nationalgrid

Massachusetts Electric Company

Financial Statements

For the years ended March 31, 2014 and 2013

MASSACHUSETTS ELECTRIC COMPANY

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Independent Auditor's Report

To the Shareholder and Board of Directors
of Massachusetts Electric Company

We have audited the accompanying financial statements of Massachusetts Electric Company (the Company), which comprise the balance sheets as of March 31, 2014 and 2013, and the related statements of income, comprehensive income, cash flows, capitalization, and changes in shareholder's equity for the years then ended.

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of the 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 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 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 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 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 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 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 financial statements referred to above present fairly, in all material respects, the financial position of Massachusetts Electric Company at March 31, 2014 and 2013, and the results of its operations and its cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

PricewaterhouseCoopers LLP, 300 Madison Avenue, New York, NY 10017
T: (646) 471 3000, F: (646) 471 8320, www.pwc.com/us

Emphasis of Matter

As discussed in Note 2 to the financial statements, the Company has restated its fiscal 2013 financial statements to correct an error. Our opinion is not modified with respect to this matter.

PricewaterhouseCoopers LLP

October 1, 2014

MASSACHUSETTS ELECTRIC COMPANY
STATEMENTS OF INCOME
(in thousands of dollars)

	Years Ended March 31,	
	2014	**2013**
		(Restated)
Operating revenues	**$ 2,352,062**	$ 2,032,553
Operating expenses:		
Purchased electricity	**973,056**	769,487
Operations and maintenance	**1,120,671**	979,718
Depreciation and amortization	**117,425**	112,678
Other taxes	**63,670**	60,491
Total operating expenses	**2,274,822**	1,922,374
Operating income	**77,240**	110,179
Other income and (deductions):		
Interest on long-term debt	**(48,231)**	(48,597)
Other interest, including affiliate interest	**(4,559)**	(2,025)
Storm penalties	**-**	(18,734)
Other income, net	**3,316**	6,307
Total other deductions, net	**(49,474)**	(63,049)
Income before income taxes	**27,766**	47,130
Income tax expense	**11,689**	20,108
Net income	**$ 16,077**	$ 27,022

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

MASSACHUSETTS ELECTRIC COMPANY
STATEMENTS OF COMPREHENSIVE INCOME
(in thousands of dollars)

	Years Ended March 31,	
	2014	**2013**
		(Restated)
Net income	**$ 16,077**	$ 27,022
Other comprehensive income:		
Unrealized gains on securities,		
net of $222 and $184 tax expense	**344**	276
Changes in pension and other postretirement obligations,		
net of $23 and $20 tax expense	**35**	31
Reclassification of gains into net income,		
net of $188 and $91 tax expense	**(291)**	(137)
Total other comprehensive income	**88**	170
Comprehensive income	**$ 16,165**	$ 27,192

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

MASSACHUSETTS ELECTRIC COMPANY
STATEMENTS OF CASH FLOWS
(in thousands of dollars)

	Years Ended March 31,	
	2014	**2013**
		(Restated)
Operating activities:		
Net income	**$ 16,077**	$ 27,022
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	**117,425**	112,678
Provision for deferred income taxes	**17,369**	88,037
Bad debt expense	**35,535**	31,259
Allowance for equity funds used during construction	**(1,571)**	(167)
Amortization of debt discount and issuance costs	**459**	414
Net pension and other postretirement benefit contributions	**(10,775)**	(24,562)
Net environmental remediation payments	**(8,076)**	(6,462)
Changes in operating assets and liabilities:		
Accounts receivable, net, and unbilled revenues	**(107,376)**	(55,689)
Accounts receivable from/payable to affiliates, net	**-**	(5,398)
Inventory	**(24,748)**	(19,790)
Regulatory assets and liabilities, net	**8,588**	(156,131)
Prepaid and accrued taxes	**(4,967)**	(34,744)
Accounts payable and other liabilities	**43,793**	81,324
Other, net	**549**	(3,433)
Net cash provided by operating activities	**82,282**	34,358
Investing activities:		
Capital expenditures	**(188,451)**	(162,932)
Changes in restricted cash	**(11,200)**	-
Affiliated money pool investing and receivables/payables, net	**(221,790)**	-
Cost of removal	**(15,554)**	(9,224)
Other	**(624)**	537
Net cash used in investing activities	**(437,619)**	(171,619)
Financing activities:		
Dividends paid on preferred stock	**(100)**	(100)
Affiliated money pool borrowing and receivables/payables, net	**(231,983)**	136,313
Advance from affiliate	**600,000**	-
Net cash provided by financing activities	**367,917**	136,213
Net increase (decrease) in cash and cash equivalents	**12,580**	(1,048)
Cash and cash equivalents, beginning of year	**1,858**	2,906
Cash and cash equivalents, end of year	**$ 14,438**	$ 1,858
Supplemental disclosures:		
Interest paid	$ (48,712)	$ (54,921)
Income taxes refunded	31,848	15,450
Significant non-cash item:		
Capital-related accruals included in accounts payable	20,672	9,104

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

MASSACHUSETTS ELECTRIC COMPANY
BALANCE SHEETS
(in thousands of dollars)

	March 31,	
	2014	2013 (Restated)
ASSETS		
Current assets:		
Cash and cash equivalents	**$ 14,438**	$ 1,858
Restricted cash and special deposits	**83,091**	71,760
Accounts receivable	**376,613**	299,159
Allowance for doubtful accounts	**(63,884)**	(53,716)
Accounts receivable from affiliates	**23,431**	7,853
Intercompany money pool	**234,354**	-
Unbilled revenues	**91,777**	87,222
Inventory	**62,303**	37,555
Regulatory assets	**162,573**	112,719
Current portion of deferred income tax assets	**-**	20,990
Prepaid taxes	**13,045**	38,769
Other	**859**	514
Total current assets	**998,600**	624,683
Property, plant, and equipment, net	**2,517,850**	2,399,271
Other non-current assets:		
Regulatory assets	**546,669**	665,010
Goodwill	**1,008,244**	1,008,244
Other	**22,486**	21,158
Total other non-current assets	**1,577,399**	1,694,412
Total assets	**$ 5,093,849**	$ 4,718,366

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

MASSACHUSETTS ELECTRIC COMPANY
BALANCE SHEETS
(in thousands of dollars)

