Orange and Rockland Utilities, Inc.
2011 Annual Financial Statements and Notes

Financial Statements

Report of Independent Registered Public Accounting Firm

Consolidated Income Statement

Consolidated Statement of Cash Flows

Consolidated Balance Sheet

Consolidated Statement of Comprehensive Income

Consolidated Statement of Common Shareholder’s Equity

Consolidated Statement of Capitalization

Notes to Financial Statements

Report of Independent Auditors

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

In our opinion, the accompanying consolidated balance sheets and the related consolidated statements of capitalization, of income, of comprehensive income, of common shareholder's equity and of cash flows present fairly, in all material respects, the financial position of Orange and Rockland Utilities, Inc. and its subsidiaries (the Company) at December 31, 2011 and 2010, and the results of their operations and their cash flows for each of the three years in the period ended December 31, 2011 in conformity with accounting principles generally accepted in the United States of America. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits. We conducted our audits of these statements in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

PricewaterhouseCoopers LLP

PricewaterhouseCoopers LLP
March 9, 2012

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Orange and Rockland Utilities, Inc.

CONSOLIDATED INCOME STATEMENT

	For the Years Ended December 31,		
	2011	2010	2009
	(Millions of Dollars)		
OPERATING REVENUES			
Electric	$ 641	$ 692	$ 648
Gas	214	218	242
TOTAL OPERATING REVENUES	855	910	890
OPERATING EXPENSES			
Purchased power	267	335	328
Gas purchased for resale	87	99	136
Other operations and maintenance	284	275	247
Depreciation and amortization	48	44	42
Taxes, other than income taxes	55	49	45
TOTAL OPERATING EXPENSES	741	802	798
OPERATING INCOME	114	108	92
OTHER INCOME (DEDUCTIONS)			
Investment and other income	2	-	2
Allowance for equity funds used during construction	3	3	1
Other deductions	(1)	(1)	(1)
TOTAL OTHER INCOME (DEDUCTIONS)	4	2	2
INCOME BEFORE INTEREST AND INCOME TAX EXPENSE	118	110	94
INTEREST EXPENSE			
Interest on long-term debt	32	32	27
Other interest	3	5	2
Allowance for borrowed funds used during construction	(1)	(2)	(1)
NET INTEREST EXPENSE	34	35	28
INCOME BEFORE TAXES	84	75	66
INCOME TAX EXPENSE	31	26	23
NET INCOME	$ 53	$ 49	$ 43

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,		
	2011	2010	2009
	(Millions of Dollars)		
OPERATING ACTIVITIES			
Net income	$ 53	$ 49	$ 43
PRINCIPAL NON-CASH CHARGES/(CREDITS) TO INCOME			
Depreciation and amortization	48	44	42
Deferred income taxes	30	19	41
Other non-cash items (net)	(23)	17	1
CHANGES IN ASSETS AND LIABILITIES			
Accounts receivable - customers, less allowance for uncollectibles	13	(13)	29
Accounts receivable from affiliated companies	17	(17)	15
Materials and supplies, including gas in storage	(3)	4	30
Prepayments, other receivables and other current assets	15	20	(40)
Recoverable energy costs	12	6	(20)
Accounts payable	(3)	-	58
Accounts payable to affiliated companies	(21)	10	(32)
Pensions and retiree benefits	42	5	(13)
Superfund and environmental remediation costs (net)	1	4	4
Accrued taxes	5	-	-
Accrued interest	2	3	(5)
Deferred charges, noncurrent assets and other regulatory assets	(33)	(9)	25
Deferred credits and other regulatory liabilities	15	(3)	(8)
Other liabilities	5	7	(4)
NET CASH FLOWS FROM OPERATING ACTIVITIES	175	146	166
INVESTING ACTIVITIES			
Utility construction expenditures	(105)	(135)	(127)
Increase in restricted cash	-	(1)	-
Cost of removal less salvage	(4)	(4)	(5)
NET CASH FLOWS USED IN INVESTING ACTIVITIES	(109)	(140)	(132)
FINANCING ACTIVITIES			
Issuance of long-term debt	-	170	120
Retirement of long-term debt	(3)	(158)	(4)
Capital contribution by parent	-	-	30
Dividend to parent	(32)	(32)	(32)
Loan to affiliate	-	-	(113)
NET CASH FLOWS (USED IN)/FROM FINANCING ACTIVITIES	(35)	(20)	1
CASH AND TEMPORARY CASH INVESTMENTS:			
NET CHANGE FOR THE PERIOD	31	(14)	35
BALANCE AT BEGINNING OF PERIOD	38	52	17
BALANCE AT END OF PERIOD	$ 69	$ 38	$ 52
SUPPLEMENTAL DISCLOSURE OF CASH FLOW INFORMATION			
Cash paid/(refunded) during the period for:			
Interest	$31	$30	$33
Income taxes	($16)	$7	($12)

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

Orange and Rockland Utilities, Inc.
CONSOLIDATED BALANCE SHEET

	December 31, 2011	December 31, 2010
	(Millions of Dollars)	
ASSETS		
CURRENT ASSETS		
Cash and temporary cash investments	$ 69	$ 38
Accounts receivable - customers, less allowance for uncollectible accounts of $6 and $5 in 2011 and 2010, respectively	58	71
Accrued unbilled revenue	32	46
Other receivables, less allowance for uncollectible accounts of $1 in 2011 and 2010	9	11
Accounts receivable from affiliated companies	12	29
Gas in storage, at average cost	29	28
Materials and supplies, at average cost	11	9
Prepayments	21	17
Deferred tax assets - current	29	11
Regulatory assets	24	52
Other current assets	12	15
TOTAL CURRENT ASSETS	306	327
INVESTMENTS	10	10
UTILITY PLANT, AT ORIGINAL COST		
Electric	1,219	1,117
Gas	527	499
General	175	165
Total	1,921	1,781
Less: Accumulated depreciation	528	494
Net	1,393	1,287
Construction work in progress	76	113
NET UTILITY PLANT	1,469	1,400
DEFERRED CHARGES, REGULATORY ASSETS AND NONCURRENT ASSETS		
Regulatory assets	676	585
Other deferred charges and noncurrent assets	25	26
TOTAL DEFERRED CHARGES, REGULATORY ASSETS AND NONCURRENT ASSETS	701	611
TOTAL ASSETS	$ 2,486	$ 2,348

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

Orange and Rockland Utilities, Inc.

CONSOLIDATED BALANCE SHEET

	December 31, 2011	December 31, 2010
	(Millions of Dollars)	
LIABILITIES AND SHAREHOLDER'S EQUITY		
CURRENT LIABILITIES		
Long-term debt due within one year	$ 3	$ 3
Accounts payable	91	88
Accounts payable to affiliated companies	13	34
Customer deposits	13	13
Accrued interest	11	9
Accrued wages	9	9
Fair value of derivative liabilities	22	22
Regulatory liabilities	39	27
Other current liabilities	38	33
TOTAL CURRENT LIABILITIES	239	238
NONCURRENT LIABILITIES		
Provision for injuries and damages	7	7
Pensions and retiree benefits	498	387
Superfund and other environmental costs	116	120
Fair value of derivative liabilities	14	24
Other noncurrent liabilities	4	3
TOTAL NONCURRENT LIABILITIES	639	541
DEFERRED CREDITS AND REGULATORY LIABILITIES		
Deferred income taxes and investment tax credits	350	324
Regulatory liabilities	116	105
Other deferred credits	3	3
TOTAL DEFERRED CREDITS AND REGULATORY LIABILITIES	469	432
LONG-TERM DEBT (See Statement of Capitalization)	607	610
SHAREHOLDER'S EQUITY		
Common shareholder's equity (See Statement of Common Shareholder's Equity)	532	527
TOTAL SHAREHOLDER'S EQUITY	532	527
TOTAL LIABILITIES AND SHAREHOLDER'S EQUITY	$ 2,486	$ 2,348

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,		
	2011	2010	2009
	(Millions of Dollars)		
NET INCOME	$ 53	$ 49	$ 43
OTHER COMPREHENSIVE INCOME/(LOSS), NET OF TAXES			
Pension plan liability adjustments, net of $(11), $6 and $7 taxes in 2011, 2010 and 2009, respectively	(16)	4	10
TOTAL OTHER COMPREHENSIVE INCOME/(LOSS), NET OF TAXES	(16)	4	10
COMPREHENSIVE INCOME	$ 37	$ 53	$ 53

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, 2008	1,000	$ -	$ 274	$ 228	$ (47)	$ 455
Net Income				43		43
Common stock dividend to parent				(32)		(32)
Capital contribution by parent			30			30
Other comprehensive income					10	10
BALANCE AS OF DECEMBER 31, 2009	1,000	$ -	$ 304	$ 239	$ (37)	$ 506
Net Income				49		49
Common stock dividend to parent				(32)		(32)
Other comprehensive income					4	4
BALANCE AS OF DECEMBER 31, 2010	1,000	$ -	$ 304	$ 256	$ (33)	$ 527
Net Income				53		53
Common stock dividend to parent				(32)		(32)
Other comprehensive income					(16)	(16)
BALANCE AS OF DECEMBER 31, 2011	1,000	$ -	$ 304	$ 277	$ (49)	$ 532

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, 2011	Shares outstanding December 31, 2010	At December 31, 2011	At December 31, 2010
					(Millions of Dollars)	
TOTAL COMMON SHAREHOLDER'S EQUITY BEFORE ACCUMULATED OTHER COMPREHENSIVE LOSS			1,000	1,000	$ 581	$ 560
TOTAL ACCUMULATED OTHER COMPREHENSIVE LOSS, NET OF TAXES - PENSION PLAN LIABILITY ADJUSTMENTS					(49)	(33)
TOTAL COMMON SHAREHOLDER'S EQUITY (SEE STATEMENT OF COMMON SHAREHOLDER'S EQUITY)					$ 532	$ 527
LONG-TERM DEBT Maturity	Interest Rate	Series				
DEBENTURES:						
2015	5.30%	2005A			$ 40	$ 40
2015	2.50	2010A			55	55
2016	5.45	2006A			75	75
2018	6.15	2008A			50	50
2019	4.96	2009A			60	60
2027	6.50	1997F			80	80
2039	6.00	2009B			60	60
2040	5.50	2010B			115	115
TOTAL DEBENTURES					535	535
FIRST MORTGAGE BONDS:						
2018	7.07%	1998C			3	3
TOTAL FIRST MORTGAGE BONDS					3	3
TRANSITION BONDS:						
2019*	5.22%	2004-1			29	32
TOTAL TRANSITION BONDS					29	32
TAX-EXEMPT DEBT - Notes Issued to New York State Energy Research and Development Authority for Pollution Control Refunding Revenue Bonds**:						
2015	0.20%	1995			44	44
TOTAL TAX-EXEMPT DEBT					44	44
Unamortized debt discount					(1)	(1)
TOTAL					610	613
Less: long-term debt due within one year					3	3
TOTAL LONG-TERM DEBT					607	610
TOTAL CAPITALIZATION					$ 1,139	$ 1,137

