

Orange and Rockland Utilities, Inc.
2010 Annual Financial Statements and Notes

Financial Statements

Report of Independent Registered Public Accounting Firm

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Report of Independent Auditors

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

In our opinion, the accompanying consolidated balance sheet and the related consolidated statements of capitalization, of income, of comprehensive income, of common shareholder's equity and of cash flows present fairly, in all material respects, the financial position of Orange and Rockland Utilities, Inc. and its subsidiaries at December 31, 2010 and 2009, and the results of their operations and their cash flows for each of the three years in the period ended December 31, 2010 in conformity with accounting principles generally accepted in the United States of America. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits. We conducted our audits of these statements in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

PricewaterhouseCoopers LLP

March 11, 2011

Orange and Rockland Utilities, Inc.
CONSOLIDATED INCOME STATEMENT

	For the Years Ended December 31,		
	2010	2009	2008
	(Millions of Dollars)		
OPERATING REVENUES			
Electric	\$ 692	\$ 648	\$ 733
Gas	218	242	259
TOTAL OPERATING REVENUES	910	890	992
OPERATING EXPENSES			
Purchased power	335	328	433
Gas purchased for resale	99	136	159
Other operations and maintenance	275	247	222
Depreciation and amortization	44	42	40
Taxes, other than income taxes	49	45	44
TOTAL OPERATING EXPENSES	802	798	898
OPERATING INCOME	108	92	94
OTHER INCOME (DEDUCTIONS)			
Investment and other income	-	2	4
Allowance for equity funds used during construction	3	1	-
Other deductions	(1)	(1)	(1)
TOTAL OTHER INCOME (DEDUCTIONS)	2	2	3
INCOME BEFORE INTEREST AND INCOME TAX EXPENSE	110	94	97
INTEREST EXPENSE			
Interest on long-term debt	32	27	25
Other interest	5	2	3
Allowance for borrowed funds used during construction	(2)	(1)	-
NET INTEREST EXPENSE	35	28	28
INCOME BEFORE TAXES	75	66	69
INCOME TAX EXPENSE	26	23	25
NET INCOME	\$ 49	\$ 43	\$ 44

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

Orange and Rockland Utilities, Inc.
CONSOLIDATED STATEMENT OF CASH FLOWS

	For the Twelve Months Ended December 31,		
	2010	2009	2008
	(Millions of Dollars)		
OPERATING ACTIVITIES			
Net income	\$ 49	\$ 43	\$ 44
PRINCIPAL NON-CASH CHARGES/(CREDITS) TO INCOME			
Depreciation and amortization	44	42	40
Deferred income taxes	19	41	16
Other non-cash items (net)	17	1	(23)
CHANGES IN ASSETS AND LIABILITIES			
Accounts receivable - customers, less allowance for uncollectibles	(13)	29	(9)
Accounts receivable from affiliated companies	(17)	15	(22)
Materials and supplies, including gas in storage	4	30	(18)
Prepayments, other receivables and other current assets	20	(40)	(9)
Recoverable energy costs	6	(20)	25
Accounts payable	-	58	(65)
Accounts payable to affiliated companies	10	(32)	19
Pensions and retiree benefits	5	(13)	37
Accrued taxes	-	-	(1)
Accrued interest	3	(5)	(1)
Deferred charges, noncurrent assets and other regulatory assets	(72)	29	(76)
Deferred credits and other regulatory liabilities	(3)	(8)	46
Superfund and other environmental costs	67	-	(3)
Other liabilities	7	(4)	11
NET CASH FLOWS FROM OPERATING ACTIVITIES	146	166	11
INVESTING ACTIVITIES			
Utility construction expenditures	(135)	(127)	(120)
Increase in restricted cash	(1)	-	-
Cost of removal less salvage	(4)	(5)	(3)
NET CASH FLOWS USED IN INVESTING ACTIVITIES	(140)	(132)	(123)
FINANCING ACTIVITIES			
Net payments of short-term debt	-	-	(45)
Issuance of long-term debt	170	120	50
Retirement of long-term debt	(158)	(4)	(3)
Capital contribution by parent	-	30	40
Dividend to parent	(32)	(32)	(31)
Loan (to)/from affiliate	-	(113)	58
NET CASH FLOWS (USED IN)/FROM FINANCING ACTIVITIES	(20)	1	69
CASH AND TEMPORARY CASH INVESTMENTS:			
NET CHANGE FOR THE PERIOD	(14)	35	(43)
BALANCE AT BEGINNING OF PERIOD	52	17	60
BALANCE AT END OF PERIOD	\$ 38	\$ 52	\$ 17
SUPPLEMENTAL DISCLOSURE OF CASH FLOW INFORMATION			
Cash paid/(refunded) during the period for:			
Interest	\$30	\$33	\$ 29
Income taxes	\$7	(\$12)	\$ 34

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

Orange and Rockland Utilities, Inc.
CONSOLIDATED BALANCE SHEET

	December 31, 2010	December 31, 2009
	(Millions of Dollars)	
ASSETS		
CURRENT ASSETS		
Cash and temporary cash investments	\$ 38	\$ 52
Accounts receivable - customers, less allowance for uncollectible accounts of \$5 in 2010 and 2009	71	58
Accrued unbilled revenue	46	56
Other receivables, less allowance for uncollectible accounts of \$1 in 2010 and 2009	11	22
Accounts receivable from affiliated companies	29	12
Gas in storage, at average cost	28	31
Materials and supplies, at average cost	9	10
Prepayments	17	15
Deferred derivative losses	39	37
Recoverable energy costs	13	31
Revenue decoupling mechanism receivable	6	10
Other current assets	9	6
TOTAL CURRENT ASSETS	316	340
INVESTMENTS	10	10
UTILITY PLANT, AT ORIGINAL COST		
Electric	1,117	1,076
Gas	499	446
General	165	158
Total	1,781	1,680
Less: Accumulated depreciation	494	464
Net	1,287	1,216
Construction work in progress	113	87
NET UTILITY PLANT	1,400	1,303
DEFERRED CHARGES, REGULATORY ASSETS AND NONCURRENT ASSETS		
Regulatory assets	585	513
Other deferred charges and noncurrent assets	26	21
TOTAL DEFERRED CHARGES, REGULATORY ASSETS AND NONCURRENT ASSETS	611	534
TOTAL ASSETS	\$ 2,337	\$ 2,187

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

Orange and Rockland Utilities, Inc.
CONSOLIDATED BALANCE SHEET

	December 31, 2010	December 31, 2009
	(Millions of Dollars)	
LIABILITIES AND SHAREHOLDER'S EQUITY		
CURRENT LIABILITIES		
Long-term debt due within one year	\$ 3	\$ 103
Accounts payable	88	88
Accounts payable to affiliated companies	34	24
Customer deposits	13	14
Accrued interest	9	6
Fair value of derivative liabilities	22	36
Deferred income taxes - recoverable energy costs	5	12
Accrued wages	9	2
Other current liabilities	33	25
TOTAL CURRENT LIABILITIES	216	310
NONCURRENT LIABILITIES		
Provision for injuries and damages	7	7
Pensions and retiree benefits	387	386
Superfund and other environmental costs	120	53
Fair value of derivative liabilities	24	30
Other noncurrent liabilities	3	-
TOTAL NONCURRENT LIABILITIES	541	476
DEFERRED CREDITS AND REGULATORY LIABILITIES		
Deferred income taxes and investment tax credits	308	268
Regulatory liabilities	132	127
Other deferred credits	3	3
TOTAL DEFERRED CREDITS AND REGULATORY LIABILITIES	443	398
LONG-TERM DEBT (See Statement of Capitalization)	610	497
SHAREHOLDER'S EQUITY		
Common shareholder's equity (See Statement of Common Shareholder's Equity)	527	506
TOTAL SHAREHOLDER'S EQUITY	527	506
TOTAL LIABILITIES AND SHAREHOLDER'S EQUITY	\$ 2,337	\$ 2,187

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

Orange and Rockland Utilities, Inc.
CONSOLIDATED STATEMENT OF COMMON SHAREHOLDER'S EQUITY

(Millions of Dollars/Except Share Data)	Shares	<u>Common Stock</u> Amount	Additional Paid-In Capital	Retained Earnings	Accumulated Other Comprehensive Income/(Loss)	Total
BALANCE AS OF DECEMBER 31, 2007	1,000	\$ -	\$ 234	\$ 215	\$ (33)	\$ 416
Net Income				44		44
Common stock dividend to parent				(31)		(31)
Capital contribution by parent			40			40
Other comprehensive loss					(14)	(14)
BALANCE AS OF DECEMBER 31, 2008	1,000	\$ -	\$ 274	\$ 228	\$ (47)	\$ 455
Net Income				43		43
Common stock dividend to parent				(32)		(32)
Capital contribution by parent			30			30
Other comprehensive income					10	10
BALANCE AS OF DECEMBER 31, 2009	1,000	\$ -	\$ 304	\$ 239	\$ (37)	\$ 506
Net Income				49		49
Common stock dividend to parent				(32)		(32)
Other comprehensive income					4	4
BALANCE AS OF DECEMBER 31, 2010	1,000	\$ -	\$ 304	\$ 256	\$ (33)	\$ 527

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

Orange and Rockland Utilities, Inc.
CONSOLIDATED STATEMENT OF COMPREHENSIVE INCOME

	For the Years Ended December 31,		
	2010	2009	2008
	(Millions of Dollars)		
NET INCOME	\$ 49	\$ 43	\$ 44
OTHER COMPREHENSIVE INCOME/(LOSS), NET OF TAXES			
Pension plan liability adjustments, net of \$3, \$7 and \$(14) taxes in 2010, 2009 and 2008, respectively	4	10	(20)
Unrealized losses on derivatives qualified as cash flow hedges, net of \$(1) taxes in 2008	-	-	(1)
Less: Reclassification adjustment gains/(losses) included in net income	-	-	1
Less: Reclassification adjustment for unrealized losses included in regulatory assets, net of \$(5) taxes in 2008	-	-	(8)
TOTAL OTHER COMPREHENSIVE INCOME/(LOSS), NET OF TAXES	4	10	(14)
COMPREHENSIVE INCOME	\$ 53	\$ 53	\$ 30

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

Orange and Rockland Utilities, Inc.
CONSOLIDATED STATEMENT OF CAPITALIZATION

	Shares outstanding		At December 31,	
	December 31, 2010	2009	2010	2009
(Millions of Dollars)				
TOTAL COMMON SHAREHOLDER'S EQUITY BEFORE ACCUMULATED OTHER COMPREHENSIVE LOSS	1,000	1,000	\$ 560	\$ 543
TOTAL ACCUMULATED OTHER COMPREHENSIVE LOSS, NET OF TAXES - PENSION PLAN LIABILITY ADJUSTMENTS			(33)	(37)
TOTAL COMMON SHAREHOLDER'S EQUITY (SEE STATEMENT OF COMMON SHAREHOLDER'S EQUITY)			\$ 527	\$ 506
LONG-TERM DEBT	Interest			
Maturity	Rate	Series		
DEBENTURES:				
2010	7.50%	2000A	\$ -	\$ 55
2015	5.30	2005A	40	40
2015	2.50	2010A	55	-
2016	5.45	2006A	75	75
2018	6.15	2008A	50	50
2019	4.96	2009A	60	60
2027	6.50	1997F	80	80
2029	7.00	1999G	-	45
2039	6.00	2009B	60	60
2040	5.50	2010B	115	-
TOTAL DEBENTURES			535	465
FIRST MORTGAGE BONDS:				
2018	7.07%	1998C	3	3
TOTAL FIRST MORTGAGE BONDS			3	3
TRANSITION BONDS:				
2019*	5.22%	2004-1	32	34
TOTAL TRANSITION BONDS			32	34
TAX-EXEMPT DEBT - Notes Issued to New York State Energy Research and Development Authority for Pollution Control Refunding Revenue Bonds**:				
2014	0.40%	1994A	-	55
2015	0.34	1995A	44	44
TOTAL TAX-EXEMPT DEBT			44	99
Unamortized debt discount			(1)	(1)
TOTAL			613	600
Less: long-term debt due within one year			3	103
TOTAL LONG-TERM DEBT			610	497
TOTAL CAPITALIZATION			\$ 1,137	\$ 1,003

* The final date to pay the entire remaining unpaid principal balance, if any, of all outstanding bonds is May 17, 2021.

