FEDERAL ENERGY REGULATORY COMMISSION
WASHINGTON, D.C. 20426

In Reply Refer To:
Office of Enforcement
Docket No. FA16-2-000
November 15, 2019

National Grid USA
Attention: Daniel Galaburda
Assistant General Counsel & Director
40 Sylvan Road
Waltham, MA 02451

Dear Mr. Galaburda:

1. The Division of Audits and Accounting (DAA) within the Office of Enforcement (OE) of the Federal Energy Regulatory Commission (Commission) has completed an audit of National Grid USA (National Grid), including its service companies and other affiliates in the National Grid holding company system. The audit covered the period from January 1, 2013 through December 31, 2018.

2. The audit evaluated National Grid's compliance with the Commission's: (1) cross-subsidization restrictions on affiliate transactions under 18 C.F.R Part 35; (2) accounting, recordkeeping, and reporting requirements under 18 C.F.R. Part 366; (3) preservation of records requirements for holding companies and service companies under 18 C.F.R. Part 368; and (4) Uniform System of Accounts for Centralized Service Companies under 18 C.F.R. Part 367. The audit also evaluated the associated public utilities' compliance with the Commission's accounting requirements for transactions with associated companies under 18 C.F.R. Part 101 and the applicable reporting requirements in the FERC Form No. 1 under 18 C.F.R. Part 141. The enclosed audit report contains seven findings and 32 recommendations that require National Grid to take corrective action.

3. On October 30, 2019, you notified DAA that National Grid accepts all seven findings and 32 recommendations in the draft audit report and will submit within 30 days of the issuance of the final audit report a plan for implementing the audit recommendations. A copy of your verbatim response is included as an appendix to this report. I hereby approve the audit report.

4. National Grid should submit its implementation plan to comply with the recommendations within 30 days of this letter order. National Grid should make quarterly submissions to DAA describing the progress made to comply with the recommendations, including the completion date for each corrective action. As directed by the audit report, these submissions should be made no later than 30 days after the end of each calendar quarter, beginning with the first quarter after this audit report is issued, and continuing until all the corrective actions are completed.

5. The Commission delegated the authority to act on this matter to the Director of OE under 18 C.F.R. § 375.311. This letter order constitutes final agency action. National Grid may file a request for rehearing with the Commission within 30 days of the date of this order under 18 C.F.R. § 385.713.

6. This letter order is without prejudice to the Commission's right to require hereafter any adjustments it may consider proper from additional information that may come to its attention. In addition, any instance of noncompliance not addressed herein or that may occur in the future may also be subject to investigation and appropriate remedies.

7. I appreciate the courtesies extended to the auditors. If you have any questions, please contact Mr. Steven D. Hunt, Director and Chief Accountant, Division of Audits and Accounting at (202) 502-6084.

Sincerely,

Larry R. Parkinson
Director
Office of Enforcement

Enclosure

Federal Energy Regulatory Commission
Office of Enforcement
Division of Audits and Accounting

AUDIT REPORT

Audit of National Grid USA's Compliance with:

- Cross-Subsidization Restrictions on Affiliate Transactions;
- Regulations Under the Public Utility Holding Company Act of 2005;
- Uniform System of Accounts for Centralized Service Companies;
- FERC Form No. 1 Reporting Requirements for Public Utilities; and
- Preservation of Records Requirements for Holding Companies and Service Companies.

Docket No. FA16-2-000
November 15, 2019

TABLE OF CONTENTS

I. Executive Summary

A. Overview

The Division of Audits and Accounting (DAA) within the Office of Enforcement has completed an audit of National Grid USA (National Grid). The audit evaluated National Grid's compliance with the Commission's: (1) cross-subsidization restrictions on affiliate transactions under 18 C.F.R Part 35; (2) accounting, recordkeeping, and reporting requirements under 18 C.F.R. Part 366; (3) preservation of records requirements for holding companies and service companies under 18 C.F.R. Part 368; and (4) Uniform System of Accounts for Centralized Service Companies under 18 C.F.R. Part 367 (USofA). The audit also evaluated the associated public utilities' compliance with the Commission's accounting requirements for transactions with associated companies under 18 C.F.R. Part 101 and the applicable reporting requirements in the Annual Report of Major Electric Utilities, Licensees and Others, FERC Form No. 1 (FERC Form No. 1) under 18 C.F.R. Part 141. The audit covered the period January 1, 2013 through December 31, 2018.

B. National Grid

National Grid is a direct wholly-owned subsidiary of National Grid North America Inc. and an indirect wholly-owned subsidiary of National Grid plc, a public limited company incorporated under the laws of England and Wales. National Grid plc conducts its United States business principally through National Grid and its subsidiaries.

National Grid is a public utility holding company and owns, directly or indirectly, a majority of the outstanding common stock of its public utility subsidiaries and varying percentages of other subsidiaries that provide other nonutility services. The main business of National Grid, through its subsidiaries, is the transmission and distribution of electricity and natural gas.

National Grid has the largest electric transmission and distribution network in the New York and New England regions. It delivers electricity to approximately 3.4 million customers in Massachusetts, New Hampshire, New York, and Rhode Island. National Grid is also the largest distributor of natural gas in the Northeast, with approximately 3.6 million customers in those same states.

C. Summary of Compliance Findings

Below is a summary of audit staff's findings. Audit staff identified seven areas of noncompliance, which are detailed in Section IV of this report.

1. *Depreciation Expense of Service Companies Assets* – National Grid USA Service Company (NGUSASCo) and National Grid Engineering & Survey Inc. (NGE&S) used improper composite depreciation rates to determine depreciation expense accrued on certain property. This led the two service companies to accrue depreciation expense at rates not consistent with Commission accounting rules. The service companies then allocated and billed the incorrectly calculated depreciation expense to their public utility and nonutility affiliates. As a result, amounts billed to public utility affiliates with transmission formula rates were included in the rates charged to wholesale transmission customers.

2. *Cost Allocation Methodologies* – NGUSASCo and NGE&S did not consistently use their documented cost allocation methods, nor timely update their general ledger system to reflect changes in the allocation percentages actually used to bill affiliates. These errors led the service companies to over-allocate costs to certain National Grid public utility subsidiaries, and these public utilities in turn overbilled their respective wholesale transmission customers.

3. *Industry Association Dues* – NGUSACo improperly accounted for and allocated a portion of the cost of its gas and electric industry associations' membership dues to National Grid's public utility subsidiaries. As a result, National Grid's public utility subsidiaries improperly included the lobbying component of industry association payments in their wholesale transmission rates.

4. *Donations* – NGUSASCo improperly recorded certain donations to Account 921, Office Supplies and Expenses, and Account 930.2, Miscellaneous General Expenses, instead of Account 426.1, Donations, as required by Commission regulations. Amounts recorded in Accounts 921 and 930.2 were allocated to National Grid's public utility subsidiaries and other affiliates and accounted for by the entities using the same accounts, and for some public utility subsidiaries were included as inputs to their respective wholesale transmission formula rate cost recovery mechanisms. As a result, in some years National Grid's public utility subsidiaries improperly included the donations in their wholesale transmission rates.

5. *Service Company Account Misclassifications* – NGUSASCo improperly accounted for various administrative and general expenses in its books and records. As a result, NGUSASCo overstated certain administrative and general accounts it billed to National Grid public utility subsidiaries, resulting in misclassifications reported in the public utilities' FERC Form No. 1.

6. *Reporting of Transactions with Associated (Affiliated) Companies* – National Grid's public utility subsidiaries did not follow the instructions on page 429, Transactions with Associated (Affiliated) Companies, of the FERC Form No. 1 and as a result reported inaccurate and incomplete information for transactions with associated companies.

7. *Annual Report of Centralized Service Companies, FERC Form No. 60 (FERC Form No. 60)* – NGUSASCo and NGE&S did not complete the FERC Form No. 60 reports filed during the audit period in accordance with the general and schedule instructions of the form.

D. Summary of Recommendations and Corrective Actions Taken

Below is a summary of audit staff's recommendations to remedy the findings in this report, which are detailed in Section IV. Audit staff recommends that National Grid:

Depreciation Expense of Service Companies' Assets

1. Conduct a full analysis of the weighted average service life calculations for each asset class and recalculate depreciation and amortization expense accrued during the audit period for service company property. Provide the results of the analysis and all applicable work papers supporting the analysis, including factors used to calculate the amount of the errors, to DAA within 60 days of receiving the final audit report.

2. Submit proposed accounting entries based on the analysis performed pursuant to Recommendation No. 1 to DAA, within 60 days of receiving the final audit report, for the removal of over accrued depreciation and amortization expenses from Account 108, Accumulated Depreciation, and other accounts affected, such as the accumulated deferred income tax (ADIT) accounts.

3. Revise accumulated depreciation, ADIT, and other accounts impacted by the over accrued depreciation and amortization expenses after receiving DAA's assessment of the proposed accounting entries, and restate and footnote the balances in the FERC Form No. 60 for current and comparative years as necessary.

4. Revise policies, procedures, and practices to help ensure weighted average service lives are accurately calculated, reviewed, and entered into the asset management accounting system.

5. Train employees on the revised procedures and provide periodic training.

6. Submit a refund analysis to DAA, within 60 days of receiving the final audit report, that explains and details the following: (1) calculation of expenses that were inappropriately recovered through the public utilities' transmission formula rates; (2) components of the refunds; (3) refund method; (4) customers to receive refunds; and (5) the period(s) in which refunds will be made.

7. File a refund report with the Commission after receiving DAA's assessment of the refund analysis.

8. Refund amounts disclosed in the refund report to transmission formula rate customers, with interest calculated in accordance with section 35.19a of Commission regulations.

Cost Allocation Methodologies

9. Strengthen policies and procedures to ensure revised allocation percentages are updated in the general ledger system and implemented on a timely basis.

10. Strengthen policies and procedures for formally approving the use of new allocators.

11. Train staff on the new policies and procedures for updating allocation percentages.

12. Quantify the dollars over or under allocated for the period April 2013 through March 2015.

13. Submit a refund analysis to DAA, within 60 days of receiving the final audit report that explains and details the following: (1) calculation of allocated service company costs that were inappropriately recovered through the public utilities' transmission formula rates in the audit period; (2) components of the refunds to be made as a result of the calculation; (3) refund method; (4) customers to receive refunds; and (5) the period(s) in which refunds will be made.

