nationalgrid

Massachusetts Electric Company

Financial Statements

For the year ended March 31, 2010

Massachusetts Electric Company

PRICEWATERHOUSECOOPERS

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Report of Independent Auditors

To the Stockholders and Board of Directors of
Massachusetts 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 Massachusetts 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.

PricewaterhouseCoopers LLP

July 29, 2010

Massachusetts Electric Company

Balance Sheets

(In thousands of dollars)

	March 31, 2010	March 31, 2009
ASSETS		
Current assets:		
Cash and cash equivalents	**$ 8,536**	$ 8,682
Restricted cash	**56,488**	5,560
Accounts receivable:		
Customers	**297,924**	310,005
Affiliates, net	**9,888**	-
Allowance for uncollectible customer accounts	**(37,276)**	(38,219)
Unbilled revenues	**81,572**	100,829
Materials and supplies, at average cost	**16,526**	18,238
Deferred federal and state income taxes	**20,352**	27,690
Prepaid and other current assets	**135,278**	46,441
Total current assets	**589,288**	479,226
Other property and investments	**20,893**	19,965
Property, plant and equipment		
Property, plant and equipment, at original cost	**3,224,515**	3,046,662
Accumulated depreciation	**(1,131,606)**	(1,079,850)
Net property, plant and equipment	**2,092,909**	1,966,812
Deferred charges:		
Goodwill	**1,008,244**	1,008,244
Regulatory assets	**551,031**	179,949
Other	**7,642**	1,498
Total deferred charges	**1,566,917**	1,189,691
Total assets	**$ 4,270,007**	$ 3,655,694

The accompanying notes are an integral part of these financial statements

Massachusetts Electric Company

Balance Sheets

(In thousands of dollars)

		March 31, 2010		March 31, 2009
LIABILITIES AND CAPITALIZATION				
Current liabilities:				
Accounts payable:				
Non-affiliates, net	$	**163,030**	$	222,731
Affiliates, net		**-**		14,655
Money pool		**193,050**		532,250
Customer deposits		**9,010**		8,089
Accrued interest		**17,676**		467
Accrued taxes		**2,507**		340
Other		**84,519**		97,579
Total current liabilities		**469,792**		876,111
Deferred credits and other liabilities				
Regulatory liabilities		**314,674**		313,164
Deferred federal and state income taxes		**402,068**		148,140
Accrued pension and other postretirement benefits		**227,033**		242,599
Other		**178,211**		126,733
Total deferred credits and other liabilities		**1,121,986**		830,636
Capitalization:				
Common stockholders' equity:				
Common stock ($25 par value)				
Authorized and outstanding - 2,398,111 shares		**59,953**		59,953
Additional paid-in capital		**1,556,766**		1,556,766
Retained earnings		**237,282**		529,316
Accumulated other comprehensive income (losses)		**4,810**		(219,058)
Total common stockholders' equity		**1,858,811**		1,926,977
Preferred equity:				
Cumulative preferred stock ($100 par value, optionally redeemable)				
Authorized and outstanding – 22,585 shares		**2,259**		2,259
Long-term debt		**817,159**		19,711
Total capitalization		**2,678,229**		1,948,947
Total liabilities and capitalization	**$**	**4,270,007**	$	3,655,694

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

Massachusetts Electric Company

Statements of Income

(In thousands of dollars)

	For the Years Ended March 31, 2010	2009
Operating revenue	**$ 2,057,968**	$ 2,377,956
Operating expenses:		
Purchased electricity	**1,019,414**	1,442,193
Operations and maintenance	**770,270**	702,139
Depreciation	**112,376**	112,634
Taxes, other than income taxes	**44,939**	39,840
Total operating expenses	**1,946,999**	2,296,806
Operating income	**110,969**	81,150
Other income (deductions):		
Interest on long-term debt	**(18,201)**	(2,763)
Other interest, including affiliate interest	**(3,160)**	(12,812)
Other income, net	**(234)**	2,096
Total other deductions	**(21,595)**	(13,479)
Income tax expenses (benefits):		
Current income tax	**(71,798)**	(28,002)
Deferred income tax	**118,131**	48,810
Total income tax expense	**46,333**	20,808
Net income	**$ 43,041**	$ 46,863

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

Massachusetts Electric Company

Statements of Comprehensive Income

(In thousands of dollars)

	For the Years Ended March 31,	
	2010	2009
Net income	**$ 43,041**	$ 46,863
Other comprehensive income (loss), net of taxes:		
Unrealized gains (losses) on securities	**605**	(340)
Change in pension and other postretirement obligations	**87,804**	(81,445)
Reclassification adjustment for (gains) losses included in net income	**(146)**	12
Tax on Medicare subsidy	**-**	(2,026)
Total other comprehensive income (loss)	**88,263**	(83,799)
Comprehensive income	**$ 131,304**	$ (36,936)
Related tax (expense) benefit:		
Investment activities	**$ (401)**	$ 219
Change in pension and other postretirement obligations	**(58,536)**	52,564
Reclassification adjustment for gain (loss) included in net income	**97**	(8)
Total tax (expense) benefit	**$ (58,840)**	$ 52,775