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

** Rate reset weekly; December 30, 2011 rate shown.

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

Notes to the Financial Statements

General

These notes accompany and form an integral part of the financial statements of Orange and Rockland Utilities, Inc., a New York corporation, and its subsidiaries (the Company or O&R). The Company is a regulated utility, the equity of which is owned entirely by Consolidated Edison, Inc. (Con Edison). O&R has two regulated utility subsidiaries: Rockland Electric Company (RECO) and Pike County Light & Power Company (Pike). For the year ended December 31, 2011, 2010, and 2009, operating revenues for RECO and Pike were 24.3 percent and 0.9 percent, 25.6 percent and 0.8 percent, and 24.9 percent and 0.8 percent, respectively, of O&R's consolidated operating revenues. O&R, along with its regulated utility subsidiaries, provides electric service in southeastern New York and adjacent areas of northern New Jersey and eastern Pennsylvania and gas service in southeastern New York and adjacent areas of eastern Pennsylvania. RECO owns Rockland Electric Company Transition Funding LLC (Transition Funding), which was formed in 2004 in connection with the securitization of certain purchased power costs. See "Long-Term Debt" in Note C.

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

The Company has, pursuant to the accounting rules for subsequent events, evaluated events or transactions that occurred after December 31, 2011 through the posting on its website (March 9, 2012) of the Annual Financial Statements for potential recognition or disclosure in the consolidated financial statements.

Note A – Summary of Significant Accounting Policies

Principles of Consolidation

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

Accounting Policies

The accounting policies of the Company conform to accounting principles generally accepted in the United States of America. These accounting principles include the accounting rules for regulated operations and the accounting requirements of the FERC and the state public utility regulatory commissions having jurisdiction.

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

The Company's principal regulatory assets and liabilities are detailed in Note B. The Company is receiving or being credited with a return on all of its regulatory assets for which a cash outflow has been made, and is paying or being charged with a return on all of its regulatory liabilities for which a cash inflow has been received. The 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 N.

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 6.6 percent, 5.8 percent and 4.2 percent for 2011, 2010 and 2009, respectively.

The Company generally computes annual charges for depreciation using the straight-line method for financial statement purposes, with rates based on average service lives and net salvage factors. The average depreciation rate for the Company was 2.8 percent for 2011, 2010 and 2009.

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

At December 31, 2011 and 2010, the capitalized cost of the Company's utility plant, net of accumulated depreciation, was as follows:

(Millions of Dollars)	2011	2010
Electric		
Transmission	$178	$134
Distribution	680	642
Gas*	403	382
General	120	116
Held for future use	12	13
Construction work in progress	76	113
NET UTILITY PLANT	$1,469	$1,400

* Primarily distribution.

Under O&R's current rate plans, the aggregate annual depreciation allowance in effect at December 31, 2011 was $43 million.

Impairments

In accordance with the accounting rules for impairment or disposal of long-lived assets, the Company evaluates the impairment of long-lived assets, based on projections of undiscounted future cash flows, whenever events or changes in circumstances indicate that the carrying amounts of such assets may not be recoverable. In the event an evaluation indicates that such cash flows cannot be expected to be sufficient to fully recover the assets, the assets are written down to their estimated fair value.

Revenues

The Company recognizes revenues for energy service on a monthly billing cycle basis. The Company generally defers over a 12-month period net interruptible gas revenues, other than those authorized by the NYSPSC to be retained by the Company, for refund to firm gas sales and transportation customers. The Company accrues revenues at the end of each month for estimated energy service not yet billed to customers. Unbilled revenues included in O&R's balance sheet at December 31, 2011 and 2010 were $32 million and $46 million, respectively.

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

O&R and Pike are required to record gross receipts tax and RECO is required to record transitional energy facilities assessment (TEFA) tax as revenues and expenses on a gross income statement presentation basis (i.e., included in both revenue and expense). The recovery of these taxes is included in the revenue requirement within each of the respective approved rate plans. O&R and Pike recorded $8.6 million and $0.3 million, $7.8 million and $0.3 million, and $6.7 million and $0.3 million, of gross receipts tax in 2011, 2010, and 2009, respectively. RECO recorded $6.3 million, $6.4 million and $6.1 million in TEFA tax in 2011, 2010 and 2009, respectively.

Recoverable Energy Costs

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

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

RECO purchases electric energy under a competitive bidding process supervised by the NJBPU for contracts ranging from one to three years. For RECO, approximately 90 percent of the energy supply is covered by fixed price contracts ranging from one to three years that are competitively bid through the NJBPU auction process and provided through the Pennsylvania-Jersey-Maryland (PJM) Independent System Operator. Basic Generation Service rates are adjusted to conform to contracted prices when new contracts take effect and differences between actual monthly costs and revenues are reconciled and charged or credited to customers on a two-month lag.

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

New York Independent System Operator

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

Temporary Cash Investments

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

Investments

Investments are recorded at cash surrender value and include the supplemental retirement income plan's corporate-owned life insurance assets.

Pension and Other Postretirement Benefits

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

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

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

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

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

Federal Income Tax

In accordance with the accounting rules for income taxes, the Company has recorded an accumulated deferred federal income tax liability for temporary differences between the book and tax basis of assets and liabilities at current tax rates. In accordance with rate agreements, O&R has recovered amounts from customers for a portion of the tax liability it will pay in the future as a result of the reversal or "turn-around" of these temporary differences. As to the remaining tax liability, in accordance with the accounting rules for regulated operations, the Company has established regulatory assets for the net revenue requirements to be recovered from customers for the related future tax expense. See Notes B and I. In 1993, the NYSPSC issued a Policy Statement approving accounting procedures consistent with accounting rules for income taxes and providing assurances that these future increases in taxes will be recoverable in rates. See Note I.

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

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

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

State Income Tax

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

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

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

Reclassification

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

Estimates

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

Note B – Regulatory Matters

Rate Agreements

Electric

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

The Joint Proposal reflected the following major items:

- an annual return on common equity of 9.4 percent;

- most of any actual earnings above a 10.2 percent return on equity (based on actual average common equity ratio, subject to a 50 percent maximum) were to be applied to reduce regulatory assets for pension and other postretirement benefit expenses (the Company did not reduce regulatory assets under this provision in 2011, 2010 or 2009);

- deferral as a regulatory asset or regulatory liability, as the case may be, of the difference between actual pension and other postretirement benefit expenses, environmental remediation expenses, property taxes, tax-exempt debt costs and certain other expenses and amounts for those expenses reflected in rates (the Company deferred recognition of $0.3 million of expenses, $0.7 million of revenue and $3 million of expenses under this provision in 2011, 2010 and 2009, respectively);

- deferral as a regulatory liability of the revenue requirement impact (i.e., return on investment, depreciation and income taxes) of the amount, if any, by which actual transmission and distribution related capital expenditures was less than amounts reflected in rates (the Company deferred $7 million, $12 million, and $8 million of revenues under this provision in 2011, 2010 and 2009, respectively);

- deferral as a regulatory asset of increases, if any, in certain expenses above a 4 percent annual inflation rate, but only if the actual annual return on common equity is less than 9.4 percent (the Company did not defer any expenses under this provision in 2011, 2010 or 2009);

- potential negative earnings adjustments of up to $3 million annually if certain customer service and system reliability performance targets are not met (the Company met the performance targets in 2011 and 2009; the Company reduced revenues by $1 million under this provision in 2010);

- implementation of a revenue decoupling mechanism under which actual energy delivery revenues was compared, on a periodic basis, with the authorized delivery revenues with the difference accrued, with interest, for refund to, or recovery from, customers, as applicable (the Company accrued $3.3 million, $5.1 million, and $12.5 million of revenues pursuant to this provision in 2011, 2010 and 2009, respectively);

- continuation of the rate provisions pursuant to which the Company recovered its purchased power costs from customers; and

- withdrawal of the litigation O&R commenced seeking to annul the NYSPSC's March and October 2007 orders relating to O&R's electric rates.

In June 2011, the NYSPSC adopted an order granting O&R an electric rate increase, effective July 1, 2011, of $26.6 million. The NYSPSC ruling reflects the following major items:

- a weighted average cost of capital of 7.22 percent, reflecting:
    - a return on common equity of 9.2 percent, assuming achievement by the Company of $825,000 of austerity measures;
    - cost of long-term debt of 5.50 percent; and
    - common equity ratio of 48 percent.
- continuation of a revenue decoupling mechanism;

- a provision for reconciliation of certain differences in actual average net utility plant to the amount reflected in rates ($718 million) and continuation of rate provisions under which pension and other postretirement benefit expenses, environmental remediation expenses, tax-exempt debt costs and certain other expenses are reconciled to amounts for those expenses reflected in rates;

- continuation of the rate provisions pursuant to which the Company recovers its purchased power costs from customers;

- discontinuation of the provisions under which property taxes were reconciled to amounts reflected in rates;
- discontinuation of the inclusion in rates of funding for the Company's annual incentive plan for non-officer management employees;
- continuation of provisions for potential operations penalties of up to $3 million annually if certain customer service and system reliability performance targets are not met (in 2011, O&R did not recognize any operations penalties under these provisions or the corresponding provisions of the Joint Proposal discussed above); and
- O&R is directed to produce a report detailing its implementation plans for the recommendations made in connection with the NYSPSC's management audit of Con Edison's other utility subsidiaries, Consolidated Edison Company of New York (CECONY), with a forecast of costs to achieve and expected savings.