	March 31,	
	2014	2013 (Restated)
LIABILITIES AND CAPITALIZATION		
Current liabilities:		
Accounts payable	**$ 217,440**	$ 227,489
Accounts payable to affiliates	**35,995**	77,534
Intercompany money pool	**-**	162,302
Advance from affiliate	**600,000**	-
Current portion of long-term debt	**20,000**	-
Interest accrued	**18,017**	18,005
Regulatory liabilities	**10,396**	39,926
Current portion of deferred income tax liabilities	**13,254**	-
Renewable energy certificate obligations	**122,763**	83,025
Other	**58,869**	32,291
Total current liabilities	**1,096,734**	640,572
Other non-current liabilities:		
Regulatory liabilities	**332,191**	353,159
Deferred income tax liabilities, net	**590,347**	581,470
Postretirement benefits	**111,973**	170,392
Environmental remediation costs	**91,858**	96,230
Other	**38,005**	39,956
Total other non-current liabilities	**1,164,374**	1,241,207
Commitments and contingencies (Note 11)		
Capitalization:		
Shareholder's equity	**2,035,024**	2,018,959
Long-term debt	**797,717**	817,628
Total capitalization	**2,832,741**	2,836,587
Total liabilities and capitalization	**$ 5,093,849**	$ 4,718,366

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

MASSACHUSETTS ELECTRIC COMPANY
STATEMENTS OF CAPITALIZATION
(in thousands of dollars)

			March 31,	
			2014	2013 (Restated)
Total shareholder's equity			**$ 2,035,024**	$ 2,018,959
Long-term debt:	Interest Rate	Maturity Date		
Notes payable - Unsecured senior notes	5.90%	November 15, 2039	**800,000**	800,000
State authority financing - Tax exempt pollution control revenue bonds	Variable	August 1, 2014	**20,000**	20,000
Unamortized discount			**(2,283)**	(2,372)
Total debt			**817,717**	817,628
Current portion of long-term debt			**20,000**	-
Long-term debt			**797,717**	817,628
Total capitalization			**$ 2,832,741**	$ 2,836,587

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

MASSACHUSETTS ELECTRIC COMPANY
STATEMENTS OF CHANGES IN SHAREHOLDER'S EQUITY
(in thousands of dollars)

				Accumulated Other Comprehensive Income (Loss)				
	Common Stock	Cumulative Preferred Stock	Additional Paid-in Capital	Unrealized Gain (Loss) on Available for Sale Securities	Pension and Postretirement Benefits	Total Accumulated Other Comprehensive Income (Loss)	Retained Earnings	Total
Balance as of March 31, 2012 - restated	**$ 59,953**	**$ 2,259**	**$ 1,558,049**	**$ 560**	**$ 4,391**	**$ 4,951**	**$ 366,655**	**$ 1,991,867**
Net income	-	-	-	-	-	-	27,022	27,022
Other comprehensive income (loss):								
Unrealized gains on securities, net of $184 tax expense	-	-	-	276	-	276	-	276
Changes in pension and other postretirement obligations, net of $20 tax expense	-	-	-	-	31	31	-	31
Reclassification of gains into net income, net of $91 tax expense	-	-	-	(137)	-	(137)	-	(137)
Total comprehensive income								27,192
Dividends on preferred stock	-	-	-	-	-	-	(100)	(100)
Balance as of March 31, 2013 - restated	**$ 59,953**	**$ 2,259**	**$ 1,558,049**	**$ 699**	**$ 4,422**	**$ 5,121**	**$ 393,577**	**$ 2,018,959**
Net income	-	-	-	-	-	-	16,077	16,077
Other comprehensive income (loss):								
Unrealized gains on securities, net of $222 tax expense	-	-	-	344	-	344	-	344
Changes in pension and other postretirement obligations, net of $23 tax expense	-	-	-	-	35	35	-	35
Reclassification of gains into net income, net of $188 tax expense	-	-	-	(291)	-	(291)	-	(291)
Total comprehensive income								16,165
Dividends on preferred stock	-	-	-	-	-	-	(100)	(100)
Balance as of March 31, 2014	**$ 59,953**	**$ 2,259**	**$ 1,558,049**	**$ 752**	**$ 4,457**	**$ 5,209**	**$ 409,554**	**$ 2,035,024**

The Company had 2,398,111 shares of common stock authorized, issued and outstanding, with a par value of $25 per share and 22,585 shares of cumulative preferred stock authorized, issued and outstanding, with a par value of $100 per share at March 31, 2014 and 2013.

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

MASSACHUSETTS ELECTRIC COMPANY
NOTES TO THE FINANCIAL STATEMENTS

1. NATURE OF OPERATIONS AND BASIS OF PRESENTATION

Massachusetts Electric Company ("the Company") is an electric retail distribution company providing electric service to approximately 1.3 million customers in 171 cities and towns in Massachusetts. The properties of the Company consist principally of substations and distribution lines interconnected with transmission and other facilities of New England Power Company ("NEP"), an affiliated entity.

The Company is a wholly-owned subsidiary of National Grid USA ("NGUSA" or "Parent"), 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 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.

The accompanying 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 financial statements reflect the ratemaking practices of the applicable regulatory authorities.

The Company has evaluated subsequent events and transactions through October 1, 2014, the date of issuance of these financial statements, and concluded that there were no events or transactions that require adjustment to or disclosure in the financial statements as of and for the year ended March 31, 2014.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Use of Estimates

In preparing 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 financial statements. Actual results could differ from those estimates.

Regulatory Accounting

The Federal Energy Regulatory Commission ("FERC") and the Massachusetts Department of Public Utilities ("DPU") regulate the rates the Company charges its customers. In certain cases, the rate actions of the DPU 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 amortized to the statements of income consistent with the treatment of the related costs in the ratemaking process.

Revenue Recognition

Revenues are recognized for energy service 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.

As approved by the DPU, the Company is allowed to pass through commodity-related costs to customers and also bills for other approved rate adjustment mechanisms. In addition, the Company has a revenue decoupling mechanism ("RDM") which requires the Company to adjust its base rates annually to reflect the over or under recovery of the Company's targeted base distribution revenues from the prior fiscal year.

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 electricity. The Company accounts for taxes that are imposed on customers (such as sales taxes) on a net basis (excluded from revenues).

Income Taxes

Federal income taxes have been computed utilizing the asset and liability approach that requires the recognition of deferred tax assets and liabilities for the tax consequences of temporary differences by applying enacted statutory tax rates applicable to future years to differences between the financial statement carrying amounts and the tax basis of existing assets and liabilities. Deferred income taxes 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 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 company determines its current and deferred taxes based on the separate return method. The Company settles its current tax liability or benefit each year with NGNA pursuant to a tax sharing arrangement between NGNA and its subsidiaries. Tax benefits attributable to the tax attributes of other group companies and allocated by NGNA are treated as capital contributions.