** Rates reset weekly; December 31, 2010 rates shown for Series 1995A (August 18, 2010 rate shown for Series 1994A).

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

Notes to the Financial Statements

General

These notes accompany and form an integral part of the 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 two regulated utility subsidiaries: Rockland Electric Company (RECO) and Pike County Light & Power Company (Pike). For the year ended December 31, 2010, 2009, and 2008, operating revenues for RECO and Pike were 25.6 percent and 0.8 percent, 24.9 percent and 0.8 percent, and 24.4 percent and 0.8 percent, respectively, of O&R's consolidated operating revenues. O&R, along with its regulated utility subsidiaries, provides electric service in southeastern New York and adjacent areas of northern New Jersey and eastern Pennsylvania and gas service in southeastern New York and adjacent areas of eastern Pennsylvania. RECO owns 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 Public Service Commission (NYSPSC), the New Jersey Board of Public Utilities (NJBPU) and the Pennsylvania Public Utility Commission (PAPUC) with respect to rates and accounting.

Note A – Summary of Significant Accounting Policies

Principles of Consolidation

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

Accounting Policies

The accounting policies of the Company conform to accounting principles generally accepted in the United States of America. These accounting principles include the accounting rules for regulated operations and the accounting requirements of the FERC and the state public utility regulatory commissions 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 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 receiving or being credited with a return on all of its regulatory assets for which a cash outflow has been made, and is paying or being charged with a return on all of its regulatory liabilities for which a cash inflow has been received. The

Notes to the Financial Statements - Continued

Company's regulatory assets and liabilities will be recovered from customers, or applied for customer benefit, in accordance with rate provisions approved by the applicable public utility regulatory commission.

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

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 (AFDC). 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 AFDC 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 AFDC rates for the Company were 5.8 percent, 4.2 percent and 3.5 percent for 2010, 2009 and 2008, 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 rate for the Company was 2.8 percent for 2010, 2009 and 2008.

The estimated lives for utility plant for the Company range from 5 to 65 years for electric, 5 to 75 years for gas and 5 to 50 years for general plant.

At December 31, 2010 and 2009, the capitalized cost of the Company's utility plant, net of accumulated depreciation, was as follows:

(Millions of Dollars)	2010	2009
Electric		
Transmission	\$134	\$137
Distribution	642	618
Gas*	382	334
General	116	115
Held for future use	13	12
Construction work in progress	113	87
NET UTILITY PLANT	\$1,400	\$1,303

* Primarily distribution.

Under O&R's current rate plans, the aggregate annual depreciation allowance in effect at December 31, 2010 was \$45 million.

Notes to the Financial Statements - Continued

Impairments

In accordance with the accounting rules for impairment or disposal of long-lived assets, the Company evaluates 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 an evaluation indicates that such cash flows cannot be expected to be sufficient to fully recover the assets, the assets are written down to their estimated fair value.

Revenues

The Company recognizes revenues for energy service on a monthly billing cycle basis. The Company generally 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. The Company accrues revenues at the end of each month for estimated energy service not yet billed to customers. Unbilled revenues included in O&R's balance sheet at December 31, 2010 and 2009 were \$46 million and \$56 million, respectively.

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 on a periodic basis, with the authorized delivery revenues and the difference accrued, with interest, for refund to, or recovery from, customers, as applicable. See "Rate Agreements" in Note B.

O&R and Pike are required to record gross receipts tax and RECO is required to record transitional energy facilities assessment (TEFA) tax as revenues and expenses on a gross income statement presentation basis (i.e., included in both revenue and expense). The recovery of these taxes is included in the revenue requirement within each of the respective approved rate plans. O&R and Pike recorded \$7.8 million and \$0.3 million, \$6.7 million and \$0.3 million, and \$6.1 million and \$0.3 million, of gross receipts tax in 2010, 2009 and 2008, respectively. RECO recorded \$6.4 million, \$6.1 million and \$6.4 million in TEFA tax in 2010, 2009 and 2008, respectively.

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.

Notes to the Financial Statements - Continued

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 price contracts ranging from one to three years that are competitively bid through the NJBPU auction process and provided through the Pennsylvania-Jersey-Maryland (PJM) Independent System Operator. 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.

Pike bills its customers for the electricity it supplies to them based on a default service rate approved by the PAPUC. Pike defers the difference between actual and billed electric supply costs to charge or refund customers during the next billing cycle (normally within one or two months) through a default service supply adjustment charge.

New York Independent System Operator

O&R purchases electricity for all its New York and Pennsylvania requirements and a portion of its New Jersey needs through the wholesale electricity market administered by the New York Independent System Operator (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 cash surrender value and include the supplemental retirement income plan's corporate-owned life insurance 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

Notes to the Financial Statements - Continued

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 net periodic benefit cost or income pursuant to the current recognition and amortization provisions.

For O&R, but not RECO and Pike, regulatory accounting treatment is applied in accordance with the accounting rules for regulated operations. Unrecognized prior service costs or credits and unrecognized gains and losses are recorded to regulatory assets or liabilities, rather than OCI. See Notes E and F.

The net 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 agreements, 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. The rate plans for RECO and Pike do not have comparable deferral provisions. See Note B – Regulatory Matters.

The Company calculates the expected return on pension and other retirement 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 for temporary differences between the book and tax basis of assets and liabilities at current tax rates. In accordance with rate agreements, 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 tax liability, in accordance with the accounting rules for regulated operations, the Company has established regulatory assets for the net revenue requirements to be recovered from customers for the related future tax expense. See Notes B and I. In 1993, the NYSPSC issued a Policy Statement approving accounting procedures consistent with accounting rules for income taxes and providing assurances that these future increases in taxes will be recoverable in rates. See Note I.

Notes to the Financial Statements - Continued

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's federal income tax return reflects certain tax positions with which the Internal Revenue Service (IRS) does not or may not agree. See "Uncertain Tax Positions" in Note I.

The Company, along with Con Edison and its other subsidiaries, files a consolidated federal income tax return. The consolidated federal 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 tax sharing agreements between the members of the consolidated group.

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 of the group pays or receives an amount 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.

Pike files a Pennsylvania Corporate Net Income Tax Return. The income of Pike is subject to Pennsylvania taxation, after adjustments for differences between federal and Pennsylvania law.

Reclassification

Certain prior year amounts have been reclassified to conform with the current year presentation.

Estimates

The preparation of financial statements in conformity with generally accepted accounting principles 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.

Note B – Regulatory Matters

Rate Agreements

Electric

In October 2007, the NYSPSC issued an order that continued O&R's rates for electric service rendered in New York at current levels. The order, which was based on an allowed annual rate of return on common equity of 9.1

Notes to the Financial Statements - Continued

percent increased, effective July 1, 2007, by \$13.1 million annually the amount recognized for pension and other postretirement benefit costs. Because O&R, in accordance with applicable New York regulatory provisions, defers the difference between the actual amount of such costs and the amounts for such costs reflected in rates, the effect of the increase was to decrease the company's deferrals of such costs and increase other operations and maintenance expense by a like amount. As required by the order, the company also reduced other operating revenues and recorded a regulatory liability of \$3 million for earnings attributable to its New York electric business in excess of a 9.1 percent annual rate of return on common equity applicable to the period March through June 2007. In June 2007, O&R commenced an action in New York State Supreme Court seeking to annul the March 2007 NYSPSC order that initiated the proceeding in which the October 2007 order was issued.

In July 2008, the NYSPSC approved a Joint Proposal among O&R, the NYSPSC staff and other parties for the rates O&R can charge its New York customers for electric service from July 2008 through June 2011. The rate plan approved by the NYSPSC provides for electric rate increases of \$15.6 million, \$15.6 million and \$5.7 million effective July 1, 2008, 2009 and 2010, respectively, and the collection of an additional \$9.9 million during the 12-month period beginning July 1, 2010.

The Joint Proposal reflected the following major items:

- an annual return on common equity of 9.4 percent;
- most of any actual earnings above a 10.2 percent return on equity (based on actual average common equity ratio, subject to a 50 percent maximum) are to be applied to reduce regulatory assets for pension and other postretirement benefit expenses (the company did not reduce regulatory assets under this provision in 2010, 2009 or 2008);
- deferral as a regulatory asset or regulatory liability, as the case may be, of the difference between actual pension and other postretirement benefit expenses, environmental remediation expenses, property taxes, tax-exempt debt costs and certain other expenses and amounts for those expenses reflected in rates (the company deferred recognition of \$0.7 million of revenue, and \$3 million and \$6 million of expenses under this provision in 2010, 2009 and 2008, respectively);
- deferral as a regulatory liability of the revenue requirement impact (i.e., return on investment, depreciation and income taxes) of the amount, if any, by which actual transmission and distribution related capital expenditures are less than amounts reflected in rates (the company deferred \$12 million, \$8 million and \$1 million of expenses under this provision in 2010, 2009 and 2008, respectively);
- deferral as a regulatory asset of increases, if any, in certain expenses above a 4 percent annual inflation rate, but only if the actual annual return on common equity is less than 9.4 percent (the company did not defer any expenses under this provision in 2010, 2009 or 2008);

Notes to the Financial Statements - Continued

- potential negative earnings adjustments of up to \$3 million annually if certain customer service and system reliability performance targets are not met (the company reduced revenues by \$0.4 million under these provisions in 2008; the company met the performance targets in 2009; and the company reduced revenues by \$1 million under these provisions in 2010);
- implementation of a revenue decoupling mechanism under which actual energy delivery revenues would be compared, on a periodic basis, with the authorized delivery revenues with the difference accrued, with interest, for refund to, or recovery from, customers, as applicable (the company accrued for recovery from customers \$5.0 million, \$12.4 million and \$3.6 million of revenues pursuant to this provision in 2010, 2009 and 2008, respectively);
- continuation of the rate provisions pursuant to which the company recovers its purchased power costs from customers; and
- withdrawal of the litigation O&R commenced seeking to annul the NYSPSC's March and October 2007 orders relating to O&R's electric rates.

