

**Orange and Rockland Utilities, Inc.**  
**Consolidated Financial Statements**  
**December 31, 2020 and 2019**



## Report of Independent Auditors

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

We have audited the accompanying consolidated financial statements of Orange and Rockland Utilities, Inc. and its subsidiaries, which comprise the consolidated balance sheets and statements of capitalization as of December 31, 2020 and 2019, and the related consolidated statements of income, of comprehensive income, of shareholder's equity and of cash flows for each of the three years in the period ended December 31, 2020.

### *Management's Responsibility for the Consolidated Financial Statements*

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

### *Auditors' Responsibility*

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

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

### *Opinion*

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of Orange and Rockland Utilities, Inc. and its subsidiaries as of December 31, 2020 and 2019, and the results of their operations and their cash flows for each of the three years in the period ended December 31, 2020 in accordance with accounting principles generally accepted in the United States of America.

A handwritten signature in black ink that reads "PricewaterhouseCoopers LLP". The signature is written in a cursive, flowing style.

March 12, 2021

**Orange and Rockland Utilities, Inc.  
Consolidated Financial Statements**

**December 31, 2020 and 2019**

[Report of Independent Auditors](#)

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## Orange and Rockland Utilities, Inc. Consolidated Income Statement

| <i>(Millions of Dollars)</i>                          | For the Years Ended December 31, |             |             |
|---|----------------------------------|-------------|-------------|
|   | 2020                             | 2019        | 2018        |
| <b>OPERATING REVENUES</b>                             |                                  |             |             |
| Electric  | \$629                            | \$634       | \$642       |
| Gas   | 233                              | 259         | 249         |
| <b>TOTAL OPERATING REVENUES</b>                       | <b>862</b>                       | <b>893</b>  | <b>891</b>  |
| <b>OPERATING EXPENSES</b>                             |                                  |             |             |
| Purchased power                                       | 169                              | 188         | 208         |
| Gas purchased for resale                              | 61                               | 90          | 86          |
| Other operations and maintenance                      | 310                              | 308         | 305         |
| Depreciation and amortization                         | 90                               | 84          | 77          |
| Taxes, other than income taxes                        | 85                               | 84          | 83          |
| <b>TOTAL OPERATING EXPENSES</b>                       | <b>715</b>                       | <b>754</b>  | <b>759</b>  |
| <b>OPERATING INCOME</b>                               | <b>147</b>                       | <b>139</b>  | <b>132</b>  |
| <b>OTHER INCOME (DEDUCTIONS)</b>                      |                                  |             |             |
| Investment and other income                           | 1                                | —           | 1           |
| Allowance for equity funds used during construction   | 3                                | 2           | 1           |
| Other deductions                                      | (18)                             | (13)        | (21)        |
| <b>TOTAL OTHER INCOME (DEDUCTIONS)</b>                | <b>(14)</b>                      | <b>(11)</b> | <b>(19)</b> |
| <b>INCOME BEFORE INTEREST AND INCOME TAX EXPENSE</b>  | <b>133</b>                       | <b>128</b>  | <b>113</b>  |
| <b>INTEREST EXPENSE</b>                               |                                  |             |             |
| Interest on long-term debt                            | 41                               | 39          | 36          |
| Other interest  | 2                                | 4           | 4           |
| Allowance for borrowed funds used during construction | (2)                              | (2)         | (1)         |
| <b>NET INTEREST EXPENSE</b>                           | <b>41</b>                        | <b>41</b>   | <b>39</b>   |
| <b>INCOME BEFORE INCOME TAX EXPENSE</b>               | <b>92</b>                        | <b>87</b>   | <b>74</b>   |
| <b>INCOME TAX EXPENSE</b>                             | <b>21</b>                        | <b>17</b>   | <b>15</b>   |
| <b>NET INCOME</b>                                     | <b>\$71</b>                      | <b>\$70</b> | <b>\$59</b> |

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

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

| <i>(Millions of Dollars)</i>  | For the Years Ended December 31, |      |      |
|---|----------------------------------|------|------|
|   | 2020                             | 2019 | 2018 |
| NET INCOME  | \$71                             | \$70 | \$59 |
| OTHER COMPREHENSIVE INCOME/(LOSS), NET OF TAXES                                   |                                  |      |      |
| Pension and other postretirement benefit plan liability adjustments, net of taxes | (2)                              | (3)  | 8    |
| TOTAL OTHER COMPREHENSIVE INCOME/(LOSS), NET OF TAXES                             | (2)                              | (3)  | 8    |
| COMPREHENSIVE INCOME  | \$69                             | \$67 | \$67 |

