nationalgrid

Granite State Electric Company

Financial Statements

For the year ended March 31, 2010

Granite State Electric Company

PRICEWATERHOUSECOOPERS

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Report of Independent Auditors

To the Stockholder and Board of Directors of
Granite State Electric Company:

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

As discussed in Note 1 to the financial statements, the Company's balance sheet and the related statements of income, of comprehensive income, of retained earnings, of capitalization, and of cash flows as of March 31, 2009 have been restated to correct errors.

PricewaterhouseCoopers LLP

July 29, 2010

Granite State Electric Company

Balance Sheets

At March 31 (in thousands of dollars)	**2010**	Restated 2009
Assets		
Current assets:		
Cash and cash equivalents	**$ 587**	$ 518
Restricted cash	**3,070**	70
Accounts receivable:		
Customers	**10,160**	12,608
Money pool	**-**	5,375
Affiliates, net	**365**	366
Allowance for uncollectible customer accounts	**(489)**	(545)
Unbilled revenues	**830**	949
Regulatory - storm cost recoveries	**120**	120
Materials and supplies, at average cost	**449**	329
Deferred federal and state income taxes	**1,245**	-
Prepaid and other current assets	**7,132**	1,415
Total current assets	**23,469**	21,205
Investments and other	**1,086**	876
Property, plant and equipment		
Property, plant and equipment, at cost	**$ 127,009**	120,547
Less accumulated depreciation	**(45,869)**	(43,472)
Net property, plant and equipment	**81,140**	77,075
Deferred charges:		
Regulatory assets	**3,880**	2,773
Goodwill	**19,352**	19,352
Other assets	**45**	41
Total deferred charges	**23,277**	22,166
Total assets	**$ 128,972**	$ 121,322

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

Granite State Electric Company

Balance Sheets

At March 31 (in thousands of dollars)	**2010**	Restated 2009
Liabilities and Capitalization		
Current liabilities:		
Accounts payable:		
Non-affiliates	**$ 7,538**	$ 7,147
Money pool	**1,575**	-
Customer deposits	**349**	354
Accrued taxes	**63**	203
Accrued interest	**583**	573
Other accrued expenses	**696**	3,377
Current portion of accumulated deferred income taxes	**-**	21
Other	**1,065**	1,382
Total current liabilities	**11,869**	13,057
Deferred credits and other liabilities:		
Deferred federal and state income taxes	**10,802**	5,980
Accrued pension and other post-retirement benefits	**8,662**	9,545
Regulatory liabilities	**8,657**	6,162
Other reserves and deferred credits	**3,934**	1,765
Total deferred credits and other liabilities	**32,055**	23,452
Capitalization:		
Common stock, par value $100 per share, authorized and outstanding 60,400 shares	**6,040**	6,040
Additional paid-in capital	**40,054**	40,054
Retained earnings	**32,317**	32,629
Accumulated other comprehensive losses	**(8,363)**	(8,910)
Total common stockholders' equity	**70,048**	69,813
Long-term debt	**15,000**	15,000
Total capitalization	**85,048**	84,813
Total liabilities and capitalization	**$ 128,972**	$ 121,322

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

Granite State Electric Company

Statements of Income

Year ended March 31 (in thousands of dollars)	2010	Restated 2009
Operating revenues	**$ 80,713**	$ 101,700
Operating expenses:		
Purchased electric energy	**44,367**	68,182
Other operations and maintenance	**26,569**	23,390
Depreciation and amortization	**4,599**	4,445
Taxes, other than income taxes	**2,700**	2,632
Total operating expenses	**78,235**	98,649
Operating income	**2,478**	3,051
Other expense:		
Interest on long-term debt	**1,133**	1,133
Other interest	**132**	231
Other	**130**	392
Operating and other expense	**1,395**	1,756
Income tax expense (benefit):		
Current	**(4,620)**	(1,701)
Deferred	**6,015**	2,340
Total income tax expense	**1,395**	639
Net income (loss)	**$ (312)**	$ 656