In July 2010, O&R filed a request with the NYSPSC for an increase in the rates it charges for electric service rendered in New York, effective July 2011, of \$61.7 million. The filing reflects a return on common equity of 11 percent and a common equity ratio of 49.9 percent. Among other things, the filing proposes continuation of the current provisions with respect to recovery from customers of the cost of purchased power and with respect to the deferral of differences between actual expenses allocable to the electric business for pensions and other postretirement benefits, environmental, and research and developmental costs to the amounts for such costs reflected in electric rates. The filing also includes an alternative proposal for a three-year electric rate plan with annual rate increases of \$47.1 million effective July 2011, and \$33.2 million effective July 2012 and 2013. The multi-year filing reflects a return on common equity of 11.55 percent.

In March 2007, the NJBPU approved a new three-year electric base rate plan for RECO that went into effect on April 1, 2007. The plan provided for a \$6.4 million rate increase during the first year, with no further increase during the final two years. The plan reflected a return on common equity of 9.75 percent and a common equity ratio of 46.5 percent of capitalization.

In May 2010, RECO, the Division of Rate Counsel, Staff of the NJBPU and certain other parties entered into a stipulation of settlement with respect to the company's August 2009 request to increase the rates that it can charge its customers for electric delivery service. The stipulation, which was approved by the Board of the NJBPU, provides for an electric rate increase, effective May 17, 2010, of \$9.8 million. The stipulation reflects a return on common equity of 10.3 percent and a common equity ratio of approximately 50 percent. The stipulation continues current provisions with respect to recovery from customers of the cost of purchased power and does

Notes to the Financial Statements - Continued

not provide for reconciliation of actual expenses to amounts reflected in electric rates for pension and other postretirement benefit costs.

In March 2009, the PAPUC approved a settlement agreement between Pike and the other parties to the proceeding which provides for increases in rates, effective April 2009, to produce additional annual electric operating revenues of \$0.9 million.

Gas

In October 2006, the NYSPSC approved the June 2006 settlement agreement among O&R, the staff of the NYSPSC and other parties. The settlement agreement established a rate plan that covered the three-year period November 1, 2006 through October 31, 2009. The rate plan provided for rate increases in base rates of \$12 million in the first year, \$0.7 million in the second year and \$1.1 million in the third year. To phase-in the effect of the increase for customers, the rate plan provided for O&R to accrue revenues for, but defer billing to customers of, \$5.5 million of the first rate year rate increase by establishing a regulatory asset which, together with interest, was billed to customers in the second and third years. As a result, O&R's billings to customers increased \$6.5 million in each of the first two years and \$6.3 million in the third. The first year rate increase included \$2.3 million relating to a change in the way customers are provided the benefit of non-firm revenue from sales of pipeline transportation capacity. Under the prior rate plan, base rates were reduced to reflect the assumption that the company would realize these revenues. Under the 2006 rate plan, such revenues were used to offset the cost of gas to be recovered from customers. The rate plan continued the provisions pursuant to which the company recovers its cost of purchasing gas and the provisions pursuant to which the effects of weather on gas income are moderated.

The rate plan provided that if the actual amount of pension or other postretirement benefit costs, environmental remediation costs, property taxes and certain other costs vary from the respective amount for each such cost reflected in gas rates (cost reconciliations), the company would defer recognition of the variation in income and, as the case may be, establish a regulatory asset or liability for recovery from, or refund to, customers of the variation (86 percent of the variation, in the case of property tax differences due to assessment changes).

Earnings attributable to its gas business excluding any revenue reductions (O&R Adjusted Earnings) in excess of an 11 percent annual return on common equity (based upon the actual average common equity ratio, subject to a maximum 50 percent of capitalization) were to be allocated as follows: above an 11 percent return were to be used to offset up to one-half of any regulatory asset to be recorded in that year resulting from the cost reconciliations (discussed in the preceding paragraph). One-half of any remaining O&R Adjusted Earnings between 11 and 12 percent return were to be retained by the company, with the balance deferred for the benefit of customers. Thirty-five percent of any remaining O&R Adjusted Earnings between a 12 and 14 percent return were to be retained by the company, with the balance deferred for the benefit of customers. Any remaining O&R Adjusted Earnings above a 14 percent return were to be deferred for the benefit of customers. For purposes of these earnings sharing provisions, if in any rate year O&R Adjusted Earnings was less than 11 percent, the

Notes to the Financial Statements - Continued

shortfall was deducted from O&R Adjusted Earnings for the other rate years. The earnings sharing thresholds were to each be reduced by 20 basis points if certain objectives relating to the company's retail choice program are not met. O&R Adjusted Earnings were not in excess of the 11 percent target return on equity for the rate years ended October 31, 2009, and 2008.

The rate plan also included up to \$1 million of potential earnings adjustments in the first year of the agreement, increasing up to \$1.2 million, if the company did not comply with certain requirements regarding gas main protection and customer service. O&R recorded regulatory liabilities of \$0.4 million for not complying with certain requirements regarding safety and customer service for the rate year ended October 31, 2008. The company met these requirements for the rate year ended October 31, 2009.

In October 2009, the NYSPSC adopted a June 2009 Joint Proposal among O&R, NYSPSC staff and other parties. As approved, the Joint Proposal establishes a gas rate plan that covers the three-year period November 1, 2009 through October 31, 2012 and provides for increases in base rates of \$9 million in each of the first two years and \$4.6 million in the third year, with an additional \$4.3 million to be collected through a surcharge in the third rate year. The rate plan reflects the following major items:

- an annual return on common equity of 10.4 percent;
- most of any actual earnings above an 11.4 percent annual return on common equity (based upon the actual average common equity ratio, subject to a maximum 50 percent of capitalization) are to be applied to reduce regulatory assets; in 2010, O&R did not apply defer any revenues under this provision and the corresponding provision;
- deferral as a regulatory asset or liability, as the case may be, of differences between the actual level of certain expenses, including expenses for pension and other postretirement benefits, environmental remediation, property taxes and long-term debt, and amounts for those expenses reflected in rates; in 2010, the company accrued \$2.7 million of revenues under this provision and the corresponding provision of the previous rate plan;
- deferral as a regulatory liability of the revenue requirement impact (i.e., return on investment, depreciation and income taxes) of the amount, if any, by which average gas net plant balances are less than balances reflected in rates in 2010, the company accrued \$1.5 million of revenues under this provision and the corresponding provision of the previous rate plan;
- deferral as a regulatory asset of increases, if any over the course of the rate plan, in certain expenses above a 4 percent annual inflation rate, but only if the actual annual return on common equity is less than 10.4 percent;

Notes to the Financial Statements - Continued

- implementation of a revenue decoupling mechanism; in 2010, the company accrued \$0.8 million of revenues under this provision and the corresponding provision of the previous rate plan;
- continuation of the provisions pursuant to which the company recovers its cost of purchasing gas and the provisions pursuant to which the effects of weather on gas income are moderated; and
- potential negative earnings adjustments of up to \$1.4 million annually if certain operations and customer service requirements are not met; in 2010, there were no negative earnings adjustments recorded.

In February 2009, the PAPUC approved a settlement agreement between Pike and the other parties to the proceeding which provides for increases in rates, effective April 2009, to produce additional annual gas operating revenues of \$0.3 million.

Other Regulatory Matters

In April 2010, the NJBPU approved a March 2010 stipulation among RECO, the Division of Rate Counsel and Staff of the NJBPU, authorizing RECO to recover, through a customer bill surcharge, the revenue requirement impact associated with 50 percent of up to \$19.4 million of the costs of certain RECO smart electric grid projects for which RECO receives grants for the remaining 50 percent of such costs from the United States Department of Energy under the American Recovery and Reinvestment Act of 2009. The revenue requirement recovered through the bill surcharge includes a return on investment based upon a return on common equity of 10.3 percent. Pursuant to the stipulation, in the company's next base rate proceeding, the NJBPU will review the projects' costs, require the company to refund to customers amounts collected for costs, if any, that were not prudent, reasonable and incremental, and include in the company's rate base the remaining projects' costs.

Regulatory Assets and Liabilities

Regulatory assets and liabilities at December 31, 2010 and 2009 were comprised of the following items:

(Millions of Dollars)	2010	2009
Regulatory assets		
Unrecognized pension and other postretirement costs	\$219	\$213
Environmental remediation costs	122	59
Future federal income tax	78	68
Transition bond charges	48	55
Pension and other postretirement benefits deferrals	49	52
Deferred derivative losses	15	20
Storm reserve	14	5
Deferred losses on interest rate swap	10	11
Surcharge for New York State Assessment	9	12
Other	21	23
Regulatory assets	585	513
Deferred derivative losses - current	39	37
Recoverable energy costs - current	13	31
Total regulatory assets	\$637	\$581
Regulatory liabilities		
Allowance for cost of removal less salvage	\$72	\$68
Refundable energy costs	30	41
Carrying Charges on T&D Net Plant	23	9
NYS tax law changes	-	-

Notes to the Financial Statements - Continued

Other	7	7
Regulatory liabilities	132	127
Deferred derivative gains – current	1	-
Total regulatory liabilities	\$133	\$127

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

The increase in Regulatory Assets – Environmental Remediation Costs reflects an increased estimate of costs for site investigation and remediation. See Note G.

Note C – Capitalization

Common Stock

At December 31, 2010 and 2009, all of the outstanding common stock of the Company was 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

Long-term debt maturing in the period 2011-2015 is as follows:

(Millions of Dollars)	
2011	\$3
2012	3
2013	3
2014	4
2015	142

O&R has issued \$44 million of tax-exempt debt through the New York State Energy Research and Development Authority (NYSERDA) that currently bears interest at a rate determined weekly and is subject to tender by bondholders for purchase by the Company.

The carrying amounts and fair values of long-term debt are:

	December 31,			
	2010		2009	
	<i>(in millions)</i>		<i>(in millions)</i>	
	Carrying Amount	Fair Value	Carrying Amount	Fair Value
Long-Term Debt (including current portion)	\$ 613	\$ 666	\$ 600	\$ 622

Fair values of long-term debt have been estimated primarily using available market information.

Notes to the Financial Statements - Continued

At December 31, 2010 and 2009, long-term debt of the Company included \$3 million of mortgage bonds, collateralized by substantially all utility plant and other physical property of Pike. Long-term debt also included \$32 million and \$34 million at December 31, 2010 and 2009, respectively, 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.

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 tax-exempt financing arrangements of the Company are subject to these covenants and the covenants discussed below. The Company believes that it was in compliance with its significant debt covenants at December 31, 2010.

The tax-exempt financing arrangements involved the issuance of an uncollateralized promissory note of the Company to NYSERDA in exchange for the net proceeds of a like amount of tax-exempt bonds with substantially the same terms sold to the public by NYSERDA. The tax-exempt financing arrangements include covenants with respect to the tax-exempt status of the financing, including covenants with respect to the use of the facilities financed. The arrangements include provisions for the maintenance of liquidity and credit facilities, the failure to comply with which would, except as otherwise provided, constitute an event of default with respect to the debt. If an event of default were to occur, the principal and accrued interest on the debt might and, in certain circumstances would, become due and payable immediately.

The liquidity and credit facilities currently in effect for the tax-exempt financing include covenants that the ratio of debt to total capital of the Company will not at any time exceed 0.65 to 1 and that, subject to certain exceptions, the utility will not mortgage, lien, pledge or otherwise encumber its assets. The liquidity facility also includes as an event of default, defaults in payments of other debt obligations in excess of \$12.5 million.