14. File a refund report with the Commission after receiving DAA's assessment of the analysis.

15. Refund amounts disclosed in the refund report to wholesale transmission customers, with interest calculated in accordance with section 35.19a of Commission regulations.

Industry Association Dues

16. Strengthen policies and procedures to ensure industry association dues are accounted for in accordance with the Commission's regulations, in particular the regulation pertaining to lobbying costs.

17. Strengthen policies and procedures to ensure costs incurred by the service companies relating to industry association dues are reallocated to the public utilities in compliance with NGUSASCo's allocation methodology.

18. Train staff on the revised procedures for recording, accounting for, and allocating costs related to industry association dues.

19. Submit a refund analysis, within 60 days of receiving the final audit report, to DAA that explains and details the following: (1) calculation of refunds that resulted from the improper accounting and allocation of the costs of membership dues during the audit period, including interest; (2) determinative components of the refund; (3) refund method; (4) customers to receive refunds; and (5) period(s) in which refunds will be made.

20. File a refund report with the Commission after receiving DAA's assessment of the analysis.

21. Refund amounts disclosed in the refund report to wholesale customers, with interest calculated in accordance with section 35.19a of the Commission's regulations.

Donations

22. Perform a review of all payments made to industry associations and organizations such as research institutes, voluntary charitable contributions, including mitigation payments, and other voluntary donations for the audit period to ensure all donations are accounted for properly.

23. Strengthen policies and procedures to ensure that voluntary payments to industry associations, organizations such as research institutes, charitable contributions, including voluntary mitigation payments, and other donations are accounted for in accordance with Commission regulations.

24. Provide training to staff on the revised policies for accounting for charitable contributions and other donations.

25. Submit a refund analysis, within 60 days of receiving the final audit report, to DAA for review that explains and details the following: (1) calculation of refunds that resulted from improper accounting for donations during the audit period, including interest; (2) determinative components of the refund; (3) refund method; (4) customers to receive refunds: and (5) period(s) in which refunds will be made.

26. File a refund report with the Commission after receiving DAA's assessment of the analysis.

27. Refund amounts disclosed in the refund report to wholesale customers, with interest calculated in accordance with section 35.19a of the Commission's regulations.

Service Company Account Misclassifications

28. Strengthen accounting policies and procedures to ensure that service company costs, and by association operating company costs, are recorded in the correct FERC accounts.

29. Train employees on the updated policies and procedures for recording administrative and general (A&G) expenses to FERC accounts.

Reporting of Transactions with Associated (Affiliated) Companies

30. Strengthen policies and procedures, to include a reconciliation to the FERC Form No. 60 for those non-power goods and services provided by the service companies, to ensure that its public utility subsidiaries accurately, completely, and consistently prepare the schedule on page 429 of the FERC Form No. 1 according to instructions.

FERC Form No. 60 Reporting

31. Enhance procedures and controls for submitting NGUSASCo's and NGE&S's FERC Form No. 60 to ensure the forms are accurate, complete, and prepared according to all instructions.

32. Train employees responsible for the FERC Form No. 60 on the new procedures to ensure accurate and complete reporting that is compliant.

E. Compliance and Implementation of Recommendations

Audit staff further recommends that National Grid submit for review the following:

- A plan for implementing the recommendations within 30 days after the final audit report is issued;

- Quarterly reports describing progress in completing each corrective action recommended. Quarterly nonpublic submissions should be made no later than 30 days after the end of each calendar quarter, beginning with the first quarter after the final audit report is issued, and continuing until all corrective actions are completed; and

- Copies of written policies and procedures developed in response to the recommendations. These documents should be submitted in the first quarterly filing after their completion.

II. Background

A. National Grid Holding Company System

National Grid is a public utility holding company under the Public Utility Holding Company Act of 2005 and a direct wholly-owned subsidiary of National Grid North America. National Grid North America's primary activity is to provide debt service to National Grid. National Grid is the parent company of two centralized service companies and several other companies, some of which are public utilities. National Grid's operations grew significantly in 2007 with the acquisition of KeySpan Corporation.

The centralized service companies provide a variety of non-power goods and services to affiliate companies. The affiliate companies also provide services amongst themselves and to the service companies. These services are discussed in more detail below.

B. National Grid Service Companies and Cost Allocations

National Grid's two centralized service companies are NGUSASCo and NGE&S. NGUSASCo provides non-power goods and services to affiliates that include activities such as construction, customer service, engineering, executive and administrative, financial, legal, employee relations, information systems, and regulatory services. The vast majority of services provided to National Grid and its non-service company subsidiaries are provided by NGUSASCo. NGE&S provides engineering services primarily to National Grid Generation, LLC.

NGUSASCo and NGE&S provide their goods and services under agreements that state that the prices received will include all costs of doing business, including a reasonable return on capital. Under the agreements, affiliate companies are required to pay the service companies for all costs incurred for the benefit of, or on behalf of, the affiliates. In accordance with the agreements, where one or more entities benefit from a particular service, costs are required to be proportionately charged to each benefiting affiliate based on a documented allocation method that results in each being charged a percentage of total costs.

In accordance with National Grid's accounting policies, costs for services provided by NGUSASCo and NGE&S are required to be charged to the affiliate companies either directly or through the use of a cost allocation methodology. National Grid has developed a cost allocation manual (CAM) that prescribes the manner in which costs incurred by the service companies or among affiliates that benefit more than one entity should be charged to affiliate companies. National Grid stated that the premise of the CAM guidelines is to ensure that allocation methods do not result in the subsidization of the cost of non-regulated services or products by regulated entities or the subsidization of the cost of services or products from one regulated entity to another. The various cost allocation methods are detailed in the CAM.

C. Operating Companies

National Grid has eight wholly-owned subsidiaries that are jurisdictional public utilities and which operate under wholesale transmission formula rates; four non-jurisdictional gas distribution companies; and a wholesale generation subsidiary, National Grid Generation LLC (NG Generation), which operates on a cost of service basis. The jurisdictional public utilities with wholesale transmission formula rates are: New England Power Company (NEP), Narragansett Electric Company (Narragansett), Massachusetts Electric Company (MECO), Nantucket Electric Company (Nantucket), Niagara Mohawk Power Corporation (NiMo), New England Electric Transmission Corporation (NEET), New England Hydro-Transmission Corporation (NEHT), and New England Hydro-Transmission Electric Company, Inc. (NEHTCo). NEP, NEET, NEHT, and NEHTCo are transmission lines only companies.

National Grid's non-jurisdictional gas distribution companies provide intrastate gas distribution services only. These companies are Boston Gas Company, Colonial Gas Company, the Brooklyn Union Gas Company, and KeySpan Gas East Corporation.

D. Accounting System Transition and Implementation

In 2007, National Grid and KeySpan Corporation merged and became the second largest utility in the United States. Following the merger, National Grid commenced an information technology (IT) initiative intended to merge the entities' legacy accounting systems (PeopleSoft and Oracle). The changes to the systems were placed in service in November 2012. However, due to system implementation issues that arose after the in-service date, National Grid affiliates that relied on the accounting systems to file their FERC Form No. 1, Quarterly Financial Report of Electric Utilities, Licensees, and Natural Gas Companies, FERC Form No. 3-Q, and FERC Form No. 60 had difficulties meeting filing deadlines and filing accurate information. This led to requests for filing extensions from the Commission that were granted each year from 2009 through 2013. National Grid eventually resolved most of the issues with its accounting systems and began to timely file its reports in 2014.

National Grid's objectives for addressing the implementation issues were to stabilize the new system and ensure that it was configured correctly. National Grid indicated that there were two main challenges to achieving these objectives: (1) the data produced by the new software was inaccurate and (2) National Grid had resource limitations. To help achieve the objectives, National Grid established an internal team that it called the U.S. Foundation Project Business Improvement Team and implemented "Stabilization" and "Finance Remediation" plans that were intended to improve controls, data quality, and the financial and regulatory reporting processes.

Stabilization Project

National Grid declared the new accounting system stabilized in August 2015 as a result of the Stabilization Project. The project included the successful implementation of a software release (Release 2), designed to enable the separation of National Grid's systems supporting its operation of the Long Island Power Authority's (LIPA) electric distribution system when LIPA transferred contractual operation of its electric distribution system to another utility in January 2014, and to update Human Resources support packs. It also included another software release (Release 3), which provided National Grid with system and process capability enhancements to pay its employees and vendors and to comply with legal, regulatory and other reporting obligations timely and accurately. A final stage of the Stabilization Project, called Enhancement Release 1, consisted of two parts and was intended, through system and process improvements, to enable the company to more fully recognize the new software's benefits beginning in the first quarter of calendar year 2015. This final stage included an account reconciliation tool, general ledger improvements designed to reduce manual activities, and FERC module enhancements.

Finance Remediation Plan

The Finance Remediation Plan started in January 2014. It required National Grid to remediate control deficiencies related to labor accounting, account reconciliations, financial statement analytics, census data and manual journal entries. The Finance Remediation Plan was composed of 15 work streams representing priorities, each led by a National Grid subject matter expert responsible and accountable for understanding the root cause of the work stream's issues, developing a detailed work plan to address it and driving execution.

Finance Accounting and Controls Excellence (ACE) Program

Towards completion of the Finance Remediation Plan, National Grid implemented its ACE Program to address weaknesses in financial controls through standardization of processes and control documentation, and through subsequent training on the system improvements. ACE is composed of controls over plant, revenue, regulatory asset and liability accounting, the financial reporting process, and the general Committee of Sponsoring Organization of the Treadway Commission framework. Each component has a dedicated work stream lead overseeing the remediation.

Costs of the Accounting Software

Although the software system implementation was budgeted at $384 million, it cost National Grid approximately $877 million. Of the total, $317 million was related to capital costs and $560 million was related to operating expenses. Audit staff noted that almost all operating expenses were charged to the National Grid holding company and were not allocated to its operating companies.