The accompanying notes are an integral part of these financial statements

Granite State Electric Company

Statements of Comprehensive Income

Year ended March 31 (in thousands of dollars)	2010	Restated 2009
Net income	**$ (312)**	$ 656
Other comprehensive income (loss), net of taxes:		
Unrealized gains (losses) on securities	**115**	(71)
Change in pension and other postretirement obligations	**451**	(3,136)
Reclassification adjustment for gains (losses) included in net income	**(19)**	2
Total other comprehensive income (losses)	**547**	(3,205)
Comprehensive income (losses)	**$ 235**	$ (2,549)

Statements of Retained Earnings

Year ended March 31 (In thousands of dollars)	2010	Restated 2009
Retained earnings at beginning of year	**$ 32,629**	$ 31,973
Net income (loss)	**(312)**	656
Retained earning at end of year	**$ 32,317**	$ 32,629

The accompanying notes are an integral part of these financial statements

Granite State Electric Company

Statements of Cash Flows

Year ended March 31 (in thousands of dollars)	2010	Restated 2009
Operating activities:		
Net income (loss)	**$ (312)**	$ 656
Adjustments to reconcile net income (loss) to net cash provided by operating activities:		
Depreciation and amorization	**4,599**	4,445
Deferred income taxes and investment tax credit, net	**6,015**	2,340
Allowance for funds used during construction	**(115)**	(79)
Changes in assets and liabilities:		
Accounts receivable, net	**2,511**	(464)
Materials and supplies	**(120)**	104
Prepaid and other current assets	**(5,717)**	(753)
Affiliate accounts receivable/ payable, net	**-**	(1,648)
Accounts payable	**72**	(749)
Pension and other post-retirement benefits	**(644)**	(915)
Other accrued liabilities	**(2,811)**	841
Other, net	**845**	(306)
Net cash provided by operating activities	**4,323**	3,472
Investing activities:		
Plant expenditures	**(6,756)**	(5,558)
Change in money pool investment	**5,375**	1,900
Change in restricted cash	**(3,000)**	-
Other investing activities	**(1,448)**	268
Net cash used in investing activities	**(5,829)**	(3,390)
Financing activities:		
Change in money pool, net	**1,575**	-
Net cash provided by financing activities	**1,575**	-
Net increase in cash and cash equivalents	**69**	82
Cash and cash equivalents at beginning of year	**518**	436
Cash and cash equivalents at end of year	**$ 587**	$ 518
Supplementary information:		
Interest paid less amounts capitalized	**$ 1,274**	$ 1,336
Federal and state income taxes paid to (refunded from) parent	**$ -**	$ (654)
Capital-related accruals included in Accounts Payable	**$ 318**	$ 68

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Granite State Electric Company

Statements of Capitalization

(in thousands of dollars, except number of shares and par value)	March 31					
	2010	2009		**2010**		Restated 2009
Common shareholders' equity	**Shares Issued**			**Amounts**		
Common stock, $100 par value	**60,400**	60,400	**$**	**6,040**	$	6,040
Additional paid-in capital				**40,054**		40,054
Retained earnings				**32,317**		32,629
Accumulated other comprehensive loss				**(8,363)**		(8,910)
Total common shareholder' equity			**$**	**70,048**	$	69,813
Long-term debt	**Interest rates**	**Maturity Date**		**Amounts**		
Unsecured Notes						
7.37% Unsecured Note 2023	7.37	November 1, 2023	**$**	**5,000**	$	5,000
7.94% Unsecured Note 2025	7.94	July 1, 2025		**5,000**		5,000
7.30% Unsecured Note 2028	7.30	June 15, 2028		**5,000**		5,000
Total long-term debt				**15,000**		15,000
Total capitalization			**$**	**85,048**	$	84,813

The accompanying notes are an integral part of these financial statements

Granite State Electric Company

Notes to the Financial Statements

NOTE 1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

A. Nature of Operations

Granite State Electric Company (the Company, we, us, and our) is an electric retail distribution company providing electric service to approximately 42,700 customers in 21 communities in New Hampshire. The Company is a wholly owned subsidiary of National Grid USA (NGUSA), a utility holding company with regulated subsidiaries engaged in the generation, transmission, distribution and sale of both natural gas and electricity in New England and New York State. NGUSA is a wholly owned subsidiary of National Grid plc, a public limited company incorporated under the laws of England and Wales.

The properties of the Company consist principally of substations and distribution lines interconnected with transmission and other facilities of New England Power Company (NEP), a wholly owned subsidiary of NGUSA.