Note D – Short-Term Borrowing

In June 2006, O&R along with Con Edison and CECONY, entered into an Amended and Restated Credit Agreement (Credit Agreement) under which banks committed to provide loans and letters of credit, on a revolving credit basis. In June 2007, the Credit Agreement, which was to expire in June 2011, was extended for an additional year. Under the Credit Agreement, there is a maximum of \$2.25 billion (\$2.2 billion in the additional year) of credit available, with \$200 million available to O&R. O&R is solely responsible for its obligations under the Credit Agreement and no company is responsible for the obligations of any company other than itself. O&R uses the Credit Agreement to support its commercial paper program and obtain letters of credit.

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

Notes to the Financial Statements - Continued

material adverse change. Upon a change of control of, or upon an event of default by Con Edison, CECONY or O&R, the banks may terminate their commitments with respect to that company and declare any amounts owed by that company under the Credit Agreement immediately due and payable. 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, 2010, this ratio was 0.53 to 1 for O&R); having liens on its assets in an aggregate amount exceeding 5 percent of its consolidated total capital, subject to certain exceptions; and the failure by O&R, following any applicable notice period, to meet certain other customary covenants. The fees charged to O&R for the revolving credit facilities and any loans made or letters of credit issued under the Credit Agreement reflect O&R's credit ratings.

At December 31, 2010 and 2009, O&R had no commercial paper outstanding. At December 31, 2010 and 2009, \$37 million and \$20 million of O&R letters of credit, and no O&R borrowings, were outstanding under the Credit Agreement, respectively. 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 and certain employees of Con Edison's competitive energy businesses. The plan is designed to comply with the Internal Revenue Code and the Employee Retirement Income Security Act of 1974. In addition, Con Edison maintains additional non-qualified pension plans covering certain current and retired O&R officers.

Net Periodic Benefit Cost

The components of the Company's net periodic benefit costs for 2010, 2009, and 2008 were as follows:

(Millions of Dollars)	2010	2009	2008
Service cost – including administrative expenses	\$11	\$10	\$10
Interest cost on projected benefit obligation	35	34	33
Expected return on plan assets	(33)	(32)	(31)
Amortization of net actuarial loss	24	27	22
Amortization of prior service costs	2	1	1
NET PERIODIC BENEFIT COST	\$39	\$40	\$35
Cost capitalized	(11)	(11)	(9)
Cost charged/(deferred)	(2)	(6)	-
Cost charged to operating expenses	\$26	\$23	\$26

Funded Status

The funded status of the Company's pension obligations at December 31, 2010, 2009, and 2008 were as follows:

(Millions of Dollars)	2010	2009	2008
CHANGE IN PROJECTED BENEFIT OBLIGATION			
Projected benefit obligation at beginning of year	\$602	\$586	\$553
Service cost – excluding administrative expenses	11	10	10
Interest cost on projected benefit obligation	35	34	33
Plan amendments	6	5	-
Net actuarial loss	29	1	19
Benefits paid	(32)	(34)	(29)
PROJECTED BENEFIT OBLIGATION AT END OF YEAR	\$651	\$602	\$586
CHANGE IN PLAN ASSETS			
Fair value of plan assets at beginning of year	\$330	\$271	\$370
Actual return on plan assets	41	54	(103)
Employer contributions	39	40	34

Notes to the Financial Statements - Continued

Benefits paid	(32)	(34)	(29)
Administrative expenses	(1)	(1)	(1)
FAIR VALUE OF PLAN ASSETS AT END OF YEAR	\$377	\$330	\$271
FUNDED STATUS	\$(274)	\$(272)	\$(315)
Unrecognized net loss	198	201	247
Unrecognized prior service costs	16	12	8
Accumulated benefit obligation	621	580	563

The increase in the pension plan's projected benefit obligation was a primary driver in the increased pension liability at O&R of \$1 million compared with December 31, 2009. This also resulted in an increase to regulatory assets of \$6 million for unrecognized net losses and unrecognized prior service costs associated with O&R's New York utility business consistent with accounting rules for regulated operations, and a credit to OCI of \$3 million (net of taxes) for the unrecognized net losses and unrecognized prior service costs associated with RECO and Pike.

The estimated net loss and prior service cost for the pension plan that will be amortized from accumulated OCI and the regulatory asset into net periodic benefit cost over the next year for O&R are \$29 million and \$2 million, respectively.

At December 31, 2010 and 2009, the Company's investments include \$10 million, held in an external trust account for benefit payments pursuant to the supplemental retirement plans. The accumulated benefit obligations for the supplemental retirement plans for O&R were \$34 million as of December 31, 2010 and 2009.

Assumptions

The actuarial assumptions were as follows:

	2010	2009	2008
Weighted-average assumptions used to determine benefit obligations at December 31:			
Discount rate	5.60%	6.05%	5.75%
Rate of compensation increase	4.25%	4.00%	4.00%
Weighted-average assumptions used to determine net periodic benefit cost for the years ended December 31:			
Discount rate	6.05%	5.75%	6.00%
Expected return on plan assets	8.50%	8.50%	8.50%
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 and were adjusted for historical and expected experience of active portfolio management results compared to benchmark returns.

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 (Aaa or Aa, by Moody's Investors Service) corporate bonds. Bonds with insufficient

Notes to the Financial Statements - Continued

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, they must have a price between 50 and 200, the yield must lie between 1 percent and 20 percent, and the amount of the issue 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:

(Millions of Dollars)	2011	2012	2013	2014	2015	2016-2020
O&R	\$34	\$36	\$38	\$39	\$41	\$224

Expected Contributions

Based on estimates as of December 31, 2010, the Company does not expect to be required under funding regulations and laws to make any contributions to the pension plan during 2011. The Company's policy is to fund its accounting cost to the extent tax deductible; therefore, O&R expects to make a discretionary contribution of \$41 million to the pension plan during 2011.

Plan Assets

The asset allocations for the pension plan at the end of 2010, 2009, and 2008, and the target allocation for 2011 are as follows:

ASSET CATEGORY	Target Allocation Range	Plan Assets at December 31,		
	2011	2010	2009	2008
Equity Securities	57%-73%	67%	67%	59%
Debt Securities	21%-33%	28%	28%	33%
Real Estate	5%-11%	5%	5%	8%
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 pension plan 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 plans' 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 named fiduciaries consist of Con Edison's chief executive, financial and accounting officers.

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, maximize the 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. 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 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 2010 reflects the results of such a study conducted in 2007.

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, manager 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.

In accordance with the accounting rules for pensions that became effective December 2009, the Company is providing the following disclosures regarding the fair value of the pension trust's investments.

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.

Assets measured at fair value on a recurring basis are summarized below under a three-level hierarchy established by the accounting rules which define the levels within the hierarchy as follows:

- Level 1 – Consists of fair value measurements whose value is based on quoted prices in active markets for identical assets or liabilities.
- Level 2 – Consists of fair value measurements whose value is based on significant other observable inputs.
- Level 3 – Consists of fair value measurements whose value is based on significant unobservable inputs.

The fair values of the pension plan assets at December 31, 2010 by asset category are as follows:

(Millions of Dollars)	Level 1	Level 2	Level 3	Total
U.S. Equity (a)	\$3,935	\$-	\$-	\$3,935
International Equity (b)	1,249	234	-	1,483
U.S. Government Issues (c)	-	1,300	-	1,300
Corporate Bonds (d)	-	571	129	700
Structured Assets (e)	-	-	87	87
Other Fixed Income (f)	-	31	66	97
Real Estate (g)	-	-	398	398
Cash and Cash Equivalents (h)	3	232	-	235

Notes to the Financial Statements - Continued

Total investments	\$5,187	\$2,368	\$680	\$8,235
Funds for retiree health benefits (i)	(226)	(103)	(30)	(359)
Investments (excluding funds for retiree health benefits)	\$4,961	\$2,265	\$650	\$7,876
Pending activities (j)				(155)
Total fair value of plan net assets				\$7,721

- (a) U.S. Equity includes both actively- and passively-managed assets with investments in domestic equity index funds, actively-managed small-capitalization equities, rights and warrants.
- (b) International Equity includes international equity index funds, actively-managed international equities, rights and warrants.
- (c) U.S. Government Issues include agency and treasury securities.
- (d) Corporate Bonds held in institutional mutual funds which are measured at Net Asset Value (NAV) are classified as Level 3.
- (e) Structured Assets are measured using broker quotes and investment manager proprietary models and include commercial-mortgage-backed securities, collateralized mortgage obligations and asset-backed securities.
- (f) Other Fixed Income includes emerging market debt valued using broker quotes, municipal bonds, sovereign debt, regional governments and government agencies.
- (g) Real Estate investments include real estate funds based on appraised values that are broadly diversified by geography and property type.
- (h) Cash and Cash Equivalents include short term investments, money markets and foreign currency.
- (i) The Companies set 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 Companies' other postretirement benefit obligation. See Note F.
- (j) 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 table below provides a reconciliation of the beginning and ending net balances for assets at December 31, 2010 classified as Level 3 in the fair value hierarchy.

(Millions of Dollars)	Beginning Balance as of January 1, 2010	Assets Still Held at Reporting Date – Unrealized Gains (Losses)	Assets Sold During the Period – Realized Gains	Purchases Sales and Settlements	Ending Balance as of December 31, 2010
International Equity	\$1	1	(1)	(1)	\$-
Corporate Bonds	143	(3)	9	(20)	129
Structured Assets	91	15	(6)	(13)	87
Other Fixed Income	46	-	2	18	66
Swaps	(3)	2	(1)	2	-
Real Estate	344	47	-	7	398
Total investments	\$622	62	3	(7)	\$680
Funds for retiree health benefits	(28)	(3)	(2)	3	(30)
Investments (excluding funds for retiree health benefits)	\$594	\$59	\$1	\$(4)	\$650

The fair values of the pension plan assets at December 31, 2009 by asset category are as follows:

(Millions of Dollars)	Level 1	Level 2	Level 3	Total
U.S. Equity (a)	\$3,470	\$-	\$-	\$3,470
International Equity (b)	1,140	196	1	1,337
U.S. Government Issues (c)	-	1,255	-	1,255
Corporate Bonds (d)	-	435	143	578
Structured Assets (e)	-	-	91	91
Other Fixed Income (f)	-	10	46	56
Swaps (g)	-	-	(3)	(3)
Real Estate (h)	-	-	344	344
Cash and Cash Equivalents (i)	197	141	-	338
Total investments	\$4,807	\$2,037	\$622	\$7,466
Funds for retiree health benefits (j)	(215)	(91)	(28)	(334)
Investments (excluding funds for retiree health benefits)	\$4,592	\$1,946	\$594	\$7,132
Pending activities (k)				(255)
Total fair value of plan net assets				\$6,877

Notes to the Financial Statements - Continued

- (a) U.S. Equity includes both actively- and passively-managed assets with investments in domestic equity index funds, actively-managed small-capitalization equities, rights and warrants.
- (b) International Equity includes international equity index funds, actively-managed international equities, rights and warrants.
- (c) U.S. Government Issues include agency and treasury securities.
- (d) Corporate Bonds held in institutional mutual funds which are measured at Net Asset Value (NAV) are classified as Level 3.
- (e) Structured Assets are measured using broker quotes and investment manager proprietary models and include commercial-mortgage-backed securities, collateralized mortgage obligations and asset-backed securities.
- (f) Other Fixed Income includes emerging market debt valued using broker quotes, municipal bonds, sovereign debt, regional governments and government agencies.
- (g) Swaps include total return swaps, interest rate swaps, credit default swaps and swap collateral. Level 3 Swaps are valued using proprietary investment manager models.
- (h) Real Estate investments include real estate funds based on appraised values that are broadly diversified by geography and property type.
- (i) Cash and Cash Equivalents include short term investments, money markets and foreign currency.
- (j) The Companies set 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 and their beneficiaries. 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 other postretirement benefit obligation. See Note F.
- (k) Pending activities include security purchases and sales that have not settled and interest and dividends that have not been received.