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

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

| <i>(Millions of Dollars)</i>  | For the Years Ended December 31, |              |              |
|---|----------------------------------|--------------|--------------|
|   | 2020                             | 2019         | 2018         |
| <b>OPERATING ACTIVITIES</b>   |                                  |              |              |
| Net income  | \$71                             | \$70         | \$59         |
| <b>PRINCIPAL NON-CASH CHARGES/(CREDITS) TO INCOME</b>                   |                                  |              |              |
| Depreciation and amortization   | 90                               | 84           | 77           |
| Deferred income taxes   | 19                               | —            | 17           |
| Rate case amortizations   | —                                | 1            | 16           |
| Common equity component of allowance for funds used during construction | (3)                              | (2)          | (1)          |
| Unbilled revenue accruals   | 10                               | (8)          | 11           |
| Other non-cash items, net   | 17                               | 8            | 30           |
| <b>CHANGES IN ASSETS AND LIABILITIES</b>                                |                                  |              |              |
| Accounts receivable - customers   | (20)                             | 15           | (15)         |
| Accounts receivable from affiliated companies                           | (2)                              | 5            | (5)          |
| Materials and supplies, including gas in storage                        | 1                                | (1)          | (1)          |
| Revenue decoupling mechanism receivable                                 | (8)                              | —            | —            |
| Prepayments, other receivables and other current assets                 | (7)                              | (9)          | 7            |
| Accounts payable  | 41                               | 16           | 1            |
| Accounts payable to affiliated companies                                | (1)                              | —            | (1)          |
| Pensions and retiree benefits obligations, net                          | 31                               | 29           | 33           |
| Pensions and retiree benefits contributions                             | (41)                             | (32)         | (40)         |
| Accrued taxes   | 7                                | (1)          | —            |
| Accrued taxes to affiliated companies                                   | (11)                             | 1            | (10)         |
| Accrued interest  | 1                                | —            | 1            |
| System benefit charge   | (7)                              | 1            | 6            |
| Superfund and environmental remediation costs, net                      | 8                                | 4            | (2)          |
| Deferred charges, noncurrent assets and other regulatory assets         | (54)                             | (15)         | (60)         |
| Deferred credits and other regulatory liabilities                       | 6                                | 17           | 52           |
| Other current and noncurrent liabilities                                | (2)                              | 7            | (3)          |
| <b>NET CASH FLOWS FROM OPERATING ACTIVITIES</b>                         | <b>146</b>                       | <b>190</b>   | <b>172</b>   |
| <b>INVESTING ACTIVITIES</b>   |                                  |              |              |
| Utility construction expenditures                                       | (214)                            | (210)        | (199)        |
| Cost of removal less salvage  | (6)                              | (8)          | (3)          |
| Proceeds from sale of assets  | —                                | —            | 4            |
| <b>NET CASH FLOWS USED IN INVESTING ACTIVITIES</b>                      | <b>(220)</b>                     | <b>(218)</b> | <b>(198)</b> |
| <b>FINANCING ACTIVITIES</b>   |                                  |              |              |
| Net issuance/(payment) of short-term debt                               | 28                               | (37)         | (42)         |
| Issuance of long-term debt  | 75                               | 125          | 150          |
| Retirement of long-term debt  | —                                | (62)         | (55)         |
| Debt issuance costs   | —                                | (1)          | (1)          |
| Capital contribution by parent  | 25                               | 30           | 25           |
| Dividend to parent  | (49)                             | (47)         | (46)         |
| <b>NET CASH FLOWS FROM FINANCING ACTIVITIES</b>                         | <b>79</b>                        | <b>8</b>     | <b>31</b>    |
| <b>CASH, TEMPORARY CASH INVESTMENTS AND RESTRICTED CASH:</b>            |                                  |              |              |
| <b>NET CHANGE FOR THE PERIOD</b>  | <b>5</b>                         | <b>(20)</b>  | <b>5</b>     |
| <b>BALANCE AT BEGINNING OF PERIOD</b>                                   | <b>32</b>                        | <b>52</b>    | <b>47</b>    |
| <b>BALANCE AT END OF PERIOD</b>   | <b>\$37</b>                      | <b>\$32</b>  | <b>\$52</b>  |
| <b>SUPPLEMENTAL DISCLOSURE OF CASH INFORMATION</b>                      |                                  |              |              |
| Cash paid during the period for:  |                                  |              |              |
| Interest  | \$40                             | \$39         | \$37         |
| Income taxes  | \$10                             | \$17         | \$10         |
| <b>SUPPLEMENTAL DISCLOSURE OF NON-CASH INFORMATION</b>                  |                                  |              |              |
| Construction expenditures in accounts payable                           | \$23                             | \$20         | \$29         |
| Software licenses acquired but unpaid as of end of period               | \$3                              | \$4          | \$5          |

