Orange and Rockland Utilities, Inc.
2007 Annual Financial Statements and Notes

Financial Statements

Report of Independent Registered Public Accounting Firm

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

In our opinion, the accompanying consolidated balance sheet and statement of capitalization and the related consolidated statements 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, 2007 and 2006, and the results of their operations and their cash flows for each of the three years in the period ended December 31, 2007 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 the standards of the Public Company Accounting Oversight Board (United States). 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.

As discussed in Notes E and F to the consolidated financial statements, the Company changed its method of accounting for defined benefit pension and other postretirement benefit plans in 2006.

PricewaterhouseCoopers LLP

PricewaterhouseCoopers LLP
New York, New York
February 20, 2008

Orange and Rockland Utilities, Inc.
CONSOLIDATED BALANCE SHEET

	December 31, 2007	December 31, 2006
	(Millions of Dollars)	
ASSETS		
UTILITY PLANT, AT ORIGINAL COST (Note A)		
Electric	$ 952	$ 903
Gas	403	385
General	133	125
Total	1,488	1,413
Less: Accumulated depreciation	423	409
Net	1,065	1,004
Construction work in progress	55	39
NET UTILITY PLANT	1,120	1,043
CURRENT ASSETS		
Cash and temporary cash investments (Note A)	60	21
Restricted cash	1	2
Accounts receivable - customers, less allowance for uncollectible accounts of $2 in 2007 and 2006	54	48
Accrued unbilled revenue (Note A)	42	36
Other receivables, less allowance for uncollectible accounts of $2 and $1 in 2007 and 2006, respectively	26	43
Accounts receivable from affiliated companies	5	5
Gas in storage, at average cost	43	57
Materials and supplies, at average cost	8	7
Prepayments	11	10
Fair value of derivative assets	4	2
Deferred derivative losses	1	24
Recoverable energy costs (Notes A and B)	23	22
TOTAL CURRENT ASSETS	278	277
INVESTMENTS (Note A)	12	11
DEFERRED CHARGES, REGULATORY ASSETS AND NONCURRENT ASSETS		
Regulatory assets (Note B)	408	414
Other deferred charges and noncurrent assets	44	23
TOTAL DEFERRED CHARGES, REGULATORY ASSETS AND NONCURRENT ASSETS	452	437
TOTAL ASSETS	$ 1,862	$ 1,768

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

Orange and Rockland Utilities, Inc.
CONSOLIDATED BALANCE SHEET

	December 31, 2007	December 31, 2006
	(Millions of Dollars)	
CAPITALIZATION AND LIABILITIES		
CAPITALIZATION		
Common shareholder's equity (See Statement of Common Shareholder's Equity)	$ 416	$ 360
Long-term debt (See Statement of Capitalization)	433	436
TOTAL CAPITALIZATION	849	796
NONCURRENT LIABILITIES		
Provision for injuries and damages (Note G)	6	6
Pensions and retiree benefits	299	299
Superfund and other environmental costs (Note G)	56	49
Hedges on variable rate long-term debt (Note N)	10	12
Uncertain income taxes	12	-
TOTAL NONCURRENT LIABILITIES	383	366
CURRENT LIABILITIES		
Long-term debt due within one year	3	22
Notes payable	45	34
Accounts payable	95	77
Accounts payable to affiliated companies	94	68
Customer deposits	15	14
Accrued taxes	1	5
Accrued interest	12	10
Deferred derivative gains (Note B)	5	1
Deferred income taxes - recoverable energy costs (Note K)	9	9
Other current liabilities	20	30
TOTAL CURRENT LIABILITIES	299	270
DEFERRED CREDITS AND REGULATORY LIABILITIES		
Deferred income taxes and investment tax credits (Notes A and K)	207	199
Regulatory liabilities (Note B)	121	134
Other deferred credits	3	3
TOTAL DEFERRED CREDITS AND REGULATORY LIABILITIES	331	336
TOTAL CAPITALIZATION AND LIABILITIES	$ 1,862	$ 1,768

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

Orange and Rockland Utilities, Inc.
CONSOLIDATED INCOME STATEMENT

	For the Years Ended December 31, 2007	2006	2005
	(Millions of Dollars)		
OPERATING REVENUES (Note A)			
Electric	$ 671	$ 582	$ 596
Gas	265	236	228
TOTAL OPERATING REVENUES	936	818	824
OPERATING EXPENSES			
Purchased power	384	307	319
Gas purchased for resale	166	150	143
Other operations and maintenance	203	185	177
Depreciation and amortization (Note A)	38	35	34
Taxes, other than income taxes	42	47	47
Income taxes (Notes A and K)	24	25	31
TOTAL OPERATING EXPENSES	857	749	751
OPERATING INCOME	79	69	73
OTHER INCOME (DEDUCTIONS)			
Investment and other income (Note A)	1	5	2
Income taxes (Notes A and K)	1	(1)	-
Other deductions	(1)	-	(1)
TOTAL OTHER INCOME (DEDUCTIONS)	1	4	1
INTEREST EXPENSE			
Interest on long-term debt	25	23	21
Other interest	9	5	3
NET INTEREST EXPENSE	34	28	24
NET INCOME	$ 46	$ 45	$ 50

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, 2007	2006	2005
	(Millions of Dollars)		
NET INCOME	$ 46	$ 45	$ 50
OTHER COMPREHENSIVE INCOME/(LOSS), NET OF TAXES			
Pension plan liability adjustments, net of $(1) taxes in 2006 and 2005	-	(1)	(1)
Unrealized gains/(losses) on derivatives qualified as cash flow hedges, net of $(2) and $3, taxes in 2006 and 2005, respectively	-	(2)	4
Less: Reclassification adjustment gains/(losses) included in net income, net of $(1) and $1, taxes in 2006 and 2005, respectively	(1)	(2)	1
TOTAL OTHER COMPREHENSIVE INCOME/(LOSS), NET OF TAXES	1	(1)	2
COMPREHENSIVE INCOME	$ 47	$ 44	$ 52

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)	Common Stock Shares	Common Stock Amount	Additional Paid-In Capital	Retained Earnings	Accumulated Other Comprehensive Income/(Loss)	Total
BALANCE AS OF DECEMBER 31, 2004	1,000	$ -	$ 194	$ 204	$ (10)	$ 388
Net Income				50		50
Common stock dividend to parent				(71)		(71)
Other comprehensive income					2	2
BALANCE AS OF DECEMBER 31, 2005	1,000	$ -	$ 194	$ 183	$ (8)	$ 369
Net Income				45		45
Common stock dividend to parent				(28)		(28)
Other comprehensive loss					(1)	(1)
Adjustment to initially apply FASB Statement No. 158, net of tax (Notes E and F)					(25)	(25)
BALANCE AS OF DECEMBER 31, 2006	1,000	$ -	$ 194	$ 200	$ (34)	$ 360
Net Income				46		46
Common stock dividend to parent				(31)		(31)
Capital contribution by parent			40			40
Other comprehensive income					1	1
BALANCE AS OF DECEMBER 31, 2007	1,000	$ -	$ 234	$ 215	$ (33)	$ 416

