nationalgrid

Massachusetts Electric Company

Financial Statements

For the years ended March 31, 2011 and March 31, 2010

MASSACHUSETTS ELECTRIC COMPANY

TABLE OF CONTENTS

	Page No.
Report of Independent Auditors	2
Balance Sheets March 31, 2011 and March 31, 2010	3
Statements of Income Years Ended March 31, 2011 and March 31, 2010	5
Statements of Cash Flows Years Ended March 31, 2011 and March 31, 2010	6
Statements of Retained Earnings Years Ended March 31, 2011 and March 31, 2010	7
Statements of Comprehensive Income Years Ended March 31, 2011 and March 31, 2010	7
Statements of Capitalization March 31, 2011 and March 31, 2010	8
Notes to Financial Statements	9

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, 2011 and 2010, 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

June 24, 2011

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MASSACHUSETTS ELECTRIC COMPANY
BALANCE SHEETS

(in thousands of dollars)	March 31,	
	2011	2010
ASSETS		
Current assets		
Cash and cash equivalents	**$ 7,541**	$ 8,536
Restricted cash	**71,965**	56,488
Accounts receivable	**302,470**	296,015
Allowance for doubtful accounts	**(40,583)**	(37,276)
Accounts receivable from affiliates, net	**-**	9,888
Unbilled revenues	**92,334**	81,572
Materials and supplies, at average cost	**19,034**	16,526
Current deferred income tax assets	**36,071**	20,352
Prepaid taxes	**8,143**	135,874
Prepaid and other current assets	**8,153**	1,313
Total current assets	**505,128**	589,288
Property, plant, and equipment, net	**2,225,764**	2,108,602
Deferred charges		
Regulatory assets	**448,708**	551,031
Goodwill	**1,008,244**	1,008,244
Other deferred charges	**12,738**	12,842
Total deferred charges	**1,469,690**	1,572,117
Total assets	**$ 4,200,582**	$ 4,270,007

The accompanying notes are an integral part of these financial statements

MASSACHUSETTS ELECTRIC COMPANY
BALANCE SHEETS

(in thousands of dollars)	March 31,	
	2011	2010
LIABILITIES AND CAPITALIZATION		
Current liabilities		
Accounts payable	**$ 164,599**	$ 163,030
Accounts payable to affiliates, net	**19,479**	-
Taxes accrued	**1,654**	2,507
Customer deposits	**9,582**	9,010
Interest accrued	**17,994**	17,676
Intercompany moneypool	**46,563**	193,050
Regulatory liabilities	**59,722**	33,471
Other current liabilities	**51,409**	51,048
Total current liabilities	**371,002**	469,792
Deferred credits and other liabilities		
Regulatory liabilities	**320,942**	314,674
Asset retirement obligations	**1,822**	1,822
Deferred income tax liabilities	**418,414**	402,068
Postretirement benefits and other reserves	**162,924**	227,033
Environmental remediation costs	**97,125**	96,629
Other deferred liabilities	**88,807**	79,760
Total deferred credits and other liabilities	**1,090,034**	1,121,986
Capitalization		
Common stock, par value $25 per share, issued and outstanding 2,398,111 shares	**59,953**	59,953
Cumulative preferred stock, par value $100 per share, issued and outstanding 22,585 shares	**2,259**	2,259
Additional paid-in capital	**1,556,766**	1,556,766
Retained earnings	**298,282**	237,282
Accumulated other comprehensive income	**4,836**	4,810
Total stockholders' equity	**1,922,096**	1,861,070
Long-term debt	**817,450**	817,159
Total capitalization	**2,739,546**	2,678,229
Total liabilities and capitalization	**$ 4,200,582**	$ 4,270,007

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

MASSACHUSETTS ELECTRIC COMPANY
STATEMENTS OF INCOME

(in thousands of dollars)	Years Ended March 31,	
	2011	2010
Operating revenues	**$ 2,025,105**	$ 2,057,968
Operating expenses		
Electricity purchased	**895,340**	1,019,414
Operations and maintenance	**825,692**	770,270
Depreciation	**103,964**	112,376
Other taxes	**49,458**	44,939
Total operating expenses	**1,874,454**	1,946,999
Operating income	**150,651**	110,969
Other income and (deductions)		
Interest on long-term debt	**(49,159)**	(18,201)
Other interest, including affiliate interest	**(2,304)**	(3,160)
Other deductions	**(4,269)**	(234)
Total deductions	**(55,732)**	(21,595)
Income taxes		
Current	**39,247**	(71,798)
Deferred	**(5,428)**	118,131
Total income taxes	**33,819**	46,333
Net income	**$ 61,100**	$ 43,041

