of First Mortgage Bonds were issued to secure a like amount of tax-exempt revenue bonds issued through NYSERDA. Approximately $575 million of such securities bear interest at short-term adjustable interest rates (with an option to convert to other rates, including a fixed interest rate) which averaged 4.36% for the fiscal year ended March 31, 2008. The bonds are currently in the auction rate mode and are backed by bond insurance. Credit rating agencies have recently downgraded the ratings of the bond insurers. The resulting interest rate on the bonds revert to the maximum rate which depends on the current commercial paper rates and the senior secured rating of Niagara Mohawk or the bond insurer, whichever is greater. The effect on interest expense has not been material at this time. The remaining $75 million are fixed rate pollution control revenue bonds which are first callable on November 1, 2008 at 102%. Pursuant to agreements between NYSERDA and Niagara Mohawk, proceeds from such issues were used for the purpose of financing the construction of certain pollution control facilities at Niagara Mohawk's generation facilities (which Niagara Mohawk subsequently sold) or to refund outstanding tax-exempt bonds and notes.

Mass Electric had $40 million outstanding at March 31, 2008 issued through Massachusetts Industrial Finance Agency. The bonds are in tax-exempt commercial paper mode with a variable interest rate of 2.40% at March 31, 2008. Of the $40 million outstanding $20 million was due on August 1, 2008 and the remaining $20 million is due on August 1, 2014. At March 31, 2008, Mass Electric had a standby bond purchase facility with banks totaling $45 million which is available to provide liquidity support for these bonds. The agreement with banks that provide the Mass Electric's standby bond purchase facility expires on November 29, 2009. There were no borrowings under this facility at March 31, 2008.

At March 31, 2008, Nantucket Electric had $53 million of tax exempt bonds in commercial paper mode with variable maturity dates and variable interest rates ranging from 1.10% to 2.83%. The tax exempt bonds are guaranteed by Mass Electric and have maturities from March 2016 through August 2042. Mass Electric unconditionally guarantees the full and prompt payment of the principal premium, if any, and interest on these tax exempt bonds. The bonds were issued by the Massachusetts Development Finance Agency in connection with Nantucket Electric's financing of its first and second underground and submarine cable projects. Mass Electric would be required to make any principal, interest or premium payments if Nantucket Electric failed to pay. This guarantee is absolute and unconditional. At March 31, 2008, Nantucket Electric had a standby bond purchase facility with banks totaling $70 million which is available to provide liquidity support for these tax-exempt bonds. The agreement with banks that provide the Nantucket Electric's standby bond purchase facility expires on November 29, 2009. There were no borrowings under this facility at March 31, 2008.

Committed Facility Agreements. At March 31, 2008, the Company had three committed bank loans outstanding. At March 31, 2008 $382.5 million were outstanding, including the impact from the cross currency and interest rate swaps. These loans, which mature in 2011, are in various currencies and were used to provide funds for working capital needs. The interest rates on these bank loans are reset periodically and range from 0.40% to 0.55% over issued currency LIBOR rate.

Inter-Company Notes. At March 31, 2008, Niagara Mohawk Holdings, Inc. has $1.2 billion of inter-company note due to an affiliate of the Parent. This note has an interest rate of 5.52% and matures in November 2010.

Debt Maturity. The following table reflects the maturity schedule for our debt repayment requirements, including capitalized leases and related maturities, at March 31, 2008:

(In Millions of Dollars)	Long-Term Debt
Repayment for fiscal years:	
2009	$ 992.6
2010	757.1
2011	1,302.0
2012	174.7
2013	517.2
Thereafter	3,803.5
	$ 7,547.1

Long-term Debt*:* The following tables depict the fair values and carrying values of the Company's long-term debt at March 31, 2008 and 2007.

Fair Values of Long-Term Debt

	At March 31,	
(In Millions of Dollars)	2008	2007
Notes	$ 3,720.9	$ 892.7
Gas Facilities Revenue Bonds	636.0	-
Promissory Notes	155.9	-
Tax Exempt Bonds	120.6	-
First Mortgage Bonds	230.5	188.6
State Authority Financing Bonds	1,221.1	1,157.9
Committed Facilities	389.4	-
Inter-company Notes	1,200.0	1,200.0
	$ 7,674.4	$ 3,439.2

Carrying Values of Long-Term Debt

(In Millions of Dollars)	At March 31, 2008	2007
Notes	$ 3,615.4	$ 861.9
Gas Facilities Revenue Bonds	640.5	-
Promissory Notes	155.4	-
Tax Exempt Bonds	128.3	-
First Mortgage Bonds	205.1	171.7
State Authority Financing Bonds	1,219.9	1,155.5
Committed Facilities	382.5	-
Inter-company Notes	1,200.0	1,200.0
	$ 7,547.1	$ 3,389.1

The Ravenswood Master lease is classified as a discontinued liability on the Consolidated Balance Sheet. The Fair Value and Carrying Value of the Ravenswood Master Lease at March 2008 were $423.3 million and $412.3 million, respectively. All other financial instruments included in the Consolidated Balance Sheet such as cash, commercial paper, accounts receivable, accounts payable and short-term debt instruments are stated at amounts that approximate fair value.

Standby Bond Purchase Agreement

At March 31, 2008 New England Power, Mass Electric and Nantucket Electric had a Standby Bond Purchase facility with banks totaling $325 million, which is available to provide liquidity support for certain tax-exempt bonds. The agreement limits are $210 million for New England Power, $45 million for Mass Electric and $70 million for Nantucket Electric. The fees for the facility are based on each entity's credit rating and are increased or decreased based on a downgrading or upgrading of the entity's rating. The facility fee for Nantucket Electric is based on the credit rating of Mass Electric. The current annual facility fee is 0.100% based on Mass Electric's and New England Power's credit rating of A3 by Moody's Investor Services and A- by Standard & Poor's.

