

133 FERC ¶ 61,241  
UNITED STATES OF AMERICA  
FEDERAL ENERGY REGULATORY COMMISSION

Before Commissioners: Jon Wellinghoff, Chairman;  
Marc Spitzer, Philip D. Moeller,  
and John R. Norris.

National Grid USA

Docket No. EL09-24-000

ORDER GRANTING WAIVER OF AFFILIATE PRICING RULES  
UNDER ORDER NOS. 707 AND 707-A

(Issued December 20, 2010)

1. National Grid USA (National Grid) filed an application and two amendments<sup>1</sup> seeking waiver of certain affiliate pricing rules as established under Order Nos. 707 and 707-A.<sup>2</sup> Specifically, National Grid requests waivers of sections 35.44(b)(1) and (b)(2) of the Commission's regulations<sup>3</sup> so that it may use cost-based pricing for a limited set of transactions involving the provision of goods and services between public utilities and non-utility affiliates in National Grid's holding company system. These transactions include: (1) the provision of services by employees of a public utility to a centralized service company at cost in instances where such employees cannot be transferred to the centralized service company because of union contract restrictions; (2) at-cost pricing for certain services provided under a Mutual Assistance Agreement executed among public utility and non-utility affiliates in the National Grid holding company system; and (3) at-cost pricing for the transfer of certain goods and equipment from public utilities to a centralized service company to implement and expand a centralized inventory management program. In this order we grant the requested waivers, as discussed below.

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<sup>1</sup> National Grid's initial filing was made on December 17, 2008. An amended application was filed on May 19, 2010 (Amended Application). A supplemental filing was made on October 15, 2010 (Supplemental Filing).

<sup>2</sup> *Cross-Subsidization Restrictions on Affiliate Transactions*, Order No. 707, FERC Stats. & Regs. ¶ 31,264, *order on reh'g*, Order No. 707-A, FERC Stats. & Regs. ¶ 31,272 (2008).

<sup>3</sup> 18 C.F.R. § 35.44(b)(1)-(2) (2010).

## **I. Background**

### **A. Description of National Grid**

2. National Grid is a public utility holding company. It acquired New England Electric System in 1999, Niagara Mohawk Power Company (Niagara Mohawk) in 2002, and KeySpan Corporation (KeySpan) in 2007. As a result of these transactions, National Grid currently has five wholly-owned subsidiaries that are franchised public utilities providing electric service. They are Granite State Electric Company (Granite State), Massachusetts Electric Company (Massachusetts Electric), Nantucket Electric Company (Nantucket Electric), The Narragansett Electric Company (Narragansett Electric), and Niagara Mohawk. National Grid states that all of these companies operate in states that have adopted retail access regimes, and their only obligation to sell power at retail is as a provider of last resort. National Grid further states that none of these companies has wholesale power customers.

3. Four of National Grid's five franchised public utility subsidiaries own or provide transmission service over Commission-jurisdictional facilities. They are: Massachusetts Electric, Narragansett Electric, Granite State, and Niagara Mohawk. The transmission facilities that Massachusetts Electric, Narragansett Electric, and Granite State own are operated by the New England Power Company under Commission-approved integrated facilities agreements.

4. All of Niagara Mohawk's bulk transmission facilities are subject to the operational control of the New York Independent System Operator, Inc. Nantucket Electric does not own any electric transmission facilities that are subject to Commission jurisdiction.

5. National Grid also owns three wholesale generation subsidiaries: National Grid Generation LLC, National Grid Glenwood Energy Center LLC, and National Grid Port Jefferson Energy Center LLC. These public utility subsidiaries are located on Long Island, New York, and their energy and capacity are wholly committed to the Long Island Power Authority (LIPA), a state authority. None of these entities has a franchised service obligation under state law.

6. National Grid's remaining public utility subsidiaries are transmission-only subsidiaries that own or operate Commission jurisdictional transmission facilities. These are: New England Electric Transmission Corporation, New England Hydro-Transmission Corporation, and New England Hydro-Transmission Electric Company, Inc. None of these entities has a franchised service obligation under state law.