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

## Orange and Rockland Utilities, Inc. Consolidated Balance Sheet

| <i>(Millions of Dollars)</i>   | December 31,<br>2020 | December 31,<br>2019 |
|--|----------------------|----------------------|
| <b>ASSETS</b>  |                      |                      |
| <b>CURRENT ASSETS</b>  |                      |                      |
| Cash and temporary cash investments  | \$37                 | \$32                 |
| Accounts receivable – customers, less allowance for uncollectible accounts of \$9 and \$5 in 2020 and 2019, respectively | 86                   | 70                   |
| Other receivables, less allowance for uncollectible accounts of \$2 and \$1 in 2020 and 2019, respectively               | 14                   | 8                    |
| Taxes receivables  | —                    | 1                    |
| Accrued unbilled revenue   | 32                   | 42                   |
| Accounts receivable from affiliated companies  | 6                    | 4                    |
| Gas in storage, at average cost  | 9                    | 11                   |
| Materials and supplies, at average cost  | 24                   | 23                   |
| Prepayments  | 31                   | 33                   |
| Regulatory assets  | 23                   | 15                   |
| Revenue decoupling mechanism receivable  | 8                    | —                    |
| Other current assets   | 7                    | 4                    |
| <b>TOTAL CURRENT ASSETS</b>  | <b>277</b>           | <b>243</b>           |
| <b>INVESTMENTS</b>   | <b>26</b>            | <b>26</b>            |
| <b>UTILITY PLANT, AT ORIGINAL COST</b>   |                      |                      |
| Electric   | 1,988                | 1,877                |
| Gas  | 910                  | 864                  |
| General  | 295                  | 291                  |
| <b>TOTAL</b>   | <b>3,193</b>         | <b>3,032</b>         |
| Less: Accumulated depreciation   | 878                  | 819                  |
| <b>Net</b>   | <b>2,315</b>         | <b>2,213</b>         |
| Construction work in progress  | 154                  | 123                  |
| <b>NET UTILITY PLANT</b>   | <b>2,469</b>         | <b>2,336</b>         |
| <b>OTHER NONCURRENT ASSETS</b>   |                      |                      |
| Regulatory assets  | 450                  | 373                  |
| Operating right-of-use asset   | 2                    | 3                    |
| Other deferred charges and noncurrent assets   | 23                   | 25                   |
| <b>TOTAL OTHER NONCURRENT ASSETS</b>   | <b>475</b>           | <b>401</b>           |
| <b>TOTAL ASSETS</b>  | <b>\$3,247</b>       | <b>\$3,006</b>       |

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

## Orange and Rockland Utilities, Inc. Consolidated Balance Sheet

| <i>(Millions of Dollars)</i>   | December 31,<br>2020 | December 31,<br>2019 |
|--|----------------------|----------------------|
| <b>LIABILITIES AND SHAREHOLDER'S EQUITY</b>                                |                      |                      |
| <b>CURRENT LIABILITIES</b>   |                      |                      |
| Notes payable  | \$45                 | \$17                 |
| Accounts payable   | 132                  | 88                   |
| Accounts payable to affiliated companies                                   | 16                   | 17                   |
| Customer deposits  | 14                   | 12                   |
| Accrued taxes  | 9                    | 2                    |
| Accrued taxes to affiliated companies                                      | 1                    | 12                   |
| Accrued interest   | 10                   | 9                    |
| Accrued wages  | 10                   | 10                   |
| Fair value of derivative liabilities                                       | 13                   | 12                   |
| Regulatory liabilities   | 24                   | 39                   |
| System benefit charge  | 53                   | 60                   |
| Operating lease liabilities  | 1                    | 1                    |
| Other current liabilities  | 28                   | 32                   |
| <b>TOTAL CURRENT LIABILITIES</b>   | <b>356</b>           | <b>311</b>           |
| <b>NONCURRENT LIABILITIES</b>  |                      |                      |
| Provision for injuries and damages   | 6                    | 5                    |
| Pensions and retiree benefits  | 314                  | 277                  |
| Superfund and other environmental costs                                    | 77                   | 80                   |
| Asset retirement obligations   | 1                    | 3                    |
| Deferred income taxes and unamortized investment tax credits               | 340                  | 316                  |
| Regulatory liabilities   | 410                  | 391                  |
| Operating lease liabilities  | 1                    | 2                    |
| Other deferred credits and noncurrent liabilities                          | 42                   | 41                   |
| <b>TOTAL NONCURRENT LIABILITIES</b>  | <b>1,191</b>         | <b>1,115</b>         |
| <b>LONG-TERM DEBT</b>  | <b>893</b>           | <b>818</b>           |
| <b>COMMON SHAREHOLDER'S EQUITY (See Statement of Shareholder's Equity)</b> | <b>807</b>           | <b>762</b>           |
| <b>TOTAL LIABILITIES AND SHAREHOLDER'S EQUITY</b>                          | <b>\$3,247</b>       | <b>\$3,006</b>       |