On February 24, 2012, O&R, the staff of the NYSPSC and the Utility Intervention Unit of New York State's Division of Consumer Protection entered into a Joint Proposal with respect to the Company's rates for electric delivery service rendered in New York. The Joint Proposal, which is subject to NYSPSC approval, covers the three-year period from July 2012 through June 2015. The Joint Proposal provides for electric base rate increases of $19.4 million, $8.8 million and $15.2 million, effective July 2012, 2013 and 2014, respectively, which can be implemented, at the NYSPSC's option, with increases of $15.2 million effective July 2012 and 2013 and an increase of $13.1 million, together with a surcharge of $2.1 million, effective July 2014. The Joint Proposal reflects the following major items:

- a weighted average cost of capital of 7.61 percent, 7.65 percent and 7.48 percent for the rate years ending June 30, 2013, 2014 and 2015, respectively, reflecting:
  - a return on common equity of 9.4 percent, 9.5 percent and 9.6 percent for the rate years ending June 30, 2013, 2014 and 2015, respectively;
  - cost of long-term debt of 6.07 percent for each of the rate years ending June 30, 2013 and 2014 and 5.64 percent for the rate year ending June 30 2015;
  - common equity ratio of 48 percent for each of the rate years ending June 30, 2013, 2014 and 2015; and
  - average rate base of $671 million, $708 million and $759 million for the rate years ending June 30, 2013, 2014 and 2015, respectively;
- sharing with electric customers of any actual earnings, excluding the effects of any penalties and certain other items, above specified percentage returns on common equity (based on the actual average common equity ratio, subject to a 50 percent maximum):

  - the Company will allocate to customers the revenue requirement equivalent of 50 percent, 75 percent and 90 percent of any such earnings for each rate year in excess of 80 basis points, 180 basis points and 280 basis points, respectively, above the return on common equity for that rate year indicated above;
  - if such earnings for a rate year are less than 80 basis points above the return on common equity for that rate year indicated above, the shortfall will be deducted from the calculation of such earnings for the other rate years;
  - the earnings sharing allocation between the Company and customers will be done on a cumulative at the end of rate year three; and
  - the customers' share will be deferred as a regulatory liability, and up to 50 percent of the Company's share will be applied to reduce certain regulatory assets;

- continuation of a revenue decoupling mechanism;

- continuation of a provision which defers as a regulatory liability for the benefit of customers or, subject to certain limitations, a regulatory asset for recovery from customers, as the case may be, the revenue requirement impact of the amount by which actual average net utility plant for each rate year is different than the average net utility plant reflected in rates ($678 million, $704 million and $753 million for the rate years ending June 30, 2013, 2014 and 2015, respectively);

- continuation of rate provisions under which pension and other post-retirement benefit expenses, environmental remediation expenses, tax-exempt debt costs and certain other expenses are reconciled to amounts for those expenses reflected in rates;

- continuation of the rate provisions pursuant to which the Company recovers its purchased power costs from customers;

- provisions under which property taxes are reconciled to amounts reflected in rates;

- inclusion in rates of partial funding for the Company's annual incentive plan for non-officer management employees; and

- continuation of provisions for potential operations penalties of up to $3 million annually if certain customer service and system reliability performance targets are not met.

In March 2007, the New Jersey Board of Public Utilities (NJBPU) approved a three-year electric base rate plan for RECO, O&R's New Jersey regulated utility subsidiary that went into effect on April 1, 2007. The plan provided for

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

In May 2010, RECO, the Division of Rate Counsel, Staff of the NJBPU and certain other parties entered into a stipulation of settlement with respect to the company's August 2009 request to increase the rates that it can charge its customers for electric delivery service. The stipulation, which was approved by the Board of the NJBPU, provided for an electric rate increase, effective May 17, 2010, of $9.8 million. The stipulation reflected a return on common equity of 10.3 percent and a common equity ratio of approximately 50 percent. The stipulation continued current provisions with respect to recovery from customers of the cost of purchased power and did not provide for reconciliation of actual expenses to amounts reflected in electric rates for pension and other postretirement benefit costs.

Gas

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

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

Earnings attributable to its gas business excluding any revenue reductions (O&R Adjusted Earnings) in excess of an 11 percent annual return on common equity (based upon the actual average common equity ratio, subject to a maximum 50 percent of capitalization) were to be allocated as follows: above an 11 percent return were to be used to offset up to one-half of any regulatory asset to be recorded in that year resulting from the cost reconciliations (discussed in the preceding paragraph). One-half of any remaining O&R Adjusted Earnings

between 11 and 12 percent return were to be retained by the Company, with the balance deferred for the benefit of customers. Thirty-five percent of any remaining O&R Adjusted Earnings between a 12 and 14 percent return were to be retained by the Company, with the balance deferred for the benefit of customers. Any remaining O&R Adjusted Earnings above a 14 percent return were to be deferred for the benefit of customers. For purposes of these earnings sharing provisions, if in any rate year O&R Adjusted Earnings was less than 11 percent, the shortfall was deducted from O&R Adjusted Earnings for the other rate years. The earnings sharing thresholds were to each be reduced by 20 basis points if certain objectives relating to the Company's retail choice program are not met. O&R adjusted earnings were not in excess of the 11 percent target return on equity for the rate years ended October 31, 2009, and 2008.

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

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

- an annual return on common equity of 10.4 percent;

- most of any actual earnings above an 11.4 percent annual return on common equity (based upon the actual average common equity ratio, subject to a maximum 50 percent of capitalization) are to be applied to reduce regulatory assets (in 2011 and 2010, the Company did not defer any revenues under this provision);

- deferral as a regulatory asset or liability, as the case may be, of differences between the actual level of certain expenses, including expenses for pension and other postretirement benefits, environmental remediation, property taxes and taxable and tax-exempt long-term debt, and amounts for those expenses reflected in rates (in 2011 and 2010, the Company deferred $2.9 million and $3.1 million, respectively, of expenses under this provision);

- deferral as a regulatory liability of the revenue requirement impact (i.e., return on investment, depreciation and income taxes) of the amount, if any, by which average gas net plant balances are less than balances reflected in rates (in 2011 and 2010, the Company deferred of $1 million of expenses and $1.5 million of revenues , respectively, under this provision);

- deferral as a regulatory asset of increases, if any over the course of the rate plan, in certain expenses above a 4 percent annual inflation rate, but only if the actual annual return on common equity is less than 10.4 percent (in 2011 and 2010, the Company did not defer any revenues under this provision);

- implementation of a revenue decoupling mechanism (in 2011 and 2010, the Company accrued $2.8 million and $0.8 million, respectively, of revenues under this provision);

- continuation of the provisions pursuant to which the Company recovers its cost of purchasing gas and the provisions pursuant to which the effects of weather on gas income are moderated; and

- potential negative earnings adjustments of up to $1.4 million annually if certain operations and customer service requirements are not met (in 2011 and 2010, the Company did not have any potential negative earnings adjustments under this provision).

Other Regulatory Matters

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

Regulatory Assets and Liabilities

Regulatory assets and liabilities at December 31, 2011 and 2010 were comprised of the following items:

(Millions of Dollars)	2011	2010
Regulatory assets		
Unrecognized pension and other postretirement costs	$298	$219
Environmental remediation costs	117	122
Future federal income tax	74	78
Deferred storm costs	48	14
Transition bond charges	44	48
Pension and other postretirement benefits deferrals	41	49
Deferred derivative losses – long term	16	26
Surcharge for New York State assessment	8	9
Other	30	20
Regulatory assets	676	585
Deferred derivative losses - current	24	39
Recoverable energy costs - current	-	13
Total regulatory assets	$700	$637
Regulatory liabilities		
Allowance for cost of removal less salvage	$76	$72
Carrying charges on transmission and distribution net plant	24	23
Other	16	10
Regulatory liabilities	116	105
Refundable Energy Cost – current	39	26
Deferred derivative gains – current	-	1
Total regulatory liabilities	$155	$132

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

Note C – Capitalization

Common Stock

At December 31, 2011 and 2010, all of the outstanding common stock of the Company was owned by Con Edison. In accordance with NYSPSC requirements, the dividends that the Company generally may pay to Con Edison are limited to not more than 100 percent of its income available for dividends calculated on a two-year rolling average basis. Excluded from the calculation of "income available for dividends" are non-cash charges to income resulting from accounting changes or charges to income resulting from significant unanticipated events. The restriction also does not apply to dividends paid in order to transfer to Con Edison proceeds from major transactions, such as asset sales, or to dividends reducing the Company's equity ratio to a level appropriate to its business risk.

Long-Term Debt

Long-term debt maturing in the period 2012-2016 is as follows:

(Millions of Dollars)	
2012	$3
2013	3
2014	4
2015	142
2016	79

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

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

	December 31,			
	2011		2010	
(Millions of Dollars)	Carrying Amount	Fair Value	Carrying Amount	Fair Value
Long-Term Debt (including current portion)	$610	$715	$613	$666

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

At December 31, 2011 and 2010, long-term debt of the Company included $3 million of mortgage bonds, collateralized by substantially all utility plant and other physical property of Pike. Long-term debt also included $29 million and $32 million at December 31, 2011 and 2010, respectively, of Transition Bonds issued by Transition Funding, in July 2004. The proceeds from the Transition Bonds were used to purchase from RECO the right to be paid a Transition Bond Charge and associated tax charges by its customers relating to previously deferred purchased power costs for which the NJBPU had authorized recovery.

Significant Debt Covenants

There are no significant debt covenants under the financing arrangements for the debentures of O&R, other than obligations to pay principal and interest when due and covenants not to consolidate with or merge into any other corporation unless certain conditions are met, and no cross default provisions. The tax-exempt financing arrangements of the Company are subject to these covenants and the covenants discussed below. The Company believes that it was in compliance with its significant debt covenants at December 31, 2011.

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

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

Note D – Short-Term Borrowing

In October 2011, O&R, along with Con Edison and CECONY, entered into a Credit Agreement (Credit Agreement) under which banks are committed to provide loans and letters of credit on a revolving credit basis, and terminated an Amended and Restated Credit Agreement (Prior Agreement) that was to expire in June 2012. Under the Credit Agreement, which expires in October 2016, there is a maximum of $200 million available to O&R (subject to increase to $250 million if the necessary regulatory approvals are requested and obtained). The Credit Agreement supports the Company's commercial paper program. The Company has not borrowed under the Credit Agreement.

The banks' commitments under the Credit Agreement are subject to certain conditions, including that there be no event of default. The commitments are not subject to maintenance of credit rating levels or the absence of a material adverse change. Upon a change of control of, or upon an event of default by the Company, the banks may terminate their commitments with respect to the Company, declare any amounts owed by the Company under the Credit Agreement immediately due and payable and require the Company to provide cash collateral relating to the letters of credit issued for it under the Credit Agreement. Events of default include the exceeding at any time of a ratio of consolidated debt to consolidated total capital of 0.65 to 1 (at December 31, 2011 this ratio was 0.52 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 the Company, following any applicable notice period, to meet certain other customary covenants. Interest and fees charged for the revolving credit facilities and any loans made or letters of credit issued under the Credit Agreement reflect the Company's credit ratings.