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

MASSACHUSETTS ELECTRIC COMPANY
STATEMENTS OF CASH FLOWS

(in thousands of dollars)	Years Ended March 31,	
	2011	2010
Operating activities:		
Net income	**$ 61,100**	$ 43,041
Adjustments to reconcile net income to net cash provided by operating activities		
Depreciation	**103,964**	112,376
(Benefit) provision for deferred income taxes	**(5,428)**	118,131
Allowance for funds used during construction	**(130)**	-
Other non-cash items	**31,647**	9,342
Net prepayments and other amortizations	**933**	460
Net pension and other postretirement expense	**1,237**	1,973
Environmental remediation, net	**(6,844)**	(4,155)
Changes in operating assets and liabilities:		
Accounts receivable, net	**(19,915)**	32,304
Materials and supplies	**(2,508)**	1,712
Accounts payable and accrued expenses	**654**	(45,171)
Prepaid taxes and accruals	**134,104**	(88,280)
Accounts payable and receivable affiliates, net	**29,367**	(27,225)
Standard offer recovery	**42,268**	-
Other, net	**2,572**	5,068
Net cash provided by operating activities	**373,021**	159,576
Investing activities:		
Capital expenditures	**(191,624)**	(208,944)
Restricted cash	**(15,477)**	(50,928)
Other, including cost of removal	**(20,328)**	(18,805)
Net cash used in investing activities	**(227,429)**	(278,677)
Financing activities:		
Dividends paid on common and preferred stock	**(100)**	(335,075)
Debt issuance cost	**-**	(6,770)
Proceeds from long-term debt	**-**	800,000
Decrease in intercompany moneypool	**(146,487)**	(339,200)
Net cash (used in) provided by financing activities	**(146,587)**	118,955
Net decrease in cash and cash equivalents	**(995)**	(146)
Cash and cash equivalents, beginning of year	**8,536**	8,682
Cash and cash equivalents, end of year	**$ 7,541**	$ 8,536
Supplemental information:		
Interest paid	**$ 50,329**	$ 2,494
Income taxes refunded from Parent	**$ (91,348)**	$ -
Capital-related accruals included in accounts payable	**$ 1,233**	$ 2,679

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

MASSACHUSETTS ELECTRIC COMPANY
STATEMENTS OF RETAINED EARNINGS

(in thousands of dollars)	Years Ended March 31,	
	2011	2010
Retained earnings, beginning of year	$ **237,282**	$ 529,316
Net income	**61,100**	43,041
Dividends on preferred stock	**(100)**	(75)
Dividend to Parent	**-**	(335,000)
Retained earnings, end of year	$ **298,282**	$ 237,282

STATEMENTS OF COMPREHENSIVE INCOME

(in thousands of dollars)	Years Ended March 31,	
	2011	2010
Net income	**$ 61,100**	$ 43,041
Other comprehensive income (loss), net of taxes:		
Unrealized gains on investments	**283**	605
Change in pension and other postretirement obligations	**(26)**	87,804
Reclassification adjustment for gains included in net income	**(231)**	(146)
Change in other comprehensive income	**26**	88,263
Total comprehensive income	**$ 61,126**	$ 131,304
Related tax (expense) benefit:		
Unrealized gains on investments	**(189)**	(401)
Change in pension and other postretirement obligations	**17**	(58,536)
Reclassification adjustment for gains included in net income	**154**	97
Total tax expense	**$ (18)**	$ (58,840)

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

MASSACHUSETTS ELECTRIC COMPANY
STATEMENTS OF CAPITALIZATION

(in thousands of dollars, except per share and number of shares data)	March 31,		March 31,	
	2011	2010	**2011**	2010
	Shares issued and outstanding		**Amounts**	
Stockholder's equity				
Common stock, $25 par value	**2,398,111**	2,398,111	**$ 59,953**	$ 59,953
Cumulative preferred stock, $100 par value				
4.44%	**22,585**	22,585	**2,259**	2,259
Additional paid-in capital			**1,556,766**	1,556,766
Retained earnings			**298,282**	237,282
Accumulated other comprehensive income			**4,836**	4,810
Total stockholder's equity	**2,420,696**	2,420,696	**1,922,096**	1,861,070
Long-term debt	**Interest Rate**	**Maturity Date**		
Notes payable				
Unsecured senior notes	5.90%	November 15, 2039	**800,000**	800,000
State authority financing - tax exempt				
Pollution control revenue bonds	Variable	August 1, 2014	**20,000**	20,000
Unamortized discounts			**(2,550)**	(2,841)
Total long-term debt			**817,450**	817,159
Total capitalization			**$ 2,739,546**	$ 2,678,229

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

NOTES TO THE FINANCIAL STATEMENTS

Note 1. Summary of Significant Accounting Policies

A. Nature of Operations

Massachusetts Electric Company (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 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 National Grid USA ("NGUSA").

The Company is an indirectly-owned subsidiary of NGUSA, a public utility holding company with regulated subsidiaries engaged in the generation of electricity and the transmission, distribution and sale of both natural gas and electricity in New England and New York State. NGUSA is an indirectly-owned subsidiary of National Grid plc, a public limited company incorporated under the laws of England and Wales.

B. Basis of Presentation

The Company's accounting policies conform to accounting principles generally accepted 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 the 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 assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting periods. Actual results could differ from those estimates.

C. Regulatory Accounting

The Federal Energy Regulatory Commission ("FERC") and the Massachusetts Department of Public Utilities ("DPU") provide the final determination of the rates we charge our customers. In certain cases, the actions of the FERC and DPU would result in an accounting treatment different from that used by non-regulated companies to determine the rates we charge our customers. In this case, the Company is required to defer the recognition of costs (a regulatory asset) or the recognition of obligations (regulatory liability) if it probable that, through the rate-making process, there will be a corresponding increase or decrease in future rates. The Company is also subject to certain regulations of in addition to the FERC.

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 impact would be material to the Company's reported financial condition and results of operations.

