

Orange and Rockland Utilities, Inc.
Consolidated Financial Statements
December 31, 2019 and 2018



Report of Independent Auditors

To the Board of Directors of Orange and Rockland Utilities, Inc.

We have audited the accompanying consolidated financial statements of Orange and Rockland Utilities, Inc. and its subsidiaries, which comprise the consolidated balance sheets and statements of capitalization as of December 31, 2019 and 2018, and the related consolidated statements of income, of comprehensive income, of shareholder's equity and of cash flows for each of the three years in the period ended December 31, 2019.

Management's Responsibility for the Consolidated Financial Statements

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

Auditors' Responsibility

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

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

Opinion

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of Orange and Rockland Utilities, Inc. and its subsidiaries as of December 31, 2019 and 2018, and the results of their operations and their cash flows for each of the three years in the period ended December 31, 2019 in accordance with accounting principles generally accepted in the United States of America.

A handwritten signature in black ink that reads "PricewaterhouseCoopers LLP". The signature is written in a cursive style and is positioned above the date.

March 9, 2020

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[Report of Independent Auditors](#)

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Orange and Rockland Utilities, Inc. Consolidated Income Statement

	For the Years Ended December 31,		
<i>(Millions of Dollars)</i>	2019	2018	2017
OPERATING REVENUES			
Electric	\$634	\$642	\$642
Gas	259	249	232
TOTAL OPERATING REVENUES	893	891	874
OPERATING EXPENSES			
Purchased power	188	208	191
Gas purchased for resale	90	86	73
Other operations and maintenance	308	305	296
Depreciation and amortization	84	77	71
Taxes, other than income taxes	84	83	82
TOTAL OPERATING EXPENSES	754	759	713
OPERATING INCOME	139	132	161
OTHER INCOME (DEDUCTIONS)			
Investment and other income	—	1	—
Allowance for equity funds used during construction	2	1	1
Other deductions	(13)	(21)	(20)
TOTAL OTHER INCOME (DEDUCTIONS)	(11)	(19)	(19)
INCOME BEFORE INTEREST AND INCOME TAX EXPENSE	128	113	142
INTEREST EXPENSE			
Interest on long-term debt	39	36	36
Other interest	4	4	1
Allowance for borrowed funds used during construction	(2)	(1)	(1)
NET INTEREST EXPENSE	41	39	36
INCOME BEFORE INCOME TAX EXPENSE	87	74	106
INCOME TAX EXPENSE	17	15	42
NET INCOME	\$70	\$59	\$64

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

Orange and Rockland Utilities, Inc.
Consolidated Statement of Comprehensive Income

<i>(Millions of Dollars)</i>	For the Years Ended December 31,		
	2019	2018	2017
NET INCOME	\$70	\$59	\$64
OTHER COMPREHENSIVE INCOME/(LOSS), NET OF TAXES			
Pension and other postretirement benefit plan liability adjustments, net of taxes	(3)	8	1
TOTAL OTHER COMPREHENSIVE INCOME/(LOSS), NET OF TAXES	(3)	8	1
COMPREHENSIVE INCOME	\$67	\$67	\$65

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

Orange and Rockland Utilities, Inc. Consolidated Statement of Cash Flows

<i>(Millions of Dollars)</i>	For the Years Ended December 31,		
	2019	2018	2017
OPERATING ACTIVITIES			
Net income	\$70	\$59	\$64
PRINCIPAL NON-CASH CHARGES/(CREDITS) TO INCOME			
Depreciation and amortization	84	77	71
Deferred income taxes	—	17	12
Rate case amortizations	1	16	18
Unbilled revenue accruals	(8)	11	3
Other non-cash items, net	6	29	5
CHANGES IN ASSETS AND LIABILITIES			
Accounts receivable - customers	15	(15)	(10)
Accounts receivable from affiliated companies	5	(5)	(1)
Materials and supplies, including gas in storage	(1)	(1)	(4)
Prepayments, other receivables and other current assets	(9)	7	(11)
Accounts payable	16	1	—
Accounts payable to affiliated companies	—	(1)	—
Pensions and retiree benefits obligations, net	29	33	42
Pensions and retiree benefits contributions	(32)	(40)	(46)
Accrued taxes	(1)	—	—
Accrued taxes to affiliated companies	1	(10)	19
Accrued interest	—	1	—
System benefit charge	1	6	17
Superfund and environmental remediation costs, net	4	(2)	(2)
Deferred charges, noncurrent assets and other regulatory assets	(15)	(60)	109
Deferred credits and other regulatory liabilities	17	52	(80)
Other current and noncurrent liabilities	7	(3)	10
NET CASH FLOWS FROM OPERATING ACTIVITIES	190	172	216
INVESTING ACTIVITIES			
Utility construction expenditures	(210)	(199)	(189)
Cost of removal less salvage	(8)	(3)	(7)
Proceeds from sale of assets	—	4	—
NET CASH FLOWS USED IN INVESTING ACTIVITIES	(218)	(198)	(196)
FINANCING ACTIVITIES			
Net issuance/(payment) of short-term debt	(37)	(42)	26
Issuance of long-term debt	125	150	—
Retirement of long-term debt	(62)	(55)	(4)
Debt issuance costs	(1)	(1)	—
Capital contribution by parent	30	25	—
Dividend to parent	(47)	(46)	(44)
NET CASH FLOWS FROM (USED IN) FINANCING ACTIVITIES	8	31	(22)
CASH, TEMPORARY CASH INVESTMENTS AND RESTRICTED CASH:			
NET CHANGE FOR THE PERIOD	(20)	5	(2)
BALANCE AT BEGINNING OF PERIOD	52	47	49
BALANCE AT END OF PERIOD	\$32	\$52	\$47
SUPPLEMENTAL DISCLOSURE OF CASH INFORMATION			
Cash paid during the period for:			
Interest	\$39	\$37	\$36
Income taxes	\$17	\$10	\$10
SUPPLEMENTAL DISCLOSURE OF NON-CASH INFORMATION			
Construction expenditures in accounts payable	\$20	\$29	\$25
Software licenses acquired but unpaid as of end of period	\$4	\$5	\$—

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

Orange and Rockland Utilities, Inc. Consolidated Balance Sheet

<i>(Millions of Dollars)</i>	December 31, 2019	December 31, 2018
ASSETS		
CURRENT ASSETS		
Cash and temporary cash investments	\$32	\$50
Accounts receivable – customers, less allowance for uncollectible accounts of \$5 in 2019 and 2018	70	85
Other receivables, less allowance for uncollectible accounts of \$1 in 2019 and 2018	8	7
Taxes receivables	1	—
Accrued unbilled revenue	42	34
Accounts receivable from affiliated companies	4	9
Gas in storage, at average cost	11	12
Materials and supplies, at average cost	23	21
Prepayments	33	29
Regulatory assets	15	12
Restricted cash	—	2
Other current assets	4	2
TOTAL CURRENT ASSETS	243	263
INVESTMENTS	26	25
UTILITY PLANT, AT ORIGINAL COST		
Electric	1,877	1,783
Gas	864	805
General	291	275
TOTAL	3,032	2,863
Less: Accumulated depreciation	819	782
Net	2,213	2,081
Construction work in progress	123	129
NET UTILITY PLANT	2,336	2,210
OTHER NONCURRENT ASSETS		
Regulatory assets	373	371
Operating right-of-use asset	3	—
Other deferred charges and noncurrent assets	25	23
TOTAL OTHER NONCURRENT ASSETS	401	394
TOTAL ASSETS	\$3,006	\$2,892

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

Orange and Rockland Utilities, Inc. Consolidated Balance Sheet

<i>(Millions of Dollars)</i>	December 31, 2019	December 31, 2018
LIABILITIES AND SHAREHOLDER'S EQUITY		
CURRENT LIABILITIES		
Long-term debt due within one year	\$—	\$62
Notes payable	17	54
Accounts payable	88	81
Accounts payable to affiliated companies	17	17
Customer deposits	12	12
Accrued taxes	2	3
Accrued taxes to affiliated companies	12	11
Accrued interest	9	9
Accrued wages	10	10
Fair value of derivative liabilities	12	7
Regulatory liabilities	39	41
System benefit charge	60	59
Operating lease liabilities	1	—
Other current liabilities	32	26
TOTAL CURRENT LIABILITIES	311	392
NONCURRENT LIABILITIES		
Provision for injuries and damages	5	6
Pensions and retiree benefits	277	277
Superfund and other environmental costs	80	85
Asset retirement obligations	3	—
Deferred income taxes and unamortized investment tax credits	316	309
Regulatory liabilities	391	374
Operating lease liabilities	2	—
Other deferred credits and noncurrent liabilities	41	43
TOTAL NONCURRENT LIABILITIES	1,115	1,094
LONG-TERM DEBT	818	694
COMMON SHAREHOLDER'S EQUITY (See Statement of Shareholder's Equity)	762	712
TOTAL LIABILITIES AND SHAREHOLDER'S EQUITY	\$3,006	\$2,892

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

Orange and Rockland Utilities, Inc.
Consolidated Statement of Shareholder's Equity

<i>(In Millions, except share data)</i>	Common Stock		Additional Paid-In Capital	Retained Earnings	Accumulated Other Comprehensive Income/(Loss)	Total
	Shares	Amount				
BALANCE AS OF DECEMBER 31, 2016	1,000	\$—	\$324	\$342	\$(21)	\$645
Net income				64		64
Common stock dividend to parent				(44)		(44)
Other comprehensive income					1	1
BALANCE AS OF DECEMBER 31, 2017	1,000	\$—	\$324	\$362	\$(20)	\$666
Net income				59		\$59
Common stock dividend to parent				(46)		\$(46)
Capital contribution by parent			25			\$25
Other comprehensive income					8	\$8
BALANCE AS OF DECEMBER 31, 2018	1,000	\$—	\$349	\$375	\$(12)	\$712
Net income				70		70
Common stock dividend to parent				(47)		(47)
Capital contribution by parent			30			30
Other comprehensive income					(3)	(3)
BALANCE AS OF DECEMBER 31, 2019	1,000	\$—	\$379	\$398	\$(15)	\$762

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

Orange and Rockland Utilities, Inc.
Consolidated Statement of Capitalization

<i>(In Millions, except share data)</i>	Shares outstanding December 31,		At December 31,	
	2019	2018	2019	2018
TOTAL SHAREHOLDER'S EQUITY (See Statement of Shareholder's Equity)	1,000	1,000	\$762	\$712
LONG-TERM DEBT (Millions of Dollars)				
Maturity	Interest Rate	Series	At December 31,	
			2019	2018
DEBENTURES:				
2019	4.96	2009A	—	60
2027	6.50	1997F	80	80
2029	2.94	2019B	44	—
2039	6.00	2009B	60	60
2039	3.46	2019C	38	—
2040	5.50	2010B	115	115
2045	4.95	2015A	120	120
2045	4.69	2015B	100	100
2046	3.88	2016A	75	75
2048	4.35	2018A	125	125
2048	4.35	2018B	25	25
2049	3.73	2019A	43	—
TOTAL DEBENTURES			825	760
TRANSITION BONDS:				
2019	5.22%	2004-1	—	2
TOTAL TRANSITION BONDS			—	2
Unamortized debt expense			(6)	(5)
Unamortized debt discount			(1)	(1)
TOTAL			818	756
Less: Long-term debt due within one year			—	62
TOTAL LONG-TERM DEBT			818	694
TOTAL CAPITALIZATION			\$1,580	\$1,406

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

Notes to the Consolidated Financial Statements

General

These notes accompany and form an integral part of the consolidated financial statements of Orange and Rockland Utilities, Inc., a New York corporation, and its subsidiaries (the Company or O&R). The Company is a regulated utility, the equity of which is owned entirely by Consolidated Edison, Inc. (Con Edison). O&R has one regulated utility subsidiary: Rockland Electric Company (RECO). For the years ended December 31, 2019, 2018 and 2017, operating revenues for RECO were 19.7 percent, 20.2 percent, and 20.4 percent, respectively, of O&R's consolidated operating revenues. O&R, along with RECO, provides electric service in southeastern New York and adjacent areas of northern New Jersey and gas service in southeastern New York. RECO has a subsidiary, Rockland Electric Company Transition Funding LLC (Transition Funding), which was formed in 2004 in connection with the securitization of certain purchased power costs. See "Long-Term Debt" in Note C.

The Company is subject to regulation by the Federal Energy Regulatory Commission (FERC), the New York State Public Service Commission (NYSPSC) and the New Jersey Board of Public Utilities (NJBPU) with respect to rates and accounting.

The Company has, pursuant to the accounting rules for subsequent events, evaluated events or transactions that occurred after December 31, 2019 through the posting on its website (March 9, 2020) of the Annual Financial Statements for potential recognition or disclosure in the consolidated financial statements.

Note A – Summary of Significant Accounting Policies

Principles of Consolidation

The Company's consolidated financial statements include the accounts of its subsidiaries. All intercompany balances and transactions have been eliminated.

Accounting Policies

The accounting policies of the Company conform to generally accepted accounting principles in the United States of America (GAAP). The Company is subject to the accounting rules for regulated operations and the accounting requirements of the FERC and the state regulators having jurisdiction.

The accounting rules for regulated operations specify the economic effects that result from the causal relationship of costs and revenues in the rate-regulated environment and how these effects are to be accounted for by a regulated enterprise. Revenues intended to cover some costs may be recorded either before or after the costs are incurred. If regulation provides assurance that incurred costs will be recovered in the future, these costs would be recorded as deferred charges or "regulatory assets" under the accounting rules for regulated operations. If revenues are recorded for costs that are expected to be incurred in the future, these revenues would be recorded as deferred credits or "regulatory liabilities" under the accounting rules for regulated operations.

The Company's principal regulatory assets and liabilities are detailed in Note B. The Company is generally receiving or being credited with a return on its regulatory assets for which a cash outflow has been made and is

Notes to the Consolidated Financial Statements - continued

paying or being charged with a return on its regulatory liabilities for which a cash inflow has been received. The Company is not receiving or being credited with a return on its regulatory asset for RECO's transition bond cost as to which Transition Bonds have been issued (see Note C) or RECO's deferred storm costs. The Company's regulatory assets and liabilities at December 31, 2019 are recoverable from customers, or to be applied for customer benefit, in accordance with rate provisions that have been approved by state regulators.

Other significant accounting policies of the Company are referenced below in this Note A and in the notes that follow.

Revenue Recognition

The following table presents, for the years ended December 31, 2019 and 2018, revenue from contracts with customers as defined in Accounting Standards Codification (ASC) Topic 606, "Revenue from Contracts with Customers," as well as additional revenue from sources other than contracts with customers, disaggregated by major source. Revenue was recognized for the year ended December 31, 2017 under ASC Topic 605, "Revenue Recognition," and was materially consistent with revenue that would have been recognized under Topic 606.

<i>(Millions of Dollars)</i>	2019			2018		
	Revenues from contracts with customers	Other revenues (a)	Total operating revenues	Revenues from contracts with customers	Other revenues (a)	Total operating revenues
Electric	\$627	\$7	\$634	\$647	\$(5)	\$642
Gas	247	12	259	256	(7)	249
Total	\$874	\$19	\$893	\$903	\$(12)	\$891

(a) This includes revenue from alternative revenue programs, such as the revenue decoupling mechanisms under the New York electric and gas rate plans.