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



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

| <i>(In Millions, except share data)</i> | Common Stock |        | Additional<br>Paid-In<br>Capital | Retained<br>Earnings | Accumulated<br>Other<br>Comprehensive<br>Income/(Loss) | Total |
|---|--------------|--------|----------------------------------|----------------------|--|-------|
|   | Shares       | Amount |                                  |                      |  |       |
| BALANCE AS OF DECEMBER 31, 2017         | 1,000        | \$—    | \$324                            | \$362                | \$(20)   | \$666 |
| Net income                              |              |        |                                  | 59                   |  | 59    |
| Common stock dividend to parent         |              |        |                                  | (46)                 |  | (46)  |
| Capital contribution by parent          |              |        | 25                               |                      |  | 25    |
| Other comprehensive income              |              |        |                                  |                      | 8  | 8     |
| BALANCE AS OF DECEMBER 31, 2018         | 1,000        | \$—    | \$349                            | \$375                | \$(12)   | \$712 |
| Net income                              |              |        |                                  | 70                   |  | 70    |
| Common stock dividend to parent         |              |        |                                  | (47)                 |  | (47)  |
| Capital contribution by parent          |              |        | 30                               |                      |  | 30    |
| Other comprehensive loss                |              |        |                                  |                      | (3)  | (3)   |
| BALANCE AS OF DECEMBER 31, 2019         | 1,000        | \$—    | \$379                            | \$398                | \$(15)   | \$762 |
| Net income                              |              |        |                                  | \$71                 |  | 71    |
| Common stock dividend to parent         |              |        |                                  | (49)                 |  | (49)  |
| Capital contribution by parent          |              |        | 25                               |                      |  | 25    |
| Other comprehensive loss                |              |        |                                  |                      | (2)  | (2)   |
| BALANCE AS OF DECEMBER 31, 2020         | 1,000        | \$—    | \$404                            | \$420                | \$(17)   | \$807 |

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

**Orange and Rockland Utilities, Inc.**  
**Consolidated Statement of Capitalization**

| <i>(In Millions, except share data)</i>                            | Shares outstanding<br>December 31, |        | At December 31,        |         |
|--|------------------------------------|--------|------------------------|---------|
|  | 2020                               | 2019   | 2020                   | 2019    |
| TOTAL SHAREHOLDER'S EQUITY (See Statement of Shareholder's Equity) | 1,000                              | 1,000  | \$807                  | \$762   |
| <b>LONG-TERM DEBT (Millions of Dollars)</b>                        |                                    |        | <b>At December 31,</b> |         |
| Maturity   | Interest Rate                      | Series | 2020                   | 2019    |
| DEBENTURES:  |                                    |        |                        |         |
| 2027   | 6.50                               | 1997F  | 80                     | 80      |
| 2029   | 2.94                               | 2019B  | 44                     | 44      |
| 2030   | 2.02                               | 2020A  | 35                     | —       |
| 2039   | 6.00                               | 2009B  | 60                     | 60      |
| 2039   | 3.46                               | 2019C  | 38                     | 38      |
| 2040   | 5.50                               | 2010B  | 115                    | 115     |
| 2045   | 4.95                               | 2015A  | 120                    | 120     |
| 2045   | 4.69                               | 2015B  | 100                    | 100     |
| 2046   | 3.88                               | 2016A  | 75                     | 75      |
| 2048   | 4.35                               | 2018A  | 125                    | 125     |
| 2048   | 4.35                               | 2018B  | 25                     | 25      |
| 2049   | 3.73                               | 2019A  | 43                     | 43      |
| 2050   | 3.24                               | 2020B  | 40                     | —       |
| TOTAL DEBENTURES   |                                    |        | 900                    | 825     |
| Unamortized debt expense   |                                    |        | (6)                    | (6)     |
| Unamortized debt discount  |                                    |        | (1)                    | (1)     |
| TOTAL  |                                    |        | 893                    | 818     |
| Less: Long-term debt due within one year                           |                                    |        | —                      | —       |
| TOTAL LONG-TERM DEBT   |                                    |        | 893                    | 818     |
| TOTAL CAPITALIZATION   |                                    |        | \$1,700                | \$1,580 |

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

## Notes to the Consolidated Financial Statements

### General

These notes accompany and form an integral part of the consolidated financial statements of Orange and Rockland Utilities, Inc., a New York corporation, and its subsidiaries (the Company or O&R). The Company is a regulated utility, the equity of which is owned entirely by Consolidated Edison, Inc. (Con Edison). O&R has one regulated utility subsidiary: Rockland Electric Company (RECO). For the years ended December 31, 2020, 2019 and 2018, operating revenues for RECO were 20.6 percent, 19.7 percent, and 20.2 percent, respectively, of O&R's consolidated operating revenues. O&R, along with RECO, provides electric service in southeastern New York and adjacent areas of northern New Jersey and gas service in southeastern New York.

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

The Company has, pursuant to the accounting rules for subsequent events, evaluated events or transactions that occurred after December 31, 2020 through the posting on its website (March 12, 2021) of the Annual Financial Statements for potential recognition or disclosure in the consolidated financial statements.

### Note A – Summary of Significant Accounting Policies

#### Principles of Consolidation

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

#### Accounting Policies

The accounting policies of the Company conform to generally accepted accounting principles in the United States of America (GAAP). For the Company, these accounting policies include the accounting rules for regulated operations and the accounting requirements of the Federal Energy Regulatory Commission (FERC) and the state regulators having jurisdiction.

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

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

## Notes to the Consolidated Financial Statements - continued

Company is not receiving or being credited with a return on its regulatory asset for RECO's deferred storm costs. The Company's regulatory assets and liabilities at December 31, 2020 are recoverable from customers, or to be applied for customer benefit, in accordance with rate provisions that have been approved by state regulators.