D. Revenue Recognition

Revenues are based on billing rates authorized by the DPU and the allowed distribution revenue as approved by the DPU in relation to the revenue decoupling mechanism ("RDM") in place. 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. Any difference between the allowed revenue and the billed revenue is recorded as a regulatory asset or liability. The Company follows the policy of accruing the estimated amount of revenues for electricity delivered but not yet billed (unbilled revenue), to match costs and revenues more closely. The unbilled revenues at March 31, 2011 and 2010 were approximately $92.3 million and $81.6 million, respectively. The Company defers for future recovery from or refunds to electric customers the difference between revenue and expenses from energy conservation programs, basic service, transmission service, contract termination charges ("CTCs"), and other charges.

During the year ended March 31, 2011, 59% of the Company's revenue from the sale and delivery of electricity was derived from residential customers, 33% from commercial customers, and 8% from industrial customers. During the year ended March 31, 2010, 60% of the Company's revenue from the sale and delivery of electricity was derived from residential customers, 33% from commercial customers, and 7% from industrial customers.

E. Property, Plant and Equipment

Property, plant, and equipment are stated at original cost. The cost of additions to property, plant, and equipment and replacements of retired units of property are capitalized. Costs include direct material, labor, overhead and allowance for funds used during construction ("AFUDC"). Replacement of minor items of property, plant, and equipment and the cost of current repairs and maintenance are charged to expense. Whenever property, plant, and equipment is retired, its original cost, together with cost of removal, less salvage, is charged to accumulated depreciation.

F. Goodwill

The goodwill represents the excess of purchase price of a business combination over the fair value of tangible and intangible assets acquired, net of the fair value of liabilities assumed and the fair value of any non-controlling interest in the acquisition. The Company tests goodwill for impairment on an annual basis and, on an interim basis, when certain events or circumstances exist.

The goodwill impairment analysis is comprised of two steps. In the first step, the Company compares the fair value of each reporting unit to its carrying value. The Company can consider both an income-based approach using projected discounted cash flows and a market-based approach using valuation multiples of comparable companies to determine fair value. The Company's estimate of fair value of each reporting unit is based on a number of subjective factors including: (i) the appropriate weighting of valuation approaches (income-based approach and market-based approach), (ii) estimates of the future revenue and cash flows, (iii) discount rate for estimated cash flows, (iv) selection of peer group companies for the market-based approach, (v) required levels of working capital, (vi) assumed terminal value, (vii) the time horizon of cash flow forecasts and (viii) control premium.

If the fair value of the reporting unit exceeds the carrying value of the net assets assigned to that unit, goodwill is not considered impaired and no further analysis is required to be performed. If the carrying value of the net assets assigned to the reporting unit exceeds the fair value, then a second step is performed to determine the implied fair value of the reporting unit's goodwill. If the carrying value of a reporting unit's goodwill exceeds its implied fair value, then an impairment charge equal to the difference is recorded.

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 5.9% and a terminal year growth rate of 2.4% based upon expected long-term average growth rates. Within its calculation of forecasted returns, the Company made certain assumptions with respect to the amount of pension and environmental costs to be recovered in future periods. Should the Company not continue to receive the same level of recovery 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. 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 that are highly liquid and have maturities of three months or less at the date of purchase as cash equivalents. These short-term investments are carried at cost which approximates fair value.

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 years ended March 31, 2011

and March 31, 2010, $15.5 million and $53.0 million, respectively, was required by the Independent System Operator ("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 income taxes reflect the tax effect of net operating losses, capital losses and general business credit carryforwards and the net tax effects of temporary differences between the carrying amount of assets and liabilities for financial statement and income tax purposes, as determined under enacted tax laws and rates. The financial effect of changes in tax laws or rates is accounted for in the period of enactment. Deferred investment tax credits are amortized over the useful life of the underlying property. 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.

J. Other 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) is unrealized gains and losses associated with certain investments held as available for sale.

K. Employee Benefits

The Company follows the provisions of the Financial Accounting Standards Board ("FASB") accounting guidance related to the accounting for defined benefit pension and postretirement plans which requires employers to fully recognize all postretirement plans' funded status on the balance sheets as a net liability or asset and required an offsetting adjustment to accumulated other comprehensive income in shareholders' equity upon implementation or, in the case of regulated enterprises, to regulatory assets or liabilities. Consistent with past practice, and as required by the guidance, the Company values its pension and postretirement benefits other than pensions ("PBOP") assets using the year-end market value of those assets. Benefit obligations are also measured at year-end

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. The following is the fair value hierarchy that prioritizes the inputs to valuation techniques used to measure fair value into three levels as follows:

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 forward curves and pricing models for the asset or liability due to little or no market activity for the asset or liability with low correlation to observable market inputs

M. Materials and Supplies

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

N. Recent Accounting Pronouncements

Prospective Accounting Pronouncements

In the preceding twelve months, the FASB have issued numerous updates to GAAP. The Company has evaluated various guidelines and has deemed them as not applicable based on its nature of operations or has implemented the new standards. A discussion of the more significant and relevant updates is as follows:

In June 2011, the FASB issued accounting guidance that eliminated the option to present the components of other comprehensive income as part of the statement of changes in stockholders' equity. This update seeks to improve financial statement users' ability to understand the causes of an entity's change in financial position and results of operations. While this update does not change the items that are reported in other comprehensive income or circumstances that require a change in comprehensive income to be reclassified to net income, the entity is now required to present reclassification adjustments from items in other comprehensive income to net income on the face of the financial statements where the components of net income and other comprehensive income are presented. Additionally, the update does not change an entity's option to present components of other comprehensive income net of or before related tax effects. This guidance is effective for public companies for fiscal years, and interim periods within that year, beginning after December 15, 2011, and it is to be applied retrospectively. Early adoption is permitted. The Company is currently in compliance with this update and expects no impact to its financial position, results of operations and operating cash flows.