Revenues are recorded as energy is delivered, generated or services are provided and billed to customers. Amounts billed are recorded in accounts receivable - customers, with payment generally due the following month. The Company's accounts receivable - customers balance also reflects the Company's purchase of receivables from energy service companies to support retail choice programs. Accrued revenues not yet billed to customers are recorded as accrued unbilled revenues.

O&R has the obligation to deliver electricity and gas to its customers. As the energy is immediately available for use upon delivery to the customer, the energy and its delivery are identifiable as a single performance obligation. The Company recognizes revenues as this performance obligation is satisfied over time as the Company delivers, and the customers simultaneously receive and consume, the energy. The amount of revenues recognized reflects the consideration the Company expects to receive in exchange for delivering the energy. Under its tariffs, the transaction price for full-service customers includes the Company's energy cost and for all customers includes delivery charges determined based on customer class and in accordance with established tariffs and guidelines of the NYSPSC or the NJBPU, as applicable. Accordingly, there is no unsatisfied performance obligation associated with these customers. The transaction price is applied to the Company's revenue generating activities through the customer billing process. Because energy is delivered

Notes to the Consolidated Financial Statements - continued

over time, the Company uses output methods that recognize revenue based on direct measurement of the value transferred, such as units delivered, which provides an accurate measure of value for the energy delivered. The Company accrues revenues at the end of each month for estimated energy delivered but not yet billed to customers. The Company defers over a 12-month period net interruptible gas revenues, other than those authorized by the NYSPSC to be retained by the Company, for refund to firm gas sales and transportation customers.

O&R's New York electric and gas rate plans each contain a revenue decoupling mechanism under which the Company's actual energy delivery revenues are compared with the authorized delivery revenues and the difference accrued, with interest, for refund to, or recovery from, customers, as applicable. See "Rate Plans" in Note B.

O&R is required to record gross receipts tax as revenues and expenses on a gross income statement presentation basis (i.e., included in both revenue and expense). The recovery of this tax is included in the revenue requirement within the approved rate plan. O&R recorded \$10.9 million, \$12.1 million, and \$10.6 million, of gross receipts tax in 2019, 2018 and 2017, respectively.

Plant and Depreciation

Utility Plant

Utility plant is stated at original cost. The cost of repairs and maintenance is charged to expense and the cost of betterments is capitalized. The capitalized cost of additions to utility plant includes indirect costs such as engineering, supervision, payroll taxes, pensions, other benefits and an allowance for funds used during construction (AFUDC). The original cost of property is charged to expense over the estimated useful lives of the assets. Upon retirement, the original cost of property is charged to accumulated depreciation. See Note M.

Rates used for AFUDC include the cost of borrowed funds and a reasonable rate of return on the Company's own funds when so used, determined in accordance with regulations of the FERC or the state public utility regulatory authority having jurisdiction. The rate is compounded semiannually, and the amounts applicable to borrowed funds are treated as a reduction of interest charges, while the amounts applicable to the Company's own funds are credited to other income (deductions). The AFUDC rates for the Company were 5.3 percent, 2.2 percent and 2.5 percent for 2019, 2018 and 2017, respectively.

The Company generally computes annual charges for depreciation using the straight-line method for financial statement purposes, with rates based on average service lives and net salvage factors. The average depreciation rates for the Company were 3.0 percent for 2019, and 2.9 percent for 2018 and 2017.

The estimated lives for utility plant for the Company range from 5 to 75 years for electric and gas and 5 to 50 years for general plant.

Notes to the Consolidated Financial Statements - continued

At December 31, 2019 and 2018, the capitalized cost of the Company's utility plant, net of accumulated depreciation, was as follows:

<i>(Millions of Dollars)</i>	2019	2018
Electric		
Transmission	\$254	\$227
Distribution	1,074	1,034
Gas (a)	655	607
General	222	204
Held for future use	8	9
Construction work in progress	123	129
Net Utility Plant	\$2,336	\$2,210

(a) Primarily distribution

General utility plant included \$5 million at December 31, 2019 and 2018, related to a May 2018 acquisition of software licenses. The estimated aggregate annual amortization expense related to the software licenses is immaterial. The accumulated amortization was \$1 million at December 31, 2019 and immaterial at December 31, 2018.

Under O&R's rate plans, the aggregate annual depreciation allowance in effect for the period ended December 31, 2019 was \$77 million.

Long-Lived Assets

The Company tests the impairment of long-lived assets, based on projections of undiscounted future cash flows, whenever events or changes in circumstances indicate that the carrying amounts of such assets may not be recoverable. In the event a test indicates that such cash flows cannot be expected to be sufficient to fully recover the assets, the assets are considered impaired and written down to their estimated fair value. No impairment charges on long-lived assets were recognized in 2019, 2018 or 2017.

Recoverable Energy Costs

O&R generally recovers all of its prudently incurred purchased power and gas costs, including hedging gains and losses, in accordance with rate provisions approved by the applicable state public utility commissions. If the actual energy supply costs for a given month are more or less than the amounts billed to customers for that month, the difference in most cases is recoverable from or refundable to customers.

For each billing cycle, O&R bills its energy costs to customers based upon its estimate of the cost to supply energy for that billing cycle. Differences between actual and billed electric supply costs are generally deferred for charge or refund to customers during the next billing cycle (normally within one or two months). For O&R's gas costs, differences between actual and billed gas costs during the 12-month period ending each August are charged or refunded to customers during a subsequent 12-month period.

RECO purchases electric energy under a competitive bidding process supervised by the NJBPU for contracts ranging from one to three years. For RECO, approximately 90 percent of the energy supply is covered by fixed

Notes to the Consolidated Financial Statements - continued

price contracts ranging from one to three years that are competitively bid through the NJBPU auction process and provided through the independent system operator, PJM Interconnection LLC (PJM). Basic Generation Service rates are adjusted to conform to contracted prices when new contracts take effect and differences between actual monthly costs and revenues are reconciled and charged or credited to customers on a two-month lag.

New York Independent System Operator (NYISO)

O&R purchases electricity for all of its New York requirements and a portion of its New Jersey needs through the wholesale electricity market administered by the NYISO. The difference between purchased power and related costs initially billed to the Company by the NYISO and the actual cost of power subsequently calculated by the NYISO is refunded by the NYISO to the Company or paid to the NYISO by the Company. Certain other payments to or receipts from the NYISO are also subject to reconciliation, with shortfalls or amounts in excess of specified rate allowances recoverable from or refundable to customers.

Temporary Cash Investments

Temporary cash investments are short-term, highly-liquid investments that generally have maturities of three months or less at the date of purchase. They are stated at cost, which approximates market. The Company considers temporary cash investments to be cash equivalents.

Investments

Investments are recorded at fair value and include the non-qualified supplemental retirement plan assets.

Pension and Other Postretirement Benefits

The accounting rules for retirement benefits require an employer to recognize an asset or liability for the overfunded or underfunded status of its pension and other postretirement benefit plans. For a pension plan, the asset or liability is the difference between the fair value of the plan's assets and the projected benefit obligation. For any other postretirement benefit plan, the asset or liability is the difference between the fair value of the plan's assets and the accumulated postretirement benefit obligation. The accounting rules generally require employers to recognize all unrecognized prior service costs and credits and unrecognized actuarial gains and losses in accumulated other comprehensive income (OCI), net of tax. Such amounts will be adjusted as they are subsequently recognized as components of total periodic benefit cost or income pursuant to the current recognition and amortization provisions.

For O&R pension and other postretirement benefits regulatory accounting treatment is applied in accordance with the accounting rules for regulated operations. RECO pension and other postretirement benefits do not have regulatory accounting treatment. For benefits subject to regulatory accounting treatment, unrecognized prior service costs or credits and unrecognized actuarial gains and losses are recorded to regulatory assets or liabilities, rather than OCI. See Notes E and F.

Notes to the Consolidated Financial Statements - continued

The total periodic benefit costs are recognized in accordance with the accounting rules for retirement benefits. Investment gains and losses are recognized in expense over a 15-year period and other actuarial gains and losses are recognized in expense over a 10-year period, subject to the deferral provisions in the rate plans.

In accordance with the Statement of Policy issued by the NYSPSC and its current electric and gas rate plans, O&R defers for payment to or recovery from customers the difference between such expenses for the Company's New York business and the amounts for such expenses reflected in O&R's rates. RECO's rate plan does not have comparable deferral provisions for retirement benefits. See Note B.

The Company calculates the expected return on pension and other postretirement benefit plan assets by multiplying the expected rate of return on plan assets by the market-related value (MRV) of plan assets at the beginning of the year, taking into consideration anticipated contributions and benefit payments that are to be made during the year. The accounting rules allow the MRV of plan assets to be either fair value or a calculated value that recognizes changes in fair value in a systematic and rational manner over not more than five years. The Company uses a calculated value when determining the MRV of the plan assets that adjusts for 20 percent of the difference between fair value and expected MRV of plan assets. This calculated value has the effect of stabilizing variability in assets to which the Company applies the expected return.

Federal Income Tax

In accordance with the accounting rules for income taxes, the Company has recorded an accumulated deferred federal income tax liability at current tax rates for temporary differences between the book and tax basis of assets and liabilities. In accordance with rate plans, O&R has recovered amounts from customers for a portion of the tax liability it will pay in the future as a result of the reversal or "turn-around" of these temporary differences. As to the remaining deferred tax liability, the Company has established regulatory assets for the net revenue requirements to be recovered from customers for the related future tax expense pursuant to the NYSPSC's 1993 Policy Statement approving accounting procedures consistent with accounting rules for income taxes and providing assurance that these future increases in taxes will be recoverable in rates. Upon enactment of the Tax Cuts and Jobs Act of 2017 on December 22, 2017 (the TCJA), O&R re-measured its deferred tax assets and liabilities based upon the 21 percent corporate income tax rate under the TCJA. See "Other Regulatory Matters" in Note B and Note I.

Accumulated deferred investment tax credits are amortized ratably over the lives of the related properties and applied as a reduction to future federal income tax expense.

The Company, along with Con Edison and its other subsidiaries, files a consolidated federal income tax return. The consolidated income tax liability is allocated to each member of the consolidated group using the separate return method. Each member pays or receives an amount based on its own taxable income or loss in accordance with a consolidated tax allocation agreement. Tax loss and tax credit carryforwards are allocated among members in accordance with consolidated tax return regulations.

Notes to the Consolidated Financial Statements - continued

State Income Tax

The Company, along with Con Edison and its other subsidiaries, files a combined New York State Corporation Business Franchise Tax Return. Similar to a federal consolidated income tax return, the income of all entities in the combined group is subject to New York State taxation, after adjustments for differences between federal and New York law. Each member's share of the New York State tax is based on its own New York State taxable income or loss.

RECO files a New Jersey Corporate Income Tax Return. The income of RECO is subject to New Jersey State taxation, after adjustments for differences between federal and New Jersey law.

Estimates

The preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

Changes in Accumulated Other Comprehensive Income/(Loss) by Component

Changes to accumulated OCI are as follows:

(Millions of Dollars)

Accumulated OCI, net of taxes, at December 31, 2016 (a)	\$(21)
OCI before reclassifications, net of tax of \$2	(3)
Amounts reclassified from accumulated OCI related to pension plan liabilities, net of tax of \$(2) (a)(b)	4
Total OCI, net of taxes, at December 31, 2017	1
Accumulated OCI, net of taxes, at December 31, 2017 (a)	\$(20)
OCI before reclassifications, net of tax of \$2	3
Amounts reclassified from accumulated OCI related to pension plan liabilities, net of tax of \$(2) (a)(b)	5
Total OCI, net of taxes, at December 31, 2018	8
Accumulated OCI, net of taxes, at December 31, 2018 (a)	\$(12)
OCI before reclassifications, net of tax of \$(5)	(7)
Amounts reclassified from accumulated OCI related to pension plan liabilities, net of tax of \$(1) (a)(b)	4
Total OCI, net of taxes, at December 31, 2019	(3)
Accumulated OCI, net of taxes, at December 31, 2019 (a)	\$(15)

(a) Tax reclassified from accumulated OCI is reported in the income tax expense line item of the consolidated income statement.

(b) Only RECO's portion of unrecognized pension and other postretirement benefit costs are recorded into, and amortized out of, OCI. All other such costs are recorded through regulatory assets. The net actuarial losses and prior service costs recognized during the period are included in the computation of total periodic pension and other postretirement benefit cost.

Reconciliation of Cash, Temporary Cash Investments and Restricted Cash

Cash, temporary cash investments and restricted cash are presented on a combined basis in the Company's consolidated statement of cash flows. At December 31, 2019 and 2018, cash, temporary cash investments and restricted cash are as follows:

Notes to the Consolidated Financial Statements - continued

<i>(Millions of Dollars)</i>	At December 31,	
	2019	2018
Cash and temporary cash investments	\$32	\$50
Restricted cash (a)	—	2
Total cash, temporary cash investments and restricted cash	\$32	\$52

(a) Restricted cash is comprised of RECO transition bond charge collections, net of principal, interest, trustee and service fees.

Note B – Regulatory Matters

Rate Plans

The Company provides service to New York customers according to the terms of tariffs approved by the NYSPSC. Tariffs for service to customers of RECO, the Company's New Jersey regulated utility subsidiary, are approved by the New Jersey Board of Public Utilities (NJBPU). The tariffs include schedules of rates for service that limit the rates charged by the Company to amounts that recover from its customers costs approved by the regulator, including capital costs, of providing service to customers as defined by the tariff. The tariffs implement rate plans adopted by state utility regulators in rate orders issued at the conclusion of rate proceedings. Pursuant to the Company's rate plans, there generally can be no change to the charges to customers during the respective terms of the rate plans other than specified adjustments provided for in the rate plans. The Company's rate plans each cover specified periods, but rates determined pursuant to a plan generally continue in effect until a new rate plan is approved by the state utility regulator.

Common provisions of the Company's New York rate plans include:

Recoverable energy costs that allow the Company to recover on a current basis the costs for the energy it supplies with no mark-up to their full-service customers.

Cost reconciliations that reconcile pension and other postretirement benefit costs, environmental remediation costs, property taxes, and certain other costs to amounts reflected in delivery rates for such costs. In addition, changes in the Company's costs not reflected in rates, in excess of certain amounts, resulting from changes in tax or other law, rule, regulation, order, or other requirement or interpretation are deferred as a regulatory asset or regulatory liability to be reflected in the Company's next rate plan or in a manner to be determined by the NYSPSC. See "Other Regulatory Matters," below. Also, the Company generally retains the right to petition for recovery or accounting deferral of extraordinary and material cost increases and provision is sometimes made for the utility to retain a share of cost reductions, for example, property tax refunds.

Revenue decoupling mechanisms that reconcile actual energy delivery revenues to the authorized delivery revenues approved by the NYSPSC. The difference is accrued with interest for refund to, or recovery from customers, as applicable.

Earnings sharing that requires the Company to defer for customer benefit a portion of earnings over specified rates of return on common equity. There is no symmetric mechanism for earnings below specified rates of return on common equity.

Notes to the Consolidated Financial Statements - continued

Negative revenue adjustments for failure to meet certain performance standards relating to service, reliability, safety and other matters.

Positive revenue adjustments for achievement of performance standards related to achievement of clean energy goals, safety and other matters.

