national**grid**

Brooklyn Union Gas Company
d/b/a National Grid New York

Consolidated Financial Statements

For the years ended March 31, 2016, 2015, and 2014

BROOKLYN UNION GAS COMPANY

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Independent Auditor's Report

To the Board of Directors
of The Brooklyn Union Gas Company

We have audited the accompanying consolidated financial statements of The Brooklyn Union Gas Company (the Company), which comprise the consolidated balance sheets and statements of capitalization as of March 31, 2016 and 2015, and the related consolidated statements of income, comprehensive income, cash flows, and changes in shareholders' equity for each of the three years in the period ended March 31, 2016.

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of the consolidated financial statements in accordance with accounting principles generally accepted in the United States of America; this includes the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of consolidated financial statements that are free from material misstatement, whether due to fraud or error.

Auditor's Responsibility

Our responsibility is to express an opinion on the consolidated financial statements based on our audits. We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the consolidated financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on our judgment, including the assessment of the risks of material misstatement of the consolidated financial statements, whether due to fraud or error. In making those risk assessments, we consider internal control relevant to the Company's preparation and fair presentation of the consolidated financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Company's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the consolidated financial statements. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Opinion

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of The Brooklyn Union Gas Company at March 31, 2016 and 2015, and the results of their operations and their cash flows for each of the three years in the period ended March 31, 2016 in accordance with accounting principles generally accepted in the United States of America.

PricewaterhouseCoopers LLP

September 12, 2016

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BROOKLYN UNION GAS COMPANY
CONSOLIDATED STATEMENTS OF INCOME
(in thousands of dollars)

	Years Ended March 31,		
	2016	2015	2014
Operating revenues	**$ 1,316,626**	$ 1,518,540	$ 1,624,511
Operating expenses:			
Purchased gas	**373,853**	598,698	662,944
Operations and maintenance	**506,224**	438,784	451,031
Depreciation and amortization	**94,634**	90,979	85,238
Other taxes	**199,615**	190,192	200,689
Total operating expenses	**1,174,326**	1,318,653	1,399,902
Operating income	**142,300**	199,887	224,609
Other income and (deductions):			
Interest on long-term debt	**(51,218)**	(48,918)	(49,022)
Other interest, including affiliate interest	**(2,958)**	1,732	(6,644)
Income from equity investments	**8,072**	16,995	16,439
Gain on sale of assets	**70,253**	-	-
Unrealized gains on investment in Dominion Midstream Partners, LP	**50,470**	-	-
Other income (deductions), net	**4,235**	(4,362)	(2,705)
Total other income (deductions), net	**78,854**	(34,553)	(41,932)
Income before income taxes	**221,154**	165,334	182,677
Income tax expense	**89,701**	66,863	77,746
Net income	**$ 131,453**	$ 98,471	$ 104,931

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

BROOKLYN UNION GAS COMPANY
CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME
(in thousands of dollars)

	Years Ended March 31,		
	2016	2015	2014
Net income	**$ 131,453**	$ 98,471	$ 104,931
Other comprehensive income (loss):			
Unrealized gains (losses) on securities from equity investments	**91**	(85)	298
Total other comprehensive income (loss)	**91**	(85)	298
Comprehensive income	**$ 131,544**	$ 98,386	$ 105,229
Related tax (expense) benefit:			
Unrealized (gains) losses on securities from equity investments	**$ (62)**	$ 59	$ (208)
Total tax (expense) benefit	**$ (62)**	$ 59	$ (208)

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

BROOKLYN UNION GAS COMPANY
CONSOLIDATED STATEMENTS OF CASH FLOWS
(in thousands of dollars)

	Years Ended March 31,		
	2016	2015	2014
Operating activities:			
Net income	**$ 131,453**	$ 98,471	$ 104,931
Adjustments to reconcile net income to net cash provided by operating activities:			
Depreciation and amortization	**94,634**	90,979	85,238
Regulatory amortizations	**53,903**	38,867	38,289
Provision for deferred income taxes	**74,143**	52,966	58,408
Bad debt expense	**21,779**	8,526	3,266
(Income) loss from equity investments, net of dividends received	**1,660**	4,345	(919)
Gain on sale of assets	**(70,253)**	-	-
Unrealized gains on investment in Dominion Midstream Partners, LP	**(50,470)**	-	-
Amortization of debt discount	**1,855**	2,249	2,280
Net postretirement benefits expense (contributions)	**15,049**	16,339	(9,041)
Net environmental remediation payments	**(45,932)**	(42,577)	(27,698)
Changes in operating assets and liabilities:			
Accounts receivable, net, and unbilled revenues	**97,722**	106,451	(118,457)
Inventory	**(21,104)**	(5,819)	5,057
Regulatory assets and liabilities, net	**(36,556)**	(631)	(36,773)
Derivative instruments	**(8,787)**	7,019	(4,109)
Prepaid and accrued taxes	**5,240**	(11,835)	(16,313)
Accounts payable and other liabilities	**12,753**	(5,562)	27,336
Other, net	**(5,847)**	4,497	(3,969)
Net cash provided by operating activities	**271,242**	364,285	107,526
Investing activities:			
Capital expenditures	**(441,352)**	(348,694)	(248,765)
Proceeds from sale of assets	**-**	-	13,877
Affiliated money pool investing and receivables/payables, net	**(356,685)**	(38,010)	(2,945)
Cost of removal	**(24,752)**	(20,676)	(27,495)
Insurance proceeds applied to capital expenditures	**-**	1,418	2,830
Other	**(394)**	3,379	(50)
Net cash used in investing activities	**(823,183)**	(402,583)	(262,548)
Financing activities:			
Proceeds from long-term debt	**994,269**	-	-
Affiliated money pool borrowing and receivables/payables, net	**(447,741)**	(2,233)	164,488
Parent loss tax allocation	**5,818**	17,461	-
Net cash provided by financing activities	**552,346**	15,228	164,488
Net increase (decrease) in cash and cash equivalents	**405**	(23,070)	9,466
Cash and cash equivalents, beginning of year	**3,829**	26,899	17,433
Cash and cash equivalents, end of year	**$ 4,234**	$ 3,829	$ 26,899
Supplemental disclosures:			
Interest paid	**$ (47,376)**	$ (48,952)	$ (61,303)
Income taxes (paid) refunded	**(3,790)**	2,505	(10,891)
Significant non-cash items:			
Capital-related accruals included in accounts payable	**44,494**	27,910	5,418

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

BROOKLYN UNION GAS COMPANY
CONSOLIDATED BALANCE SHEETS
(in thousands of dollars)

	March 31,	
	2016	2015
ASSETS		
Current assets:		
Cash and cash equivalents	**$ 4,234**	$ 3,829
Accounts receivable	**305,287**	392,544
Allowance for doubtful accounts	**(37,252)**	(30,942)
Accounts receivable from affiliates	**1,768**	793
Intercompany money pool	**581,040**	118,055
Unbilled revenues	**61,323**	87,257
Inventory	**82,296**	61,192
Regulatory assets	**18,644**	9,314
Derivative instruments	**3,518**	3,086
Prepaid taxes	**34,591**	39,759
Other	**7,390**	9,204
Total current assets	**1,062,839**	694,091
Equity investments	**-**	72,416
Property, plant and equipment, net	**3,603,782**	3,214,812
Other non-current assets:		
Regulatory assets	**1,276,177**	1,184,939
Goodwill	**1,451,141**	1,451,141
Financial investments	**192,076**	50
Other	**22,954**	19,827
Total other non-current assets	**2,942,348**	2,655,957
Total assets	**$ 7,608,969**	$ 6,637,276

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

BROOKLYN UNION GAS COMPANY
CONSOLIDATED BALANCE SHEETS
(in thousands of dollars)

	March 31, 2016	March 31, 2015
LIABILITIES AND CAPITALIZATION		
Current liabilities:		
Accounts payable	**$ 138,249**	$ 126,122
Accounts payable to affiliates	**115,242**	61,236
Current portion of long-term debt	**810,500**	-
Taxes accrued	**16,181**	13,068
Customer deposits	**26,798**	28,764
Interest accrued	**13,309**	10,952
Regulatory liabilities	**64,289**	75,347
Intercompany money pool	**-**	394,472
Derivative instruments	**3,715**	11,119
Other	**17,233**	20,046
Total current liabilities	**1,205,516**	741,126
Other non-current liabilities:		
Regulatory liabilities	**404,937**	373,581
Asset retirement obligations	**14,145**	13,567
Deferred income tax liabilities, net	**903,955**	821,252
Postretirement benefits	**222,320**	182,188
Environmental remediation costs	**567,370**	542,411
Derivative instruments	**-**	951
Other	**85,367**	77,972
Total other non-current liabilities	**2,198,094**	2,011,922
Commitments and contingencies (Note 12)		
Capitalization:		
Shareholders' equity	**2,981,090**	2,843,728
Long-term debt	**1,224,269**	1,040,500
Total capitalization	**4,205,359**	3,884,228
Total liabilities and capitalization	**$ 7,608,969**	$ 6,637,276

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

BROOKLYN UNION GAS COMPANY
CONSOLIDATED STATEMENTS OF CAPITALIZATION
(in thousands of dollars)

			March 31,	
			2016	2015
Total shareholders' equity			**$ 2,981,090**	$ 2,843,728
Long-term debt:	Interest Rate	Maturity Date		
Unsecured Notes:				
Senior Note	5.60%	November 29, 2016	**400,000**	400,000
Senior Note	3.41%	March 10, 2026	**500,000**	-
Senior Note	4.50%	March 10, 2046	**500,000**	-
Gas Facilities Revenue Bonds:				
1993A and 1993B(1)	6.37%	April 1, 2020	**75,000**	75,000
1997	Variable	December 1, 2020	**125,000**	125,000
1996(1)	5.50%	January 1, 2021	**153,500**	153,500
2005A(1)	4.70%	February 1, 2024	**82,000**	82,000
2005B	Variable	June 1, 2025	**55,000**	55,000
1991A and 1991B(1)	6.95%	July 1, 2026	**100,000**	100,000
1991D	Variable	July 1, 2026	**50,000**	50,000
Total debt			**2,040,500**	1,040,500
Unamortized debt premium			**5,731**	-
Current portion of long-term debt			**810,500**	-
Long-term debt			**1,224,269**	1,040,500
Total capitalization			**$ 4,205,359**	$ 3,884,228

(1) During March 2016, the Company issued Notice of Optional Redemption letters to the bond holders of the fixed interest rate gas facilities revenue bonds. The Company fully repaid these bonds during April 2016 and hence is classifying these bonds within current portion of long-term debt.