Conclusion

Despite implementation of these programs, at the commencement of DAA's audit, management conceded that clean-up of its audit system and processes was still in progress. Audit staff noted that issues persisted regarding the accuracy and completeness of data, and believes these issues contributed to National Grid's tardiness in filing FERC reports and its inability to respond timely to the audit inquiry. However, audit staff also noted that the timeliness issues and data accuracy and completeness National Grid experienced improved over the course of the audit.

III. Introduction

A. Objectives

Audit objectives included evaluation of National Grid's compliance with the Commission's cross-subsidization restrictions on affiliate transactions under 18 C.F.R Part 35; service companies' accounting, recordkeeping, and FERC Form No. 60 reporting requirements under 18 C.F.R. Parts 366 and 367; preservation of records requirements for holding companies and service companies under 18 C.F.R. Part 368; and accounting and reporting requirements for public utilities for their transactions with associated companies under 18 C.F.R. Parts 101 and 141. The audit covered the period January 1, 2013 through December 31, 2018.

B. Scope and Methodology

Audit staff reviewed publicly available and company-provided information to evaluate compliance risk. Audit staff then conducted substantive testing to determine whether National Grid complied with accounting, reporting, and recordkeeping requirements, affiliate transaction restrictions, and FERC Form No. 60 instructions.

Audit staff performed the following to facilitate testing and evaluation of National Grid's compliance with Commission requirements relevant to audit objectives:

- *Review of Public Information* – Conducted an extensive review of public information before commencing the audit. The review provided a high-level understanding of National Grid's corporate structure, the services it provides, major events affecting operations and finances, mergers, significant contracts, prior audit issues, and other key regulatory and business activities. Examples of materials reviewed include National Grid's annual reports and SEC Form 20-F filings, its subsidiaries' FERC Form Nos. 1, 1-F, 2, 2-A, 3Q and 60 submissions, prior FERC and external audit reports, company web sites, and other relevant regulatory and media sources.

- *Identification of Audit Criteria* – Identified regulatory requirements and criteria for use in evaluating National Grid's compliance with audit objectives, including Commission accounting and reporting requirements in 18 C.F.R. Parts 35, 101, 141, 366, 367, and 368, and other Commission rules, regulations, and orders generally applicable to jurisdictional service companies and public utilities.

- *Issuance of Data Requests* – Issued data requests to collect information not commonly available to the public. The information related to internal policies, procedures, and controls, business practices, risk management, corporate structure, contractual agreements, financial accounting and reporting activity, corporate compliance, regulatory filings, and other matters.

- *Interviews and Meetings* – Held an opening teleconference with National Grid management to discuss audit objectives, scope, and process, and a closing conference, at the time of audit fieldwork completion, to discuss audit findings and recommendations. Audit staff also held regular teleconferences with National Grid employees to clarify data requests and to discuss technical and administrative matters, and one in-person meeting with National Grid's Chief Financial Officer at FERC headquarters.

- *External Auditor Working Papers Review* – Reviewed National Grid's external auditor's working papers prepared as part of that auditor's annual audits for 2013 through 2015.

- *Site Visits* – Conducted three site visits to National Grid headquarters in Brooklyn, NY to discuss and observe controls and procedures related to audit objectives. The visits enabled audit staff to:

    - Better understand National Grid's corporate structure, departmental functions, and employee responsibilities, and meet key company officials;

    - Learn about National Grid's holding company system and operations, in particular, the relationship the service companies have to its assets, departments, activities, and processes;

    - Interview executives, managers, and staff responsible for accounting, financial reporting, records retention and corporate compliance;

    - Meet with Internal Audit management and discuss concerns regarding compliance with Commission regulations;

    - Discuss the management and operation of National Grid's corporate compliance program;

    - Discuss and observe accounting and reporting procedures, processes, and controls relevant to audit scope; and

  - Discuss National Grid’s preservation of records policies, procedures, and practices.

- *Collaboration with Commission Staff* – Conferred with Commission staff in other divisions within the Office of Enforcement, particularly the previous Division of Energy Market Oversight, which had knowledge of and expertise regarding National Grid’s compliance history.

Audit staff also tested and evaluated National Grid’s compliance with rates, accounting, and reporting requirements. The most significant areas are covered below:

- *Cross-Subsidization Restrictions* – To evaluate compliance with the Commission’s cross-subsidization restrictions on affiliate transactions, audit staff reviewed policies, procedures, and practices related to the sale of non-power goods and services. Audit staff interviewed National Grid employees who account for and report the transfer of non-power goods and services. Audit staff also reviewed and tested the pricing mechanisms for non-power goods and services that the public utility subsidiaries provided to and received from each other, service companies, and other nonutility affiliates. To test compliance with Commission rules, audit staff sampled charges and payments to verify accurate and permissible pricing for the sale of such goods and services.

- *Accounting, Recordkeeping, and Financial Reporting* – To evaluate compliance with Commission books, records, and filing requirements, audit staff reviewed NGUSASCo’s and NGE&S’s FERC Form No. 60 filings and the public utility subsidiaries’ FERC Form No. 1 submissions. Audit staff tested select information reported on the forms against supporting records to determine whether it was accurate and complete. To verify accuracy and consistency, audit staff compared select information in the FERC Form No. 1 with the FERC Form No. 60, including page 429 of the FERC Form No. 1, which presents non-power goods and services transactions for each of the public utility subsidiaries. To evaluate NGUSASCo’s and NGE&S’s compliance with the Commission’s accounting regulations, audit staff reviewed, analyzed, and tested selected centralized service company accounting data. To evaluate the public utilities’ compliance with Commission accounting regulations, audit staff tested the accounting for selected costs billed to utilities by the centralized service companies.

- *Cost Allocation and Billings* – Audit staff identified cost allocation methods to facilitate review of the service companies’ costs billed to National Grid’s public utility subsidiaries. Audit staff also reviewed and tested the support for selected allocation methods.

- *Affiliate Transactions* – Audit staff reviewed transactions between the service companies and the public utility subsidiaries to ensure proper assignment and allocation of labor and other costs, and to ensure costs were recorded in the correct accounts.

Accounting, Reporting, and Recordkeeping

- *Accounting Processes and Procedures* – Audit staff evaluated National Grid's accounting processes, procedures, and controls for compliance with Commission accounting regulations under 18 C.F.R. Parts 101 and 367. Audit staff interviewed National Grid employees regarding accounting practices, adherence to policies and procedures, systems used for FERC accounting, and controls for ensuring compliance.

- *Chart of Accounts* – Audit staff evaluated accounting controls and tested National Grid's chart of accounts for consistency with the USofA.

- *Accounting Systems* – Audit staff evaluated the ability of National Grid's accounting systems to capture, manage and retain financial information, including on National Grid's general ledger and in work orders, expenses and billing. Audit staff evaluated the systems' ability to ensure reported financial information was accurate and complete.

- *Account Variance Analysis* – Audit staff performed variance analyses of accounts reported in the FERC Form Nos. 1 and 60 with large balances, unusual activity, and/or significant year-to-year fluctuations. Audit staff discussed the variances with National Grid to understand the nature of the fluctuations and to obtain additional information and support if necessary.

- *FERC Form No. 1 and Form No. 60 Reporting* – Audit staff reviewed National Grid's financial reporting processes, procedures, and quality controls to ensure compliance with Commission regulations. Audit staff examined financial statements, supplemental pages, and footnotes to identify significant or unusual accounting transactions and changes in accounting practices, and to confirm accuracy and completeness. Audit staff sampled accounts and compared reported balances to National Grid's general ledger and supporting documentation to ensure consistency.

- *Significant Accounting Matters* – Audit staff tested selected income statement accounts to ensure costs recorded complied with the USofA under 18 C.F.R. Part 367, including:

    - Labor and Outside Contractors – For a sample of direct charges, audit staff verified the account classification was correct. For a sample of indirect charges, audit staff evaluated the process for determining the classification of charges as overhead, and for accumulating and subsequently allocating those charges.

    - Advertising and Miscellaneous Expenses – For a sample of charges, audit staff verified the account classification was correct. Audit staff further tested payments of dues to industry associations to ensure no charges for lobbying were recorded in accounts where costs were recovered from ratepayers.

    - Depreciation and Amortization Expense – For a sample of charges, audit staff verified the account classification was correct. Audit staff also reviewed and tested how depreciation rates were developed and set up in the fixed assets system for monthly calculation of depreciation expense.

- *Preservation of Records* – Audit staff tested National Grid's administration of its records retention program to ascertain compliance, and interviewed employees to understand processes, procedures, and controls for maintenance of records. Audit staff tested selected records to determine whether retention periods aligned with Commission preservation of records regulations, and to test whether any records prematurely destroyed or lost were reported. Further, audit staff tested document retention practices to evaluate compliance with audit scope areas.

- *Cash Management Program* – Audit staff reviewed National Grid's oversight of its cash management program, including participants' compliance with cash management agreements and how the company ensures deposits and borrowings are restricted in accordance with Commission regulations.

- *Federal Income Taxes* – Audit staff evaluated National Grid's tax allocation agreements to understand how the company's tax liability is shared by the regulated and unregulated subsidiaries. Audit staff reviewed the calculation of deferred income taxes for accuracy and any effects on customer rates.

IV. Findings and Recommendations

1. Depreciation Expense of Service Companies' Assets

NGUSASCo and NGE&S used improper composite depreciation rates to determine depreciation expense accrued on certain property. This led the two service companies to accrue depreciation expense at rates not consistent with Commission accounting rules. The service companies then allocated and billed the incorrectly calculated depreciation expense to their public utility and nonutility affiliates. As a result, amounts billed to public utility affiliates with transmission formula rates were included in the rates charged to wholesale transmission customers.

Pertinent Guidance

- 18 C.F.R. § 367.20, Depreciation Accounting, states:

> (a) *Method.* Service companies must use a method of depreciation that allocates in a systematic and rational manner the service value of depreciable property over the service life of the property.
> (b) *Service lives.* Estimated useful service lives of depreciable property must be supported by objective evidence and analysis, including where appropriate engineering, economic, or other depreciation studies.
> (c) *Rate.* Service companies must use percentage rates of depreciation that are based on a method of depreciation that allocates the service value of depreciable property over the service life of the property. Where composite depreciation rates are used, they must be based on the weighted average estimated useful service lives of the depreciable property comprising the composite group.