Statements of Retained Earnings

(In thousands of dollars)

	For the Years Ended March 31,	
	2010	2009
Retained earnings at beginning of year	**$ 529,316**	$ 482,576
Net income	**43,041**	46,863
Dividends declared on preferred stock	**(75)**	(123)
Dividends declared on common stock	**(335,000)**	-
Retained earnings at end of year	**$ 237,282**	$ 529,316

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

Massachusetts Electric Company

Statements of Cash Flows

(In thousands of dollars)

	For the Years Ended March 31, 2010	2009
Operating activities:		
Net income	**$ 43,041**	$ 46,863
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation	**112,376**	112,634
Deferred federal and state income taxes and investment tax credits, net	**118,131**	48,810
Changes in assets and liabilities:		
Accounts receivable, net and unbilled revenues	**30,395**	16,006
Materials and supplies	**1,712**	(3,297)
Prepaid and other current assets	**(88,837)**	338
Intercompany payables and receivable, net	**(24,543)**	1,637
Regulatory assets	**(27,138)**	(40,179)
Accounts payable	**(62,380)**	602
Other current liabilities	**7,237**	11,037
Pension and other postretirement benefits	**(25,079)**	(17,352)
Reserves and other deferred credits	**61,617**	(20,079)
Other, net	**13,105**	(14,184)
Net cash provided by operating activities	**159,637**	142,836
Investing activities:		
Construction additions	**(208,944)**	(197,227)
Change in restricted cash	**(50,928)**	(2,007)
Other, net	**(18,866)**	4,317
Net cash used in investing activities	**(278,738)**	(194,917)
Financing activities:		
Dividends paid on common stock	**(335,000)**	-
Dividends paid on preferred stock	**(75)**	(123)
Proceeds from long-term debt	**800,000**	-
Reduction in long-term debt	**-**	(75,000)
Net change in money pool to affiliates	**(339,200)**	124,100
Debt issuance costs	**(6,770)**	-
Net cash provided by financing activities	**118,955**	48,977
Net decrease in cash and cash equivalents	**(146)**	(3,104)
Cash and cash equivalents at beginning of year	**8,682**	11,786
Cash and cash equivalents at end of year	**$ 8,536**	$ 8,682
Supplemental information:		
Interest paid	**$ 2,494**	$ 14,973
Income taxes received from Parent	**$ -**	$ (1,485)
Capital related accruals included in accounts payable	**$ 2,679**	$ 2,977

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

Massachusetts Electric Company

Statements of Capitalization

(In thousands of dollars except number of shares)

		Shares March 31, 2010	Shares March 31, 2009		March 31, 2010		March 31, 2009
Common stockholders' equity							
Common stock, $25 par value		**2,398,111**	2,398,111	**$**	**59,953**	$	59,953
Additional paid-in capital					**1,556,766**		1,556,766
Retained earnings					**237,282**		529,316
Accumulated other comprehensive income (loss)					**4,810**		(219,058)
Total common stockholders' equity		**2,398,111**	2,398,111		**1,858,811**		1,926,977
Preferred equity							
Cumulative preferred stock, $100 par value							
4.44%		**22,585**	22,585		**2,259**		2,259
Total preferred equity		**22,585**	22,585		**2,259**		2,259
Long-term debt	**Interest Rate**						
Notes payable:							
Unsecured senior notes	5.90%				**800,000**		-
State authority financing - tax exempt:							
Pollution control revenue bonds	Variable				**20,000**		20,000
Unamortized discounts					**(2,841)**		(289)
Total long-term debt					**817,159**		19,711
Total capitalization				**$**	**2,678,229**	$	1,948,947

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

Massachusetts Electric Company

Notes to Financial Statements

Note 1 - Significant Accounting Policies

A. Nature of Operations:
Massachusetts Electric Company (Massachusetts Electric, the Company, we, us, and our) is an electric retail distribution company providing electric service to approximately 1.3 million customers in 171 cities and towns in Massachusetts. 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 – Rates and Regulatory), and are in accordance with the accounting requirements and ratemaking practices of the applicable regulatory authorities.

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

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

The Company has evaluated events or transactions that occurred after March 31, 2010 through July 29, 2010 for potential recognition or disclosure in the financial statements. There were no subsequent events, other than regulatory matters included in Note 2 (Rates and Regulatory), that needed to be disclosed.

C. Accounting for the Effects of Rate Regulation:
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. The Company is also subject to certain regulations of the Massachusetts Department of Public Utilities (DPU) in addition to FERC.