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

BROOKLYN UNION GAS COMPANY
CONSOLIDATED STATEMENT OF CHANGES IN SHAREHOLDERS' EQUITY
(in thousands of dollars)

	Common Stock	Cumulative Preferred Stock	Additional Paid-in Capital	Accumulated Other Comprehensive Income (Loss): Equity Investments	Accumulated Other Comprehensive Income (Loss): Total Accumulated Other Comprehensive Income (Loss)	Retained Earnings	Total
Balance as of March 31, 2013	**$ -**	**$ -**	**$ 2,614,795**	**$ (410)**	**$ (410)**	**$ 8,267**	**$ 2,622,652**
Net income	-	-	-	-	-	104,931	104,931
Other comprehensive income:							
Unrealized gains on securities from equity investments, net of $208 tax expense	-	-	-	298	298	-	298
Total comprehensive income							105,229
Balance as of March 31, 2014	**$ -**	**$ -**	**$ 2,614,795**	**$ (112)**	**$ (112)**	**$ 113,198**	**$ 2,727,881**
Net income	-	-	-		-	98,471	98,471
Other comprehensive loss:							
Unrealized losses on securities from equity investments, net of $59 tax benefit	-	-	-	(85)	(85)	-	(85)
Total comprehensive income							98,386
Parent loss tax allocation	-	-	17,461	-	-	-	17,461
Balance as of March 31, 2015	**$ -**	**$ -**	**$ 2,632,256**	**$ (197)**	**$ (197)**	**$ 211,669**	**$ 2,843,728**
Net income	-	-	-		-	131,453	131,453
Other comprehensive income:							
Unrealized gains on securities from equity investments, net of $62 tax expense	-	-	-	91	91	-	91
Total comprehensive income							131,544
Parent loss tax allocation	-	-	5,818	-	-	-	5,818
Balance as of March 31, 2015	**$ -**	**$ -**	**$ 2,638,074**	**$ (106)**	**$ (106)**	**$ 343,122**	**$ 2,981,090**

The Company had 100 shares of common stock authorized, issued and outstanding, with a par value of $0.01 per share and 1 share of preferred stock, authorized, issued and outstanding, with a par value of $1 per share at March 31, 2016, 2015, and 2014.

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

BROOKLYN UNION GAS COMPANY
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

1. NATURE OF OPERATIONS AND BASIS OF PRESENTATION

Brooklyn Union Gas Company d/b/a National Grid New York (the "Company") distributes natural gas to approximately 994,000 retail customers and transports natural gas to approximately 249,000 customers in the boroughs of Brooklyn and Staten Island and two-thirds of the borough of Queens, all in New York City.

The Company is a wholly-owned subsidiary of KeySpan Corporation ("KeySpan" or the "Parent"), which is a wholly-owned subsidiary of National Grid USA ("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. NGUSA is a direct wholly-owned subsidiary of National Grid North America Inc. ("NGNA") and an indirect wholly-owned subsidiary of National Grid plc, a public limited company incorporated under the laws of England and Wales.

Through its wholly-owned subsidiary, North East Transmission Co., Inc. ("NETCO"), the Company owned a 19.4% interest in Iroquois Gas Transmission System L.P. ("Iroquois"), which owns a 375-mile pipeline that transports Canadian gas supply daily to markets in the northeastern United States. Through another wholly-owned subsidiary, the total interest in Iroquois under KeySpan's common control was 20.4%. Because this interest provided KeySpan and its subsidiaries the ability to exercise significant influence over the operating and financial policies of Iroquois, the Company accounted for its interest under the equity method of accounting. The Company's share of the earnings or losses of the affiliate is included as income from equity investments in the accompanying consolidated statements of income.

On September 29, 2015, NETCO contributed its 19.4% interest in Iroquois to Dominion Midstream Partners, LP ("DM") in exchange for approximately 6.5 million common units (representing approximately an 8% interest) of DM. DM was formed to grow a portfolio of natural gas terminals, processing, storage and transportation assets. The transaction resulted in a gain on sale of assets of $70.3 million. The Company has elected the fair value option with respect to its investment in DM and as such, any changes in the fair value of these common units are recorded as unrealized gains on investment in Dominion Midstream Partners, LP in the accompanying consolidated statements of income. The Company's investment in DM is included within financial investments in the accompanying consolidated balance sheets.

The accompanying consolidated financial statements are prepared in accordance with accounting principles generally accepted in the United States of America ("U.S. GAAP"), including the accounting principles for rate-regulated entities. The consolidated financial statements reflect the ratemaking practices of the applicable regulatory authorities. All intercompany balances and transactions have been eliminated in consolidation.

The Company has evaluated subsequent events and transactions through September 12, 2016, the date of issuance of these consolidated financial statements, and concluded that there were no events or transactions that require adjustment to, or disclosure in, the consolidated financial statements as of and for the year ended March 31, 2016, except as described in Note 14, "Subsequent Events."

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Use of Estimates

In preparing consolidated financial statements that conform to U.S. GAAP, the Company must make estimates and assumptions that affect the reported amounts of assets, liabilities, revenues, and expenses, and the disclosure of contingent assets and liabilities included in the consolidated financial statements. Actual results could differ from those estimates.

Regulatory Accounting

The New York Public Service Commission (“NYPSC”) regulates the rates the Company charges its customers. In certain cases, the rate actions of the NYPSC can result in accounting that differs from non-regulated companies. In these cases, the Company defers costs (as regulatory assets) or recognizes obligations (as regulatory liabilities) if it is probable that such amounts will be recovered from, or refunded to, customers through future rates. Regulatory assets and liabilities are reflected in the consolidated statements of income consistent with the treatment of the related costs in the ratemaking process.

Revenue Recognition

Revenues are recognized for gas distribution services provided on a monthly billing cycle basis. The Company records unbilled revenues for the estimated amount of services rendered from the time meters were last read to the end of the accounting period.

With respect to base distribution rates, the NYPSC has approved a Revenue Decoupling Mechanism ("RDM"), which applies only to the Company's firm residential heating sales and transportation customers. The RDM requires the Company to adjust its base rates annually to reflect the over or under recovery of the Company’s allowed revenues per customer from the prior year (May-April).

The Company’s tariff includes a cost of gas adjustment factor which requires an annual reconciliation of recoverable gas costs and revenues. Any difference is deferred pending recovery from, or refund to, customers.

The gas distribution business is influenced by seasonal weather conditions, and, therefore, the Company’s tariff contains a weather normalization adjustment that provides for recovery from, or refund to, firm customers of material shortfalls or excesses of firm delivery revenues (revenues less applicable gas costs and revenue taxes) during a heating season due to variations from normal weather.

Other Taxes

The Company collects taxes and fees from customers such as sales taxes, other taxes, surcharges, and fees that are levied by state or local governments on the sale or distribution of gas. The Company accounts for taxes that are imposed on customers (such as sales taxes) on a net basis (excluded from revenues), while taxes imposed on the Company, such as excise taxes, are recognized on a gross basis. Excise taxes collected and paid for the years ended March 31, 2016, 2015 and 2014 were $43.3 million, $35.9 million and $52.6 million, respectively.

The state of New York imposes on corporations a franchise tax that is computed as the higher of a tax based on income or a tax based on capital. To the extent the Company’s state tax based on capital is in excess of the state tax based on income, the Company reports such excess in other taxes and taxes accrued in the accompanying consolidated financial statements.

Income Taxes

Federal and state 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 consolidated financial statement carrying amounts and the tax basis of existing assets and liabilities. Deferred income taxes also reflect the tax effect of net operating losses, capital losses, and general business credit carryforwards.

The effects of tax positions are recognized in the consolidated financial statements when it is more likely than not that the position taken, or expected to be taken, in a tax return will be sustained upon examination by taxing authorities based on the technical merits of the position. The financial effect of changes in tax laws or rates is accounted for in the period of enactment. Deferred investment tax credits are amortized over the useful life of the underlying property.

NGNA files consolidated federal tax returns including all of the activities of its subsidiaries. Each subsidiary determines its current and deferred taxes based on the separate return method, modified by benefits-for-loss allocation pursuant to a tax sharing agreement between NGNA and its subsidiaries. To the extent that the consolidated return group settles cash differently than the amount reported as realized under the benefit-for-loss allocation, the difference is accounted for as either a capital contribution or as a distribution.

Cash and Cash Equivalents

Cash equivalents consist of short-term, highly liquid investments with original maturities of three months or less. Cash and cash equivalents are carried at cost which approximates fair value.

Accounts Receivable and Allowance for Doubtful Accounts

The Company recognizes an allowance for doubtful accounts to record accounts receivable at estimated net realizable value. The allowance is determined based on a variety of factors including, for each type of receivable, applying an estimated reserve percentage to each aging category, taking into account historical collection and write-off experience and management's assessment of collectability from individual customers as appropriate. The collectability of receivables is continuously assessed and, if circumstances change, the allowance is adjusted accordingly. Receivable balances are written off against the allowance for doubtful accounts when the accounts are disconnected and/or terminated and the balances are deemed to be uncollectible.

Inventory

Inventory is comprised of materials and supplies as well as gas in storage. Materials and supplies are stated at the lower of weighted average cost or market and are expensed or capitalized as used. The Company's policy is to write-off obsolete inventory; there were no material write-offs of obsolete inventory for the years ended March 31, 2016, 2015, or 2014.

Gas in storage is stated at weighted average cost and the related cost is recognized when delivered to customers. Existing rate orders allow the Company to pass directly through to customers the cost of gas purchased, along with any applicable authorized delivery surcharge adjustments. Gas costs passed through to customers are subject to regulatory approvals and are reported periodically to the NYPSC.

The Company had materials and supplies of $19.2 million and $11.5 million and gas in storage of $63.1 million and $49.7 million at March 31, 2016 and 2015, respectively.

Derivative Instruments

The Company uses derivative instruments (including purchase, options, and swaps) to manage commodity price risk. All derivative instruments are recorded in the accompanying consolidated balance sheets at their fair value. All commodity costs, including the impact of derivative instruments, are passed on to customers through the Company's gas cost adjustment mechanism. Therefore, gains or losses on the settlement of these contracts are initially deferred and then refunded to, or collected from, customers consistent with regulatory requirements.

The Company's accounting policy is to not offset fair value amounts recognized for derivative instruments and related cash collateral receivable or payable with the same counterparty under a master netting agreement, and to record and present the fair value of the derivative instrument on a gross basis, with related cash collateral recorded within restricted cash and special deposits in the accompanying consolidated balance sheets. There was no related cash collateral as of March 31, 2016 or 2015.