In April 2011, the FASB issued accounting guidance that substantially amended existing guidance with respect to the fair value measurement topic ("the Topic"). The guidance seeks to amend the Topic in order to achieve common fair value measurement and disclosure requirements in GAAP and International Financial Reporting Standards. Consequently, the guidance changes the wording used to describe many of the requirements in GAAP for measuring fair value and for disclosing information about fair value measurements as well as changing specific applications of the Topic. Some of the amendments clarify the FASB's intent about the application of existing fair value measurement requirements. Other amendments change a particular principle or requirement for measuring fair value or for disclosing information about fair value measurements including, but not limited to, fair value measurement of a portfolio of financial instruments, fair value measurement of premiums and discounts and additional disclosures about fair value measurements. This guidance is effective for financial statements issued for interim and annual periods beginning after December 15, 2011. The early adoption of this guidance is not permitted and can only be applied prospectively. The Company is currently determining the potential impact of the guidance on its financial position, results of operations and cash flows.

In March 2011, the FASB issued updated guidance over the agreements between two entities to transfer financial assets. Prior to this update, an entity could recognize this transfer when it was deemed that the transferee had effective control over the transferred asset, specifically whether the entity has the ability to repurchase substantially the same asset based on the transferor's collateral. This accounting update evaluates the effectiveness of the entity's control by focusing on the transferor's contractual rights and obligations as opposed to the entity's ability to perform on those rights and obligations. This update also eliminates the requirement to demonstrate that the transferor possesses adequate collateral to fund substantially all the cost of purchasing replacement financial assets. This guidance is treated prospectively and effective for annual or interim reporting periods beginning on or after December 15, 2011. The Company does not expect adoption of this guidance to have an impact on the Company's financial position, results of operations or cash flows.

In December 2010, the FASB issued an accounting update to address inconsistencies in the application of accounting guidance related to reporting pro forma revenue and earnings of business combinations. This update is effective for entities who entered into an acquisition and whose acquisition date is on or after the beginning of the first annual reporting period beginning on or after December 15, 2010. This disclosure requires revenue and earnings of the combined entity to be disclosed as though the combination had occurred at the beginning of the prior reporting period. The supplemental disclosure related to this activity now is required to provide a description of the nature and amount of material, nonrecurring pro forma adjustments directly attributable to the business combination. The Company does not expect the adoption of this guidance to have an impact on the Company's financial position, results of operations or cash flows.

In December 2010, the FASB issued an accounting update that modified the goodwill impairment procedures necessary for entities with zero or negative carrying value. The FASB created this guidance to require entities to complete Step 2 of

the impairment test, which requires the entity to assess whether or not it was likely that impairment existed throughout the period. To do this, an entity should consider whether there were adverse qualitative factors throughout the period that would contribute to impairment. This update is effective for fiscal years and interim periods beginning after December 15, 2011. The Company does not expect the adoption of this guidance to have an impact on the Company's financial position, results of operations or cash flows.

Recently Adopted Accounting Pronouncements

In March 2010, the FASB issued updated guidance that provides for scope exceptions applicable to financial instrument contracts with embedded credit derivative features. This FASB guidance is effective for financial statements issued for interim periods beginning after June 15, 2010. On an ongoing basis, the Company evaluates new and existing transactions and agreements to determine whether they are derivatives, or have provisions that meet the characteristics of embedded derivatives. Those transactions designated for any of the elective accounting treatments for derivatives must meet specific, restrictive criteria, both at the time of designation and on an ongoing basis. None of the financial instrument contracts or credit agreements the Company has entered were identified and designated as meeting the criteria for derivative or embedded derivative treatment. The adoption of this guidance did not have an impact on the Company's financial position, results of operations or cash flows.

In February 2010, the FASB issued an amendment to certain recognition and disclosure requirements for events that occur after the balance sheet date but before the financial statements are issued or are available to be issued. The amendment applies to both issued financial statements and financial statements revised as a result of either a correction of an error or retrospective application of GAAP. The new provisions require non-public entities to disclose both the date that the financial statements were issued, or available to be issued, and the date the revised financial statements were issued or available to be issued. The amendment is effective for interim or annual periods ending after June 15, 2010. The adoption of this guidance did not have an impact on the Company's financial position, results of operations or cash flows.

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 statements 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. The adoption of this guidance did not have an impact on the Company's financial position, results of operations or cash flows.

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 beginning after November 15, 2009 and are to be applied to transfers occurring on or after the date of adoption. The adoption of this guidance did not have an impact on the Company's financial position, results of operations or cash flows.

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. The adoption of this guidance did not have an impact on the Company's financial position, results of operations or cash flows.

In May 2009, the FASB issued accounting guidance establishing the general standards of accounting for the 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. The FASB guidance is effective for financial statements issued for interim and annual periods ending after June 15, 2009. The Company adopted this standard for the reporting period beginning April 1, 2010 and noted no impact on the Company's financial position, results of operations or cash flows due to the adoption of this standard.

O. Reclassifications

Certain amounts from prior years have been reclassified in the accompanying financial statements to conform to the current year presentation. These reclassifications had no effect on the results of operations.