D. Revenue Recognition:
Revenues are based on billing rates authorized by the DPU. The Company follows the policy of accruing the estimated amount of base rate revenue for electricity delivered but not yet billed (unbilled revenue), to match costs and revenues more closely. The unbilled revenues at March 31, 2010 and 2009 were approximately $81.6 million and $100.8 million, respectively. The Company records revenue in an amount management believe to be recoverable pursuant to provisions of approved settlement agreements and the Massachusetts Electric Industry Restructuring Act. The Company defers for future recovery from or refunds to electric customers the difference between revenue and expenses from energy conservation programs, standard offer/default service, transmission service, and contract termination charges (CTCs).

E. Property, Plant and Equipment:

The cost of additions to plant, property 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, reflects a debt component only. AFUDC is capitalized in “Property, plant and equipment, net” with offsetting credits to “Other interest”. This method is in accordance with an established DPU rate-making practice under which the Company is permitted to recover, prudently incurred capital costs through their ultimate inclusion in rate base and in the provision for depreciation. The composite AFUDC rates were 0.7% and 2.8% for the years ended March 31, 2010 and 2009, respectively.

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

	2010		2009	
	Provsion	**Service Life**	Provsion	Service Life
Asset Category:				
Electric	**3.7%**	**27**	3.9%	26

The increase in the remaining service life was a result of a rate case filing detailed in Note 2 (Rates and Regulatory)

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. Restricted Cash:
Restricted cash consists of special deposits the Company is required to have available as security for long-term debt. Deposits are also recorded for property, health insurance and worker's compensation. In the year ended March 31, 2009, $2 million was required by the Independent System Operator of New England Inc. (the ISO) to be on deposit, which was released back to the Company on July 31, 2009. During the year ended March 31, 2010, $53 million was again required by the ISO to be on deposit.

I. 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. (See Note 6 – Income Taxes)

J. 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 significant component of comprehensive income (loss) is change in pension and other postretirement obligations.

K. Pension and Other Postretirement Plan Assets:
In March 31, 2007, NGUSA adopted certain accounting guidance that requires employers to fully recognize all postretirement plans' funded status on the balance sheet as a net liability or asset and required an offsetting adjustment to "Regulatory assets" upon implementation. Under the Company's rate order, we are allowed recovery of non-capitalized pension and postretirement benefits other pensions (PBOP) costs. 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.)

L. 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. (See Note 7 – Fair Value Measurements)

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.

M. Reclassifications:
Certain amounts from prior years have been reclassified in the accompanying financial statements to conform to the current year presentation.

For the year ended March 31, 2009, the dividend declared on preferred stock was included as a component of net income. The 2009 presentation was changed to reflect the dividend on preferred stock as a direct charge against retained earnings.

N. 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.

O. Related Party Reimbursement:
In accordance with the Credit and Operating Support Agreement dated March 26, 1996 between the Company and an NGUSA affiliate, Nantucket Electric Company (Nantucket Electric), the Company will reimburse Nantucket Electric an amount equal to the difference between Nantucket Electric's actual net income for the year and the net income necessary for Nantucket Electric to earn a return on common equity (ROE) equivalent to Nantucket Electric's DPU approved weighted average allowed ROE for the fiscal year, currently 10.35%. This reimbursement shall constitute additional revenue to Nantucket Electric and an expense to the Company. To the extent Nantucket Electric's actual ROE for the year exceeds its allowed ROE, there will be no reimbursement. For the years ended March 31, 2010 and 2009, the Company reimbursed Nantucket Electric $3.3 million and $2.0 million, respectively.

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

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

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

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

Note 2 – Rates and Regulatory

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

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

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

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

Massachusetts Electric Company

Notes to Financial Statements

Rate Matters: Rates for services rendered by the Company are subject to approval by the DPU. In March 2000, the DPU approved a long-term rate plan for the Company, which became effective on May 1, 2000. During the period from March 1, 2005 through December 31, 2009, the Rate Index Period, distribution rates were adjusted annually, based upon the movement of a distribution index rate (in cents per kilowatt-hour) of similarly unbundled distribution utilities in New England, New York, Pennsylvania and New Jersey. The Company implemented increases in distribution rates pursuant to this mechanism of 1.90% and 1.54% effective March 1, 2008, and 2009, respectively. The rate plan also included provisions for recovery of major storm costs and recovery or passback to customers for exogenous events.