7. National Grid has four non-utility subsidiaries that are centralized service companies: National Grid USA Service Company, Inc. (ServCo), National Grid Corporate Services, LLC (Corporate Services), National Grid Engineering & Survey Inc.

(Engineering & Survey), and National Grid Utility Services LLC (Utility Services). National Grid states that these entities are “non-utility affiliates” as the Commission defines them for purposes of its affiliate pricing rules. As centralized service companies, these entities provide their services to National Grid affiliates at cost.

8. ServCo and Corporate Services provide general administrative services and related goods and other non-power goods and services to companies in the National Grid holding company system. Most of the personnel providing these services are employed directly by ServCo or Corporate Services. National Grid states that the remaining employees providing these services are employees of Niagara Mohawk who cannot be transferred to, and become employees of, the centralized service company due to restrictions in Niagara Mohawk’s union contract.

9. Engineering & Survey performs the following functions: (1) assisting National Grid’s subsidiaries in the study, planning, engineering, maintenance, and construction of energy plant facilities, gas systems, and electric systems; (2) advising, assisting and managing the planning, engineering (including maps and records) and construction operations of National Grid affiliates; (3) developing and administering quality assurance programs; and (4) developing long-range operational programs and advising and assisting the coordination of these programs. Engineering & Survey also provides surveying services to National Grid’s affiliates and to LIPA under a Management Services Agreement.

10. Utility Services provides services only to regulated National Grid affiliates, including gas and electric transmission and distribution system planning, gas supply planning and procurement, marketing services, research and development service, and meter repair operations. Utility Services does not provide services to any non-affiliated third party.

11. National Grid Electric Services, LLC (Electric Services) is a non-utility affiliate that provides transmission and distribution operations services to LIPA under the terms of an amended and restated management services agreement, dated as of January 1, 2006, as amended December 22, 2009 (Management Services Agreement). The State of New York established LIPA under the New York Public Authorities Law to acquire the transmission and distribution assets of Long Island Lighting Company, which merged with the Brooklyn Union Gas Company to form what eventually became National Grid’s subsidiary, KeySpan. The transmission and distribution employees that operated the assets acquired by LIPA remained with KeySpan, and manage LIPA’s assets on behalf of Electric Services under the Management Services Agreement. Electric Services provides day-to-day utility operations and maintenance and construction management services to

LIPA under the pricing terms of the Management Services Agreement. To the extent that Electric Services receives any services from National Grid's regulated subsidiaries, those services are provided directly to Electric Services, and thus to LIPA, at cost, under the Management Services Agreement.

## **B. Waiver Requests**

12. The Commission's pricing rules for affiliate transactions provide that "unless otherwise permitted by Commission rule or order," the transfer or sale of non-power goods or services to a non-utility affiliate from a franchised utility that owns or provides transmission service over jurisdictional transmission facilities "must be at the higher of cost or market price."<sup>4</sup> Also, the Commission's pricing rules provide that "unless otherwise permitted by Commission rule or order," the purchase of non-power goods or services by a franchised utility that owns or provides transmission service over jurisdictional facilities from a non-utility affiliate may not be "at a price above market."<sup>5</sup>

13. The Commission has stated that "[a] public utility with no captive customers but that owns or provides transmission service over Commission-jurisdictional facilities may seek a waiver of the affiliate restrictions if it can demonstrate that transmission customers are adequately protected against inappropriate cross-subsidization."<sup>6</sup> To be granted such a waiver, "the public utility would need to demonstrate that the transmission customers of a franchised public utility that does not have captive customers do not bear the costs of inappropriate cross-subsidization."<sup>7</sup>

14. National Grid states that the centralized service companies provide the overwhelming majority of non-power goods and services within its system, and these transactions are priced at cost, consistent with the Commission's affiliate pricing rules.<sup>8</sup> National Grid further states that none of its public utility subsidiaries have captive customers.<sup>9</sup> Additionally, for the reasons set forth below, National Grid believes that its public utility subsidiaries' transmission customers are adequately protected against inappropriate cross-subsidization, and do not otherwise bear the cost of any inappropriate cross-subsidization as a result of the transactions that are the subject of its application. National Grid seeks waivers for a limited set of transactions that fall into three classes

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<sup>4</sup> 18 C.F.R. § 35.44(b)(1) (2010).