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

### Financial Instruments – Credit Losses

#### Adoption of New Standard

In January 2020, the Company adopted Accounting Standards Update (ASU) 2016-13, "Financial Instruments-Credit Losses (Topic 326): Measurement of Credit Losses on Financial Instruments." The amendments replace the incurred loss impairment methodology which involved delayed recognition of credit losses. The amendments introduce an expected credit loss impairment model which requires immediate recognition of anticipated losses over the instrument's life. A broader range of reasonable and supportable information must be considered in developing the credit loss estimates. The Company's financial instruments subject to the amendments are included in the lines "Accounts receivable - customers" and "Other receivables". Substantially all of these in-scope financial instruments are expected to be collected within one year of billing.

The Company adopted the amendments using the modified retrospective method for all financial instruments measured at amortized costs. Results for reporting periods beginning after January 1, 2020 are presented under Accounting Standards Codification (ASC) 326 while prior period amounts continue to be reported in accordance with previously applicable GAAP. No prior period adjustment or charge to retained earnings for cumulative impact was required as a result of the Company's adoption of the amendments.

#### Allowance for Uncollectible Accounts

The Company's "Account receivable - customers" balance consists of utility bills due (bills are generally due the month following billing) from customers who have energy delivered, generated, or services provided by the Company. The balance also reflects the Company's purchase of receivables from energy service companies to support the retail choice programs.

"Other receivables" balance generally reflects costs billed by the Company for goods and services provided to external parties, such as accommodation work for private parties and certain governmental entities, real estate rental and pole attachments.

The Company develops expected loss estimates using past events data and considers current conditions and future reasonable and supportable forecasts. Changes to the Company's reserve balances that result in write-offs of customer accounts receivable balances above existing rate allowances are not reflected in rates during the term of the current rate plans. For the Company's customer accounts receivable allowance for uncollectible accounts, past events considered include write-offs relative to customer accounts receivable; current conditions include macro-and micro-economic conditions related to trends in the local economy, bankruptcy rates and

## Notes to the Consolidated Financial Statements - continued

aged customer accounts receivable balances, among other factors; and forecasts about the future include assumptions related to the level of write-offs and recoveries. Generally, the Company writes off customer accounts receivable as uncollectible 90 days after the account is turned off for non-payment, or the account is closed during the collection process. See "COVID-19 Regulatory Matters" in Note B.

Other receivables allowance for uncollectible accounts is calculated based on a historical average of collections relative to total other receivables, including current receivables. Current macro- and micro-economic conditions are also considered when calculating the current reserve. Probable outcomes of pending litigation, whether favorable or unfavorable to the Company, are also included in the consideration.

During the year of 2020, the potential economic impact of the COVID-19 pandemic was also considered in forward-looking projections related to write-off and recovery rates and resulted in increases to the allowance for uncollectible accounts. The increase to the allowance for customer uncollectible accounts was \$4.1 million for the year ended December 31, 2020.

Customer accounts receivable and the associated allowance for uncollectible accounts are included in the line "Accounts receivable – customers" on the Company's consolidated balance sheet. Other receivables and the associated allowance for uncollectible accounts are included in "Other receivables" on the consolidated balance sheet.

The table below presents a rollforward by major portfolio segment type for the year ended December 31, 2020:

| <i>(Millions of Dollars)</i>         | Accounts<br>receivable -<br>customers | Other<br>receivables |
|--------------------------------------|---------------------------------------|----------------------|
| Allowance for credit losses          |                                       |                      |
| Beginning Balance at January 1, 2020 | \$4.6                                 | \$1.4                |
| Recoveries                           | 1.5                                   | 0.1                  |
| Write-offs                           | (3.7)                                 | (1.0)                |
| Reserve adjustments                  | 6.3                                   | 1.9                  |
| Ending Balance at December 31, 2020  | \$8.7                                 | \$2.4                |

### Revenues

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

The NYSPSC requires utilities to record gross receipts tax revenues and expenses on a gross income statement presentation basis (i.e., included in both revenue and expense). The recovery of these taxes is generally provided for in the revenue requirement within each of the respective NYSPSC-approved rate plans. Total excise taxes (inclusive of gross receipts taxes) recorded in operating revenues were \$11.3 million, \$10.9 million, and \$12.1 million, in 2020, 2019 and 2018, respectively.

## Notes to the Consolidated Financial Statements - continued

### Plant and Depreciation

#### Utility Plant

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

Rates used for AFUDC include the cost of borrowed funds and a reasonable rate of return on the Company's own funds when so used, determined in accordance with regulations of the FERC or the state public utility regulatory authority having jurisdiction. The rate is compounded semiannually, and the amounts applicable to borrowed funds are treated as a reduction of interest charges, while the amounts applicable to the Company's own funds are credited to other income (deductions). The AFUDC rates for the Company were 5.3 percent, 5.3 percent and 2.2 percent for 2020, 2019 and 2018, respectively.

The Company generally computes annual charges for depreciation using the straight-line method for financial statement purposes, with rates based on average service lives and net salvage factors. The average depreciation rates for the Company were 3.2 percent for 2020, 3.0 percent for 2019 and 2.9 percent for 2018.