At December 31, 2011 and 2010, O&R had no commercial paper outstanding. At December 31, 2011 and 2010, $23 million and $37 million of letters of credit, respectively, and no other borrowings were outstanding for O&R under the Credit Agreement and Prior Credit Agreement.

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

Note E – Pension Benefits

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

Net Periodic Benefit Cost

The components of the Company's net periodic benefit costs for 2011, 2010 and 2009 were as follows:

(Millions of Dollars)	2011	2010	2009
Service cost – including administrative expenses	$13	$11	$10
Interest cost on projected benefit obligation	35	35	34
Expected return on plan assets	(35)	(33)	(32)
Amortization of net actuarial loss	29	24	27
Amortization of prior service costs	2	2	1
NET PERIODIC BENEFIT COST	$44	$39	$40
Cost capitalized	(13)	(11)	(11)
Cost charged/(deferred)	3	(2)	(6)
Cost charged to operating expenses	$34	$26	$23

Funded Status

The funded status at December 31, 2011, 2010 and 2009 was as follows:

(Millions of Dollars)	2011	2010	2009
CHANGE IN PROJECTED BENEFIT OBLIGATION			
Projected benefit obligation at beginning of year	$651	$602	$586
Service cost – excluding administrative expenses	12	11	10
Interest cost on projected benefit obligation	36	35	34
Plan amendments	-	6	5
Net actuarial loss	83	29	1
Benefits paid	(34)	(32)	(34)
PROJECTED BENEFIT OBLIGATION AT END OF YEAR	$748	$651	$602
CHANGE IN PLAN ASSETS			
Fair value of plan assets at beginning of year	$377	$330	$271
Actual return on plan assets	3	41	54
Employer contributions	44	39	40
Benefits paid	(34)	(32)	(34)
Administrative expenses	(1)	(1)	(1)
FAIR VALUE OF PLAN ASSETS AT END OF YEAR	$389	$377	$330
FUNDED STATUS	$(359)	$(274)	$(272)
Unrecognized net loss	285	198	201
Unrecognized prior service costs	15	16	12
Accumulated benefit obligation	715	621	580

The increase in the pension plan's projected benefit obligation was a primary driver in the increased pension liability at O&R of $85 million compared with December 31, 2010. This also resulted in an increase to regulatory assets of $64 million for unrecognized net losses and unrecognized prior service costs associated with O&R's New York utility business consistent with the accounting rules for regulated operations, and a debit to OCI of $13 million (net of taxes) for the unrecognized net losses and unrecognized prior service costs associated with RECO and Pike.

A portion of the estimated net loss and prior service cost for the pension plan, equal to $38 million and $2 million, respectively, will be amortized from accumulated OCI and the regulatory asset into net periodic benefit cost over the next year for O&R.

At December 31, 2011 and 2010, the Company's investments include $9 million and $10 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 $37 million and $34 million as of December 31, 2011 and 2010.

Assumptions

The actuarial assumptions were as follows:

	2011	2010	2009
Weighted-average assumptions used to determine benefit obligations at December 31:			
Discount rate	4.70%	5.60%	6.05%
Rate of compensation increase	4.25%	4.25%	4.00%
Weighted-average assumptions used to determine net periodic benefit cost for the years ended December 31:			
Discount rate	5.60%	6.05%	5.75%
Expected return on plan assets	8.50%	8.50%	8.50%
Rate of compensation increase	4.25%	4.00%	4.00%

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

Discount Rate Assumption

To determine the assumed discount rate, the Company uses a model that produces a yield curve based on yields on selected highly rated (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 $50 million. The spot rates defined by the yield curve and the plan's projected benefit payments are used to develop a weighted average discount rate.

Expected Benefit Payments

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

(Millions of Dollars)	2012	2013	2014	2015	2016	2017-2021
O&R	$36	$38	$39	$41	$43	$234

Expected Contributions

Based on estimates as of December 31, 2011, O&R expects to make contributions to the pension plan during 2012 of $52 million. O&R's policy is to fund its accounting cost to the extent tax deductible.

Plan Assets

The asset allocations for the pension plan at the end of 2011, 2010, and 2009, and the target allocation for 2012 are as follows:

ASSET CATEGORY	Target Allocation Range 2012	Plan Assets at December 31, 2011	2010	2009
Equity Securities	55%-65%	61%	67%	67%
Debt Securities	27%-33%	32%	28%	28%
Real Estate	8%-12%	7%	5%	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 participants and beneficiaries and payment of plan expenses.

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

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

The strategic asset allocation is intended to meet the objectives of the pension plan by diversifying its funds across asset classes, investment styles and fund managers. An asset/liability study typically is conducted every few years to determine whether the current strategic asset allocation continues to represent the appropriate balance of expected risk and reward for the plan to meet expected liabilities. Each study considers the investment risk of the asset allocation and determines the optimal asset allocation for the plan. The target asset allocation for 2012 reflects the results of such a study conducted in 2011.

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

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

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

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

The fair values of the pension plan assets at December 31, 2011 by asset category are as follows:

(Millions of Dollars)	Level 1	Level 2	Level 3	Total
U.S. Equity (a)	$2,506	$-	$-	$2,506
International Equity (b)	1,904	637	-	2,541
U.S. Government Issues (c)	-	1,618	-	1,618
Corporate Bonds (d)	-	668	94	762
Structured Assets (e)	-	-	13	13
Other Fixed Income (f)	-	67	29	96
Real Estate (g)	-	-	572	572
Cash and Cash Equivalents (h)	13	395	-	408
Total investments	$4,423	$3,385	$708	$8,516
Funds for retiree health benefits (i)	(174)	(134)	(28)	(336)
Investments (excluding funds for retiree health benefits)	$4,249	$3,251	$680	$8,180
Pending activities (j)				(380)
Total fair value of plan net assets				$7,800

(a) U.S. Equity includes both actively- and passively-managed assets with investments in domestic equity index funds and actively-managed small-capitalization equities.
(b) International Equity includes international equity index funds and actively-managed international equities.
(c) U.S. Government Issues include agency and treasury securities.
(d) Corporate Bonds classified as Level 3 include 144A illiquid securities.
(e) Structured Assets are measured using broker quotes and investment manager proprietary models and include commercial-mortgage-backed securities and collateralized mortgage obligations.
(f) Other Fixed Income includes municipal bonds, sovereign debt and regional governments.
(g) Real Estate investments include real estate funds based on appraised values that are broadly diversified by geography and property type.
(h) Cash and Cash Equivalents include short term investments, money markets, foreign currency and cash collateral.
(i) Con Edison and its subsidiaries set aside funds for retiree health benefits through a separate account within the pension trust, as permitted under Section 401(h) of the Internal Revenue Code of 1986, as amended. In accordance with the Code, the plan's investments in the 401(h) account may not be used for, or diverted to, any purpose other than providing health benefits for retirees. The net assets held in the 401(h) account are calculated based on a pro-rata percentage allocation of the net assets in the pension plan. The related obligations for health benefits are not included in the pension plan's obligations and are included in Con Edison and its subsidiaries' other postretirement benefit obligation. See Note F.
(j) Pending activities include security purchases and sales that have not settled, interest and dividends that have not been received and reflects adjustments for available estimates at year end.

The table below provides a reconciliation of the beginning and ending net balances for assets at December 31, 2011 classified as Level 3 in the fair value hierarchy.

(Millions of Dollars)	Beginning Balance as of January 1, 2011	Assets Still Held at Reporting Date – Unrealized Gains/ (Losses)	Assets Sold During the Period – Realized Gains	Purchases Sales and Settlements	Ending Balance as of December 31, 2011
Corporate Bonds	$129	$(9)	$11	$(37)	$94
Structured Assets	87	(1)	2	(75)	13
Other Fixed Income	66	(1)	3	(39)	29
Real Estate	398	65	-	109	572
Total investments	$680	$54	$16	$(42)	$708
Funds for retiree health benefits	(30)	3	1	(2)	(28)
Investments (excluding funds for retiree health benefits)	$650	$57	$17	$(44)	$680

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

(Millions of Dollars)	Level 1	Level 2	Level 3	Total
U.S. Equity (a)	$3,935	$-	$-	$3,935
International Equity (b)	1,249	234	-	1,483
U.S. Government Issues (c)	-	1,300	-	1,300
Corporate Bonds (d)	-	571	129	700
Structured Assets (e)	-	-	87	87
Other Fixed Income (f)	-	31	66	97
Real Estate (g)	-	-	398	398
Cash and Cash Equivalents (h)	3	232	-	235
Total investments	$5,187	$2,368	$680	$8,235
Funds for retiree health benefits (i)	(226)	(103)	(30)	(359)
Investments (excluding funds for retiree health benefits)	$4,961	$2,265	$650	$7,876
Pending activities (j)				(155)
Total fair value of plan net assets				$7,721

(a) U.S. Equity includes both actively- and passively-managed assets with investments in domestic equity index funds, actively-managed small-capitalization equities, rights and warrants.
(b) International Equity includes international equity index funds, actively-managed international equities, rights and warrants.
(c) U.S. Government Issues include agency and treasury securities.
(d) Corporate Bonds held in institutional mutual funds which are measured at Net Asset Value (NAV) are classified as Level 3.
(e) Structured Assets are measured using broker quotes and investment manager proprietary models and include commercial-mortgage-backed securities, collateralized mortgage obligations and asset-backed securities.
(f) Other Fixed Income includes emerging market debt valued using broker quotes, municipal bonds, sovereign debt, regional governments and government agencies.
(g) Real Estate investments include real estate funds based on appraised values that are broadly diversified by geography and property type.
(h) Cash and Cash Equivalents include short term investments, money markets and foreign currency.
(i) Con Edison and its subsidiaries set aside funds for retiree health benefits through a separate account within the pension trust, as permitted under Section 401(h) of the Internal Revenue Code of 1986, as amended. In accordance with the Code, the plan's investments in the 401(h) account may not be used for, or diverted to, any purpose other than providing health benefits for retirees. The net assets held in the 401(h) account are calculated based on a pro-rata percentage allocation of the net assets in the pension plan. The related obligations for health benefits are not included in the pension plan's obligations and are included in Con Edison and its subsidiaries other postretirement benefit obligation. See Note F.
(j) Pending activities include security purchases and sales that have not settled, interest and dividends that have not been received and reflects adjustments for available estimates at year end.