<sup>5</sup> 18 C.F.R. § 35.44(b)(2) (2010).

<sup>6</sup> Order No. 707, FERC Stats. & Regs. ¶ 31,264 at n.46.

<sup>7</sup> Order No. 707-A, FERC Stats. & Regs. ¶ 31,272 at P 69.

<sup>8</sup> Amended Application at 11.

<sup>9</sup> *Id.* at 2-3.

and do not fit neatly into the Commission's rules for transactions between public utility and non-utility affiliates, including centralized service companies. A diagram depicting these transactions is attached to this order as Appendix 1.

**1. Utility Providing Services to Non-Utility Affiliates At Cost**

15. The first class of transactions for which National Grid seeks waiver involves the at-cost allocation of Niagara Mohawk union employees performing centralized service company functions for ServCo, one of National Grid's service companies. National Grid seeks waiver of the requirements of section 35.44(b)(1) of the Commission's regulations for these transactions.<sup>10</sup>

16. National Grid states that when Niagara Mohawk became part of its holding company system in 2002, National Grid sought to centralize in ServCo general and administrative services like those previously provided by Niagara Mohawk personnel. However, the union agreement covering Niagara Mohawk employees performing accounts payable, information services, and other administrative functions prohibited their transfer to ServCo. National Grid states that to comply with the union contract restrictions and still realize the efficiencies of a centralized service company, these union employees have remained Niagara Mohawk employees, but their services have been provided to ServCo by Niagara Mohawk at cost. National Grid states that it plans that additional union employees hired in Syracuse will perform these services under this arrangement.

17. As explained by National Grid, the employees who will be affected are housed in Niagara Mohawk because of their union contract, and that, absent the obligations under the union contract, these employees would be employed directly by ServCo and used to provide services to all affiliates at cost. With the waiver requested, National Grid states that it could replicate that result while maintaining at-cost pricing for all of the general and administrative services provided to National Grid's centralized service companies.

18. National Grid further states that concerns about forgone profits of a public utility do not apply to situations such as this, where the public utility employees do not provide their services to non-affiliates. National Grid explains that the combination of the services provided and the unique circumstances of the Niagara Mohawk union contract create the justification for the Commission to find that the subject transactions do not create risks of inappropriate cross-subsidization. National Grid also notes that the New York Public Service Commission's (New York Commission) order approving National

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<sup>10</sup> Amended Application at 7, 14-16.

Grid's acquisition of KeySpan directs that all transactions for non-power goods and services among and between regulated affiliates, including those between Niagara Mohawk and ServCo, are to be settled at cost in both directions.

## **2. Services At Cost under Mutual Assistance Agreement**

19. National Grid also seeks waiver with respect to transactions performed under the Mutual Assistance Agreement, specifically waiver of:

(1) the requirements of section 35.44(b)(1) of the Commission's regulations as they pertain to the provision of services under the Mutual Assistance Agreement at cost by Massachusetts Electric, Granite State, Narragansett Electric or Niagara Mohawk to Engineering & Survey, Utility Services, or Electric Services; and

(2) the requirements of section 35.44(b)(2) of the Commission's regulations as they pertain to the provision of services under the Mutual Assistance Agreement at cost by Electric Services to Massachusetts Electric, Granite State, Narragansett Electric, or Niagara Mohawk.<sup>11</sup>

20. National Grid states that a number of affiliated companies within the National Grid holding company system executed a Mutual Assistance Agreement, dated March 28, 2008. The parties to this agreement include Granite State, Massachusetts Electric, Narragansett Electric, and Niagara Mohawk (franchised public utilities), as well as three subsidiaries that are non-utility affiliates – Utility Services and Engineering & Survey, which, as indicated, are centralized service companies, and Electric Services.