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.

Restricted Cash and Special Deposits

Restricted cash primarily consists of deposits held by ISO New England, Inc. (“ISO-NE”). Special deposits primarily include collateral paid to the Company’s counterparties for outstanding derivative contracts, health insurance and worker’s compensation. The Company had restricted cash of $79.7 million and $68.5 million and special deposits of $3.4 million and $3.3 million at March 31, 2014 and 2013, respectively.

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 and Renewable Energy Certificates ("RECs"). Materials and supplies are stated at the lower of weighted average cost or market value 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, 2014 or 2013. RECs are used to measure compliance with renewable energy standards and are held primarily for consumption.

At March 31, 2014 and 2013 the Company had materials and supplies of $19.4 million and $20.0 million and purchased RECs of $42.9 million and $17.5 million respectively.

Fair Value Measurements

The Company measures derivatives and available-for-sale securities 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 DPU. The average composite rates for each of the years ended March 31, 2014 and 2013 was 3.2%. The average service lives for each of the years ended March 31, 2014 and 2013 was 44 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 of removal recovered in excess of costs incurred of $234.7 million and $219.5 million at March 31, 2014 and 2013, 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 statements of income as non-cash income in other income, 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 $1.6 million and $0.2 million and AFUDC related to debt of $1.3 million and $0.2 million for the years ended March 31, 2014 and 2013, respectively. The average AFUDC rates for the years ended March 31, 2014 and 2013 were 3.4% and 0.9%, respectively.

Goodwill

The Company tests goodwill for impairment annually on January 31, 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, 2014 utilizing both income and market approaches.

- To estimate fair value utilizing the income approach, the Company used a discounted cash flow methodology incorporating its most recent business plan forecasts together with a projected terminal year calculation. Key assumptions used in the income approach were: (a) expected cash flows for the period from April 1, 2014 to March 31, 2019; (b) a discount rate of 5.5%, which was based on the Company's best estimate of its after-tax weighted-average cost of capital; and (c) a terminal growth rate of 2.25%, based on the Company's expected long-term average growth rate in line with estimated long-term U.S. economic inflation.

- To estimate fair value utilizing the market approach, the Company followed a market comparable methodology. Specifically, the Company applied a valuation multiple of earnings before interest, taxes, depreciation and amortization ("EBITDA"), derived from data of publicly-traded benchmark companies, to business operating data. Benchmark companies were selected based on comparability of the underlying business and economics. Key assumptions used in the market approach included the selection of appropriate benchmark companies and the selection of an EBITDA multiple of 10.0, which the Company believes is appropriate based on comparison of its business with the benchmark companies.

The Company determined the fair value of the business using 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, 2014 or 2013.

Available-For-Sale Securities

The Company holds available-for-sale securities that include equities, municipal bonds and corporate bonds. These investments are recorded at fair value and are included in other non-current assets in the accompanying balance sheets. Changes in the fair value of these assets are recorded within other comprehensive income.

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 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,	
	2014	2013
	(in thousands of dollars)	
Balance as of the beginning of the year	**$ 1,596**	$ 1,633
Accretion expense	**77**	77
Liabilities settled	**-**	(114)
Liabilities incurred in the current year	**144**	-
Balance as of the end of the year	**$ 1,817**	$ 1,596

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 subsidiaries in defined benefit pension plans ("Pension Plans") and postretirement benefit other than pension ("PBOP") plans for its employees, administered by NGUSA. The Company recognizes its portion of the Pension Plans' and PBOP plans' funded status in the 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 Plans' and PBOP plan's 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 2014

Presentation of an Unrecognized Tax Benefit When a Net Operating Loss Carryforward, a Similar Tax Loss, or a Tax Credit Carryforward Exists

In July 2013, the FASB issued amendments to address diversity in practice related to the presentation of unrecognized tax benefits in certain situations. The amendments require a liability related to an unrecognized tax benefit to be presented on a net basis with its associated deferred tax asset when utilization of such deferred tax assets is required or expected in the event the uncertain tax position is disallowed. Otherwise, the unrecognized tax benefit will be presented as a liability and will not be netted against deferred tax assets. The Company early adopted this guidance effective April 1, 2013 with no material impact on its financial position, results of operations or cash flows.

Accounting Guidance Not Yet Adopted

Reclassifications From Accumulated Other Comprehensive Income

In February 2013, the FASB issued amendments to improve the reporting of reclassifications out of accumulated other comprehensive income ("AOCI"). The amendments require an entity to provide information either on the face of the financial statements or in a single footnote on significant amounts reclassified out of AOCI and the related income statement line items to the extent an amount is reclassified in its entirety to net income. For significant items not reclassified to net income in their entirety, an entity is required to cross-reference to other disclosures that provide additional information. For non-public entities, the amendments are effective prospectively for reporting periods beginning after December 15, 2013. Early adoption is permitted. The Company will adopt this guidance effective April 1, 2014, which will only impact its disclosures.

Financial Statement Restatement

During the preparation of the fiscal year 2014 financial statements, management determined that certain accounting transactions were not properly recorded in the Company's previously issued financial statements. The Company corrected the accounting by restating the prior period financial statements, the impacts of which are described below.

- Historically, the Company has calculated carrying charges on its storm costs regulatory asset using its weighted average cost of capital ("WACC"). WACC has both a debt and equity component. Accounting standards allow for the capitalization of all or part of an incurred cost that would otherwise be charged to expense if the regulator's actions create probable recovery of those costs through future rates. Because the equity component of a WACC is not an incurred cost that would otherwise be charged to expense, accounting guidance for rate regulated activities does not allow for the capitalization of such equity amounts, and thus, the equity component should not have been included in the Company's storm costs calculation.

  A cumulative adjustment of $7.3 million (net of income taxes) was recorded in the financial statements for the year ended March 31, 2013 of which $2.7 million was recorded as a decrease to opening retained earnings (as of March 31, 2012), and $4.6 million was recorded as a decrease to net income within operations and maintenance expense for the year ended March 31, 2013 to reflect the fiscal year 2013 activity related to this correction. This adjustment also resulted in a decrease of $12.0 million in non-current regulatory assets and a decrease of $4.7 million in deferred income tax liabilities as of March 31, 2013.