The facility contains certain financial covenants that require New England Power and Mass Electric to maintain a debt to total capitalization ratio of no more than 65% at the last day of each fiscal quarter. For this calculation, indebtedness of Mass Electric does not include the guaranties by Mass Electric of certain tax-exempt bonds issued by Nantucket Electric and up to $50 million of additional indebtedness of Nantucket Electric. At March 31, 2008, New England Power's indebtedness was 28% of its total capitalization and Mass Electric's indebtedness was 20% of its total capitalization. The agreement expires on November 29, 2009. There were no borrowings under the standby bond purchase agreement at March 31, 2008

Credit Facility Agreements

At March 31, 2008, the Company and certain of its subsidiaries had a Credit Facility agreement with a number of banks totaling $355 million, which is available to provide letter of credit support and, in the case of New England Power, to provide liquidity support and other corporate purposes. The agreement provides for an aggregate letter of credit limit of $125 million, and a New England Power borrowing limit of $230 million within which is included a New England Power letter of credit limit of $30 million. The facility fee and utilization fee for the facility are based on the credit rating of New England Power and is increased or decreased based on a downgrading or upgrading of the rating. The current annual facility fee is 0.100% and the utilization fee is 0.125% based on New England Power's credit rating of A3 by Moody's Investor Services and A- by Standard & Poor's. The facility contains certain financial covenants that require the Company and certain of its subsidiaries named in the facility to maintain a debt to total capitalization ratio of no more than 65% at the last day of each fiscal quarter. For this calculation, indebtedness of Mass Electric does not include guaranties by Mass Electric of certain tax-exempt bonds issued by Nantucket Electric and of up to $50 million of additional indebtedness of Nantucket Electric. At March 31, 2008, the Company and each of its subsidiaries named in the facility were in compliance with this covenant. The agreement expires on November 29, 2009. At March 31, 2008 $42.4 million of letters of credit have been issued.

NOTE I – SHORT-TERM DEBT

Commercial Paper and Revolving Credit Agreements.

At March 31, 2008, KeySpan had two credit facilities totaling $1.5 billion - $920 million for five years through 2010, and $580 million through 2009, which continue to support KeySpan's commercial paper program for ongoing working capital needs.

The fees for the facilities are based on KeySpan's current credit ratings and are increased or decreased based on a downgrading or upgrading of our ratings. The current annual facility fee is 0.08% based on our credit rating of Baa1 by Moody's Investor Services and A- by Standard & Poor's for each facility. Both credit facilities allow for KeySpan to borrow using several different types of loans; specifically, Eurodollar loans, ABR loans, or competitively bid loans. Eurodollar loans are based on the Eurodollar rate plus a margin that is tied to our applicable credit ratings. ABR loans are based on the higher of the Prime Rate, the base CD rate plus 1%, or the Federal Funds Effective Rate plus 0.5%. Competitive bid loans are based on bid results requested by KeySpan from the lenders. We do not anticipate borrowing against these facilities; however, if the credit rating on our commercial paper program were to be downgraded, it may be necessary to do so.

The facilities contain certain affirmative and negative operating covenants, including restrictions on KeySpan's ability to mortgage, pledge, encumber or otherwise subject its utility property to any lien, as well as certain financial covenants that require us to, among other things, maintain a consolidated indebtedness to consolidated capitalization ratio of no more than 65% at the last day of any fiscal quarter. Violation of these covenants could result in the termination of the facilities and the required repayment of amounts borrowed thereunder, as well as possible cross defaults under other debt agreements. At March 31, 2008, KeySpan was in compliance with all covenants.

Subject to certain conditions set forth in the credit facility, KeySpan has the right, at any time, to increase the commitments under the $920 million facility up to an additional $300 million. In addition, KeySpan has the right to request that the termination date be extended for an additional period of 365 days prior to each anniversary of the closing date. This extension option, however, requires the approval of lenders holding more than 50% of the total commitments to such extension request. Under the agreements, KeySpan has the ability to replace non-consenting lenders with other pre-approved banks or financial institutions.

At March 31, 2008, $286.8 million of commercial paper was outstanding and KeySpan had the ability to issue up to an additional $1.2 billion under its commercial paper program.

At March 31, 2008, the Company was a named borrower under a credit facility in the name of the Parent totaling $1.5 billion. This facility supports the Parent's and the Company's commercial paper programs for ongoing working capital needs.

The current annual facility fee is 0.09%. The credit facility allows both the Parent and the Company to borrow in Sterling or US Dollars, at the appropriate LIBOR rate plus a margin of 0.325%, or 0.375% if over $750 million has been borrowed under the facility. We do not anticipate borrowing against this facility; however, if for any reason we were not able to issue sufficient commercial paper or source funds from other sources, it may be necessary to do so. The facility contains certain affirmative and negative operating covenants, including restrictions on the Company's utility subsidiaries' ability to mortgage, pledge, encumber or otherwise subject their utility property to any lien, as well as financial covenants that require the Company and the Parent to limit the total indebtedness in US and non-US subsidiaries to pre-defined limits. Violation of these covenants could result in the termination of the facilities and the required repayment of amounts borrowed there under, as well as possible cross defaults under other debt agreements. At March 31, 2008 the Company was in compliance with all covenants.