21. National Grid further states that the parties to the Mutual Assistance Agreement recognize that each may, from time to time, need assistance and services in connection with their respective business operations, and that each may find it economic and efficient to obtain such services or assistance from another party to the Mutual Assistance Agreement, rather than obtain such services or assistance from the market. These services include construction and maintenance, emergency assistance, engineering, stores, and various other services and assistance. According to National Grid, the Mutual Assistance Agreement does not require that the parties to it obtain such services or assistance from another party. It states that all assistance and services will be at actual cost and that direct charges will be made for assistance and services. National Grid further states that the bulk of the transactions under the Mutual Assistance Agreement

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<sup>11</sup> Amended Application at 8-9, 17-22, as amended by Supplemental Filing at 2-4.

take place between National Grid's franchised public utility affiliates and are not governed by the Commission's affiliate pricing rules. The transactions under the Mutual Assistance Agreement for which National Grid seeks waiver are those between National Grid's franchised public utilities and certain of its non-utility affiliates, specifically, Utility Services, Engineering & Survey, and Electric Services.

22. National Grid asserts that the pricing structure under the Mutual Assistance Agreement will not cause transmission customers of the franchised public utilities to subsidize non-regulated activities of the non-utility affiliates, or otherwise cause such transmission customers to bear the cost of inappropriate cross-subsidization for two reasons. First, the non-utility affiliate recipients of goods or service provided pursuant to the Mutual Assistance Agreement do not sell or provide such goods or services to any non-utility affiliated third-party, with the exception of LIPA. In this regard, however, National Grid states that LIPA is an "allowed" or previously-approved exception, which is discussed in greater detail below. As a result, National Grid states that these non-utility affiliates do not capture for National Grid's shareholders any profit that might be available by reselling at market prices the goods or services they receive under the Mutual Assistance Agreement at cost. Thus, National Grid states that the Mutual Assistance Agreement does not provide a means to transfer benefits from the customers of a franchised utility to a non-utility affiliate. Second, National Grid states that the at-cost pricing under the Mutual Assistance Agreement does not result in a franchised public utility foregoing profits because the franchised public utilities providing goods or services under the Mutual Assistance Agreement do not provide such goods or services to non-affiliated third parties.

23. With respect to the provision of services at cost by certain of National Grid's non-utility affiliates to its franchised public utility affiliates pursuant to the Mutual Assistance Agreement, National Grid explains that two of the non-utility affiliates, namely, Engineering & Survey and Utility Services, are centralized service companies. As such, they are permitted under the Commission's affiliate pricing rules to provide non-power goods and services to affiliates at cost. Thus, the pricing structure under the Mutual Assistance Agreement for these two companies is fully consistent with the Commission's treatment of pricing by centralized service companies to their affiliated operating companies.<sup>12</sup> Additionally, National Grid explains that Electric Services' inclusion in the Mutual Assistance Agreement reflects its unique function as the provider of day-to-day utility operations and maintenance and construction management services to LIPA under the Management Services Agreement. As such, National Grid states that Electric Services should be viewed as yet another operating utility for affiliate pricing services, and suggests that, given Electric Services' unique position and role in the National Grid

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<sup>12</sup> Amended Application at 20-21; 18 C.F.R. § 35.44(b)(3) (2010).

holding company system, the requirements of section 35.44(b)(2) should not apply to transactions between Electric Services and the franchised public utility signatories of the Mutual Assistance Agreements.<sup>13</sup>

24. Finally, National Grid notes that its negotiations with the New York Commission leading up to the acquisition of KeySpan produced a settlement that became part of the New York Commission's order approving the acquisition. That order provides that transactions among and between centralized service companies and regulated affiliates are to settle at cost in both directions. The definition of regulated affiliates includes affiliates that provide services to LIPA, including Electric Services. National Grid states that the New York Commission's exercise of jurisdiction over and monitoring of such transactions provides additional confirmation that the Mutual Assistance Agreement's requirement that all transactions between operating utilities and non-utility affiliates settle on an at-cost basis does not result in inappropriate cross-subsidization.