- During management's review of the Company's allowance for doubtful accounts methodology, in connection with the preparation of the financial statements, management determined it had insufficiently provided for its allowance for doubtful accounts reserve in prior years. A cumulative adjustment of $11.6 million (net of income taxes) was recorded in the financial statements for the year ended March 31, 2013, of which $8.5 million was recorded as an adjustment to opening retained earnings (as of March 31, 2012), and $3.1 million was recorded as a decrease to net income for the year ended March 31, 2013 to reflect the fiscal year 2013 activity related to this correction.

In addition, the Company has corrected certain other immaterial account balances which were improperly recorded in prior years. A cumulative adjustment of $4.4 million (net of income taxes) was recorded in the financial statements for the year ended March 31, 2013, of which $1.3 million was recorded as an adjustment to opening retained earnings (as of March 31, 2012), and $3.1 million was recorded as an increase to net income for the year ended March 31, 2013 to reflect the fiscal year 2013 activity related to these items.

In connection with these adjustments, the Company recorded an adjustment of $6.7 million to net cash provided by operating activities, an adjustment of $9.5 million to net cash used in investing activities, and an adjustment of $2.9 million to net cash provided by financing activities, all for the year ended March 31, 2013.

The following table shows the amounts previously reported as restated:

	As Previously Reported [i]	Adjustments	As Restated
		(in thousands of dollars)	
	March 2013		March 2013
Statement of Income			
Operating revenues	$ 2,032,180	$ 373	$ 2,032,553
Operating income	115,826	(5,647)	110,179
Other deductions, net	(56,471)	(6,578)	(63,049)
Income before income taxes	59,355	(12,225)	47,130
Income tax expense	27,686	(7,578)	20,108
Net income	31,669	(4,647)	27,022
Statement of Cash Flows			
Net cash provided by operating activities	$ 41,106	$ (6,748)	$ 34,358
Net cash used in investing activities	(181,082)	9,463	(171,619)
Net cash provided by financing activities	139,094	(2,881)	136,213

	As Previously Reported [i]	Adjustments	As Restated
		(in thousands of dollars)	
	March 2013		March 2013
Balance Sheet			
Total current assets	$ 625,782	$ (1,099)	$ 624,683
Property, plant, and equipment, net	2,408,734	(9,463)	2,399,271
Total other non-current assets	1,692,499	1,913	1,694,412
Total assets	4,727,015	(8,649)	4,718,366
Total current liabilities	643,862	(3,290)	640,572
Total other non-current liabilities	1,229,744	11,463	1,241,207
Total liabilities	1,873,606	8,173	1,881,779
Additional Paid-in Capital			
March 31, 2013	1,560,318	(2,269)	1,558,049
March 31, 2012	1,558,551	(502)	1,558,049
Retained Earnings			
March 31, 2013	408,130	(14,553)	393,577
March 31, 2012	376,561	(9,906)	366,655
Total capitalization	2,853,409	(16,822)	2,836,587

(i) Certain reclassifications have been made to the financial statements to conform prior year’s data to the current year’s presentation.

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 balance sheets.

	March 31,	
	2014	2013
	(in thousands of dollars)	
Regulatory assets		
Current:		
Energy efficiency	**$ 23,593**	$ -
Rate adjustment mechanisms	**20,882**	27,383
Renewable energy certificates	**79,633**	65,404
Transmission service	**38,465**	19,932
Total	**162,573**	112,719
Non-current:		
Environmental response costs	**92,415**	98,044
Postretirement benefits	**253,046**	319,231
Smart Grid Program	**19,607**	2,321
Storm costs	**169,561**	236,389
Other	**12,040**	9,025
Total	**546,669**	665,010
Regulatory liabilities		
Current:		
Rate adjustment mechanisms	**7,780**	37,521
Solar Generation Program	**2,616**	2,405
Total	**10,396**	39,926
Non-current:		
Cost of removal	**234,716**	219,514
Environmental response fund	**64,894**	70,001
Postretirement benefits	**24,946**	34,739
Regulatory deferred tax liabilities	**3,971**	23,702
Other	**3,664**	5,203
Total	**332,191**	353,159
Net regulatory assets	**$ 366,655**	$ 384,644

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.

Energy efficiency ("EE"): This amount represents the difference between revenue billed to customers through its EE Charge and the costs of the Company's EE programs as approved by the DPU.

Environmental response costs: This regulatory asset represents deferred costs associated with the Company's share of the estimated costs to investigate and perform certain remediation activities at sites with which it may be associated. The Company's rate plans provide for specific rate allowances for these costs at a level of $4.4 million per year, with variances deferred for future recovery or return to customers. The Company believes future costs, beyond the expiration of current rate plans, will continue to be recovered through rates.

Environmental response fund: This amounts represents the amount of customer contributions and insurance proceeds recovered to pay for costs to investigate and perform certain remediation activities at sites with which it may be associated.

Postretirement benefits: This amount primarily represents the excess costs of the Company's pension and PBOP plans over amounts received in rates that are deferred as a regulatory asset to be recovered in future periods and the non-cash accrual of net actuarial gains and losses.

Rate adjustment mechanisms: The Company is subject to a number of rate adjustment mechanisms, for example RDM, 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 DPU.

Regulatory deferred tax liabilities: This net amount represents over recovered federal and state deferred taxes of the Company primarily as a result of regulatory flowthrough accounting treatment and tax rate changes. The income tax benefits or charges for certain plant related timing differences, such as equity AFUDC, are immediately flowed through to or collected from customers. The amortization of the related regulatory deferred tax asset, for these items, follows the book life of the underlying plant asset. The Company expects to address the recovery period of the net regulatory liability in its next rate case.

Renewable energy certificates: Represents deferred costs associated with the Company's compliance obligation with Massachusetts's Renewable Portfolio Standard ("RPS"). The RPS is legislation established to foster the development of new renewable energy sources. The regulatory asset will be recovered over the next year.

Smart Grid Program: This amount represents the difference between revenue billed to customers and the costs of the Company's Smart Grid Pilot programs as approved by the DPU. The balance will be recovered over the remaining useful life of the pilot program assets.

Storm costs: This regulatory asset represents the incremental costs to restore power to customers resulting from major storms. Additionally, the Company's rate order allows for the operation of a storm fund whereby the Company collects through rates an amount meant to offset incurred storm costs. The Company may use money in the fund for incremental storm costs that exceed a $1.25 million threshold per event, subject to the Department reviewing the costs and determining that they have been reasonably and prudently incurred. The regulatory asset recorded represents the excess of incremental operation and maintenance costs which have been incurred by the Company to restore power to customers resulting from major storms above the amount collected in the storm fund.