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, 2007	2006	2005
	(Millions of Dollars)		
OPERATING ACTIVITIES			
Net income	$ 46	$ 45	$ 50
PRINCIPAL NON-CASH CHARGES/(CREDITS) TO INCOME			
Depreciation and amortization	38	35	34
Deferred income taxes	15	16	4
Other non-cash items (net)	4	(9)	-
CHANGES IN ASSETS AND LIABILITIES			
Accounts receivable - customers, less allowance for uncollectibles	(6)	13	(30)
Accounts receivable from affiliated companies	-	22	(7)
Materials and supplies, including gas in storage	13	4	(20)
Prepayments, other receivables and other current assets	10	(10)	(15)
Recoverable energy costs	(12)	(6)	-
Accounts payable	18	(4)	15
Accounts payable to affiliated companies	(7)	15	(7)
Pensions and retiree benefits	2	4	3
Accrued taxes	(4)	1	2
Accrued interest	2	4	-
Deferred charges, noncurrent assets and other regulatory assets	5	(17)	(5)
Deferred credits and other regulatory liabilities	(22)	17	2
Superfund and other environmental costs	7	(4)	(5)
Other assets	-	-	(1)
Other liabilities	(9)	18	(1)
NET CASH FLOWS FROM OPERATING ACTIVITIES	100	144	19
INVESTING ACTIVITIES			
Utility construction expenditures	(112)	(110)	(87)
Decrease in restricted cash	1	-	-
Cost of removal less salvage	(3)	-	(3)
NET CASH FLOWS USED IN INVESTING ACTIVITIES	(114)	(110)	(90)
FINANCING ACTIVITIES			
Net proceeds from/(payments of) short-term debt	11	(67)	101
Issuance of long-term debt	-	75	40
Retirement of long-term debt	(22)	(2)	(2)
Capital contribution from parent	40	-	-
Dividend to parent	(31)	(28)	(71)
Loan from affiliate	55	-	-
NET CASH FLOWS (USED IN)/FROM FINANCING ACTIVITIES	53	(22)	68
CASH AND TEMPORARY CASH INVESTMENTS:			
NET CHANGE FOR THE PERIOD	39	12	(3)
BALANCE AT BEGINNING OF PERIOD	21	9	12
BALANCE AT END OF PERIOD	$ 60	$ 21	$ 9
SUPPLEMENTAL DISCLOSURE OF CASH FLOW INFORMATION			
Cash paid during the period for:			
Interest	$ 24	$ 23	$ 24
Income Taxes	$ 23	$ 36	$ 30

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

Orange and Rockland Utilities, Inc.
Consolidated Statement of Capitalization

	Interest Rate	Series	Shares outstanding December 31, 2007	Shares outstanding December 31, 2006	At December 31, 2007	At December 31, 2006
					(Millions of Dollars)	
TOTAL COMMON SHAREHOLDER'S EQUITY LESS ACCUMULATED OTHER COMPREHENSIVE LOSS			1,000	1,000	$ 449	$ 394
ACCUMULATED OTHER COMPREHENSIVE LOSS						
Pension plan minimum liability adjustments					(2)	(2)
Adjustment to initially apply FASB Statement No. 158, net of $(15) taxes in 2007 and 2006 (Notes E and F)					(25)	(25)
Unrealized losses on derivatives qualified as cash flow hedges net of $(5) taxes in 2007 and 2006					(7)	(7)
Less: Reclassification adjustment for losses included in net income					(1)	-
TOTAL ACCUMULATED OTHER COMPREHENSIVE LOSS, NET OF TAXES					(33)	(34)
TOTAL COMMON SHAREHOLDER'S EQUITY (SEE STATEMENT OF COMMON SHAREHOLDER'S EQUITY AND NOTE C)					$ 416	$ 360
LONG-TERM DEBT (NOTE C) Maturity	Interest Rate	Series				
DEBENTURES:						
2010	7.50%	2000A			$ 55	$ 55
2015	5.30	2005A			40	40
2016	5.45	2006A			75	75
2027	6.50	1997F			80	80
2029	7.00	1999G			45	45
TOTAL DEBENTURES					295	295
FIRST MORTGAGE BONDS:						
2007	7.125	1997J			-	20
2018	7.07	1998C			3	3
TOTAL FIRST MORTGAGE BONDS					3	23
TRANSITION BONDS:						
2019	5.22	2004-1			40	42
TOTAL TRANSITION BONDS					40	42
TAX-EXEMPT DEBT - Notes Issued to New York State Energy Research and Development Authority for Facilities Revenue Bonds:						
2014 (Note N)	3.37	1994A*			55	55
2015	3.37	1995A*			44	44
TOTAL TAX-EXEMPT DEBT					99	99
Unamortized debt discount					(1)	(1)
TOTAL					436	458
Less: long-term debt due within one year					3	22
TOTAL LONG-TERM DEBT					433	436
TOTAL CAPITALIZATION					$ 849	$ 796

* Issued for pollution control financing.

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 interim 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 period ended December 31, 2007 and 2006, operating revenues for RECO and Pike were 22.7 percent and 0.8 percent and 21.7 percent and 1.2 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.

The Company is subject to regulation by the Federal Energy Regulatory Commission (FERC), the New York Public Service Commission (PSC), the New Jersey Board of Public Utilities (NJBPU) and the Pennsylvania Public Utility Commission (PPUC) 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 Financial Accounting Standards Board's (FASB) Statement of Financial Accounting Standards (SFAS) No. 71 (SFAS No. 71), "Accounting for the Effects of Certain Types of Regulation," and, in accordance with SFAS No. 71, the accounting requirements of the FERC and the state public utility regulatory commissions having jurisdiction.

SFAS No. 71 specifies 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 SFAS No. 71. 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 SFAS No. 71.

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

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 O.

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 5.2 percent, 5.0 percent and 3.9 percent for 2007, 2006 and 2005, respectively.

The Company generally computes annual charges for depreciation using the straight-line method for financial statement purposes, with rates based on average service lives and net salvage factors. The average depreciation rates for the Company were 2.8 percent for 2007 and 2006 and 2.9 percent for 2005.

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 55 years for general plant.

At December 31, 2007 and 2006, the capitalized cost of the Company's utility plant, net of accumulated depreciation, was as follows:

(Millions of Dollars)	2007	2006
Electric		
Transmission	$124	$112
Distribution	544	517
Gas*	305	292
General	87	79
Held for future use	5	4
Construction work in progress	55	39
NET UTILITY PLANT	$1,120	$1,043

* Primarily distribution.

Impairments

In accordance with SFAS No. 144, "Accounting for the 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 would be written down to their estimated fair value. There we no triggering events in 2005 to 2007.

Revenues

The Company recognizes revenues for electric and gas 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 PSC 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, 2007 and 2006 were $42 million and $36 million, respectively.

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 $3.7 million and $0.3 million of gross receipts tax, respectively, in 2007. RECO recorded $8.2 million in TEFA tax in 2007.

Recoverable Energy Costs

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

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

RECO purchases electric energy under a competitive bidding process supervised by the NJBPU for contracts ranging from one to three years. 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. See Note B for a description of the 2003 NJBPU ruling regarding previously deferred purchased power costs.

Pike bills its customers for the electricity it supplies to them based on a default service rate approved by the PPUC. Prior to 2008, Pike neither collected nor refunded to customers differences between actual amounts billed for electric supply and electric supply costs it incurred. In January 2008, Pike began deferring 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. See Note B.

Independent System Operators

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.

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.

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 either cost or cash surrender value and include the supplemental retirement income plan’s corporate-owned life insurance assets.

Federal Income Tax

In accordance with SFAS No. 109, “Accounting for Income Taxes” (SFAS No. 109), the Company has recorded an accumulated deferred federal income tax liability for temporary differences between the book and tax bases 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 they 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 SFAS No. 71, 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 K. In 1993, the PSC issued a Policy Statement approving accounting procedures consistent with SFAS No. 109 and providing assurances that these future increases in taxes will be recoverable in rates. In January 2007, the Company adopted FASB Interpretation No. 48, “Accounting for Uncertainty in Income Taxes – and interpretation of FASB Statement No. 109” (FIN 48). This interpretation clarifies the accounting for uncertain tax positions in accordance with FASB Statement No. 109. See Note K.