Note 2. Rates and Regulatory

The following table presents the Company's regulatory assets and regulatory liabilities at March 31, 2011 and 2010:

(in thousands of dollars)	March 31,	
	2011	2010
Regulatory assets – current		
Rate adjustment mechanisms, included in accounts receivable	**$ 32,979**	$ 23,737
Regulatory liabilities – current		
Rate adjustment mechanisms	**(59,722)**	(33,471)
Total current regulatory assets ,net	**(26,743)**	(9,734)
Regulatory assets – non-current		
Pension and postretirement benefit plans	**296,911**	345,578
Loss on reacquired debt	**6,140**	6,988
Long-term portion of standard offer under-recovery	**(1,557)**	40,711
Deferred environmental restoration costs	**98,501**	97,038
Storm costs	**38,716**	37,362
Other	**9,997**	23,354
Total non-current regulatory assets	**448,708**	551,031
Regulatory liabilities – non-current		
Cost of removal reserve	**(177,889)**	(169,953)
Deferred environmental restoration costs	**(75,369)**	(76,160)
Postretirement benefit	**(42,304)**	(45,074)
Regulatory tax liability	**(22,268)**	(22,750)
Other	**(3,112)**	(737)
Total non-current regulatory liabilities	**(320,942)**	(314,674)
Total non-current regulatory assets, net	**127,766**	236,357
Net regulatory assets	**$ 101,023**	$ 226,623

The regulatory items above are not included in the utility rate base.

Rate Matters

Rates for services rendered by the Company are subject to approval by the DPU. In May 2009, the Company, together with its affiliate Nantucket Electric Company ("Nantucket Electric"), filed an application for an increase of $111.3 million in electric base distribution rates. In April 2010, the DPU approved an overall increase in base distribution revenue of approximately $43.9 million based upon a 10.35% rate of return on equity and a 43.15% equity ratio. Approximately $6.0 million of the increase relates to storm costs associated with restoration of service following an ice storm in December 2008.

In addition, the DPU approved, with modification, the revenue decoupling mechanism ("RDM") proposed by the Company, as well as the reconciliation of commodity-related bad debt and working capital, and pension and PBOP costs to actual costs. In November 2010 and subsequently revised in February 2011, the Company and Nantucket Electric filed an application of approval under its RDM for recovery of $2.6 million. In March 2011, the DPU opened a proceeding, as requested by the Massachusetts Attorney General Office, for an independent audit related to this filing to recover the revenue requirement associated with the 2009 capital investments. The DPU has not yet established the full scope of this proceeding.

This rate order also allowed recovery of non-capitalized pension and PBOP costs to occur outside of base rates through a separate factor. As a result, the Company is authorized to recover all pension and PBOP expenses from its customers. The difference in the costs of the Company's pension and PBOP plans from the amounts billed through this separate factor is deferred to a regulatory asset to be recovered or refunded over the following three years. Consequently in 2010, 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.

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 in accordance with the tariff agreement. In December 2009, NEP filed with the FERC a proposed amendment to the Company's formula rate revenue requirements which decreased the Company's compensation for its electric transmission facilities by approximately $1.7 million. In March 2010, the FERC issued an order establishing hearing and settlement procedures for this filing and made the new rates effective January 1, 2010. In March 2011, NEP filed an uncontested settlement agreement with the FERC resolving all issues raised by the Massachusetts Attorney General in this proceeding.

Other Regulatory Matters

In the general rate case involving the Company's Massachusetts gas distribution affiliates, the DPU opened an investigation to address the allocation and assignment of costs to the gas affiliates by the National Grid service companies. In June 2011, the Attorney General's Office requested DPU to increase the scope of the audit to address the allocation and assignment of costs to the Company by the National Grid service companies and to review the National Grid's cost allocation practices. The Company has agreed to expand the scope of the audit to its Massachusetts electric distribution companies. As of the date of this report, DPU has not yet established the full scope of the audit.

In January 2011, the DPU opened an investigation into the Company and Nantucket Electric's preparation and response to a December 2010 winter storm. The DPU has the authority to issue fines not to exceed approximately $0.3 million for each violation for each day that the violation persists. The maximum fine may not exceed $20 million for any related series of violations. On June 7, 2011, the Company and the Attorney General's Office filed a proposed settlement with a total value of approximately $1.0 million. The settlement requests DPU approval by August 1, 2011. The DPU has informed the Company and the AG that it will not rule on the settlement but will proceed with its initial investigation.

In November 2008, FERC commenced an audit of NGUSA, including its service companies and other affiliates in the National Grid holding company system. The audit evaluated our compliance with: 1) cross-subsidization restrictions on affiliate transactions; 2) accounting, recordkeeping and reporting requirements; 3) preservation of records requirements for holding companies and service companies; and 4) Uniform System of Accounts for centralized service companies. The final audit report from the FERC was received in February 2011. In April 2011, NGUSA replied to the FERC and outlined its plan to address the findings in the report, which we are currently in the process of implementing. None of the findings had a material impact on the financial statements of the Company.

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 its customers, all transmission costs, and costs charged by the Company's affiliate NEP, for stranded costs associated with NEP's former electric generation investments.