Solar Generation Program: This represents the recovery of the final cost and annual revenue requirement for approximately five megawatts of solar generation at five separate sites: Haverhill, Everette, Revere, Whitinsville and Dorchester Solar Generation facilities, which the company constructed, owns, and operates. Actual capital and incremental operations and maintenance costs, as approved is recovered from its retail delivery service customers through the fully-reconciling per kilowatt-hour solar cost adjustment factor as provided in the Company's solar cost adjustment provision tariff.

Transmission service: The Company arranges transmission service on behalf of its customers' and bills the costs of those services to customers pursuant to the Company's Transmission Service Cost Adjustment Provision. Any over or under recoveries of these costs are passed on to customers receiving transmission service through the Company over the subsequent twelve months.

The Company records carrying charges on regulatory balances related to rate adjustment mechanisms, storm costs, environmental response costs, postretirement benefits, and renewable energy certificates 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

2009 Capital Investments Audit

Rates for services rendered by the Company are subject to approval by the DPU. The DPU approved an RDM arising from the 2009 distribution rate case filed by the Company and its affiliate, Nantucket Electric Company ("Nantucket Electric"). As part of its RDM provision, the Company files a report by July 1st of each year on its capital investment for the prior calendar year. In connection with the Company's first capital expenditure ("CapEx") filing made in July 2010, the DPU opened a proceeding in March 2011, as requested by the Massachusetts Attorney General's Office ("Attorney General"), for an independent audit of the Company's 2009 capital investments which, in part, formed the basis for the Company's RDM rate adjustment. On July 31, 2014, the DPU issued an order approving the sole bidder's bid to perform the CapEx audit. As required by the Order, National Grid has conferred with the Attorney General and the auditor, and on August 21, 2014 National Grid submitted a revised work plan and final contract for the audit to the DPU. After a comment period the DPU will issue a final order on the revised work plan and contract, which will determine the next steps for the audit. The Company cannot currently predict the outcome of this proceeding.

Cost Recovery

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

DPU Audit Settlement Agreement

In the general rate case involving the Company's Massachusetts gas distribution affiliates, the DPU opened an investigation to address the allocation and assignment of costs to the gas affiliates by the National Grid service companies. The audit was later expanded to include the Company's Massachusetts electric distribution affiliates. The Company and the Attorney General's Office executed a Settlement Agreement that the DPU approved on July 25, 2014. As a result of the approval of the Settlement, there is no need for an audit, the Company will implement reporting and review practices similar to those in place for its New York affiliates, and NGUSA contributed $1 million to the Massachusetts Association for Community Action that will be used for the benefit of Company's electric customers and customers of its Massachusetts gas distribution affiliates who are eligible for fuel assistance.

Storm Management Audit

In January 2011, the DPU opened an investigation into the Company and Nantucket Electric's preparation and response to a December 2010 winter storm. The DPU has the authority to issue fines not to exceed approximately $0.3 million for each violation for each day that the violation persists. On September 22, 2011, the DPU approved a settlement between the Company and the Attorney General that included a $1.2 million refund to customers. The DPU also investigated the Company and Nantucket Electric's response to Tropical Storm Irene and the October 2011 winter storm in a consolidated proceeding. On December 11, 2012, the DPU issued an order in which it assessed the Company and Nantucket Electric a penalty of $18.7 million associated with the Company and Nantucket Electric's performance in responding to these two weather events, consisting of $8.1 million for Tropical Storm Irene and $10.6 million for the October 2011 winter storm. The Company and Nantucket Electric appealed this ruling and on September 4, 2014 the Court affirmed all but two violations, reducing the penalty by $0.9 million. The Company had recorded the original penalty and credited customers during March 2013. In addition, in the December 11, 2012 order, the DPU ordered a management audit of the Company and Nantucket Electric's emergency planning, outage management, and restoration. The auditors have completed their audit, and submitted their Final Report to the DPU on July 9, 2014. No parties submitted comments on the Final Report. The Company cannot predict the outcome of the management audit.

2010 Service Quality Report

On December 30, 2013, the DPU issued an order on Massachusetts Electric's calendar year 2010 Service Quality Report, ordering that the Company refund to customers a net penalty of $6.7 million. On January 21, 2014, the Company filed a Motion for Clarification/Reconsideration regarding a portion of the penalty amount related to Circuit Average Interruption Frequency Index which totaled $2.7 million. In addition, the Company filed a proposal to credit customers the $6.7 million penalty along with a proposed tariff that would allow for recovery of the $2.7 million if the DPU rules in favor of the Company regarding the Motion for Clarification/Reconsideration. On May 21, 2014, the DPU denied the Company's motion.

5. PROPERTY, PLANT AND EQUIPMENT

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

	March 31,	
	2014	2013
	(in thousands of dollars)	
Plant and machinery	**$ 3,591,604**	$ 3,438,586
Land and buildings	**187,091**	169,739
Assets in construction	**107,758**	74,937
Property held for future use	**562**	562
Total property, plant and equipment	**3,887,015**	3,683,824
Accumulated depreciation and amortization	**(1,369,165)**	(1,284,553)
Property, plant and equipment, net	**$ 2,517,850**	$ 2,399,271

6. FAIR VALUE MEASUREMENTS

The following table presents available-for-sale securities measured and recorded at fair value in the accompanying balance sheets on a recurring basis and their level within the fair value hierarchy as of March 31, 2014 and 2013:

	March 31, 2014			
	Level 1	**Level 2**	**Level 3**	**Total**
	(in thousands of dollars)			
Assets:				
Available-for-sale securities	2,796	3,851	-	6,647

	March 31, 2013			
	Level 1	**Level 2**	**Level 3**	**Total**
	(in thousands of dollars)			
Assets:				
Available-for-sale securities	2,584	3,491	-	6,075

Available-for-sale securities are included in other non-current assets in the accompanying balance sheets and primarily include equity and debt investments based on quoted market prices (Level 1) and municipal and corporate bonds based on quoted prices of similar traded assets in open markets (Level 2).

Other Fair Value Measurements

The Company's 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, where available or estimated using quoted market prices for similar debt. The fair value of this debt at March 31, 2014 and 2013 was $1 billion.

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

7. EMPLOYEE BENEFITS

The Company participates with other NGUSA subsidiaries in a qualified and non-qualified non-contributory defined benefit plan (the "Pension Plan") and PBOP plan (together with the Pension Plan (the "Plan")), covering substantially all employees.