The table below provides a reconciliation of the beginning and ending net balances for assets at December 31, 2010 classified as Level 3 in the fair value hierarchy.

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

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

(Millions of Dollars)	For the Years Ended December 31 2011	2010	2009
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.

Net Periodic Benefit Cost

The components of the Company's net periodic postretirement benefit costs for 2011, 2010 and 2009 were as follows:

(Millions of Dollars)	2011	2010	2009
Service cost	$5	$4	$4
Interest cost on accumulated other postretirement benefit obligation	11	11	11
Expected return on plan assets	(9)	(8)	(8)
Amortization of net actuarial loss	8	7	9
Amortization of prior service costs	2	2	2
NET PERIODIC POSTRETIREMENT BENEFIT COST	$17	$16	$18
Cost capitalized	(6)	(6)	(6)
Cost charged/(deferred)	2	3	2
Cost charged to operating expenses	$13	$13	$14

Funded Status

The funded status of the programs at December 31, 2011, 2010 and 2009 were as follows:

Notes to the Financial Statements - Continued

(Millions of Dollars)	2011	2010	2009
CHANGE IN BENEFIT OBLIGATION			
Benefit obligation at beginning of year	$215	$201	$206
Service cost	5	4	4
Interest cost on accumulated postretirement benefit obligation	11	11	11
Net actuarial loss/(gain)	23	9	(11)
Benefits paid and administrative expenses	(12)	(12)	(11)
Participant contributions	1	1	1
Medicare prescription subsidy	1	1	1
BENEFIT OBLIGATION AT END OF YEAR	$244	$215	$201
CHANGE IN PLAN ASSETS			
Fair value of plan assets at beginning of year	$102	$88	$68
Actual return on plan assets	1	12	15
Employer contributions	11	11	14
Benefits paid	(8)	(9)	(9)
FAIR VALUE OF PLAN ASSETS AT END OF YEAR	$106	$102	$88
FUNDED STATUS	(138)	$(113)	$(113)
Unrecognized net loss	66	43	45
Unrecognized prior service costs	14	16	17

The increase in the value of other postretirement benefit plan assets, offset by the increase in the OPEB benefit obligation resulted in an increase to the liability for other postretirement benefits of $26 million at O&R compared with December 31, 2010. This also resulted in an increase to regulatory assets of $15 million for unrecognized net losses and unrecognized prior service costs associated with O&R consistent with accounting rules for regulated operations, and a debit to OCI of $3 million (net of taxes) for the unrecognized net losses and unrecognized prior service costs associated with RECO and Pike.

The estimated net loss and prior service costs for the other postretirement benefits, equal to $11 million and $1 million, respectively, will be amortized from accumulated OCI and the regulatory asset into net periodic benefit cost over the next year for O&R.

Assumptions

The actuarial assumptions were as follows:

	2011	2010	2009
Weighted-average assumptions used to determine benefit obligations at December 31:			
Discount Rate	4.55%	5.40%	5.95%
Weighted-average assumptions used to determine net periodic benefit cost for the years ended December 31:			
Discount Rate	5.40%	5.95%	5.75%
Expected Return on Plan Assets			
Tax-Exempt	8.50%	8.50%	8.50%
Taxable	8.00%	8.00%	8.00%

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

The health care cost trend rate used to determine net periodic benefit cost for the year ended December 31, 2011 was 6.00 percent, which is assumed to decrease gradually to 4.50 percent by 2014 and remain at that level thereafter. The health care cost trend rate used to determine benefit obligations as of December 31, 2011 was 6.00 percent, which is assumed to decrease gradually to 4.50 percent by 2018 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, 2011:

(Millions of Dollars)	1-Percentage-Point Increase	1-Percentage-Point Decrease
Effect on accumulated other postretirement benefit obligation	$33	$(27)
Effect on service cost and interest cost components for 2010	3	(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)	2012	2013	2014	2015	2016	2017-2021
Gross Benefit Payments	$12	$13	$13	$14	$14	$81
Medicare Prescription Benefit Receipts	1	1	1	1	2	9

Expected Contributions

Based on estimates as of December 31, 2011, O&R expects to make a contribution of $14 million to the other postretirement benefit plans in 2012.

Plan Assets

The asset allocations for O&R's other postretirement benefit plans at the end of 2011, 2010 and 2009, and the target allocation for 2012 are as follows:

ASSET CATEGORY	Target Allocation Range 2012	Plan Assets at December 31 2011	2010	2009
Equity Securities	57%-73%	62%	67%	66%
Debt Securities	26%-44%	38%	33%	34%
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.

The fair values of the plan assets at December 31, 2011 by asset category (see description of levels in Note E) are as follows:

(Millions of Dollars)	Level 1	Level 2	Level 3	Total
U.S. Equity (a)	$17	$33	$-	$50
International Equity (b)	-	17	-	17
Other Fixed Income (c)	-	37	-	37
Cash and Cash Equivalents (d)	-	2	-	2
Total investments	$17	$89	$-	$106
Total fair value of plan net assets				$106

(a) U.S. Equity includes both actively- and passively-managed assets with investments in domestic equity index funds and commingled funds.
(b) International Equity includes commingled international equity funds.
(c) Other Fixed Income includes commingled funds, which are valued at Net Asset Value (NAV).
(d) Cash and Cash Equivalents include short term investments and money markets.

(e) Con Edison and its subsidiaries set aside funds for retiree health benefits through a separate account within the pension trust, as permitted under Section 401(h) of the Internal Revenue Code of 1986, as amended. In accordance with the Code, the plan's investments in the 401(h) account may not be used for, or diverted to, any purpose other than providing health benefits for retirees. The net assets held in the 401(h) account are calculated based on a pro-rata percentage allocation of the net assets in the pension plan. The related obligations for health benefits are not included in the pension plan's obligations and are included in Con Edison and its subsidiaries' other postretirement benefit obligation. See Note E.

(f) Pending activities include security purchases and sales that have not settled, interest and dividends that have not been received, and reflects adjustments for available estimates at year end.

The table below provides a reconciliation of the beginning and ending net balances for assets at December 31, 2011 classified as Level 3 in the fair value hierarchy.

(Millions of Dollars)	Beginning Balance as of January 1, 2011	Assets Still Held at Reporting Date – Unrealized Gains/ (Losses)	Assets Sold During the Period – Realized(Losses)	Purchases Sales and Settlements	Transfers Out of Level 3	Ending Balance as of December 31, 2011
Other Fixed Income	$34	$-	$-	$-	$(34)	$-
Insurance Contracts	-	-	-	-	-	-
Total investments	$34	-	-	-	(34)	$-
Investments (including funds for retiree health benefits)	$34	$-	$-	$-	$(34)	$-

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

(Millions of Dollars)	Level 1	Level 2	Level 3	Total
U.S. Equity (a)	$17	$33	$-	$50
International Equity (b)	-	18	-	18
Other Fixed Income (c)	-	-	34	34
Cash and Cash Equivalents (d)	-	-	-	-
Total investments	$17	$52	$34	$102
Total fair value of plan net assets				$102

(a) U.S. Equity includes both actively- and passively-managed assets with investments in domestic equity index funds and commingled funds.

(b) International Equity includes commingled international equity funds.

(c) Other Fixed Income includes commingled funds, which are valued at Net Asset Value (NAV).

(d) Cash and Cash Equivalents include short term investments and money markets.

(e) Con Edison and its subsidiaries set aside funds for retiree health benefits through a separate account within the pension trust, as permitted under Section 401(h) of the Internal Revenue Code of 1986, as amended. In accordance with the Code, the plan's investments in the 401(h) account may not be used for, or diverted to, any purpose other than providing health benefits for retirees. The net assets held in the 401(h) account are calculated based on a pro-rata percentage allocation of the net assets in the pension plan. The related obligations for health benefits are not included in the pension plan's obligations and are included in Con Edison and its subsidiaries' other postretirement benefit obligation. See Note E.

(f) Pending activities include security purchases and sales that have not settled, interest and dividends that have not been received, and reflects adjustments for available estimates at year end.

The table below provides a reconciliation of the beginning and ending net balances for assets at December 31, 2010 classified as Level 3 in the fair value hierarchy.

(Millions of Dollars)	Beginning Balance as of January 1, 2010	Assets Still Held at Reporting Date – Unrealized Gains (Losses)	Assets Sold During the Period – Realized Gains	Purchases Sales and Settlements	Ending Balance as of December 31, 2010
Other Fixed Income	$27	$2	$(1)	$6	$34
Insurance Contracts	8	-	(1)	(7)	-
Total investments	$35	$2	$(2)	$(1)	$34
Investments (including funds for retiree health benefits)	$35	$2	$(2)	$(1)	$34

Effect of Medicare Prescription Benefit

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

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

Note G – Environmental Matters

Superfund Sites

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

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

its manufactured gas plant sites and any neighboring areas to which contamination may have migrated, are referred to herein as "Superfund Sites."

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

The accrued liabilities and regulatory assets related to Superfund Sites at December 31, 2011 and 2010 were as follows:

(Millions of Dollars)	2011	2010
Accrued Liabilities:		
Manufactured gas plant sites	$115	$119
Other Superfund Sites	1	1
Total	$116	$120
Regulatory assets	$117	$121

The Superfund Sites have been investigated. However, for some of the sites, the extent and associated cost of the required remediation has not yet been determined. As information pertaining to the required remediation becomes available, the company expects that additional liability may be accrued, the amount of which is not presently determinable but may be material. Under its current rate plans for provision of electric and gas service in New York, O&R is permitted to recover or defer as regulatory assets (for subsequent recovery through rates) certain site investigation and remediation costs. In February 2011, the NYSPSC initiated a proceeding to examine the existing mechanisms pursuant to which the Company recovers such costs and possible alternatives.

Insurance recoveries related to Superfund Sites for the year ended December 31, 2011 were immaterial. There were no insurance recoveries received related to Superfund Sites for the year ended December 31, 2010. Environmental remediation costs incurred related to Superfund Sites at December 31, 2011 and 2010 were as follows:

(Millions of Dollars)	2011	2010
Remediation costs incurred	$4.0	$3.0

In 2010, O&R estimated that for its manufactured gas plant sites, each of which has been investigated, the aggregate undiscounted potential liability for the remediation of coal tar and/or other manufactured gas plant related environmental contaminants could range up to $200 million. These estimates were based on assumptions regarding the extent of contamination and the type and extent of remediation that may be required. Actual experience may be materially different.