### **3. Transfer of Goods and Equipment "At Cost"**

25. The third class of transactions for which National Grid seeks waiver involves the expansion of National Grid's centralized inventory management program. National Grid seeks waiver of the requirements of section 35.44(b)(1) of the Commission's regulations as they pertain to the transfer of certain inventory held by Massachusetts Electric, Granite State, Narragansett Electric, or Niagara Mohawk to ServCo in order to expand National Grid's centralized inventory management program to all operating utilities within the National Grid holding company system and to include precapitalized equipment.<sup>14</sup>

26. National Grid states that, beginning in 1999, ServCo (then known as New England Power Service Company) implemented a centralized inventory management program to procure and manage transmission and distribution materials and supplies for its operating utility company affiliates. National Grid's predecessor obtained approval from the Securities and Exchange Commission (SEC) under the Public Utility Holding Company Act of 1935 (PUHCA 1935) to implement this program. The centralized inventory management program was implemented before either Niagara Mohawk or KeySpan and its subsidiaries became part of the National Grid holding company system. The program also predates the Commission's oversight of centralized service companies that commenced with the repeal of PUHCA 1935 and the enactment of the Public Utility Holding Company Act of 2005.<sup>15</sup>

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<sup>13</sup> Amended Application at 21.

<sup>14</sup> Amended Application at 9-11, 22-25.

<sup>15</sup> 42 U.S.C. § 16451 *et seq.* (2006).

27. Under the centralized inventory management program, ServCo employees operate central distribution centers that stock items such as electrical cable and conductors, switches, cutouts, reclosers, splices, connectors, arrestors, clamps, streetlamps and fixtures, conduit, spacers, poles, pole line hardware, distribution gas materials, and consumables. ServCo assumed the task of contracting for and paying vendors on behalf of the operating utility affiliates. Material and stockroom costs associated with the inventory management program are billed to the operating utility affiliates in three ways: (1) materials issued from a central distribution center to any operating utility are billed directly based on the average unit cost of the material transferred; (2) each operating utility affiliate is billed for its allocated share of the change in inventory balance at month end; and (3) each central distribution center's overhead such as rent, property taxes, operating and maintenance costs, and the wages and benefits of central distribution center personnel are allocated to the operating utility affiliates based on their respective average usage of each central distribution center during the prior fiscal year.

28. ServCo administers the centralized inventory management plan for the utility affiliates pursuant to the service contracts with the utility affiliates. National Grid states that ServCo does not purchase the inventory for its own use. The utility affiliates prepay for the inventory based on their rolling 13-month historic usage, and ServCo uses the prepayments to purchase the inventory. ServCo then holds the inventory and title to the inventory until a utility affiliate requests and accepts delivery of specific inventory. The costs charged to the utility affiliates for the inventory are the average unit cost of the inventory plus an adder to cover ServCo's administrative costs.

29. National Grid states that it seeks to expand this centralized inventory management program in two respects. First, National Grid seeks to extend the centralized inventory management program to Niagara Mohawk and KeySpan, in connection with which National Grid will have all such materials and supplies currently held by Niagara Mohawk transferred to ServCo at cost. National Grid states that these transfers will put Niagara Mohawk, the only franchised public utility included in this proposed expansion, in the same position as the other public utility affiliates that are already in the program. After all transfers are complete, all affiliated operating utility companies participating in ServCo's centralized inventory management program, including Niagara Mohawk, will do so under the terms that were previously in place. Second, National Grid plans to include precapitalized equipment such as transformers, regulators, and capacitors in the program.<sup>16</sup> The utilities will make a one-time transfer of precapitalized materials and goods currently inventoried at individual utility companies to ServCo at cost. National Grid states that section 35.44(b)(1) of the Commission's regulations would require that

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<sup>16</sup> National Grid defines "precapitalized equipment" as goods that are capitalized on the books of the public utility that currently owns them.

these transactions be at the higher of cost or market price. Therefore, National Grid is seeking waiver of this requirement to allow the transfers from the utility affiliates to ServCo to occur at cost.