Background

Pursuant to two service agreements, NGUSASCo and NGE&S allocated costs incurred that were associated with goods acquired and services performed on their behalf to National Grid and its subsidiaries. As part of an overall assessment of costs incurred and allocated to the service companies' public utility affiliates, audit staff evaluated whether depreciation expenses accrued on the service companies' property were calculated and accounted for in accordance with the Commission's accounting requirements. In addition, audit staff assessed the service companies' allocations of the expenses to their public utility affiliates and the inclusion of the expenses in the public utilities' transmission formula rate determinations. To accomplish this, audit staff reviewed the accuracy of input data used to calculate depreciation expense and subsequent allocation of the expense to public utility subsidiaries.

NGUSASCo and NGE&S applied composite depreciation rates to their long-lived property to allocate the service value of the property over its service life. The composite rates were determined based on a weighting of the average service lives of depreciable property, by asset class. NGUSASCo and NGE&S manually calculated the weighted average service life of their depreciable property for each class of assets. The weighted average service life data was then manually entered into the companies' PowerPlan asset management system.[1]

Audit staff evaluated a sample of transactions and found that in some instances NGUSASCo and NGE&S incorrectly calculated the weighted average service lives of their property. For example, the companies used an eight-year weighted average service life for a property class when it should have used 22 years. This resulted in incorrect information on the average service lives as inputs to PowerPlan. In addition, the companies entered rounded numbers into PowerPlan in some instances when they should have used exact numbers. These mistakes led the companies to accrue depreciation expenses using depreciation rates that were not consistent with Commission accounting rules, which require the use of depreciation rates that allocate the service value of property over its service life.

Accrued depreciation expenses computed using the incorrect depreciation rates were then recorded in Accounts 403, Depreciation Expense, and 403.1, Depreciation Expense for Asset Retirement Costs, on NGUSASCo's and NGE&S' books and billed to the public utility and nonutility affiliates. Amounts billed to public utility affiliates with transmission formula rates were included in wholesale transmission service cost determinations. In the cases of over accrued depreciation expense noted above, the public utilities overcharged their wholesale transmission formula rate customers.

Recommendations

[1] The PowerPlan asset management system provides project and work order management functionality including charge collection, budget assignment, project authorization, work order initiation, project estimating, project and work order monitoring/reporting, and closing.

We recommend that National Grid:

1. Conduct a full analysis of the weighted average service life calculations for each asset class and recalculate depreciation and amortization expense accrued during the audit period for service company property. Provide the results of the analysis and all applicable work papers supporting the analysis, including factors used to calculate the amount of the error, to DAA within 60 days of receiving the final audit report.

2. Submit proposed accounting entries based on the analysis performed pursuant to Recommendation No. 1 to DAA, within 60 days of receiving the final audit report, for the removal of over accrued depreciation and amortization expenses from Account 108, Accumulated Depreciation, and other accounts affected, such as the accumulated deferred income tax (ADIT) accounts.

3. Revise accumulated depreciation, ADIT, and other accounts impacted by the over accrued depreciation and amortization expenses after receiving DAA's assessment of the proposed accounting entries, and restate and footnote the balances in the FERC Form No. 60 for current and comparative years as necessary.

4. Revise policies, procedures, and practices to help ensure weighted average service lives are accurately calculated, reviewed, and entered into the asset management accounting system.

5. Train employees on the revised procedures and provide periodic training.

6. Submit a refund analysis to DAA, within 60 days of receiving the final audit report, that explains and details the following: (1) calculation of expenses that were inappropriately recovered through the public utilities' transmission formula rates; (2) components of the refunds; (3) refund method; (4) customers to receive refunds; and (5) the period(s) in which refunds will be made.

7. File a refund report with the Commission after receiving DAA's assessment of the refund analysis.

8. Refund amounts disclosed in the refund report to transmission formula rate customers, with interest calculated in accordance with section 35.19a of Commission regulations.

2. **Cost Allocation Methodologies**

NGUSASCo and NGE&S did not consistently apply their documented cost allocation methods, nor timely update their general ledger system to reflect changes in the allocation percentages actually used to bill affiliates. These errors led the service companies to over-allocate costs to certain National Grid public utility subsidiaries, and these public utilities in turn overbilled their respective wholesale transmission customers.

Pertinent Guidance

- 18 C.F.R. § 35.44, Protections Against Affiliate Cross-Subsidization, states in subsection (b)(3):

  (3) A franchised public utility that has captive customers or that owns or provides transmission service over jurisdictional transmission facilities, may only purchase or receive non-power goods and services from a centralized service company at cost.

- In Order No. 667, the Commission stated:

  [T]he Commission has a responsibility to ensure that the costs of non-power goods and services provided by a traditional, centralized service company to public utilities within the holding company system are just, reasonable, and not unduly discriminatory or preferential. [2]

  Further, the Commission stated:

  In reviewing centralized service company cost allocations, the Commission focus would be on the costs allocated to the jurisdictional public utilities, whether the jurisdictional public utilities are bearing their fair share of the costs vis-à-vis the non-regulated affiliates (i.e., whether the non-regulated affiliates are receiving an undue preference), and whether costs are fairly allocated among public utilities.[3]

---

[2] *Repeal of the Public Utility Holding Company Act of 1935 and Enactment of the Public Utility Holding Company Act of 2005*, Order No. 667, 113 FERC ¶ 61,248 at P 167 (2005), *order on reh'g*, Order No. 667-A, 115 FERC ¶ 61,096, *order on reh'g*, Order No. 667-B, 116 FERC ¶ 61,073 (2006), *order on reh'g,* Order No. 667-C, 118 FERC ¶ 61,133 (2007).

[3] *Id.*

Background

Audit staff performed tests to determine whether costs allocated by NGUSASCo and NGE&S to affiliates resulted in an appropriate allocation to affiliated public utilities. Specifically, audit staff reviewed National Grid's policies, procedures, and supporting documentation for its cost allocation methods. Primary documentation included National Grid's CAM, considered a reference and official documentation of cost allocators, and National Grid's master allocation spreadsheets, which were used to document the bases and calculation of percentages for the allocation of costs for each methodology in use.

Audit staff evaluated the CAM for reasonableness, completeness, and consistency with the supporting cost allocation studies. Further, audit staff compared the allocation methods documented in the CAM to those actually used, independently calculated allocation percentages for each allocation method, and compared audit staff's calculated percentages to those allocation percentages in the master allocation spreadsheets. Audit staff also tested a sample of allocation methods in the master allocation spreadsheets to verify their set up in the general ledger to determine whether amounts allocated to National Grid's public utility subsidiaries were recorded correctly. As discussed below, audit staff found that National Grid did not (1) consistently use the documented allocation methods from its CAM to allocate costs and (2) timely update its general ledger system to reflect changes in the allocation percentages actually used to bill affiliates, which led to over or under allocation of service company costs to certain National Grid public utility subsidiaries.

Documented Allocation Methods

National Grid's CAM is a document intended to support its allocation methodologies, and explains the manner in which costs are to be charged to affiliates that receive services from NGUSASCo and NGE&S. The CAM was developed as part of a cost study performed by a consultant in 2012 and was updated in 2014. National Grid continues to refine and revise the CAM as organizational changes arise. National Grid informed audit staff that only new allocation bases require formal approval from National Grid's regulatory department, i.e., approvals are not required for mere changes in department names or names of allocators.

Audit staff compared the allocators approved for use and included in the six master allocation spreadsheets covering the audit period to the allocators in the CAM for the same time frame. Audit staff found allocators listed in the CAM that were not included in the master allocation spreadsheet, and vice versa. Audit staff also found a new allocator used in the audit period titled "RTU" with no evidence of its approval by National Grid's regulatory department. Combined allocated costs for the RTU allocator in 2014 and 2015 were approximately $4.8 million, and all were allocated to National Grid's public utility subsidiaries.

General Ledger System Updates

National Grid's service company cost allocation methods were developed using allocation bases that are supported by defined methodologies. The bases and methodologies were established using cost drivers that include input data and balances from fiscal year-end (e.g. number of employees, number of customers, etc.). National Grid's cost allocation procedures require updates to the cost drivers at least annually at the start of each fiscal year so that costs are allocated in a fair and equitable manner, reflect changes in the business, and result in the pricing of goods and services at cost. To do this, National Grid created a new version of its master allocation spreadsheet to reflect the updated cost drivers and calculated updated percentages for each allocation method. Then, National Grid's cost allocation procedures required it to input the updated percentages into its accounting system so that all allocated costs are based on current data and result in allocations that are consistent with documented methodologies and supporting studies.

Audit staff found National Grid did not follow its procedures to timely update allocation percentages in its accounting system. As a result, allocated costs were not based on current cost drivers and resulted in allocations that were inconsistent with the documented methodologies and supporting studies. Audit staff determined that for the month of August 2013, the service companies over-allocated several hundred thousand dollars to their public utility affiliates.

Audit staff determined National Grid did not follow its procedures to update the general ledger system for the period April 2013 through March 2015. Audit staff notes that the National Grid service companies billed affiliates for non-power goods and services in the same manner and at similar volume throughout this period, reflecting the lack of updates. National Grid acknowledges that from April 2013 through March 2015, updates to the general ledger system for allocations were not done on a timely basis.

Recommendations

We recommend that National Grid:

9. Strengthen policies and procedures to ensure revised allocation percentages are updated in the general ledger system and implemented on a timely basis.

10. Strengthen policies and procedures for formally approving the use of new allocators.

11. Train staff on the new policies and procedures for updating allocation percentages.

12. Quantify the dollars over or under allocated for the period April 2013 through March 2015.

13. Submit a refund analysis to DAA, within 60 days of receiving the final audit report, that explains and details the following: (1) calculation of allocated service company costs that were inappropriately recovered through the public utilities' transmission formula rates in the audit period; (2) components of the refunds to be made as a result of the calculation; (3) refund method; (4) customers to receive refunds; and (5) the period(s) in which refunds will be made.

14. File a refund report with the Commission after receiving DAA's assessment of the analysis.

15. Refund amounts disclosed in the refund report to wholesale transmission customers, with interest calculated in accordance with section 35.19a of Commission regulations.