Net utility plant reconciliations that require deferral as a regulatory liability of the revenue requirement impact of the amount, if any, by which actual average net utility plant balances are less than amounts reflected in rates. There is generally no symmetric mechanism if actual average net utility plant balances are more than amounts reflected in rates.

Rate base as reflected in rate plans, is, in general, the sum of the Company's net plant, working capital and certain regulatory assets less deferred taxes and certain regulatory liabilities. For each rate plan, the NYSPSC uses a forecast of the average rate base for each year that new rates would be in effect ("rate year"). The NJBPU uses the rate base balances that exist at the end of the historical 12-month period on which base rates are set.

Weighted average cost of capital is determined based on the authorized common equity ratio, return on common equity, cost of long-term debt and customer deposits reflected in each rate plan. For each rate plan, the revenues designed to provide the utility a return on invested capital for each rate year is determined by multiplying its rate base by its pre-tax weighted average cost of capital. The Company's actual return on common equity will reflect its actual operations for each rate year and may be more or less than the authorized return on equity reflected in its rate plan (and if more, may be subject to earnings sharing).

Notes to the Consolidated Financial Statements - continued

The following tables contain a summary of the Company's rate plans.

O&R New York – Electric

Effective period	November 2015 - October 2017 (a)	January 2019 – December 2021 (d)
Base rate changes	Yr. 1 – \$9.3 million Yr. 2 – \$8.8 million Yr. 3 – None	Yr. 1 – \$13.4 million (e) Yr. 2 – \$8.0 million (e) Yr. 3 – \$5.8 million (e)
Amortizations to income of net regulatory (assets) and liabilities	Yr. 1 – \$(8.5) million (b) Yr. 2 – \$(9.4) million (b) Yr. 3 – None	Yr. 1 – \$(1.5) million (f) Yr. 2 – \$(1.5) million (f) Yr. 3 – \$(1.5) million (f)
Other revenue sources		<p>Potential earnings adjustment mechanism incentives for peak reduction, energy efficiency, Distributed Energy Resources utilization and other potential incentives of up to: Yr. 1 - \$3.6 million Yr. 2 - \$4.0 million Yr. 3 - \$4.2 million</p> <p>Potential incentive if performance target related to service terminations is met: \$0.5 million annually.</p> <p>In 2019, the company recorded \$2.6 million of earnings adjustment mechanism incentives for energy efficiency and \$0.2 million of incentives for service terminations.</p>
Revenue decoupling mechanisms	In 2015, 2016, 2017 and 2018, the company deferred for the customer's benefit an immaterial amount, \$6.3 million as regulatory liabilities, \$11.2 million as regulatory asset and \$0.5 million as regulatory asset, respectively.	<p>Continuation of reconciliation of actual to authorized electric delivery revenues.</p> <p>In 2019 the company deferred \$0.1 million as a regulatory asset.</p>
Recoverable energy costs	Continuation of current rate recovery of purchased power costs.	Continuation of current rate recovery of purchased power costs.
Negative revenue adjustments	Potential charges (up to \$4 million annually) if certain performance targets are not met. In 2015 the company recorded \$1.25 million in negative revenue adjustments. In 2016, 2017 and 2018, the company did not record any negative revenue adjustments.	<p>Potential charges if certain performance targets relating to service, reliability and other matters are not met: Yr. 1 - \$4.4 million Yr. 2 - \$4.4 million Yr. 3 - \$4.5 million</p> <p>In 2019, the company did not record any negative revenue adjustments.</p>
Cost reconciliations	In 2015, 2016 and 2017, the company deferred \$0.3 million, \$7.4 million and \$3.2 million as net decreases to regulatory assets, respectively. In 2018, the company deferred \$5 million as a net regulatory asset.	<p>Reconciliation of expenses for pension and other postretirement benefits, environmental remediation costs, property taxes (g), energy efficiency program (h), major storms, the impact of new laws and certain other costs to amounts reflected in rates. (i)</p> <p>In 2019, the company deferred \$4.3 million as a net regulatory asset.</p>
Net utility plant reconciliations	<p>Target levels reflected in rates are: Yr. 1 – \$928 million (c) Yr. 2 – \$970 million (c)</p> <p>The company increased/(reduced) its regulatory asset by \$2.2 million, \$(1.9) million, \$(1.9) million and \$1.4 million in 2015, 2016, 2017 and 2018, respectively.</p>	<p>Target levels reflected in rates were: Electric average net plant target excluding advanced metering infrastructure (AMI): Yr. 1 - \$1,008 million Yr. 2 - \$1,032 million Yr. 3 - \$1,083 million AMI (j): Yr. 1 - \$48 million Yr. 2 - \$58 million Yr. 3 - \$61 million</p> <p>The company increased regulatory asset by an immaterial amount in 2019.</p>
Average rate base	Yr. 1 – \$763 million Yr. 2 – \$805 million Yr. 3 – \$805 million	Yr. 1 – \$878 million Yr. 2 – \$906 million Yr. 3 – \$948 million
Weighted average cost of capital (after-tax)	Yr. 1 – 7.10 percent Yr. 2 – 7.06 percent Yr. 3 – 7.06 percent	Yr. 1 – 6.97 percent Yr. 2 – 6.96 percent Yr. 3 – 6.96 percent
Authorized return on common equity	9.0 percent	9.0 percent
Actual return on common equity (k)	Yr. 1 – 10.8 percent Yr. 2 – 9.7 percent Yr. 3 – 7.2 percent	Yr. 1 – 9.6 percent

Notes to the Consolidated Financial Statements - continued

Earnings sharing	Most earnings above an annual earnings threshold of 9.6 percent are to be applied to reduce regulatory assets. In 2015, earnings did not exceed the earnings threshold. Actual earnings were \$6.1 million, \$0.3 million above the threshold for 2016 and 2017, respectively. In 2018, earnings did not exceed the earnings threshold.	Most earnings above an annual earnings threshold of 9.6 percent are to be applied to reduce regulatory assets for environmental remediation and other costs accumulated in the rate year. In 2019, earnings did not exceed the earnings threshold.
Cost of long-term debt	Yr. 1 – 5.42 percent Yr. 2 – 5.35 percent Yr. 3 – 5.35 percent	Yr. 1 – 5.17 percent Yr. 2 – 5.14 percent Yr. 3 – 5.14 percent
Common equity ratio	48 percent	48 percent

- (a) Rates determined pursuant to this rate plan continued in effect until the subsequent rate plan became effective.
- (b) \$59.3 million of the regulatory asset for deferred storm costs is to be recovered from customers over a 5 year period, including \$11.85 million in each of years 1 and 2, \$1 million of the regulatory asset for such costs will not be recovered from customers, and all outstanding issues related to Superstorm Sandy and other past major storms prior to November 2014 are resolved. Approximately \$4 million of regulatory assets for property tax and interest rate reconciliations will not be recovered from customers. Amounts that will not be recovered from customers were charged-off in June 2015.
- (c) Excludes electric AMI as to which the company will be required to defer as a regulatory liability the revenue requirement impact of the amount, if any, by which actual average net utility plant balances are less than amounts reflected in rates: \$1 million in year 1 and \$9 million in year 2.
- (d) If at the end of any year, Con Edison's investments in its non-utility businesses exceed 15 percent of Con Edison's total consolidated revenues, assets or cash flow, or if the ratio of holding company debt to total consolidated debt rises above 20 percent, O&R is required to notify the NYSPSC and submit a ring-fencing plan or a demonstration why additional ring-fencing measures (see Note N) are not necessary.
- (e) The electric base rate increases shown above will be implemented with increases of: Yr. 1 - \$8.6 million; Yr. 2 - \$12.1 million; and Yr. 3 - \$12.2 million.
- (f) Reflects amortization of, among other things, the company's net benefits under the TCJA prior to January 1, 2019, amortization of net regulatory liability for future income taxes and reduction of previously incurred regulatory assets for environmental remediation costs. Also, for electric, reflects amortization over a six-year period of previously incurred incremental major storm costs. See "Other Regulatory Matters," below.
- (g) Deferrals for property taxes are limited to 90 percent of the difference from amounts reflected in rates, subject to an annual maximum for the remaining difference of not more than a maximum number of basis points impact on return on common equity: Yr. 1 - 10.0 basis points; Yr. 2 - 7.5 basis points; and Yr. 3 - 5.0 basis points.
- (h) Energy efficiency costs are expensed as incurred. Such costs are subject to a downward-only reconciliation over the terms of the electric and gas rate plans. The company will defer for the benefit of customers any cumulative shortfall over the terms of the electric and gas rate plans between actual expenditures and the levels provided in rates.
- (i) In addition, amounts reflected in rates relating to income taxes and excess deferred federal income tax liability balances will be reconciled (i.e., refunded to or collected from customers) to any final, non-appealable NYSPSC-ordered findings in its investigation of O&R's income tax accounting. See "Other Regulatory Matters," in Note B.
- (j) Net plant reconciliation for AMI expenditures will be implemented for a single category of AMI capital expenditures that includes amounts allocated to both electric and gas customers.
- (k) Calculated in accordance with the earnings calculation method prescribed in the rate order.

Notes to the Consolidated Financial Statements - continued

O&R New York – Gas

Effective period	November 2015 – October 2018 (a)	January 2019 – December 2021 (d)
Base rate changes	Yr. 1 – \$16.4 million Yr. 2 – \$16.4 million Yr. 3 – \$5.8 million Yr. 3 – \$10.6 million collected through a surcharge	Yr. 1 – \$(7.5) million (e) Yr. 2 – \$3.6 million (e) Yr. 3 – \$0.7 million (e)
Amortization to income of net regulatory (assets) and liabilities	Yr. 1 – \$(1.7) million (b) Yr. 2 – \$(2.1) million (b) Yr. 3 – \$(2.5) million (b)	Yr. 1 – \$1.8 million (f) Yr. 2 – \$1.8 million (f) Yr. 3 – \$1.8 million (f)
Other revenue sources		<p>Continuation of retention of annual revenues from non-firm customers of up to \$4.0 million, with variances to be shared 80 percent by customers and 20 percent by company.</p> <p>Potential earnings adjustment mechanism incentives of up to \$0.3 million annually.</p> <p>Potential incentives if performance targets related to gas leak backlog, leak prone pipe, emergency response, damage prevention and service terminations are met: Yr. 1 - \$1.2 million; Yr. 2 - \$1.3 million; and Yr. 3 - \$1.3 million.</p> <p>In 2019, the company recorded \$0.3 million of earnings adjustment mechanism incentives for energy efficiency and \$0.7 million of incentives for gas leak backlog, leak prone pipe and service terminations.</p>
Revenue decoupling mechanisms	In 2015, 2016, 2017 and 2018, the company deferred \$0.8 million of regulatory assets, \$6.2 million of regulatory liabilities, \$1.7 million of regulatory liabilities and \$6.3 million of regulatory liabilities, respectively.	<p>Continuation of reconciliation of actual to authorized gas delivery revenues.</p> <p>In 2019, the company deferred \$0.8 million of regulatory assets.</p>
Recoverable energy costs	Current rate recovery of purchased gas costs.	Continuation of current rate recovery of purchased gas costs.
Negative revenue adjustments	Potential charges (up to \$3.7 million in Yr. 1, \$4.7 million in Yr. 2 and \$4.9 million in Yr. 3) if certain performance targets are not met. In 2015, 2016 and 2017, the company did not record any negative revenue adjustments. In 2018, the company recorded a \$0.1 million negative revenue adjustment.	<p>Potential charges if performance targets relating to service, safety and other matters are not met: Yr. 1 - \$5.5 million; Yr. 2 - \$5.7 million; and Yr. 3 - \$6.0 million.</p> <p>In 2019, the company recorded a \$0.2 million negative revenue adjustment.</p>
Cost reconciliations	In 2015 and 2016, the company deferred \$4.5 million and \$6.6 million as net regulatory liabilities and assets, respectively. In 2017 and 2018, the company deferred \$3.5 million and \$7.4 million as net regulatory liabilities, respectively.	<p>Reconciliation of expenses for pension and other postretirement benefits, environmental remediation costs, property taxes (g), energy efficiency program (h), the impact of new laws and certain other costs to amounts reflected in rates. (i)</p> <p>In 2019, the company deferred \$6 million as net regulatory liabilities.</p>
Net utility plant reconciliations	Target levels reflected in rates are: Yr. 1 – \$492 million (c) Yr. 2 – \$518 million (c) Yr. 3 – \$546 million (c) No deferral was recorded for 2015 and immaterial amounts were recorded as regulatory liabilities in 2016 and 2017. In 2018, the company deferred \$0.4 million as regulatory asset.	<p>Target levels reflected in rates were: Gas average net plant target excluding AMI: Yr. 1 - \$593 million Yr. 2 - \$611 million Yr. 3 - \$632 million AMI (j): Yr. 1 - \$20 million Yr. 2 - \$24 million Yr. 3 - \$25 million</p> <p>In 2019, the company deferred an immaterial amount as regulatory asset.</p>
Average rate base	Yr. 1 – \$366 million Yr. 2 – \$391 million Yr. 3 – \$417 million	Yr. 1 – \$454 million Yr. 2 – \$476 million Yr. 3 – \$498 million
Weighted average cost of capital (after-tax)	Yr. 1 – 7.10 percent Yr. 2 – 7.06 percent Yr. 3 – 7.06 percent	Yr. 1 – 6.97 percent Yr. 2 – 6.96 percent Yr. 3 – 6.96 percent
Authorized return on common equity	9.0 percent	9.0 percent
Actual return on common equity (k)	Yr. 1 – 11.2 percent Yr. 2 – 9.7 percent Yr. 3 – 8.1 percent	Yr. 1 – 8.9 percent

Notes to the Consolidated Financial Statements - continued

Earnings sharing	Most earnings above an annual earnings threshold of 9.6 percent are to be applied to reduce regulatory assets. In 2015, earnings did not exceed the earnings threshold. Actual earnings were \$4 million, \$0.2 million above the threshold for 2016 and 2017, respectively. In 2018, earnings did not exceed the earnings threshold.	Most earnings above an annual earnings threshold of 9.6 percent are to be applied to reduce regulatory assets for environmental remediation and other costs accumulated in the rate year. In 2019, earnings did not exceed the earnings threshold.
Cost of long-term debt	Yr. 1 – 5.42 percent Yr. 2 – 5.35 percent Yr. 3 – 5.35 percent	Yr. 1 – 5.17 percent Yr. 2 – 5.14 percent Yr. 3 – 5.14 percent
Common equity ratio	48 percent	48 percent

- (a) Rates pursuant to this rate plan continued in effect until the subsequent rate plan became effective.
- (b) Reflects that the company will not recover from customers a total of approximately \$14 million of regulatory assets for property tax and interest rate reconciliations. Amounts that will not be recovered from customers were charged-off in June 2015.
- (c) Excludes gas AMI as to which the company will be required to defer as a regulatory liability the revenue requirement impact of the amount, if any, by which actual average net utility plant balances are less than amounts reflected in rates: \$0.5 million in year 1, \$4.2 million in year 2 and \$7.2 million in year 3.
- (d) If at the end of any year, Con Edison's investments in its non-utility businesses exceed 15 percent of Con Edison's total consolidated revenues, assets or cash flow, or if the ratio of holding company debt to total consolidated debt rises above 20 percent, O&R is required to notify the NYPSC and submit a ring-fencing plan or a demonstration why additional ring-fencing measures (see Note N) are not necessary.
- (e) The gas base rate changes shown above will be implemented with changes of: Yr. 1 - \$(5.9) million; Yr. 2 - \$1.0 million; and Yr. 3 - \$1.0 million.
- (f)-(k) See footnotes (f) - (k) to the table under "O&R New York - Electric," above.