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

The Company, along with Con Edison and its other subsidiaries, files a consolidated federal income tax return. The consolidated income tax liability is allocated to each member of the consolidated group using the separate return method. Each member pays or receives an amount based on its own taxable income or loss in accordance with 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 and apportionment of income among the states in which the Company does business. 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. Similar to a federal 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. Similar to a federal 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 and Restructuring Agreements

Electric

In October 2003, the PSC approved an agreement among O&R, the staff of the PSC and other parties with respect to the rates O&R can charge to its New York customers for electric service. The electric agreement, which covered the period from July 2003 through October 2006, provided for no changes to electric base rates and provided for the amortization and offset of regulatory assets and liabilities, the net effect of which was to reduce electric operating income by a total of $11 million (pre tax) over the period covered by the agreement. The agreement provided for recovery of energy costs from customers on a current basis. It also provided for O&R to share equally with customers earnings above a 12.75 percent return on common equity during the three-year period from July 2003 through June 2006. Beginning July 2006, O&R was not subject to earnings sharing. Pursuant to these provisions, $3.6 million and $6.7 million were deferred for future customer benefit in 2006 and 2005, respectively.

In October 2007, the PSC issued an order that continues O&R's rates for electric service rendered in New York at current levels. The order, which is based on an allowed annual rate of return on common equity of 9.1 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. O&R commenced actions in New York State Supreme Court seeking to annul the March 2007 PSC order that initiated the proceeding and the October 2007 order.

In August 2007, O&R filed a request with the PSC for an increase in the rates it charges for electric service rendered in New York, effective July 2008, of $47.8 million. The filing reflects a return on common equity of 11.5 percent and a common equity ratio of 48.6 percent. The filing proposes continuation of the current provisions with respect to recovery from customers of the cost of purchased power, and the reconciliation of actual expenses allocable to the electric business to the amounts for such costs reflected in electric rates for pension and other postretirement benefit costs, environmental and research and development costs. In October 2007, O&R submitted to the PSC a revenue decoupling proposal applicable to the company's electric service in New York. In November 2007, O&R updated its rate request to reflect the impact of applying all available credits, including $3.3 million of earnings above the 9.1 percent allowed ROE during March through June 2007, as directed by the PSC in its October 2007 Order. The impact of this and other changes reduced the requested rate increase to $43.7 million. In December 2007, PSC Staff submitted direct testimony and exhibits supporting a $17.5 million rate increase, based on a return on equity of 8.9 percent and an equity ratio of 48 percent. A decision in this case is expected in June 2008.

In July 2003, the NJBPU ruled on the petitions of RECO for an increase in electric rates and recovery of deferred purchased power costs. The NJBPU ordered a $7 million decrease in RECO's electric base rates, effective August 2003, authorized RECO's recovery of approximately $83 million of previously deferred purchased power costs and associated interest and disallowed recovery of approximately $19 million of such costs and associated interest.

In July 2004, the NJBPU approved RECO's Phase II petition to increase base rates annually by $2.7 million, effective August 1, 2004. The Phase II decision provided for the recovery of carrying costs for two substation projects and specified additional reliability programs. Also in July 2004, Transition Funding issued $46 million of 5.22% 15-year Transition Bonds and used the proceeds thereof to purchase from RECO the right to be paid a Transition Bond Charge (TBC) and associated tax charges by its customers relating to the balance of previously deferred purchased power costs, discussed above.

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 provides for a $6.4 million rate increase during the first year, with no further increase during the final two years. The plan reflects a return on common equity of 9.75 percent and a common equity ratio of 46.5 percent of capitalization.

Pike bills its customers for the electricity it supplies to them based on a default service rate approved by the PPUC. Prior to 2008, Pike neither collected from nor refunded to customers differences between actual amounts billed for electric supply and electric supply costs it incurred. In January 2006, based upon the results of an auction overseen by the PPUC in which an affiliate of Con Edison was the winning bidder, an increase in the default service rate of approximately 70 percent was approved by the PPUC. In February 2006, the PPUC initiated a fact-finding investigation in the competitive electric market in Pike's service territory, which investigation is ongoing. On June 1, 2006, the Law Bureau of the PPUC issued a report that contained various recommendations for future action. The report recommended that the PPUC consider integrating Pike's energy procurement with that of either O&R, RECO or another Pennsylvania electric distribution company, having an independent study performed regarding the costs and benefits of interconnecting Pike with PJM, and having an independent study performed regarding the costs and benefits of the sale of Pike to another Pennsylvania electric distribution company or a rural electric cooperative. The PPUC has yet to act on any of these recommendations.

In July 2007, Pike and a majority of the 50 customers that filed complaints with the PPUC regarding a January 2006 increase in the Pike's default service rates entered into a joint Petition for Settlement, resolving all issues pertaining to the complaints. In February 2008, the PPUC approved the joint Petition for Settlement.

In January 2008, Pike began deferring 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.

Pike is obligated under Pennsylvania law to serve those customers who do not purchase electricity from other suppliers. See “Recoverable Energy Costs” in Note A.

Gas

In October 2003, the PSC approved a gas rate agreement among O&R, the PSC staff and other parties. This agreement, which covered the period November 2003 through October 2006, provided for annual increases in gas base rates of $9 million effective November 2003, $9 million effective November 2004 and $5 million effective November 2005. The agreement provided for O&R to share equally with customers earnings in excess of an 11 percent return on common equity. Earnings for the rate years ended October 2004, 2005 and 2006 were below this level. The rate agreement also included the amortization of certain regulatory assets and liabilities. The net effect of this amortization was a non-cash increase in gas revenues of $2 million over the period of the three-year rate plan.

In October 2006, the PSC approved the June 2006 settlement agreement among O&R, the staff of the PSC and other parties. The settlement agreement establishes a rate plan that covers the three-year period November 1, 2006 through October 31, 2009. The rate plan provides 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 provides 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, will be billed to customers in the second and third years. As a result, O&R’s billings to customers will increase $6.5 million in each of the first two years and $6.3 million in the third. The first year rate increase includes $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 new rate plan, such revenues will be used to offset the cost of gas to be recovered from customers. The rate plan continues 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 provides 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 will 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) up to an 11 percent annual return on common equity (based upon the actual average common equity ratio, subject to a maximum 50 percent of capitalization) are retained by the company. O&R Adjusted Earnings above an 11 percent return are 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 are retained by the company, with the balance being deferred for the benefit of customers. Thirty-five percent of any remaining O&R Adjusted Earnings between a 12 and 14 percent return are retained by the company, with the balance deferred for the benefit of customers. Any remaining O&R Adjusted Earnings above a 14 percent return are to be deferred for the benefit of customers. For purposes of these earnings sharing provisions, if in any rate year O&R Adjusted Earnings is less than 11 percent, the shortfall will be deducted from O&R Adjusted Earnings for the other rate years. The earnings sharing thresholds will each be reduced by 20 basis points if certain objectives relating to the company's retail choice program are not met. In 2007, O&R recorded a $1.3 million regulatory liability for earnings in excess of the 11 percent target return on equity for the rate year ended October 31, 2007.

The rate plan also includes up to $1 million of potential revenue reductions in the first year of the agreement, increasing up to $1.2 million, if the company does not comply with certain requirements regarding customer satisfaction and work practices associated with underground facilities. In 2007, O&R recorded a $0.2 million regulatory liability for not complying with certain requirements regarding customer satisfaction and work practices associated with underground facilities for the rate year ended October 31, 2007.

In May 2005, the PPUC approved an increase to the rates Pike charges for gas service by $0.1 million, effective June 1, 2005.

Regulatory Assets and Liabilities

Regulatory assets and liabilities at December 31, 2007 and 2006 were comprised of the following items:

(Millions of Dollars)	2007	2006
Regulatory assets		
Unrecognized pension and other postretirement costs	$150	$152
Environmental remediation costs	65	63
Transition bond charges	63	67
Pension and other postretirement benefits deferrals	56	59
Future federal income tax	55	54
Other	19	19
Regulatory assets	408	414
Deferred derivative losses - current	1	24
Recoverable energy costs - current	23	22
Total regulatory assets	$432	$460
Regulatory liabilities		
Allowance for cost of removal less salvage	$61	$60
Refundable energy costs	29	40
Unrealized gains on hedging	13	1
NYS tax law changes	2	10
Property tax deferral	-	5
Other	16	18
Regulatory liabilities	121	134
Deferred derivative gains – current	5	1
Total regulatory liabilities	$126	$135

"Unrecognized pension and other postretirement costs" represents the net regulatory asset associated with the Company's adoption of FASB Statement No. 158, "Employers' Accounting for Defined Benefit Pension and Other Postretirement Plans - an amendment of FASB Statements No. 87, 88,106, and 132(R)" (SFAS No. 158) in December 2006. See Notes E and F.