Subject to certain conditions set forth in the credit facility, the Parent and the Company have the right to "Term Out" the facility, whereby they may borrow in total up to the full facility amount of $1.5 billion and this borrowing may remain outstanding for a further year beyond the expiration date of the facility. In addition, the Parent has the right to request that the termination date be extended for an additional period of 364 days prior to each anniversary of the closing date. This extension option requires the approval of lenders holding more than 50% of the total commitments to such extension request and only the lenders that consent will have their commitment extended. Under the agreements, the Parent has the ability to replace non-consenting lenders with other banks or financial institutions.

At March 31, 2008, $828.2 million of commercial paper was outstanding under this facility. At March 31, 2008, the Company had the ability to issue up to an additional $672 million under this facility.

Uncommitted Facility Agreements

At March 31, 2008, the Company had uncommitted loan facilities totaling $720 million available from five banks of which, $298 million was outstanding at March 31, 2008. These facilities provide liquidity for ongoing working capital needs by allowing the Company to borrow at very short notice. However, the lenders are not obliged to make a loan under the facilities at any time. The interest rates are set at the time of issuance and range from 20 basis points to 45 basis points over LIBOR. Maturities are also set at the time of issuance and differ for from lender to lender. The drawn amounts outstanding at March 31, 2008 matured in April and May 2008.

Inter-company money pool

The Company and certain subsidiaries operate a money pool to more effectively utilize cash resources and to reduce outside short-term borrowings. Short-term borrowing needs are met first by available funds of the money pool participants. Borrowing companies pay interest at a rate designed to approximate the cost of third-party short-term borrowings. 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 pool at any time without prior notice. The Company has the ability to borrow up to $4 billion from the Parent (through intermediary entities) and certain other subsidiaries of the Parent, including for the purpose of funding the money pool, if necessary. At March 31, 2008, the Company had borrowed $850 million under this arrangement. Additionally, the Company has a $286.4 million promissory note outstanding with an affiliate of the Parent for the partial financing of certain notes issued by the Parent.

NOTE J – CUMULATIVE PREFERRED STOCK

The Company's subsidiaries have certain issues of non-participating preferred stock which provide for redemption at the option of the Company, as shown in the table below. From time to time, the Company's subsidiaries repurchase shares of its common stock or its preferred stock when it is approached on behalf of its shareholders. In fiscal year 2008, three of the subsidiaries redeemed total shares of 203,822 of its preferred stock for a combined consideration of $17 million.

A summary of cumulative preferred stock at March 31, 2008 and 2007 is as follows (in thousands except for share data and call price):

	Company	Shares Outstanding		Amount (in millions)		Call Price
		March 31, 2008	March 31, 2007	**March 31, 2008**	March 31, 2007	
$100 par value -						
3.40% Series	Niagara Mohawk	**57,524**	57,536	**$ 5.7**	$ 5.7	$ 103.500
3.60% Series	Niagara Mohawk	**137,139**	137,139	**13.7**	13.7	104.850
3.90% Series	Niagara Mohawk	**94,967**	94,967	**9.5**	9.5	106.000
4.10% Series	Niagara Mohawk	**-**	52,830	**-**	5.3	102.000
4.44% Series	Mass Electric	**22,585**	22,585	**2.3**	2.3	104.068
4.76% Series	Mass Electric	**-**	24,680	**-**	2.4	103.730
4.85% Series	Niagara Mohawk	**-**	35,128	**-**	3.5	102.000
5.25% Series	Niagara Mohawk	**-**	34,115	**-**	3.4	102.000
6.00% Series	New England Power	**11,117**	11,117	**1.1**	1.1	(a)
$50 par value -				**-**	-	
4.50% Series	Narragansett	**49,089**	49,089	**2.5**	2.5	55.000
4.64% Series	Narragansett	**-**	57,057	**-**	2.9	52.125
Total		**372,421**	576,243	**$ 34.8**	$ 52.3	

(a) Noncallable

NOTE K – COST OF REMOVAL AND ASSET RETIREMENT OBLIGATION

SFAS No. 143, "Accounting for Asset Retirement Obligations" provides the accounting requirements for retirement obligations associated with tangible long-lived assets. Asset retirement obligations arising from legal obligations as defined under SFAS No. 143 amounted to $48.7 million at March 31, 2008. 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 SFAS No. 143 definition of an asset retirement obligation 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 to a regulatory liability account to reflect future use. The Company estimates it has collected over time approximately $1.3 billion and $642 million for cost of removal through March 31, 2008 and 2007, respectively.

NOTE L –ACQUISITIONS

Acquisition of KeySpan

On August 24, 2007 National Grid plc purchased all the outstanding stock of KeySpan Corporation for $42.00 per share in cash. The transaction has been accounted for using the purchase method of accounting for business combinations in accordance with SFAS 141 "Business Combination." As a result of the acquisition, KeySpan ceased to be publicly traded. The purchase price of $7.6 billion was allocated to KeySpan's assets and liabilities based on their estimated fair values at the date of acquisition. The historical cost basis of KeySpan's assets and liabilities associated with its gas distribution businesses, with minor exceptions, was determined to represent fair value due to the existence of regulatory-approved rate plans based upon the recovery of historical costs and a fair return thereon. Further, the historical cost basis of assets and liabilities associated with electric generating units on Long Island that are under long-term power supply agreements with LIPA, with minor exceptions, was determined to represent fair value due to the Power Supply Agreement with LIPA that provides for the recovery of historical costs and a fair return thereon. The excess of the purchase price over the fair value of the net assets acquired, or goodwill, was calculated to be $3.9 billion including previously recorded goodwill at KeySpan. KeySpan has been consolidated into National Grid plc from August 24, 2007 onward.