Notes to the Consolidated Financial Statements - continued

In January 2020, the NJBPU approved an electric rate increase, effective February 1, 2020, of \$12 million for RECO. The following table contains a summary of the terms of the distribution rate plans.

RECO		
Effective period	March 2017 – January 2020	February 2020
Base rate changes	Yr. 1 – \$1.7 million	Yr. 1 – \$12 million
Amortization to income of net regulatory (assets) and liabilities	\$0.2 million over three years and continuation of \$(25.6) million of deferred storm costs over four years which expired on July 31, 2018 (a)	\$4.8 million over four years.
Recoverable energy costs	Current rate recovery of purchased power costs.	Current rate recovery of purchased power costs.
Cost reconciliations	None	None
Average rate base	Yr. 1 – \$178.7 million	Yr. 1 – \$229.9 million
Weighted average cost of capital (after-tax)	7.47 percent	7.11 percent
Authorized return on common equity	9.6 percent	9.5 percent
Actual return on common equity	Yr. 1 – 7.5 percent Yr. 2 – 5.7 percent	
Cost of long-term debt	5.37 percent	4.88 percent
Common equity ratio	49.7 percent	48.32 percent

(a) In January 2016, the NJBPU approved RECO's plan to spend \$15.7 million in capital over three years to harden its electric system against storms, the costs of which RECO, beginning in 2017, is collecting through a customer surcharge.

In November 2017, FERC approved a September 2017 settlement agreement among RECO, the New Jersey Division of Rate Counsel and the NJBPU that increases RECO's annual transmission revenue requirement from \$11.8 million to \$17.7 million, effective April 2017. The revenue requirement reflects a return on common equity of 10.0 percent.

Other Regulatory Matters

O&R, under its current electric and gas rate plans, has reflected its net benefits of the TCJA in its electric and gas rates beginning as of January 1, 2019. Under the rate plans, O&R is amortizing its net benefits prior to January 1, 2019 (\$22 million) over a three-year period, the protected portion of its net regulatory liability for future income taxes (\$123 million) over the remaining lives of the related assets and the unprotected portion (\$30 million) over a fifteen-year period. See "Rate Plans," above.

In January 2018, the NYSPSC issued an order initiating a focused operations audit of the income tax accounting of certain utilities, including O&R. The Company is unable to estimate the amount or range of its possible loss related to this matter. At December 31, 2019, the Company had not accrued a liability related to this matter.

In March 2018, Winter Storms Riley and Quinn caused damage to the Company's electric distribution systems and interrupted service to approximately 93,000 O&R customers and 44,000 RECO customers. At December 31, 2019, O&R and RECO costs related to 2018 storms amounted to \$43 million and \$17 million, respectively, most of which were deferred as regulatory assets pursuant to their electric rate plans. In January 2019, O&R began recovering its deferred storm costs over a six-year period in accordance with its New York electric rate plan. The NYSPSC investigated the preparation and response to the storms by O&R, and other New York electric utilities, including all aspects of their emergency response plans. In April 2019, following the

Notes to the Consolidated Financial Statements - continued

issuance of a NYSPSC staff report on the investigation, the NYSPSC ordered the utilities to show cause why the NYSPSC should not commence a penalty action against them for violating their emergency response plans. The Company is unable to estimate the amount or range of their possible loss related to this matter. At December 31, 2019, the Company had not accrued a liability related to this matter.

Regulatory Assets and Liabilities

Regulatory assets and liabilities at December 31, 2019 and 2018 were comprised of the following items:

<i>(Millions of Dollars)</i>	2019	2018
Regulatory assets		
Unrecognized pension and other postretirement costs	\$138	\$127
Environmental remediation costs	85	94
Deferred storm costs (a)	77	76
Pension and other postretirement benefits deferrals	23	17
Revenue taxes	14	12
Property tax reconciliation	8	15
Deferred derivative losses	8	6
Recoverable energy costs	5	3
Transition bond charges (a)	—	2
Other	15	19
Regulatory assets – noncurrent	373	371
Deferred derivative losses	15	7
Recoverable energy costs	—	5
Regulatory assets – current	15	12
Total Regulatory Assets	\$388	\$383
Regulatory liabilities		
Allowance for cost of removal less salvage	\$146	\$138
Future federal income tax (b)	143	143
Pension and other postretirement benefit deferrals	28	22
TCJA net benefits	17	23
Carrying charges on deferred tax liability	11	15
Unrecognized other postretirement costs	9	—
Earnings sharing - electric and gas	6	10
System benefit charge carrying charge	5	3
Other	26	20
Regulatory liabilities – noncurrent	391	374
Refundable energy costs	32	23
Revenue decoupling mechanism	7	17
Deferred derivative gains	—	1
Regulatory liabilities – current	39	41
Total Regulatory Liabilities	\$430	\$415

(a) See "Accounting Policies" in Note A.

(b) See "Federal Income Tax" in Note A, "Other Regulatory Matters," above, and Note I.

Unrecognized pension and other postretirement costs represent the net regulatory asset associated with the accounting rules for retirement benefits. See Note A.

Deferred storm costs represent response and restoration costs, other than capital expenditures, in connection with Superstorm Sandy and other major storms that were deferred by the Company.

Notes to the Consolidated Financial Statements - continued

Note C – Capitalization

Common Stock

At December 31, 2019 and 2018, 1,000 shares of the Company's common stock (\$5.00 par value) were outstanding, all of which were owned by Con Edison. In accordance with NYSPSC requirements, the dividends that the Company generally may pay to Con Edison are limited to not more than 100 percent of its income available for dividends calculated on a two-year rolling average basis. Excluded from the calculation of "income available for dividends" are non-cash charges to income resulting from accounting changes or charges to income resulting from significant unanticipated events. The restriction also does not apply to dividends paid in order to transfer to Con Edison proceeds from major transactions, such as asset sales, or to dividends reducing the Company's equity ratio to a level appropriate to its business risk.

Long-Term Debt

There are no long-term debt maturities for periods 2020-2024.

The carrying amounts and fair values of long-term debt at December 31, 2019 and 2018 are:

<i>(Millions of Dollars)</i>	2019		2018	
	Carrying Amount	Fair Value	Carrying Amount	Fair Value
Long-Term Debt (including current portion) (a)	\$818	\$934	\$756	\$782

(a) Amounts shown are net of unamortized debt expense and unamortized debt discount of \$7 million and \$6 million as of December 31, 2019 and 2018, respectively.

Fair values of long-term debt have been estimated primarily using available market information and are classified as Level 2 liabilities (see the fair value hierarchy defined in Note L). Long-term debt included \$2 million at December 31, 2018 of Transition Bonds issued by Transition Funding in July 2004. The proceeds from the Transition Bonds were used to purchase from RECO the right to be paid a Transition Bond Charge and associated tax charges by its customers relating to previously deferred purchased power costs for which the NJBPU had authorized recovery. In May 2019, RECO paid the remaining \$1 million principal amounts of the Transition Bonds.

Significant Debt Covenants

There are no significant debt covenants under the financing arrangements for the debentures of O&R, other than obligations to pay principal and interest when due and covenants not to consolidate with or merge into any other corporation unless certain conditions are met, and no cross-default provisions. The Company was in compliance with its significant debt covenants at December 31, 2019.

The failure to comply with debt covenants would, except as otherwise provided, constitute an event of default for the debt to which such provisions applied. If an event of default were to occur, the principal and accrued interest on the debt to which such provisions applied might and, in certain circumstances would, become due and payable immediately.

Notes to the Consolidated Financial Statements - continued

Note D – Short-Term Borrowing

In December 2016, O&R, along with Con Edison and Consolidated Edison Company of New York, Inc. (CECONY), entered into a credit agreement (Credit Agreement), under which banks are committed to provide loans and letters of credit on a revolving credit basis. The Credit Agreement, as amended, expires in December 2023. There is a maximum of \$200 million of credit available to O&R (subject to increase to \$250 million of credit if the necessary regulatory approvals are requested and obtained). The Credit Agreement supports the Company's commercial paper programs. The Company has not borrowed under the Credit Agreement. At December 31, 2019 and 2018, O&R had \$17 million and \$54 million of commercial paper outstanding, respectively. The weighted average interest rate at December 31, 2019 and December 31, 2018 was 2.0 percent and 3.0 percent, respectively. At December 31, 2019 and 2018, an immaterial amount of letters of credit were outstanding for O&R under the Credit Agreement.

The banks' commitments under the Credit Agreement are subject to certain conditions, including that there be no event of default. The commitments are not subject to maintenance of credit rating levels or the absence of a material adverse change. Upon a change of control of, or upon an event of default by the Company, the banks may terminate their commitments with respect to the Company, declare any amounts owed by the Company under the Credit Agreement immediately due and payable and require the Company to provide cash collateral relating to the letters of credit issued for it under the Credit Agreement. Events of default include the exceeding at any time of a ratio of consolidated debt to consolidated total capital of 0.65 to 1 (at December 31, 2019 this ratio was 0.53 to 1); having liens on its assets in an aggregate amount exceeding five percent of its consolidated total capital, subject to certain exceptions; the Company or any of its material subsidiaries failing to make one or more payments in respect of material financial obligations (in excess of an aggregate \$150 million of debt or derivative obligations other than non-recourse debt) of the Company; the occurrence of an event or condition which results in the acceleration of the maturity of any material debt (in excess of an aggregate \$150 million of debt other than non-recourse debt) of the Company or enables the holders of such debt to accelerate the maturity thereof; and other customary events of default. Interest and fees charged for the revolving credit facilities and any loans made or letters of credit issued under the Credit Agreement reflect the Company's credit ratings. The Company was in compliance with its covenants at December 31, 2019.

See Note N for information about short-term borrowing between related parties.

Note E – Pension Benefits

Substantially all employees of O&R are covered by a tax-qualified, non-contributory pension plan maintained by Con Edison, which also covers substantially all employees of CECONY, Con Edison Transmission, Inc. and certain employees of Con Edison's Clean Energy Businesses, Inc. The plan is designed to comply with the Internal Revenue Code and the Employee Retirement Income Security Act of 1974. Con Edison also maintains additional non-qualified supplemental pension plans.

Notes to the Consolidated Financial Statements - continued

Total Periodic Benefit Cost

The components of the Company's total periodic benefit costs for 2019, 2018 and 2017 were as follows:

<i>(Millions of Dollars)</i>	2019	2018	2017
Service cost – including administrative expenses	\$16	\$19	\$18
Interest cost on projected benefit obligation	37	35	37
Expected return on plan assets	(51)	(53)	(50)
Recognition of net actuarial loss	27	36	31
Recognition of prior service costs	2	2	2
TOTAL PERIODIC BENEFIT COST	\$31	\$39	\$38
Cost capitalized	(7)	(8)	(12)
Reconciliation to rate level	(2)	8	6
Total expense recognized	\$22	\$39	\$32

In March 2017, the FASB issued amendments to the guidance for retirement benefits through ASU 2017-07, "Compensation-Retirement Benefits (Topic 715): Improving the Presentation of Net Periodic Pension Cost and Net Periodic Postretirement Benefit Cost." The Company adopted ASU 2017-07 beginning on January 1, 2018. The guidance requires that components of net periodic benefit cost other than service cost be presented outside of operating income on consolidated income statements, and that only the service cost component is eligible for capitalization. Accordingly, the service cost components are included in the line "Other operations and maintenance" and the non-service cost components are included in the line "Other deductions" in the Company's consolidated income statement. As permitted by a practical expedient under ASU 2017-07, the Company applied the presentation requirements retrospectively for both pension and other postretirement benefit costs using amounts disclosed in prior-period financial statements as appropriate estimates.

Funded Status

The funded status at December 31, 2019, 2018 and 2017, as related to O&R, was as follows:

<i>(Millions of Dollars)</i>	2019	2018	2017
CHANGE IN PROJECTED BENEFIT OBLIGATION			
Projected benefit obligation at beginning of year	\$901	\$963	\$885
Service cost – excluding administrative expenses	16	19	17
Interest cost on projected benefit obligation	37	35	37
Net actuarial (gain)/loss	115	(59)	60
Plan amendments	15	—	7
Benefits paid	(49)	(57)	(43)
PROJECTED BENEFIT OBLIGATION AT END OF YEAR	\$1,035	\$901	\$963
CHANGE IN PLAN ASSETS			
Fair value of plan assets at beginning of year	\$700	\$748	\$650
Actual return on plan assets	130	(28)	105
Employer contributions	32	39	38
Benefits paid	(49)	(57)	(43)
Administrative expenses	(3)	(2)	(2)
FAIR VALUE OF PLAN ASSETS AT END OF YEAR	\$810	\$700	\$748
FUNDED STATUS	\$(225)	\$(201)	\$(215)
Unrecognized net loss	\$137	\$125	\$136
Unrecognized prior service costs	30	17	19
Accumulated benefit obligation	998	863	919

Notes to the Consolidated Financial Statements - continued

The increase in the pension liability at O&R of \$24 million, compared with December 31, 2018, was primarily due to an increase in the plan's projected benefit obligation as a result of a decrease in discount rate, partially offset by an increase in plan assets as a result of the actual return on plan assets. This increase in pension liability corresponds with an increase to regulatory assets of \$20 million for unrecognized net losses and unrecognized prior service costs associated with O&R's New York utility business consistent with the accounting rules for regulated operations, a debit to OCI of \$5 million (net of taxes) for the unrecognized net losses and a debit to OCI of \$3 million (net of taxes) for the unrecognized prior service costs associated with RECO.

A portion of the unrecognized net loss and prior service cost for the pension plan, equal to \$36 million and \$3 million, respectively, will be recognized from accumulated OCI and the regulatory asset into net periodic benefit cost over the next year for O&R.

At December 31, 2019 and 2018, the Company's investments included \$26 million and \$25 million, respectively, held in external trust accounts for benefit payments pursuant to the supplemental retirement plan. See Note L. The accumulated benefit obligations for the supplemental retirement plan for O&R were \$35 million and \$31 million as of December 31, 2019 and 2018, respectively.

Assumptions

The actuarial assumptions were as follows:

	2019	2018	2017
Weighted-average assumptions used to determine benefit obligations at December 31:			
Discount rate	3.35%	4.25%	3.70%
Rate of compensation increase	3.20%	4.00%	4.00%
Weighted-average assumptions used to determine net periodic benefit cost for the years ended December 31:			
Discount rate	4.25%	3.70%	4.25%
Expected return on plan assets	7.00%	7.50%	7.50%
Rate of compensation increase	4.00%	4.00%	4.00%

The expected return assumption reflects anticipated returns on the plan's current and future assets. The Company's expected return was based on an evaluation of the current environment, market and economic outlook, relationships between the economy and asset class performance patterns, and recent and long-term trends in asset class performance. The projections were based on the plan's target asset allocation.