Note C – Capitalization

Common Stock

At December 31, 2007 and 2006, all of the outstanding common stock of the Company was owned by Con Edison. In accordance with PSC 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 2008-2012 is as follows:

(Millions of Dollars)	
2008	$3
2009	3
2010	58
2011	3
2012	3

O&R has issued $99 million of tax-exempt debt through the New York State Energy Research and Development Authority (NYSERDA) that currently bear interest at a rate determined weekly and is subject to tender by bondholders for purchase by the Company. Of this amount, $55 million is insured by Financial Guaranty Insurance Company and $44 million is insured by Ambac Assurance Corporation. Recent downgrades in the credit ratings of these insurers have resulted in increased interest rates on this O&R debt. A substantial portion of this debt has been tendered by bondholders for purchase by the Company. O&R is evaluating alternatives with respect to its tax-exempt debt.

Long-term debt is stated at cost, which in total, as of December 31, 2007, approximates fair value (estimated based on current rates for debt of the same remaining maturities).

At December 31, 2007 and 2006, long-term debt of the Company included $3 million of mortgage bonds, collateralized by substantially all utility plant and other physical property of Pike. Also, outstanding at December 31, 2006 were $20 million of RECO mortgage bonds, which were paid at maturity in February 2007. Long-term debt also included $40 million and $42 million at December 31, 2007 and 2006, respectively, of Transition Bonds issued by Transition Funding. See Note B.

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 they were in compliance with their significant debt covenants at December 31, 2007.

The tax-exempt financing arrangements involved the issuance of uncollateralized promissory notes 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 and 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 to which such provisions applied. If an event of default were to occur, the principal and accrued interest on the debt to which such event of default applied 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 obligated utility 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. Certain of the facilities also include as events 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 its other regulated utility subsidiary, Consolidated Edison of New York, Inc. (Con Edison of New York), 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 an aggregate amount of up to $2.25 billion, with $200 million available to O&R. In June 2007, the Credit Agreement, which was to expire in June 2011, was extended for an additional year. O&R is solely responsible for its obligations under the credit agreements and no company is responsible for the obligations of any company other than itself. O&R uses the credit agreements to support its commercial paper program and obtain letters of credit.

At December 31, 2007 and 2006, O&R had $45 million and $34 million of commercial paper outstanding at a weighted average interest rate of 5.6 percent and 5.4 percent, respectively. At December 31, 2007 and 2006, $25 million and $2 million of letters of credit were outstanding under the agreements, respectively.

The banks' commitments under the Credit Agreement are subject to certain conditions, including that there be no event of default. The commitments are not subject to maintenance of credit rating levels or the absence of a material adverse change. Upon a change of control of, or upon an event of default by Con Edison, Con Edison of New York 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 agreements 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, 2007, this ratio was 0.54 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 agreements reflect O&R's credit ratings.

In December 2007, Con Edison of New York loaned O&R $55 million, which was repaid in January 2008. See Note P 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 Con Edison of New York 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.

Investment gains and losses are fully recognized in expense over a 15-year period and other actuarial gains and losses are fully recognized in expense over a 10-year period, subject to the deferral provisions in the next paragraph. This amortization is in accordance with the Statement of Policy issued by the PSC and is permitted under SFAS No. 87, "Employers' Accounting for Pensions," which provides a "corridor method" for moderating the effect of investment gains and losses on pension expense, or alternatively, allows for any systematic method of amortization of unrecognized gains and losses that is faster than the corridor method and is applied consistently to both gains and losses.

In accordance with O&R's current electric and gas rate plans, the Company defers any difference between expenses recognized under SFAS No. 87 for the Company's New York business and the amount reflected in O&R's rates for such expenses. The rate plans for RECO and Pike do not have comparable deferral provisions.

Net Periodic Benefit Cost

The components of the Company's net periodic benefit costs for 2007, 2006 and 2005 were as follows:

(Millions of Dollars)	2007	2006	2005
Service cost – including administrative expenses	$9	$10	$9
Interest cost on projected benefit obligation	31	29	28
Expected return on plan assets	(27)	(25)	(24)
Amortization of net actuarial loss	21	22	17
Amortization of prior service costs	1	1	1
NET PERIODIC BENEFIT COST	$35	$37	$31
Cost capitalized	(9)	(8)	(7)
Cost expensed/(deferred)	1	(13)	(11)
Cost charged to operating expenses	$27	$16	$13

Notes to the Financial Statements - Continued

Funded Status

The funded status of the Company's pension obligations at December 31, 2007, 2006 and 2005 were as follows:

(Millions of Dollars)	2007	2006	2005
CHANGE IN PROJECTED BENEFIT OBLIGATION			
Projected benefit obligation at beginning of year	$527	$521	$471
Service cost – excluding administrative expenses	9	9	9
Interest cost on projected benefit obligation	31	29	28
Plan amendments	-	-	-
Net actuarial loss	15	(5)	38
Benefits paid	(29)	(27)	(25)
PROJECTED BENEFIT OBLIGATION AT END OF YEAR	$553	$527	$521
CHANGE IN PLAN ASSETS			
Fair value of plan assets at beginning of year	$339	$294	$267
Actual return on plan assets	25	37	22
Employer contributions	36	37	31
Benefits paid	(29)	(27)	(25)
Administrative expenses	(1)	(2)	(1)
FAIR VALUE OF PLAN ASSETS AT END OF YEAR	$370	$339	$294
FUNDED STATUS	$(183)	$(188)	$(227)
Unrecognized net loss	115	118	157
Unrecognized prior service costs	10	11	12
NET PREPAID BENEFIT COST	$-	$-	$(58)
ACCUMULATED BENEFIT OBLIGATION	$529	$505	$498

In December 2006, O&R adopted SFAS No. 158. This Statement requires 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 Statement requires employers to recognize all unrecognized prior service costs and credits and unrecognized actuarial gains and losses in accumulated other comprehensive income (OCI), net of tax. Such amounts will be adjusted as they are subsequently recognized as components of net periodic benefit cost or income pursuant to the current recognition and amortization provisions.

Upon adoption of SFAS No. 158, the Company recognized an additional pension liability of $125 million. A regulatory asset of $99 million was recorded for the unrecognized net losses and unrecognized prior service costs associated with the Company consistent with SFAS No. 71. An OCI charge of $15 million (net of taxes) was recorded for the unrecognized net losses and unrecognized prior service costs associated with O&R's New Jersey and Pennsylvania utility subsidiaries. In the first quarter of 2007, in accordance with SFAS No. 158 and based on the final actuarial valuation as of December 31, 2006, O&R adjusted the estimated amounts recorded upon adoption of SFAS No. 158 by increasing its pension liability by $5 million and the related regulatory asset by $4 million and recognizing a charge of $1 million (net of taxes) to OCI.

The estimated net loss and prior service cost for the pension plan that will be amortized into net periodic benefit cost over the next year for O&R are $21 million and $1 million, respectively.

At December 31, 2007 and 2006, the Company's investments include $12 million and $11 million, respectively, 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 $33 million as of December 31, 2007 and 2006.