On May 15, 2009, the Company, together with Nantucket Electric, filed for an increase in base distribution rates effective January 1, 2010. The DPU issued its initial order on the Company's case on November 30, 2009. In that order the DPU approved, with modification, the revenue decoupling mechanism (RDM) proposed by the Company, as well as the reconciliation of commodity-related bad debt, pension and PBOP costs to our actual costs. The reconciliation of pension and PBOP costs will occur outside of base rates through a separate factor. The RDM allows for annual adjustments to the Company's distribution rates as a result of incremental capital investment and the reconciliation between allowed revenue and billed revenue. As a result of the RDM, the Company's future revenues are not solely dependent on volumes of electricity delivered. In addition, the actual costs incurred for commodity related bad debt and pension and PBOPs are fully recoverable. The DPU issued a second order on April 13, 2010 which partially modified the initial order by approving an overall increase in base distribution revenue of approximately $42 million as compared to the revenue generated at the old rates, and increased the ratio of equity to debt in the capital structure to 49.99% for ratemaking purposes. Approximately $6 million of the increase relates to storm costs associated with restoration of service following an ice storm on December 11 and 12, 2008 that severely damaged parts of the electric distribution system and caused numerous power outages in the central and northeast portions of the Company's service territory.

This rate order also allowed recovery of non-capitalized pension and PBOP costs to occur outside of base rates through a separate factor. Costs of the Company's pension and postretirement benefits plans over or under amounts reflected in rates are deferred to a regulatory asset to be recovered in a future period. As a result the Company reclassified "Accumulated Other Comprehensive Income" of $195.4 million and related "accumulated deferred income taxes" of $129.1 million to "regulatory assets" of $324.5 million.

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

Under the terms of NEP's FERC Electric Tariff No. 1, NEP operates the transmission facilities of its New England affiliates as a single integrated system and reimburses the Company for the cost of its transmission facilities in Massachusetts, including a return on those facilities. In turn, these costs are allocated among transmission customers in New England, including the Company, in accordance with the terms of the ISO New England Open Access Transmission Tariff. On December 30, 2009, NEP filed with FERC a proposed amendment to the Company's formula rate revenue requirements under Tariff No.1 for two reasons. First, the proposed filing adjusted the Company's depreciation rates and Postretirement Benefits Other than Pension according to recent depreciation and actuarial studies updating such costs. Second, the proposed filing sought to update the formula rate to be more transparent and consistent with the existing formula rate in place under Schedule III-B. The result of the proposed rate change is to decrease the Company's compensation for its electric transmission facilities by approximately $1.7 million from the levels received during calendar year 2008. On March 29, 2010, FERC issued an order establishing hearing and settlement procedures for this filing and made the new rates effective January 1, 2010, subject to refund, pending the outcome of the proceeding. The Company cannot predict the outcome of this filing at this time.

Other Regulatory Matters: Pursuant to the 2008 Green Communities Act (GCA), the Massachusetts Legislature mandated large scale and innovative ideas for implementing renewable energy and alternative energy, as well as increased energy efficiency spending. The legislation sets forth numerous requirements for utilities including the filing of three-year energy efficiency plans that would cover calendar years 2010 through 2012 and result in significantly increased energy efficiency spending over increases in 2008 and 2009. Statewide three-year electric plans were approved by the newly created Energy Efficiency Advisory Council on October 27, 2009. The Company's 2010 through 2012 energy efficiency plan (offered as a single combined program with Nantucket Electric) was approved by the DPU on January 28, 2010, including the budget and cost recovery proposed by the Company. The proposed budget for the two electric companies in Massachusetts, exclusive of lost base revenue, that is, revenues reduced as a result of installed energy efficiency measures, for the calendar years 2010 through 2012 is $572.8 million. The combined approved budget for 2009 was $85.3 million. A performance incentive mechanism was also approved by the DPU. The sources used to fund our energy efficiency programs are recoverable from out ratepayers. The Company expected programs to ramp overtime.

The Company and Nantucket Electric obtain cost recovery through each company's systems benefit charge. In addition, the companies can earn performance incentives depending on whether certain set goals are met, and are also entitled to seek recovery of lost base revenues, that is, revenues reduced as a result of installed energy efficiency measures. Lost base revenues may be recovered from a set point in time until the companies' revenue decoupling proposal was approved by the DPU. The Company has requested recovery of lost base revenues in its 2010 Energy Efficiency Reconciliation Factor (EERF) pending before the DPU. The EERF is a separate charge to customers that covers energy efficiency plan costs not otherwise covered by other allowed regulatory cost recovery mechanisms. The DPU allowed the propose EERF to go into effect on May 1, 2010 pending final decision by the DPU. The matter as of this date is still pending. The proposed EERF was filed on Feb 1, 2010.

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

Other provisions of the GCA that will affect the Company include requirements to enter into long-term contracts with renewable electricity suppliers for up to 3% of the utilities' load, the development of a smart grid pilot program, and net metering to allow customers to sell self-generated electricity back to the utilities. Utilities would be allowed to recover costs associated with these new requirements and have the opportunity to earn incentives for certain of these provisions. In addition, under the new law, the maximum level of service quality penalties has been increased from 2% to 2.5% of distribution revenues.