The following table summarizes the fair value adjustments and calculation of goodwill:

(In Millions of Dollars)	
Purchase Price	$ 7,574.3
KeySpan's Consolidated Equity at August 24, 2007	4,300.8
Goodwill Prior to Acquisition	1,665.9
KeySpan's Adjusted Consolidated Equity	2,634.9
Goodwill before Fair Value Adjustments	4,939.4
Fair Value Adjustments	
Assets Impacted:	
Accounts Receivable	(12.4)
Inventory	251.5
Other Property and Investments	(11.3)
Property Plant and Equipment	224.4
Regulatory Assets	221.6
Other Non-Current Assets	(75.3)
Liabilities Impacted:	
Accounts Payable	(46.7)
Accrued Taxes	(130.1)
Regulatory Liabilities	(189.6)
Accrued Employee Pension and Other Benefits and Reserves	(145.1)
Other Non-current Liabilities	(612.2)
Accumulated Deferred Income Tax	(20.0)
Long-term Debt	(58.2)
Net Adjustment	(603.4)
Intangible Asset Adjustment	230.8
Assets Held for Sale Fair Value Adjustments	1,373.7
Total Goodwill After Acquisition	$ 3,938.3

A discussion of the more significant fair value adjustment follows.

Other property and investments: KeySpan owns a 600,000 barrel liquefied natural gas ("LNG") storage and receiving facility in Providence, Rhode Island, through its wholly owned subsidiary KeySpan LNG. KeySpan LNG proposed to upgrade the liquefied natural gas facility to accept marine deliveries and to triple vaporization (or regasification) capacity to provide these services. The proposed upgrade was subject to numerous FERC proceedings, as well as proceedings with the Federal District Court in Rhode Island. At the time of the KeySpan acquisition, National Grid plc decided not to pursue the upgrade of the LNG facility. As a result, deferred project costs of $11.3 million were written-off as a direct charge to equity.

Property, Plant and Equipment: As required by SFAS 141, upon acquisition KeySpan calculated the fair value of its property, plant and equipment for all its business segments. As noted previously, the historical cost basis of KeySpan's assets and liabilities associated with its gas distribution businesses, with minor exceptions, was determined to represent fair value due to the existence of regulatory-approved rate plans based upon the recovery of historical costs and a fair return thereon. Further, the historical cost basis of KeySpan's electric generating units on Long Island that are under long-term power supply agreements with LIPA, with minor exceptions, was determined to represent fair value. The historical cost basis of property, plant and equipment related to KeySpan's non-regulated business, primarily land, was increased by $263.2 million to represent fair value at date of acquisition.

As discussed in Note A - "Significant Accounting Policies" under Item 9 – "Depreciation and Amortization", the Company maintains gas production and development activities through its two wholly-owned subsidiaries - KeySpan Exploration and Seneca-Upshur. As of March 31, 2008, the Company estimated that the capitalized costs associated with natural gas and oil reserves of these entities did not exceed the ceiling test limitation. However, the fair value exercise associated with SFAS 141 required a higher level of estimated operating costs and capital expenditures, compared to the same estimates required to be used in the ceiling test calculation resulting in a write down of $30 million to the natural gas and oil reserves.

As part of its synergy savings strategy, the Company is relinquishing three floors in its Brooklyn headquarters at MetroTech. As a result, the Company reduced its property, plant and equipment by $10.3 million associated with past leasehold improvement costs. Additionally, the Company will incur a $10 million fee in consideration for the early termination of part of its lease of the MetroTech office. This fee has been recorded as a current liability on the Consolidated Balance Sheet.

Regulatory Assets and Reserves: Upon acquisition, KeySpan made certain adjustments to its pension and other postretirement reserve balances, as well as to its environmental reserve balances. KeySpan adjusted certain assumptions underlying the calculations for its pension and other postretirement reserves to align those assumptions with National Grid pension and postretirement reserve assumptions where appropriate. This alignment reduced KeySpan's pension and other postretirement reserves approximately $180 million. Certain gas distribution subsidiaries are subject to certain deferral accounting requirements mandated by the various state regulators for pension costs and other postretirement benefit costs. As a result, approximately $109 million of the decrease to the pension and other postretirement reserves was recorded as an "offset" to regulatory assets.

KeySpan also adjusted certain assumptions underlying the calculations for its environmental reserve to align those assumptions with National Grid plc's environmental reserve assumptions where appropriate. This alignment increased the Company's environmental reserve approximately $343 million. Certain gas distribution subsidiaries are subject to certain deferral accounting requirements mandated by the various state regulators for environmental costs. As a result, approximately $331 million of the increase to the environmental reserve was recorded as an "offset" to regulatory assets.

As noted in Note C, “Commitments and Contingencies”, the United States Court of Appeals for the District of Columbia Circuit ("Court") denied the petitions of the NYISO and various New York Transmission Owners seeking refunds for charges in the January - March 2000 reserve market. As a result of this favorable decision, KeySpan reversed a previously established reserve for these proceedings of $18.1 million. As required by SFAS 141, this amount was recorded as a direct benefit to equity.

Accounts Payable and Other Liabilities: As discussed in Note E, “Derivative Contracts and Hedging Activities”, on March 7, 2008, the FERC approved the NYISO In-City capacity mitigation measures and revised the In-City capacity bid caps. The revised bid caps are expected to result in the Swap Agreement (between the Company and Morgan Stanley) floating price being set to equal the strike price, thereby eliminating all cash flow between the two parties for the remaining term of the Swap Agreement. The fair value of this derivative instrument was calculated to be a liability of $17.9 million at August 24, 2007; such amount was recorded as a current liability and a direct charge to equity.