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

At December 31, 2020 and 2019, the capitalized cost of the Company's utility plant, net of accumulated depreciation, was as follows:

| <i>(Millions of Dollars)</i>  | 2020    | 2019    |
|-------------------------------|---------|---------|
| Electric                      |         |         |
| Transmission                  | \$290   | \$254   |
| Distribution                  | 1,115   | 1,074   |
| Gas (a)                       | 681     | 655     |
| General                       | 221     | 222     |
| Held for future use           | 8       | 8       |
| Construction work in progress | 154     | 123     |
| Net Utility Plant             | \$2,469 | \$2,336 |

(a) Primarily distribution

General utility plant included \$5 million at December 31, 2020 and 2019, related to a May 2018 acquisition of software licenses. The estimated aggregate annual amortization expense related to the software licenses is immaterial. The accumulated amortization was \$1 million at December 31, 2020 and December 31, 2019.

Under O&R's rate plans, the aggregate annual depreciation allowance for the period ended December 31, 2020 was \$90 million.

## Notes to the Consolidated Financial Statements - continued

### Prepayments and Other Deferred Charges and Noncurrent Assets

Prepayments and Other deferred charges and noncurrent assets of O&R, net of accumulated depreciation, included \$1 million and \$3 million, respectively at December 31, 2020, related to implementation costs incurred in cloud computing arrangements. The amounts recorded in 2019 were not material. Depreciation on these assets is computed using the straight-line method for financial statement purposes over their estimated useful lives. Depreciation expense related to these assets incurred during the year ended December 31, 2020 was \$1 million. Accumulated depreciation related to these assets was \$2 million at December 31, 2020 and was not material at December 31, 2019.

### Long-Lived Assets

The Company tests the impairment of long-lived assets, based on projections of undiscounted future cash flows, whenever events or changes in circumstances indicate that the carrying amounts of such assets may not be recoverable. In the event a test indicates that such cash flows cannot be expected to be sufficient to fully recover the assets, the assets are considered impaired and written down to their estimated fair value. No impairment charges on long-lived assets were recognized in 2020, 2019 or 2018.

### 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 regulators. 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 and costs of its electric demand management programs 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 independent system operator, PJM Interconnection LLC (PJM). Basic Generation Service rates are adjusted to conform to contracted prices when new contracts take effect and differences between actual monthly costs and revenues are reconciled and charged or credited to customers on a two-month lag.

## Notes to the Consolidated Financial Statements - continued

### **New York Independent System Operator (NYISO)**

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

### **Temporary Cash Investments**

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

### **Investments**

Investments are recorded at fair value and include the Company's supplemental retirement plan assets.

### **Pension and Other Postretirement Benefits**

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

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

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

In accordance with the Statement of Policy issued by the NYSPSC and its current electric and gas rate plans, O&R defers for payment to or recovery from customers the difference between such expenses for the



## Notes to the Consolidated Financial Statements - continued

Company's New York business and the amounts for such expenses reflected in O&R's rates. RECO's rate plan does not have comparable deferral provisions for retirement benefits. See Note B.

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

### Federal Income Tax

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

Upon enactment of the Tax Cuts and Jobs Act of 2017 on December 22, 2017 (the TCJA), O&R re-measured its deferred tax assets and liabilities based upon the 21 percent corporate income tax rate under the TCJA. The tax effects of changes in tax laws are to be recognized in the period in which the law is enacted and deferred tax assets and liabilities are to be re-measured at the enacted tax rate expected to apply when temporary differences are to be realized or settled. For O&R, in accordance with its New York rate plans and the accounting rules for regulated operations, the change in deferred taxes was recorded as either an offset to a regulatory asset or a regulatory liability. See "Other Regulatory Matters" and "Regulatory Assets and Liabilities" in Note B and Note I.

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

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

## Notes to the Consolidated Financial Statements - continued

### State Income Tax

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

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

### Reclassification

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

### Estimates

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

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

Changes to accumulated OCI are as follows:

| <i>(Millions of Dollars)</i>  |        |
|---|--------|
| Accumulated OCI, net of taxes, at December 31, 2017 (a)   | \$(20) |
| OCI before reclassifications, net of taxes of \$2   | 3      |
| Amounts reclassified from accumulated OCI related to pension plan liabilities, net of tax of \$(2) (a)(b) | 5      |
| Total OCI, net of taxes, at December 31, 2018   | 8      |
| Accumulated OCI, net of taxes, at December 31, 2018 (a)   | \$(12) |
| OCI before reclassifications, net of tax of \$(5)   | (7)    |
| Amounts reclassified from accumulated OCI related to pension plan liabilities, net of tax of \$(1)(a)(b)  | 4      |
| Total OCI, net of taxes, at December 31, 2019   | (3)    |
| Accumulated OCI, net of taxes, at December 31, 2019 (a)   | \$(15) |
| OCI before reclassifications, net of tax of \$3   | (7)    |
| Amounts reclassified from accumulated OCI related to pension plan liabilities, net of tax of \$(2)(a)(b)  | 5      |
| Total OCI, net of taxes, at December 31, 2020   | (2)    |
| Accumulated OCI, net of taxes, at December 31, 2020 (a)   | \$(17) |