Green Communities Act

Pursuant to the Green Communities Act, in October 2009 the DPU approved the Company and Nantucket Electric's proposal 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, Revere, and a location on the Sutton/Northbridge border. The estimated total capital cost of the projects is approximately $31 million. 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 by the DPU in the Company's most recent rate proceeding. The Company and Nantucket Electric requested rate adjustments under this mechanism for the Sutton/Northbridge facility in August 2010 for recovery of approximately $1.0 million, and for the Revere, Everett and Haverhill facilities in February 2011 for recovery of approximately $2.5 million. In each instance, the DPU issued an order approving recovery subject to its ongoing review and further investigation and reconciliation of the Company's costs for the sites. The DPU has not yet issued a final order approving recovery for any of the sites. Construction of the Dorchester site is expected to be completed by the end of 2011.

In May 2010, the Company and Nantucket Electric announced that they entered into a 15-year PPA with Cape Wind Associates, LLC to purchase half of the energy, capacity and renewable energy credits generated by the proposed 468 MW offshore wind project at an adjusted price of 18.7 cents per kilowatt hour beginning in 2013 (escalated for inflation by 3.5% thereafter). In November 2010, the DPU approved the PPA including the Company's proposed cost recovery mechanism. The DPU's decision to approve the PPA has been appealed to the Supreme Judicial Court of Massachusetts with oral arguments to be held in September 2011.

Note 3. Employee Benefits

Summary

The Company sponsors a non-contributory defined benefit pension plan and PBOP plan (the "Plans"), covering substantially all employees.

The pension plan is a non-contributory, tax-qualified defined benefit plan which provides union employees with a retirement benefit and non-union employees hired before January 1, 2011 with a retirement benefit.

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

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, 2011 and March 31, 2010, the pension plans have a net underfunded obligation of $354.8 million and $420.7 million, respectively. The Company's net periodic pension cost for the year ended March 31, 2011 and March 31, 2010 was approximately $21.9 million and $16.9 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 $3.0 million and $3.2 million were expensed for the years ended March 31, 2011 and March 31, 2010, 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, 2011 and 2010, the PBOP plans have a net underfunded obligation of $401.6 million and $477.3 million, respectively. The Company's net periodic postretirement benefits cost for the year ended March 31, 2011 and March 31, 2010 was approximately $16.2 million and $13.9 million, respectively.

Health Care Reform Act

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 that 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 and $10.8 million for the years ended March 31, 2011 and March 31, 2010, respectively.

Workforce Reduction Program

In connection with National Grid plc's acquisition of KeySpan, National Grid plc and KeySpan offered 673 non-union employees a voluntary early retirement offer ("VERO") in an effort to reduce the workforce. Eligible employees must have been working in a targeted area as of April 13, 2007 and be at least 52 years of age with seven or more years of service as of September 30, 2007. For eligible employees who have elected to accept the VERO offer, National Grid plc and KeySpan had the right to retain that employee for up to three years before VERO payments are made. An employee who accepted the VERO offer but elects to terminate employment with National Grid plc or KeySpan prior to the three year period, without consent of National Grid plc or KeySpan, forfeits all rights to VERO payments. The VERO is completed and the Company has accrued approximately $15.7 million which has been deferred for recovery from gas sales customers as part of the synergy savings and cost to achieve calculations.

Note 4. Debt

Short-term

The Company had no short-term debt outstanding to third parties at March 31, 2011 and 2010.

The Company has regulatory approval from the FERC to issue up to $750.0 million of short-term debt.

At March 31, 2011 and 2010, the Company had a standby bond purchase facility with banks totaling $22.0 million, which were available to provide liquidity support for $20.0 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, 2011.

Notes Payable

In November 2009, the Company issued $800.0 million of unsecured long-term debt at 5.9% 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 resulted in a more optimal and cost efficient capital structure for the Company and leaves the Company with an appropriate capital structure for the nature of its business and attendant risk profile.

State Authority Financing Bonds

At March 31, 2011, the Company has outstanding a $20.0 million bond issued through Massachusetts Industrial Finance Agency. The bond is due on August 1, 2014 with a variable interest rate ranging from 0.75% to 0.95% for the year ended March 31, 2011.

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

(in thousands of dollars)

Year Ended March 31,		Amount
2012	$	-
2013		-
2014		-
2015		20,000
2016		-
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 $52.8 million at March 31, 2011 and extends through 2042. This guarantee is absolute and unconditional.

Note 5. Property, Plant and Equipment

At March 31, 2011 and March 31, 2010, property, plant and equipment at cost and accumulated depreciation are as follows:

	March 31,			
(in thousands of dollars)		**2011**		2010
Plant and machinery	**$**	**3,182,214**	$	3,016,059
Land and buildings		**151,142**		127,688
Assets in construction		**81,014**		98,350
Total		**3,414,370**		3,242,097
Accumulated depreciation		**(1,188,606)**		(1,133,495)
Property, plant and equipment, net	**$**	**2,225,764**	$	2,108,602

AFUDC

The Company capitalizes AFUDC as part of construction costs. AFUDC represents an allowance for the cost of funds used to finance construction and includes a debt component and an equity component. AFUDC is capitalized in “Property, plant and equipment” with offsetting credits to “Other interest, including affiliate interest” for the debt component and “Other deductions” for the equity component. 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 its ultimate inclusion in rate base and in the provision for depreciation. The composite AFUDC rates were 0.8% and 0.7% for the years ended March 31, 2011 and 2010, respectively. AFUDC capitalized during the years ended March 31, 2011 and March 31, 2010 was $0.3 million and $0.1 million, respectively.