Prior to the KeySpan Acquisition, KeySpan had a proposed project for the construction of a 250 MW combined cycle electric generation plant. In anticipation of this facility, KeySpan purchased a gas turbine generator several years ago. KeySpan and LIPA executed a “memo of understanding” for a power purchase agreement (“PPA”) in 2001; however the PPA was never executed by LIPA. As previously noted, the NYPSC ordered the Company to divest the Ravenswood Generating Station to mitigate concerns on vertical market power. National Grid plc is proceeding with such divestiture and as a result it is highly unlikely that a new investment in electric generation by National Grid plc would be possible. As a result, a $7.5 million current liability was recorded for consideration of contract breakage costs associated with a maintenance contract for the gas turbine generator.

As discussed in Note C, “Commitments and Contingencies”, on May 31, 2007, KeySpan received a Civil Investigative Demand (“CID”) from the United States Department of Justice, Antitrust Division, requesting the production of documents and information relating to its investigation of competitive issues in the New York City electric energy capacity market. A $5.3 million current liability was recorded representing the fair value for estimated legal fees associated with this proceeding.

Regulatory Liabilities: As part of the NYPSC approval of the KeySpan Acquisition, a Gas Rates Joint Proposal (“the Rates JP”) was agreed to by KeySpan, the NYPSC and the other parties. The Rates JP provides for five-year rate plans for KEDNY and KEDLI which go into effect on January 1, 2008. Included in the Rates JP are approximately $189.6 million of certain ratepayer refunds that were agreed to by KEDNY and KEDLI. The significant terms of the Rates JP are discussed in Note B - “Rate and Regulatory.”

Long-term Debt: As part of the fair value exercise, KeySpan calculated the fair value of outstanding debt for all its non-regulated enterprises. This analysis required KeySpan to eliminate prior balances associated with debt discounts and premiums, as well as settled interest rate hedges that were being amortized. A $58 million long-term liability was recorded as a result of this fair value analysis. The long-term debt associated with certain regulated gas distribution businesses were not fair valued due to the existence of regulatory-approved rate plans that provide for the recovery of historical costs.

Intangible Asset: In addition to the above, certain intangible assets were created as a result of the acquisition. The MSA Agreement and the EMA Agreement with LIPA were valued at $150.7 million. These intangible assets will be amortized over 20 years and 6 years respectively. Additionally, intangible assets of $35.4 million were recorded for appliance service subsidiaries. These intangible assets relate to contractual relationships and plumbing licenses. The intangible asset associated with the plumbing license will be amortized over eight years, while the intangible asset associated with contractual relationships has an indefinite life.

Fair Value of Assets Held for Sale: As part of the purchase accounting exercise and in conjunction with the sale of the Ravenswood Generating Station and the engineering and telecommunications companies, an evaluation of the fair value of these investments was conducted. The evaluation resulted in an increase to the net book value of these companies of approximately $1.3 billion, net of deferred taxes and estimated selling costs.

Other Items: As discussed in Note C, "Commitments and Contingencies" the Company will continue to be responsible for lease payments under the Sale/Leaseback arrangement associated with the Ravenswood Expansion throughout the remaining life of the arrangement. The remaining lease payments have been valued at $363 million; such amount has been recorded in deferred credits and other liabilities.

KeySpan is entitled to emission credits associated with its electric generating facilities on Long Island. These emission credits had a fair value of $296.2 million on August 24, 2007. As agreed to in the EMA Agreement with LIPA, LIPA is entitled to $251.5 million of this amount which is included in inventory. The LIPA portion of the emission credits is reflected in deferred credits and other non-current liabilities and $44.7 million as an intangible asset.

As allowed for under SFAS 141, the fair value measurement of assets, liabilities and intangible assets, and the resulting impact on goodwill and related allocations to the Company's business units can be adjusted during the allocation period. However, such period is not to exceed one year. The fair value measurements discussed above are subject to change as a result of the following: (i) continued measurement of the fair value of the Ravenswood Generating Station assets that are held for sale; (ii) continued measurement of the fair value of the LIPA Service Agreements; (iii) finalization and measurement of the financial implications associated with the more significant aspects of the Gas Rates Joint Proposal;" (iv) measurement of the financial implications of the more significant aspects of the LIPA Service Agreement amendments; (v) continued measurement and identification of intangible assets; (vi) continue assessment of the deferred tax implications associated with the above adjustments and (vii) continued review of contingent liabilities. The preceding list is not intended to be all inclusive and the final determination of goodwill and intangible assets may be impacted by other fair value measurement adjustments.

Acquisition of Rhode Island Gas Assets

In fiscal year 2007, (August 24, 2006), the Company, acquired the Rhode Island gas distribution assets of New England Gas Company from Southern Union Company for approximately $574 million which consisted of $497 million in cash and the assumption of $77 million of debt. The Company received a contribution from the Parent company in the amount of $500 million to finance the acquisition, which is reflected in "Additional paid in capital". As part of this transaction, the Company also acquired four small non-regulated businesses.

The acquisition was accounted for using the purchase method of accounting under SFAS 141. The assets acquired and liabilities assumed have been recorded in Narragansett's balance sheet beginning August 24, 2006 at their fair values and the results of operations have been included in the Company's statement of operations since August 24, 2006. Therefore, the Consolidated Balance Sheet and Statements of Operations for the periods subsequent to the acquisition are not comparable to the same periods in prior years.

The following table summarizes the fair values of NEG's assets and liabilities assumed by Narragansett at the date of acquisition.