Discount Rate Assumption

To determine the assumed discount rate, the Company uses a model that produces a yield curve based on yields on selected highly rated (Aa or higher by either Moody's Investor Service or S&P Global Ratings) corporate bonds. Bonds with insufficient liquidity, bonds with questionable pricing information and bonds that are not representative of the overall market are excluded from consideration. For example, the bonds used in the model cannot be callable (with the exception of "make-whole" callable bonds), and the amount of the bond

Notes to the Consolidated Financial Statements - continued

issue outstanding must be in excess of \$50 million. The spot rates defined by the yield curve and the plan's projected benefit payments are used to develop a weighted average discount rate.

Expected Benefit Payments

Based on current assumptions, the Company expects to make the following benefit payments over the next ten years:

<i>(Millions of Dollars)</i>	2020	2021	2022	2023	2024	2025-2029
O&R	\$55	\$56	\$57	\$59	\$59	\$296

Expected Contributions

Based on estimates as of December 31, 2019, O&R expects to make contributions to the pension plan during 2020 of \$39 million. O&R's policy is to fund the total periodic benefit cost of the qualified plan to the extent tax deductible.

Plan Assets

The asset allocations for the pension plan at the end of 2019, 2018 and 2017, and the target allocation for 2020 are as follows:

Asset Category	Target Allocation Range	Plan Assets at December 31,			
	2020	2019	2018	2017	
Equity Securities	45% - 55%	51%	51%	58%	
Debt Securities	33% - 43%	38%	39%	33%	
Real Estate	10% - 14%	11%	10%	9%	
Total	100%	100%	100%	100%	

Con Edison has established a pension trust for the investment of assets to be used for the exclusive purpose of providing retirement benefits to participants and beneficiaries and payment of plan expenses.

Pursuant to resolutions adopted by Con Edison's Board of Directors, the Management Development and Compensation Committee of the Board of Directors (the Committee) has general oversight responsibility for Con Edison's pension and other employee benefit plans. The pension plan's named fiduciaries have been granted the authority to control and manage the operation and administration of the plans, including overall responsibility for the investment of assets in the trust and the power to appoint and terminate investment managers.

The investment objectives of the Con Edison pension plan are to maintain a level and form of assets adequate to meet benefit obligations to participants, to achieve the expected long-term total return on the trust assets within a prudent level of risk and maintain a level of volatility that is not expected to have a material impact on the Company's expected contribution and expense or the Company's ability to meet plan obligations. The assets of the plan have no significant concentration of risk in one country (other than the United States), industry or entity.

Notes to the Consolidated Financial Statements - continued

The strategic asset allocation is intended to meet the objectives of the pension plan by diversifying its funds across asset classes, investment styles and fund managers. An asset/liability study typically is conducted every few years to determine whether the current strategic asset allocation continues to represent the appropriate balance of expected risk and reward for the plan to meet expected liabilities. Each study considers the investment risk of the asset allocation and determines the optimal asset allocation for the plan. The target asset allocation for 2020 reflects the results of such a study conducted in 2018.

Individual fund managers operate under written guidelines provided by Con Edison, which cover such areas as investment objectives, performance measurement, permissible investments, investment restrictions, trading and execution, and communication and reporting requirements. Con Edison management regularly monitors, and the named fiduciaries review and report to the Committee regarding, asset class performance, total fund performance, and compliance with asset allocation guidelines. Management changes fund managers and rebalances the portfolio as appropriate. At the direction of the named fiduciaries, such changes are reported to the Committee.

The pension plan is one tax-qualified plan for Con Edison and its subsidiaries. O&R employee benefits are paid out of the assets detailed below which represent the assets of the entire plan.

The fair values of the pension plan assets at December 31, 2019 by asset category are as follows:

<i>(Millions of Dollars)</i>	Level 1	Level 2	Total
Investments within the fair value hierarchy			
U.S. Equity (a)	\$3,652	\$—	\$3,652
International Equity (b)	3,354	—	3,354
U.S. Government Issued Debt (c)	—	1,496	1,496
Corporate Bonds Debt (d)	—	3,260	3,260
Structured Assets Debt (e)	—	173	173
Other Fixed Income Debt (f)	—	955	955
Cash and Cash Equivalents (g)	—	326	326
Futures (h)	—	—	—
Total investments within the fair value hierarchy	\$7,006	\$6,210	\$13,216
Investments measured at NAV per share (n)			
Private Equity (i)			555
Real Estate (j)			1,806
Hedge Funds (k)			270
Total investments valued using NAV per share			\$2,631
Funds for retiree health benefits (l)	(110)	(98)	(208)
Funds for retiree health benefits measured at NAV per share (l)(n)			(42)
Total funds for retiree health benefits			\$(250)
Investments (excluding funds for retiree health benefits)	\$6,896	\$6,112	\$15,597
Pending activities (m)			11
Total fair value of plan net assets			\$15,608

- (a) U.S. Equity includes both actively- and passively-managed assets with investments in domestic equity index funds and actively-managed small-capitalization equities.
- (b) International Equity includes international equity index funds and actively-managed international equities.
- (c) U.S. Government Issued Debt includes agency and treasury securities.

Notes to the Consolidated Financial Statements - continued

- (d) Corporate Bonds Debt consists of debt issued by various corporations.
- (e) Structured Assets Debt includes commercial-mortgage-backed securities and collateralized mortgage obligations.
- (f) Other Fixed Income Debt includes municipal bonds, sovereign debt and regional governments.
- (g) Cash and Cash Equivalents include short term investments, money markets, foreign currency and cash collateral.
- (h) Futures consist of exchange-traded financial contracts encompassing U.S. Equity, International Equity and U.S. Government indices.
- (i) Private Equity consists of global equity funds that are not exchange-traded.
- (j) Real Estate investments include real estate funds based on appraised values that are broadly diversified by geography and property type.
- (k) Hedge Funds are within a commingled structure which invests in various hedge fund managers who can invest in all financial instruments.
- (l) The Company sets aside funds for retiree health benefits through a separate account within the pension trust, as permitted under Section 401(h) of the Internal Revenue Code of 1986, as amended. In accordance with the Code, the plan's investments in the 401(h) account may not be used for, or diverted to, any purpose other than providing health benefits for retirees. The net assets held in the 401(h) account are calculated based on a pro-rata percentage allocation of the net assets in the pension plan. The related obligations for health benefits are not included in the pension plan's obligations and are included in the Company's other postretirement benefit obligation. See Note F.
- (m) Pending activities include security purchases and sales that have not settled, interest and dividends that have not been received and reflects adjustments for available estimates at year end.
- (n) In accordance with ASU 2015-07, Fair Value Measurements (Topic 820): Disclosures for Investments in Certain Entities That Calculate Net Asset Value per Share (or its equivalent), certain investments that are measured at fair value using the net asset value per share (or its equivalent) practical expedient have not been classified in the fair value hierarchy.

The fair values of the pension plan assets at December 31, 2018 by asset category are as follows:

<i>(Millions of Dollars)</i>	Level 1	Level 2	Total
Investments within the fair value hierarchy			
U.S. Equity (a)	\$3,515	\$10	\$3,525
International Equity (b)	2,896	—	2,896
U.S. Government Issued Debt (c)	—	1,886	1,886
Corporate Bonds Debt (d)	—	2,619	2,619
Structured Assets Debt (e)	—	6	6
Other Fixed Income Debt (f)	—	121	121
Cash and Cash Equivalents (g)	160	556	716
Futures (h)	568	—	568
Total investments within the fair value hierarchy	\$7,139	\$5,198	\$12,337
Investments measured at NAV per share (n)			
Private Equity (i)			440
Real Estate (j)			1,310
Hedge Funds (k)			255
Total investments valued using NAV per share			\$2,005
Funds for retiree health benefits (l)	(118)	(86)	(204)
Funds for retiree health benefits measured at NAV per share (l)(n)			(33)
Total funds for retiree health benefits			\$(237)
Investments (excluding funds for retiree health benefits)	\$7,021	\$5,112	\$14,105
Pending activities (m)			(655)
Total fair value of plan net assets			\$13,450

(a) - (n) Reference is made to footnotes (a) through (n) in the above table of pension plan assets at December 31, 2019 by asset category.

O&R also offers a defined contribution savings plan that covers substantially all employees and made contributions to the plan as follows:

<i>(Millions of Dollars)</i>	For the Years Ended December 31,		
	2019	2018	2017
O&R	\$4	\$4	\$4

Notes to the Consolidated Financial Statements - continued

Note F – Other Postretirement Benefits

The Company currently has contributory comprehensive hospital, medical and prescription drug programs for eligible retirees, their dependents and surviving spouses. In addition, the Company has a non-contributory life insurance program for retirees.

Total Periodic Benefit Cost

The components of the Company's total periodic other postretirement benefit costs for 2019, 2018 and 2017 were as follows:

<i>(Millions of Dollars)</i>	2019	2018	2017
Service cost – including administrative expenses	\$5	\$6	\$6
Interest cost on projected other postretirement benefit obligation	8	8	9
Expected return on plan assets	(11)	(10)	(9)
Recognition of net actuarial loss	1	5	6
Recognition of prior service credit	(1)	(4)	(6)
TOTAL PERIODIC OTHER POSTRETIREMENT BENEFIT COST	\$2	\$5	\$6
Cost capitalized	(2)	(2)	(2)
Reconciliation to rate level	5	(1)	(2)
Total expense recognized	\$5	\$2	\$2

For information about the adoption of ASU 2017-07, "Compensation-Retirement Benefits (Topic 715): Improving the Presentation of Net Periodic Pension Cost and Net Periodic Postretirement Benefit Cost," see Note E.

Funded Status

The funded status of the programs at December 31, 2019, 2018 and 2017 were as follows:

<i>(Millions of Dollars)</i>	2019	2018	2017
CHANGE IN BENEFIT OBLIGATION			
Benefit obligation at beginning of year	\$201	\$234	\$191
Service cost	5	6	6
Interest cost on accumulated postretirement benefit obligation	8	8	9
Amendments	(14)	—	—
Net actuarial loss/(gain)	12	(38)	37
Benefits paid and administrative expenses, net of subsidies	(10)	(10)	(10)
Participant contributions	1	1	1
BENEFIT OBLIGATION AT END OF YEAR	\$203	\$201	\$234
CHANGE IN PLAN ASSETS			
Fair value of plan assets at beginning of year	\$125	\$144	\$122
Actual return on plan assets	32	(12)	20
Employer contributions	1	1	8
Employer group waiver plan subsidies	1	2	3
Participant contributions	1	1	1
Benefits paid	(8)	(11)	(10)
FAIR VALUE OF PLAN ASSETS AT END OF YEAR	\$152	\$125	\$144
FUNDED STATUS	\$(51)	\$(76)	\$(90)
Unrecognized net loss	\$6	\$16	\$38
Unrecognized prior service costs	(16)	(3)	(7)

Notes to the Consolidated Financial Statements - continued

The decrease in the other postretirement benefits liability at O&R of \$25 million, compared with December 31, 2018, was primarily due to an increase in plan assets as a result of the actual return on plan assets. This decreased liability corresponds with a decrease to regulatory assets of \$19 million for unrecognized net losses and unrecognized prior service costs associated with O&R's New York utility business consistent with the accounting rules for regulated operations, a credit to OCI of \$2 million (net of taxes) for the unrecognized net losses and a credit to OCI of \$3 million (net of taxes) for the unrecognized prior service costs associated with RECO.

A portion of the unrecognized net losses and prior service costs for the other postretirement benefits, equal to \$5 million and \$(2) million, respectively, will be recognized from accumulated OCI and the regulatory asset into net periodic benefit cost over the next year for O&R.

Assumptions

The actuarial assumptions were as follows:

	2019	2018	2017
Weighted-average assumptions used to determine benefit obligations at December 31:			
Discount Rate	3.35%	4.30%	3.70%
Weighted-average assumptions used to determine net periodic benefit cost for the years ended December 31:			
Discount Rate	4.30%	3.70%	4.20%
Expected Return on Plan Assets	8.10%	7.50%	7.50%

Refer to Note E for descriptions of the basis for determining the expected return on assets, investment policies and strategies and the assumed discount rate.

The health care cost trend rate used to determine net periodic benefit cost for the years ended December 31, 2019, 2018 and 2017 was 5.40 percent, 5.60 percent and 5.80 percent, respectively, which is assumed to decrease gradually 4.50 percent by 2024 and remain at that level thereafter. The health care cost trend rate used to determine benefit obligations as of December 31, 2019, 2018 and 2017 was 5.20 percent, 5.40 percent and 5.60 percent, respectively, which is assumed to decrease gradually to 4.50 percent by 2024 and remain at that level thereafter.

A one-percentage point change in the assumed health care cost trend rate would have the following effects at December 31, 2019:

<i>(Millions of Dollars)</i>	One-Percentage Point	
	Increase	Decrease
Effect on accumulated other postretirement benefit obligation	\$27	\$(20)
Effect on service cost and interest cost components for 2019	3	(2)

Notes to the Consolidated Financial Statements - continued

Expected Benefit Payments

Based on current assumptions, O&R expects to make the following benefit payments over the next ten years, net of receipt of governmental subsidies and participant contributions:

<i>(Millions of Dollars)</i>	2020	2021	2022	2023	2024	2025-2029
O&R	\$10	\$10	\$10	\$10	\$10	\$54

Expected Contributions

Based on estimates as of December 31, 2019, O&R expects to make an immaterial contribution to the other postretirement benefit plans in 2020.

Plan Assets

The asset allocations for O&R's other postretirement benefit plans at the end of 2019, 2018 and 2017 and the target allocation for 2020 are as follows:

Asset Category	Target Allocation Range	Plan Assets at December 31,		
	2020	2019	2018	2017
Equity Securities	75% -85%	81%	79%	80%
Debt Securities	15% - 25%	19%	21%	20%
Total	100%	100%	100%	100%

Con Edison has established postretirement health and life insurance benefit plan trusts for the investment of assets to be used for the exclusive purpose of providing other postretirement benefits to participants and beneficiaries.

Refer to Note E for a discussion of Con Edison's investment policy for the assets held by its benefit plans.

The fair values of the plans' assets at December 31, 2019 by asset category as defined by the accounting rules for fair value measurements (see the fair value hierarchy defined in Note L) are as follows:

<i>(Millions of Dollars)</i>	Level 1	Level 2	Total
Equity (a)	\$—	\$123	\$123
Other Fixed Income Debt (b)	—	28	28
Cash and Cash Equivalents (c)	—	1	1
Total investments	\$—	\$152	\$152
Pending activities (d)			—
Total fair value of plan net assets			\$152

- (a) Equity includes a passively managed commingled index fund benchmarked to the MSCI All Country World Index.
- (b) Other Fixed Income Debt includes a passively managed commingled index fund benchmarked to the Bloomberg Barclays U.S. Long Credit Index and an active separately managed fund indexed to the Bloomberg Barclays U.S. Long Credit Index.
- (c) Cash and Cash Equivalents include short term investments and money markets.
- (d) Pending activities include security purchases and sales that have not settled, interest and dividends that have not been received, and reflects adjustments for available estimates at year-end.