The table below provides a reconciliation of the beginning and ending net balances for assets at December 31, 2009 classified as Level 3 in the fair value hierarchy.

(Millions of Dollars)	Beginning Balance as of January 1, 2009	Assets Still Held at Reporting Date – Unrealized Gains (Losses)	Assets Sold During the Period – Realized Gains	Purchases Sales and Settlements	Ending Balance as of December 31, 2009
U.S. Equity	\$1	\$2	\$(2)	\$(1)	\$-
International Equity	-	-	-	1	1
Corporate Bonds	172	35	(7)	(57)	143
Structured Assets	194	93	(70)	(126)	91
Other Fixed Income	52	2	1	(9)	46
Swaps	(32)	13	(51)	67	(3)
Options	5	(4)	4	(5)	-
Real Estate	515	(177)	-	6	344
Total investments	\$907	\$(36)	\$(125)	\$(124)	\$622
Funds for retiree health benefits	(41)	2	6	5	(28)
Investments (excluding funds for retiree health benefits)	\$866	\$(34)	\$(119)	\$(119)	\$594

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

(Millions of Dollars)	For the Years Ended December 31		
	2010	2009	2008
O&R	\$2	\$2	\$2

Note F – Other Postretirement Benefits

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

Notes to the Financial Statements - Continued

Net Periodic Benefit Cost

The components of the Company's net periodic postretirement benefit costs for 2010, 2009, and 2008 were as follows:

(Millions of Dollars)	2010	2009	2008
Service cost	\$4	\$4	\$4
Interest cost on accumulated other postretirement benefit obligation	11	11	11
Expected return on plan assets	(8)	(8)	(7)
Amortization of net actuarial loss	7	9	8
Amortization of prior service costs	2	2	2
NET PERIODIC POSTRETIREMENT BENEFIT COST	\$16	\$18	\$18
Cost capitalized	(6)	(6)	(5)
Cost charged/(deferred)	3	2	(2)
Cost charged to operating expenses	\$13	\$14	\$11

Funded Status

The funded status of the programs at December 31, 2010, 2009, and 2008 were as follows:

(Millions of Dollars)	2010	2009	2008
CHANGE IN BENEFIT OBLIGATION			
Benefit obligation at beginning of year	\$201	\$206	\$196
Service cost	4	4	4
Interest cost on accumulated postretirement benefit obligation	11	11	11
Net actuarial loss/(gain)	9	(11)	3
Benefits paid and administrative expenses	(12)	(11)	(10)
Participant contributions	1	1	1
Medicare prescription subsidy	1	1	1
Plan amendments	-	-	-
BENEFIT OBLIGATION AT END OF YEAR	\$215	\$201	\$206
CHANGE IN PLAN ASSETS			
Fair value of plan assets at beginning of year	\$88	\$68	\$80
Actual return on plan assets	12	15	(17)
Employer contributions	11	14	13
Benefits paid	(9)	(9)	(8)
FAIR VALUE OF PLAN ASSETS AT END OF YEAR	\$102	\$88	\$68
FUNDED STATUS	\$(113)	\$(113)	\$(138)
Unrecognized net loss	43	45	71
Unrecognized prior service costs	16	17	19

The increase in the value of other postretirement benefit plan assets, offset by the increase in the OPEB benefit obligation resulted in no change to the liability for other postretirement benefits at O&R compared with December 31, 2009. This also resulted in a decrease to regulatory assets of \$1 million for unrecognized net losses and unrecognized prior service costs associated with O&R consistent with accounting rules for regulated operations, and a credit to OCI of \$1 million (net of taxes) for the unrecognized net losses and unrecognized prior service costs associated with RECO and Pike.

The estimated net loss and prior service costs for the other postretirement benefits that will be amortized from accumulated OCI and the regulatory asset into net periodic benefit cost over the next year for O&R are \$9 million and \$1 million, respectively.

Assumptions

The actuarial assumptions were as follows:

	2010	2009	2008
Weighted-average assumptions used to determine benefit obligations at December 31:			
Discount Rate	5.40%	5.95%	5.75%

Notes to the Financial Statements - Continued

Weighted-average assumptions used to determine net periodic benefit cost for the years ended December 31:			
Discount Rate	5.95%	5.75%	6.00%
Expected Return on Plan Assets			
Tax-Exempt	8.50%	8.50%	8.50%
Taxable	8.00%	8.00%	8.00%

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 year ended December 31, 2010 was 6.5 percent, which is assumed to decrease gradually to 4.5 percent by 2014 and remain at that level thereafter. The health care cost trend rate used to determine benefit obligations as of December 31, 2010 was 6.0 percent, which is assumed to decrease gradually to 4.5 percent by 2014 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, 2010:

(Millions of Dollars)	1-Percentage-Point	
	Increase	Decrease
Effect on accumulated other postretirement benefit obligation	\$24	\$(20)
Effect on service cost and interest cost components for 2010	2	(2)

Expected Benefit Payments

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

(Millions of Dollars)	2011	2012	2013	2014	2015	2016-2020
Gross Benefit Payments	\$12	\$13	\$13	\$13	\$14	\$80
Medicare Prescription Benefit Receipts	\$1	\$1	\$1	\$1	\$2	\$9

Expected Contributions

Based on estimates as of December 31, 2010, O&R expects to make a contribution of \$12 million to the other postretirement benefit plans in 2011.

Plan Assets

The asset allocations for O&R's other postretirement benefit plans at the end of 2010, 2009, and 2008, and the target allocation for 2011 are as follows:

ASSET CATEGORY	Target Allocation Range	Plan Assets at December 31		
	2011	2010	2009	2008
Equity Securities	57%-73%	67%	66%	56%
Debt Securities	26%-44%	33%	34%	44%
Total	100%	100%	100%	100%

O&R 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 the investment policy for its benefit plans.

Notes to the Financial Statements - Continued

The fair values of the plan assets at December 31, 2010 by asset category (see description of levels in Note E) are as follows:

(Millions of Dollars)	Level 1	Level 2	Level 3	Total
U.S. Equity (a)	\$118	\$172	\$-	\$290
International Equity (b)	-	107	-	107
Other Fixed Income (c)	-	-	189	189
Cash and Cash Equivalents (d)	-	11	-	11
Total investments	\$118	\$290	\$189	\$597
Funds for retiree health benefits (e)	226	103	30	359
Investments (including funds for retiree health benefits)	\$344	\$393	\$219	\$956
Pending activities (f)				(14)
Total fair value of plan net assets				\$942

- (a) U.S. Equity includes both actively- and passively-managed assets with investments in domestic equity index funds and commingled funds.
- (b) International Equity includes commingled international equity funds.
- (c) Other Fixed Income includes commingled funds, which are valued at Net Asset Value (NAV).
- (d) Cash and Cash Equivalents include short term investments and money markets.
- (e) The Companies set 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 Companies' other postretirement benefit obligation. See Note E.
- (f) 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 table below provides a reconciliation of the beginning and ending net balances for assets at December 31, 2010 classified as Level 3 in the fair value hierarchy.

(Millions of Dollars)	Beginning Balance as of January 1, 2010	Assets Still Held at Reporting Date – Unrealized Gains (Losses)	Assets Sold During the Period – Realized Gains	Purchases Sales and Settlements	Ending Balance as of December 31, 2010
Other Fixed Income	\$173	\$11	\$1	\$4	\$189
Insurance Contracts	8	-	(1)	(7)	-
Total investments	\$181	\$11	\$-	\$(3)	\$189
Funds for retiree health benefits	28	3	2	(3)	30
Investments (including funds for retiree health benefits)	\$209	\$14	\$2	\$(6)	\$219

The fair values of the plan assets at December 31, 2009 by asset category (see description of levels in Note E) are as follows:

(Millions of Dollars)	Level 1	Level 2	Level 3	Total
U.S. Equity (a)	\$101	\$143	\$-	\$244
International Equity (b)	-	92	-	92
Other Fixed Income (c)	-	-	173	173
Insurance Contracts (d)	-	-	8	8
Cash and Cash Equivalents (e)	-	9	-	9
Total investments	\$101	\$244	\$181	\$526
Funds for retiree health benefits (f)	215	91	28	334
Investments (including funds for retiree health benefits)	\$316	\$335	\$209	\$860
Pending activities (g)				6
Total fair value of plan net assets				\$866

- (a) U.S. Equity includes both actively-and passively-managed assets with investments in domestic equity index funds and commingled funds.
- (b) International Equity includes commingled international equity funds.
- (c) Other Fixed Income includes commingled funds, which are valued at Net Asset Value (NAV).
- (d) Insurance Contracts represent the cash surrender value of life insurance policies. The contracts are measured at NAV, adjusted for fees charged by the insurance company.
- (e) Cash and Cash Equivalents include short term investments and money markets.

Notes to the Financial Statements - Continued

- (f) The Companies set 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 and their beneficiaries. 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 other postretirement benefit obligation. See Note E.
- (g) Pending activities include security purchases and sales that have not settled and interest and dividends that have not been received.

The table below provides a reconciliation of the beginning and ending net balances for assets at December 31, 2009 classified as Level 3 in the fair value hierarchy.

(Millions of Dollars)	Beginning Balance as of January 1, 2009	Assets Still Held at Reporting Date – Unrealized Gains (Losses)	Assets Sold During the Period – Realized Gains	Purchases Sales and Settlements	Ending Balance as of December 31, 2009
Other Fixed Income	\$197	\$11	\$3	\$(38)	\$173
Insurance Contracts	8	-	-	-	8
Total investments	\$205	\$11	\$3	\$(38)	\$181
Funds for retiree health benefits	41	(2)	(6)	(5)	28
Investments (including funds for retiree health benefits)	\$246	\$9	\$(3)	\$(43)	\$209

Effect of Medicare Prescription Benefit

The Medicare Prescription Drug, Improvement and Modernization Act of 2003 created a benefit for certain employers who provide postretirement drug programs. The accounting rules for retirement benefits provide accounting and disclosure requirements relating to the Act. The Company's actuaries have determined that the Company's prescription drug plan provides a benefit that is at least actuarially equivalent to the Medicare prescription drug plan and projections indicate that this will be the case for 20 years; therefore, the Company has determined that it is eligible to receive the benefit that the Act makes available. When the plans' benefits are no longer actuarially equivalent to the Medicare plan, 25 percent of the retirees in each plan are assumed to begin to decline participation in the Company's prescription programs.

In March 2010, the Patient Protection and Affordable Care Act and the Health Care and Education Reconciliation Act of 2010 became law. In the first half of 2010, O&R reduced their deferred tax asset to reflect the laws' repeal, effective 2013, of the deduction for federal income tax purposes of the portion of the cost of an employer's retiree prescription drug coverage for which the employer received a benefit under the Medicare Prescription Drug Improvement and Modernization Act of 2003. For O&R's New York electric and gas services the reductions in their deferred tax assets of \$3 million had no effect on net income because a regulatory asset in a like amount on a pre-tax basis was established to reflect future recovery from customers of the increased cost of their retiree prescription drug coverage resulting from the loss of the tax deduction. For RECO and Pike, the reduction in their deferred tax assets of \$1 million was taken as a charge to net income.