Massachusetts Electric Company

Notes to Financial Statements

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

On May 7, 2010, the Company and Nantucket Electric announced that they had entered into a 15-year Power Purchase Agreement (PPA) with Cape Wind Associates, LLC to purchase half of the power generated by the proposed 468 MW offshore wind project at an initial price of 20.7 cents per kilowatt hour beginning in 2013. Under the terms of the PPA, the contract price would increase by 3.5% annually to account for inflation. The Company's filing requesting approval of the PPA is pending before the DPU.

The components of regulatory assets (liabilities) are as follows:

At March 31 *(In thousands of dollars)*		**2010**		2009
Current regulatory assets included in accounts receivable:				
Rate adjustment mechanisms	**$**	**23,737**	$	6,163
Current regulatory liabilities included in other accrued expenses:				
Rate adjustment mechanisms		**(33,471)**		(65,373)
Total current regulatory liabilities, net		**(9,734)**		(59,210)
Non-current regulatory assets:				
Pension and postretirement benefit plans		**345,578**		-
Unamortized losses on reacquired debt		**6,988**		7,168
Long-term portion of standard offer under-recovery		**40,711**		51,112
Environmental response costs		**97,038**		74,649
Storm costs		**37,362**		32,636
Other		**23,354**		14,384
Total non-current regulatory assets		**551,031**		179,949
Non-current regulatory liabilities:				
Regulatory tax liability		**(22,750)**		(23,195)
Postretirement benefits		**(45,074)**		(47,845)
Environmental response costs		**(76,160)**		(73,787)
Cost of removal		**(169,953)**		(160,980)
Other		**(737)**		(7,357)
Total non-current regulatory liabilities		**(314,674)**		(313,164)
Total non-current regulatory assets (liabilities), net		**236,357**		(133,215)
Net regulatory assets (liabilities)	**$**	**226,623**	$	(192,425)

Cost of Removal and Asset Retirement Obligations:
The Company adheres to the accounting guidance related to asset retirement obligations associated with tangible long-lived assets. The Company does not have any material asset retirement obligations arising from legal obligations as defined under accounting guidance related to asset retirement obligations. However, under the Company's current and prior rate plans, it has collected through rates an implied cost of removal for its plant assets. This cost of removal collected from customers differs from the accounting guidance related to asset retirement obligations associated with tangible long-lived assets definition in that these collections are for costs to remove an asset when it is no longer deemed usable (i.e. broken or obsolete) and not necessarily from a legal obligation. These collections have been recorded to a regulatory liability account to reflect future use. The Company estimates it has collected over time approximately $170 million and $161 million for cost of removal through March 31, 2010 and 2009, respectively.

Massachusetts Electric Company

Notes to Financial Statements

Note 3 - Employee Benefits

Summary
The Company participates with certain other NGUSA subsidiaries in a non-contributory defined benefit pension plan and 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 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 approximately $16.9 million and $5.6 million, respectively.

Defined Contribution Plan: The Company has a defined contribution pension plan (employee savings fund plan) that covers substantially all employees. Employer matching contributions of approximately $3.2 million and $3.3 million were expensed for the years ended March 31, 2010 and 2009, respectively.

Postretirement Benefits Other than Pension:
The Company participates in the PBOP plans with certain other NGUSA subsidiaries. PBOP costs are allocated to the Company. At March 31, 2010 and 2009, the PBOP plans have a net underfunded obligation of $477.3 million and $476.8 million, respectively. The Company's net periodic postretirement benefits cost for the year ended March 31, 2010 and 2009 was approximately $13.9 million and $10.7 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 $10.8 million.

Special Termination Benefits (Voluntary Early Retirement Offer):
In connection with National Grid plc's acquisition of KeySpan Corporation (KeySpan), which was completed on August 24, 2007, National Grid plc and KeySpan offered certain non-union employees voluntary early retirement offer (VERO) packages in June 2007 in an effort to achieve necessary staff reduction through voluntary means. Of the 560 enrolled in the VERO, 5 were the Company's employees. Employees enrolled in the early retirement program will retire by October 1, 2010. The Company's share of the cost of the VERO program was estimated to be $14.6 million, which has been expensed through March 31, 2010. For the year ended March 31, 2010 the Company expensed $3.0 million.

During the year ended March 31, 2010, an additional VERO package was offered to further efforts to reduce staff through voluntary means. Employees enrolled in the early retirement program will retire between January 1, 2010 and December 31, 2010. The Company recorded $1.9 million of allocated costs associated with this VERO package.

During the year ending March 31, 2010, an additional VERO package was offered to 38 union employees as part of National Grid plc's acquisition of KeySpan to further the effort to achieve necessary staff reduction through voluntary means. Of the 38 eligible employees, 33 enrolled in the VERO and were all employees of a National Grid affiliate. Employees enrolled in the early retirement program retired in fiscal year 2010. The Company recorded $0.4 million of allocated costs associated with this VERO package.