The fair values of the plan assets at December 31, 2018 by asset category (see the fair value hierarchy defined in Note L) are as follows:

Notes to the Consolidated Financial Statements - continued

<i>(Millions of Dollars)</i>	Level 1	Level 2	Total
Equity (a)	\$—	\$99	\$99
Other Fixed Income Debt (b)	—	25	25
Cash and Cash Equivalents (c)	—	1	1
Total investments	\$—	\$125	\$125
Pending activities (d)			—
Total fair value of plan net assets			\$125

(a) - (d) Reference is made to footnotes (a) through (d) in the above table of other postretirement benefit plan assets at December 31, 2019 by asset category.

Note G – Environmental Matters

Superfund Sites

Hazardous substances, such as asbestos, polychlorinated biphenyls (PCBs) and coal tar, have been used or generated in the course of operations of O&R and its predecessors and are present at sites and in facilities and equipment they currently or previously owned, including sites at which gas was manufactured or stored.

The Federal Comprehensive Environmental Response, Compensation and Liability Act of 1980 and similar state statutes (Superfund) impose joint and several liability, regardless of fault, upon generators of hazardous substances for investigation and remediation costs (which include costs of demolition, removal, disposal, storage, replacement, containment and monitoring) and natural resource damages. Liability under these laws can be material and may be imposed for contamination from past acts, even though such past acts may have been lawful at the time they occurred. The sites at which O&R has been asserted to have liability under these laws, including its manufactured gas plant sites and any neighboring areas to which contamination may have migrated, are referred to herein as “Superfund Sites.”

For Superfund Sites where there are other potentially responsible parties and O&R is not managing the site investigation and remediation, the accrued liability represents an estimate of the amount O&R will need to pay to investigate and, where determinable, discharge its related obligations. For Superfund Sites (including the manufactured gas plant sites) for which O&R is managing the investigation and remediation, the accrued liability represents an estimate of the Company’s share of the undiscounted cost to investigate and remediate the sites. Remediation costs are estimated in light of the information available, applicable remediation standards and experience with similar sites.

The accrued liabilities and regulatory assets related to Superfund Sites at December 31, 2019 and 2018 were as follows:

<i>(Millions of Dollars)</i>	2019	2018
Accrued Liabilities:		
Manufactured gas plant sites	\$79	\$84
Other Superfund Sites	1	1
Total	\$80	\$85
Regulatory assets	\$85	\$94

Notes to the Consolidated Financial Statements - continued

The Superfund Sites have been investigated. However, for some of the sites, the extent and associated cost of the required remediation has not yet been determined. As information pertaining to the required remediation becomes available, the Company expects that additional liability may be accrued, the amount of which is not presently determinable but may be material. The Company is permitted to recover or defer as regulatory assets (for subsequent recovery through rates) prudently incurred site investigation and remediation costs. See “Other Regulatory Matters” in Note B.

Environmental remediation costs incurred related to Superfund Sites were \$7 million for the years ended December 31, 2019 and 2018.

No insurance or other third-party recoveries were received by the Company for the year ended December 31, 2019. Insurance and other third-party recoveries received by the Company for the year ended December 31, 2018 were immaterial.

O&R estimates that in 2020, it will incur costs for remediation of approximately \$3 million. The Company is unable to estimate the time period over which the remaining accrued liability will be incurred because, among other things, the required remediation has not been determined for some of the sites.

In 2019, O&R estimated that for its manufactured gas plant sites, each of which has been investigated, the aggregate undiscounted potential liability for the remediation of coal tar and/or other environmental contaminants could range up to \$136 million. These estimates were based on assumptions regarding the extent of contamination and the type and extent of remediation that may be required. Actual experience may be materially different.

Notes to the Consolidated Financial Statements - continued

Asbestos Proceedings

Suits have been brought in New York State and federal courts against O&R and many other defendants, wherein a large number of plaintiffs sought large amounts of compensatory and punitive damages for deaths and injuries allegedly caused by exposure to asbestos at various O&R premises. The suits that have been resolved, which are many, have been resolved without any payment by O&R, or for amounts that were not, in the aggregate, material to the Company. The amounts specified in all the remaining suits total billions of dollars; however, the Company believes that these amounts are greatly exaggerated, based on the disposition of previous claims. At December 31, 2019 and 2018, the Company had accrued its estimated aggregate undiscounted potential liability for these suits and additional suits that may be brought over the next 15 years as shown in the following table. The estimates were based upon a combination of modeling, historical data analysis and risk factor assessment. Courts have begun, and unless otherwise determined on appeal may continue, to apply different standards for determining liability in asbestos suits than the standard that applied historically. As a result, the Company currently believes that there is a reasonable possibility of an exposure to loss in excess of the liability accrued for the suits. The Company is unable to estimate the amount or range of such loss. In addition, certain current and former employees have claimed or are claiming workers' compensation benefits based on alleged disability from exposure to asbestos. The Company defers as regulatory assets (for subsequent recovery through rates) liabilities incurred for asbestos claims by employees and third-party contractors relating to its divested generating plants.

The Company's accrued liability for asbestos suits and workers' compensation proceedings (including those related to asbestos exposure) and the amounts deferred as regulatory assets for the Company at December 31, 2019 and 2018 were as follows:

<i>(Millions of Dollars)</i>	2019	2018
Accrued liability – asbestos suits	\$0.4	\$0.4
Regulatory assets – asbestos suits	0.4	0.4
Accrued liability – workers' compensation	\$5.0	\$4.0

Note H - Leases

In January 2019, the Company early adopted Accounting Standards Update (ASU) No. 2016-02, "Leases (Topic 842)," including the amendments thereto, using a modified retrospective transition method of adoption that required no prior period adjustments or charges to retained earnings for cumulative impact. The standard supersedes the lease requirements within ASC Topic 840, "Leases."

The Company leases office buildings, equipment and access rights to support electric distribution facilities. Upon adoption of Topic 842, the Company recognized lease right-of-use assets and lease liabilities on its balance sheets for virtually all of its leases (other than leases that meet the definition of a short-term lease, the expense for which was immaterial). A lease right-of-use asset represents a right to use an identifiable underlying asset and obtain substantially all of the economic benefits from the use of that asset for the lease term. A lease liability represents an obligation to make lease payments arising from the lease. Leases are

Notes to the Consolidated Financial Statements - continued

classified as either operating leases or finance leases. Operating leases are included in operating lease right-of-use asset and operating lease liabilities on the Company's balance sheet. Finance leases are included in other noncurrent assets, other current liabilities and other noncurrent liabilities. The Company, as a regulated entity, is permitted to continue to recognize expense for operating leases using the timing that conforms to the regulatory rate treatment as rental payments are recovered from our customers and to account the same way for finance leases. Lessor accounting is similar to the previous model but updated to align with ASC Topic 606 "Revenue from Contracts with Customers."

The Company elected the following practical expedients: (1) a package of practical expedients that allows the Company to not reassess: (a) whether expired or existing contracts contained leases; (b) the lease classification for expired or existing leases and (c) the initial direct costs for existing leases; (2) for all underlying asset classes, an expedient that allows the Company to not apply the recognition requirements to short-term leases and an expedient that will allow the Company to account for lease and associated non-lease components as a single lease component; (3) an expedient that allows the use of hindsight to determine lease term; and (4) an expedient that allows the Company to not evaluate under Topic 842 land easements that exist or expired before the entity's adoption of Topic 842 and that were not previously accounted for as leases under Topic 840.

The Company, upon adoption of Topic 842 recognized, and for new operating leases at commencement date recognizes, operating lease right-of-use assets and operating lease liabilities based on the present value of the future minimum lease payments over the lease term. As most of the Company's leases do not provide an implicit rate, the Company used its collateralized incremental borrowing rate based on the information available at the commencement date to determine the present value of future payments. Most of the Company's leases have remaining lease terms of one year to 12 years and may include options to renew or extend the leases for up to five years at the fair rental value. The Company's lease terms include options to renew, extend or terminate the lease when it is reasonably certain that the Company will exercise that option. There were no leases with material variable lease payments or residual value guarantees.

Operating lease cost and cash paid for amounts included in the measurement of lease liabilities for the twelve months ended December 31, 2019, were as follows:

<i>(Millions of Dollars)</i>	2019
Operating lease cost	\$1.0
Operating lease cash flows	\$0.9

As of December 31, 2019, assets recorded as finance leases for O&R were \$1.0 million, and the accumulated amortization associated with finance leases for O&R was \$1.7 million. For the twelve months ended December 31, 2019, finance lease costs and cash flows for O&R were immaterial.

Right-of-use assets obtained in exchange for lease obligations were immaterial for O&R for the twelve months ended December 31, 2019.

Notes to the Consolidated Financial Statements - continued

Other information related to leases for O&R at December 31, 2019 was as follows:

Weighted Average Remaining Lease Term:	
Operating leases	3.7 years
Finance leases	19.2 years
Weighted Average Discount Rate:	
Operating leases	3.8%
Finance leases	3.1%

Future minimum lease payments under non-cancellable leases at December 31, 2019 were as follows:

<i>(Millions of Dollars)</i>			
Year Ending December 31,	Operating Leases	Finance Leases	
2020	\$1.0	\$—	
2021	1.0	—	
2022	0.5	—	
2023	—	—	
2024	—	0.1	
All years thereafter	0.2	0.7	
Total future minimum lease payments	\$2.7	\$0.8	
Less: imputed interest	(0.1)	(0.2)	
Total	\$2.6	\$0.6	
Reported as of December 31, 2019			
Operating lease liabilities (current)	\$0.9	\$—	
Operating lease liabilities (noncurrent)	1.7	—	
Other noncurrent liabilities	—	0.6	
Total	\$2.6	\$0.6	

At December 31, 2019, the Company does not have material obligations under operating or finance leases that have not yet commenced.

Disclosures related to the twelve months ended December 31, 2019 are presented as required under Topic 842. Prior period disclosures for the year ended December 31, 2018 are presented under Topic 840. The Company has elected to use a practical expedient provided by Topic 842 whereby comparative disclosures for prior periods are allowed to be presented under Topic 840. The disclosures presented under Topic 842 and Topic 840 will not be fully comparable in specific disclosure requirements.

The future minimum lease commitments at December 31, 2018, accounted for under Topic 840, for the Company's operating lease agreements that are not cancellable by the Company were as follows:

Notes to the Consolidated Financial Statements - continued

(Millions of Dollars)

2019	\$1.0
2020	0.9
2021	0.9
2022	0.5
2023	0.1
All years thereafter	0.2
Total	\$3.6

The Company is a lessor under certain leases whereby the Company owns real estate and leases portions of it to others. Revenue under such leases was immaterial for O&R for the twelve months ended December 31, 2019.

Note I – Income Tax

The components of income tax for O&R are as follows:

<i>(Millions of Dollars)</i>	2019	2018	2017
State			
Current	\$2	\$—	\$7
Deferred	4	4	(1)
Federal			
Current	15	(2)	23
Deferred	(4)	13	13
Total income tax expense	\$17	\$15	\$42

The tax effects of temporary differences, which gave rise to deferred tax assets and liabilities, are as follows:

<i>(Millions of Dollars)</i>	2019	2018
Deferred tax liabilities:		
Property basis differences	\$426	\$419
Regulatory assets:		
Unrecognized pension and other postretirement costs	39	35
Environmental remediation costs	24	26
Deferred storm costs	21	21
Other regulatory assets	21	21
Operating lease right-of-use asset	1	—
Total deferred tax liabilities	532	522
Deferred tax assets:		
Accrued pension and other postretirement costs	\$68	\$68
Regulatory liabilities		
Future income tax	40	40
Other regulatory liabilities	78	75
Superfund and other environmental costs	22	23
Asset retirement obligations	1	—
Loss carryforwards	1	2
Operating lease liabilities	1	—
Other	6	6
Total deferred tax assets	217	214
Net deferred tax liabilities	\$315	\$308
Unamortized investment tax credits	1	1
Net deferred tax liabilities and unamortized investment tax credits	\$316	\$309

Notes to the Consolidated Financial Statements - continued

Upon enactment of the TCJA in December 2017, O&R and RECO re-measured their deferred tax assets and liabilities based upon the TCJA's 21 percent corporate federal income tax rate. As a result, O&R decreased its net deferred tax liabilities by \$261 million (including \$45 million for RECO), decreased its regulatory asset for future income tax by \$68 million (including \$17 million for RECO), decreased the regulatory asset for revenue taxes by \$4 million, and accrued a regulatory liability for future income tax of \$189 million (including \$28 million for RECO). Since O&R is in a net regulatory liability position with respect to these income tax matters, O&R netted the regulatory asset for future income tax against the regulatory liability for future income tax. Under the rate normalization requirements continued by the TCJA, \$142 million of the net regulatory liability (including \$16 million for RECO) related to certain accelerated tax depreciation benefits is to be amortized over the remaining lives of the related assets. The remainder of the net regulatory liability is to be refunded (or credited) to customers as determined by the NYSPSC or NJBPU, as applicable. See "Other Regulatory Matters" in Note B. The re-measurement had no impact on O&R's and RECO's cash flows for 2017.

At December 31, 2017, O&R recorded provisional income tax amounts in its accounting for certain effects of the provisions of the TCJA as allowed under SEC Staff Accounting Bulletin 118 (SAB 118). SAB 118 allowed a one-year period for companies to finalize the provisional amounts recorded as of December 31, 2017. In August 2018, the Internal Revenue Service (IRS) and U.S. Department of Treasury issued proposed regulations that clarified provisions in the TCJA on the allowance for additional first-year depreciation for qualified property of regulated public utilities placed in service in the fourth quarter of 2017. Under this guidance, which Con Edison and its subsidiaries elected to adopt, O&R deducted \$29 million (and \$2 million for RECO) in additional depreciation in Con Edison's 2017 federal income tax return. The additional depreciation and other adjustments to O&R's temporary differences required a re-measurement of deferred tax assets and liabilities associated with the filing of its 2017 federal income tax return. As a result, O&R decreased its net deferred tax liabilities by \$7 million (including \$1 million for RECO), recorded an increase in O&R's retained earnings associated with the early adoption of ASU 2018-02, "Income Statement - Reporting Comprehensive Income (Topic 220): Reclassification of Certain Tax Effects from Accumulated Other Comprehensive Income," and accrued a regulatory liability for future income tax of \$3 million (including \$1 million for RECO). O&R and RECO completed their assessment in the fourth quarter of 2018 and no further adjustments to the provisional amounts were recorded.

Reconciliation of the difference between income tax expense and the amount computed by applying the prevailing statutory income tax rate to income before income taxes is as follows:

<i>(% of Pre-tax income)</i>	2019	2018	2017
STATUTORY TAX RATE			
Federal	21%	21%	35%
Changes in computed taxes resulting from:			
State income tax	6	6	4
Cost of removal	2	2	2
Amortization of excess deferred federal income taxes	(7)	(7)	—
Reversal of uncertain tax positions	—	(1)	—
Research and development credits	(1)	—	—
Other	(1)	—	(1)
Effective tax rate	20%	21%	40%

Notes to the Consolidated Financial Statements - continued

O&R deferred as regulatory liabilities its estimated net benefits under the TCJA for the year ended December 31, 2018. RECO deferred as a regulatory liability its estimated net benefits under the TCJA for the three months ended March 31, 2018. The net benefits include the revenue requirement impact of the reduction in the corporate federal income tax rate to 21 percent, the elimination for utilities of bonus depreciation and the amortization of excess deferred federal income taxes the utilities collected from customers that will not be paid to the IRS under the TCJA. See “Other Regulatory Matters” in Note B.