The Pension Plan is a defined benefit plan which provides union employees, as well as non-union employees hired before January 1, 2011, with a retirement benefit. Supplemental nonqualified, non-contributory executive retirement programs provide additional defined pension benefits for certain executives. 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, 2014 and 2013, the Company made contributions of approximately $31.4 million and $59.4 million, respectively, to the Plan.

Plan assets are commingled and cannot be allocated to an individual company. The Plan's costs are first directly charged to the Company based on the Company's employees that participate in the Plan. Costs associated with affiliated service companies' employees are then allocated as part of the labor burden for work performed on the Company's behalf. The Company applies deferral accounting for pension and PBOP expenses associated with its regulated electric operations. Any differences between actual pension costs and amounts used to establish rates are deferred and collected from or refunded to customers in subsequent periods. Pension and PBOP expense is included in operations and maintenance expense in the accompanying statements of income.

The NGUSA companies' pension and PBOP plans that the Company participates in have unfunded obligations at March 31, 2014 and 2013 as follows:

	March 31,	
	2014	2013
	(in thousands of dollars)	
Pension	**$ 402,928**	$ 471,000
PBOP	**302,360**	368,100
	$ 705,288	$ 839,100

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, 2014 and 2013 are as follows:

	March 31,			
	2014		2013	
	(in thousands of dollars)			
Pension	**$**	**25,492**	$	27,454
PBOP		**8,758**		14,732
	$	**34,250**	$	42,186

Defined Contribution Plan

NGUSA has a defined contribution pension plan that covers substantially all employees. For the years ended March 31, 2014 and 2013, the Company recognized an expense in the accompanying statements of income of $3.4 million and $3.2 million, respectively, for matching contributions.

Other Benefits

During the year ended March 31, 2014, NGUSA improved its methodology for allocating to its subsidiaries the expense and liability for workers compensation, auto, and general insurance claims which have been incurred but not yet reported ("IBNR"). In prior years, such costs and liabilities were allocated to NGUSA's subsidiaries based on each subsidiary's pro-rata share of known outstanding case reserves. As of and for the year ended March 31, 2014, such IBNR amounts are allocated proportionally based on various factors including revenue, payroll, and number of fleet vehicles, as applicable to the related exposure source. Management believes this improved methodology provides a more accurate and appropriate allocation to each of its subsidiaries. The change in allocation methodology resulted in a decrease in income before taxes of approximately $3.6 million in the current fiscal year. At March 31, 2014 and 2013, the Company had accrued IBNR of $4.4 million and $5.7 million respectively.

8. CAPITALIZATION

Debt Authorizations

The Company had regulatory approval from the FERC to issue up to $750 million of short-term debt, which expired on November 30, 2013. Effective April 2014, the Company entered into an Equity Contribution Agreement with the Parent which provides the Company with the ability to call upon the Parent for contributions to the Company's capital, in an aggregate amount equal to the short-term borrowing limit until such time as regulatory approval for short-term borrowing is regained. The Company has not made use of this facility since its effective date. The Company had no short-term debt outstanding to third parties as of March 31, 2014 or 2013.

Pollution Control Revenue Bonds

In 2004, the Company issued $20 million of Pollution Control Revenue Bonds in tax exempt commercial paper mode maturing on August 1, 2014. The debt had variable interest rates ranging from 0.32% to 0.40% and from 0.35% to 0.90% in each of the years ended March 31, 2014 and 2013.

The Company has a Standby Bond Purchase Agreement ("SBPA") of $20 million which expires on November 20, 2015. This agreement was available to provide liquidity support for the Company's Pollution Control Revenue Bonds. At March 31, 2014 and 2013, there were no bond purchases made by the banks participating in this agreement.

Senior Note

In November 2009, the Company issued $800 million of unsecured long-term debt at 5.9% with a maturity date of November 15, 2039. In conjunction with this debt issuance, the Company incurred debt issuance costs of $6.8 million which are being amortized over the life of the debt.

Current Maturities of Long-term Debt

(in thousands of dollars)	
Years Ending March 31,	
2015	$ 20,000
2016	-
2017	-
2018	-
2019	-
Thereafter	800,000
Total	$ 820,000

The Company is obligated to meet certain financial and non-financial covenants. During the years ended March 31, 2014 and 2013, the Company was in compliance with all such covenants.

Dividend Restrictions

Pursuant to the preferred stock arrangement, as long as any preferred stock is outstanding, certain restrictions on payment of common stock dividends would come into effect if the common stock equity was, or by reason of payment of such dividends became, less than 25% of total capitalization. Common stock equity at March 31, 2014 and 2013 was approximately 71.9% and 71.2%, respectively, of total capitalization. Accordingly, the Company was not restricted as to the payment of common stock dividends under the foregoing provisions at March 31, 2014 or 2013.

Cumulative Preferred Stock

The Company has non-participating cumulative preferred stock outstanding which can be redeemed at the option of the Company. There are no mandatory redemption provisions on the Company's cumulative preferred stock. A summary of cumulative preferred stock is as follows:

	Shares Outstanding		**Amount**		
	March 31,		**March 31,**		Call
Series	**2014**	2013	**2014**	2013	Price
	(in thousands of dollars, except per share and number of shares data)				
$100 par value - 4.44% Series	**22,585**	22,585	**$ 2,259**	$ 2,259	$ 104.068

The Company did not redeem any preferred stock during the years ended March 31, 2014 or 2013. The annual dividend requirement for cumulative preferred stock was $0.1 million for the years ended March 31, 2014 and 2013.

9. INCOME TAXES

The components of federal and state income tax expense for the years ended March 31, 2014 and 2013 are as follows:

	Years Ended March 31,	
	2014	2013
	(in thousands of dollars)	
Current tax expense (benefit):		
Federal	**$ (8,824)**	$ (64,303)
State	**3,144**	(3,626)
Total current tax benefit	**(5,680)**	(67,929)
Deferred tax expense:		
Federal	**15,857**	79,590
State	**2,320**	9,332
Total deferred tax expense	**18,177**	88,922
Amortized investment tax credits [1]	**(808)**	(885)
Total deferred tax expense	**17,369**	88,037
Total income tax expense	**$ 11,689**	$ 20,108

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

The Company's effective tax rate for the years ended March 31, 2014 and 2013 is 42% and 43%, respectively. A reconciliation between the expected federal income tax expense, using the federal statutory rate of 35%, to the Company's actual income tax expense for the years ended March 31, 2014 and March 31, 2013 is as follows:

	Years Ended March 31,	
	2014	2013
	(in thousands of dollars)	
Computed tax	**$ 9,718**	$ 16,496
Change in computed taxes resulting from:		
State income tax, net of federal benefit	**3,551**	3,709
Allowance for equity funds used during construction	**(507)**	(37)
Investment tax credit	**(808)**	(885)
Adjustments related to prior year, federal and state	**-**	692
Other items, net	**(265)**	133
Total	**1,971**	3,612
Federal and state income taxes	**$ 11,689**	$ 20,108

The Company is a member of the NGNA and subsidiaries consolidated federal income tax return. The Company has joint and several liability for any potential assessments against the consolidated group.