Assumptions

The actuarial assumptions were as follows:

	2007	2006	2005
Weighted-average assumptions used to determine benefit obligations at December 31:			
Discount rate	6.00%	6.00%	5.70%
Rate of compensation increase	4.00%	4.00%	4.00%
Weighted-average assumptions used to determine net periodic benefit cost for the years ended December 31:			
Discount rate	6.00%	5.70%	5.90%
Expected return on plan assets	8.50%	8.50%	8.80%
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 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 $100 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)	2008	2009	2010	2011	2012	2013-2017
O&R	$30	$31	$32	$34	$36	$194

Notes to the Financial Statements - Continued

Expected Contributions

Based on current estimates, the Company is not required under funding regulations and laws to make any contributions to the pension plan during 2008. 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 $32 million to the pension plan during 2008.

Plan Assets

The asset allocations for the pension plan at the end of 2007, 2006 and 2005, and the target allocation for 2008 are as follows:

ASSET CATEGORY	Target Allocation 2008	Plan Assets at December 31 2007	2006	2005
Equity Securities	65%	65%	66%	67%
Debt Securities	27%	28%	28%	28%
Real Estate	8%	7%	6%	5%
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.

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 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, chief financial and chief accounting officers and others the Board of Trustees may appoint in addition to or in place of the designated Named Fiduciaries.

The investment objective for the pension trust is to maximize the long-term total return on the trust assets within a prudent level of risk. The investment strategy is to diversify its funds across asset classes, investment styles and fund managers. The target asset allocation is reviewed periodically based on asset/liability studies and may be modified as appropriate. The target asset allocation for 2008 reflects the results of such a study conducted in 2007.

Individual 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. Manager performance, total fund performance, and compliance with asset allocation guidelines are monitored on an ongoing basis, and reviewed by the Named Fiduciaries and reported to the Committee on a regular basis. Changes in fund managers and rebalancing of the portfolio are undertaken as appropriate. The Named Fiduciaries approve such changes, which are also reported to the Committee.

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

	For the Years Ended December 31,		
(Millions of Dollars)	2007	2006	2005
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.

Investment plan gains and losses are fully recognized in expense over a 15-year period and other actuarial gains and losses are fully recognized in expense over a 10-year period, provided, however, that O&R defers any difference between expenses recognized under SFAS No. 106, “Employers' Accounting for Postretirement Benefits Other Than Pension,” and the current rate allowance for its electric and gas operations. The electric rate plan for Pike has a comparable deferral provision. The rate plan for RECO and the gas rate plan for Pike do not have comparable deferral provisions.

Net Periodic Benefit Cost

The components of the Company's net periodic postretirement benefit costs for 2007, 2006 and 2005 were as follows:

(Millions of Dollars)	2007	2006	2005
Service cost	$4	$4	$4
Interest cost on accumulated other postretirement benefit obligation	11	10	10
Expected return on plan assets	(7)	(6)	(5)
Amortization of net actuarial loss	9	9	9
NET PERIODIC POSTRETIREMENT BENEFIT COST	$17	$17	$18
Cost capitalized	(5)	(4)	(4)
Cost deferred	(3)	(5)	(6)
Cost charged to operating expenses	$9	$8	$8

Funded Status

The funded status of the programs at December 31, 2007, 2006 and 2005 were as follows:

(Millions of Dollars)	2007	2006	2005
CHANGE IN BENEFIT OBLIGATION			
Benefit obligation at beginning of year	$189	$184	$157
Service cost	4	4	4
Interest cost on accumulated postretirement benefit obligation	11	10	10
Net actuarial loss	(11)	(8)	23
Benefits paid and administrative expenses	(11)	(10)	(10)
Medicare prescription subsidy	-	1	-
Plan amendments	14	8	-
BENEFIT OBLIGATION AT END OF YEAR	$196	$189	$184
CHANGE IN PLAN ASSETS			
Fair value of plan assets at beginning of year	$77	$64	$55
Actual return on plan assets	(1)	8	3
Employer contributions	12	13	13
Benefits paid	(8)	(8)	(7)
FAIR VALUE OF PLAN ASSETS AT END OF YEAR	$80	$77	$64
FUNDED STATUS	$(116)	$(112)	$(120)
Unrecognized net loss	50	61	80
Unrecognized prior service costs	21	7	(1)
ACCRUED POSTRETIREMENT BENEFIT COST	-	-	$(41)

For discussion of SFAS No. 158, see Note E. Upon adoption of SFAS No. 158, O&R recognized an additional liability for other postretirement benefits of $69 million. A regulatory asset of $53 million was recorded for the unrecognized net losses, unrecognized prior service costs and unrecognized transition liability associated with the Company consistent with SFAS No. 71. An OCI charge of $10 million (net of taxes) was recorded for the unrecognized net losses, unrecognized prior service costs and unrecognized transition liability associated with O&R's New Jersey and Pennsylvania utility subsidiaries. In the first quarter of 2007, in accordance with SFAS No. 158 and based on the final actuarial valuation as of December 31, 2006, O&R adjusted the estimated amounts recorded upon adoption of SFAS No. 158 by decreasing its liability for other postretirement benefits by $9 million and the related regulatory asset by $7 million and recognizing a credit of $1 million (net of taxes) to OCI.

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 $2 million, respectively.

Assumptions

The actuarial assumptions were as follows:

	2007	2006	2005
Weighted-average assumptions used to determine benefit obligations at December 31:			
Discount Rate	6.00%	6.00%	5.70%
Weighted-average assumptions used to determine net periodic benefit cost for the years ended December 31:			
Discount Rate	6.00%	5.70%	5.90%
Expected Return on Plan Assets			
Tax-Exempt	8.50%	8.50%	8.80%
Taxable	8.00%	8.00%	8.30%

Notes to the Financial Statements - Continued

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, 2007 was 9 percent, which is assumed to decrease gradually to 4.5 percent by 2012 and remain at that level thereafter. The health care cost trend rate used to determine benefit obligations as of December 31, 2007 was 8 percent, which is assumed to decrease gradually to 4.5 percent by 2012 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, 2007:

	1-Percentage-Point	
(Millions of Dollars)	Increase	Decrease
Effect on accumulated other postretirement benefit obligation	$20	$(17)
Effect on service cost and interest cost components for 2007	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)	2008	2009	2010	2011	2012	2013-2017
Gross Benefit Payments	$12	$12	$13	$14	$14	$78
Medicare Prescription Benefit Receipts	1	1	1	1	1	8

Expected Contributions

Based on current estimates, O&R expects to make contributions of $14 million to the other postretirement benefit plans in 2008.

Plan Assets

The asset allocations for O&R's other postretirement benefit plans at the end of 2007, 2006 and 2005, and the target allocation for 2008 are as follows:

	Target Allocation	Plan Assets at December 31		
ASSET CATEGORY	2008	2007	2006	2005
Equity Securities	65%	63%	63%	64%
Debt Securities	35%	37%	37%	36%
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.

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. FASB Staff Position (FSP) No. FAS 106-2, issued by the FASB in May 2004, provides accounting and disclosure requirements relating to the Act. The Company's actuaries have determined that each 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.

Note G – Environmental Matters

Hazardous substances, such as coal tar and asbestos, 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 (the MGP Sites).

MGP Sites

The New York State Department of Environmental Conservation (DEC) requires O&R to develop and implement remediation programs for its MGP Sites. O&R has investigated and detected soil and/or groundwater contamination to varying degrees at its MGP Sites. Remediation has been completed at one MGP site and is currently underway at another MGP site. Additional investigation will be required for three of the remaining MGP sites and remediation required at all of them. At December 31, 2007 and 2006, O&R had an accrued liability of $56 million and $49 million, respectively, for its MGP Sites.

In 2007, O&R estimated that for its MGP Sites, each of which has been investigated, the aggregate undiscounted potential liability for the remediation of such contaminants could range up to $115 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.