(In millions of dollars)	**At August 24, 2006**
Net utility plant	$ 357.7
Goodwill	235.8
Other property and investments	4.5
Accounts receivable	72.5
Inventory	36.1
Other current assets	0.5
Regulatory assets	92.7
Other non-current assets	0.4
Total assets acquired	800.2
Long-term debt	76.1
Current portion of long-term debt	0.5
Accounts payable	29.4
Other current liabilities	39.5
Customer deposits	3.3
Accrued pension and other postretirement benefits	46.9
Other non-current liabilities	107.8
Total liabilities assumed	303.5
Net assets acquired	$496.7

NOTE M – DISCONTINUED OPERATIONS

The information below highlights the major classes of assets and liabilities of the discontinued operations, as well as major income and expense captions (in millions).

Income Statement Data				
	For the year ended March 31,			
(In millions of dollars)		**2008**		2007
Total operating revenues	**$**	**374.4**	$	74.0
Total operating expenses		**315.2**		62.1
Operating income		**59.2**		11.9
Total other income (expense)		**14.0**		(109.8)
Income (loss) before income taxes		**73.2**		(97.9)
Income tax provision (benefit)		**30.2**		10.6
Net income	**$**	**43.0**	$	(108.5)

Balance Sheet Data				
	At March 31,			
(In millions of dollars)		**2008**		2007
ASSETS				
Total current assets	**$**	**167.1**	$	23.1
Deferred Charges		**65.6**		-
Property and Other Long Term Assets		**2,792.7**		286.1
LIABILITIES AND STOCKHOLDER'S EQUITY				
Total current liabilities	**$**	**608.1**	$	288.3
Deferred Credits and Other Liabilities		**1,252.7**		17.3
Total stockholder's equity		**-**		3.6

National Grid Wireless

National Grid Wireless (Wireless), a subsidiary of the Company, owns, operates and manages towers and other communications structures. Wireless also manages a fiber optic telecommunications system in the Northeastern United States.

As part of the Company's strategy of focusing on energy markets, it committed during fiscal year 2007 to exit our wireless infrastructure operations. The wireless infrastructure operations were expanded during fiscal year 2007 with acquisitions at a cost of $160 million. On August 15, 2007, the Company completed the sale of its wireless infrastructure operations for proceeds of approximately $290 million. In fiscal year 2007, the Company reduced the carrying value of the assets held for sale by $120 million, net of tax, to approximate fair value less selling costs. The final sale resulted in a pre-tax gain of approximately $24 million primarily reflecting final working capital adjustments and other adjustments to the estimated selling price.

Following the guidance of SFAS No. 144, "Accounting for the Impairment or Disposal of Long-Lived Assets," the Company has reported Wireless as a discontinued operation for all periods presented.

KeySpan

On August 22, 2007 the NYPSC approved the merger application between KeySpan and National Grid plc. As a condition of the approval of the KeySpan Acquisition, the Company is required to divest the Ravenswood Generating Station. In addition, National Grid plc, has determined that the KeySpan telecommunications and engineering subsidiaries do not fit into the post-merger business model. As such, the Company will be exiting these businesses. The operating results and financial positions of these companies are reflected as discontinued operations on the Consolidated Statement of Income, Consolidated Balance Sheet and Consolidated Cash Flows. The sale of KeySpan's telecommunications business was completed on July 25, 2008. The assets and liabilities of this subsidiary were fair valued at August 24, 2008 and as a result the final sale has no material impact on the Consolidated Income Statement.

Ravenswood Sale Transaction

On March 31, 2008, the Company announced that it had signed an agreement to sell KeySpan Ravenswood, LLC to TransCanada Corporation for total cash consideration of $2.9 billion, payable upon completion of the sale ("Ravenswood Sale Transaction".) The total cash consideration includes working capital, fuel stock and a lease prepayment and is subject to customary closing conditions and adjustments.

The sale is subject to regulatory approvals of the FERC, the NYPSC and clearance under US anti-trust and foreign investment laws. Subject to these approvals, we expect to complete the sale by 2008 summer. On August 20, 2008 the NYPSC approved the sale of KeySpan Ravenswood, LLC.

In advance of this sale, the Company terminated the Ravenswood Master Lease (the lease under which KeySpan operates the Ravenswood Facility) on June 20, 2008, which was otherwise due to expire in 2009. Termination of the Master Lease results in the Company's ownership of the assets held under the lease. These assets and other assets are part of the assets being sold to TransCanada. The Ravenswood Sale Transaction also provides for the restructuring and transfer of our interest in the Ravenswood Expansion. However, we will remain responsible for all future lease payments under the sales/leaseback arrangement through May 2040. The total consideration received from the Ravenswood Sale Transaction includes a prepayment from TransCanada of the future payments under the sales/leaseback arrangement on a present value basis. (See Note C - "Commitments and Contingencies" for further details on the Master Lease and sales/leaseback arrangement.)

NOTE N - 2006 LIPA SETTLEMENT

LIPA is a corporate municipal instrumentality and a political subdivision of the State of New York. On May 28, 1998, certain of the Long Island Lighting Company's ("LILCO's") business units were merged with KeySpan and LILCO's common stock and remaining assets were acquired by LIPA. Also effective on that date, KeySpan and LIPA entered into three major long-term service agreements that (i) provide to LIPA all operation, maintenance and construction services and significant administrative services relating to the Long Island electric transmission and distribution (T&D) system pursuant to a Management Services Agreement (the "1998 MSA"); (ii) supply LIPA with electric generating capacity, energy conversion and ancillary services from our Long Island generating units pursuant to a Power Supply Agreement (the "1998 PSA") and other long-term agreements through which we provide LIPA with approximately one half of its customers' energy needs; and (iii) manage all aspects of the fuel supply for our Long Island generating facilities, as well as all aspects of the capacity and energy owned by or under contract to LIPA pursuant to an Energy Management Agreement (the "1998 EMA"). We also purchase energy, capacity and ancillary services in the open market on LIPA's behalf under the 1998 EMA. The 1998 MSA, 1998 PSA and 1998 EMA all became effective on May 28, 1998 and are collectively referred to as the "1998 LIPA Agreements".