3. **Industry Association Dues**

NGUSACo improperly accounted for and allocated a portion of the cost of its gas and electric industry associations' membership dues to National Grid's public utility subsidiaries. As a result, National Grid's public utility subsidiaries improperly included the lobbying component of industry association payments in their wholesale transmission rates.

Pertinent Guidance

- 18 C.F.R. § 367.4264, Account 426.4, Expenditures for Certain Civic, Political and Related Activities, states in part:

  (a) This account must include expenditures for the purpose of influencing public opinion with respect to the election or appointment of public officials, referenda, legislation, or ordinances (either with respect to the possible adoption of new referenda, legislation or ordinances or repeal or modification of existing referenda, legislation or ordinances) or approval, modification, or revocation of franchises; or for the purpose of influencing the decisions of public officials.

- 18 C.F.R. § 367.9302, Account 930.2, Miscellaneous General Expenses, states in part:

  (c) This account must include the following expenses items:
  (1) Industry association dues for company memberships.

- 18 C.F.R. § 367.28, Methods of Allocation, states:

  Indirect costs and compensation for use of capital must be allocated to projects in accordance with the service company's applicable and currently effective methods of allocation. Both direct and allocated indirect costs on projects must be assigned among those companies in the same manner. The cost accumulation system must identify the methods of allocation and the accounts to be charged. Companies must be notified in writing of any change in the methods of allocation.

Background

NGUSASCo paid membership dues on behalf of National Grid and its affiliates that were members of gas and electric industry associations. In accordance with the service agreement between NGUSASCo and its affiliates, the amounts paid were required to be allocated to the affiliates that owned and operated natural gas or electric systems. These membership dues included a portion of costs for lobbying by the associations on behalf of their members, which should be recorded in Account 426.4, Expenditures for Certain Civic, Political and Related Activities. Audit staff performed tests to determine whether the membership dues and the lobbying component were properly accounted for by NGUSASCo, appropriately allocated to affiliates, and correctly accounted for by the operating companies.

Misclassification of Industry Association Dues

Audit staff found that NGUSASCo improperly accounted for its gas industry association payments from 2013 through 2015. In those years, NGUSASCo recorded the entirety of the payments, including the lobbying portion, in Account 921, Office Supplies and Expense. Audit staff also found that from 2015 to 2018, NGUSASCo recorded the membership dues, excluding the lobbying-related portion, of its electric industry association payments in Account 921. The lobbying-related portion was recorded in Account 426.4.

Under the Commission's accounting requirements, the membership dues, excluding the lobbying-related portion of the expenses, should have been charged to Account 930.2, Miscellaneous General Expenses, and the lobbying portion should have been charged to Account 426.4. According to the Commission's accounting regulations, Account 930.2 should include industry association dues for company memberships. Further, Account 426.4 provides for the inclusion of expenditures incurred for the purpose of influencing public opinion, such as lobbying.

Improper Allocation Among Affiliates

Audit staff found that NGUSASCo either did not allocate or allocated the wrong amount of the gas and electric industry associations' membership dues among its natural gas and public utility affiliates that were members of those associations. This practice was not consistent with the then-effective allocation methods and, as such, was not consistent with the Commission's regulations. 18 C.F.R. § 367.28, Methods of Allocation, requires indirect costs to be allocated to affiliates in accordance with NGUSASCo's applicable and currently effective methods of allocation. The inconsistently applied methodology was noted by audit staff across all companies and in many accounts, in addition to the previously discussed misclassification of industry association dues. For example, from 2013 through 2015, Narragansett Gas Company and NG LNG LP were not allocated any of the costs of gas industry association membership dues. Further, from 2016 to 2018, NGUSASCo changed to an allocation method that continued to exclude NG LNG LP in the same manner.

Similar errors occurred with electric industry association membership dues allocated by NGUSASCo to public utility affiliates. From 2013 to 2018, allocations of membership dues to all affiliates that were members of the electric industry association incorrectly excluded several companies in various years.

As a result of the allocation errors, the gas and electric industry associations' membership dues were incorrectly included in or excluded from, as applicable, the operating costs of natural gas and public utility affiliates. This resulted in over or under allocation of the expenses to those entities, some of which use wholesale formula rates. NGUSASCo's allocation practices caused certain companies to subsidize the costs of others' industry association dues.

Recommendations

We recommend that National Grid:

16. Strengthen policies and procedures to ensure industry association dues are accounted for in accordance with the Commission's regulations, in particular the regulations pertaining to lobbying costs.

17. Strengthen policies and procedures to ensure costs incurred by the service companies relating to industry association dues are reallocated to the public utilities in compliance with NGUSASCo's allocation methodology.

18. Train staff on the revised procedures for recording, accounting for, and allocating costs related to industry association dues.

19. Submit a refund analysis, within 60 days of receiving the final audit report, to DAA that explains and details the following: (1) calculation of refunds that resulted from the improper accounting and allocation of the costs of membership dues during the audit period, including interest; (2) determinative components of the refund; (3) refund method; (4) customers to receive refunds: and (5) period(s) in which refunds will be made.

20. File a refund report with the Commission after receiving DAA's assessment of the analysis.

21. Refund amounts disclosed in the refund report to wholesale customers, with interest calculated in accordance with section 35.19a of the Commission's regulations.

4. **Donations**

NGUSASCo improperly recorded certain donations to Account 921, Office Supplies and Expenses, and Account 930.2, Miscellaneous General Expenses, instead of Account 426.1, Donations, as required by Commission regulations. Amounts recorded in Accounts 921 and 930.2 were allocated to National Grid's public utility subsidiaries and other affiliates and accounted for by the entities using the same accounts, and for some public utility subsidiaries were included as inputs to their respective wholesale transmission formula rate cost recovery mechanisms. As a result, in some years National Grid's public utility subsidiaries improperly included the donations in their wholesale transmission rates.

Pertinent Guidance

- 18 C.F.R. § 367.4261, Account 426.1, Donations, states:

  This account must include all payments or donations for charitable, social or community welfare purposes.

- Letter Order, *Transcontinental Gas Pipe Line Corp*., Docket No. AC06-1-000 (Nov. 1, 2006), states in part:

  A *voluntary* mitigation payment or contribution, conversely, is not a payment necessary for construction and must be treated as a payment made for charitable, social or community welfare purposes and charged to Account 426.1, Donations.

Background

National Grid was a member of an electric industry association and was billed for annual membership dues, a portion of which was designated as a charitable contribution. Specifically, in each year from 2013 to 2017, NGUSASCo made a charitable contribution of $30,000 through the association. NGUSASCo recorded the payments to Account 921, Office Supplies and Expenses, or Account 930.2, Miscellaneous General Expenses. The payments were charged to Account 930.2 in 2013 and 2014 and to Account 921 in 2015, 2016, and 2017. The amounts charged to Accounts 930.2 and 921 were then allocated to National Grid's electric affiliates, some of which had transmission formula rates, which recorded the charitable donations using the same accounts. The electric industry association invoices identified the donations as contributions to a foundation that is a "501(c)(3) educational and charitable organization." The public utility subsidiaries with transmission formula rates included these donation amounts in the rates billed to their transmission customers.

In 2014, NGUSASCo also contributed $25,000 to a research institute it described as "co-funding" for a program aimed at encouraging high school students to pursue electrical engineering careers. NGUSASCo recorded the donation in Account 930.2, Miscellaneous General Expenses. The amounts paid were then allocated to National Grid's public utility subsidiaries, which recorded the donations using the same account.

National Grid stated it considers the donation to the research institute a "long term investment in potential future employees and that it is an indirect business expense to support ratepayers rather than a public relations effort to benefit shareholders." It also stated "the educational initiative aims to produce a workforce that is trained in new technologies, so that recent graduates can be hired by utilities, including National Grid." However, the Commission has found that such voluntary contributions should be accounted for as a non-operating expense.[4] Specifically, the Commission has directed such expenses be accounted for in Account 426.1, consistent with the instructions for that account. Account 426.1 provides for the recording of all payments or donations for charitable, social or community welfare purposes.

Distinguishing amounts required to be recorded in Accounts 921 and 930.2 from amounts required to be recorded in Account 426.1 is important because expenses in Accounts 921 and 930.2 are included in the calculation of the public utility subsidiaries' respective annual transmission rates; whereas, amounts recorded in Account 426.1 generally are not. By including the donations in Accounts 921 and 930.2 instead of in

---

[4] *See* Letter Order, *Transcontinental Gas Pipe Line Corp.*, Docket No. AC06-1-000 (Nov. 1, 2006). *See also Williston Basin Interstate Pipeline Co.*, 95 FERC ¶ 63,008 at 65,095 (2001) (rejecting inclusion of civic and charitable donations in cost of service even where the donations were made to local charities benefiting communities served by the utility and "represent[ed] a minimal amount of the overall cost of service"), *aff'd in relevant part, and rev. in part*, 104 FERC ¶ 61,036, at P 65 (2003) (even if ratepayers chose charities to which utility made contributions "and there was such a demonstrable connection between the charities and the ratepayers," this does not "overcome[] the conclusion that such costs are not operating expenses and bear no relationship to the necessary costs of providing utility service."); *id.* P 65 n.89 stating:

> Because our policy of denying inclusion of charitable contributions in a pipeline's cost of service is premised upon such contributions being primarily for the benefit of a company's shareholders, and that they are not operating expenses and bear no relationship to the necessary costs of providing utility service, a pipeline has a heavy burden indeed in including any amounts for charitable contributions in its cost of service.

Account 426.1, NGUSASCo and National Grid's affiliates were not in compliance with the Commission's accounting requirements, which led to over billings in some of the public utility subsidiaries' wholesale transmission formula rates.

Recommendations

We recommend that National Grid:

22. Perform a review of all payments made to industry associations, organizations such as research institutes, voluntary charitable contributions, including mitigation payments, and other voluntary donations for the audit period to ensure all donations are accounted for properly.

23. Strengthen policies and procedures to ensure that voluntary payments to industry associations, organizations such as research institutes, charitable contributions, including voluntary mitigation payments, and other donations are accounted for in accordance with Commission regulations.

24. Provide training to staff on the revised policies for accounting for charitable contributions and other donations.

25. Submit a refund analysis, within 60 days of receiving the final audit report, to DAA for review that explains and details the following: (1) calculation of refunds that resulted from improper accounting for donations during the audit period, including interest; (2) determinative components of the refund; (3) refund method; (4) customers to receive refunds: and (5) period(s) in which refunds will be made.