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

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

### Note B – Regulatory Matters

#### Rate Plans

The Company provides service to New York customers according to the terms of tariffs approved by the NYS PSC. Tariffs for service to customers of RECO, the Company's New Jersey regulated utility subsidiary, are approved by the New Jersey Board of Public Utilities (NJ BPU). The tariffs include schedules of rates for service

## Notes to the Consolidated Financial Statements - continued

that limit the rates charged by the Company to amounts that recover from its customers costs approved by the regulator, including capital costs, of providing service to customers as defined by the tariff. The tariffs implement rate plans adopted by state utility regulators in rate orders issued at the conclusion of rate proceedings.

Pursuant to the Company's rate plans, there generally can be no change to the charges to customers during the respective terms of the rate plans other than specified adjustments provided for in the rate plans. The Company's rate plans each cover specified periods, but rates determined pursuant to a plan generally continue in effect until a new rate plan is approved by the state utility regulator.

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

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

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

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

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

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

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

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

## Notes to the Consolidated Financial Statements - continued

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

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

## Notes to the Consolidated Financial Statements - continued

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

| <b>O&amp;R New York – Electric</b>                                 |  |  |
|--|--|--|
| Effective period   | November 2015 - October 2017 (a)   | January 2019 – December 2021 (d)   |
| Base rate changes  | Yr. 1 – \$9.3 million<br>Yr. 2 – \$8.8 million<br>Yr. 3 – None   | Yr. 1 – \$13.4 million (e)<br>Yr. 2 – \$8.0 million (e)<br>Yr. 3 – \$5.8 million (e)   |
| Amortizations to income of net regulatory (assets) and liabilities | Yr. 1 – \$(8.5) million (b)<br>Yr. 2 – \$(9.4) million (b)<br>Yr. 3 – None   | Yr. 1 – \$(1.5) million (f)<br>Yr. 2 – \$(1.5) million (f)<br>Yr. 3 – \$(1.5) million (f)  |
| Other revenue sources  |  | <p>Potential earnings adjustment mechanism incentives for peak reduction, energy efficiency, Distributed Energy Resources utilization and other potential incentives of up to:</p> <p>Yr. 1 - \$3.6 million<br/>Yr. 2 - \$4.0 million<br/>Yr. 3 - \$4.2 million</p> <p>Potential incentive if performance target related to customer service is met: \$0.5 million annually.</p> <p>In 2019 and 2020, the company recorded \$2.6 million and \$1.9 million of earnings adjustment mechanism incentives for energy efficiency, respectively. In 2019 and 2020, the company recorded \$0.2 million and \$0.5 million of incentives for customer service, respectively.</p> |
| Revenue decoupling mechanisms                                      | In 2015, 2016, 2017 and 2018, the company deferred for the customer's benefit an immaterial amount, \$6.3 million as regulatory liabilities, \$11.2 million as regulatory asset and \$0.5 million as regulatory asset, respectively.   | <p>Continuation of reconciliation of actual to authorized electric delivery revenues.</p> <p>In 2019 and 2020, the company deferred \$0.1 million and \$6 million as regulatory assets.</p>  |
| Recoverable energy costs   | Continuation of current rate recovery of purchased power costs.  | Continuation of current rate recovery of purchased power costs.  |
| Negative revenue adjustments                                       | Potential charges (up to \$4 million annually) if certain performance targets are not met. In 2015 the company recorded \$1.25 million in negative revenue adjustments. In 2016, 2017 and 2018, the company did not record any negative revenue adjustments.                             | <p>Potential charges if certain performance targets relating to service, reliability and other matters are not met:</p> <p>Yr. 1 - \$4.4 million<br/>Yr. 2 - \$4.4 million<br/>Yr. 3 - \$4.5 million</p> <p>In 2019 and 2020, the company did not record any negative revenue adjustments.</p>   |
| Cost reconciliations   | In 2015, 2016 and 2017, the company deferred \$0.3 million, \$7.4 million and \$3.2 million as net decreases to regulatory assets, respectively. In 2018, the company deferred \$5 million as a net regulatory asset.  | <p>Reconciliation of expenses for pension and other postretirement benefits, environmental remediation costs, property taxes (g), energy efficiency program (h), major storms, the impact of new laws and certain other costs to amounts reflected in rates. (i)</p> <p>In 2019 and 2020, the company deferred \$4.3 million and \$30.3 million as a net regulatory assets.</p>  |
| Net utility plant reconciliations                                  | <p>Target levels reflected in rates are:</p> <p>Yr. 1 – \$928 million (c)<br/>Yr. 2 – \$970 million (c)</p> <p>The company increased/(reduced) its regulatory asset by \$2.2 million, \$(1.9) million, \$(1.9) million and \$1.4 million in 2015, 2016, 2017 and 2018, respectively.</p> | <p>Target levels reflected in rates were:</p> <p>Electric average net plant target excluding advanced metering infrastructure (AMI):</p> <p>Yr. 1 - \$1,008 million<br/>Yr. 2 - \$1,032 million<br/>Yr. 3 - \$1,083 million</p> <p>AMI (j):</p> <p>Yr. 1 - \$48 million<br/>Yr. 2 - \$58 million<br/>Yr. 3 - \$61 million</p> <p>The company increased regulatory asset by an immaterial amount in 2019 and deferred \$0.4 million as a regulatory liability in 2020.</p>  |
| Average rate base  | Yr. 1 – \$763 million<br>Yr. 2 – \$805 million<br>Yr. 3 – \$805 million  | Yr. 1 – \$878 million<br>Yr. 2 – \$906 million<br>Yr. 3 – \$948 million  |
| Weighted average cost of capital (after-tax)                       | Yr. 1 – 7.10 percent<br>Yr. 2 – 7.06 percent<br>Yr. 3 – 7.06 percent   | Yr. 1 – 6.97 percent<br>Yr. 2 – 6.96 percent<br>Yr. 3 – 6.96 percent   |
| Authorized return on common equity                                 | 9.0 percent  | 9.0 percent  |