On February 1, 2006, KeySpan and LIPA entered into (i) an amended and restated Management Services Agreement (the "2006 MSA"), pursuant to which we will continue to operate and maintain the electric T&D System owned by LIPA on Long Island; (ii) a new Option and Purchase and Sale Agreement (the "2006 Option Agreement"), to replace the Generation Purchase Rights Agreement (as amended, the "GPRA"), pursuant to which LIPA had the option, through December 15, 2005, to acquire substantially all of the electric generating facilities owned by the Company on Long Island; and (iii) a Settlement Agreement (the "2006 Settlement Agreement") resolving outstanding issues between the parties regarding the 1998 LIPA Agreements. The 2006 MSA, the 2006 Option Agreement and the 2006 Settlement Agreement are collectively referred to herein as the "2006 LIPA Agreements." The applicable rate components of each of the 2006 LIPA Agreements became effective retroactive to January 1, 2006, upon receipt of the required governmental approvals in 2007.

Following the announcement of the KeySpan Acquisition, LIPA, National Grid plc and KeySpan engaged in discussions concerning the impact of the transaction on LIPA's operations. KeySpan, National Grid plc and LIPA reached an agreement pursuant to which LIPA agreed to waive its contractual right to terminate the 1998 LIPA Agreements and the 2006 LIPA Agreements upon consummation of the KeySpan Acquisition, in exchange for enhancements to certain of the 2006 LIPA Agreements and certain other considerations. The amended and enhanced agreements became effective upon the completion of the KeySpan Acquisition and the approval by the New York State Attorney General and the New York State Comptroller.

2006 Settlement Agreement

Pursuant to the terms of the 2006 Settlement Agreement, KeySpan and LIPA agreed to resolve issues that existed between the parties relating to the various 1998 LIPA Agreements. In addition to the resolution of these matters, KeySpan's entitlement to utilize LILCO's available tax credits and other tax attributes increased from approximately $50 million to approximately $200 million. These credits and attributes were used to satisfy KeySpan's previously incurred indemnity obligation to LIPA for any federal income tax liability that resulted from the settlement with the IRS regarding the audit of LILCO's tax returns for the years ended December 31, 1996 through March 31, 1999. On October 30, 2006, the IRS submitted the settlement provisions of the concluded IRS audit to the Joint Committee on Taxation for approval – such approval was granted in December 2007. Key provisions of the settlement included the resolution of the tax basis of assets transferred to KeySpan at the time of the KeySpan/LILCO merger, the tax deductibility of certain merger related costs and the tax deductibility of certain environmental expenditures. The settlement enabled KeySpan to utilize 100% of the available tax credits. In recognition of these items, as well as for the modification and extension of the 1998 MSA and the amendments to the GPRA, KeySpan recorded a contractual asset in the amount of approximately $160 million, of which approximately $110 million was attributed to the right to utilize such additional credits and attributes and approximately $50 million to be amortized over the eight year term of the 2006 MSA. This amount was subsequently adjusted to a $ 130 million intangible asset upon the KeySpan Acquisition. In order to compensate LIPA for the foregoing, KeySpan paid LIPA $69 million in cash and settled certain accounts receivable in the amount of approximately $90 million due from LIPA.

Generation Purchase Rights Agreement and 2006 Option Agreement.

Under an amended GPRA, LIPA had the right to acquire certain of KeySpan's Long Island-based generating assets formerly owned by LILCO, at fair market value at the time of the exercise of such right. LIPA was initially required to make a determination by May 2005, but KeySpan and LIPA agreed to extend the date by which LIPA was to make this determination to December 15, 2005. As part of the 2006 settlement between KeySpan and LIPA, the parties entered into the 2006 Option Agreement whereby LIPA had the option during the period January 1, 2006 to December 31, 2006 to purchase only the steam generating units of the Far Rockaway and/or E.F. Barrett Generating Stations (and certain related assets) at a price equal to the net book value of each facility. In December 2006, KeySpan and LIPA entered into an amendment to the 2006 Option Agreement whereby the parties agreed to extend the expiration of the option period to the later of (i) December 31, 2007 or (ii) 180 days following the effective date of the 2006 Option Agreement. Pursuant to the National Grid plc, KeySpan and LIPA negotiations, the parties further amended the 2006 Option Agreement to extend the expiration of the option period to May 31, 2008, which was subsequently extended to December 31, 2008. The 2006 Option Agreement, as amended, replaces the GPRA. If LIPA were to exercise the option and purchase one or both of the generation facilities (i) LIPA and the Company will enter into an operation and maintenance agreement, pursuant to which the Company will continue to operate these facilities, through May 28, 2013, for a fixed management fee plus reimbursement for certain costs; and (ii) the 1998 PSA and 1998 EMA will be amended to reflect that the purchased generating facilities would no longer be covered by those agreements. It is anticipated that the fees received pursuant to the operation and maintenance agreement will offset the reduction in the operation and maintenance expense recovery component of the 1998 PSA and the reduction in fees under the 1998 EMA.