Fair Value Measurements

The Company measures derivative instruments and financial assets for which it has elected the fair value option at fair value. Fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. The following is the fair value hierarchy that prioritizes the inputs to valuation techniques used to measure fair value:

- Level 1: quoted prices (unadjusted) in active markets for identical assets or liabilities that a company has the ability to access as of the reporting date;
- Level 2: inputs other than quoted prices included within Level 1 that are directly observable for the asset or liability or indirectly observable through corroboration with observable market data; and
- Level 3: unobservable inputs, such as internally-developed forward curves and pricing models for the asset or liability due to little or no market activity for the asset or liability with low correlation to observable market inputs.

The asset or liability’s fair value measurement level within the fair value hierarchy is based on the lowest level of any input that is significant to the fair value measurement. The Company uses valuation techniques that maximize the use of observable inputs and minimize the use of unobservable inputs.

Property, Plant and Equipment

Property, plant and equipment is stated at original cost. The cost of repairs and maintenance is charged to expense and the cost of renewals and betterments that extend the useful life of property, plant and equipment is capitalized. The capitalized cost of additions to property, plant and equipment includes costs such as direct material, labor and benefits, and an allowance for funds used during construction (“AFUDC”).

Depreciation is computed over the estimated useful life of the asset using the composite straight-line method. Depreciation studies are conducted periodically to update the composite rates and are approved by the NYPSC. The average composite rates for the years ended March 31, 2016, 2015 and 2014 were 2.3%, 2.5% and 2.6%, respectively. The average service life for each of the years ended March 31, 2016, 2015 and 2014 was 54 years.

Depreciation expense includes a component for estimated future cost of removal, which is recovered through rates charged to customers. Any difference in cumulative costs recovered and costs incurred is recognized as a regulatory liability. When property, plant and equipment is retired, the original cost, less salvage, is charged to accumulated depreciation, and the related cost of removal is removed from the associated regulatory liability. The Company had cumulative costs recovered in excess of costs incurred of $194.1 million and $194.4 million at March 31, 2016 and 2015, respectively.

Allowance for Funds Used During Construction

In accordance with applicable accounting guidance, the Company records AFUDC, which represents the debt and equity costs of financing the construction of new property, plant and equipment. AFUDC equity is reported in the consolidated statements of income as non-cash income in other income (deductions), net, and AFUDC debt is reported as a non-cash offset to other interest, including affiliate interest. After construction is completed, the Company is permitted to recover these costs through their inclusion in rate base and corresponding depreciation expense. The Company recorded AFUDC related to equity of $1.3 million, zero and $0.2 million and AFUDC related to debt of $1.9 million, $0.2 million and $0.5 million for the years ended March 31, 2016, 2015 and 2014, respectively. The average AFUDC rates for the years ended March 31, 2016, 2015 and 2014 were 1.3%, 0.3% and 3.2%, respectively.

Goodwill

The Company tests goodwill for impairment annually on January 1, and when events occur or circumstances change that would more likely than not reduce the fair value of the Company below its carrying amount. Goodwill is tested for impairment using a two-step approach. The first step compares the estimated fair value of the Company with its carrying value, including goodwill. If the estimated fair value exceeds the carrying value, then goodwill is considered not impaired. If the carrying value exceeds the estimated fair value, then a second step is performed to determine the implied fair value of goodwill. If the carrying value of goodwill exceeds its implied fair value, then an impairment charge equal to the difference is recorded.

The fair value of the Company was calculated in the annual goodwill impairment test for the year ended March 31, 2016 utilizing both income and market approaches. The Company uses a 50% weighting for each valuation methodology, as it believes that each methodology provides equally valuable information. Based on the resulting fair value from the annual analyses, the Company determined that no adjustment of the goodwill carrying value was required at March 31, 2016 or 2015.

Asset Retirement Obligations

Asset retirement obligations are recognized for legal obligations associated with the retirement of property, plant and equipment, primarily associated with the Company's gas distribution facilities. Asset retirement obligations are recorded at fair value in the period in which the obligation is incurred, if the fair value can be reasonably estimated. In the period in which new asset retirement obligations, or changes to the timing or amount of existing retirement obligations are recorded, the associated asset retirement costs are capitalized as part of the carrying amount of the related long-lived asset. In each subsequent period the asset retirement obligation is accreted to its present value.
The following table represents the changes in the Company's asset retirement obligations:

	Years Ended March 31,	
	2016	2015
	(in thousands of dollars)	
Balance as of the beginning of the year	**$ 13,567**	$ 12,205
Accretion expense	**681**	732
Liabilities settled	**(103)**	-
Revaluations to present values of estimated cash flows	**-**	630
Balance as of the end of the year	**$ 14,145**	$ 13,567

At March 31, 2015, the Company carried out a revaluation study that resulted in an upward revaluation in estimated costs related to the asset retirement obligations. These increases were due to changes in remediation cost and enhanced asset replacement programs.

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

Employee Benefits

The Company participates with other KeySpan subsidiaries in defined benefit pension plans and postretirement benefit other than pension ("PBOP") plans for its employees, administered by the Parent. The Company recognizes its portion of the pension and PBOP plans' funded status in the accompanying consolidated balance sheets as a net liability or asset. The cost of providing these plans is recovered through rates; therefore, the net funded status is offset by a regulatory asset or liability. The pension and PBOP plans' assets are commingled and cannot be allocated to an individual company. The Company measures and records its pension and PBOP funded status at the year-end date. Pension and PBOP plan assets are measured at fair value, using the year-end market value of those assets.

New and Recent Accounting Guidance

Accounting Guidance Adopted in Fiscal Year 2016

The new accounting guidance that was adopted for fiscal year 2016 had no material impact on the results of operations, cash flows, or financial position of the Company.

Presentation of Financial Statements – Balance Sheet Classification of Deferred Taxes

In November 2015, the Financial Accounting Standards Board ("FASB") issued Accounting Standards Update ("ASU") 2015-17, "Balance Sheet Classification of Deferred Taxes." The new guidance requires that all deferred tax assets and liabilities, along with any related valuation allowance be classified as non-current in the balance sheets; the new guidance does not change the existing requirement of prohibiting the offsetting of deferred tax liabilities from one jurisdiction against deferred tax assets of another jurisdiction. The Company early adopted this guidance, retrospectively, effective April 1, 2015.

Accounting Guidance Not Yet Adopted

The Company is currently evaluating the impact of recently issued accounting guidance on the presentation, results of operations, cash flows, and financial position of the Company.

Leases

In February 2016, the FASB issued a new lease accounting standard, ASU 2016-02, "Leases (Topic 842)." The key objective of the new standard is to increase transparency and comparability among organizations by recognizing lease assets and lease liabilities on the balance sheet and disclosing key information about leasing arrangements. Lessees will need to recognize a right-of-use asset and a lease liability for virtually all of their leases (other than leases that meet the definition of a short-term lease). For income statement purposes, a dual model has been retained, with leases to be designated as operating leases or finance leases. Expenses will be recognized on a straight-line basis for operating leases, and a front-loaded basis for finance leases. For non-public entities, the new standard is effective for periods beginning after December 15, 2019, with early adoption permitted. The new standard must be adopted using a modified retrospective transition, and provides for certain practical expedients.

Revenue Recognition

In August 2015, the FASB issued ASU 2015-14, "Revenue from Contracts with Customers – Deferral of the Effective Date." The new standard defers by one year the effective date of ASU 2014-09 "Revenue from Contracts with Customers (Topic 606)." The underlying principle of "Revenue from Contracts with Customers" is that an entity will recognize revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration the entity expects to be entitled to, in exchange for those goods or services. The new guidance must be adopted using either a full retrospective approach or a modified retrospective approach. For non-public entities, the new guidance is effective for periods beginning after December 15, 2018, with early adoption permitted for periods beginning after December 15, 2016.

Further, in March 2016, the FASB issued ASU 2016-08, which clarifies the implementation guidance on principal versus agent considerations. In May 2016, the FASB issued ASU 2016-12, providing additional clarity on various aspects of Topic 606, including a) Assessing the Collectibility Criterion and Accounting for Contracts That Do Not Meet the Criteria for Step 1, b) Presentation of Sales Taxes and Other Similar Taxes Collected from Customers, c) Noncash Consideration, d) Contract Modifications at Transition, e) Completed Contracts at Transition, and f) Technical Correction. The effective date and transition requirements for the amendments in these updates are the same as the effective date and transition requirements of ASU 2014-09.

Measurement of Inventory

In July 2015, the FASB issued ASU 2015-11, "Simplifying the Measurement of Inventory." The new guidance requires that inventory be measured at the lower of cost and net realizable value (other than inventory measured using "last-in, first out" and the "retail inventory method"). The new guidance, which must be applied prospectively, is effective for non-public entities for periods beginning after December 15, 2016, with early adoption permitted.

Intangibles – Goodwill and Other – Internal-Use Software, Customer's Accounting for Fees Paid in a Cloud Computing Arrangement

In April 2015, the FASB issued ASU 2015-05 "Intangibles – Goodwill and Other – Internal-Use Software (Subtopic 350-40): Customer's Accounting for Fees Paid in a Cloud Computing Arrangement." The amendments provide guidance to customers about whether a cloud computing arrangement includes a software license. If a cloud computing arrangement includes a software license, then the customer should account for the software license element of the arrangement consistent with the acquisition of other software licenses. If a cloud computing arrangement does not include a software license, the customer should account for the arrangement as a service contract. The guidance will not change GAAP for a customer's accounting for service contracts. In addition, all software licenses within the scope of Subtopic 350-40 will be accounted for consistent with other licenses of intangible assets. For non-public entities, the new guidance is effective for annual periods beginning after December 15, 2015, and interim periods in annual periods beginning after December 15, 2016, with early adoption permitted.

Presentation of Financial Statements – Balance Sheet Classification of Debt Issuance Costs

In April 2015, the FASB issued ASU 2015-03, "Simplifying the Presentation of Debt Issuance Costs." The new guidance requires that debt issuance costs related to term loans, be presented in the balance sheets as a direct deduction from the carrying value of debt. The new guidance, which requires retrospective application, is effective for periods beginning after December 15, 2015, with early adoption permitted.

Consolidation

In February 2015, the FASB issued ASU 2015-02, "Consolidation (Topic 810): Amendments to the Consolidation Analysis." The new guidance eliminates entity specific consolidation guidance for limited partnerships. It also revises other aspects of the consolidation analysis, including how kick-out rights, fee arrangements and related parties are assessed. The new guidance, which requires either modified retrospective or full retrospective basis application, is effective for periods beginning after December 15, 2016, with early adoption permitted.