30. National Grid states that the at-cost pricing contemplated to implement this expansion of National Grid's centralized inventory management program will not cause transmission customers of any franchised utility to subsidize the activities of the non-utility affiliate, ServCo, or otherwise bear the cost of inappropriate cross-subsidization. National Grid explains that the sole purposes of the transactions at issue here is to consolidate inventory within National Grid's centralized service company, ServCo, in order to maximize efficiency and reduce costs. National Grid states that ServCo would not derive any benefit from the transactions and that all goods transferred by the public utility companies to ServCo will be used by one of the National Grid public utilities or sold at replacement cost by ServCo and credited back to the relevant public utility. National Grid states that ServCo does not own any of the inventory for its own benefit, but rather administers the program and facilitates what is essentially inventory sharing among the public utilities. As a result, National Grid states that none of the transactions contemplated to expand the existing centralized inventory management program result in transmission customers of the franchised utility subsidizing non-regulated activities of a non-utility affiliate, or otherwise cause such transmission customers to bear the cost of inappropriate cross-subsidization.

## **II. Notice of Filings and Responsive Pleadings**

31. Notice of National Grid's filing was published in the *Federal Register*, 74 Fed. Reg. 1,212 (2009), with interventions and protests due on or before January 14, 2009. Northeast Utilities Service Company filed a timely motion to intervene.

32. Notice of National Grid's Amended Application was published in the *Federal Register*, 75 Fed. Reg. 34,108 (2010), with interventions and protests due on or before June 16, 2010. None was filed.

33. Notice of National Grid's Supplemental Filing was published in the *Federal Register*, 75 Fed. Reg. 66,079 (2010), with interventions and protests due on or before November 5, 2010. None was filed.

## **III. Discussion**

### **A. Procedural Matters**

34. Pursuant to Rule 214 of the Commission's Rules of Practice and Procedure, 18 C.F.R. § 385.214 (2010), Northeast Utilities Service Company's timely, unopposed motion to intervene serves to make it a party to this proceeding.

## B. Commission Determination

35. As noted above, the Commission's regulations specify that unless otherwise permitted by Commission rule or order: (1) a franchised public utility that has captive customers or owns or provides transmission service over jurisdictional transmission facilities and that provides non-power goods and services to a market-regulated power sales affiliate or a non-utility affiliate must sell them at a price that is the higher of cost or market price and (2) a franchised public utility that has captive customers or owns or provides transmission service over jurisdictional transmission facilities may not purchase non-power goods or services from a market-regulated power sales affiliate or a non-utility affiliate at a price above market price. The Commission's regulations further specify that a company in a single-state holding company system may provide or receive such non-power goods and services from its affiliates at cost.<sup>17</sup> In Order No. 707-A, the Commission stated that, in the case of multi-state holding company systems, it would consider requests to waive these requirements on a case-by-case basis.<sup>18</sup> National Grid operates a multi-state holding company system, and therefore cannot rely on the waiver provided under section 35.44(b)(4) of the Commission's regulations for at-cost pricing of any of the transactions described in its amended application. Nevertheless, based on the information National Grid has provided, we will grant the requested waivers.<sup>19</sup>

36. We find that the first category of transactions (at-cost pricing for the services Niagara Mohawk union employees provide to ServCo) will not result in inappropriate cross-subsidization of non-utility affiliates. We note at the outset that the at-cost pricing for services Niagara Mohawk employees provide to ServCo were both required and approved by the New York Commission, and the New York Commission exercises oversight of them. This Commission has recognized the importance of such state regulatory determinations, and it is reluctant to interfere with settled practices that are already subject to state oversight, where there is no showing that suggests that these practices are leading to improper cross-subsidization.<sup>20</sup> Additionally, as the Commission stated in Order No. 707-A, if a franchised public utility does not provide general and administrative goods and services to non-affiliates, it cannot be said with certainty that it is foregoing profits when it sells such goods and services at cost to an affiliate.<sup>21</sup> In this

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<sup>17</sup> 18 C.F.R. § 35.44(b)(4) (2010).

<sup>18</sup> Order No. 707-A, FERC Stats. & Regs. ¶ 31,272 at P 28.

<sup>19</sup> We note that our action does not preclude complaints in specific instances alleging that an at-cost price for a specific service supplied to a franchised public utility exceeds the market price and leads to effects on rates that are unjust and unreasonable.