Asbestos Proceedings

Suits have been brought in New York State and federal courts against O&R and many other defendants, wherein a large number of plaintiffs sought large amounts of compensatory and punitive damages for deaths and injuries allegedly caused by exposure to asbestos at various O&R premises. The suits that have been resolved, which are many, have been resolved without any payment by O&R, or for amounts that were not, in the aggregate, material to the Company. The amounts specified in all the remaining suits total billions of dollars, but the Company believes that these amounts are greatly exaggerated, based on the disposition of previous claims.

In addition, certain current and former employees have claimed or are claiming workers' compensation benefits based on alleged disability from exposure to asbestos. The Company defers as regulatory assets (for subsequent recovery through rates) liabilities incurred for asbestos claims by employees and third-party contractors relating to its divested generating plants.

The Company's accrued liability for asbestos suits and workers' compensation proceedings (including those related to asbestos exposure) at December 31, 2011 and 2010 were as follows:

(Millions of Dollars)	2011	2010
Accrued liability – asbestos suits	$0.3	$0.3
Regulatory assets – asbestos suits	0.3	0.3
Accrued liability – workers' compensation	$4.7	$5.0
Regulatory assets – workers' compensation	0.3	0.4

Note H – Leases

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

Capital leases: For ratemaking purposes, capital leases are treated as operating leases; therefore, in accordance with accounting rules for regulated operations, the amortization of the leased asset is based on the rental payments recovered from customers. The following asset under capital leases is included in O&R's balance sheet at December 31, 2011 and 2010:

(Millions of Dollars)	2011	2010
UTILITY PLANT		
Common	$1.6	$ -
TOTAL	$1.6	$ -

The accumulated amortization of the capital lease was $0.5 million at December 31, 2011.

There is no future minimum lease commitment for the above asset.

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

(Millions of Dollars)	
2012	$0.6
2013	0.5
2014	0.5
2015	0.5
2016	0.6
All years thereafter	3.0
Total	$5.7

Note I – Income Tax

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

(Millions of Dollars)	2011	2010	2009
State			
Current	$5	$8	$(3)
Deferred – net	2	(1)	9
Federal			
Current	(4)	(1)	(16)
Deferred – net	28	20	32
TOTAL CHARGE TO OPERATIONS	31	26	22
TOTAL CHARGE/(BENEFIT) TO OTHER INCOME	-	-	1
TOTAL	$31	$26	$23

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

(Millions of Dollars)	2011	2010
Deferred tax liabilities:		
Depreciation	$213	$168
Regulatory assets – future income tax	80	94
Unrecognized pension and other postretirement costs	298	89
State income tax	21	22
Capitalized overheads	66	64
Pension	(27)	(13)
Investment tax credits	3	3
Other	32	46
Total deferred tax liabilities	686	473
Deferred tax assets:		
Unrecognized pension and other postretirement costs	298	89
Regulatory liabilities – future income tax	6	16
Other	61	55
Total deferred tax assets	365	160
Net deferred tax liabilities and investment tax credits	321	313
Deferred tax liabilities and investment tax credits – non current	350	324
Deferred tax assets – current	(29)	(11)
Total deferred tax liabilities and investment tax credits	$321	$313

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)	2011	2010	2009
STATUTORY TAX RATE			
Federal	35%	35%	35%
Changes in computed taxes resulting from:			
State income tax	5	6	6
Depreciation related differences	2	(1)	(1)
Cost of removal	(3)	(2)	(3)
AFUDC	(2)	(2)	(1)
Medicare Reimbursement	(0)	(2)	(1)
Other	(1)	1	(1)
Effective Tax Rate	36%	35%	34%

For federal income tax purposes, O&R has a net operating loss carryforward available from 2011 of $50.7 million, primarily as a result of accelerated depreciation, which if unused will expire in 2031. O&R has recorded a deferred tax asset for its loss carryforward, and no valuation allowance has been provided, as it is more likely than not that the deferred tax asset will be realized. Con Edison had a 2010 net operating loss for federal income tax purposes. In 2011, Con Edison received a refund using the 2010 net operating loss to offset a prior year's taxable income, of which $6.4 million related to O&R.

For New York State income tax purposes, Con Edison has a net operating loss carryforward available from 2009 of $220 million, of which $37.2 million related to O&R. This loss is primarily a result of repair allowance deductions discussed below. A deferred tax asset has been recognized for this New York State net operating loss that will not expire until 2029. A valuation allowance has not been provided as it is more likely than not that the deferred tax asset will be realized.

Uncertain Tax Positions

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

The IRS has essentially completed its field audits of Con Edison's federal income tax returns through 2010. Con Edison's federal income tax returns for 1998 through 2010 reflect certain tax positions with which the IRS does not or may not agree. Any adjustments to federal income tax refunds would result in changes to Con Edison's New York state income tax returns. In addition, Con Edison's New York State income tax returns for years beginning with 2006 remain open for examination.

Con Edison's 2010 and 2009 federal income tax returns reflect, among other things, an incremental current deduction for the costs of certain repairs to utility plant (the "repair allowance deductions"). Prior to 2009, Con Edison capitalized such costs and included these costs in depreciation expense in its federal income tax returns. At December 31, 2011, with respect to the repair allowance deductions, Con Edison recorded a liability for uncertain tax positions of $88 million ($3 million attributable to O&R).

In August 2011, the IRS issued guidance regarding the use and evaluation of statistical samples and sampling estimates. This guidance provides a safe harbor method of determining whether certain expenditures for electric transmission and distribution property can be currently deducted for federal income tax purposes. No guidance was issued related to gas property. At December 31, 2011, O&R's estimated liabilities for uncertain tax positions reflect its anticipated adoption of the new IRS guidance, which did not have a material impact on net income.

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

(Millions of Dollars)	2011	2010	2009
Balance at the beginning of the year	$8	$(11)	$9
Additions based on tax positions of prior years	3	18	-
Reductions for tax positions of prior years	(1)	-	(14)
Settlements	-	1	(6)
Balance at the end of the year	$10	$8	$(11)

At December 31, 2011, O&R's estimated liabilities for uncertain tax positions were classified on its consolidated balance sheet either as current liabilities ($8.4 million) or as a reduction to current deferred tax assets ($1.6 million). The Company reasonably expects to resolve these uncertain tax positions with the IRS in the next 12 months.

O&R recognizes interest accrued related to the liability for uncertain tax positions in interest expense and would recognize penalties, if any, in operating expenses in O&R's consolidated income statements. In 2011, 2010 and 2009, O&R recognized an immaterial amount of interest and no penalties for uncertain tax positions in its consolidated income statements. At December 31, 2011 and 2010, O&R recognized an immaterial amount of interest and no penalties in its consolidated balance sheets.

At December 31, 2011, there are no unrecognized tax benefits that if recognized would materially affect O&R's effective tax rate.

Note J – Stock-Based Compensation

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

Shares of Con Edison common stock used to satisfy the obligations with respect to O&R's stock-based compensation may be new (authorized, but unissued) shares, treasury shares or shares purchased in the open market. The shares used during the period ended December 31, 2011 were treasury shares and new shares. The shares used during the period ended December 31, 2010 were new shares.

Under the accounting rules for stock compensation, the Company has recognized the cost of stock-based compensation as an expense using a fair value measurement method. The following table summarizes stock-based compensation expense recognized by the Company in the period ended December 31, 2011, 2010, and 2009:

(Millions of Dollars)	2011	2010	2009
Restricted stock units	$0.1	$0.1	$0.1
Performance-based restricted stock	2.9	1.7	1.1
Total	$3.0	$1.8	$1.2
Income Tax Benefit	$1.2	$0.7	$0.5

Stock Options

Stock options were last granted in 2006. The stock options generally vested over a three-year period and have a term of ten years. Options were granted at an exercise price equal to the fair market value of a Con Edison common share when the option was granted. The Company generally recognizes compensation expense (based on the fair value of stock option awards) over the continuous 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 forfeited in 2011 and 2010.

A summary of changes in the status of stock options awarded to O&R employees as of December 31, 2011 is as follows:

	Shares	Weighted Average Exercise Price
Outstanding at 12/31/10	307,000	$43.591
Exercised	(223,500)	$43.820
Outstanding at 12/31/11	83,500	$42.976

The change in the fair value of all outstanding options from their grant dates to December 31, 2011 and 2010 (aggregate intrinsic value) for O&R were $2 million. The aggregate intrinsic value of options exercised in 2011 and 2010 were $2 million and $1 million respectively, and the cash received by Con Edison for payment of the exercise price was $10 million and $8 million, respectively. The weighted average remaining contractual life of options outstanding is three years as of December 31, 2011.

The following table summarizes O&R employees’ stock options outstanding at December 31, 2011 for each plan year:

Plan Year	Remaining Contractual Life	Options Outstanding/ Exercisable	Weighted Average Exercise Price
2006	4	30,000	$44.514
2005	3	15,500	42.180
2004	2	20,500	43.796
2003	1	10,500	38.470
2002	1	7,000	42.510
Total		83,500	$42.976

Restricted Stock Units

Restricted stock unit awards under the LTIP have been made to O&R officers and certain employees, including awards that provide for adjustment of the number of units (performance-restricted stock units or Performance RSUs). Each restricted stock unit represents the right to receive, upon vesting, one share of Con Edison common stock, the cash value of a share or a combination thereof.

In accordance with accounting rules for stock compensation, for outstanding restricted stock awards other than Performance RSUs, the Company has accrued a liability based on the market value of a common share on the grant date and are recognizing compensation expense over the vesting period. The vesting period for 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 summary of changes in the status of restricted stock (other than Performance RSUs or awards under the directors' deferred compensation plan) during the period ended December 31, 2011 is as follows:

	Units	Weighted Average Grant Date Fair Value
Non-vested at 12/31/10	3,400	$41.378
Granted	1,200	50.720
Vested	(865)	39.700
Forfeited	(235)	40.730
Non-vested at 12/31/11	3,500	$45.039

The total expense to be recognized by the Company in future periods for unvested awards outstanding as of December 31, 2011 was $91,494 and is expected to be recognized over a weighted average period of one year.

The number of units in each annual Performance RSU is subject to adjustment as follows: (i) 50 percent of the units awarded will be multiplied by a factor that may range from 0 to 150 percent based on Con Edison's total shareholder return relative to a peer group of utilities for a specified performance period (the TSR portion); and (ii) 50 percent of the units awarded will be multiplied by a factor that may range from 0 to 200 percent based on determinations made in connection with the O&R Annual Team Incentive Plan (the EIP portion). Units generally vest when the performance period ends.