Depreciation

Depreciation expense is determined using the straight-line method. The depreciation rates are based on periodic studies of the estimated useful lives of the assets and the estimated cost to remove them, net of salvage value.

The provisions for depreciation, as a percentage of weighted average depreciable property, and the weighted average service life, in years, for each asset category for the years ended March 31 are presented in the table below:

	2011		2010	
Asset Category	**Provsion**	**Service Life**	Provsion	Service Life
Electric	**3.3%**	**31**	3.7%	27

The increase in the remaining service life was a result of a rate case filed on May 15, 2009.

Note 6. Income Taxes

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

	Years Ended March 31,	
(in thousands of dollars)	**2011**	2010
Components of federal and state income taxes:		
Current tax expense (benefit):		
Federal	**$ 28,323**	$ (67,835)
State	**10,924**	(3,963)
Total current tax (benefit) expense	**39,247**	(71,798)
Deferred tax expense (benefit):		
Federal	**793**	87,039
State	**(5,346)**	32,036
Total deferred tax expense (benefit)	**(4,553)**	119,075
Investment tax credits [(1)]	**(875)**	(944)
Total income tax expense	**$ 33,819**	$ 46,333

(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, 2011 and 2010 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, 2011 and 2010 is presented in the following table:

	Years Ended March 31,	
(in thousands of dollars)	**2011**	2010
Computed tax	**$ 33,221**	$ 31,281
Increase (reduction) including those attributable to flow-through of certain tax adjustments:		
State income tax, net of federal benefit	**3,626**	10,105
Medicare subsidy, including Patient Protection & Affordable Care Act, net	**-**	8,623
Investment tax credit	**(875)**	(944)
Intercompany tax allocation	**(618)**	-
Employee Stock Ownership Plan dividends	**(256)**	(273)
Other items, net	**(1,279)**	(2,459)
Total	**$ 598**	$ 15,052
Federal and state income taxes	**$ 33,819**	$ 46,333

Significant components of the Company's net deferred tax assets and liabilities at March 31, 2011 and 2010 are presented in the following table:

(in thousands of dollars)	March 31, 2011	2010
Pension, other post-employment benefits ("OPEB") and other employee benefits	**$ 81,779**	$ 99,743
Reserve - environmental	**42,067**	41,862
Regulatory liabilities - assets/other	**32,260**	(4,919)
Future federal benefit on state taxes	**20,391**	21,689
Allowance for uncollectible accounts	**16,842**	15,470
Other items	**7,101**	2,793
Total deferred tax assets[1]	**200,440**	176,638
Property related differences	**(429,160)**	(392,467)
Regulatory assets - pension and OPEB	**(115,590)**	(124,709)
Regulatory assets - storm costs	**(15,926)**	(15,787)
Regulatory assets - environmental	**(9,603)**	(8,664)
Property taxes	**(8,686)**	(8,686)
Other items	**(765)**	(4,113)
Total deferred tax liabilities	**(579,730)**	(554,426)
Net accumulated deferred income tax liability	**(379,290)**	(377,788)
Deferred investment tax credit	**(3,053)**	(3,928)
Net accumulated deferred income tax liability and investment tax credit	**$ (382,343)**	$ (381,716)
Current portion of net deferred tax asset	**36,071**	20,352
Non-current accumulated deferred income tax liability	**$ (418,414)**	$ (402,068)

[1]There were no valuation allowances for deferred tax assets at March 31, 2011 and March 31, 2010.

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.

The Company adopted the provisions of the FASB guidance which clarifies the accounting for uncertainty in income taxes recognized 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.

As of March 31, 2011 and 2010, the Company's unrecognized tax benefits totaled $72.2 million and $66.7 million, respectively, none of which would affect the effective tax rate, if recognized.

The unrecognized tax benefits are included in "Other deferred liabilities" on the balance sheets.

The following table reconciles the changes to the Company's unrecognized tax benefits for the years ended March 31, 2011 and 2010:

Reconciliation of Unrecognized Tax Benefits *(In thousands of dollars)*	Years Ended March 31, 2011	2010
Beginning balance	**$ 66,742**	$ 25,149
Gross decreases related to prior period	**(15)**	-
Gross increases related to current period	**5,433**	41,593
Ending balance	**$ 72,160**	$ 66,742

As of March 31, 2011 and March 31, 2010, the Company has accrued for interest related to unrecognized tax benefits of $1.6 million and nil, respectively. During the years ended March 31, 2011 and March 31, 2010, the Company recorded interest expense of $1.6 million and $0.4 million, respectively. The Company recognizes accrued interest related to unrecognized 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, 2011 and March 31, 2010.

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, 2011, the NGHI consolidated group reached an agreement with the IRS the contained a settlement of the majority of the income tax issues related to the years ending March 31, 2005 through March 31, 2007 as well as an acknowledgment that certain discrete items remained disputed.

The Company is in the process of appealing certain disputed issues with the IRS Office of Appeals relating to its tax returns for March 31, 2005 through March 31, 2007. The Company does not anticipate a change in its unrecognized tax positions in the next twelve months as a result of filing the appeals. However, the Company's tax sharing agreement may result in a change to allocated tax as a result of current and future audits or appeals. The years ended March 31, 2008 through 2011 remain subject to examination by the IRS.