Presentation of Financial Statements – Going Concern, Disclosure of Uncertainties about an Entity's Ability to Continue as a Going Concern

In August 2014, the FASB issued amendments on reporting about an entity's ability to continue as a going concern in ASU 2014-15, "Presentation of Financial Statements – Going Concern (Subtopic 205 - 40): Disclosure of Uncertainties about an Entity's Ability to Continue as a Going Concern." The amendments provide guidance about management's responsibility to evaluate whether there is substantial doubt surrounding an entity's ability to continue as a going concern. If management concludes that substantial doubt exists, the amendments require additional disclosures relating to management's evaluation and conclusion. The amendments are effective for the annual reporting period ending after December 15, 2016 and interim periods thereafter.

Financial Statement Revision

During 2016, management determined that certain accounting transactions were not properly recorded in the Company's previously issued financial statements. The Company has corrected the accounting by revising the prior period financial statements presented herein, the impacts of which are described below. The Company concluded that the corrections were not material to any prior periods.

During a review of the Company's open work orders within capital work in progress, management identified charges that were inappropriately classified as capital instead of expense. A cumulative adjustment of $7.2 million (net of income taxes) was recorded, of which $1.7 million was recorded as a decrease to opening retained earnings (as of March 31, 2013), and $3.3 million and $2.2 million were recorded as a decrease to net income with the correction recorded within operations and maintenance expense for the years ended March 31, 2015 and 2014, respectively.

In addition, during a review of the Company's accounting for its unbilled revenue accrual, management identified a gas costs deferral for the year ended March 31, 2014 that had not reversed into the subsequent fiscal year. An adjustment of $7.5 million (net of income taxes) was recorded as a decrease to net income with the correction recorded within purchased gas, for the year ended March 31, 2015.

Finally, the Company has corrected other immaterial adjustments. A cumulative adjustment of $0.1 million (net of income taxes) was recorded, of which $0.7 million was recorded as an increase to opening retained earnings (as of March 31, 2013) and $0.3 million and $0.5 million were recorded as a decrease to net income for the years ended March 31, 2015 and March 31, 2014, respectively.

The following table shows the amounts previously reported as revised:

	As Previously Reported [1]	Adjustments	As Revised
		(in thousands of dollars)	
Consolidated Statement of Income	**March 2015**		**March 2015**
Operating revenues	$ 1,518,784	$ (244)	$ 1,518,540
Total operating expenses	1,300,637	18,016	1,318,653
Operating income	218,147	(18,260)	199,887
Total other income (deductions)	(34,366)	(187)	(34,553)
Income before income taxes	183,781	(18,447)	165,334
Income tax expense	74,354	(7,491)	66,863
Net income	109,427	(10,956)	98,471
Consolidated Statement of Income	**March 2014**		**March 2014**
Operating revenues	$ 1,624,557	$ (46)	$ 1,624,511
Total operating expenses	1,396,165	3,737	1,399,902
Operating income	228,392	(3,783)	224,609
Total other income (deductions)	(41,168)	(764)	(41,932)
Income before income taxes	187,224	(4,547)	182,677
Income tax expense	79,592	(1,846)	77,746
Net income	107,632	(2,701)	104,931
Consolidated Statement of Cash Flows	**March 2015**		**March 2015**
Net cash provided by operating activities	$ 373,839	$ (9,554)	$ 364,285
Net cash used in investing activities	(412,137)	9,554	(402,583)
Consolidated Statement of Cash Flows	**March 2014**		**March 2014**
Net cash provided by operating activities	$ 108,361	$ (835)	$ 107,526
Net cash used in investing activities	(263,383)	835	(262,548)

	As Previously Reported [1]	Adjustments	As Revised
		(in thousands of dollars)	
Consolidated Balance Sheet	**March 2015**		**March 2015**
Total current assets	$ 705,938	$ (11,847)	$ 694,091
Property, plant, and equipment, net	3,227,937	(13,125)	3,214,812
Total assets	6,662,248	(24,972)	6,637,276
Total current liabilities	742,323	(1,197)	741,126
Total other non-current liabilities	2,021,051	(9,129)	2,011,922
Total liabilities and capitalization	6,662,248	(24,972)	6,637,276
Retained Earnings			
March 31, 2015	226,316	(14,647)	211,669
March 31, 2014	116,889	(3,691)	113,198
March 31, 2013	9,257	(990)	8,267
Shareholders' equity			
March 31, 2015	2,858,375	(14,647)	2,843,728
March 31, 2014	2,731,571	(3,690)	2,727,881
March 31, 2013	2,623,640	(988)	2,622,652

[1] During 2016, the Company early adopted ASU 2015-17 “Balance Sheet Classification of Deferred Taxes” retrospectively (as discussed in Note 10, “Income Taxes”). This change in accounting policy resulted in the reclassification of balances reported at March 31, 2015.

3. REGULATORY ASSETS AND LIABILITIES

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

	March 31, 2016	March 31, 2015
	(in thousands of dollars)	
Regulatory assets		
Current:		
Derivative instruments	**$ 198**	$ 8,984
Gas costs adjustment	**16,722**	-
Rate adjustment mechanism	**1,568**	-
Other	**156**	330
Total	**18,644**	9,314
Non-current:		
Environmental response costs	**770,589**	738,119
Postretirement benefits	**367,057**	341,974
Temperature control/interruptible sharing	**82,676**	48,710
Other	**55,855**	56,136
Total	**1,276,177**	1,184,939
Regulatory liabilities		
Current:		
Energy efficiency	**38,936**	41,879
Gas costs adjustment	**-**	5,471
Revenue decoupling mechanism	**19,561**	11,586
Temporary state assessment	**3,188**	13,330
Other	**2,604**	3,081
Total	**64,289**	75,347
Non-current:		
Cost of removal	**194,051**	194,425
Delivery rate adjustment	**44,974**	44,974
Excess earnings	**88,082**	88,082
Other	**77,830**	46,100
Total	**404,937**	373,581
Net regulatory assets	**$ 825,595**	$ 745,325

Cost of removal: Represents cumulative amounts collected, but not yet spent, to dispose of property, plant and equipment. This liability is discharged as removal costs are incurred.

Delivery rate adjustment: The NYPSC authorized a surcharge for recovery of regulatory assets ("Delivery Rate Surcharge") of $5 million beginning January 1, 2008, which increased incrementally by $5 million in rate years two through five; aggregating to a total of approximately $75 million over the term of the rate agreement. In its order issued and effective November 28, 2012 (Order Authorizing Recovery of Deferred Balances), the NYPSC authorized a Site Investigation and Remediation ("SIR") Surcharge in the amount of $25 million which superseded the Delivery Rate Surcharge effective January 1, 2013. These SIR recoveries will be used to amortize existing SIR deferral balances. On June 5, 2015, the Company submitted a petition to the NYPSC to increase its existing SIR Surcharge by $37.5 million annually and remaining in effect until new base rates are set. The proposed increase in the SIR Surcharge will allow the Company to recover some of its environmental remediation costs and minimize future bill impacts for customers. On October 19, 2015, the NYPSC issued an order authorizing the Company to increase its annual SIR Surcharge by $37.5 million annually, commencing November 1, 2015.

Derivative instruments: The Company evaluates open derivative instruments for regulatory deferral by determining if they are probable of recovery from, or refund to, customers through future rates. Derivative instruments that qualify for recovery are recorded at fair value, with changes in fair value recorded as regulatory assets or regulatory liabilities in the period in which the change occurs.

Energy efficiency: Represents the difference between revenue billed to customers through the Company's energy efficiency charge and the costs of the Company's energy efficiency programs as approved by the NYPSC.

Environmental response costs: Represents deferred costs associated with the Company's shares of the estimated costs to investigate and perform certain remediation activities at former manufactured gas plant ("MGP") sites and related facilities. The Company believes future costs, beyond the expiration of current rate plans, will continue to be recovered through rates.

Excess earnings: At the end of each rate year (calendar year), the Company is required to provide the NYPSC with a computation of its return on common equity capital ("ROE"). During the primary term of the rate plan (2008-2012), if the ROE in the applicable rate year exceeded 10.5%, the Company was required to defer a portion of the revenue equivalent associated with any over earnings for the benefit of customers. Beginning January 1, 2013, the threshold for earnings sharing has been reduced from 10.5% to 9.4% and the sharing mechanism is calculated based upon a cumulative average ROE over rate years 2013 and 2014 with 80% of any excess earnings applied as a credit against the SIR deferral balance.

Gas costs adjustment: The Company is subject to rate adjustment mechanisms for commodity costs, whereby an asset or liability is recognized resulting from differences between actual revenues and the underlying cost being recovered or differences between actual revenues and targeted amounts as approved by the NYPSC. These amounts will be refunded to, or recovered from, customers over the next year.

Postretirement benefits: Represents the excess costs of the Company's pension and PBOP plans over amounts received in rates that are deferred to a regulatory asset to be recovered in future periods and the non-cash accrual of net actuarial gains and losses. Also included within this amount are certain pension deferral amounts from prior to the acquisition of KeySpan by NGUSA, which are being recovered in rates over a ten year period ending August 2017.

Rate adjustment mechanisms: The Company is subject to a number of rate adjustment mechanisms whereby an asset or liability is recognized resulting from differences between actual revenues and the underlying cost being recovered, or differences between actual revenues and targeted amounts as approved by the NYPSC. These amounts will be refunded to, or recovered from, customers.

Revenue decoupling mechanism: As approved by the NYPSC, the Company has a RDM which applies only to the Company's firm residential heating sales and transportation customers. The RDM allows for annual adjustment to the Company's delivery rates as a result of the reconciliation between allowed revenue per customer and actual revenue per customer. Any difference between the allowed revenue per customer and the actual revenue per customer is recorded as a regulatory asset or regulatory liability.

Temperature control/interruptible ("TC/IT") sharing: Under the existing rate agreement, the revenue requirement reflects certain levels of imputed TC/IT margins. Differences between the actual margins and imputed margins are shared 90% by ratepayers and 10% by shareholders. This regulatory asset represents the ratepayer share of the differences.

Temporary state assessment: In June 2009, the NYPSC authorized utilities, including the Company, to recover the costs required for payment of the Temporary State Energy & Utility Service Conservation Assessment ("Temporary State Assessment"), including carrying charges. The Temporary State Assessment is subject to reconciliation over a five year period which began July 1, 2009. On June 18, 2014, the NYPSC issued an order authorizing certain utilities, including the

Company, to recover the Temporary State Assessment subject to reconciliation, including carrying charges, from July 1, 2014 through June 30, 2017. As of March 31, 2016, the Company over-collected on these costs. The Company is required to net any deferred over-collected amounts against the amount to be collected during fiscal years 2014 and 2015 as well as the first payment relating to fiscal years 2015 and 2016.