In September 2013, the IRS issued final regulations, effective for tax years beginning in 2014, that provide guidance on the appropriate tax treatment of costs incurred to acquire, produce or improve tangible property, as well as routine maintenance and repair costs. Proposed regulations were issued addressing the tax treatment of asset dispositions. The Company has evaluated tax accounting method changes that may be elected or required by the final regulations. At March 31, 2014, $10 million of deferred tax liabilities have been classified as current in the Company's balance sheets, representing the cumulative adjustment expected to be reflected in income for tax purposes during the twelve months ending March 31, 2015. The application of these regulations is not expected to have a material impact on the Company's financial position, results of operations or cash flow.

On July 24, 2013, Massachusetts legislature enacted into law transportation finance legislation which included significant tax changes affecting the classification of utility corporations. For tax years beginning on or after January 1, 2014, Massachusetts utility corporations will be taxed in the same manner as general business corporations. The state income tax rate will increase from 6.5% to 8.0%. Also, any unitary net operating loss generated post-2013 and allocated to the utilities will be allowed as a carry forward tax attribute. As of March 31, 2014, all state deferred tax balances at the regulated utilities were remeasured to the 8% rate, resulting in an increase in deferred tax liabilities of $18.7 million with an offset to regulatory deferred tax asset. The application of this legislation is not expected to have a material impact on the Company's financial position, results of operations or cash flows.

Significant components of the Company's net deferred tax assets and liabilities at March 31, 2014 and 2013 are as follows:

	March 31,	
	2014	2013
	(in thousands of dollars)	
Deferred tax assets:		
Pensions, PBOP and other employee benefits	**$ 59,354**	$ 78,740
Reserve - environmental	**41,319**	42,140
Future federal benefit on state taxes	**34,338**	27,424
Regulatory assets/ liabilities - other	**-**	72,471
Allowance for uncollectible accounts	**27,470**	22,292
Net operating losses	**24,678**	22,145
Other items	**52,055**	-
Total deferred tax assets [1]	**239,214**	265,212
Deferred tax liabilities:		
Property related differences	**572,114**	536,454
Regulatory assets - pension and PBOP	**100,467**	113,006
Regulatory assets - storm costs	**87,483**	104,893
Regulatory assets - other	**74,051**	43,764
Other items	**-**	18,403
Total deferred tax liabilities	**834,115**	816,520
Net deferred income tax liabilities	**594,901**	551,308
Deferred investment tax credits	**8,700**	9,172
Net deferred income tax liability and investment tax credits	**603,601**	560,480
Current portion of deferred income tax (liabilities) asset	**(13,254)**	20,990
Deferred income tax liabilities	**$ 590,347**	$ 581,470

(1) There were no valuation allowances for deferred tax assets at March 31, 2014 or 2013.

The following table presents the amounts and expiration dates of operating losses as of March 31, 2014:

Expiration of net operating losses:	Federal	
	(in thousands of dollars)	
03/31/2029	$	59,503
03/31/2030		6,769
03/31/2032		17,897
03/31/2033		63,272
03/31/2034		24,278

Unrecognized Tax Benefits

As of March 31, 2014 and 2013, the Company's unrecognized tax benefits totaled $45.7 million and $37.9 million, respectively, none of which would affect the effective tax rate, if recognized. The unrecognized tax benefits are included in other deferred liabilities in the accompanying balance sheets.

The following table reconciles the changes to the Company's unrecognized tax benefits for the years ended March 31, 2014 and 2013:

	Years Ended March 31,			
	2014		2013	
	(in thousands of dollars)			
Balance as of the beginning of the year	**$**	**37,877**	$	50,108
Gross increases related to prior period		**11,147**		359
Gross decreases related to prior period		**(4,279)**		(12,100)
Gross increases related to current period		**959**		1,111
Gross decreases related to current period		**-**		(1,601)
Balance as of the end of the year	**$**	**45,704**	$	37,877

As of March 31, 2014 and March 31, 2013, the Company has accrued for interest related to unrecognized tax benefits of $0.5 million and $1.3 million, respectively. During years ended March 31, 2014 and March 31, 2013, the Company recorded interest income of $0.8 million and $0.5 million, respectively. The Company recognizes accrued interest related to unrecognized tax benefits in other interest, including affiliate interest in the accompanying statement of income. Related penalties, if applicable, are recorded to other income (deductions). No penalties were recognized during the years ended March 31, 2014 and March 31, 2013.

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, the Company does not believe any such increases or decreases would be material to their results of operations, financial position, or cash flows.

Federal income tax returns have been examined and all appeals and issues have been agreed with the Internal Revenue Service (IRS) and the NGNA consolidated filing group through March 31, 2007.

During fiscal year 2014 the IRS has concluded its examination of the NGNA consolidated filing group's corporate income tax returns for the periods ended March 31, 2008 and March 31, 2009. The examinations were completed on March 31, 2014, with an agreement on the majority of income tax issues for the years referenced above, as well as an acknowledgment that certain discrete items remain disputed. NGNA is in the process of appealing these disputed items with the IRS Office of Appeals. The Company does not anticipate a change in its unrecognized tax positions in the next twelve months as a result

of the appeals. However, pursuant to the Company's tax sharing agreement, the audit or appeals may result in a change to allocated tax. Fiscal years ended March 31, 2010 through March 31, 2014 remain subject to examination by the IRS.

The Company is a member of the NGUSA Service Company Massachusetts unitary group since fiscal year ended March 31, 2010. The tax returns for the fiscal years ended March 31, 2010 through March 31, 2014 remain subject to examination by the State of Massachusetts.

The following table indicates the earliest tax year subject to examination:

Jurisdiction	Tax Year
Federal	March 31, 2008 *
Massachusetts	March 31, 2010

*The NGNA consolidated filing group is in the process of appealing certain disputed issues with the IRS Office of Appeals for the fiscal years ended March 31, 2008 through March 31, 2009.

10. 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.