Note 4 - Long-term Debt

Notes Payable: In November 2009, the Company issued $800 million of unsecured long-term debt at 5.90% with a maturity date of November 15, 2039. The debt is not registered under the U.S. Securities Act of 1933 (Securities Act) and was sold in the United States only to qualified institutional buyers in reliance on Rule 144A under the Securities Act and to certain non-U.S. persons in transactions outside the United States in reliance on Regulation S under the Securities Act. In conjunction with this debt issuance, the Company incurred debt issuance cost of $6.8 million. The debt issuance cost will be amortized over the life of the debt. The proceeds from the financing were used to: (i) replenish internally generated cash funds that were provided by retained earnings and were used to finance past capital investments in long-lived utility plant assets and refund long-term debt that was issued to finance those investments; (ii) fund future capital expenditures; (iii) term out existing short-term debt so that these financing resources can be made available for ongoing working capital needs, and (iv) pay dividends. The payment of dividends will result in a more optimal and cost efficient capital structure for the Company and result in an appropriate capital structure for the nature of its business and attendant risk profile.

State Authority Financing Bonds: At March 31, 2010, the Company has outstanding a $20 million bond issued through Massachusetts Industrial Finance Agency. The bond is due on August 1, 2014 with a variable interest rate ranging from 0.50% to 1.00% for the twelve months ended March 31, 2010.

Massachusetts Electric Company

Notes to Financial Statements

The aggregate maturities of long-term debt for the five years subsequent to March 31, 2011 are approximately:

(In thousands of dollars)

Year	**Amount**
2011	$ -
2012	-
2013	-
2014	-
2015	20,000
Thereafter	800,000
Total	$ 820,000

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

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 thousand of dollars)	**Plant and Machinery**	**Land and Buildings**	**Vehicles and Equipment**	**Assets in Construction**	**Total**
Balance at March 31, 2008	$ 2,590,917	$ 105,496	$ 198	$ 50,703	$ 2,747,314
Additions	(220)	-	-	163,535	163,315
Disposals	(43,100)	(744)	-	-	(43,844)
Reclassifications	316,249	12,597	240	(149,209)	179,877
Balance at March 31, 2009	2,863,846	117,349	438	65,029	3,046,662
Accumulated depreciation at March 31, 2009	(1,050,762)	(29,088)	-	-	(1,079,850)
Net book value at March 31, 2009	$ 1,813,084	$ 88,261	$ 438	$ 65,029	$ 1,966,812
Balance at March 31, 2009	2,863,846	117,349	438	65,029	3,046,662
Additions	-	-	-	211,623	211,623
Disposals	(25,404)	(8,827)	-	(5)	(34,236)
Reclassifications	159,306	18,815	643	(178,298)	466
Balance at March, 31, 2010	$ 2,997,748	$ 127,337	$ 1,081	$ 98,349	$ 3,224,515
Accumulated depreciation at March 31, 2010	(1,109,173)	(22,433)	-	-	(1,131,606)
Net book value at March 31, 2010	$ 1,888,575	$ 104,904	$ 1,081	$ 98,349	$ 2,092,909

Massachusetts Electric Company

Notes to Financial Statements

Note 6 - Income Taxes

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

(In thousands of dollars)	Fiscal Year Ended March 31, **2010**	2009
Components of federal and state income taxes:		
Current tax expense (benefit):		
Federal	**$ (67,835)**	$ (27,920)
State	**(3,963)**	(82)
Total current tax benefit	**(71,798)**	(28,002)
Deferred tax expense (benefit):		
Federal	**$ 87,039**	$ 43,300
Investment tax credits (1)	**(944)**	(1,094)
State	**32,036**	6,604
Total deferred tax expense	**118,131**	48,810
Total income tax expense	**$ 46,333**	$ 20,808

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

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

(In thousands of dollars)	Fiscal Year Ended March 31, **2010**	2009
Computed tax	**$ 31,281**	$ 23,641
Increase (reduction) including those attributable to flow-through of certain tax adjustments:		
State income taxes, net of federal income tax benefit	**10,105**	4,277
Medicare charge attributable to Patient Protection & Affordable Care Act	**8,623**	(1,103)
Investment tax credit	**(944)**	(1,095)
E.S.O.P. dividends	**(273)**	(309)
Provision to return adjustments	**85**	(334)
Intercompany tax allocation	**-**	(4,264)
Other items, net	**(2,544)**	(5)
Total	**$ 15,052**	$ (2,833)
Federal and state income taxes	**$ 46,333**	$ 20,808