The Company records carrying charges on all regulatory balances (with the exception of derivative instruments, cost of removal, environmental response costs, and regulatory deferred tax balances), for which cash expenditures have been made and are subject to recovery, or for which cash has been collected and is subject to refund. Carrying charges are not recorded on items for which expenditures have not yet been made.

4. RATE MATTERS

Rate Case Filing

On January 29, 2016, the Company filed to adjust its base gas rates, which, if adopted, would be effective from January 1, 2017. The filing seeks to increase gas delivery base revenues. On June 17, 2016, the Company filed for a month-extension in the suspension period in the proceedings with a make whole provision, such that new rates would become effective February 1, 2017. On July 21, 2016, to allow additional time for the parties to conduct settlement discussions and finalize a joint proposal with KeySpan Gas East Corporation (“KeySpan Gas East”), the Company requested an additional one-month extension in the suspension period, subject to a make whole, such that new rates would become effective no later than March 1, 2017.

On September 7, 2017, the Company filed a Joint Proposal establishing a three year rate plan for the Company and KeySpan Gas East, beginning January 1, 2017 and ending December 31, 2019. The Joint Proposal is supported by several parties, including Department of Public Service Staff and the City of New York. It is expected that the NYPSC will issue an order on the Joint Proposal in December or January and that new rates would go into effect in either January or February. The Joint Proposal includes a make whole provision that, if approved, is designed to ensure the Company and KeySpan Gas East are restored to the same financial position by December 31, 2017 as if new rates went into effect beginning January 1, 2017.

General Rate Case

On June 13, 2013, the NYPSC approved a rate plan extension covering the Company’s 2013 and 2014 rate years. The Company’s revenue requirements for both years have been modified as follows: (i) there is no change in base delivery rates, other than those previously approved by the NYPSC in the rate plan extension, (ii) the allowed ROE decreased from 9.8% to 9.4%, and (iii) the common equity ratio in the capital structure increased from 45% to 48%.

Management Audit

In February 2011, the NYPSC selected Overland Consulting Inc., (“Overland”) to perform a management audit of NGUSA’s affiliate cost allocations, policies and procedures. The Company disputed certain of Overland’s final audit conclusions and the NYPSC ordered that further proceedings be conducted to address what, if any, ratemaking adjustments were necessary. On September 5, 2014, the NYPSC approved a settlement that resolves all outstanding issues relating to the audit and establishes a $13.3 million regulatory liability.

Gas Management Audit

In February 2013, the NYPSC initiated a comprehensive management and operational audit of NGUSA’s New York gas businesses, including the Company, pursuant to the Public Service Law requirement that major electric and gas utilities undergo an audit every five years. The audit commenced in August 2013 and the NYPSC issued an audit findings report in October 2014. The audit findings found that the Company’s operations performed well in providing reliable gas service, and strength in operations, network planning, project management, work management, load forecasting, supply procurement and customer systems support. Also included were 31 recommendations for improvement, including: reconstituting the boards of directors of NGUSA and the gas companies in New York to include more objective oversight; establishing stronger reporting authority between the New York jurisdictional president and operational organizations; preparing a true strategic plan for NGUSA's New York operations to serve as a road map for investments, programs and operations to build upon the state energy plan and energy initiatives; developing a five-year, integrated, system-wide plan that includes all gas reliability work, mandated replacements, growth projects and system planning work; enhancing internal service level agreements to promote accountability for performance and costs; and undertaking a full accounting of all costs associated with NGUSA's SAP enterprise wide system. In November 2014, NGUSA's New York gas businesses filed joint audit implementation plans addressing each of the audit recommendations. On May 14, 2015, the NYPSC issued an order accepting without modifications the joint implementation plans and directing NGUSA's New York gas businesses to execute the plans.

Operations Audit

In August 2013, the NYPSC initiated an operational audit to review the accuracy of the customer service, electric reliability, and gas safety data reported by the investor owned utilities operating in New York, including the Company. On December 19, 2013, the NYPSC selected Overland to conduct the audit, which commenced in February 2014. On April 20, 2016, the NYPSC released Overland's audit report publicly and adopted the majority of recommendations in the report. The audit report found that the Company, in general, is meeting its obligations to supply self-reported data. The report contains recommendations to improve internal controls and allow for greater consistency in reporting among the New York utilities. The recommendations do not affect current rate case performance targets or mechanisms and may be considered for potential implementation in future rate plans. The Company filed its plan to implement the audit recommendations with the NYPSC on May 19, 2016. On May 26, 2016, the NYPSC issued a Notice Seeking Comments on the draft customer service recommendations that were not addressed in the previous order. The Company filed comments on the draft recommendations on July 20, 2016.

Operations Staffing Audit

In January 2014, the NYPSC initiated an operational audit to review internal staffing levels and use of contractors for the core utility functions of the investor owned utilities operating in New York, including the Company. On June 26, 2014, the NYPSC selected The Liberty Consulting Group to conduct the audit. At the time of the issuance of these consolidated financial statements, the Company cannot predict the outcome of this operational audit.

Capital Reconciliation Mechanism Petition

In June 2015, the Company submitted a petition to the NYPSC requesting a modification to the Capital Expenditures and Net Utility Plant and Depreciation Expense Reconciliation Mechanism ("Capital Reconciliation Mechanism") in its current rate plan. The Capital Reconciliation Mechanism is a downward only net utility plant reconciliation mechanism that permits a cumulative, two-year reconciliation for the two years ended December 31, 2014 and annual reconciliations thereafter. While the Company implemented and largely completed its capital program for 2013 and 2014, its ability to launch certain programs was hampered by SuperStorm Sandy and its aftermath. The impact of these delays and other related issues was a deferred liability, which was offset against the regulatory asset recorded in relation to the primary term of the rate plan. The Company requested a modification to the Capital Reconciliation Mechanism to extend the reconciliation period for two years (calendar years 2015 and 2016) to complete more capital projects and facilitate the Company's plan to invest in its distribution system infrastructure. On October 19, 2015, the NYPSC issued an order granting the requested two year extension to the reconciliation period.

5. PROPERTY, PLANT AND EQUIPMENT

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

	March 31, 2016	March 31, 2015
	(in thousands of dollars)	
Plant and machinery	**$ 4,047,563**	$ 3,787,992
Land and buildings	**188,580**	190,530
Assets in construction	**345,534**	228,037
Software and other intangibles	**124,399**	124,399
Total property, plant and equipment	**4,706,076**	4,330,958
Accumulated depreciation and amortization	**(1,102,294)**	(1,116,146)
Property, plant and equipment, net	**$ 3,603,782**	$ 3,214,812

6. DERIVATIVE INSTRUMENTS

The Company utilizes derivative instruments to manage commodity price risk associated with its natural gas purchases. The Company's commodity risk management strategy is to reduce fluctuations in firm gas sales prices to its customers.

The Company's financial exposures are monitored and managed as an integral part of the Company's overall financial risk management policy. The Company engages in risk management activities only in commodities and financial markets where it has an exposure, and only in terms and volumes consistent with its core business.

Volumes

Volumes of outstanding commodity derivative instruments measured in dekatherms ("dths") are as follows:

	March 31, 2016	March 31, 2015
	(in thousands)	
Gas option contracts	**7,450**	2,220
Gas purchase contracts	**13,979**	17,564
Gas swap contracts	**23,786**	18,252
Total	**45,215**	38,036

Amounts Recognized in the Accompanying Consolidated Balance Sheets

	Asset Derivatives			Liability Derivatives	
	March 31,			March 31,	
	2016	2015		**2016**	2015
	(in thousands of dollars)			*(in thousands of dollars)*	
Current assets:			Current liabilities:		
Rate recoverable contracts:			Rate recoverable contracts:		
Gas option contracts	**$ 194**	$ 36	Gas option contracts	**$ 222**	$ 290
Gas purchase contracts	**224**	1,478	Gas purchase contracts	**1,216**	4,547
Gas swap contracts	**3,100**	$ 1,572	Gas swap contracts	**2,277**	$ 6,282
	3,518	3,086		**3,715**	11,119
Other non-current assets:			Other non-current liabilities:		
Rate recoverable contracts:			Rate recoverable contracts:		
Gas purchase contracts	**-**	-	Gas purchase contracts	**-**	951
	-	-		**-**	951
Total	**$ 3,518**	$ 3,086	Total	**$ 3,715**	$ 12,070

The changes in fair value of the Company's rate recoverable contracts are offset by changes in regulatory assets and liabilities. As a result, the changes in fair value of those contracts had no impact in the accompanying consolidated statements of income. The Company had no derivative instruments not subject to rate recovery as of March 31, 2016 and 2015.

Credit and Collateral

The Company is exposed to credit risk related to transactions entered into for commodity price risk management. Credit risk represents the risk of loss due to counterparty non-performance. Credit risk is managed by assessing each counterparty's credit profile and negotiating appropriate levels of collateral and credit support.

The credit policy for commodity transactions is managed and monitored by the Finance Committee to National Grid plc's Board of Directors ("Finance Committee"), which is responsible for approving risk management policies and objectives for risk assessment, control and valuation, and the monitoring and reporting of risk exposures. NGUSA's Energy Procurement Risk Management Committee ("EPRMC") is responsible for approving transaction strategies, annual supply plans, and counterparty credit approval, as well as all valuation and control procedures. The EPRMC is chaired by the Vice President of U.S. Treasury and reports to both the NGUSA Board of Directors and the Finance Committee.

The EPRMC monitors counterparty credit exposure and appropriate measures are taken to bring such exposures below the limits, including, without limitation, netting agreements, and limitations on the type and tenor of trades. The Company enters into enabling agreements that allow for payment netting with its counterparties, which reduce its exposure to counterparty risk by providing for the offset of amounts payable to the counterparty against amounts receivable from the counterparty. In instances where a counterparty's credit quality has declined, or credit exposure exceeds certain levels, the Company may limit its credit exposure by restricting new transactions with the counterparty, requiring additional collateral or credit support, and negotiating the early termination of certain agreements. Similarly, the Company may be required to post collateral to its counterparties.

The Company's credit exposure for all commodity derivative instruments, applicable payables and receivables, and instruments that are subject to master netting agreements, was an asset of $2.2 million and a liability of $8.7 million as of March 31, 2016 and 2015, respectively.