For the years ended March 31, 2011 and March 31, 2010, the Company is a member of the National Grid USA Service Company Massachusetts unitary group. The tax returns for these years remain subject to examination by the State of Massachusetts. Prior to filing as a member of this unitary group, the Company filed on a separate basis. The separate tax returns for the years ended March 31, 2008 and March 31, 2009 remain subject to examination by the State of Massachusetts.

Note 7. Fair Value Measurements

Available for sale securities are primarily in equities and are 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 the Company's balance sheets on a recurring basis and their level within the fair value hierarchy as of March 31, 2011:

Fair Value Measurement Level Summary Table

(in thousands of dollars)	Level 1	Level 2	Level 3	Total
Assets				
Available for sale securities	$ 2,157	$ 2,847	$ -	$ 5,004
Total assets	2,157	2,847	-	5,004

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 sheets reflect the long term debt at carrying value. The fair value of this debt at March 31, 2011 is $856.6 million.

Note 8. 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, 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
Other comprehensive income (loss):			
Unrealized gains on securities	283		283
Changes in pension and other postretirement obligations		(26)	(26)
Reclassification adjustment for gains included in net income	(231)		(231)
March 31, 2011 balance, net of tax	$ 371	$ 4,465	$ 4,836

(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 9. Commitments and Contingencies

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. The Company's commitments under these long-term contracts, as of March 31, 2011, are summarized in the table below.

(in thousands of dollars) Years Ended March 31,	
2012	$ 568,851
2013	23,125

The Company purchases any additional energy needed to meet its load requirements and can purchase the electricity through the ISO at market prices.

Legal Matters

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, financial condition, or cash flows.

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 years 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, 2011 and March 31, 2010, the Company had total reserves for environmental response costs of approximately $97.1 million and $96.6 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 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.

Note 10. Related Party Transactions

Moneypool

The Company participates with NGUSA and certain affiliates in a system moneypool. The money pool is administered by the NGUSA service company as the agent for the participants. Short-term borrowing needs are met first by available funds of the moneypool participants. Borrowings from the moneypool 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 moneypool depositors from an eligible investment in readily marketable money market funds or the existing short-term investment accounts maintained by moneypool 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 moneypool share the interest earned on a basis proportionate to their average monthly investment in the moneypool. Funds may be withdrawn from or repaid to the moneypool at any time without prior notice. At March 31, 2011 and March 31, 2010, the Company had short-term to the moneypool borrowings of $46.6 million and $193.1 million, respectively. The average interest rate for the moneypool was 0.27% for the year ended March 31, 2011 and 2010.

Advances to/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, 2011, the Company had a net accounts payable from affiliates of $19.5 million and at March 31, 2010, the Company had net accounts receivable from affiliates of $9.9 million, for these services.

Reimbursement

In accordance with the Credit and Operating Support Agreement dated March 26, 1996 between the Company and Nantucket Electric, an NGUSA affiliate, 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 equity ("ROE") equivalent to Nantucket Electric's DPU approved 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, 2011 and 2010, the Company reimbursed Nantucket Electric $3.7 million and $3.3 million, respectively.

Service Company Charges

The affiliated service companies of NGUSA provide certain services to the Company at their cost. The service company costs are generally allocated to associated companies through a tiered approach. First and foremost, costs are directly charged to the benefited company whenever practicable. Secondly, in cases where direct charging cannot be readily determined, costs are typically allocated using cost/causation principles linked to the relationship of that type of service, such as meters, square footage, number of employees, etc. Lastly, all other costs are allocated based on a general allocator. These costs include operating and capital expenditures of $217.7 million and $97.0 million for the year ended March 31, 2011 and $163.0 million and $72.6 million for the year ended March 31, 2010, respectively.

Holding Company Charges

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 $5.8 million and $3.6 million before taxes, and $3.8 million and $2.4 million after taxes, for the years ended March 31, 2011 and 2010, respectively.

Organization Restructuring

On January 31, 2011, National Grid plc announced substantial changes to the organization, including new global, US and UK operating models, and changes to the leadership team. The announced structure seeks to create a leaner, more-efficient business backed by streamlined operations that will help meet, more efficiently, the needs of regulators, customers and shareholders. The implementation of the new U.S. business structure commenced on April 4, 2011 and targets annualized savings of $200.0 million by March 2012 primarily through the reduction of approximately 1,200 positions. As of March 31, 2011, NGUSA had recorded a $66.8 million reserve for one-time employment termination benefits related to severance, payroll taxes, healthcare continuation, outplacement services as well as consulting fees related to the restructuring program. These charges have been recorded by NGUSA and none have been allocated to the Company as of March 31, 2011. Subsequently in June 2011, we offered a voluntary severance plan to certain individuals which is expected to cost up to an additional $20 million across all entities affiliated with NGUSA.

Note 11. Cumulative Preferred Stock

The Company has cumulative preferred stock which provide for redemption at the option of the Company. The Company did not redeem any shares of its preferred stock during the years ended March 31, 2011 and March 31, 2010.

Note 12. 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 30% of "Total Capitalization." However, the junior stock equity at March 31, 2011 and 2010, was 70% and 69%, respectively, of total capitalization and, accordingly, none of the Company's retained earnings at March 31, 2011 were restricted as to dividends on common stock under the foregoing provisions.

Note 13. Subsequent Events

In accordance with current authoritative accounting guidance, the Company has evaluated for disclosure subsequent events that have occurred up through June 24, 2011, the date of issuance of these financial statements. As of June 24, 2011, there were no subsequent events which required recognition or disclosure.