Notes to the Financial Statements - Continued

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 seven 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 undiscounted cost to investigate the sites and, for sites that have been investigated in whole or in part, the cost to 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, 2010 and December 31, 2009 were as follows:

(Millions of Dollars)	2010	2009
Accrued Liabilities:		
Manufactured gas plant sites	\$119	\$52
Other Superfund Sites	1	1
Total	\$120	\$53
Regulatory assets	\$122	\$59

Most of the accrued Superfund Site liability relates to sites that have been investigated, in whole or in part. However, for some of the sites, the extent and associated cost of the required remediation has not yet been determined. As investigations progress and 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. Under its current rate plans for provision of electric and gas service in New York, O&R is permitted to recover or defer as regulatory assets (for subsequent recovery through rates) certain site investigation and remediation costs. In February 2011, the NYSPSC initiated a proceeding to examine the existing mechanisms pursuant to which the Company recovers such costs and possible alternatives.

Notes to the Financial Statements - Continued

There were no insurance recoveries received related to Superfund Sites for the year ended December 31, 2010 and 2009. Environmental remediation costs incurred related to Superfund Sites at December 31, 2010 and 2009 were as follows:

(Millions of Dollars)	2010	2009
Remediation costs incurred	\$3.0	\$2.4

In 2010, 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 such contaminants could range up to \$200 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.

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, but the Company believes that these amounts are greatly exaggerated, based on the disposition of previous claims.

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) at December 31, 2010 and 2009 were as follows:

(Millions of Dollars)	2010	2009
Accrued liability – asbestos suits	\$0.3	\$0.4
Regulatory assets – asbestos suits	0.3	0.4
Accrued liability – workers' compensation	\$5.0	\$5.9
Regulatory assets – workers' compensation	0.4	0.6

Note H – Leases

O&R's leases include rights of way for electric and gas distribution facilities, office buildings and automobiles. In accordance with accounting rules for leases, these leases are classified as operating leases. Generally, it is expected that leases will be renewed or replaced in the normal course of business.

For ratemaking purposes, capital leases are treated as operating leases; therefore, in accordance with accounting rules for regulated operations, the amortization of the leased asset is based on the rental payments recovered from customers.

Notes to the Financial Statements - Continued

The future minimum lease commitments under the Company's non-cancelable operating lease agreements are as follows:

(Millions of Dollars)	
2011	\$0.6
2012	0.5
2013	0.5
2014	0.5
2015	0.5
All years thereafter	3.6
Total	\$6.2

Note I – Income Tax

The components of income tax for the Company are as follows:

(Millions of Dollars)	2010	2009	2008
State			
Current	\$8	\$(3)	\$2
Deferred – net	(1)	9	4
Federal			
Current	(1)	(16)	5
Deferred – net	20	32	13
TOTAL CHARGE TO OPERATIONS	26	22	24
TOTAL CHARGE/(BENEFIT) TO OTHER INCOME	-	1	1
TOTAL	\$26	\$23	\$25

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

(Millions of Dollars)	2010	2009
Deferred tax liabilities:		
Depreciation	\$168	\$143
Regulatory assets – future income tax	94	85
Unrecognized pension and other postretirement costs	89	87
State income tax	32	27
Capitalized overheads	64	58
Other	(1)	11
Total deferred tax liabilities	446	411
Deferred tax assets:		
Unrecognized pension and other postretirement costs	89	87
Regulatory liabilities – future income tax	16	17
Other	36	41
Total deferred tax assets	141	145
NET LIABILITIES	305	266
INVESTMENT TAX CREDITS	3	3
DEFERRED INCOME TAXES AND INVESTMENT TAX CREDITS	308	269
DEFERRED INCOME TAXES – RECOVERABLE ENERGY COSTS	5	12
TOTAL DEFERRED INCOME TAXES AND INVESTMENT TAX CREDITS	\$313	\$281

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:

(% of Pre-tax income)	2010	2009	2008
STATUTORY TAX RATE			
Federal	35%	35%	35%
Changes in computed taxes resulting from:			
State income tax	6	6	6
Depreciation related differences	(1)	(1)	(1)
Cost of removal	(2)	(3)	(2)
AFUDC	(2)	(1)	(1)
Medicare Reimbursement	(2)	(1)	(2)
Other	1	(1)	1
Effective Tax Rate	35%	34%	36%

Notes to the Financial Statements - Continued

For federal income tax purposes in 2010, Con Edison has estimated 2010 federal income tax payments of \$16 million which were classified as a prepayment on the Con Edison consolidated balance sheet.

For New York State income tax purposes in 2010, Con Edison has a net operating loss carryforward available from the 2009 tax return filing of \$37 million, primarily as a result of repair allowance deductions. A deferred tax asset has been recognized for this New York State net operating loss that will not expire until year end 2029. A valuation allowance has not been provided against the deferred tax asset, as it is more likely than not that the deferred tax asset will be realized.

Uncertain Tax Positions

Under the accounting rules for income taxes, an enterprise is not allowed to recognize, in its financial statements, the benefit of a tax position unless that 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.

O&R files a consolidated tax return with Con Edison and its other subsidiaries. See "Federal Income Tax" and "State Income Tax" in Note A. The IRS has essentially completed its field audits of Con Edison's consolidated federal income tax returns through 2009. Con Edison's consolidated federal income tax returns for 1998 through 2009, which remain open to examination by the IRS, reflect certain tax positions with which the IRS does not or may not agree. Any adjustments to federal income tax returns will result in Con Edison filing the federal audit changes with New York State to incorporate in the applicable state income tax returns. In addition, Con Edison's consolidated New York State tax returns for years beginning with 2006 remain open to examination by New York State.

In September 2010, Con Edison filed its consolidated federal income tax return for 2009 reflecting, among other things, the deduction of the costs of certain repairs to utility plant as an operating expense (the "repair allowance deductions"). Previously, such costs were capitalized and reported as depreciation in Con Edison's consolidated tax returns. Taking the repair allowance deductions accelerated the timing of the deduction of the cost of the repairs. O&R had a net operating loss for federal income tax purposes in 2009 reflecting, among other things, the repair allowance deductions and the bonus depreciation provisions of the American Recovery and Reinvestment Act of 2009. In November 2010, O&R received a \$14 million refund of certain prior years' federal tax payments based upon the carry-back of the 2009 net operating loss. O&R also estimates that it had a net operating loss for state income tax purposes for 2009, which is being carried forward and as to which, at December 31, 2010, O&R has included a \$3 million other current asset in its consolidated balance sheet. At December 31, 2010, with respect to the repair allowance deductions, O&R accrued a liability for uncertain tax positions of \$2 million.

Notes to the Financial Statements - Continued

The methods used in Con Edison's consolidated tax returns to determine which construction-related costs incurred from 2002 through 2008 could be deducted resulted in an uncertain tax position. In July 2008, the IRS entered into a closing agreement with Con Edison covering the extent to which such costs could be deducted in 2002 through 2004. In August 2010, the IRS entered into a closing agreement with Con Edison, covering the extent to which such costs could be deducted in 2005 through 2008. In 2010 Con Edison instructed the IRS to use the \$160 million deposit that it paid to the IRS in June 2007 (of which, \$13 million was attributable to O&R) to pay the taxes due pursuant to the closing agreements. At December 31, 2010, O&R had no unrecognized tax benefits relating to the deduction of construction-related costs for New York State income tax purposes in 2005 through 2008.

At December 31, 2010, O&R's estimated liabilities for uncertain tax positions (\$8 million) were classified as current liabilities on its consolidated balance sheets. O&R reasonably expects to resolve these uncertain tax positions with the IRS in the next 12 months.

O&R recognizes interest accrued related to the liability for uncertain tax positions in interest expense and would recognize penalties, if any, in operating expenses in its consolidated income statements. In 2010 and 2009, O&R recognized an immaterial amount of interest expense for uncertain tax positions.

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

(Millions of Dollars)	2010	2009	2008
Balance at the beginning of the year	\$(11)	\$9	\$12
Additions based on tax positions of prior years	18	-	-
Reductions for tax positions of prior years	-	(14)	(1)
Settlements	1	(6)	(2)
Balance at the end of the year	\$8	\$(11)	\$9

Note J – Stock-Based Compensation

O&R provides stock-based compensation to its employees under Con Edison's stock-based compensation plans. These plans include stock options, restricted stock units and contributions to a discount stock purchase plan. The Stock Option Plan (the 1996 Plan) provided for awards of stock options to officers and employees of Con Edison and its subsidiaries for up to 10 million shares of common stock. The Long Term Incentive Plan (LTIP) among other things, provides for awards of restricted stock units, stock options and, to Con Edison's non-officer directors, deferred stock units for up to 10 million shares of common stock (of which not more than four million shares may be restricted stock or stock units).

Shares of Con Edison common stock used to satisfy the obligations with respect to O&R's stock-based compensation may be new (authorized, but unissued) shares, treasury shares or shares purchased in the open market. The shares used during the period ended December 31, 2010 and 2009 have been new shares.

Notes to the Financial Statements - Continued

Under the accounting rules for stock compensation, the Company has recognized the cost of stock-based compensation as an expense using a fair value measurement method. The following table summarizes stock-based compensation expense recognized by the Company in the period ended December 31, 2010, 2009, and 2008:

(Millions of Dollars)	2010	2009	2008
Stock options	\$-	\$-	\$-
Restricted stock units	0.1	0.1	0.1
Performance-based restricted stock	1.7	1.1	0.8
Total	\$1.8	\$1.2	\$0.9

Stock Options

Stock options were last granted in 2006. The stock options generally vested over a three-year period and have a term of ten years. Options were granted at an exercise price equal to the fair market value of a Con Edison common share when the option was granted. The Company generally recognizes compensation expense (based on the fair value of stock option awards) over the continuous service period in which the options vest. Awards to employees currently eligible for retirement are expensed in the month awarded.

The outstanding options are "equity awards" because shares of Con Edison common stock are delivered upon exercise of the options. As equity awards, the fair value of the options is measured at the grant date. There were no options granted and forfeited in 2010 and 2009.

A summary of changes in the status of stock options awarded to O&R employees as of December 31, 2010 is as follows:

	Shares	Weighted Average Exercise Price
Outstanding at 12/31/09	496,000	\$42.914
Exercised	189,000	41.815
Outstanding at 12/31/10	307,000	\$43.591

The change in the fair value of all outstanding options from their grant dates to December 31, 2010 and 2009 (aggregate intrinsic value) for O&R was \$2 million and \$1 million, respectively. The aggregate intrinsic value of options exercised in 2010 and 2009 were \$1 million and \$0.2 million, respectively, and the cash received by Con Edison for payment of the exercise price was \$8 million and \$1 million, respectively. The weighted average remaining contractual life of options outstanding is four years as of December 31, 2010.