The aggregate fair value of the Company's commodity derivative instruments with credit-risk-related contingent features that are in a liability position at March 31, 2016 and 2015 was $0.7 million and $5.3 million, respectively. The Company had no collateral posted for these instruments at March 31, 2016 or 2015. If the Company's credit rating were to be downgraded by one or two levels, it would not be required to post any additional collateral. If the Company's credit rating were to be downgraded by three levels, it would be required to post $0.8 million and $5.4 million additional collateral to its counterparties at March 31, 2016 and 2015, respectively.

Offsetting Information for Derivative Instruments Subject to Master Netting Arrangements

March 31, 2016

Gross Amounts Not Offset in the Consolidated Balance Sheets

(in thousands of dollars)

ASSETS:	Gross amounts of recognized assets *A*	Gross amounts offset in the Consolidated Balance Sheets *B*	Net amounts of assets presented in the Consolidated Balance Sheets *C=A+B*	Financial instruments *Da*	Cash collateral received *Db*	Net amount *E=C-D*
Derivative instruments						
Gas option contracts	$ 194	$ -	$ 194	$ -	$ -	$ 194
Gas purchase contracts	224	-	224	-	-	224
Gas swap contracts	3,100	-	3,100	-	-	3,100
Total	$ 3,518	$ -	$ 3,518	$ -	$ -	$ 3,518

LIABILITIES:	Gross amounts of recognized liabilities *A*	Gross amounts offset in the Consolidated Balance Sheets *B*	Net amounts of liabilities presented in the Consolidated Balance Sheets *C=A+B*	Financial instruments *Da*	Cash collateral paid *Db*	Net amount *E=C-D*
Derivative instruments						
Gas option contracts	$ 222	$ -	$ 222	$ -	$ -	$ 222
Gas purchase contracts	1,216	-	1,216	-	-	1,216
Gas swap contracts	2,277	-	2,277	-	-	2,277
Total	$ 3,715	$ -	$ 3,715	$ -	$ -	$ 3,715

March 31, 2015

Gross Amounts Not Offset in the Consolidated Balance Sheets

(in thousands of dollars)

ASSETS:	Gross amounts of recognized assets *A*	Gross amounts offset in the Consolidated Balance Sheets *B*	Net amounts of assets presented in the Consolidated Balance Sheets *C=A+B*	Financial instruments *Da*	Cash collateral received *Db*	Net amount *E=C-D*
Derivative instruments						
Gas option contracts	$ 36	$ -	$ 36	$ -	$ -	$ 36
Gas purchase contracts	1,478	-	1,478	-	-	1,478
Gas swap contracts	1,572	-	1,572	-	-	1,572
Total	$ 3,086	$ -	$ 3,086	$ -	$ -	$ 3,086

LIABILITIES:	Gross amounts of recognized liabilities *A*	Gross amounts offset in the Consolidated Balance Sheets *B*	Net amounts of liabilities presented in the Consolidated Balance Sheets *C=A+B*	Financial instruments *Da*	Cash collateral paid *Db*	Net amount *E=C-D*
Derivative instruments						
Gas option contracts	$ 290	$ -	$ 290	$ -	$ -	$ 290
Gas purchase contracts	5,498	-	5,498	-	-	5,498
Gas swap contracts	6,282	-	6,282	-	-	6,282
Total	$ 12,070	$ -	$ 12,070	$ -	$ -	$ 12,070

7. FAIR VALUE MEASUREMENTS

The following tables present assets and liabilities measured and recorded at fair value in the accompanying consolidated balance sheets on a recurring basis and their level within the fair value hierarchy as of March 31, 2016 and 2015:

	March 31, 2016			
	Level 1	Level 2	Level 3	Total
		(in thousands of dollars)		
Assets:				
Derivative instruments				
Gas option contracts	$ -	$ -	$ 194	$ 194
Gas purchase contracts	-	6	218	224
Gas swap contracts	-	3,100	-	3,100
Investment in Dominion Midstream Partners, LP	-	192,026	-	192,026
Total	-	195,132	412	195,544
Liabilities:				
Derivative instruments				
Gas option contracts	-	-	222	222
Gas purchase contracts	-	82	1,134	1,216
Gas swap contracts	-	2,277	-	2,277
Total	-	2,359	1,356	3,715
Net assets (liabilities)	$ -	$ 192,773	$ (944)	$ 191,829

	March 31, 2015			
	Level 1	Level 2	Level 3	Total
		(in thousands of dollars)		
Assets:				
Derivative instruments				
Gas option contracts	$ -	$ -	$ 36	$ 36
Gas purchase contracts	-	17	1,461	1,478
Gas swap contracts	-	1,572	-	1,572
Total	-	1,589	1,497	3,086
Liabilities:				
Derivative instruments				
Gas option contracts	-	-	290	290
Gas purchase contracts	-	84	5,414	5,498
Gas swap contracts	-	6,282	-	6,282
Total	-	6,366	5,704	12,070
Net liabilities	$ -	$ (4,777)	$ (4,207)	$ (8,984)

Derivative instruments: The Company’s Level 2 fair value derivative instruments primarily consist of over-the-counter (“OTC”) gas swap contracts and gas purchase contracts with pricing inputs obtained from the New York Mercantile Exchange and the Intercontinental Exchange (“ICE”), except in cases where the ICE publishes seasonal averages or where there were no transactions within the last seven days. The Company may utilize discounting based on quoted interest rate curves, including consideration of non-performance risk, and may include a liquidity reserve calculated based on bid/ask spread for the Company’s Level 2 derivative instruments. Substantially all of these price curves are observable in the marketplace throughout at least 95% of the remaining contractual quantity, or they could be constructed from market observable curves with correlation coefficients of 95% or higher.

The Company's Level 3 fair value derivative instruments primarily consist of OTC gas option contracts and gas purchase contracts, which are valued based on internally-developed models. Industry-standard valuation techniques, such as the Black-Scholes pricing model, Monte Carlo simulation, and Financial Engineering Associates libraries are used for valuing such instruments. A derivative is designated Level 3 when it is valued based on a forward curve that is internally developed, extrapolated or derived from market observable curves with correlation coefficients less than 95%, where optionality is present, or if non-economic assumptions are made. The internally developed forward curves have a high level of correlation with Platts Mark-to-Market curves and are reviewed by the middle office. The Company considers non-performance risk and liquidity risk in the valuation of derivative instruments categorized in Level 2 and Level 3.

Investment in Dominion Midstream Partners, LP: The Company's Level 2 Investment in DM is valued based on Level 1 quoted market prices for DM common units, combined with a discount to the quoted market price which is calculated using Level 2 inputs, to reflect restrictions on the transfer of the units and resulting lack of marketability.

Changes in Level 3 Derivative Instruments

	Years Ended March 31,	
	2016	2015
	(in thousands of dollars)	
Balance as of the beginning of the year	**$ (4,207)**	$ (217)
Total gains or losses included in regulatory assets and liabilities	**1,645**	(10,423)
Settlements	**1,618**	6,433
Balance as of the end of the year	**$ (944)**	$ (4,207)

A transfer into Level 3 represents existing assets or liabilities that were previously categorized at a higher level for which the inputs became unobservable during the year. A transfer out of Level 3 represents assets and liabilities that were previously classified as Level 3 for which the inputs became observable based on the criteria discussed previously for classification in Level 2. These transfers, which are recognized at the end of each period, result from changes in the observability of forward curves from the beginning to the end of each reporting period. There were no transfers between Level 1 and Level 2, and no transfers into or out of Level 3, during the years ended March 31, 2016, 2015, or 2014.

For valuations that include both observable and unobservable inputs, if the unobservable input is determined to be significant to the overall inputs, the entire valuation is categorized in Level 3. This includes derivative instruments valued using indicative price quotations whose contract tenure extends into unobservable periods. In instances where observable data is unavailable, consideration is given to the assumptions that market participants would use in valuing the asset or liability. This includes assumptions about market risks such as liquidity, volatility, and contract duration. Such instruments are categorized in Level 3 as the model inputs generally are not observable. The forward curves used for financial reporting are developed and verified by the middle office.

Quantitative Information About Level 3 Fair Value Measurements

The following tables provide information about the Company's Level 3 valuations:

Commodity	Level 3 Position	Fair Value as of March 31, 2016			Valuation Technique(s)	Significant Unobservable Input	Range
		Assets	(Liabilities)	Total			
		(in thousands of dollars)					
Gas	Purchase contracts	$ -	$ (1,134)	$ (1,134)	Discounted Cash Flow	Forward Curve (A)	$1.891 - $1.891/dth
Gas/Power	Cross commodity contracts	218	-	218	Discounted Cash Flow	Forward Curve	$14.162 - $251.197/dth
Gas	Option contracts	194	(222)	(28)	Discounted Cash Flow	Implied Volatility	34% - 38%
	Total	$ 412	$ (1,356)	$ (944)			

(A) Includes deals with valuation assumptions on gas supply.

Commodity	Level 3 Position	Fair Value as of March 31, 2015			Valuation Technique(s)	Significant Unobservable Input	Range
		Assets	(Liabilities)	Total			
		(in thousands of dollars)					
Gas	Purchase contracts	$ 1,161	$ (5,414)	$ (4,253)	Discounted Cash Flow	Forward Curve (A)	$0.96 - $11.47/dth
Gas/Power	Cross commodity contracts	300	-	300	Discounted Cash Flow	Forward Curve	$23.61 - $378.51/dth
Gas	Option contracts	36	(290)	(254)	Discounted Cash Flow	Implied Volatility	34% - 41%
	Total	$ 1,497	$ (5,704)	$ (4,207)			

(A) Includes deals with valuation assumptions on gas supply.

The significant unobservable inputs listed above would have a direct impact on the fair values of the Level 3 instruments if they were adjusted. The significant unobservable inputs used in the fair value measurement of the Company's gas purchase and gas option derivative instruments are forward commodity prices, implied volatility and valuation assumptions pertaining to peaking gas deals based on forward gas curves. A relative change in commodity price at various locations underlying the open positions can result in significantly different fair value estimates.

Other Fair Value Measurements

The Company's consolidated balance sheets reflect long-term debt at amortized cost. The fair value of the Company's long-term debt was based on quoted market prices when available, or estimated using quoted market prices for similar debt. The fair value of this debt at March 31, 2016 and 2015 was $2.1 and $1.2 billion, respectively.

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

8. EMPLOYEE BENEFITS

The Company participates with certain other KeySpan subsidiaries in qualified and non-qualified non-contributory defined benefit plans (the “Pension Plans”) and a PBOP plan (together with the Pension Plans (the “Plans”)), covering substantially all employees.