For the TSR portion of Performance RSU, the Company uses a Monte Carlo simulation model to estimate the fair value of the awards. The fair value is recomputed each reporting period as of the earlier of the reporting date and the vesting date. For the EIP portion of Performance RSU, the fair value of the awards is determined using the market price as of the earlier of the reporting date or the vesting date multiplied by the average EIP determination over the vesting period. Performance RSU awards are "liability awards" because each Performance RSU represents the right to receive, upon vesting, one share of Con Edison common stock, the cash value of a share

or a combination thereof. As such, changes in the fair value of the Performance RSUs are reflected in net income. The following table illustrates the assumptions used to calculate the fair value of the awards:

	2011
Risk-free interest rate	0.12% - 3.73%
Expected term	3 years
Expected volatility	16.37%

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

A summary of changes in the status of the Performance RSUs TSR portion during the period ended December 31, 2011 is as follows:

	Units	Weighted Average Grant Date Fair Value*
Non-vested at 12/31/10	28,260	$38.579
Granted	16,335	43.828
Vested	(8,736)	32.262
Forfeited	(107)	42.071
Non-vested at 12/31/11	35,752	$42.511

* Fair value is determined using the Monte Carlo simulation described above. Weighted average grant date fair value does not reflect any accrual or payment of dividends prior to vesting.

A summary of changes in the status of the Performance RSUs' EIP portion during the period ended December 31, 2011 is as follows:

	Units	Weighted Average Grant Date Fair Value*
Non-vested at 12/31/10	28,260	$42.932
Granted	16,335	50.048
Vested	(8,736)	40.759
Forfeited	(107)	44.780
Non-vested at 12/31/11	35,752	$46.709

*Fair value is determined using the market price of one share of Con Edison common stock on the grant date. The market price has not been discounted to reflect that dividends do not accrue and are not payable on Performance RSUs until vesting.

The total expense to be recognized by O&R in future periods for unvested Performance RSUs outstanding as of December 31, 2011 is $2.8 million, and is expected to be recognized over a weighted average period of two years.

Stock Purchase Plan

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

Participants in the plan immediately vest in shares purchased by them under the plan. The fair value of the shares of Con Edison common stock purchased under the plan was calculated using the average of the high and low composite sale prices at which shares were traded at the New York Stock Exchange on the trading day immediately preceding such purchase dates. During 2011, 2010, and 2009, 721,520, 738,951, and 868,622 shares were purchased under the Stock Purchase Plan at a weighted average price of $52.50, $45.52, and $38.15 per share, respectively.

Note K – Financial Information by Business Segment

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

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

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

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

The financial data for the business segments are as follows:

As of and for the Year Ended December 31, 2011 (Millions of Dollars)	Operating revenues	Inter-segment revenues	Depreciation and amortization	Operating income	Interest charges	Income tax expense	Total assets*	Construction expenditures
Electric	$641	$-	$35	$81	$20	$21	$1,755	$79
Gas	214	-	13	33	12	9	722	32
Other*	-	-	-	-	2	-	8	-
Total	$855	$-	$48	$114	$34	$30	$2,485	$111

As of and for the Year Ended December 31, 2010 (Millions of Dollars)	Operating revenues	Inter-segment revenues	Depreciation and amortization	Operating income	Interest charges	Income tax expense	Total assets*	Construction expenditures
Electric	$692	$-	$32	$74	$22	$18	$1,630	$99
Gas	218	-	12	34	12	8	686	36
Other*	-	-	-	-	1	-	32	-
Total	$910	$-	$44	$108	$35	$26	$2,348	$135

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

* Includes amounts related to the RECO securitization.

Note L – Derivative Instruments and Hedging Activities

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

Energy Price Hedging

The Company hedges market price fluctuations associated with physical purchases of electricity by using electric and gas derivative instruments including futures, forwards, and options. The fair values of these hedges at December 31, 2011 and 2010 were as follows:

(Millions of Dollars)	2011	2010
Fair value of net derivative assets/ (liabilities) – gross	$(28)	$(48)
Impact of netting of cash collateral	2	15
Fair value of net derivative assets/ (liabilities) – net	$(26)[a]	$(33)[a]

(a) Includes derivative liabilities of $3 million with Con Edison's competitive energy businesses at December 31, 2010. See Note O.

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

Credit Exposure

The Company is exposed to credit risk related to transactions entered into primarily for the various electric supply and hedging activities. The Company uses credit policies to manage this risk, including an established credit approval process, monitoring of counterparty limits, netting provisions within agreements and collateral or prepayment arrangements.

The Company had $1 million of credit exposure in connection with electricity supply and hedging activities, net of collateral, at December 31, 2011. The Company's net credit exposure was primarily with commodity exchange brokers.

Economic Hedges

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

The fair values of the Company's commodity derivatives at December 31, 2011 and 2010 were:

Fair Value of Commodity Derivatives [(a)]

(Millions of Dollars)	Balance Sheet Location	2011	2010
	Derivative Assets		
Current	Other current assets	$-	$1
Long term	Other deferred charges and non-current assets	1	3
Total derivative assets		$1	$4
Impact of netting		-	(1)
Net derivative assets		$1	$3
	Derivative Liabilities		
Current	Fair value of derivative liabilities	$22	$37
Long term	Fair value of derivative liabilities	7	15
Total derivative liabilities		29	$52
Impact of netting		(2)	(16)
Net derivative liabilities		$27[(b)]	$36[(b)]

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

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

The following table presents the changes in the fair values of commodity derivatives that have been deferred for the year ended December 31, 2011 and 2010:

Realized and Unrealized Gains/(Losses) on Commodity Derivatives[(a)]

(Millions of Dollars)	Balance Sheet Location	Deferred for the Year Ended December 31, 2011	Deferred for the Year Ended December 31, 2010
Pre-tax (losses)/gains deferred in accordance with the accounting rules for regulated operations:			
Current	Deferred derivative gains	$(1)	$1
Long term	Regulatory liabilities	(1)	1
Total deferred (losses)/gains		$(2)	$2
Current	Deferred derivative losses	$15	$(2)
Current	Recoverable energy costs[(b)]	(73)	(78)
Long term	Regulatory assets	7	5
Total deferred losses		$(51)	$(75)
Net deferred losses		$(53)	$(73)

(a) Qualifying derivative contracts, which have been designated as normal purchases or normal sales contracts, are not reported at fair value under the accounting rules for derivatives and hedging and, therefore, are excluded from the table.
(b) Includes payments of $11 million and $32 million to Con Edison's competitive energy businesses for the years ended December 31, 2011 and 2010, respectively. See Note O.

As of December 31, 2011, the Company had 82 electric or gas derivative contracts hedging electric energy or capacity market prices, which were considered to be derivatives under the accounting rules for derivatives and hedging (excluding qualifying derivative contracts, which have been designated as normal purchases or normal sales contracts). The following table presents the number of contracts by commodity type:

Electric Derivatives				Gas Derivatives		
Number of Energy Contracts[a]	MWhs[b]	Number of Capacity Contracts[a]	MWs[b]	Number of Contracts[a]	Dths[b]	Total Number of Contracts[a]
13	2,007,305	1	769	68	5,330,000	82

(a) Qualifying derivative contracts, which have been designated as normal purchases or normal sales contracts, are not reported at fair value under the accounting rules for derivative and hedging and, therefore, are excluded from the table.
(b) Volumes are reported net of long and short positions.

The collateral requirements associated with, and settlement of, derivative transactions are included in net cash flows from operating activities in the Company's consolidated statement of cash flows. Most derivative instrument contracts contain provisions that may require the Company to provide collateral on derivative instruments in net liability positions. The Utilities enter into separate derivative instruments for electric energy or capacity, and CECONY enters into derivative instruments in connection with the Utilities' joint gas supply arrangements (See Note O). The amount of collateral to be provided will depend on the fair value of the derivative instruments and the Utilities' credit ratings.

The aggregate fair value of all derivative instruments with credit-risk-related contingent features that are in a net liability position, and collateral posted at December 31, 2011, and the additional collateral that would have been required to be posted had the lowest applicable credit rating been reduced one level and to below investment grade were:

(Millions of Dollars)	
Aggregate fair value – net liabilities[a]	$27
Collateral posted[b]	5
Additional collateral[c] (downgrade one level from current rating[d])	9
Additional collateral[c] (downgrade to below investment grade from current rating[d])	26[e]

(a) Non-derivative transactions for the purchase and sale of electricity and qualifying derivative instruments, which have been designated as normal purchases or normal sales, are excluded from the table. These transactions primarily include purchases of electricity from independent system operators. For certain other such non-derivative transactions, the Company could be required to post collateral under certain circumstances, including in the event counterparties had reasonable grounds for insecurity.
(b) Across the Utilities' energy derivative positions, credit limits for the same counterparties are generally integrated. At December 31, 2011, the Utilities posted combined collateral of $58 million, including the collateral posted that is estimated to be attributable to O&R shown above.
(c) The additional collateral amounts shown above are based upon the estimated O&R allocation of the Utilities' collateral requirements. The Utilities measure the collateral requirements by taking into consideration the fair value amounts of derivative instruments that contain credit-risk-related contingent features that are in a net liability position plus amounts owed to counterparties for settled transactions and amounts required by counterparties for minimum financial security. The fair value amounts represent unrealized losses, net of any unrealized gains where the Utilities have a legally enforceable right of setoff.
(d) The current long-term ratings of O&R are Baa1/A-/A- by Moody's, S&P, and Fitch, respectively. Credit ratings assigned by rating agencies are expressions of opinions that are subject to revision or withdrawal at any time by the assigning rating agency.
(e) Derivative instruments that are net assets have been excluded from the table. At December 31, 2011, if O&R had been downgraded to below investment grade, it would have been required to post additional collateral for such derivative instruments of not more than $4 million.

Interest Rate Swaps

O&R has an interest rate swap pursuant to which it pays a fixed-rate of 6.09 percent and receives a LIBOR-based variable rate. The fair value of this interest rate swap at December 31, 2011 was an unrealized loss of $8 million, which has been included in the company's consolidated balance sheet as a noncurrent liability/fair value of derivative liabilities and a regulatory asset. The increase in the fair value of the swap for the year ended December 31, 2011 was $2 million. In the event O&R's credit rating was downgraded to BBB- or lower by S&P or

Baa3 or lower by Moody's, the swap counterparty could elect to terminate the agreement and, if it did so, the parties would then be required to settle the transaction.