O&R is permitted under its New York rate agreements to recover or defer as regulatory assets (for subsequent recovery through rates) certain site investigation and remediation costs. At December 31, 2007 and 2006, O&R's regulatory asset for recovery of these costs were $65 million and $63 million, respectively. The environmental remediation costs for the years ended December 31, 2007 and 2006 were approximately $8 million each period. There were no insurance recoveries during these periods.

Asbestos Proceedings

Suits have been brought 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) was $5 million at December 31, 2007 and 2006.

Note H – Closure of Lovett Generating Station

In June 1999, O&R sold its electric generating assets, including the Lovett generating station. The generating station includes pollution control facilities that were financed by O&R with the proceeds of $99 million of tax-exempt debt that remains outstanding. The owner of the generating station has indicated that it will discontinue all operations at the station, which could prevent use of certain O&R equipment that had been permitted to remain on the site following the sale. O&R does not expect that the closure of the station will have a material adverse effect on its financial position, results of operations or liquidity.

Note I – Non-Utility Generators and Other Power Purchase Agreements

O&R had long-term power purchase agreements (PPAs) with non-utility generators (NUGs) and others for generating capacity. The Company recovers its purchase power costs in accordance with provisions approved by the applicable state public utility commissions. See "Recoverable Energy Costs" in Note A.

On December 31, 2006, O&R terminated the Crossroads PPA, which obligated O&R to make capacity and other fixed payments with an agreement to pay Crossroads a $1.4 million buyout amount.

For energy delivered under the PPAs, the Company was obligated to pay variable prices. The Company's payments under the PPAs for capacity, energy and other fixed payments in 2007, 2006 and 2005 were as follows:

	For the Years Ended December 31,		
(Millions of Dollars)	2007	2006	2005
Lederle*	$-	$2	$14
Crossroads**	-	3	2

* Contract ended January 31, 2006.
** Contract terminated on December 31, 2006.

Note J – Leases

O&R's leases include rights of way for electric and gas distribution facilities, office buildings and automobiles. In accordance with SFAS No. 13, "Accounting 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 SFAS No. 71, the amortization of the leased asset is based on the rental payments recovered from customers. At December 31, 2007, $2 million related to a new capital lease was included on the Company's balance sheet. The Company expects to make an upfront payment of $2 million for this lease in the first quarter of 2008.

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

(Millions of Dollars)	
2008	$1
2009	1
2010	1
2011	1
2012	-
All years thereafter	-
Total	$4

Note K – Income Tax

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

(Millions of Dollars)	2007	2006	2005
Charge/(benefit) to operations:			
State			
Current	$1	$1	$4
Deferred – net	5	5	3
Federal			
Current	8	8	23
Deferred – net	10	11	1
TOTAL CHARGE TO OPERATIONS	24	25	31
TOTAL CHARGE/(BENEFIT) TO OTHER INCOME	(1)	1	-
TOTAL	$23	$26	$31

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

(Millions of Dollars)	2007	2006
Deferred tax liabilities:		
Depreciation	$121	$116
Regulatory liability – future income tax	75	70
Unrecognized pension and other postretirement costs – SFAS No. 158	61	62
State income tax	19	16
Capitalized overheads	33	33
Other	27	31
Total deferred tax liabilities	336	328
Deferred tax assets:		
Unrecognized pension and other postretirement costs – SFAS No. 158	61	62
Regulatory asset – future income tax	17	16
Other	55	55
Total deferred tax assets	133	133
NET LIABILITIES	203	195
INVESTMENT TAX CREDITS	4	4
DEFERRED INCOME TAXES AND INVESTMENT TAX CREDITS	207	199
DEFERRED INCOME TAXES – RECOVERABLE ENERGY COSTS	9	9
TOTAL DEFERRED INCOME TAXES AND INVESTMENT TAX CREDITS	$216	$208

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)	2007	2006	2005
STATUTORY TAX RATE			
Federal	35%	35%	35%
Changes in computed taxes resulting from:			
State income tax	6	6	6
Depreciation related differences	-	(1)	-
Cost of removal	(3)	(2)	(1)
Other	(4)	(2)	(1)
Effective Tax Rate	34%	36%	39%

Uncertain Tax Positions

In January 2007, Con Edison and its subsidiaries adopted FIN 48. This interpretation clarifies the accounting for uncertain tax positions in accordance with FASB Statement No. 109. Under the interpretation, an enterprise would not be 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.

The IRS has essentially completed its audits of Con Edison's federal income tax returns, which include O&R, through 2006. Con Edison's federal income tax returns for 2002 through 2006 reflect certain tax positions with which the IRS does not or may not agree, including tax positions with respect to the deduction of certain construction-related costs for which the ultimate deductibility is highly certain but for which there is uncertainty about the timing of such deductibility. The field audits of Con Edison's New York state income tax returns have been completed through 2002. 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 state income tax returns.

The Company's uncertain tax positions include use of the "simplified service cost method" (SSCM) to determine the extent to which construction-related costs could be deducted in 2002 through 2005. The Company expects that it will be required to repay, with interest, a portion of its past SSCM tax benefits ($28 million) and to capitalize and depreciate over a period of years costs it previously deducted under SSCM. Interest on all past SSCM tax benefits for O&R could be approximately $9 million. Repayment of the SSCM tax benefits would not otherwise affect the Company's results of operations because deferred taxes have been previously provided for the related temporary differences between the SSCM deductions taken for federal income tax purposes and the corresponding amounts charged to expense for financial reporting purposes.

In June 2007, Con Edison paid $160 million to the Internal Revenue Service, $13 million of which is attributable to O&R, as a deposit for the repayment, including related interest, that the Company expects will be required with respect to the past SSCM benefits. As a result, for federal income tax purposes, interest will continue to accrue only on the portion of the liability, if any, that exceeds the deposit. O&R has recorded the deposit as a noncurrent asset on its consolidated balance sheet.

Upon adoption of FIN 48, the Company reclassified previously recorded tax liabilities of $12 million, which primarily related to SSCM, to a liability for uncertain tax positions. At December 31, 2007, the liability for uncertain tax positions was $12 million, and accrued interest on the liability amounted to $4 million. The Company recognizes interest accrued related to the liability for uncertain tax positions in interest expense and penalties, if any, in operating expenses in the Company's consolidated income statements. In 2007, the Company recognized interest expense for uncertain tax positions of $2 million.

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

(Millions of Dollars)	
Balance at January 1, 2007	$12
Additions based on tax positions related to the current year	-
Additions based on tax positions of prior years	1
Reductions for tax positions of prior years	(1)
Balance at December 31, 2007	$12

The Company does not expect the total amounts of uncertain tax positions to significantly increase or decrease within the next 12 months.

Note L – 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, 2007 have been new shares.

In January 2006, Con Edison adopted SFAS No. 123(R), "Share-Based Payment" (SFAS No. 123(R)), applying the modified prospective approach. Pursuant to SFAS No. 123(R), 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 periods ended December 31, 2007, 2006 and 2005:

(Thousands of Dollars)	2007	2006	2005
Stock options	$44	$527	$-
Restricted stock units	(49)	2	601
Performance-based restricted stock	421	767	198
Total	$416	$1,296	$799

Stock Options

Stock options generally vest over a three-year period and have a term of ten years. Options are granted at an exercise price equal to the fair market value of a 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 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 in 2007. The weighted average fair values of options granted in 2006 and 2005 were $3.81 and $4.51 per share, respectively. These values were estimated at the date of grant using the Black-Scholes option pricing model with the following weighted-average assumptions:

	2006	2005
Risk-free interest rate	4.62%	3.95%
Expected life	4.6 years	4.6 years
Expected stock volatility	13.41%	19.00%
Expected dividend yield	5.06%	5.37%

The weighted average risk-free rate is calculated using the five-year U.S. Treasury securities rate on the grant date of each stock option and then weighted for the number of shares awarded. The expected life of the options is based on historical employee exercise behavior and post-vesting cancellations. The expected stock volatility is calculated using the quarterly closing prices of Con Edison stock over a period of five years, which approximates the expected term of the options. The expected dividend yield is calculated using the annualized dividend divided by the stock price on the date of grant.