The following table summarizes O&R employees' stock options outstanding at December 31, 2010 for each plan year:

Plan Year	Remaining Contractual Life	Options Outstanding	Weighted Average Exercise Price	Options Exercisable
2006	5	103,000	\$45.863	103,000
2005	4	75,500	43.241	75,500
2004	3	71,500	43.695	71,500
2003	2	21,500	38.470	21,500
2002	1	21,500	42.510	21,500
2001	1	14,000	37.750	14,000
Total		307,000	\$43.591	307,000

Notes to the Financial Statements - Continued

Restricted Stock Units

Restricted stock unit awards under the LTIP have been made to O&R officers and certain employees, including awards that provide for adjustment of the number of units (performance-restricted stock units or Performance RSUs). 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.

In accordance with accounting rules for stock compensation, for outstanding restricted stock awards other than Performance RSUs, the Company has accrued a liability based on the market value of a common share on the grant date and are recognizing compensation expense over the vesting period. The weighted average vesting period for outstanding awards is one year and is based on the employees' 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. At December 31, 2010 and 2009, there were 38,400 and 38,450 units outstanding for O&R. The weighted average fair value as of the grant date of the outstanding units for December 31, 2010 and 2009 was \$35.368 and \$35.577 per unit, respectively, for O&R. The total expense to be recognized by the Company in future periods for unvested awards outstanding as of December 31, 2010 was \$73 thousand.

The number of units in each annual Performance RSU 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 150 percent based on Con Edison's total shareholder return relative to a peer group of utilities for a specified performance period (the TSR portion); and (ii) 50 percent of the units awarded will be multiplied by a factor that may range from 0 to 132 percent based on determinations made in connection with the O&R Annual Team Incentive Plan (the EIP portion). Units generally vest when the performance period ends.

For the TSR portion of Performance RSU, the Company uses a Monte Carlo simulation model to estimate the fair value of the awards. The fair value is recomputed each reporting period as of the earlier of the reporting date and the vesting date. For the EIP portion of Performance RSU, the fair value of the awards is determined using the market price as of the earlier of the reporting date or the vesting date multiplied by the average EIP determination over the vesting period. Performance RSU awards 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 following table illustrates the assumptions used to calculate the fair value of the awards:

	2010
Risk-free interest rate	0.30% -5.62 %
Expected term	3 years
Expected volatility	21.85%

Notes to the Financial Statements - Continued

The risk-free rate is based on the U.S. Treasury zero-coupon yield curve on the date of grant. The expected term of the Performance RSUs is three years, which equals the vesting period. The Company does not expect significant forfeitures to occur. The expected volatility is calculated using daily closing stock prices over a period of three years, which approximates the expected term of the awards.

A summary of changes in the status of the Performance RSUs TSR portion during the period ended December 31, 2010 is as follows:

	Units	Weighted Average Fair Value*
Non-vested at 12/31/09	19,325	\$55.364
Granted	17,085	41.340
Vested	(7,766)	72.297
Forfeited	(384)	-
Non-vested at 12/31/10	28,260	\$58.262

* Fair value is determined using the Monte Carlo simulation described above. Weighted average fair value at December 31, 2010 and weighted average fair value of Performance RSUs granted do not reflect any accrual or payment of dividends prior to vesting.

A summary of changes in the status of the Performance RSUs' EIP portion during the period ended December 31, 2010 is as follows:

	Units	Weighted Average Price*
Non-vested at 12/31/09	19,325	\$45.430
Granted	17,085	44.540
Vested	(7,766)	54.202
Forfeited	(384)	-
Non-vested at 12/31/10	28,260	\$55.103

* Fair value is determined using the market price of one share of Con Edison common stock on the respective dates indicated or the grant or vesting dates multiplied by the average Executive Incentive Plan determination over the vesting period. The market price has not been discounted to reflect that dividends do not accrue and are not payable on Performance RSUs until vesting.

The total expense to be recognized by O&R in future periods for unvested Performance RSUs outstanding as of December 31, 2010 is \$1.8 million.

Stock Purchase Plan

Under the Con Edison Stock Purchase Plan, O&R contributes up to \$1 for each \$9 invested by its employees to purchase Con Edison common stock. Eligible participants may invest up to \$25,000 during any calendar year (subject to an additional limitation for employees of not more than 20% 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 2010, 2009 and 2008, 738,951, 868,622 and 745,869 shares were purchased under the Stock Purchase Plan at a weighted average price of \$45.52, \$38.15 and \$42.47 per share, respectively.

Notes to the Financial Statements - Continued

Note K – Financial Information by Business Segment

The business segments of the Company were determined based on management's reporting and decision-making requirements in accordance with the accounting rules for segment reporting.

The Company's principal business segments are its regulated electric and gas utility activities.

All revenues of these business segments are from customers located in the United States of America. Also, all assets of the business segments are located in the United States of America. The accounting policies of the segments are the same as those described in Note A.

Common services shared by the business segments are assigned directly or allocated based on various cost factors, depending on the nature of the service provided.

The financial data for the business segments are as follows:

As of and for the Year Ended December 31, 2010 (Millions of Dollars)	Operating revenues	Depreciation and amortization	Operating income	Interest charges	Income tax expense	Total assets*	Construction expenditures
Electric	\$692	\$32	\$74	\$22	\$18	\$1,621	\$99
Gas	218	12	34	12	8	684	36
Other*	-	-	-	1	-	32	-
Total	\$910	\$44	\$108	\$35	\$26	\$2,337	\$135

As of and for the Year Ended December 31, 2009 (Millions of Dollars)	Operating revenues	Depreciation and amortization	Operating income	Interest charges	Income tax expense	Total assets*	Construction expenditures
Electric	\$648	\$30	\$64	\$18	\$15	\$1,525	\$85
Gas	242	12	28	9	7	627	42
Other*	-	-	-	2	-	35	-
Total	\$890	\$42	\$92	\$29	\$22	\$2,187	\$127

As of and for the Year Ended December 31, 2008 (Millions of Dollars)	Operating revenues	Depreciation and amortization	Operating income	Interest charges	Income tax expense	Total assets*	Construction expenditures
Electric	\$733	\$29	\$68	\$18	\$18	\$1,514	\$88
Gas	258	11	25	9	6	590	32
Other*	-	-	-	1	-	58	-
Total	\$991	\$40	\$93	\$28	\$24	\$2,162	\$120

* Includes amounts related to Transition Funding.

Note L – Derivative Instruments and Hedging Activities

Under the accounting rules for derivatives and hedging, derivatives are recognized on the balance sheet at fair value, unless an exception is available under the accounting rules. Certain qualifying derivative contracts have been designated as normal purchases or normal sales contracts. These contracts are not reported at fair value under the accounting rules.

Notes to the Financial Statements - Continued

Energy Price Hedging

The Company hedges market price fluctuations associated with physical purchases of electricity by using electric and gas derivative instruments including futures, forwards, and options. The fair values of these hedges at December 31, 2010 and 2009 were as follows:

(Millions of Dollars)	2010	2009
Fair value of net derivative assets/ (liabilities) – gross	\$(48)	\$ (52)
Impact of netting of cash collateral	15	-
Fair value of net derivative assets/ (liabilities) – net	\$(33) ^(a)	\$ (52) ^(a)

(a) Includes derivative liabilities of \$3 million and \$9 million with Con Edison's competitive energy businesses at December 31, 2010 and 2009, respectively. See Note N.

O&R and CECONY (together, 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 in accordance with provisions approved by the NYSPSC. See Note N.

Credit Exposure

The Company is exposed to credit risk related to transactions entered into primarily for the various electric supply and hedging activities. 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 had \$3 million of credit exposure in connection with electricity supply and hedging activities, net of collateral, at December 31, 2010. The Company's net credit exposure consisted of \$2 million with investment-grade counterparties and \$1 million with commodity exchange brokers.

Economic Hedges

The Company enters into certain derivative instruments that do not qualify or are not designated as hedges under the accounting rules for derivatives and hedging. However, management believes these instruments represent economic hedges that mitigate exposure to fluctuations in commodity prices.

The fair values of the Company's commodity derivatives at December 31, 2010 and 2009 were:

Fair Value of Commodity Derivatives ^(a)			
(Millions of Dollars)	Balance Sheet Location	2010	2009
Derivative Assets			
Current	Fair value of derivative assets	\$-	\$2
Current	Other current assets	1	-
Long term	Other deferred charges and non-current assets	3	2
Total derivative assets		\$4	\$4
Impact of netting		(1)	(1)
Net derivative assets		\$3	\$3
Derivative Liabilities			
Current	Fair value of derivative liabilities	\$37	\$36
Long term	Fair value of derivative liabilities	15	20
Total derivative liabilities		\$52	\$56

Notes to the Financial Statements - Continued

Impact of netting	(16)	(1)
Net derivative liabilities	\$36 ^(b)	\$55 ^(b)

- (a) Qualifying derivative contracts, which have been designated as normal purchases or normal sales contracts, are not reported at fair value under the accounting rules for derivative and hedging and, therefore, are excluded from the table.
- (b) Includes derivative liabilities of \$3 million and \$9 million with Con Edison's competitive energy businesses at December 31, 2010 and 2009, respectively. See Note N.

The Company 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 utility commissions. 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 commodity derivatives. As gains and losses are realized in future periods, they will be recognized as purchased power costs in the Company's consolidated income statement.

The following table presents the changes in the fair values of commodity derivatives that have been deferred for the year ended December 31, 2010 and 2009:

Realized and Unrealized Gains/(Losses) on Commodity Derivatives ^(a)			
(Millions of Dollars)	Balance Sheet Location	Deferred for the Year Ended December 31, 2010	Deferred for the Year Ended December 31, 2009
Pre-tax gains/(losses) deferred in accordance with the accounting rules for regulated operations:			
Current	Deferred derivative gains	\$1	\$-
Long term	Regulatory liabilities	1	-
Total deferred gains		\$2	\$-
Current	Deferred derivative losses	\$(2)	\$4
Current	Recoverable energy costs ^(b)	(78)	(124)
Long term	Regulatory assets	5	6
Total deferred losses		\$(75)	\$(114)
Net deferred losses		\$(73)	\$(114)

- (a) Qualifying derivative contracts, which have been designated as normal purchases or normal sales contracts, are not reported at fair value under the accounting rules for derivatives and hedging and, therefore, are excluded from the table.
- (b) Includes payments of \$32 million and \$37 million to Con Edison's competitive energy businesses for the years ended December 31, 2010 and 2009, respectively. See Note N.

As of December 31, 2010, the Company had 99 electric or gas derivative contracts hedging electric energy or capacity market prices, which were considered to be derivatives under the accounting rules for derivatives and hedging (excluding qualifying derivative contracts, which have been designated as normal purchases or normal sales contracts). The following table presents the number of contracts by commodity type:

Number of Energy Contracts ^{(a) (c)}	Electric Derivatives		Gas Derivatives		Total Number Of Contracts ^(a)	
	MWhs ^{(b) (c)}	Number of Capacity Contracts ^(a)	MWhs ^(b)	Number of Contracts ^(a)		Dths ^(b)
10	3,447,550	1	1,303	88	6,770,000	99

- (a) Qualifying derivative contracts, which have been designated as normal purchases or normal sales contracts, are not reported at fair value under the accounting rules for derivative and hedging and, therefore, are excluded from the table.
- (b) Volumes are reported net of long and short positions.
- (c) Includes one contract of 93,766 MWhs with Con Edison's competitive energy businesses. See Note N.