B. Basis of Presentation

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

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

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

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

C. Accounting for the Effects of Rate Regulation

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

D. Revenue Recognition

Revenues are based on billing rates authorized by the NHPUC. The Company records revenues in an amount management believes to be recoverable pursuant to provisions of approved tariffs, settlement agreements and state legislation. The Company defers for future recovery from or refunds to electric customers the difference between revenue and expenses from, default service, transmission service, and contract termination charges (CTC). The Company also records the distribution component of revenue for electricity delivered but not yet billed.

E. Property, Plant and Equipment

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

AFUDC: The Company capitalizes AFUDC as part of construction costs. AFUDC represents an allowance for the cost of funds used to finance construction and, for the Company, includes a debt component and an equity component. AFUDC is capitalized in "Property, plant and equipment" with offsetting credits to "Other interest" for the debt component and "Other income (expense), net" for the equity component. This method is in accordance with an established FERC rate-making practice under which the Company is permitted to recover prudently incurred capital costs through their ultimate inclusion in rate base and in the provision for depreciation. AFUDC rates vary by company and regulatory jurisdiction. The composite AFUDC rate was 9.2% for the years ended March 31, 2010 and 2009.

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

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

F. Goodwill

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

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

G. Cash and Cash Equivalents

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

H. Income Taxes:

Federal and state income taxes are recorded under the current accounting provisions for the accounting and reporting of income taxes. Income taxes have been computed utilizing the asset and liability approach that requires the recognition of deferred tax assets and liabilities for the tax consequences of temporary differences by applying enacted statutory tax rates applicable to future years to differences between the financial statement carrying amounts and the tax basis of existing assets and liabilities. Deferred investment tax credits are amortized over the useful life of the underlying property. Additionally, the Company follows the current accounting guidance relating to uncertainty in income taxes which applies to all income tax positions reflected on the Company's balance sheets that have been included in previous tax returns or are expected to be included in future tax returns.

I. Comprehensive Income (Loss)

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

J. Pension and Other Postretirement Plan Assets

On March 31, 2007, NGUSA adopted certain accounting guidance that requires employers to fully recognize all postretirement plans' funded status on the balance sheet as a net liability or asset and required an offsetting adjustment to "Accumulated other comprehensive income" in shareholders' equity upon implementation. Consistent with past practice and as required by the current accounting guidance, NGUSA values its pension and other postretirement assets using the year-end market value of those assets. Benefit obligations are also measured at year-end. (See Note 3 - Employee Benefits for additional details on the Company's pension and other postretirement plans.)

K. Fair Value Measurements

Fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date - exit price. The determination of the fair value incorporates various factors required including not only the credit standing of the counterparties involved but also the impact of the Company's nonperformance risk on its liabilities. To increase consistency and comparability in fair value measurements, a fair value hierarchy was established that prioritizes the inputs to valuation techniques used to measure fair value into three levels. The following is a fair value hierarchy:

Level 1 — quoted prices (unadjusted) in active markets for identical assets or liabilities that a company has the ability to access as of the reporting date.

Level 2 — inputs other than quoted prices included within Level 1 that are directly observable for the asset or liability or indirectly observable through corroboration with observable market data.

Level 3 — unobservable inputs, such as internally-developed pricing models for the asset or liability due to little or no market activity for the asset or liability with low correlation to observable market inputs.

The determination of the fair value incorporates various factors including not only the credit standing of the counterparties involved but also the impact of the Company's nonperformance risk on its liabilities. (See Note 7 – Fair Value Measurement)

L. Inventory

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

M. Recent Accounting Pronouncements

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

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

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

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

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

N. Restatement of the Previously Issued Financial Statements:

In connection with the preparation of the Company's financial statements, management concluded that the operating revenues were overstated by $3.2 million for the year ended March 31, 2009. The overstatement resulted from an error in the reconciliation of regulatory items that are recovered from electric sales customers and accumulated deferred federal and state income taxes. These adjustments resulted in a decrease to net income of $1.8 million.

In addition, during the year ended March 31, 2010, the Company has corrected its accounting policy related to its treatment of unbilled revenues specific to its distribution rates. It has determined that a monthly accrual is appropriate in order to align the Company's accounting policies with industry standards and provide increased transparency for the readers of the financial statements. As a result, net income decreased by $0.2 million. Additionally, beginning retained earnings balance increased by $0.7 million.