A summary of changes in the status of stock options awarded to O&R employees as of December 31, 2007, 2006 and 2005 is as follows:

	Shares	Weighted Average Exercise Price
Outstanding at 12/31/04	465,000	40.139
Granted	105,000	43.031
Exercised	(32,000)	38.715
Forfeited	-	-
Outstanding at 12/31/05	538,000	40.788
Granted	124,000	45.599
Exercised	(47,150)	38.337
Forfeited	-	-
Outstanding at 12/31/06	614,850	$41.946
Granted	-	-
Exercised	(66,650)	39.313
Forfeited	-	-
Outstanding at 12/31/07	548,200	$42.266

The change in the fair value of all outstanding options from their grant dates to December 31, 2007 and 2006 (aggregate intrinsic value) for O&R were $4 million. The aggregate intrinsic value of options exercised in 2007 and 2006 were $0.7 million and $0.5 million, respectively, and the cash received by Con Edison for payment of the exercise price was $3 million and $2 million, respectively. The weighted average remaining contractual life of options outstanding is six years as of December 31, 2007.

The following table summarizes O&R employees' stock options outstanding at December 31, 2007 for each plan year:

Plan Year	Remaining Contractual Life	Options Outstanding	Weighted Average Exercise Price	Options Exercisable
2006	9	124,000	$45.599	-
2005	8	105,000	43.031	-
2004	7	85,000	43.760	85,000
2003	6	81,200	39.911	81,200
2002	5	87,000	42.510	87,000
2001	4	37,000	37.750	37,000
2000	3	29,000	32.500	29,000
Total		548,200	$42.266	319,200

The exercise prices of options awarded in 2006 and 2005 range from $43.50 to 46.88 and $42.18 to $43.72, respectively. The total expense to be recognized in future periods for the unvested stock options outstanding as of December 31, 2007 is $66 thousand for O&R.

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 SFAS No. 123(R), 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 three years 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. A senior officer of O&R was awarded restricted stock units in 2000 and 2002. The units, each of which represented the right to receive one share of Con Edison common stock, became fully vested in 2005 and the receipt of certain of these units was deferred by the officer until a future date. Pursuant to APB No. 25, O&R recognized compensation expense for the units, which was not material, over the vesting period. At December 31, 2007 and 2006, there were 36,200 and 35,000 units outstanding for O&R. The weighted average fair value as of the grant date of the outstanding units for December 31, 2007 and 2006 was $35.322 and $34.783

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, 2007 was $44 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 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 on the date of grant. 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:

	2007
Risk-free interest rate	2.91% - 4.00%
Expected term	3 years
Expected volatility	13.92%
Expected quarterly dividends	$0.58 - $0.595

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. Expected annual escalation of dividends is based on historical trends.

A summary of changes in the status of the Performance RSUs TSR portion during the period ended December 31, 2007 is as follows:

	Units	Weighted Average Fair Value*
Non-vested at 12/31/06	8,575	$18.58
Granted	12,725	46.18
Vested and Exercised	(1,470)	22.51
Forfeited	(2,205)	-
Non-vested at 12/31/07	17,625	$33.10

* Fair value is determined using the Monte Carlo simulation described above.

A summary of changes in the status of the Performance RSUs' EIP portion during the period ended December 31, 2007 is as follows:

	Units	Weighted Average Price
Non-vested at 12/31/06	8,575	$48.07
Granted	12,725	48.22
Vested and Exercised	(3,675)	48.85
Forfeited	-	-
Non-vested at 12/31/07	17,625	$48.85

The total expense to be recognized by O&R in future periods for unvested Performance RSUs outstanding as of December 31, 2007 is $0.9 million.

Stock Purchase Plan

Under the Con Edison Stock Purchase Plan, O&R contributes $1 for each $9 invested by its officers and 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 officers and 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 2007, 2006 and 2005, 633,647, 624,751 and 590,413 shares were purchased under the Stock Purchase Plan at a weighted average price of $47.70, $45.33 and $45.05 per share, respectively.

Note M – 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 SFAS No. 131, "Disclosures About Segments of an Enterprise and Related Information."

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, 2007 (Millions of Dollars)	Operating revenues	Depreciation and amortization	Income tax expense	Operating income	Interest charges	Total assets	Construction expenditures
Electric	$ 671	$27	$19	$57	$21	$1,271	$80
Gas	265	11	5	22	11	530	32
Other*	-	-	-	-	2	61	-
Total	$936	$38	$24	$79	$34	$1,862	$112

As of and for the Year Ended December 31, 2006 (Millions of Dollars)	Operating revenues	Depreciation and amortization	Income tax expense	Operating income	Interest charges	Total assets	Construction expenditures
Electric	$582	$25	$20	$ 53	$18	$1,230	$84
Gas	236	10	5	16	7	495	26
Other*	-	-	-	-	3	43	-
Total	$818	$35	$25	$69	$28	$1,768	$110

As of and for the Year Ended December 31, 2005 (Millions of Dollars)	Operating revenues	Depreciation and amortization	Income tax expense	Operating income	Interest charges	Total assets	Construction expenditures
Electric	$596	$ 25	$25	$57	$15	$1,082	$61
Gas	228	9	6	16	7	459	26
Other*	-	-	-	-	2	47	-
Total	$824	$34	$31	$73	$24	$1,588	$87

* Includes amounts related to Transition Funding.

Note N – Derivative Instruments and Hedging Activities

Derivative instruments and hedging activities are accounted for in accordance with SFAS No. 133, "Accounting for Derivative Instruments and Hedging Activities," as amended (SFAS No. 133). Under SFAS No. 133, derivatives are recognized on the balance sheet at fair value, unless an exception is available under the standard.

Energy Price Hedging

The Company hedges market price fluctuations associated with physical purchases and sales of electricity and natural gas by using derivative instruments including futures, forwards, basic swaps, or options. The fair values of these hedges at December 31, 2007 and 2006 were as follows:

(Millions of Dollars)	2007	2006
Fair value of net assets	$14	$(19)

The Company is permitted by its regulators to reflect in rates all reasonably incurred gains and losses on hedge instruments. See “Recoverable Energy Costs” in Note A.

Generally, 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.

Credit Exposure

The Company is exposed to credit risk related to transactions entered into primarily for the various energy 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 $27 million credit exposure in connection with energy supply and hedging activities, net of collateral and reserves, at December 31, 2007. The entire $27 million was with investment-grade counterparties.

Interest Rate Hedging

In 1992, the Company entered into a forward interest rate swap agreement to manage interest rate exposure associated with its $55 million of tax-exempt debt that matures in 2014. Under the agreement, the Company pays a counter-party a fixed amount determined based on a 6.09 percent per annum rate and the counter-party pays O&R a floating amount. Prior to February 20, 2008, the floating amount was determined based on the variable interest rate on the specific tax-exempt debt instrument it hedged. Effective February 20, 2008, the floating amount paid by the counter-party was determined based on a tax-affected LIBOR.

At December 31, 2007 and 2006, the swap agreement was accounted for as a cash flow hedge under SFAS No. 133. The fair values of this interest rate swap agreement at December 31, 2007 and 2006 were as follows:

(Millions of Dollars)	2007	2006
Fair value of interest rate swaps	$(11)	$(12)

As a cash flow hedge, any gain or loss on the swap agreement was recorded in OCI, to be reclassified to interest expense and included in earnings during the periods in which the hedged interest payments occur.

The following table presents selected information related to this cash flow hedge included in accumulated OCI at December 31, 2007:

(Millions of Dollars)	Accumulated Other Comprehensive Income/(Loss) Net of Tax	Portion Expected to be Reclassified to Earnings during the Next 12 Months
Interest Rate Swaps	$(6)	$(1)

Effective February 20, 2008, the swap agreement no longer satisfied the criteria for it to be accounted for as a cash flow hedge. As a result, in the first quarter of 2008, the mark-to-market loss on the swap agreement of approximately $8 million, net of taxes, will be reclassified from OCI and a regulatory asset will be established to reflect the expected recovery of the loss from the Company's customers.