Notes to the Financial Statements - Continued

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 of the Company's derivative instrument contracts contain provisions that may require the Company to provide collateral on derivative instruments in net liability positions. The Utilities enter into separate derivative instruments for electric energy or capacity, and CECONY enters into derivative instruments in connection with the Utilities' joint gas supply arrangements (See Note N). The amount of collateral to be provided will depend on the fair value of the derivative instruments and the Utilities' credit ratings.

The aggregate fair value of all of the Company's derivative instruments with credit-risk-related contingent features that are in a net liability position, and collateral posted at December 31, 2010, 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 were:

(Millions of Dollars)	
Aggregate fair value – net liabilities ^(a)	\$48
Collateral posted ^(b)	24
Additional collateral ^(c) (downgrade one level from current rating ^(d))	5
Additional collateral ^(c) (downgrade to below investment grade from current rating ^(d))	27 ^(e)

- (a) Non-derivative transactions for the purchase and sale of electricity 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. 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) Across the Utilities' energy derivative positions, credit limits for the same counterparties are generally integrated. At December 31, 2010, the Utilities posted a combined collateral of \$102 million, including the collateral posted that is estimated to be attributable to O&R shown above.
- (c) 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 liability 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 Utilities have a legally enforceable right of setoff.
- (d) The current long-term ratings of O&R are Baa1/A-/A- by Moody's, S&P, and Fitch, respectively. Credit ratings assigned by rating agencies are expressions of opinions that are subject to revision or withdrawal at any time by the assigning rating agency.
- (e) Derivative instruments that are net assets have been excluded from the table. At December 31, 2010, if O&R had been downgraded to below investment grade, it would have been required to post additional collateral for such derivative instruments of not more than \$1 million.

Interest Rate Swaps

O&R has an interest rate swap pursuant to which it pays a fixed-rate of 6.09 percent and receives a LIBOR-based variable rate. The swap agreement is scheduled to terminate in October 2014. The fair value of this interest rate swap at December 31, 2010 was an unrealized loss of \$10 million, which has been included in the company's consolidated balance sheet as a noncurrent liability/fair value of derivative liabilities and a regulatory asset. The increase in the fair value of the swap for the year ended December 31, 2010 was \$1 million. In the event O&R's credit rating was downgraded to BBB- or lower by S&P or Baa3 or lower by Moody's, the swap counterparty could elect to terminate the agreement and, if it did so, the parties would then be required to settle the transaction.

Notes to the Financial Statements - Continued

Note M – Asset Retirement Obligations

In accordance with accounting rules for asset retirement obligations, companies are required to recognize a liability for legal obligations associated with the retirement of long-lived assets. Any such obligations identified by the Company were immaterial.

The Company includes in depreciation the estimated removal costs, less salvage, for utility plant assets. In accordance with accounting rules for asset retirement obligations, future removal costs that do not represent legal asset retirement obligations are recorded as regulatory liabilities pursuant to accounting rules for regulated operations. The related regulatory liabilities recorded for the Company were \$72 million and \$68 million at December 31, 2010 and 2009, respectively.

Note N – Related Party Transactions

The Company provides and receives administrative and other services to and from Con Edison and its subsidiaries pursuant to cost allocation procedures developed in accordance with rules approved by the NYSPSC and/or other regulatory authorities, as applicable. The services received include substantial administrative support operations, such as corporate secretarial and associated ministerial 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, 2010, 2009 and 2008 were as follows:

(Millions of Dollars)	2010	2009	2008
Cost of services provided	\$17	\$18	\$19
Cost of services received	\$40	\$41	\$31

In addition, CECONY and O&R have joint gas supply arrangements, in connection with which O&R purchased from CECONY \$99 million, \$124 million, and \$183 million of natural gas for the years ended December 31, 2010, 2009, and 2008, respectively. These amounts are net of the effect of related hedging transactions. At December 31, 2010 and 2009, O&R's net payable to CECONY associated with these gas purchases was \$11 million and \$16 million, respectively.

RECO purchased from Consolidated Edison Energy, Inc. \$32 million, \$37 million and \$24 million of electricity for the periods ended December 31, 2010, 2009 and 2008, respectively, pursuant to energy auctions.

At December 31, 2010 and 2009, the Company's receivable from Con Edison for income taxes was \$25 million and \$12 million, respectively. See Note A.

FERC has authorized CECONY through 2011 to lend funds to O&R from time to time, 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, 2009 and 2010, there were no loans outstanding for O&R.

Notes to the Financial Statements - Continued

Note O – 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 participant's 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 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, 2010, the Company determined that nonperformance risk would have no material impact on their financial position or results of operations. To assess nonperformance risk, the Company considered information such as collateral requirements, master netting arrangements, letters of credit and parent company guarantees, and applied a market-based method by using the counterparty (for an asset) or the Company's (for a liability) credit default swaps rates.

The accounting rules for fair value measurements and disclosures establish 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.
- 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.

Notes to the Financial Statements - Continued

- 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.

Effective January 1, 2010, the Company adopted Accounting Standards Update (ASU) No. 2010-06, "Fair Value Measurements and Disclosures (Topic 820): Improving Disclosures about Fair Value Measurements." This update requires the Company to disclose significant transfers in and out of Level 1 and Level 2 fair value measurements and describe the reasons for the transfers. The guidance also clarifies level of disaggregation and disclosure requirements about inputs and valuation techniques used to measure fair value for both recurring and nonrecurring fair value measurements and the meaning of a class of assets and liabilities. In addition, the update requires the Company to present information about purchases, sales, issuances, and settlements on a gross basis in the reconciliation for fair value measurements using significant unobservable inputs (Level 3).

The valuation technique used by the Company with regard to commodity derivatives and other assets that fall into either Level 2 or Level 3 is the market approach, which uses prices and other relevant information generated by market transactions involving identical or comparable assets and liabilities. The valuation technique used by the Company with regard to the interest rate contract that falls into Level 3 is the income approach which uses valuation techniques to convert future income stream amounts to a single amount in present value terms.

Assets and liabilities measured at fair value on a recurring basis as of December 31, 2010 are summarized below.

(Millions of Dollars)	Level 1	Level 2	Level 3	Netting Adjustments ⁽⁴⁾	Total
Derivative assets:					
Commodity ⁽¹⁾	-	2	2	(1)	3
Other assets ⁽³⁾	1	-	9	-	10
Total	\$1	\$2	\$11	\$(1)	\$13
Derivative liabilities:					
Commodity ⁽¹⁾	-	-	51 ⁽⁵⁾	(15)	36 ⁽⁴⁾
Interest rate contract ⁽²⁾	-	-	10	-	10
Total	\$-	\$-	\$61	\$(15)	\$46

(1) A significant portion of the commodity derivative contracts categorized in Level 3 is valued using either an industry acceptable model or an internally developed model with observable inputs. The models also include some less readily observable inputs resulting in the classification of the respective contract as Level 3. See Note L.

(2) See Note L.

(3) Other assets are comprised of assets such as life insurance contracts within the Supplemental Employee Retirement Plan, held in a rabbi trust.

(4) Amounts represent the impact of legally-enforceable master netting agreements that allow the Companies to net gain and loss positions and cash collateral held or placed with the same counterparties.

(5) Includes derivative liabilities of \$3 million with Con Edison's competitive energy businesses. See Note N.

Assets and liabilities measured at fair value on a recurring basis as of December 31, 2009 are summarized below.

Notes to the Financial Statements - Continued

(Millions of Dollars)	Level 1	Level 2	Level 3	Total
Derivative assets:				
Commodity ⁽¹⁾	\$ -	\$ 4	\$ -	\$ 4
Other assets ⁽³⁾	-	-	9	9
Total	\$ -	\$ 4	\$ 9	\$ 13
Derivative liabilities:				
Commodity ⁽¹⁾	\$ -	\$ 1	\$ 55 ⁽⁴⁾	\$ 56 ⁽⁴⁾
Interest rate contract ⁽²⁾	-	-	11	11
Total	\$ -	\$ 1	\$ 66	\$ 67

- (1) A significant portion of the commodity derivative contracts categorized in Level 3 is valued using either an industry acceptable model or an internally developed model with observable inputs. The models also include some less readily observable inputs resulting in the classification of the entire contract as Level 3. See Note L.
- (2) See Note L.
- (3) Other assets are comprised of assets such as life insurance contracts within the Supplemental Employee Retirement Plan, held in a rabbi trust.
- (4) Includes derivative liabilities of \$9 million with Con Edison's competitive energy businesses. See Note N.

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, 2010 and 2009 and classified as Level 3 in the fair value hierarchy:

(Millions of Dollars)	For the Year Ended December 31, 2010					Ending Balance as of December 31, 2010
	Beginning Balance as of January 1, 2010	Total Gains/(Losses) – Realized and Unrealized		Purchases, Issuances, Sales and Settlements	Transfer In/Out of Level 3	
		Included in Earnings	Included in Regulatory Assets and Liabilities			
Derivatives:						
Commodity	\$ (55)	\$(69)	\$6	\$69	\$-	\$(49)
Interest rate contract	(11)	(3)	1	3	-	(10)
Other assets ⁽¹⁾	9	-	-	-	-	9
Total	\$ (57)	\$(72)	\$7	\$72	\$-	(50)

- (1) Amounts included in earnings are reported in investment and other income on the consolidated income statement.

(Millions of Dollars)	For the Year Ended December 31, 2009					Ending Balance as of December 31, 2009
	Beginning Balance as of January 1, 2009	Total Gains/(Losses) – Realized and Unrealized		Purchases, Issuances, Sales and Settlements	Transfer In/Out of Level 3	
		Included in Earnings	Included in Regulatory Assets and Liabilities			
Derivatives:						
Commodity	\$ (53)	\$ (93)	\$ (2)	\$ 93	\$ -	\$ (55)
Interest rate contract	(15)	(3)	4	3	-	(11)
Other assets ⁽¹⁾	8	-	1	-	-	9
Total	\$(60)	\$(96)	\$ 3	\$ 96	\$ -	\$(57)

- (1) Amounts included in earnings are reported in investment and other income on the consolidated income statement.

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 commissions. See Note A. Unrealized gains and losses for

Notes to the Financial Statements - Continued

commodity derivatives are generally deferred on the consolidated balance sheet in accordance with the accounting rules for regulated operations.

Note P – New Financial Accounting Standards

In February 2010, the Financial Accounting Standards Board (FASB) issued new guidance for subsequent events through Accounting Standards Update (ASU) No. 2010-09, "Subsequent Events (Topic 855): Amendments to Certain Recognition and Disclosure Requirements." The amendments in this update eliminates requirements for SEC filers to disclose the date through which subsequent events have been evaluated. The application of this guidance did not have a material impact on the Company's financial position, results of operations or liquidity.

In December 2010, the FASB issued amendments to the guidance for intangibles through ASU No. 2010-28, "Intangibles – Goodwill and Other (Topic 360): When to Perform Step 2 of the Goodwill Impairment Test for Reporting Units with Zero or Negative Carrying Amounts." The amendments in this update to the Accounting Standard Codification modifies Step 1 of the goodwill impairment test to require those reporting units with zero or negative carrying value to be evaluated under Step 2 of the impairment test if circumstances or events indicate that it is more likely than not that a goodwill impairment exists. For public entities, this update is effective for the fiscal year and interim periods within those years, beginning after December 15, 2010. The application of this guidance is not expected to have a material impact on the Company's financial position, results of operations or liquidity.