Due to the decrease in net income, other comprehensive income (loss) decreased from a loss of $0.6 million to a loss of $2.5 million, for the year ended March 31, 2009.

To correct these errors, we have restated the Statement of Income, Statement of Cash Flows, Balance Sheet, Statement of Retained Earnings, Statement of Comprehensive Income and Statement of Capitalization for the period ended March 31, 2009. The following items have been adjusted to reflect the necessary corrections to prior financial statements:

	March 31, 2009		
(In thousands)	As Originally Presented	Adjustments	As Restated
Operating revenue	$ 104,941	$ (3,241)	$ 101,700
Other operation and maintenance	23,338	52	23,390
Income taxes expense	2,080	(1,441)	639
Other expense	285	107	392
Net income	$ 2,615	$ (1,959)	$ 656

	March 31, 2009		
	As Originally Presented	Adjustments	As Restated
Assets:			
Accounts Receivable-customers	$ 17,040	$ (4,432)	$ 12,608
Unbilled Revenues	-	949	949
Total assets	$ 17,040	$ (3,483)	$ 13,557
Liabilities:			
Deferred federal and state income taxes	6,827	(847)	5,980
Total liabilities	$ 6,827	$ (847)	$ 5,980

	March 31, 2009		
	As Originally Presented	Adjustments	As Restated
Retained Earnings:			
Retained Earnings at March 31, 2009	$ 33,871	$ 717	$ 34,588
Regulatory Adjustment			(1,780)
Unbilled Revenues			(179)
Retained Earnings - Restated			$ 32,629

Notes to the Financial Statements

NOTE 2. RATES AND REGULATORY

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

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

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

Management continues to believe that rates are based on the Company's incurred costs and investment levels and therefore should continue to apply the current accounting guidance for rate regulated enterprises.
The components of regulatory assets (liabilities) at March 31 are as follows:

(in thousands of dollars)	**2010**	Restated 2009
Current regulatory assets included in accounts receivable:		
Rate adjustment mechanisms	**$ 2,126**	$ 2,934
Current regulatory assets:		
Storm cost recoveries	**120**	120
Current regulatory (liabilities) included in other accrued expenses:		
Rate adjustment mechanisms	**(4)**	(2,744)
Total current regulatory assets, net	**2,242**	310
Non-current regulatory assets:		
Regulatory tax asset	**-**	320
Storm cost recoveries	**3,260**	1,645
Other	**620**	808
Total non-current regulatory assets	**3,880**	2,773
Non-current regulatory liabilities:		
Regulatory tax liability	**(2,430)**	-
Post retirement benefits	**(1,816)**	(1,988)
Cost of removal	**(4,411)**	(4,174)
Total non-current regulatory liabilities	**(8,657)**	(6,162)
Total non-current regulatory liabilities, net	**(4,777)**	(3,389)
Net regulatory liabilities	**$ (2,535)**	$ (3,079)

On July 12, 2007, the NHPUC approved a settlement agreement between the Company, the Staff of the NHPUC and the New Hampshire Office of Consumer Advocate related to issues surrounding the merger of NGUSA and KeySpan Corporation (KeySpan) (the 2007 Settlement). Among other things, the 2007 Settlement provided for a $2.2 million reduction in the Company's distribution rates in two steps: the first $1.1 million reduction became effective August 11, 2007 and the second $1.1 million reduction became effective January 1, 2008. The 2007

Settlement also contained a distribution rate plan spanning 5 years effective January 1, 2008 (Rate Plan). During the Rate Plan, distribution rates are frozen except for rate adjustments in the event of certain uncontrollable exogenous events and moderate annual rate adjustments related to specific Reliability Enhancement and Vegetation Management Plans (REP/VMP). The Rate Plan also includes an earnings sharing mechanism based on an imputed capital structure of 50% debt and 50% equity and a return on equity ("ROE") of 11%. Earnings above 11% are shared equally between customers and the Company. The Rate Plan also establishes a storm contingency fund and customer service commitments by the Company. On June 27, 2008 the NHPUC approved the Company's first annual REP/VMP rate adjustment of $0.2 million effective July 1, 2008. On July 31, 2009, the NHPUC approved the Company's second annual REP/VMP rate adjustment of $0.2 million effective August 1, 2009. Current pending before the NHPUC is the third REP/VMP request which, if approved, would result in a rate adjustment effective July 1, 2010 of $1.1 million.