At December 31, 2019 RECO had a New Jersey State net operating loss carryover from tax years 2018 and 2019 of approximately \$14 million, due primarily to storm related costs and state tax depreciation. RECO will carry forward its New Jersey State net operating loss to future years, which will begin to expire, if unused, in 2038. A deferred tax asset for these tax attribute carryforwards was recorded, and no valuation allowance has been provided, as it is more likely than not that the deferred tax asset will be realized.

The Protecting Americans from Tax Hikes Act of 2015 extended bonus depreciation applying a 50 percent rate for property acquired and placed in service for years 2015 through 2017 with reduced rates of 40 percent and 30 percent for years 2018 and 2019, respectively. The TCJA does not allow bonus depreciation after December 31, 2017 (excluding certain transition rules) for companies that qualify as a utility company for the consolidated group under the de minimis exception to Treasury regulations.

In December 2019, the Federal government issued final regulations providing guidance on provisions in the TCJA allowing for full expensing of qualified plant additions. These provisions, which Con Edison and its subsidiaries adopted under the proposed regulations of August 2018, allowed O&R and RECO a full expense tax deduction for plant additions in the fourth quarter of 2017 and to continue additional first year depreciation transition rules for plant additions placed in service in tax years beginning in 2018, under long-term construction contracts entered into before September 28, 2017. The impact on O&R and RECO of these regulations is discussed above.

The TCJA provides for an exception to the interest expense limitation for utility companies allowing O&R and RECO the full deduction of interest expense for the years ended December 31, 2019 and 2018.

Uncertain Tax Positions

Under the accounting rules for income taxes, O&R is not permitted to recognize the tax benefit attributable to a tax position unless such position is more likely than not to be sustained upon examination by taxing authorities, including resolution of any related appeals and litigation processes, based solely on the technical merits of the position.

A reconciliation of the beginning and ending amounts of unrecognized tax benefits for O&R follows:

Notes to the Consolidated Financial Statements - continued

<i>(Millions of Dollars)</i>	2019	2018	2017
Balance at January 1,	\$2	\$3	\$3
Additions based on tax positions of prior years	—	—	—
Reductions for tax positions of prior years	(2)	—	—
Reductions from expiration of statute of limitations	—	(1)	—
Balance at December 31,	\$—	\$2	\$3

At December 31, 2019, the estimated liability for uncertain tax positions for O&R was an immaterial amount. In June 2019, the New Jersey Superior Court, Appellate Division, upheld the New Jersey Tax Court's ruling that RECO is required to add back the transitional energy facility assessment (TEFA) in computing its New Jersey taxable income. RECO will not ask for reconsideration or appeal this decision, and therefore, reversed both its \$2 million refund claim and its \$2 million reserve for uncertain tax positions. There was no impact to O&R's or RECO's effective tax rate.

O&R recognizes interest on liabilities for uncertain tax positions in interest expense and would recognize penalties, if any, in operating expenses in O&R's consolidated income statement. In 2019, 2018 and 2017, O&R recognized an immaterial amount of interest and no penalties for uncertain tax positions in its consolidated income statement. At December 31, 2019 and 2018, O&R recognized an immaterial amount of accrued interest on its consolidated balance sheet.

Con Edison and its subsidiaries' federal tax return for 2018 remains under examination. State income tax returns remain open for examination in New York for tax years 2010 through 2018 and in New Jersey for tax years 2008 through 2018.

Note J - Stock-Based Compensation

O&R may compensate employees under Con Edison's stock-based compensation plans with, among other things, stock options, restricted stock units and contributions to the stock purchase plan. The Long Term Incentive Plan, which was approved by Con Edison's shareholders in 2003 (2003 LTIP), and the Long Term Incentive Plan, which was approved by Con Edison's shareholders in 2013 (2013 LTIP), are collectively referred to herein as the LTIP. The LTIP provides for, among other things, awards to employees of restricted stock units and stock options. Existing awards under the 2003 LTIP continue in effect, however no new awards may be issued under the 2003 LTIP. The 2013 LTIP provides for awards for up to five million shares of common stock.

Shares of Con Edison common stock used to satisfy O&R's obligations with respect to stock-based compensation may be new (authorized, but unissued) shares, treasury shares or shares purchased in the open market. The shares used during the year ended December 31, 2019 were new shares. Con Edison intends to use new shares to fulfill its stock-based compensation obligations for 2020.

The Company has recognized stock-based compensation expense using a fair value measurement method. The following table summarizes stock-based compensation expense recognized by the Company in the years ended December 31, 2019, 2018, and 2017:

Notes to the Consolidated Financial Statements - continued

<i>(Millions of Dollars)</i>	2019	2018	2017
Performance-based restricted stock	\$2.9	\$0.1	\$4.9
Time-based restricted stock	0.2	0.1	0.1
Stock purchase plan	0.4	0.4	0.3
Total	\$3.5	\$0.6	\$5.3
Income tax benefit	\$1.0	\$0.2	\$2.1

Restricted Stock Units

Restricted stock unit awards under the LTIP have been made as follows: (i) awards that provide for adjustment of the number of units (performance-restricted stock units or Performance RSUs) to certain officers and employees; and (ii) time-based awards to certain employees. Restricted stock units awarded represents the right to receive, upon vesting, shares of Con Edison common stock, or the cash value of shares or a combination thereof.

The number of units in each annual Performance RSU award is subject to adjustment as follows: (i) 50 percent of the units awarded will be multiplied by a factor that may range from 0 to 200 percent, based on Con Edison's total shareholder return relative to a specified peer group during a specified performance period (the TSR portion); and (ii) 50 percent of the units awarded will be multiplied by factors that may range from 0 to 200 percent, based on determinations made in connection with O&R's annual incentive plans or, for certain executive officers, actual performance as compared to certain performance measures during a specified performance period (the non-TSR portion). Performance RSU awards generally vest upon completion of the performance period.

Performance against the established targets is recomputed each reporting period as of the earlier of the reporting date and the vesting date. The TSR portion applies a Monte Carlo simulation model, and the non-TSR portion is the product of the market price at the end of the period and the average non-TSR determination over the vesting period. Performance RSUs are "liability awards" because each Performance RSU represents the right to receive, upon vesting, one share of Con Edison common stock, the cash value of a share or a combination thereof. As such, changes in the fair value of the Performance RSUs are reflected in net income. The assumptions used to calculate the fair value of the awards were as follows:

	2019	2018	2017
Risk-free interest rate (a)	1.58% - 1.59%	2.48% - 2.63%	1.76% - 1.89%
Expected term (b)	3 years	3 years	3 years
Expected share price volatility (c)	12.89% - 15.51%	14.76% - 17.71%	11.01% - 14.70%

(a) The risk-free rate is based on the U.S. Treasury zero-coupon yield curve.

(b) The expected term of the Performance RSUs equals the vesting period. The Company does not expect significant forfeitures to occur.

(c) Based on historical experience.

Notes to the Consolidated Financial Statements - continued

A summary of changes in the status of the Performance RSUs' TSR and non-TSR portions during the year ended December 31, 2019 is as follows:

	Weighted Average Grant Date Fair Value (a)		
	Units	TSR Portion (b)	Non-TSR Portion (c)
Non-vested at December 31, 2018	81,758	\$74.82	\$74.25
Granted	33,640	64.21	79.93
Vested	(28,762)	83.33	71.73
Forfeited	(1,994)	65.31	78.21
Transferred (d)	64	66.80	77.01
Non-vested at December 31, 2019	84,706	\$67.93	\$77.18

- (a) The TSR and non-TSR Portions each account for 50 percent of the awards' value.
 (b) Fair value is determined using the Monte Carlo simulation described above. Weighted average grant date fair value does not reflect any accrual or payment of dividends prior to vesting.
 (c) Fair value is determined using the market price of one share of Con Edison common stock on the grant date. The market price has not been discounted to reflect that dividends do not accrue and are not payable on Performance RSUs until vesting.
 (d) Represents allocation to another Con Edison subsidiary of a portion of the Performance RSUs that had been awarded to an O&R officer who transferred to the other subsidiary.

The total expense to be recognized by the Company in future periods for unvested Performance RSUs outstanding at December 31, 2019 is \$3 million and is expected to be recognized over a weighted average period of one year. The Company paid cash of \$2 million in 2019, and \$1 million in 2018 and 2017 to settle vested Performance RSUs.

In accordance with the accounting rules for stock compensation, for time-based awards, the Company has accrued a liability based on the market value of a Con Edison common share on the grant date and is recognizing compensation expense over the vesting period. The vesting period for awards is three years and is based on the employee's continuous service to O&R. Prior to vesting, the awards are subject to forfeiture in whole or in part under certain circumstances. The awards are "liability awards" because each restricted stock unit represents the right to receive, upon vesting, one share of Con Edison common stock, the cash value of a share or a combination thereof. As such, prior to vesting, changes in the fair value of the units are reflected in net income. A summary of changes in the status of time-based awards during the year ended December 31, 2019 is as follows:

	Weighted Average Grant Date Fair Value	
	Units	Fair Value
Non-vested at December 31, 2018	3,800	\$77.46
Granted	1,500	84.81
Vested	(1,150)	76.62
Non-vested at December 31, 2019	4,150	\$80.35

The total expense to be recognized by the Company in future periods for unvested time-based awards outstanding at December 31, 2019 was immaterial and is expected to be recognized over a weighted average period of one year. The Company paid an immaterial amount of cash in 2019, 2018 and 2017 to settle vested time-based awards.

Notes to the Consolidated Financial Statements - continued

Stock Purchase Plan

Under the Con Edison Stock Purchase Plan, which was approved by shareholders in 2004 and 2014, the Company contributes up to \$1 for each \$9 invested by its officers or employees to purchase Con Edison common stock under the plan. Eligible participants may invest up to \$25,000 during any calendar year (subject to an additional limitation for officers and employees of not more than 20 percent of their pay). Dividends paid on shares held under the plan are reinvested in additional shares unless otherwise directed by the participant.

Participants in the plan immediately vest in shares purchased by them under the plan. The fair value of the shares of Con Edison common stock purchased under the plan was calculated using the average of the high and low composite sale prices at which shares were traded at the New York Stock Exchange on the trading day immediately preceding such purchase dates. During 2019, 2018 and 2017, 747,899, 786,385 and 719,125 shares were purchased under the Stock Purchase Plan at a weighted average price of \$85.45, \$78.27 and \$79.57 per share, respectively.

Note K – Derivative Instruments and Hedging Activities

The Company hedges market price fluctuations associated with physical purchases and sales of electricity, natural gas and, to a lesser extent, refined fuels by using derivative instruments including futures, forwards and options. These are economic hedges, for which the Company does not elect hedge accounting. Derivatives are recognized on the consolidated balance sheet at fair value (see Note L), unless an exception is available under the accounting rules for derivatives and hedging. Qualifying derivative contracts that have been designated as normal purchases or normal sales contracts are not reported at fair value under the accounting rules.

In August 2017, the FASB issued amendments to the guidance for derivatives and hedging through ASU 2017-12, "Derivatives and Hedging (Topic 815): Targeted Improvements to Accounting for Hedging Activities." The amendments in this update provide greater clarification on hedge accounting for risk components, presentation and disclosure of hedging instruments, and overall targeted improvements to simplify hedge accounting. The amendments are effective for reporting periods beginning after December 15, 2019. The application of the guidance would not have a material impact on the Company's financial position, results of operations and liquidity because the Company does not elect hedge accounting for its derivative instruments and hedging activities.

Notes to the Consolidated Financial Statements - continued

The fair values of the Company's commodity derivatives including the offsetting of assets and liabilities on the consolidated balance sheet at December 31, 2019 and 2018 were:

<i>(Millions of Dollars)</i>	2019			2018		
Balance Sheet Location	Gross Amounts of Recognized Assets/ (Liabilities)	Gross Amounts Offset	Net Amounts of Assets/ (Liabilities) (a)	Gross Amounts of Recognized Assets/ (Liabilities)	Gross Amounts Offset	Net Amounts of Assets/ (Liabilities) (a)
Fair value of derivative assets						
Current	\$—	\$—	\$— (b)	\$1	\$—	\$1
Noncurrent	—	—	—	3	(2)	1
Total fair value of derivative assets	\$—	\$—	\$—	\$4	\$(2)	\$2
Fair value of derivative liabilities						
Current	\$(13)	\$1	\$(12)	\$(6)	\$(1)	\$(7)
Noncurrent	(8)	1	(7)	(6)	2	(4)
Total fair value of derivative liabilities	\$(21)	\$2	\$(19)	\$(12)	\$1	\$(11)
Net fair value derivative assets/(liabilities)	\$(21)	\$2	\$(19)	\$(8)	\$(1)	\$(9)

- (a) Derivative instruments and collateral were offset on the consolidated balance sheet as applicable under the accounting rules. The Company enters into master agreements for its commodity derivatives. These agreements typically provide offset in the event of contract termination. In such case, generally the non-defaulting party's payable will be offset by the defaulting party's payable. The non-defaulting party will customarily notify the defaulting party within a specific time period and come to an agreement on the early termination amount.
- (b) At December 31, 2019, margin deposits of \$1 million were classified as derivative assets on the consolidated balance sheet, but not included in the table. Margin is collateral, typically cash, that the holder of a derivative instrument is required to deposit in order to transact on an exchange and to cover its potential losses with its broker or the exchange

The Company generally recovers its prudently incurred purchased power and gas costs, including hedging gains and losses, in accordance with rate provisions approved by the applicable state utility regulators. See "Recoverable Energy Costs" in Note A. In accordance with the accounting rules for regulated operations, the Company records a regulatory asset or liability to defer recognition of unrealized gains and losses on its electric and gas derivatives. As gains and losses are realized in future periods, they will be recognized as purchased power, gas and fuel costs in the Company's consolidated income statements.

O&R and CECONY (CECONY together with O&R, the Utilities) have combined their gas requirements, and contracts to meet those requirements, into a single portfolio. The combined portfolio is administered by, and related management services (including hedging market price fluctuations associated with the physical purchase of gas) are provided by, CECONY (for itself and as agent for O&R) and costs (net of the effect of the related hedging transactions) are allocated between the Utilities in accordance with provisions approved by the NYSPSC. See Note N.

Notes to the Consolidated Financial Statements - continued

The following table presents the realized and unrealized gains or losses on commodity derivatives that have been deferred for the years ended December 31, 2019 and 2018:

<i>(Millions of Dollars)</i>	Balance Sheet Location	2019	2018
Pre-tax gains/(losses) deferred in accordance with accounting rules for regulated operations:			
Current	Deferred derivative gains	\$(1)	\$(1)
Noncurrent	Deferred derivative gains	(2)	1
Total deferred gains/(losses)		\$(3)	\$—
Current	Deferred derivative losses	\$(8)	\$(5)
Current	Recoverable energy costs	(18)	—
Noncurrent	Deferred derivative losses	(2)	1
Total deferred gains/(losses)		\$(28)	\$(4)
Net deferred gains/(losses)		\$(31)	\$(4)

The following table presents the hedged volume of the Company's commodity derivative transactions at December 31, 2019:

Electric Energy (MWh) (a)	Capacity (MW) (a)	Natural Gas (Dt) (a)
2,380,870	3,990	15,680,000

(a) Volumes are reported net of long and short positions.