The United States Environmental Protection Agency (“EPA”) and the Massachusetts Department of Environmental Protection (“DEP”), as well as private entities, have alleged that the Company is a potentially responsible party under state or federal law for a number of sites at which hazardous waste is alleged to have been disposed. The Company’s most significant liabilities relate to former Manufactured Gas Plant (“MGP”) facilities. The Company is currently investigating and remediating, as necessary, those MGP sites and certain other properties under agreements with the EPA and DEP. Expenditures incurred for the years ended March 31, 2014 and 2013 were $8.1 million and $6.8 million, respectively.

At March 31, 2014 and 2013, the Company had total reserves for environmental remediation costs of $91.9 million and $96.2 million, respectively, which include reserves established in connection with the Company’s hazardous waste fund referred to below. These costs are expected to be incurred over the next 34 years. However, remediation costs for each site may be materially higher than estimated, depending upon 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.

The DPU has approved a settlement agreement that provides for rate recovery of remediation costs of former MGP sites and certain other hazardous waste sites located in Massachusetts. Under that agreement, qualified costs related to these sites are paid out of a special fund established as a regulatory liability in the accompanying balance sheets. Rate-recoverable contributions of approximately $4.0 million are made along with interest, lease payments, and any recoveries from insurance carriers and other third-parties. Accordingly, as of March 31, 2014 and 2013, the Company has recorded environmental regulatory assets of $92.4 million and $98.0 million, respectively, and environmental regulatory liabilities of $64.9 million and $70.0 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.

11. COMMITMENTS AND CONTINGENCIES

The Company has several long-term contracts for the purchase of electric power. The Company is liable for these payments regardless of the level of service required from third-parties. The Company also 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, 2014 are summarized in the table below:

(in thousands of dollars) Years Ending March 31,	Energy Purchases	Capital Expenditures
2015	$ 689,192	$ 75,925
2016	25,068	-
2017	-	1,248
2018	-	-
2019	-	-
Thereafter	-	-
Total	$ 714,260	$ 77,173

The Company purchases additional energy to meet load requirements from independent power producers, other utilities, energy merchants or the ISO-NE at market prices.

Guarantees

The Company unconditionally guarantees the full and prompt payment of the principal, premium, if any, and interest on certain tax exempt bonds issued by the Massachusetts Development Finance Agency in connection with Nantucket Electric's financing of its first and second underground and submarine cable projects. The Company would be required to make any principal, interest or premium payments if Nantucket Electric failed to pay. The carrying value of the debt guaranteed is approximately $52 million at March 31, 2014 and has maturities extending through 2042. This guarantee is absolute and unconditional.

Legal Matters

The Company is subject to various legal proceedings, primarily injury claims, 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.

12. RELATED PARTY TRANSACTIONS

Advance from Affiliate

The Company has an agreement with NGUSA whereby the Company can borrow up to $600 million from time to time for working capital needs. The advance is non-interest bearing. At March 31, 2014 and 2013, the Company had an outstanding advance from affiliate of $600 million and zero, respectively.

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 payables to and receivables from certain of its affiliates in the ordinary course of business. The amounts payable to and receivable from 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 balances is as follows:

	Accounts Receivable from Affiliates		Accounts Payable to Affiliates	
	March 31,		March 31,	
	2014	2013	**2014**	2013
	(in thousands of dollars)		*(in thousands of dollars)*	
New England Power Company	**$ -**	$ -	**$ 6,889**	$ 27,610
NGUSA Service Company	**-**	-	**23,313**	43,991
National Grid Engineering Services, LLC	**2,817**	349	**-**	-
Nantucket Electric	**8,380**	-	**-**	1,685
Niagara Mohawk Power Corporation	**-**	-	**4,653**	3,833
The Narragansett Electric Company	**7,221**	1,786		-
Metrowest Realty	**1,418**	1,451		-
Boston Gas Company	**1,552**	2,905	**-**	-
Colonial Gas Company	**510**	623	**-**	-
Other	**1,533**	739	**1,140**	415
Total	**$ 23,431**	$ 7,853	**$ 35,995**	$ 77,534

Recovery of Transmission Costs

NEP operates the transmission facilities of its New England affiliates as a single integrated system and reimburses the Company for the cost of its transmission facilities in Rhode Island, including a return on those facilities under NEP's Tariff No. 1. In turn, these costs are allocated among transmission customers in New England in accordance with the ISO New England transmission tariff. The Company is compensated for its actual monthly transmission costs with its authorized ROE ranging from 11.14% to 12.64%. The amounts reimbursed to the Company by NEP for the years ended March 31, 2014 and 2013 were $16.6 million and $10.3 million, respectively, which are included within operations and maintenance expense in the accompanying statements of income.

Intercompany Money Pool

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

The Regulated Money Pool is funded by operating funds from participants. Collectively, NGUSA, and its subsidiary, KeySpan, have the ability to borrow up to $3 billion from National Grid plc for working capital needs including funding of the intercompany money pools, if necessary. The Company had short-term intercompany money pool investments of $234.4 million and borrowings of $162.3 million at March 31, 2014 and 2013, respectively. The average interest rates for the intercompany money pool were 0.7% and 0.6% for the years ended March 31, 2014 and 2013, respectively.

Related Party Reimbursement

In accordance with the Credit and Operating Support Agreement dated March 26, 1996, the Company will reimburse Nantucket Electric an amount equal to the difference between Nantucket Electric's actual net income for the year and the net income necessary for Nantucket Electric to earn an ROE equivalent to Nantucket Electric's DPU approved ROE for the fiscal year, currently 10.35%. This reimbursement shall constitute additional revenue to Nantucket Electric and expense to the Company. To the extent Nantucket Electric's actual ROE for the year exceeds its allowed ROE, there will be no reimbursement. For the years ended March 31, 2014 and 2013, the Company reimbursed Nantucket Electric $5.8 million and $3.3 million, respectively.

Service Company Charges

The affiliated service companies of NGUSA provide certain services to the Company at their cost. The service company costs are generally allocated to associated companies through a tiered approach. First and foremost, costs are directly charged to the benefited company whenever practicable. Secondly, in cases where direct charging cannot be readily determined, costs are 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, total transmission and distribution expenditures. Lastly, all other 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, 2014 and 2013 were $305.2 million and $317.2 million, respectively.

Holding Company Charges

NGUSA received charges from National Grid Commercial Holdings Limited (an affiliated company in the U.K.) 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 on these financial statements. Were these amounts allocated to the Company, the estimated effect on net income would be $8.7 million and $5.3 million before taxes, and $5.2 million and $3.4 million after taxes, for each of the years ended March 31, 2014 and 2013.