On April 8, 2010, the Company filed a request with the NHPUC for a temporary increase in funding to its Storm Contingency Fund of $0.7 million annually over 3 years to replenish the Company's newly formed fund after the devastating ice storm of December 11-12, 2008. The rate adjustment was approved by the NHPUC for to increase funding of $0.4 million effective July 1, 2010.

The Company continues to be authorized to recover all costs associated with procuring electricity for its customers, all transmission costs, and costs charged by the Company's affiliate, New England Power Company (NEP) for stranded costs associated with NEP's former electric generation investments.

Cost of Removal and Asset Retirement Obligations:
The Company adheres to the current accounting guidance relating to asset retirement obligations associated with tangible long-lived assets. Asset retirement obligations arising from legal obligations amounted to $0.1 million at March 31, 2010 and 2009. Under the Company's current and prior rate plans, it has collected through rates an implied cost of removal for its plant assets. This cost of removal collected from customers differs from the accounting guidance 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 as a regulatory liability to accumulated depreciation. The Company estimates it has collected over time $4.4 million and $4.2 million for the cost of removal through March 31, 2010 and 2009, respectively.

NOTE 3. EMPLOYEE BENEFITS

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

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

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

PBOPs provide health care and life insurance coverage to eligible retired employees. Eligibility is based on certain age and length of service requirements and, in most cases, retirees must contribute to the cost of their coverage.

Pension Benefits:
The Company participates in the pension plans with certain other NGUSA subsidiaries. Pension plan assets are commingled and cannot be allocated to an individual company. Pension costs are allocated to the Company. At March 31, 2010 and 2009, the pension plans have a net underfunded obligation of $420.7 million and $469.8 million, respectively. The Company's net periodic pension cost for the year ended March 31, 2010 and 2009 was $0.6 million and $0.2 million, respectively.

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

Postretirement Benefits Other than Pension Benefits:
The Company participates in the PBOP plans with certain other NGUSA subsidiaries. PBOP costs are allocated to the Company. At March 31, 2010 and 2009, the PBOP plans have a net underfunded obligation of $477.3 million and $476.8 million, respectively. The Company's net periodic postretirement benefit cost for the year ended March 31, 2010 and 2009 was $0.6 million and $0.5 million, respectively.

Health Care Reform
In March 2010, the Patient Protection and Affordable Care Act and the Health Care and Education Reconciliation Act of 2010 became law. These laws' included provisions which resulted in the repeal, with effect from 2012, of the deduction for federal income tax purposes of the portion of the cost of an employer's retiree prescription drug coverage for which the employer received a benefit under the Medicare Prescription Drug Improvement and Modernization Act of 2003. The consequential reduction in the deferred tax asset balance resulted in a net charge to the income statement of approximately $0.4 million.

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. Of the 560 employees enrolled in the VERO, none were employees of the Company. Employees enrolled in the VERO program will retire by October 1, 2010. The Company's share of the cost of the VERO program was estimated to be $0.6 million, which consists of VERO costs allocated from affiliates. For the year ended March 31, 2010, the Company expensed $0.1 million.

During the year ending March 31, 2010, an additional VERO package was offered to 38 union employees in connection with National Grid plc's acquisition of KeySpan to further the effort to achieve necessary staff reduction through voluntary means. Of the 38 eligible employees, 33 enrolled in the VERO and none were employees of the Company. Employees enrolled in the early retirement program retired during fiscal year 2010. The Company recorded $0.02 million of allocated costs associated with this VERO package.

Granite State Electric Company

Notes to the Financial Statements

NOTE 4. DEBT

Short-term: The Company has regulatory approval from the NHPUC to issue up to $10 million of short-term debt. The company had no short-term debt outstanding to third-parties at March 31, 2010 or 2009.