The Pension Plans provide union employees, as well as all non-union employees hired before January 1, 2011, with a retirement benefit. Supplemental non-qualified, non-contributory executive retirement programs provide additional defined pension benefits for certain executives. The PBOP plan provides health care and life insurance coverage to eligible retired employees. Eligibility is based on age and length of service requirements and, in most cases, retirees must contribute to the cost of their coverage.

During the years ended March 31, 2016, 2015, and 2014, the Company made contributions of approximately $24.6 million, $22.8 million, and $45.6 million, respectively, to the Plans.

The Plans’ assets are commingled and cannot be allocated to an individual company. The Plans’ costs are first directly charged to the Company based on the Company’s employees that participate in the Plans. Costs associated with affiliated service companies’ employees are then allocated as part of the labor burden for work performed on the Company’s behalf. In addition, certain changes in the funded status of the Plans are also allocated based on the employees associated with the Company through an intercompany payable account and are presented as postretirement benefits in the accompanying consolidated balance sheets. Pension and PBOP expenses are included within operations and maintenance expense in the accompanying consolidated statements of income.

KeySpan’s unfunded obligations at March 31, 2016 and 2015 are as follows:

	March 31,	
	2016	2015
	(in thousands of dollars)	
Pension	**$ 979,081**	$ 1,055,558
PBOP	**946,860**	985,669
	$ 1,925,941	$ 2,041,227

The Company’s net pension and PBOP expenses directly charged and allocated from affiliated service companies, net of capital, for the years ended March 31, 2016, 2015, and 2014 are as follows:

	Years Ended March 31,		
	2016	**2015**	2014
	(in thousands of dollars)		
Pension	**$ 15,625**	$ 15,656	$ 15,634
PBOP	**19,186**	19,186	19,186
	$ 34,811	$ 34,842	$ 34,820

Defined Contribution Plan

NGUSA has a defined contribution pension plan that covers substantially all employees. For the years ended March 31, 2016, 2015, and 2014, the Company recognized an expense in the accompanying consolidated statements of income of $1.6 million, $1.1 million, and $1 million, respectively, for matching contributions.

Other Benefits

At March 31, 2016 and 2015, the Company had accrued workers compensation, auto, and general insurance claims which have been incurred but not yet reported of $11.9 million and $10.5 million, respectively.

9. CAPITALIZATION

The aggregate maturities of long-term debt for the years subsequent to March 31, 2016 are as follows:

(in thousands of dollars)	
Years Ending March 31,	
2017	$ 810,500
2018	-
2019	-
2020	-
2021	125,000
Thereafter	1,105,000
Total	$ 2,040,500

The Company's debt agreements and banking facilities contain covenants, including those relating to the periodic and timely provision of financial information by the issuing entity and financial covenants such as restrictions on the level of indebtedness. Failure to comply with these covenants, or to obtain waivers of those requirements, could in some cases trigger a right, at the lender's discretion, to require repayment of some of the Company's debt and may restrict the Company's ability to draw upon its facilities or access the capital markets. During the years ended March 31, 2016 and 2015, the Company was in compliance with all such covenants.

Unsecured Notes

In March 2016, the Company issued $500 million of unsecured senior long-term debt at 3.407% with a maturity date of March 10, 2026 and $500 million of unsecured senior long-term debt at 4.504% with a maturity date of March 10, 2046.

Gas Facilities Revenue Bonds

The Company has outstanding tax-exempt Gas Facilities Revenue Bonds ("GFRB") issued through the New York State Energy Research and Development Authority. At March 31, 2016 and 2015, $640.5 million of GFRB were outstanding; $230 million of which are variable-rate, auction rate bonds. The GFRB currently in auction rate mode are backed by bond insurance. These bonds cannot be put back to the Company and, in the case of a failed auction, the resulting interest rate on the bonds would revert to the maximum auction rate which depends on the current appropriate, short-term benchmark rates and the senior unsecured rating of the Company's bonds. The effect of the failed auctions on interest on long-term debt was not material for the years ended March 31, 2016, 2015, or 2014.

Dividend Restrictions

Pursuant to the NYPSC's orders, the ability of the Company to pay dividends to KeySpan is conditioned upon maintenance of a utility capital structure with debt not exceeding 56% of total utility capitalization. At March 31, 2016 and 2015, the Company was in compliance with the utility capital structure required by the NYPSC.

Preferred Stock

In connection with the acquisition of KeySpan by NGUSA, the Company became subject to a requirement to issue a class of preferred stock, having one share (the "Golden Share") subordinate to any existing preferred stock. The holder of the Golden Share would have voting rights that limit the Company's right to commence any voluntary bankruptcy, liquidation, receivership, or similar proceeding without the consent of the holder of the Golden Share. The NYPSC subsequently authorized the issuance of the Golden Share to a trustee, GSS Holdings, Inc. ("GSS"), who will hold the Golden Share subject to a Services and Indemnity Agreement requiring GSS to vote the Golden Share in the best interests of New York State ("NYS"). On July 8, 2011, the Company issued the Golden Share with a par value of $1.

10. INCOME TAXES

Components of Income Tax Expense

	Years Ended March 31,		
	2016	2015	2014
	(in thousands of dollars)		
Current tax expense (benefit):			
Federal	**$ 9,741**	$ 9,486	$ 10,596
State	**5,817**	4,411	8,742
Total current tax expense (benefit)	**15,558**	13,897	19,338
Deferred tax expense (benefit):			
Federal	**61,010**	43,764	49,362
State	**14,044**	10,113	9,957
Total deferred tax expense (benefit)	**75,054**	53,877	59,319
Amortized investment tax credits (1)	**(911)**	(911)	(911)
Total deferred tax expense (benefit)	**74,143**	52,966	58,408
Total income tax expense	**$ 89,701**	$ 66,863	$ 77,746

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

Statutory Rate Reconciliation

The Company's effective tax rates for the years ended March 31, 2016, 2015, and 2014 are 40.6%, 40.4%, and 42.6%, respectively. The following table presents a reconciliation of income tax expense at the federal statutory tax rate of 35% to the actual tax expense:

	Years Ended March 31,		
	2016	2015	2014
	(in thousands of dollars)		
Computed tax	**$ 77,403**	$ 57,866	$ 63,936
Change in computed taxes resulting from:			
Investment tax credit	**(911)**	(911)	(911)
State income tax, net of federal benefit	**12,910**	9,440	12,155
Temporary differences flowed through	**-**	-	1,404
Other items, net	**299**	468	1,162
Total	**12,298**	8,997	13,810
Total income tax expenses	**$ 89,701**	$ 66,863	$ 77,746

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

During the period there was no material change in the Company's deferred tax liability for the decrease in the tax rate from 7.1% to 6.5% applicable to New York entities beginning with the fiscal year ended March 31, 2017. Likewise there was no material change in the Company's deferred tax liability for the increase in the Metropolitan Transportation Authority surcharge from 25.6% to 28%.

On August 26, 2016, Internal Revenue Service ("IRS") issued Revenue Procedure 2016-48 that enables the Company to claim prior year's unclaimed bonus depreciation in its federal income tax return for the period ended March 31, 2016. As a result of the adoption of this procedure, the Company will increase its other long term liability and reduce its deferred tax liability by $4.6 million in the next fiscal year.

Deferred Tax Components

	March 31,	
	2016	2015
	(in thousands of dollars)	
Deferred tax assets:		
Environmental remediation costs	**$ 245,785**	$ 259,968
Future federal benefit on state taxes	**46,449**	40,300
Net operating losses	**63,204**	1,874
Postretirement benefits and other employee benefits	**134,572**	115,245
Regulatory liabilities - other	**136,996**	140,693
Other items	**45,018**	39,981
Total deferred tax assets [1]	**672,024**	598,061
Deferred tax liabilities:		
Property related differences	**886,031**	786,264
Regulatory assets - environmental response costs	**334,330**	344,783
Regulatory assets - postretirement benefits	**151,494**	135,724
Regulatory assets - other	**92,868**	89,293
Other items	**109,264**	60,346
Total deferred tax liabilities	**1,573,987**	1,416,410
Net deferred income tax liabilities	**901,963**	818,349
Deferred investment tax credits	**1,992**	2,903
Deferred income tax liabilities, net	**$ 903,955**	$ 821,252

[1] The Company established a valuation allowance for deferred tax assets in the amount of $0.9 million related to expiring charitable contribution carryforwards at March 31, 2016. There was no valuation allowance for deferred tax assets at March 31, 2015.

As a result of retrospective adoption of ASU 2015-17, the Company adjusted its current portion of deferred income tax assets and non-current deferred income tax liabilities, net by $26.7 million as of March 31, 2015.

Net Operating Losses

The following table presents the amounts and expiration dates of net operating losses as of March 31, 2016:

Expiration of net operating losses:	Federal	NYS
	(in thousands of dollars)	
3/31/2029	$ 35,906	$ -
3/31/2033	12,085	-
3/31/2035	4,173	108,620
3/31/2036	161,600	103,820

Unrecognized Tax Benefits

As of March 31, 2016, 2015, and 2014, the Company's unrecognized tax benefits totaled $76.7 million, $72.3 million, and $73.4 million, respectively, of which $$0.8 million, $0.8 million, and zero, respectively, would affect the effective tax rate, if recognized. The unrecognized tax benefits are included in other non-current liabilities in the accompanying consolidated balance sheets.

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

	Years Ended March 31,		
	2016	2015	2014
		(in thousands of dollars)	
Balance as of the beginning of the year	**$ 72,315**	$ 73,428	$ 113,030
Gross increases - tax positions in prior periods	**-**	1,331	2,046
Gross decreases - tax positions in prior periods	**(4,057)**	(13,988)	(16,622)
Gross increases - current period tax positions	**8,477**	11,544	13,727
Settlements with tax authorities	**-**	-	(38,753)
Balance as of the end of the year	**$ 76,735**	$ 72,315	$ 73,428

As of March 31, 2016 and 2015, the Company has accrued for interest related to unrecognized tax benefits of $4.7 million and $3.6 million, respectively. During the years ended March 31, 2016, 2015, and 2014, the Company recorded interest expense of $1.2 million, $1.4 million, and $3.9 million, respectively. The Company recognizes interest related to unrecognized tax benefits in other interest, including affiliate interest and related penalties, if applicable, in other income (deductions), net in the accompanying consolidated statements of income. During year ended March 31, 2016 the Company recorded a tax penalty expense of $0.2 million. Immaterial tax penalties were recorded during the year ended March 31, 2015 and none during the year ended March 31, 2014

The Company is included in NGNA and subsidiaries' administrative appeal with the IRS related to the issues disputed in the examination cycles for the years ended August 24, 2007, March 31, 2008 and March 31, 2009. During the period, the IRS commenced its next examination cycle which includes income tax returns for the years ended March 31, 2010 through March 31, 2012. The examination is not expected to conclude until December 2017. The income tax returns for the years ended March 31, 2013 through March 31, 2016 remain subject to examination by the IRS.