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

(In thousands of dollars)	**2010**	2009
Pension, OPEB and other employee benefits	**$ 99,809**	$ 119,759
Reserve - Environmental	**41,861**	33,558
Future federal benefit on state taxes	**21,566**	13,155
Allowance for uncollectible accounts	**15,470**	16,026
Other items	**2,794**	164
Total deferred tax assets[1]	**181,500**	182,662
Property related differences	**(392,467)**	(287,586)
Regulatory assets - Pension and OPEB	**(122,160)**	-
Other regulatory assets	**(21,301)**	-
Property taxes	**(8,686)**	(7,610)
Investment tax credit	**(3,928)**	(4,872)
Other items	**(14,674)**	(3,044)
Total deferred tax liabilities	**(563,216)**	(303,112)
Net accumulated deferred income tax liability	**(381,716)**	(120,450)
Current portion (net deferred tax asset)	**20,352**	27,690
Net accumulated deferred income tax liability (non-current)	**$ (402,068)**	$ (148,140)

[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 liability for any potential assessments against the consolidated group. In December 2009, NGHI, the parent company of NGUSA, made an income tax accounting method change for routine repair and maintenance of network assets pursuant to Internal Revenue Code Section 162 and Treasury Regulation §1.162-4 in its consolidated federal income tax return for the tax year ended March 31, 2009 which resulted in a current tax benefit during the year ended March 31, 2010.

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.

With the application of this FASB guidance, as of March 31, 2010 and 2009, the Company’s unrecognized tax benefits totaled $66.7 million and $25.1 million, respectively, of which $5 million and $0, respectively, would affect the effective tax rate, if recognized. The unrecognized tax benefits are included in “Deferred credits and liabilities – Other” on the Balance Sheets.

Massachusetts Electric Company

Notes to Financial Statements

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	**$**	**25,149**	$	-
Gross increases related to prior period		**-**		-
Gross increases related to current period		**41,593**		25,149
Settlements with tax authorities		**-**		-
Ending balance	**$**	**66,742**	$	25,149

As of March 31, 2010 and 2009, the Company has no accrued interest related to its unrecognized tax benefits. During the years ended March 31, 2010 and 2009, the Company recorded interest expense of $0.4 million and $0, respectively. The Company recognizes interest related to uncertain tax positions 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.

The IRS is currently auditing the federal NGHI consolidated income tax returns for March 31, 2005 through March 31, 2007. The Company neither expects to make any cash tax payments to the IRS within the next twelve months related to the 2005-2007 audit, nor does it expect any material change in its total gross unrecognized tax benefits over the same period. The years ended March 31, 2008 and 2009 remain subject to examination by the IRS.

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

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

Massachusetts Electric Company

Notes to Financial Statements

Note 7 – Fair Value Measurements

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

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

(In thousands of dollars) Recurring Fair Value Measurements	Level 1	Level 2	Level 3	Total
Available for sale securities (AFS)				
Assets	$ 2,040	$ 2,708	$ -	$ 4,748
Net fair value - AFS	2,040	2,708	-	4,748

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 $821 million.

Note 8 – Goodwill

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

(In thousands of dollars)	2010	2009
Balance at beginning of year	$ 1,008,244	$ 1,008,244
Goodwill acquired	-	-
Goodwill disposed	-	-
Adjustments	-	-
Impairment	-	-
Balance at end of year	$ 1,008,244	$ 1,008,244

Massachusetts Electric Company

Notes to Financial Statements

Note 9 - Accumulated Other Comprehensive Income (Loss)

(In thousands of dollars)	Unrealized Gain (Loss) on Available-for-Sale Securities	Postretirement Benefit Liabilities	Total Accumulated Other Comprehensive Income (Loss)
March 31, 2008 balance, net of tax	$ 191	$ (135,450)	$ (135,259)
Other comprehensive income (loss):			
Unrealized losses on securities	(340)	-	(340)
Changes in pension and other postretirement obligations	-	(83,471)	(83,471)
Reclassification adjustment for losses included in net income	12	-	12
March 31, 2009 balance, net of tax	(137)	(218,921)	(219,058)
Other comprehensive income (loss):			
Unrealized gains on securities	602	-	602
Changes in pension and other postretirement obligations	-	87,804	87,804
Reclassification adjustment for gains included in net income	(146)	-	(146)
Adjustment to accumulated other comprehensive income (1)	-	135,608	135,608
March 31, 2010 balance, net of tax	$ 319	$ 4,491	$ 4,810

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

Note 10 - Commitments and Contingencies

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

Long-Term Contracts for the Purchase of Electric Power:
The Company has several types of long-term contracts for the purchase of electric power. The Company is liable for these payments regardless of the level of service required from third parties. In addition, the Company purchases additional energy to meet its load through the ISO at market prices but is not legally obligated to do so. The Company's commitments under these long-term contracts, as of March 31, 2010, are summarized in the table below.