Long-term: The Company had outstanding $15.0 million of unsecured long-term notes at March 31, 2010 and 2009. The interest rates on these unsecured notes range from 7.30% to 7.94% and the maturity dates extend from November 2023 to June 2028. These unsecured notes have 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, 2010 and 2009, the total long-term debt was 18% of total capitalization.

NOTE 5. PROPERTY, PLANT AND EQUIPMENT

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

(in thousands of dollars)	Plant and Machinery	Land and Buildings	Assets in Construction	Other Intangible	Total
Balance at March 31, 2008	$ 109,081	$ 5,443	$ 1,573	$ 25	$ 116,122
Additions	-	-	5,569	-	5,569
Disposals	(1,137)	(7)	-	-	(1,144)
Reclassifications	5,279	-	(5,279)	-	-
Balance at March 31, 2009	113,223	5,436	1,863	25	120,547
Accumulated Depreciation at March 31, 2009	(42,662)	(810)	-	-	(43,472)
Net book value at March 31, 2009	$ 70,561	$ 4,626	$ 1,863	$ 25	$ 77,075
Balance at March 31, 2009	$ 113,223	$ 5,436	$ 1,863	$ 25	$ 120,547
Additions	-	-	7,189	-	7,189
Disposals	(708)	(19)	-	-	(727)
Reclassifications	7,683	-	(7,683)	-	-
Balance at March, 31, 2010	120,198	5,417	1,369	25	127,009
Accumulated Depreciation at March 31, 2010	(45,040)	(829)	-	-	(45,869)
Net book value at March 31, 2010	$ 75,158	$ 4,588	$ 1,369	$ 25	$ 81,140

Granite State Electric Company

Notes to the Financial Statements

NOTE 6. INCOME TAXES

Following is a summary of the components of federal and state income tax expense (benefit):

	Year Ended March 31,	
(in thousands of dollars)	**2010**	Restated 2009
Components of federal and state income taxes:		
Current tax expense (benefit):		
Federal	**$ (4,475)**	$ (1,670)
State	**(145)**	(31)
Total current tax benefit	**(4,620)**	(1,701)
Deferred tax expense (benefit):		
Federal	**$ 4,772**	$ 1,990
Investment tax credits [(1)]	**(45)**	(52)
State	**1,288**	402
Total deferred tax expense	**6,015**	2,340
Total income tax expense	**$ 1,395**	$ 639

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

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

(in thousands of dollars)	**2010**	Restated 2009
Computed tax	**$ 379**	$ 472
Increase (reduction) including those attributable to flow-through of certain tax adjustments:		
State income tax, net of federal benefit	**743**	345
Provision to return adjustments	**7**	(245)
Medicare charge attributable to Patient Protection & Affordable Care Act	**320**	(44)
Depreciation differences not normalized	**69**	105
Investment tax credit	**(45)**	(52)
Allowance for equity funds used during construction	**(40)**	(28)
Other items - net	**(38)**	86
Total	**$ 1,016**	$ 167
Federal and state income taxes	**$ 1,395**	$ 639

Notes to the Financial Statements

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

(in thousands of dollars)	2010	Restated 2009
Pension, OPEB and other employee benefits	**$ 4,841**	$ 5,093
Unbilled revenue	**1,287**	1,009
Regulatory tax liability	**1,383**	132
Future federal benefit on state taxes	**705**	487
Other items	**360**	925
Total deferred tax assets[1]	**8,576**	7,646
Property related differences	**(15,558)**	(12,117)
Regulatory assets - storm costs	**(1,435)**	(768)
Investment tax credit	**(204)**	(250)
Other items	**(936)**	(512)
Total deferred tax liabilities	**(18,133)**	(13,647)
Net accumulated deferred income tax liability	**(9,557)**	(6,001)
Current portion of net deferred tax asset (liability)	**1,245**	(21)
Non-current portion of net deferred income tax liability	**$ (10,802)**	$ (5,980)

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

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

The Company adopted the provisions of the FASB guidance which clarifies the accounting for uncertain tax positions in the financial statements. This guidance provides that the financial effects of a tax position shall initially be recognized when it is more likely than not, based on the technical merits, that the position will be sustained upon examination, assuming the position will be audited and the taxing authority has full knowledge of all relevant information.

The unrecognized tax benefits are included in “Deferred credits and other liabilities - other reserves and deferred credits” on the Balance Sheets.