The state of New York is in the process of examining the Company's NYS income tax returns for the years ended August 24, 2007 through March 31, 2008. In June 2016, the Company received a preliminary audit report with proposed decreases to state taxable income primarily related to transition property depreciation deduction. The Company conducted an internal review of the audit report, agreed with its findings and will enter into settlement discussions with the state of New York in the next fiscal year.

The income tax returns for the years ended March 31, 2009 through March 31, 2015 remain subject to examination by the state of New York.

It is reasonably possible that other events will occur during the next twelve months that would cause the total amount of unrecognized tax benefits to increase or decrease. However, excluding the impact of the potential settlement with the state of New York, the Company does not believe any such increases or decreases would be material to its results of operations, financial position, or cash flows.

The following table indicates the earliest tax year subject to examination for each major jurisdiction:

Jurisdiction	**Tax Year**
Federal	March 31, 2010
New York	August 24, 2007

11. ENVIRONMENTAL MATTERS

The normal ongoing operations and historic activities of the Company are subject to various federal, state, and local environmental laws and regulations. Under federal and state Superfund laws, potential liability for the historic contamination of property may be imposed on responsible parties jointly and severally, without regard to fault, even if the activities were lawful when they occurred.

In March of 2010, the Gowanus Canal was named to the United States Environmental Protection Agency ("EPA") Superfund List. The Company's predecessor owned three historical manufactured gas plants located along the Canal. In September of 2013, the EPA issued its Record of Decision, which prescribes the remedy for the Canal. The EPA estimates the entire remedy will cost $506 million. On March 21, 2014, the EPA issued a Unilateral Administrative Order to the Company and more than twenty-five other industrial potentially responsible parties ("PRPs"), to commence the design of the remedy. Although no estimate for the design of the remedy was given, an estimate of 10% of remedy cost is typically used when estimating design costs. The Company is negotiating with the other PRPs to share work and costs.

The Company has identified numerous MGP sites and related facilities, which were owned or operated by the Company or its predecessors. These former sites, some of which are no longer owned by the Company, have been identified to the NYPSC and the New York State Department of Environmental Conservation ("DEC") for inclusion on appropriate site inventories. Administrative Orders on Consent or Voluntary Cleanup Agreements have been executed with the DEC to address the investigation and remediation activities associated with certain sites. Expenditures incurred for the years ended March 31, 2016, 2015, and 2014 were $45.9 million, $42.6 million, and $27.7 million, respectively.

Upon the acquisition of KeySpan by NGUSA, the Company recognized its environmental liabilities at fair value. The fair values included discounting of the reserve, which is being accreted over the period for which remediation is expected to occur. Following the acquisition, these environmental liabilities are recognized in accordance with the current accounting guidance for environmental obligations.

The Company estimated the remaining costs of environmental remediation activities were $567.4 million and $542.4 million at March 31, 2016 and 2015, respectively. The Company's environmental obligation is discounted at a rate of 6.5%; the undiscounted amount of environmental liabilities at March 31, 2016 and 2015 was $684.3 million and $658.5 million, respectively. These costs are expected to be incurred over approximately 45 years, and the discounted amounts have been recorded as reserves in the accompanying consolidated balance sheets. However, remediation costs for each site may be materially higher than estimated, depending on changing technologies and regulatory standards, selected end use for each site, and actual environmental conditions encountered. The Company has recovered amounts from certain insurers and potentially responsible parties, and, where appropriate, the Company may seek additional recovery from other insurers and from other potentially responsible parties, but it is uncertain whether, and to what extent, such efforts will be successful.

By rate orders, the NYPSC has provided for the recovery of SIR costs. Accordingly, as of March 31, 2016 and 2015, the Company has recorded net environmental regulatory assets of $761 million and $736.4 million, respectively.

The Company believes that its ongoing operations, and its approach to addressing conditions at historic sites, are in substantial compliance with all applicable environmental laws. Where the Company has regulatory recovery, it believes that the obligations imposed on it because of the environmental laws will not have a material impact on its results of operations or financial position.

12. COMMITMENTS AND CONTINGENCIES

Operating Lease Obligations

The Company has an operating lease for office space which is utilized by both the Company and its affiliates. A portion of the lease expense is allocated from the service company to the affiliated entities that benefit from its use. The gross rental expense for the leasehold was approximately $12.2 million, $11.9 million, and $11.5 million the years ended March 31, 2016, 2015, and 2014, respectively. The rental expense, net of amounts allocated to affiliated entities, recognized by the Company in the accompanying consolidated statements of income was approximately $4.1 million, $4 million, and $3.1 million for the years ended March 31, 2016, 2015, and 2014, respectively.

The future minimum lease payments for the years subsequent to March 31, 2016 are as follows:

(in thousands of dollars) Years Ending March 31,		
2017	$	12,756
2018		13,426
2019		14,139
2020		14,900
2021		15,729
Thereafter		69,397
Total	$	140,347

Purchase Commitments

The Company has entered into various contracts for gas delivery, storage, and supply services. Certain of these contracts require payment of annual demand charges, which are recoverable from customers. The Company is liable for these payments regardless of the level of service required from third-parties. In addition, the Company has various capital commitments related to the construction of property, plant and equipment.

The Company's commitments under these long-term contracts for the years subsequent to March 31, 2016 are summarized in the table below:

(in thousands of dollars) Years Ending March 31,	Gas	Capital Expenditures
2017	$ 192,126	$ 12,922
2018	156,860	9,830
2019	129,653	-
2020	91,784	-
2021	82,800	-
Thereafter	531,982	-
Total	$ 1,185,205	$ 22,752

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, individually or in the aggregate, to its business or likely to result in a material adverse effect on its results of operations, financial position, or cash flows.

SuperStorm Sandy

In October 2012, SuperStorm Sandy hit the northeastern U.S. affecting energy supply to customers in the Company's service territory. Total costs associated with gas customer service restoration from this storm (including capital expenditures) through March 31, 2014 were approximately $69.1 million.

In December 2014, NGUSA reached a final settlement with its insurers, of which the Company's allocated portion was $52.2 million (inclusive of advance payments of $29.2 million), and received final payment for the remaining amounts due. This resulted in the Company recognizing a gain of $2.6 million for the year ended March 31, 2015, recorded as a reduction to operations and maintenance expense in the accompanying consolidated statements of income.

13. RELATED PARTY TRANSACTIONS

Accounts Receivable from and Accounts Payable to Affiliates

NGUSA and its affiliates provide various services to the Company, including executive and administrative, customer services, financial (including accounting, auditing, risk management, tax, and treasury/finance), human resources, information technology, legal, and strategic planning, that are charged between the companies and charged to each company.

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

	Accounts Receivable from Affiliates		Accounts Payable to Affiliates	
	March 31,		March 31,	
	2016	2015	**2016**	2015
	(in thousands of dollars)			
KeySpan Corporation	**$ -**	$ -	**$ 72,621**	$ 35,323
KeySpan Gas East Corporation	**-**	-	**4,645**	6,005
National Grid Engineering Services	**1,619**	588	**-**	-
National Grid Generation LLC	**147**	-	**-**	-
NGUSA Service Company	**-**	-	**34,320**	17,264
Niagara Mohawk Power Corporation	**-**	180	**469**	-
Other	**2**	25	**3,187**	2,644
Total	**$ 1,768**	$ 793	**$ 115,242**	$ 61,236

Intercompany Money Pool

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

The Regulated and Unregulated Money Pools are funded by operating funds from participants in the applicable pool. Collectively, NGUSA and KeySpan have the ability to borrow up to $3 billion from National Grid plc for working capital needs including funding of the Money Pools, if necessary. The Company had short-term intercompany money pool investments of $451.2 million and a short-term intercompany money pool payable of $394.5 million at March 31, 2016 and 2015, respectively. NETCO had short-term intercompany money pool investments of $129.8 million and $118.1 million at March 31, 2016 and 2015, respectively. The average interest rates for the intercompany money pool were 0.7%, 0.4%, and 0.7% for the years ended March 31, 2016, 2015, and 2014, respectively.

Service Company Charges

The affiliated service companies of NGUSA provide certain services to the Company at their cost. The service company costs are generally allocated to associated companies through a tiered approach. First and foremost, costs are directly charged to the benefited company whenever practicable. Secondly, in cases where direct charging cannot be readily determined, costs are allocated using cost/causation principles linked to the relationship of that type of service, such as number of employees, number of customers/meters, capital expenditures, value of property owned, and total transmission and distribution expenditures. Lastly, when a specific cost/causation principle is not determinable, costs are allocated based on a general allocator determined using a 3-point formula based on net margin, net property, plant and equipment, and operations and maintenance expense.

Net charges from the service companies of NGUSA to the Company for the years ended March 31, 2016, 2015, and 2014 were $374.3 million, $288.8 million, and $243.1 million, respectively.

Holding Company Charges

NGUSA received charges from National Grid Commercial Holdings Limited (an affiliated company in the United Kingdom) for certain corporate and administrative services provided by the corporate functions of National Grid plc to its U.S. subsidiaries. These charges, which are recorded on the books of NGUSA, have not been reflected in these consolidated financial statements. The estimated effect on net income would be $3.7 million, $5.1 million, and $5.4 million before taxes and $2.2 million, $3.1 million, and $3.5 million after taxes, for each of the years ended March 31, 2016, 2015, and 2014, respectively, if these amounts were allocated to the Company.

14. SUBSEQUENT EVENTS

During March 2016, the Company issued Notice of Optional Redemption letters to the bond holders of the fixed interest rate gas facilities revenue bonds. The Company fully repaid these bonds during April 2016.

The following table shows the bonds that have been fully paid subsequent to March 2016:

	Interest Rate	Maturity Date	**March 31, 2016**
Gas Facilities Revenue Bonds:			
1993A and 1993B	6.37%	April 1, 2020	**75,000**
1996	5.50%	January 1, 2021	**153,500**
2005A	4.70%	February 1, 2024	**82,000**
1991A and 1991B	6.95%	July 1, 2026	**100,000**
Total debt			**410,500**