<sup>20</sup> Order No. 707-A, FERC Stats. & Regs. ¶ 31,272 at P 28.

<sup>21</sup> *Id.* P 25.

case, moreover, the transactions in question simply replicate the result that would have been reached but for the requirements of the union contract, i.e., if the employees were employed by ServCo directly. As National Grid states in its application, ServCo provides general and administrative services and related goods and non-power goods and services at cost to the companies in the National Grid holding company system, and the overwhelming majority of these employees are directly employed by ServCo. Likewise, the services provided by Niagara Mohawk's union employees to ServCo will, in turn, be billed to ServCo's other affiliates at cost. ServCo will not procure such services for its own use or to service non-affiliates. Thus, the arrangement between Niagara Mohawk and ServCo cannot give rise to inappropriate cross-subsidization of non-utility affiliates.

37. We also find that the provision of services at cost between the franchised public utilities and non-utility affiliates under the Mutual Assistance Agreement will not result in inappropriate cross-subsidization. Section 35.44(b)(1) of the Commission's regulations requires that sales of non-power goods and services by franchised public utilities to non-utility affiliates be made at the higher of cost or market price. In two instances the purchasers of such services under the Mutual Assistance Agreement will be centralized service companies – Engineering & Survey and Utility Services – which, for purposes of section 35.44, are non-utility affiliates. However, since Engineering & Survey and Utility Services only provide goods or services, including goods and services that they procure from utility affiliates under the Mutual Assistance Agreement, to other National Grid affiliates, at cost, there is no opportunity for inappropriate cross-subsidization of a non-utility affiliate. Moreover, the franchised public utilities do not provide such non-power goods or services to unaffiliated third parties. Hence, there is no basis for finding that they are foregoing profits when making at-cost sales under the Mutual Assistance Agreement.

38. Similarly, although Electric Services, the third non-utility affiliate that receives goods and services from utility affiliates under the Mutual Assistance Agreement, sells goods and services to a non-affiliate, i.e., LIPA, the terms of the Management Services Agreement governing how Electric Services is compensated should alleviate any concern that sales or transfers to Electric Services by a franchised public utility affiliate under the Mutual Assistance Agreement could result in a transfer of benefits to Electric Services and through it to National Grid's shareholders. In this regard, National Grid explains that, under the Management Services Agreement, Electric Services is required to obtain field support and logistics support from its utility affiliates via the Mutual Assistance Agreement in the event of storm or other adverse operational conditions affecting LIPA and that costs incurred by Electric Services under the Mutual Assistance Agreement to provide such support are simply passed through to LIPA.<sup>22</sup> Thus, according to National

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<sup>22</sup> Supplemental Filing at 3-4.

Grid, the participation by Electric Services in the Mutual Assistance Agreement on behalf of LIPA does not allow Electric Services to capture benefits on behalf of National Grid's shareholders.

39. We also find it appropriate to grant a waiver under section 35.44(b)(2) of the Commission's regulations to permit at-cost pricing of transactions under the Mutual Assistance Agreement, where Massachusetts Electric, Granite State, Narragansett Electric, or Niagara Mohawk purchase services from Electric Services under the Mutual Assistance Agreement at cost instead of at a price that does not exceed the market price, as required by section 35.44(b)(2) of the Commission's regulations. As explained by National Grid, Electric Services occupies a unique position that results from the acquisition by LIPA of the transmission and distribution assets of Long Island Lighting Company, a predecessor of Key Span. Key Span's transmission and distribution employees manage LIPA's facilities for Electric Services under the Management Services Agreement. Given these facts, the services that Massachusetts Electric, Granite State, Narragansett Electric, or Niagara Mohawk acquire from Electric Services resemble services that they could acquire from a franchised public utility affiliate. The Commission's regulations do not prohibit at-cost pricing in such cases. Finally, National Grid notes that the New York Commission requires at-cost pricing for these transactions.