26. File a refund report with the Commission after receiving DAA's assessment of the analysis.

27. Refund amounts disclosed in the refund report to wholesale customers, with interest calculated in accordance with section 35.19a of the Commission's regulations.

5. Service Company Account Misclassifications

NGUSASCo improperly accounted for various administrative and general expenses in its books and records. As a result, NGUSASCo overstated certain administrative and general accounts it billed to National Grid public utility subsidiaries, resulting in misclassifications reported in the public utilities' FERC Form No. 1.

Pertinent Guidance

- 18 C.F.R. § 367.9200, Account 920, Administrative and General Salaries, states:

  (a) This account must include salaries, wages, bonuses and other consideration for services, with the exception of director's fees paid directly to officers and employees of the service company.
  (b) This account must be supported by time records and appropriately referenced to detailed records subdividing salaries and wages by departments or other functional organization units.

- 18 C.F.R. § 367.9210, Account 921, Office Supplies and Expense, states in part:

  (a) This account must include office supplies and expenses incurred in connection with the general administration of service company operations assignable to specific administrative or general departments and not specifically provided for in other accounts. This includes the expenses of the various administrative and general departments, the salaries and wages of which are included in account 920, Administrative and general salaries (§ 367.9200).

- 18 C.F.R. § 367.9350, Account 935, Maintenance of Structures and Equipment, states in part:

  This account must include materials used and expenses incurred in the maintenance of property owned, the cost of which is included in accounts 390 through 399 (§§ 367.3900 through 367.3990), and of property leased from others.

Background

Audit staff tested amounts recorded by National Grid's service company, NGUSASCo, in A&G expense accounts. To test whether NGUSASCo's accounting was consistent with Commission requirements, audit staff selected a sample of transactions from the months of August 2013 and December 2014. The sample focused on transactions allocated to National Grid's public utility subsidiaries. To verify proper

FERC account classification, audit staff discussed transactions with National Grid employees and reviewed source documentation for each.

Audit staff's testing identified transactions that were not posted to the correct FERC accounts, as outlined in the following table.

Expense Description	Month	Account Charged	Correct Account	
			Number	Description
Employee labor	Dec 2014	921	920	A&G Salaries
Employee travel	Dec 2014	926	921	Office Supplies and Expenses
Communications	Dec 2014	930.2	921	Office Supplies and Expenses
Software maintenance	Aug 2013	930.2	935	Maintenance of Structures and Equipment

National Grid acknowledged these A&G accounting misclassifications and explained they occurred for various reasons, including administrative oversights and typographical errors. Audit staff notes that the misclassifications at the operating companies had no effect on wholesale transmission customer rates. However, audit staff believes the errors show the need for National Grid to strengthen its accounting policies and procedures to ensure proper classification and affiliate billing of A&G expenses.

Recommendations

We recommend that National Grid:

28. Strengthen accounting policies and procedures to ensure that service company costs, and by association operating company costs, are recorded in the correct FERC accounts.

29. Train employees on the updated policies and procedures for recording A&G expenses to FERC accounts.

6. Reporting of Transactions with Associated (Affiliated) Companies

National Grid's public utility subsidiaries did not follow the instructions on page 429, Transactions with Associated (Affiliated) Companies, of the FERC Form No. 1 and as a result reported inaccurate and incomplete information for transactions with associated companies.

Pertinent Guidance

- The instructions on the Transactions with Associated (Affiliated) Companies schedule of the FERC Form No. 1 state:

> 1. Report below the information called for concerning all non-power goods or services received from or provided to associated (affiliated) companies.
>
> 2. The reporting threshold for reporting purposes is $250,000. The threshold applies to the annual amount billed to the respondent or billed to an associated/affiliated company for non-power goods and services. The good or service must be specific in nature. Respondents should not attempt to include or aggregate amounts in a nonspecific category such as "general."
>
> 3. Where amounts billed to or received from the associated (affiliated) company are based on an allocation process, explain in a footnote.[5]

Background

Audit staff reviewed the FERC Form No. 1 reports submitted by National Grid's public utility subsidiaries during the audit period, including those for NiMo, MECO, NEP, and Narragansett. This review focused on page 429, Transactions with Associated (Affiliated) Companies. The instructions on that page require public utilities to disclose non-power goods and services provided by, or received from, affiliated companies during the calendar year, including descriptions of these goods or services, affiliate names, accounts used to record the transactions, amounts charged, and allocation methods used. Audit staff identified several reporting deficiencies, discussed below.

---

[5] FERC, *FERC Financial Report FERC Form No. 1: Annual Report of Major Electric Utilities,* at 426, available at www.ferc.gov/docs-filing/forms/form-1/form-1.pdf.

Audit staff discovered that each National Grid public utility subsidiary reported on page 429 all costs billed between it and its affiliates, contrary to the instructions that require companies to report only non-power goods and services. This overstated the total amount of non-power goods and services provided and received by each National Grid public utility subsidiary.

Audit staff further found that each public utility did not identify the specific non-power goods and services provided to and received from its respective affiliates. The instructions require descriptions of the good or service to be specific in nature, and not included or aggregated in nonspecific categories such as "general." However, the National Grid public utility subsidiaries reported aggregate totals of the costs billed, by affiliate, on the page and reported in a footnote breakdowns of each total by cost type. This method of reporting did not identify the specific nature of the goods and services provided and received, and included nonspecific categories such as "labor" and "other."

Finally, audit staff found that National Grid's service companies, NGUSASCo and NGE&S, billed certain non-power goods and services to the National Grid public utility subsidiaries based on allocation methods. However, the public utility subsidiaries did not explain in a footnote the allocation processes used, as required by the instructions.

These errors occurred for various reasons, including administrative oversights, misinterpretation of the instructions, and ineffective coordination between National Grid's FERC Form No. 1 and FERC Form No. 60 reporting staffs.

Recommendations

We recommend that National Grid:

30. Strengthen policies and procedures, to include a reconciliation to the FERC Form No. 60 for those non-power goods and services provided by the service companies, to ensure that its public utility subsidiaries accurately, completely, and consistently prepare the schedule on page 429 of the FERC Form No. 1 according to instructions.

7. FERC Form No. 60 Reporting

NGUSASCo and NGE&S did not complete the FERC Form No. 60 reports filed during the audit period in accordance with the general and schedule instructions of the form.

Pertinent Guidance

- 18 C.F.R. § 366.23(a)(1), FERC Form No. 60, Annual Reports of Centralized Service Companies, states in part,

  > Every report must be submitted on the FERC Form No. 60 then in effect and must be prepared in accordance with the instructions incorporated in that form.

- 18 C.F.R. § 369.1(b)(2)(ii), FERC Form No. 60, Annual Report of Centralized Service Company, states in part:

  > (ii) The annual report in effect must be filed with the Commission as prescribed in § 385.2011 of this chapter and as indicated in the General Instructions set out in the form, and must be properly completed and verified.

- The instructions to the FERC Form No. 60 Schedule IV, Investments, state in part, "(2) For temporary cash investments (Account 136), list each investment separately in a footnote."

- The instructions to the FERC Form No. 60 Schedule XI-Proprietary Capital, state,

  > (1) For miscellaneous paid-in capital (Account 211) and appropriated retained earnings (Account 215), classify amounts in each account, with a brief explanation, disclosing the general nature of transactions which give rise to the reported amounts.
  >
  > (2) For the unappropriated retained earnings (Account 216), in a footnote, give particulars concerning net income or (loss) during the year, distinguishing between compensation for the use of capital owed or net loss remaining from servicing non-associates per the General Instructions of the Uniform System of Accounts. For dividends paid during the year in cash or otherwise, provide rate percentages, amount of dividend, date declared and date paid.

- The instructions to the FERC Form No. 60 Schedule XVI-Analysis of Charges for Service-Associate and Non-Associate Companies state:

  (1) Total cost of service will equal for associate and nonassociate companies the total amount billed under their separate analysis of billing schedules.

- The instructions to the FERC Form No. 60 Schedule XVIII-Analysis of Billing Non-Associate Companies, state in part:

  (1) For services rendered to nonassociate companies (Account 458), list all of the nonassociate companies. In a footnote, describe the services rendered to each respective nonassociate company.

- The instructions to the FERC Form No. 60 Schedule XX-Organization Chart, state in part:

  (1) Provide a graphical presentation of the relationships and inter relationships within the service company that identifies lines of authority and responsibility in the organization.

- The instructions to the FERC Form No. 60 Schedule XXI, Methods of Allocation, state in part:

  (1) Indicate the service department or function and the basis for allocation used when employees render services to more than one department or functional group.

Background

The FERC Form No. 60 instructions are meant to guide FERC filers and ensure consistent presentation of data, essential in providing users a standard against which to evaluate a service company's performance and financial condition relative to others. Audit staff reviewed NGUSASCo's and NGE&S's 2014 FERC Form No. 60 in detail to determine whether information in the reports was complete, accurate, and followed the form's general and schedule instructions. Audit staff identified multiple reporting deficiencies in 2014, and subsequently expanded its testing to the 2013, 2015, 2016 and 2017 FERC Form No. 60s. Testing revealed the reporting deficiencies described below relating to (1) disclosure of the methods used to allocate costs to affiliates on Schedule XXI – Methods of Allocation and (2) adherence with various other schedule and page instructions.

Reporting of Cost Allocation Methodologies

Audit staff reviewed cost allocation methods and costs billed to affiliates during the audit period to determine whether the methodologies reported by NGUSASCo and NGE&S on Schedule XXI – Methods of Allocation, in the FERC Form No. 60, were complete and accurate. Audit staff compared and tested the allocation methods disclosed in the FERC Form No. 60 to (1) the allocation methods outlined in NGUSASCo's and NGE&S's cost allocation manuals to test consistency and transparency and (2) the allocation percentages contained in National Grid's master allocation spreadsheets, used to determine the costs billed to affiliates.