Note O – Asset Retirement Obligations

In accordance with SFAS No. 143, "Accounting for Asset Retirement Obligations" (SFAS No. 143), companies are required to recognize a liability for legal obligations associated with the retirement of long-lived assets. The Company has not identified any such obligations and, accordingly, has not recognized any asset retirement obligation under SFAS No. 143.

The Company includes in depreciation the estimated removal costs, less salvage, for utility plant assets. In accordance with SFAS No. 143, future removal costs that do not represent legal asset retirement obligations are recorded as regulatory liabilities pursuant to SFAS No. 71. The related regulatory liabilities recorded for the Company were $61 million and $60 million in 2007 and 2006, respectively.

Note P – 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 PSC 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, 2007, 2006 and 2005 were as follows:

(Millions of Dollars)	2007	2006	2005
Cost of services provided	$17	$16	$14
Cost of services received	$30	$28	$25

In addition, Con Edison of New York and O&R have joint gas supply arrangements, in connection with which O&R purchased from Con Edison of New York $161 million, $149 million and $185 million of natural gas for the years ended December 31, 2007, 2006 and 2005, respectively. These amounts are net of the effect of related hedging transactions.

Con Edison of New York also hedges electricity purchases for O&R. Electric hedging transactions executed by Con Edison of New York on behalf of O&R resulted in a charge to purchase power of $5 million and $9 million for the years ended December 31, 2007 and 2006, respectively, and a credit to purchase power of $3 million for the year ended December 31, 2005.

At December 31, 2007 and 2006, O&R's net payable to Con Edison of New York associated with derivatives for energy price hedging was $4 million and $49 million, respectively. See Note N.

At December 31, 2007, the Company's receivable from Con Edison for income taxes was $2 million. At December 31, 2006, the receivable was immaterial. See Note A.

In December 2006, the FERC authorized Con Edison of New York to lend funds to O&R, for periods of not more than 12 months, in amounts not to exceed $200 million outstanding at any time, at prevailing market rates. In December 2007, Con Edison of New York loaned O&R $55 million, which was repaid in January 2008.

Note Q – New Financial Accounting Standards

In December 2007, the FASB issued Statement No. 160, "Noncontrolling Interests in Consolidated Financial Statements, an amendment of ARB No. 51" (SFAS No. 160), which is effective for financial statements issued for fiscal years beginning after December 15, 2008. This Statement requires ownership interests in subsidiaries held by parties other than the parent be clearly identified, labeled, and presented in the consolidated statement of financial position within equity, but separate from the parent's equity. It also requires the amount of consolidated net income attributable to the parent and to the non-controlling interest be clearly identified and presented on the face of the consolidated statement of income. The adoption of SFAS No. 160 is not expected to have a material impact on the Company's financial position, results of operations or liquidity.

In December 2007, the FASB issued Statement No. 141R, "Business Combinations" (SFAS No. 141R), which is effective for financial statements issued for fiscal years beginning after December 15, 2008. This Statement requires an acquiring entity to recognize all the assets acquired and liabilities assumed in a transaction at the acquisition-date fair value with limited exceptions. The adoption of SFAS No. 141R is not expected to have a material impact on the Company's financial position, results of operations or liquidity.

In November 2007, the FASB issued FSP No. SFAS 142-f, "Determination of the Useful Life of Intangible Assets." The guidance in this FSP would amend the factors used to determine the useful life of a recognized intangible asset under FASB Statement No. 142, "Goodwill and Other Intangible Assets." The guidance in this FSP becomes effective for fiscal years beginning after June 15, 2008, and interim periods within those fiscal years. Early adoption is prohibited. The Company is currently evaluating the impact of this FSP on its financial position, results of operations and liquidity.

In June 2007, the FASB issued Emerging Issues Task Force (EITF) Issue No. 07-3, "Accounting for Nonrefundable Advance Payments for Goods or Services to be used in Future Research and Development Activities." The EITF concluded that nonrefundable advance payments for future research and development activities should be deferred and capitalized. Such amounts should be recognized as an expense as the related goods are delivered or the related services are performed. If an entity does not expect the goods to be delivered or services to be rendered, the capitalized advance payment should be charged to expense. The guidance in this EITF becomes effective for fiscal years beginning after December 15, 2007. The Company does not expect this EITF to have a material effect on its financial position, results of operations or liquidity.

In June 2007, the FASB ratified the consensus reached by the EITF in Issue No. 06-11, "Accounting for Income Tax Benefits of Dividends on Share-Based Payment Awards," which is effective for fiscal years beginning after December 15, 2007. The EITF concluded that a realized income tax benefit from dividends or dividend equivalents that are charged to retained earnings and are paid to employees for equity classified as nonvested equity shares, nonvested equity share units, and outstanding equity share options should be recognized as an increase to additional paid-in capital. The amount recognized in additional paid-in capital for the realized income tax benefit from dividends on those awards should be included in the pool of excess tax benefits available to absorb tax deficiencies on share-based payment awards. The adoption of EITF No. 06-11 is not expected to have a material impact on the Company's financial position, results of operations or liquidity.

In May 2007, the FASB issued FSP No. FIN 48-1, "Definition of *Settlement* in FASB Interpretation No. 48, Accounting for Uncertainty in Income Taxes." The guidance in this FSP clarifies how an enterprise should determine whether a tax position is effectively settled for the purpose of recognizing previously unrecognized tax benefits. The guidance in this FSP became effective upon adoption of the FASB Interpretation No. 48, which the Company adopted in January 2007. See Note K. The application of this FSP did not have a material impact on the Company's financial position, results of operations or liquidity.

In April 2007, the FASB issued FSP No. 39-1, "Amendment of FASB Interpretation No. 39." This FSP permits a reporting entity to offset fair value amounts recognized for the right to reclaim cash collateral (a receivable) or the obligation to return cash collateral (a payable) against fair value amounts recognized for derivative instruments that have been offset provided that the receivable or payable arises from the same master netting arrangement with the same counterparty as the derivative instruments. The guidance in this FSP becomes effective for fiscal years beginning after November 15, 2007. The adoption of this FSP is not expected to have a material impact on the Company's financial position, results of operations or liquidity.

In February 2007, the FASB issued Statement No. 159, "The Fair Value Option for Financial Assets and Financial Liabilities - including an amendment of FASB Statement No. 115." This Statement permits entities to choose to measure many financial instruments and certain other items at fair value that are not currently required to be measured at fair value. The guidance in the Statement becomes effective for fiscal periods beginning after November 15, 2007. The Company has not elected the fair value option.

In September 2006, the FASB issued EITF Issue 06-4, "Accounting for Deferred Compensation and Postretirement Benefit Aspects of Endorsement Split Dollar Life Insurance Arrangements." This EITF requires employers to record a liability for future benefits for endorsement split-dollar life insurance arrangements that provide a postretirement benefit to an employee. The guidance in this EITF becomes effective for fiscal periods beginning after December 15, 2007. The Company does not expect this EITF to have a material impact on its financial statements, results of operations or liquidity.

In September 2006, the FASB issued Statement No. 157, "Fair Value Measurements." This Statement defines fair value, establishes a framework for measuring fair value and expands the disclosures about fair value measurements. It applies to other accounting pronouncements that require fair value measurements and, accordingly, does not require any new fair value measurements. The guidance in this Statement becomes effective for financial statements issued for fiscal years beginning after November 15, 2007. The Company has evaluated the impact of this Statement on its financial position, results of operations and liquidity. The application of this Statement will not impact the financial statements of the Company. It will, however, require additional disclosures for items that are measured at fair value.