40. Lastly, with respect to the transfer of goods under National Grid's centralized inventory management plan, we grant waiver under section 35.44(b)(1) of the Commission's regulations for the one-time transfer of an at-cost basis of inventory from Niagara Mohawk and the KeySpan utility companies to ServCo and for National Grid's plan to include in the inventory management program precapitalized equipment, i.e., equipment owned by a National Grid utility and classified as capital equipment for accounting purposes. As National Grid explains, the sole purpose of the transaction is to consolidate inventory to maximize efficiency and reduce costs for National Grid's franchised public utility subsidiaries, and ServCo does not own any of the inventory for its own benefit. Since this equipment is intended for the ultimate use of the franchised public utility subsidiaries and not ServCo, the policy underlying the requirement that such transfers to non-utility affiliates must be at the higher of cost or market does not apply. In addition, as described above, the centralized inventory management program, which National Grid seeks to expand and extend, was approved by the SEC under PUHCA 1935. National Grid states that this program provides savings through streamlined contract negotiation and administration, as well as from aggregating the purchases of the operating utility affiliates in larger volume transactions. Therefore, we find that the transfer of goods, as proposed, will not result in inappropriate cross-subsidization.

The Commission orders:

(A) National Grid's request for waivers of the affiliate restrictions under sections 35.44(b)(1) and 35.44(b)(2) is hereby granted for the three categories of transactions identified above, as discussed in the body of this order.

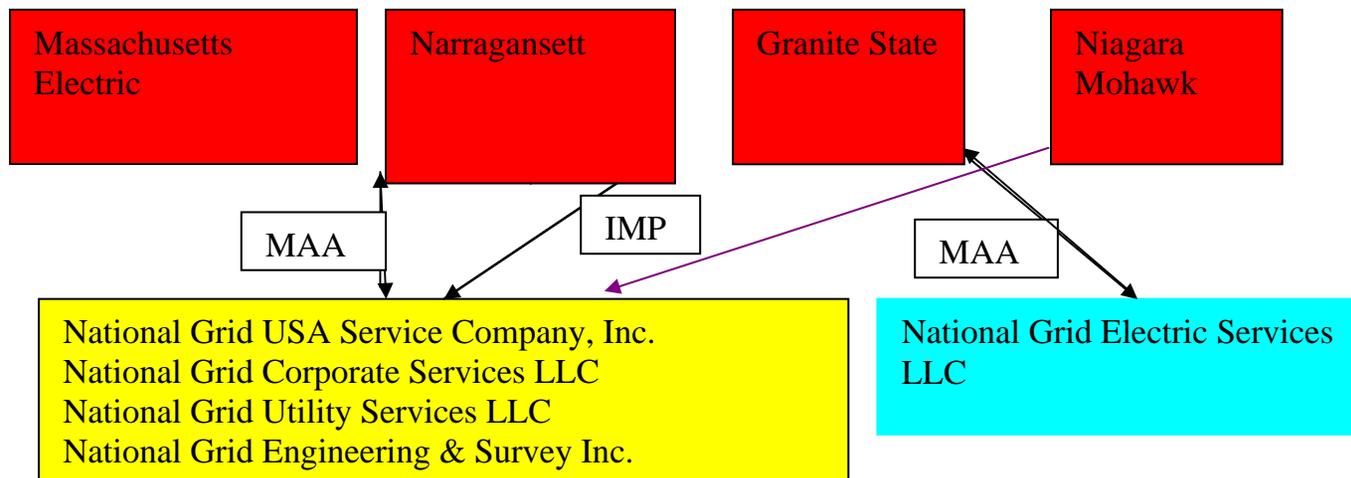
(B) National Grid must inform the Commission within 30 days of any material change in circumstances that would reflect a departure from the facts, policies, and procedures the Commission relied upon in granting the waivers herein.

By the Commission. Commissioner LaFleur is not participating.

( S E A L )

Nathaniel J. Davis, Sr.,  
Deputy Secretary.

**Appendix 1**



**Red** = Franchised Public Utilities that Own or Operate Transmission Facilities

**Yellow** = Non-Utility Affiliates that are Centralized Service Companies

**Blue** = Non-utility Affiliate

MAA = Mutual Assistance Agreement

IMP = Inventory Management Plan

→ = Services Provided by Niagara Mohawk Union Employees