Note M – Fair Value Measurements

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

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

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

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

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

that expire after the period of time for which quoted prices are available and internal models are used to determine a significant portion of the value.

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

Assets and liabilities measured at fair value on a recurring basis as of December 31, 2011 are summarized below.

(Millions of Dollars)	Level 1	Level 2	Level 3	Netting Adjustments [4]	Total
Derivative assets:					
Commodity [1]	$-	$1	$-	$-	$1
Other assets [3]	-	-	9	-	9
Total	$-	$1	$9	$-	$10
Derivative liabilities:					
Commodity	$-	$-	$29	$(2)	$27[4]
Transfer in[5][6]	-	1	-	-	1
Transfer out[5][6]	-	-	(1)	-	(1)
Commodity[1]	$-	$1	$28	$(2)	$27
Interest rate contract [2]	-	-	8	-	8
Total	$-	$1	$36	$(2)	$35

(1) A significant portion of the commodity derivative contracts categorized in Level 3 is valued using either an industry acceptable model or an internally developed model with observable inputs. The models also include some less readily observable inputs resulting in the classification of the respective contract as Level 3. See Note L.
(2) See Note L.
(3) Other assets are comprised of assets such as life insurance contracts within the Supplemental Employee Retirement Plan, held in a rabbi trust.
(4) Amounts represent the impact of legally-enforceable master netting agreements that allow the Company to net gain and loss positions and cash collateral held or placed with the same counterparties.
(5) The Company's policy is to recognize transfers into and transfers out of the levels at the end of the reporting period.
(6) Transferred from Level 3 to Level 2 because of availability of observable market data due to decrease in the terms of certain contracts from beyond one year as of December 31, 2010 to less than one year as of December 31, 2011.

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

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

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

(3) Other assets are comprised of assets such as life insurance contracts within the Supplemental Employee Retirement Plan, held in a rabbi trust.
(4) Amounts represent the impact of legally-enforceable master netting agreements that allow the Company to net gain and loss positions and cash collateral held or placed with the same counterparties.
(5) Includes derivative liabilities of $3 million with Con Edison's competitive energy businesses. See Note O.

The table listed below provides a reconciliation of the beginning and ending net balances for assets and liabilities measured at fair value for the years ended December 31, 2011 and 2010 and classified as Level 3 in the fair value hierarchy:

	For the Year Ended December 31, 2011								
		Total Gains/(Losses) – Realized and Unrealized							
(Millions of Dollars)	Beginning Balance as of January 1, 2011	Included in Earnings	Included in Regulatory Assets and Liabilities	Purchases	Issuances	Sales	Settlements	Transfer In/Out of Level 3	Ending Balance as of December 31, 2011
Derivatives:									
Commodity	$(49)	$(40)	$19	$-	$-	$-	$40	$1	$(29)
Interest rate contract	(10)	(3)	2	-	-	-	3	-	(8)
Other assets (1)	9	-	-	-	-	-	-	-	9
Total	$(50)	$(43)	$21	$-	$-	$-	$43	$1	$(28)

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

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

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

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

The accounting rules for fair value measurements and disclosures require consideration of the impact of nonperformance risk (including credit risk) from a market participant perspective in the measurement of the fair value of assets and liabilities. At December 31, 2011, the Company determined that nonperformance risk would have no material impact on their financial position or results of operations. To assess nonperformance risk, the Company considered information such as collateral requirements, master netting arrangements, letters of credit

and parent company guarantees, and applied a market-based method by using the counterparty (for an asset) or the Company's (for a liability) credit default swaps rates.

Note N – Asset Retirement Obligations

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

The Company includes in depreciation the estimated removal costs, less salvage, for utility plant assets. In accordance with accounting rules for asset retirement obligations, future removal costs that do not represent legal asset retirement obligations are recorded as regulatory liabilities pursuant to accounting rules for regulated operations. The related regulatory liabilities recorded for the Company were $76 million and $72 million at December 31, 2011 and 2010, respectively.

Note O – Related Party Transactions

The Company provides and receives administrative and other services to and from Con Edison and its subsidiaries pursuant to cost allocation procedures developed in accordance with rules approved by the NYSPSC and/or other regulatory authorities, as applicable. The services received include substantial administrative support operations, such as corporate secretarial and associated ministerial duties, accounting, treasury, investor relations, information resources, legal, human resources, fuel supply, and energy management services. The costs of administrative and other services provided by the Company, and received from Con Edison and its other subsidiaries for the years ended December 31, 2011, 2010, and 2009 were as follows:

(Millions of Dollars)	2011	2010	2009
Cost of services provided	$19	$17	$18
Cost of services received	$41	$40	$41

At December 31, 2011, 2010, and 2009, O&R's payable to CECONY associated with these services was $3 million, $3 million, and $4 million, respectively.

In addition, CECONY and O&R have joint gas supply arrangements, in connection with which O&R purchased from CECONY $81 million, $99 million, and $124 million of natural gas for the years ended December 31, 2011, 2010, and 2009, respectively. These amounts are net of the effect of related hedging transactions. At December 31, 2011, 2010, and 2009, O&R's net payable to CECONY associated with these gas purchases was $4 million, $11 million, and $16 million, respectively. At December 31, 2011, 2010, and 2009, O&R's payable to Con Edison's competitive energy businesses associated with electricity purchases and retail services was $2 million, $4 million, and $3 million, respectively.

RECO purchased from Consolidated Edison Energy, Inc. $11 million, $32 million and $37 million of electricity for the periods ended December 31, 2011, 2010 and 2009, respectively, pursuant to energy auctions.

At December 31, 2011, 2010, and 2009, the Company's receivable from Con Edison for income taxes was $4, $27 million, and $13 million, respectively.

At December 31, 2011, the Company's receivable from CECONY for an Economic Stimulus Grant was $1 million. There was no receivable for December 31, 2010.

FERC has authorized CECONY through 2013 to lend funds to O&R from time to time, for periods of not more than 12 months, in amounts not to exceed $250 million outstanding at any time, at prevailing market rates. At December 31, 2011 and 2010, there were no loans outstanding for O&R.

Note P – New Financial Accounting Standards

In May 2011, the Financial Accounting Standards Board (FASB) issued amendments to the guidance for fair value measurement through Accounting Standards Update (ASU) No. 2011-04, "Fair Value Measurement (Topic 820): Amendments to Achieve Common Fair Value Measurement and Disclosure Requirements in U.S. GAAP and IFRSs." The amendments expand Accounting Standards Codification 820's existing disclosure requirements for fair value measurements and makes other amendments. Many of these amendments were made to eliminate unnecessary wording differences between U.S. generally accepted accounting principles and International Financial Reporting Standards. For public entities, the amendments are effective prospectively during interim and annual periods beginning after December 15, 2011. The application of this guidance is not expected to have a material impact on the Company's financial position, results of operations and liquidity.

In June 2011, the FASB issued new guidance for presentation of comprehensive income through ASU No. 2011−05, "Comprehensive Income (Topic 220): Presentation of Comprehensive Income." The amendments require that the comprehensive income be presented either in a single continuous statement of comprehensive income or in two separate but consecutive statements. In the two-statement approach, the first statement should present total net income and its components followed consecutively by a second statement that should present total other comprehensive income, the components of other comprehensive income, and the total of comprehensive income. The amendments in this update are applicable retrospectively for public entities effective for fiscal years, and interim periods within those years, beginning after December 15, 2011. Early adoption is permitted. The application of this guidance does not have a material impact on the Company's financial position, results of operations and liquidity.

In September 2011, the FASB issued amendments to the guidance for goodwill impairment testing through ASU No. 2011-08, "Intangibles-Goodwill and Other (Topic 350): Testing Goodwill for Impairment." The amendments provide guidance that exempts an entity from calculating the fair value of a reporting unit, if on an initial assessment of qualitative factors it is more likely than not that the fair value of a reporting unit is greater than its carrying amount. For public entities, the amendments are effective for interim and annual goodwill tests performed

for years beginning after December 15, 2011. The application of this guidance is not expected to have a material impact on the Company's financial position, results of operations or liquidity.

In September 2011, the FASB issued amendments to guidance for disclosures related to retirement benefits through ASU No. 2011-09, "Compensation—Retirement Benefits—Multiemployer Plans (Subtopic 715-80): Disclosures about an Employer's Participation in a Multiemployer Plan." The amendment provides guidance that requires employers to provide additional separate disclosures for multiemployer pension plans and multiemployer other postretirement benefit plans about the commitments an employer has made to a multiemployer plan and the potential future cash flow implication of participation in such a plan. For public entities, the amendments are effective for interim and annual periods ending after December 15, 2011. The application of this guidance is not expected to have a material impact on the Company's financial position, results of operations or liquidity.

In December 2011, the FASB issued amendments to guidance for disclosures related to balance sheet off-setting through ASU No. 2011-11," Balance Sheet (Topic 210): Disclosures about Offsetting Assets and Liabilities." The amendments provide guidance that requires a reporting entity to disclose certain quantitative information concerning financial and derivative instruments that are offset in the balance sheet and a description of the rights of setoff, including the nature of such rights, associated with recognized assets and liabilities that are subject to an enforceable master netting arrangement or similar agreement. For public companies, the amendments are effective for annual periods beginning on or after January 1, 2013 and retrospectively for all comparative periods presented. The application of this guidance is not expected to have a material impact on the Company's financial position, results of operations or liquidity.

In December 2011, the FASB issued amendments to guidance for disclosures related to reclassification adjustments through ASU No. 2011-12, "Comprehensive Income (Topic 220): Deferral of the Effective Date for Amendments to the Presentation of Reclassifications of Items Out of Accumulated Other Comprehensive Income in Accounting Standards Update No. 2011-05." The amendments defer the effective date for the requirements per ASU No. 2011-05 for the presentation of reclassification adjustments and the effect of such reclassification adjustments as a component of net income and a component of other comprehensive income. The guidance requires reporting entities to continue reporting reclassifications out of accumulated other comprehensive income on the face of, or the notes to the financial statements consistent with the presentation requirements in effect before update ASU No. 2011-05. The amendments in this update are applicable retrospectively for public entities effective for fiscal years, and interim periods within those years, beginning after December 15, 2011. Early adoption is permitted. The application of this guidance does not have a material impact on the Company's financial position, results of operations and liquidity.