Audit staff cross-referenced the methodologies outlined in the cost allocation manuals to those reported in the 2014 FERC Form No. 60, Schedule XXI, and noted instances where the names of affiliates reported in the FERC Form No. 60 differed from those listed in the CAM and from those used in actual allocations during the year. National Grid acknowledged the deficiencies and explained that an outdated version of the CAM was used to populate the 2014 FERC Form No. 60.

Audit staff next compared the allocation methodologies in the master allocation spreadsheets to those in the 2013 through 2015 NGUSASCo and NGE&S FERC Form No. 60. The spreadsheets cover the audit period and document the bases and calculation of percentages for the allocation of costs for each methodology in use during the respective spreadsheet's timeframe. Audit staff quantified the dollars allocated for the methodologies according to the spreadsheets that were not reported in the FERC Form No. 60. Two methodologies, responsible for allocations totaling $15.1 million, were not disclosed.

National Grid management acknowledged the reporting omissions and explained they were largely due to the two documents not being updated concurrently, resulting in the FERC Form No. 60 being inconsistent with the actual allocation methods used.

FERC Form No. 60 Reporting Deficiencies

Audit staff reviewed the 2014 NGUSASCo and NGE&S Form No. 60 in detail to evaluate whether they were completed according to the instructions included therein. For those schedules found to be not compliant, testing was expanded to include the 2013, 2015, 2016, and 2017 filings.

Audit staff found the following deficiencies:

- NGUSASCo omitted a footnote to separately list temporary cash investments, as required on Schedule IV-Investments, in 2014, 2015, and 2017.
- NGUSASCo omitted a footnote to describe services rendered to each company listed, as required on Schedule XVIII-Analysis of Billing Non-Associate Companies, in 2014.
- For amounts reported in Account 211, Miscellaneous Paid-In Capital, NGUSASCo did not describe the transactions or the general nature of transactions giving rise to the reported amounts, and detail was not provided in a footnote of net income/loss and dividends, as required on Schedule XI-Proprietary Capital, in 2013 and 2014. Audit staff found these same deficiencies for NGE&S in each year during the audit period.
- The total cost of services reported by NGUSASCo and NGE&S on Schedule XVI-Analysis of Charges for Service-Associate and Non-Associate Companies did not equal the total amount billed under separate analyses of billing schedules, for each year during the audit period.
- The organizational chart reported by NGUSASCo and NGE&S did not identify the lines of authority and responsibility, as required by Schedule XX-Organization Chart, in each year during the audit period.

These errors occurred for a number of reasons, including inadvertent administrative oversight and a lack of sufficient procedures for the review and verification of information reported on the form. Subsequently to stabilizing its accounting system, National Grid implemented general financial reporting enhancements. However, audit staff believes the errors identified indicate the need for National Grid to more precisely enhance procedures and controls for NGUSASCo and NGE&S so that the companies follow all FERC Form No. 60 instructions.

Recommendations

We recommend that National Grid:

31. Enhance procedures and controls for submitting NGUSASCo’s and NGE&S’s FERC Form No. 60 to ensure the forms are accurate, complete, and prepared according to all instructions.

32. Train employees responsible for the FERC Form No. 60 on the new procedures to ensure accurate and complete reporting that is compliant.

National Grid's Response to Draft Audit Report

nationalgrid

October 30, 2019

Steven D. Hunt
Director and Chief Accountant
Division of Audits and Accounting
Office of Enforcement
Federal Energy Regulatory Commission
888 First Street, NE, Room 5K-13
Washington, DC 20426

Re: Docket No. FA16-2-000

Dear Mr. Hunt:

National Grid USA ("National Grid" or "the Company") has carefully reviewed Audit Staff's October 15, 2019 draft Audit Report in the above-referenced docket addressing National Grid's compliance with: (1) cross subsidization restrictions on affiliate transactions under 18 C.F.R. Part 35; (2) accounting, recordkeeping, and reporting requirements under 18 C.F.R. Part 366; (3) preservation of records requirements for holding companies and service companies; (4) Uniform System of Accounts for Centralized Service Companies under 18 C.F.R. Part 368; and (5) associated public utilities' compliance with accounting requirements of the Federal Energy Regulatory Commission ("FERC" or "Commission") for transactions with associated companies under 18 C.F.R. Part 101 and the applicable reporting requirements in the FERC Form 1 under 18 C.F.R. Part 141.

The following details National Grid's responses to each Recommendation contained in the draft Audit Report. National Grid agrees with the Audit Report findings and recommendations and agrees to implement those recommendations. National Grid believes that the comments provided below are consistent with discussions we have had with Audit Staff. We are, of course, happy to discuss these further as well as provide any additional information that Audit Staff would find helpful.

As is noted in the draft Audit Report, the audit covered the period from January 1, 2013 through December 31, 2018. Concurrently with the audit and in the years that have followed the data collection period for the audit, the Company has self-identified and begun to correct issues contributing to the findings that are listed in the draft Audit Report. The Company has undertaken broad measures toward remediating concerns and driving continuous improvement into the future. Specifically, the Company implemented a "Finance Remediation Plan" that

Steven Hunt
Director and Chief Accountant
October 30, 2019
Page 2

addressed SAP stabilization and immediate post go-live issues and the areas impacted as well as the "Accounting Controls Enhancement" (ACE) Program that is noted in the draft Audit Report (a longer-term program focused on improvements to the control environment more broadly). The stabilization of SAP was completed in November 2014 and the Finance Remediation Plan allowed National Grid to resume timely filing of its FERC financial forms in 2014, as is noted in the draft Audit Report. The ACE Program continued to run after this date and included various components: controls over plant accounting; controls over revenue accounting; controls over regulatory asset and liability accounting; controls over the financial reporting process; and the establishment of a dedicated work stream lead overseeing each of these components as well as the remediation of the identified issues. All control issues identified and managed through the ACE Program were cleared by the spring of 2018 (as validated by National Grid's external auditors).

As is stated in the Company's below responses to the draft Audit Reports' specific findings, National Grid accepts the findings identified by FERC Audit Staff during this process and acknowledges that further updates and improvements in National Grid's control environment are required as recommended. The Company notes, however, that significant process has been achieved to date through the Finance Remediation Plan and the ACE Program.

National Grid will establish a team to lead the implementation of the recommendations outlined in the draft Audit Report and expects that all recommendations will be implemented within one year of issuance of the final Audit Report, if not sooner. The Company will work with Audit Staff to update the progress of implementation through the compliance reporting process outlined in the draft Audit Report.

I. FINDING 1: Depreciation Expense of Service Companies' Assets

Recommendation No. 1:
Conduct a full analysis of the weighted average service life calculations for each asset class and recalculate depreciation and amortization expense accrued during the audit period for service company property. Provide the results of the analysis and all applicable work papers supporting the analysis, including factors used to calculate the amount of the error, to the Division of Audits and Accounting ("DAA") within 60 days of receiving the final audit report.

Recommendation No. 2:
Submit proposed accounting entries based on the analysis performed pursuant to Recommendation No. 1 to DAA, within 60 days of receiving the final audit report, for the removal of over accrued depreciation and amortization expenses from Account 108,

Steven Hunt
Director and Chief Accountant
October 30, 2019
Page 4

With respect to Recommendation Nos. 4 and 5, National Grid will revise its policies, procedures, and practices to help ensure weighted average service lives are accurately calculated, reviewed, and entered into the asset management accounting system. The Company will provide training to employees on the revised procedures and will provided periodic training.

With respect to Recommendation Nos. 6, 7, and 8, National Grid will provide a refund analysis to DAA as recommended, will file a refund report following DAA's assessment, and will issue refunds as necessary. National Grid will provide this analysis to DAA within 60 days of the issuance of the final Audit Report in this docket.

II. FINDING 2: Cost Allocation Methodologies

Recommendation No. 9:
Strengthen policies and procedures to ensure revised allocation percentages are updated in the general ledger system and implemented on a timely basis.

Recommendation No. 10:
Strengthen policies and procedures for formally approving the use of new allocators.

Recommendation No. 11:
Train staff on the new policies and procedures for updating allocation percentages.

Recommendation No. 12:
Quantify the dollars over or under allocated for the period April 2013 through March 2015.

Recommendation No. 13.
Submit a refund analysis to DAA, within 60 days of receiving the final audit report, that explains and details the following: (1) calculation of allocated service company costs that were inappropriately recovered through the public utilities' transmission formula rates in the audit period; (2) components of the refunds to be made as a result of the calculation; (3) refund method; (4) customers to receive refunds; and (5) the period(s) in which refunds will be made.

Recommendation No. 14:
File a refund report with the Commission after receiving DAA's assessment of the analysis.

Recommendation No. 15:
Refund amounts disclosed in the refund report to wholesale transmission customers, with interest calculated in accordance with section 35.19a of Commission regulations.

Steven Hunt
Director and Chief Accountant
October 30, 2019
Page 3

Accumulated Depreciation, and other accounts affected, such as the accumulated deferred income tax (ADIT) accounts.

Recommendation No. 3:
Revise accumulated depreciation, ADIT, and other accounts impacted by the over accrued depreciation and amortization expenses after receiving DAA's assessment of the proposed accounting entries, and restate and footnote the balances in the FERC Form No. 60 for current and comparative years as necessary.

Recommendation No. 4:
Revise policies, procedures, and practices to help ensure weighted average service lives are accurately calculated, reviewed, and entered into the asset management accounting system.

Recommendation No. 5:
Train employees on the revised procedures and provide periodic training.

Recommendation No. 6:
Submit a refund analysis to DAA, within 60 days of receiving the final audit report that explains and details the following: (1) calculation of expenses that were inappropriately recovered through the public utilities' transmission formula rates; (2) components of the refunds; (3) refund method; (4) customers to receive refunds; and (5) the period(s) in which refunds will be made.

Recommendation No. 7:
File a refund report with the Commission after receiving DAA's assessment of the refund analysis.

Recommendation No. 8:
Refund amounts disclosed in the refund report to transmission formula rate customers, with interest calculated in accordance with section 35.19a of Commission regulations.

National Grid Response:

With respect to Recommendation Nos. 1, 2, and 3, National Grid will conduct a full analysis of the weighted average service life calculations for each asset, will recalculate depreciation and amortization expense accrued during the audit period for service company property, and will share the results with the Commission Office of Enforcements' Division of Audits and Accounting (DAA), including proposed accounting entries for the removal of over accrued depreciation and amortization expenses from appropriate accounts. The Company will revise impacted accounts for the current period following DAA's assessment, and will restate, and provide explanatory footnotes to, the balances as necessary in the next FERC Form 60 filing.