The Company is exposed to credit risk related to transactions entered into primarily for the various electric supply and hedging activities. Credit risk relates to the loss that may result from a counterparty's nonperformance. The Company uses credit policies to manage this risk, including an established credit approval process, monitoring of counterparty limits, netting provisions within agreements and collateral or prepayment arrangements. The Company measures credit risk exposure as the replacement cost for open energy commodity and derivative positions plus amounts owed from counterparties for settled transactions. The replacement cost of open positions represents unrealized gains, net of any unrealized losses where the Company has a legally enforceable right of offset.

At December 31, 2019, the Company had \$1 million of credit exposure in connection with open energy supply net receivables and hedging activities, net of collateral, related to investment-grade counterparties and exchange brokers.

The collateral requirements associated with, and settlement of, derivative transactions are included in net cash flows from operating activities in the Company's consolidated statement of cash flows. Most derivative instrument contracts contain provisions that may require a party to provide collateral on its derivative instruments that are in a net liability position. The amount of collateral to be provided will depend on the fair value of the derivative instruments and the party's credit ratings.

The following table presents the aggregate fair value of the Company's derivative instruments with credit-risk-related contingent features that are in a net liability position, the collateral posted for such positions and the additional collateral that would have been required to be posted had the lowest applicable credit rating been reduced one level and to below investment grade at December 31, 2019:

Notes to the Consolidated Financial Statements - continued

(Millions of Dollars)

Aggregate fair value – net liabilities (a)	\$19
Collateral posted	—
Additional collateral (b) (downgrade one level from current ratings)	8
Additional collateral (b) (downgrade to below investment grade from current ratings)	23 (c)

- (a) Non-derivative transactions for the purchase and sale of electricity, gas and qualifying derivative instruments, which have been designated as normal purchases or normal sales, are excluded from the table. These transactions primarily include purchases of electricity from independent system operators. In the event the Company was no longer extended unsecured credit for such purchases, the Company would not be required to post collateral at December 31, 2019. For certain other such non-derivative transactions, the Company could be required to post collateral under certain circumstances, including in the event counterparties had reasonable grounds for insecurity.
- (b) The additional collateral amounts shown above are based upon the estimated O&R allocation of the Utilities' collateral requirements. The Utilities measure the collateral requirements by taking into consideration the fair value amounts of derivative instruments that contain credit-risk-related contingent features that are in a net liabilities position plus amounts owed to counterparties for settled transactions and amounts required by counterparties for minimum financial security. The fair value amounts represent unrealized losses, net of any unrealized gains where the Company has a legally enforceable right of offset.
- (c) Derivative instruments that are net assets have been excluded from the table. At December 31, 2019, if the Company had been downgraded to below investment grade, it would have been required to post an immaterial amount of additional collateral.

Note L – Fair Value Measurements

The accounting rules for fair value measurements and disclosures define fair value as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date in a principal or most advantageous market. Fair value is a market-based measurement that is determined based on inputs, which refer broadly to assumptions that market participants use in pricing assets or liabilities. These inputs can be readily observable, market corroborated, or generally unobservable firm inputs. The Company often makes certain assumptions that market participants would use in pricing the asset or liability, including assumptions about risk, and the risks inherent in the inputs to valuation techniques. The Company uses valuation techniques that maximize the use of observable inputs and minimize the use of unobservable inputs.

The accounting rules for fair value measurements and disclosures established a fair value hierarchy, which prioritizes the inputs to valuation techniques used to measure fair value in three broad levels. The rules require that assets and liabilities be classified in their entirety based on the level of input that is significant to the fair value measurement. Assessing the significance of a particular input may require judgment considering factors specific to the asset or liability and may affect the valuation of the asset or liability and their placement within the fair value hierarchy. The Company classifies fair value balances based on the fair value hierarchy defined by the accounting rules for fair value measurements and disclosures as follows:

- Level 1 – Consists of assets or liabilities whose value is based on unadjusted quoted prices in active markets at the measurement date. An active market is one in which transactions for assets or liabilities occur with sufficient frequency and volume to provide pricing information on an ongoing basis. This category includes contracts traded on active exchange markets valued using unadjusted prices quoted directly from the exchange.

Notes to the Consolidated Financial Statements - continued

- Level 2 – Consists of assets or liabilities valued using industry standard models and based on prices, other than quoted prices within Level 1, that are either directly or indirectly observable as of the measurement date. The industry standard models consider observable assumptions including time value, volatility factors, and current market and contractual prices for the underlying commodities, in addition to other economic measures. This category includes contracts traded on active exchanges or in over-the-counter markets priced with industry standard models.

- Level 3 – Consists of assets or liabilities whose fair value is estimated based on internally developed models or methodologies using inputs that are generally less readily observable and supported by little, if any, market activity at the measurement date. Unobservable inputs are developed based on the best available information and subject to cost benefit constraints. This category includes contracts priced using models that are internally developed and contracts placed in illiquid markets. It also includes contracts that expire after the period of time for which quoted prices are available and internal models are used to determine a significant portion of the value.

Assets and liabilities measured at fair value on a recurring basis as of December 31, 2019 and 2018 are summarized below.

<i>(Millions of Dollars)</i>	2019					2018				
	Level 1	Level 2	Level 3	Netting Adjustment (e)	Total	Level 1	Level 2	Level 3	Netting Adjustment (e)	Total
Derivative assets:										
Commodity (a)(b)(c)	\$—	\$—	\$—	\$1	\$1	\$—	\$3	\$—	\$—	\$3
Other (a)(b)(d)	20	6	—	—	26	20	5	—	—	25
Total assets	\$20	\$6	\$—	\$1	\$27	\$20	\$8	\$—	\$—	\$28
Derivative liabilities:										
Commodity (a)(b)(c)	\$1	\$11	\$9	\$(2)	\$19	\$—	\$2	\$9	\$—	\$11

- (a) The Company's policy is to review the fair value hierarchy and recognize transfers into and transfers out of the levels at the end of each reporting period. There were \$2 million of commodity derivative liabilities transferred from level 3 to level 2 during the year ended December 31, 2019 because of availability of observable market data due to the decrease in the terms of certain contracts from beyond three years as of September 30, 2019 to less than three years as of December 31, 2019. There were no transfers between levels 1, 2 and 3 for the year ended December 31, 2018.
- (b) Level 2 assets and liabilities include investments held in the deferred compensation plan and/or non-qualified retirement plans, exchange-traded contracts where there is insufficient market liquidity to warrant inclusion in Level 1, and certain over-the-counter derivative instruments for electricity and natural gas. Derivative instruments classified as Level 2 are valued using industry standard models that incorporate corroborated observable inputs; such as pricing services or prices from similar instruments that trade in liquid markets, time value and volatility factors.
- (c) The accounting rules for fair value measurements and disclosures require consideration of the impact of nonperformance risk (including credit risk) from a market participant perspective in the measurement of the fair value of assets and liabilities. At December 31, 2019 and 2018, the Company determined that nonperformance risk would have no material impact on its financial position or results of operation.
- (d) Other assets are comprised of assets such as life insurance contracts within the non-qualified retirement plan.
- (e) Amounts represent the impact of legally-enforceable master netting agreements that allow the Company to net gain and loss positions and cash collateral held or placed with the same counterparties.

CECONY's risk management group develops and maintains the valuation policies and procedures for, and verifies pricing and fair value valuation of, commodity derivatives for the Utilities. Under CECONY's policies and procedures, multiple independent sources of information are obtained for forward price curves used to value commodity derivatives. Fair value and changes in fair value of commodity derivatives are reported on a monthly

Notes to the Consolidated Financial Statements - continued

basis to the Utilities' risk committees, comprised of officers and employees of the Utilities that oversee energy hedging. The risk management group reports to CECONY's Vice President and Treasurer.

Commodity	Fair Value of Level 3 at December 31, 2019 (Millions of Dollars)	Valuation Techniques	Unobservable Inputs	Range
Electricity	\$(9)	Discounted Cash Flow	Forward capacity prices (a)	\$0.15-\$8.90 per kW- month

(a) Generally, increases/(decreases) in this input in isolation would result in a higher/(lower) fair value measurement.

The table listed below provides a reconciliation of the beginning and ending net balances for assets and liabilities measured at fair value for the years ended December 31, 2019 and 2018 and classified as Level 3 in the fair value hierarchy:

<i>(Millions of Dollars)</i>	2019	2018
Beginning balance as of January 1,	\$(9)	\$(4)
Included in earnings	(7)	2
Included in regulatory assets and liabilities	1	(6)
Purchases	—	—
Settlements	8	(1)
Transfer out of level 3	(2)	—
Ending balance as of December 31,	\$(9)	\$(9)

Realized gains and losses on Level 3 commodity derivative assets and liabilities are reported as part of purchased power costs. The Company generally recovers these costs in accordance with rate provisions approved by the applicable state public utilities regulators. See Note A. Unrealized gains and losses for commodity derivatives are generally deferred on the consolidated balance sheet in accordance with the accounting rules for regulated operations.

Note M - Asset Retirement Obligations

The Company recognizes a liability at fair value for legal obligations associated with the retirement of long-lived assets in the period in which they are incurred, or when sufficient information becomes available to reasonably estimate the fair value of such legal obligations. The Company evaluates these assumptions underlying the asset retirement obligation liability on an annual basis or as frequently as needed. The Company recorded asset retirement obligations associated with the removal of asbestos and asbestos-containing material in its substations and electric equipment. At December 31, 2019, the liabilities for asset retirement obligations of the Company were \$3 million. At December 31, 2018, the liabilities for asset retirement obligations of the Company were immaterial.

The Company includes in depreciation rates the estimated removal costs, less salvage, for utility plant assets. The amounts related to removal costs that are associated with asset retirement obligations are classified as an asset retirement liability. Pursuant to accounting rules for regulated operations, future removal costs that do not represent legal asset retirement obligations are recorded as regulatory liabilities. Accretion and depreciation

Notes to the Consolidated Financial Statements - continued

expenses related to removal costs that represent legal asset retirement obligations are applied against the Company's regulatory liabilities. Asset retirement costs that are recoverable from customers are recorded as regulatory liabilities to reflect the timing difference between costs recovered through the rate-making process and recognition of costs. The related net regulatory liabilities recorded for the Company were \$146 million and \$138 million at December 31, 2019 and 2018, respectively.

Note N – Related Party Transactions

The NYSPSC generally requires that the Company and Con Edison's other subsidiaries be operated as separate entities. The Company and Con Edison's unregulated subsidiaries are required to have separate operating employees and operating officers of the Company may not be operating officers of Con Edison's unregulated subsidiaries. The Company may provide and receive administrative and other services to and from Con Edison and its subsidiaries only pursuant to cost allocation procedures developed in accordance with rules approved by the NYSPSC and/or other regulatory authorities, as applicable. Transfers of assets between the Company and Con Edison or its other subsidiaries may be made only as approved by the NYSPSC. The debt of the Company is to be raised directly by the Company and not derived from Con Edison. Without the prior permission of the NYSPSC, the Company may not make loans to, guarantee the obligations of, or pledge assets as security for the indebtedness of Con Edison or its other subsidiaries. The NYSPSC limits the dividends that the Company may pay Con Edison. See "Common Stock" in Note C. As a result, substantially all of the net assets of O&R (\$762 million) at December 31, 2019 are considered restricted net assets. The NYSPSC may impose additional measures to separate, or "ring fence," the Company from Con Edison and its other subsidiaries. See "Rate Plans" in Note B.

The services received include substantial administrative support operations, such as corporate secretarial and associated managerial duties, accounting, treasury, investor relations, information resources, legal, human resources, fuel supply and energy management services. The costs of administrative and other services provided by the Company, and received from Con Edison and its other subsidiaries for the years ended December 31, 2019, 2018 and 2017 were as follows:

<i>(Millions of Dollars)</i>	2019	2018	2017
Cost of services provided	\$19	\$28	\$17
Cost of services received	\$57	\$55	\$52

At December 31, 2019 and 2018, O&R's payable to Con Edison and its other subsidiaries associated with these services was \$4 million and \$5 million, respectively. In addition, at December 31, 2019 and 2018, the Company's receivable from CECONY related to aid provided for storm restoration activities was an immaterial amount and \$6 million, respectively.

In addition, CECONY and O&R have joint gas supply arrangements, in connection with which O&R purchased from CECONY \$71 million and \$83 million of natural gas for the years ended December 31, 2019 and 2018, respectively. These amounts are net of the effect of related hedging transactions. At December 31, 2019 and

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2018, O&R's net payable to CECONY associated with these gas purchases was \$8 million and \$9 million, respectively.

At December 31, 2019 and 2018, the Company's net payable to Con Edison for income taxes was \$12 million and \$11 million, respectively.

FERC has authorized CECONY through 2019 to periodically lend funds to O&R, for periods of not more than 12 months, in amounts not to exceed \$250 million outstanding at any time, at prevailing market rates. At December 31, 2019 and 2018, there were no loans outstanding for O&R.

Note O – New Financial Accounting Standards

In January 2020, the Company adopted ASU 2016-13, "Financial Instruments-Credit Losses (Topic 326): Measurement of Credit Losses on Financial Instruments." The amendments replace the incurred loss impairment methodology which involved delayed recognition of credit losses. The amendments introduce an expected credit loss impairment model which requires immediate recognition of anticipated losses over the instrument's life. A broader range of reasonable and supportable information must be considered in developing the credit loss estimates. The Company's financial instruments subject to the amendments include their accounts receivable - customers and other receivables. The adoption of this guidance will not have a material impact on the Company's financial position, results of operations and liquidity. The Company will prepare additional disclosures as required by the amendments beginning in 2020. The Company implemented additional internal controls related to the amendments, however the adoption of the amendments will not require a change that will materially affect the Company's internal control over financial reporting.

In January 2020, the Company adopted ASU 2017-04, "Intangibles-Goodwill and Other (Topic 350): Simplifying the Test for Goodwill Impairment." The amendments in this update simplify goodwill impairment testing by eliminating Step 2 of the goodwill impairment test wherein an entity has to compute the implied fair value of goodwill by performing procedures to determine the fair value of its assets and liabilities. Under the new guidance, an entity will recognize an impairment charge for the amount by which the carrying amount exceeds the reporting unit's fair value up to the total amount of goodwill allocated to that reporting unit. The adoption of this guidance will not have a material impact on the Company's financial position, results of operations and liquidity.

In December 2019, the FASB issued amendments to the guidance for income taxes through ASU 2019-12, "Income Taxes (Topic 740): Simplifying the Accounting for Income Taxes." The amendments in this update simplify the accounting for income taxes by removing certain exceptions such as: 1) the incremental approach for intraperiod tax allocation when there is a loss from continuing operations and income or a gain from other items, 2) the requirement to recognize a deferred tax liability for equity method investments when a foreign subsidiary becomes an equity method investment, 3) the ability not to recognize a deferred tax liability for a foreign subsidiary when a foreign equity method investment becomes a subsidiary, and 4) the general methodology for calculating income taxes in an interim period when a year-to-date loss exceeds the anticipated

Notes to the Consolidated Financial Statements - continued

loss for the year. The amendments are effective for fiscal years beginning after December 15, 2021 and interim periods within fiscal years beginning after December 15, 2022, with early adoption permitted. The Company is in the process of evaluating the potential impact of the new guidance on the Company's financial position, results of operations and liquidity.