Management Services Agreements

In place of the previous compensation structure (whereby KeySpan was reimbursed for budgeted costs, and earned a management fee and certain performance and cost-based incentives), the Company's compensation for managing the T&D System under the 2006 MSA consists of two components: a minimum compensation component of $224 million per year and a variable component based on electric sales. The $224 million component remains unchanged for three years and then increase annually by 1.7%, plus inflation. The variable component, which comprises no more than 20% of the Company's compensation under the 2006 MSA, is based on electric sales on Long Island exceeding a base amount of 16,558 gigawatt hours, increasing by 1.7% in each year. Above that level, the Company receives approximately 1.34 cents per kilowatt hour for the first contract year, 1.29 cents per kilowatt hour in the second contract year (plus an annual inflation adjustment), 1.24 cents per kilowatt hour in the third contract year (plus an annual inflation adjustment), with the per kilowatt hour rate thereafter adjusted annually by inflation. Subject to certain limitations, the Company retains all operational efficiencies realized during the term of the 2006 MSA.

LIPA continues to reimburse the Company for certain expenditures incurred in connection with the operation and maintenance of the transmission and distribution system, and other payments made on behalf of LIPA, including: real property and other transmission and distribution system taxes, return postage, capital construction expenditures and storm costs.

On July 19, 2007, LIPA signed an agreement addressing KeySpan's receipt of a Civil Investigative Demand (CID) from the United States Department of Justice, Antitrust Division (DOJ) regarding the DOJ's investigation into competitive issues in the New York City electric capacity market. The Letter Amendment to the 2006 MSA, dated as of June 29, 2007, amends the 2006 MSA to add an additional event of default, such that LIPA will have the contractual right to terminate the 2006 MSA if, in connection with the DOJ's investigation referenced in the CID, (a) there is a finding (through either a final, non-appealable judgment by a court of competent jurisdiction or final consent decree with the DOJ) that KeySpan or any of its affiliates violated Section 1 or 2 of the Sherman Act and (b) pursuant to which KeySpan or any of its affiliates is assessed or has agreed to be assessed a monetary or criminal penalty or sanction or is the subject of injunctive relief.

NOTE O - APPLICATION OF SFAS 101 "REGULATED ENTERPRISES: ACCOUNTING FOR THE DISCONTINUATION OF APPLICATION OF FASB STATEMENT NO. 71" FOR THE LIPA SERVICE AGREEMENTS.

As discussed in more detail in Note N "2006 LIPA Settlement," on May 28, 1998, KeySpan and LIPA entered into three major long-term service agreements. Negotiations between KeySpan and LIPA to amend certain aspects of these agreements were substantially concluded in 2006 and while KeySpan and LIPA performed in accordance with certain elements of these restated agreements beginning January 1, 2006, additional changes to these contract terms and the approvals needed to create binding agreements were not obtained until 2007. The changes in these service agreements impacted KeySpan's accounting for certain transactions conducted between KeySpan and LIPA.

Under both the original and amended and restated service agreements, KeySpan and now the Company are responsible for the management of employee benefit plans associated with employees providing service to LIPA and LIPA is responsible for the cost of funding and maintaining those plans. From May 28, 1998 through December 31, 2006, KeySpan followed SFAS 71, "Accounting for the Effects of Certain Types of Regulation", in accounting for the agreements with LIPA and capitalized as a receivable the difference between the accrued liability associated with these plans and the funding based upon the recoveries agreed to in the rate plans with LIPA.

Certain events occurred over the course of 2006 and 2007 that constituted a change in facts and circumstances that made the continued application of SFAS 71 no longer appropriate and therefore KeySpan implemented Statement of Financial Accounting Standard 101 "Regulated

Enterprises - Accounting for the Discontinuation of Application of FASB Statement No. 71" ("SFAS 101") effective January 1, 2007. Specifically, management's determination to apply SFAS 101, was based upon its analyses of the continued applicability of paragraph 5 of SFAS 71, as well as its assessment of the increasing competitive environment in relation to renewal of the service agreements with LIPA.

Paragraph 5 of SFAS 71, requires that regulated rates be set to recover the enterprise's specific costs of providing the regulated services or products. However, in two material respects these amended and restated agreements did not maintain the direct link between the cost of providing LIPA with the agreed to services and the revenues recovered in providing those services. First, these amended and restated agreements contained a revised revenue formula that introduced a departure from cost of service recovery that had been in place since 1998. Second, although, the Company's rights to be reimbursed for employee benefit plan costs in the future have been completely preserved in the amended and restated service agreements, these rights of recovery are not fully reflected in the revised service agreements' rates. Management has therefore concluded that the cause-and-effect relationship between costs and revenues no longer exists for its service agreements with LIPA.

Moreover, recent actions taken and comments made by New York State officials indicate renewal of the service agreements with LIPA will be based on competitive tendering using New York State procurement practices and standards as opposed to the practice to date where the utility franchise had effectively been awarded to KeySpan.

Based on facts and circumstances detailed above, management has concluded that the amended and restated service agreements no longer meet all of the relevant SFAS 71 criteria. As a result, KeySpan implemented SFAS 101 effective January 1, 2007, the beginning of the period in which the changes that give rise to the need for the discontinuance of SFAS 101 became probable. Implementation of SFAS 101 resulted in KeySpan derecognizing a $442 million receivable with LIPA. KeySpan recorded a $113.9 million (after tax) extraordinary charge for the pre-acquisition period January 1, 2007 through August 24, 2007. The remaining amount was initially recorded through accumulated other comprehensive income and then ultimately charged to goodwill, net of tax, as a result of purchase accounting adjustments.

NOTE P – CHANGES IN EQUITY

The increase in additional paid in capital on the Consolidated Balance Sheet from March 31, 2007 to March 31, 2008 primarily reflects the KeySpan Acquisition. Additionally, in June 2007, the Company repurchased its common stock for $753 million which resulted in a decrease to other paid in capital of $425 million and a return of capital to the Parent of $328 million.