Steven Hunt
Director and Chief Accountant
October 30, 2019
Page 4

With respect to Recommendation Nos. 4 and 5, National Grid will revise its policies, procedures, and practices to help ensure weighted average service lives are accurately calculated, reviewed, and entered into the asset management accounting system. The Company will provide training to employees on the revised procedures and will provided periodic training.

With respect to Recommendation Nos. 6, 7, and 8, National Grid will provide a refund analysis to DAA as recommended, will file a refund report following DAA's assessment, and will issue refunds as necessary. National Grid will provide this analysis to DAA within 60 days of the issuance of the final Audit Report in this docket.

II. FINDING 2: Cost Allocation Methodologies

Recommendation No. 9:
Strengthen policies and procedures to ensure revised allocation percentages are updated in the general ledger system and implemented on a timely basis.

Recommendation No. 10:
Strengthen policies and procedures for formally approving the use of new allocators.

Recommendation No. 11:
Train staff on the new policies and procedures for updating allocation percentages.

Recommendation No. 12:
Quantify the dollars over or under allocated for the period April 2013 through March 2015.

Recommendation No. 13.
Submit a refund analysis to DAA, within 60 days of receiving the final audit report, that explains and details the following: (1) calculation of allocated service company costs that were inappropriately recovered through the public utilities' transmission formula rates in the audit period; (2) components of the refunds to be made as a result of the calculation; (3) refund method; (4) customers to receive refunds; and (5) the period(s) in which refunds will be made.

Recommendation No. 14:
File a refund report with the Commission after receiving DAA's assessment of the analysis.

Recommendation No. 15:
Refund amounts disclosed in the refund report to wholesale transmission customers, with interest calculated in accordance with section 35.19a of Commission regulations.

Steven Hunt
Director and Chief Accountant
October 30, 2019
Page 5

National Grid Response:

With respect to Recommendation Nos. 9, 10, and 11, National Grid will strengthen: (1) policies and procedures to ensure timely and accurate ledger updates for revised allocation percentages, and (2) policies and procedures for formally approving the use of new allocators. The Company will provide training to employees on new policies and procedures for updating allocation percentages.

With respect to Recommendation Nos. 12, 13, 14, and 15, National Grid will quantify the dollars over or under allocated for the designated period, will provide a refund analysis to DAA as recommended, will file a refund report following DAA's assessment, and will issue refunds as necessary.

III. FINDING 3: Industry Association Dues

Recommendation No. 16:
Strengthen policies and procedures to ensure industry association dues are accounted for in accordance with the Commission's regulations, in particular the regulations pertaining to lobbying costs.

Recommendation No. 17:
Strengthen policies and procedures to ensure costs incurred by the service companies relating to industry association dues are reallocated to the public utilities in compliance with NGUSASCo's allocation methodology.

Recommendation No. 18:
Train staff on the revised procedures for recording, accounting for, and allocating costs related to industry association dues.

Recommendation No. 19:
Submit a refund analysis, within 60 days of receiving the final audit report, to DAA that explains and details the following: (1) calculation of refunds that resulted from the improper accounting and allocation of the costs of membership dues during the audit period, including interest; (2) determinative components of the refund; (3) refund method; (4) customers to receive refunds: and (5) period(s) in which refunds will be made.

Recommendation No. 20:
File a refund report with the Commission after receiving DAA's assessment of the analysis.

Steven Hunt
Director and Chief Accountant
October 30, 2019
Page 6

Recommendation No. 21:
Refund amounts disclosed in the refund report to wholesale customers, with interest calculated in accordance with section 35.19a of the Commission's regulations.

National Grid Response:

With respect to Recommendation Nos. 16, 17, and 18, National Grid has strengthened policies and procedures to ensure industry association dues and lobbying costs are correctly accounted for and are reallocated properly in accordance with the Company's allocation methodology and will review improvements with Audit Staff. The Company has provided some training to employees on new policies and procedures for updating allocation percentages, will verify the training that has occurred, and will implement additional training as necessary to meet this recommendation.

With respect to Recommendation Nos. 19, 20, and 21, National Grid has already computed but has not yet issued refunds. The Company will provide the refund analysis to DAA within 60 days of receiving the final audit report and will issue refunds as necessary following DAA review.

IV. FINDING 4: Donations

Recommendation No. 22:
Perform a review of all payments made to industry associations, organizations such as research institutes, voluntary charitable contributions, including mitigation payments, and other voluntary donations for the audit period to ensure all donations are accounted for properly.

Recommendation No. 23:
Strengthen policies and procedures to ensure that voluntary payments to industry associations, organizations such as research institutes, charitable contributions, including voluntary mitigation payments, and other donations are accounted for in accordance with Commission regulations.

Recommendation No. 24:
Provide training to staff on the revised policies for accounting for charitable contributions and other donations.

Recommendation No. 25:
Submit a refund analysis, within 60 days of receiving the final audit report, to DAA for review that explains and details the following: (1) calculation of refunds that resulted from improper accounting for donations during the audit period, including interest; (2) determinative

Steven Hunt
Director and Chief Accountant
October 30, 2019
Page 7

components of the refund; (3) refund method; (4) customers to receive refunds: and (5) period(s) in which refunds will be made.

Recommendation No. 26:
File a refund report with the Commission after receiving DAA's assessment of the analysis.

Recommendation No. 27:
Refund amounts disclosed in the refund report to wholesale customers, with interest calculated in accordance with section 35.19a of the Commission's regulations.

National Grid Response:

With respect to Recommendation Nos. 22, 23, and 24, National Grid will perform a review of all payments made to industry associations, organizations such as research institutes, and other voluntary charitable contributions, for the audit period to ensure proper accounting and will strengthen policies and procedures to ensure proper accounting of such donations. The Company will provide training to employees on new policies and procedures regarding proper accounting for donations.

With respect to Recommendation No. 25, 26, and 27, National Grid will provide a refund analysis to DAA as recommended within 60 days of receiving the final audit report, will file a refund report following DAA's assessment, and will issue refunds as necessary.

V. FINDING 5: Service Company Account Misclassifications

Recommendation No. 28:
Strengthen accounting policies and procedures to ensure that service company costs, and by association operating company costs, are recorded in the correct FERC accounts.

Recommendation No. 29:
Train employees on the updated policies and procedures for recording A&G expenses to FERC accounts.

National Grid Response:

With respect to Recommendation Nos. 28 and 29, National Grid will strengthen policies and procedures to ensure that service company costs and associated operating company costs are

Steven Hunt
Director and Chief Accountant
October 30, 2019
Page 8

recorded in the correct FERC accounts. The Company will provide training to employees on new policies and procedures regarding proper service company accounting.

VI. FINDING 6: Reporting of Transactions with Associated (Affiliated) Companies

Recommendation No. 30:
Strengthen policies and procedures, to include a reconciliation to the FERC Form No. 60 for those non-power goods and services provided by the service companies, to ensure that its public utility subsidiaries accurately, completely, and consistently prepare the schedule on page 429 of the FERC Form No. 1 according to instructions.

National Grid Response:

With respect to Recommendation No. 30, National Grid will strengthen policies and procedures to ensure accurate, complete, and consistent preparation of page 429 of FERC Form 1 according to instructions, including a reconciliation of non-power goods and services provided by service companies as reported on FERC Form 60.

VII. FINDING 7: FERC Form No. 60 Reporting

Recommendation No. 31:
Enhance procedures and controls for submitting NGUSASCo's and NGE&S's FERC Form No. 60 to ensure the forms are accurate, complete, and prepared according to all instructions.

Recommendation No. 32:
Train employees responsible for the FERC Form No. 60 on the new procedures to ensure accurate and complete reporting that is compliant.

National Grid Response:

With respect to Recommendation Nos. 31 and 32, National Grid will strengthen procedures and controls for submitting FERC Form No. 60 to ensure accuracy, completeness and compliance with instructions. The Company will provide training to employees on new policies and procedures regarding proper FERC Form 60 preparation and submission.

National Grid appreciates Audit Staff's professionalism in conducting this audit. As a Company, we take our compliance obligations very seriously, and we welcome the opportunity to improve and enhance our regulatory compliance efforts.

recorded in the correct FERC accounts. The Company will provide training to employees on new policies and procedures regarding proper service company accounting.

VI. FINDING 6: Reporting of Transactions with Associated (Affiliated) Companies

Recommendation No. 30:
Strengthen policies and procedures, to include a reconciliation to the FERC Form No. 60 for those non-power goods and services provided by the service companies, to ensure that its public utility subsidiaries accurately, completely, and consistently prepare the schedule on page 429 of the FERC Form No. 1 according to instructions.

National Grid Response:

With respect to Recommendation No. 30, National Grid will strengthen policies and procedures to ensure accurate, complete, and consistent preparation of page 429 of FERC Form 1 according to instructions, including a reconciliation of non-power goods and services provided by service companies as reported on FERC Form 60.

VII. FINDING 7: FERC Form No. 60 Reporting

Recommendation No. 31:
Enhance procedures and controls for submitting NGUSASCo's and NGE&S's FERC Form No. 60 to ensure the forms are accurate, complete, and prepared according to all instructions.

Recommendation No. 32:
Train employees responsible for the FERC Form No. 60 on the new procedures to ensure accurate and complete reporting that is compliant.

National Grid Response:

With respect to Recommendation Nos. 31 and 32, National Grid will strengthen procedures and controls for submitting FERC Form No. 60 to ensure accuracy, completeness and compliance with instructions. The Company will provide training to employees on new policies and procedures regarding proper FERC Form 60 preparation and submission.

National Grid appreciates Audit Staff's professionalism in conducting this audit. As a Company, we take our compliance obligations very seriously, and we welcome the opportunity to improve and enhance our regulatory compliance efforts.

Steven Hunt
Director and Chief Accountant
October 30, 2019
Page 9

Thank you for your time and attention in this matter.

Sincerely,

Kate Sturgess
US Controller
National Grid
1 MetroTech Center
Brooklyn, NY 11201