(In thousands of dollars)

Years Ended March 31,	Estimated Payments
2011	$ 601,080
2012	24,757
Thereafter	-

Massachusetts Electric Company

Notes to Financial Statements

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 wastes. 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 United States Environmental Protection Agency (EPA), the Massachusetts Department of Environmental Protection (DEP), as well as private entities have alleged that the Company is a potentially responsible party (PRP) under state or federal law for a number of sites at which hazardous waste is alleged to have been disposed. The Company's most significant liabilities relate to former manufactured gas plant (MGP) facilities. The Company is currently investigating and remediating, as necessary, those MGP sites and certain other properties under agreements with the EPA and DEP.

In 1993, the DPU approved a settlement agreement that provides for rate recovery of remediation costs of former MGP sites and certain other hazardous waste sites located in Massachusetts. Under that agreement, qualified costs related to these sites are paid out of a special fund established on the Company's books. Rate-recoverable contributions of approximately $4 million are added annually to the fund along with interest, lease payments, and any recoveries from insurance carriers and other third parties.

During the year, the Company completed additional investigations at a legacy environmental site in Massachusetts. The Company is developing remedial alternatives to address contamination on a portion of this site. The Company estimates that the cost to remediate this portion of the site could be $20 million higher than previously estimated and has increased its environmental reserves by such amount during 2010. It is uncertain when these costs will be incurred; however at this point in time we anticipate that the costs will be equally incurred in fiscal year 2012 and 2013.

The Company has recovered amounts from certain insurers, and, where appropriate, the Company intends to seek recovery from other insurers and from other PRPs, but it is uncertain whether, and to what extent, such efforts will be successful. At March 31, 2010 and March 31, 2009, the Company had total reserves for environmental response costs of approximately $96.6 million and $75.2 million, respectively, which include reserves established in connection with the Company's hazardous waste fund referred to above. The Company has also recorded a matching regulatory asset on the Company's Balance Sheet, under "Deferred charges", since environmental expenditures are recoverable from rate payers.

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

Massachusetts Electric Company

Notes to Financial Statements

Note 11 - Related Party Transactions

Accounts 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 years ending March 31, 2010 and 2009, respectively. At March 31, 2010 and March 31, 2009, the Company had accounts payable to the money pool of $193.1 million and $532.3 million, respectively.

Accounts Payable to/Receivable from Affiliates: Additionally, the Company engages in various transactions with NGUSA and its affiliates. Certain activities and costs, such as executive and administrative, financial (including accounting, auditing, risk management, tax and treasury/finance) human resources, information technology, legal and strategic planning are shared between the companies and allocated to each company appropriately. In addition, the Company has a tax sharing agreement with NGHI, a NGUSA affiliate, in filing consolidated tax returns. The Company's share of the tax liability is allocated resulting in a payment to or refund from the Company. At March 31, 2010, the Company had a net accounts receivable from affiliates of $9.9 million and at March 31, 2009, the Company had net accounts payable to affiliates of $14.7 million, for these services.

Service Company Charges: The affiliated service companies of National Grid have furnished services to the Company at the cost of such services. These costs, including operating costs and capital expenditures, were approximately $235.6 million and $204.8 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 $3.6 million before tax and $2.4 million after tax.

Massachusetts Electric Company

Notes to Financial Statements

Note 12 - Cumulative Preferred Stock

A summary of cumulative preferred stock at March 31, 2010 and 2009 is as follows (in thousands except for share data and call prices):

	Shares Outstanding		Amount		Dividends Declared		Call Price
	2010	2009	**2010**	2009	**2010**	2009	
$100 par value-							
4.440% Series	**22,585**	22,585	**$ 2,259**	$ 2,259	**$ 75**	$ 100	$ 104.07

The dividend requirement for cumulative preferred stock was approximately $0.1 million for the years ended March 31, 2010 and 2009, respectively.

Note 13 - Short-term Borrowings

The Company has regulatory approval from the FERC to issue up to $750 million of short-term debt.

The Company had no short-term debt outstanding to third parties at March 31, 2010 and 2009.

At March 31, 2010 and 2009, the Company had a standby bond purchase facility with banks totaling $22 million and $45 million, respectively, which were available to provide liquidity support for $20 million of the Company's long-term bonds in tax-exempt commercial paper mode. The agreement with banks that provide the Company's standby bond purchase facility expires on November 30, 2011. There were no borrowings under this facility at March 31, 2010.

Note 14 - Restrictions on Retained Earnings Available for Dividends on Common Stock

As long as any preferred stock is outstanding, certain restrictions on payment of dividends on common stock would come into effect if the "junior stock equity" was, or by reason of payment of such dividends became, less than 25% of "Total Capitalization." However, the junior stock equity at March 31, 2010 was 69.4% of total capitalization and, accordingly, none of the Company's retained earnings at March 31, 2010 were restricted as to dividends on common stock under the foregoing provisions.