With the application of this FASB guidance, as of March 31, 2010 and 2009, the Company’s unrecognized tax benefits totaled $3.6 million and $1.3 million, respectively, of which $0.4 million and $0.1 million, respectively, would affect the effective tax rate, if recognized.

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

Reconciliation of Unrecognized Tax Benefits		
(in thousands of dollars)	**2010**	2009
Beginning balance	**$ 1,351**	$ 211
Gross increases related to prior period	**-**	140
Gross increases related to current period	**2,287**	1,201
Settlements with tax authorities	**-**	(201)
Reductions due to a lapse of statute of limitations	**-**	-
Ending balance at March 31	**$ 3,638**	$ 1,351

As of March 31, 2010 and March 31, 2009, the Company has accrued for total interest of $0.2 million and $0.1 million, respectively, on its unrecognized tax benefits. During the years ended March 31, 2010 and March 31 2009, the Company recorded interest expense of $0.02 million and $0.07 million, respectively. The Company recognizes interest accrued related to unrecognized tax benefits in interest expense or interest income and related penalties, if applicable, in operating expenses. No penalties were recognized during the years ended March 31, 2010 and 2009.

Federal income tax returns have been examined and all appeals and issues have been agreed with the Internal Revenue Service ("IRS") and the NGHI consolidated filing group through March 31, 2004. During the year ended March 31, 2009, the NGHI consolidated group settled certain proposed IRS audit adjustments related to the years ending March 31, 2003 and 2004 with the IRS Office of Appeals.

The IRS is currently auditing the federal NGHI consolidated income tax returns, which include the Company, for March 31, 2005 through March 31, 2007. The Company does not expect to make any cash tax payments to the IRS within the next twelve months related to the 2005-2007 audits, and it doesn't expect any change in its total gross unrecognized tax benefits as a result of the audit. The years ended March 31, 2008 and 2009 remain subject to examination by the IRS.

The Company participates with certain other National Grid subsidiaries in filing a unitary New Hampshire business profits tax return. The New Hampshire unitary returns have been amended for all agreed IRS adjustments. There is currently no ongoing audit by the State of New Hampshire, although the tax returns for the years ending March 31, 2007 through 2009 are still open under the statute of limitations.

NOTE 7. FAIR VALUE MEASUREMENTS

Fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date - exit price. The determination of the fair value incorporates various factors required including not only the credit standing of the counterparties involved but also the impact of the Company's nonperformance risk on its liabilities. To increase consistency and comparability in fair value measurements, a fair value hierarchy was established that prioritizes the inputs to valuation techniques used to measure fair value into three levels

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

Long term debt is based on quoted market prices where available or calculated prices based on the remaining cash flows of the underlying bond discounted at the Company's incremental borrowing rate. The Company's Balance Sheet reflects the long term debt at carrying value. The fair value of this debt at March 31, 2010 is $18.5 million.

The following table presents assets and liabilities measured and recorded at fair value on the Company's Balance Sheets on a recurring basis and their level within the fair value hierarchy at March 31, 2010:

(in thousands of dollars)	Level 1	Level 2	Level 3	Total
Available for sale securities				
Assets	$ 437	$ 579	$ -	$ 1,016
Total available for sale securities	$ 437	$ 579	$ -	$ 1,016

NOTE 8. GOODWILL

The balance of goodwill represents the excess of acquisition cost over the fair value of net assets acquired relating to the acquisition of the Company by National Grid. The acquisition was accounted for by the acquisition method of accounting, the application of which includes the recognition of goodwill.

Goodwill: Changes in the carrying amount of the Company's goodwill, net of accumulated impairment losses for the years ended March 31, were as follows:

(in thousands of dollars)	**2010**	2009
Balance at beginning of the year	**$ 19,352**	$ 19,352
Goodwill acquired during the year	**-**	-
Goodwill disposed of during the year	**-**	-
Adjustments	**-**	-
Impairment	**-**	-
Balance at end of the year	**$ 19,352**	$ 19,352

Granite State Electric Company

Notes to the Financial Statements

NOTE 9. ACCUMULATED OTHER COMPREHENSIVE INCOME(LOSS)

The following table details the components of accumulated other comprehensive income (loss) for the years ended March 31, 2010 and 2009:

(in thousands of dollars)	Unrealized Gain (Loss) on Available-for-Sale Securities	Postretirement Liability	Total Accumulated Other Comprehensive Income/(Loss)
March 31, 2008 balance, net of tax	$ 38	$ (5,743)	$ (5,705)
Other comprehensive income (loss):			
Unrealized (loss) on securities	(71)	-	(71)
Reclassification adjustment for gains included in net income	2	-	2
Net loss arising during period	-	(3,263)	(3,263)
Change in postretirement benefits	-	238	238
Tax on Medicare subsidy	-	(111)	(111)
March 31, 2009 balance, net of tax	$ (31)	$ (8,879)	$ (8,910)
Other comprehensive income (loss):			
Unrealized gains on securities	115	-	115
Reclassification adjustment for (loss) included in net income	(19)	-	(19)
Net gain arising during period	-	90	90
Change in pension and postretirement benefits	-	361	361
March 31, 2010 balance, net of tax	$ 65	$ (8,428)	$ (8,363)

NOTE 10. COMMITMENTS AND CONTINGENCIES

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

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

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

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

Long-term Contracts for the Purchase of Electric Power:
The Company has 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, 2010, are summarized in the table below.

(In thousands of dollars)

Year Ended March 31,		**Estimated Payments**
2011	$	19,577
Thereafter		-
Total	$	19,577

NOTE 11. RELATED PARTY TRANSACTIONS

Accounts Receivable/Payable, Money Pool: The Company participates with NGUSA and its affiliates in a system money pool. The money pool is administered by a NGUSA Service Company as the agent for the participants. Short-term borrowing needs are met first by available funds of the money pool participants. Borrowings from the money pool bear interest at the higher of (i) the monthly average rate for high-grade, 30-day commercial paper sold through dealers by major corporations as published in The Wall Street Journal, or (ii) the monthly average rate then available to money pool depositors from an eligible investment in readily marketable money market funds or the existing short-term investment accounts maintained by money pool depositors or the NGUSA Service Company during the period in question. In the event neither rate is one that is permissible for a transaction because of constraints imposed by the state regulatory commission having jurisdiction over a utility participating in the transaction, the rate is adjusted to a permissible rate as determined under the requirements of the state regulatory commission. Companies that invest in the money pool share the interest earned on a basis proportionate to their average monthly investment in the money pool. Funds may be withdrawn from or repaid to the money pool at any time without prior notice. The average interest rate for the money pool was 0.27% and 1.96% for the year ended March 31, 2010 and 2009, respectively. The Company had accounts payable to the money pool of $1.6 million at March 31, 2010 and accounts receivable from the money pool of $5.4 million at March 31, 2009.

Accounts Receivable from Affiliates: Additionally, the Company engages in various transactions with NGUSA and its affiliates. Certain activities and costs, such as executive and administrative, financial (including accounting, auditing, risk management, tax and treasure/finance), human resources, information technology, legal and strategic planning are shared between the companies and allocated to each company appropriately. In addition, the Company has a tax sharing agreement with NGHI, a NGUSA affiliate, in filing consolidated tax returns. The Company's share of the tax liability is allocated resulting in a payment to or refund from NGHI. (See note 6 – Income taxes on filing consolidated tax returns). At March 31, 2010 and 2009, the Company had net accounts receivable from affiliates of $0.4 million, for those services.

Service Company Charges: The affiliated service companies of National Grid have furnished services to the Company at the cost of such services. These costs, including operating costs and capital expenditures, were $8.0 million and $7.2 million for the years ended March 31, 2010 and 2009, respectively.

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

These charges, which are recorded on the books of NGUSA, have not been reflected on these financial statements. Were these amounts allocated to this subsidiary, the estimated effect on net income would be approximately $0.13 million before tax, and $0.09 million after tax.

NOTE 12. RESTRICTIONS ON PAYMENTS ON DIVIDENDS

Pursuant to the provisions of the long-term note agreement, payment of dividends on common stock would not be permitted if, after giving effect to such payment of dividends, common equity becomes less than 30% of total capitalization. At March 31, 2010 and 2009, common equity was 82% of total capitalization. Under these provisions, none of the Company's retained earnings at March 31, 2010 and 2009 were restricted as to common dividends.