## Notes to the Consolidated Financial Statements - continued

|                                    |   |  |
|------------------------------------|---|--|
| Actual return on common equity (k) | Yr. 1 – 10.8 percent<br>Yr. 2 – 9.7 percent<br>Yr. 3 – 7.2 percent  | Yr. 1 – 9.60 percent<br>Yr. 2 – 8.76 percent   |
| Earnings sharing                   | Most earnings above an annual earnings threshold of 9.6 percent are to be applied to reduce regulatory assets. In 2015, earnings did not exceed the earnings threshold. Actual earnings were \$6.1 million, \$0.3 million above the threshold for 2016 and 2017, respectively. In 2018, earnings did not exceed the earnings threshold. | Most earnings above an annual earnings threshold of 9.6 percent are to be applied to reduce regulatory assets for environmental remediation and other costs accumulated in the rate year.<br><br>In 2019 and 2020, earnings did not exceed the earnings threshold. |
| Cost of long-term debt             | Yr. 1 – 5.42 percent<br>Yr. 2 – 5.35 percent<br>Yr. 3 – 5.35 percent  | Yr. 1 – 5.17 percent<br>Yr. 2 – 5.14 percent<br>Yr. 3 – 5.14 percent   |
| Common equity ratio                | 48 percent  | 48 percent   |

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

In January 2021, O&R filed a request with the NYSPSC for an increase in the rates it charges for electric service rendered in New York, effective January 1, 2022, of \$24.5 million. The filing reflects a return on common equity of 9.5 percent and a common equity ratio of 50 percent. The filing proposes continuation of the provisions with respect to recovery from customers of the cost of purchased power, and the reconciliation of actual expenses allocable to the electric business to the amounts for such costs reflected in electric rates for storm costs, pension and other postretirement benefit costs, environmental remediation and property taxes.

## Notes to the Consolidated Financial Statements - continued

### O&R New York – Gas

| Effective period  | November 2015 – October 2018 (a)  | January 2019 – December 2021 (d)   |
|---|---|--|
| Base rate changes   | Yr. 1 – \$16.4 million<br>Yr. 2 – \$16.4 million<br>Yr. 3 – \$5.8 million<br>Yr. 3 – \$10.6 million collected through a surcharge   | Yr. 1 – \$(7.5) million (e)<br>Yr. 2 – \$3.6 million (e)<br>Yr. 3 – \$0.7 million (e)  |
| Amortization to income of net regulatory (assets) and liabilities | Yr. 1 – \$(1.7) million (b)<br>Yr. 2 – \$(2.1) million (b)<br>Yr. 3 – \$(2.5) million (b)   | Yr. 1 – \$1.8 million (f)<br>Yr. 2 – \$1.8 million (f)<br>Yr. 3 – \$1.8 million (f)  |
| Other revenue sources   |   | Continuation of retention of annual revenues from non-firm customers of up to \$4.0 million, with variances to be shared 80 percent by customers and 20 percent by company.<br><br>Potential earnings adjustment mechanism incentives of up to \$0.3 million annually.<br><br>Potential incentives if performance targets related to gas leak backlog, leak prone pipe, emergency response, damage prevention and customer service are met: Yr. 1 - \$1.2 million; Yr. 2 - \$1.3 million; and Yr. 3 - \$1.3 million.<br><br>In 2019 and 2020, the company recorded \$0.3 million of earnings adjustment mechanism incentives for energy efficiency. In 2019 and 2020, the company recorded \$0.7 million and \$0.5 million of positive incentives, respectively. |
| Revenue decoupling mechanisms                                     | In 2015, 2016, 2017 and 2018, the company deferred \$0.8 million of regulatory assets, \$6.2 million of regulatory liabilities, \$1.7 million of regulatory liabilities and \$6.3 million of regulatory liabilities, respectively.  | Continuation of reconciliation of actual to authorized gas delivery revenues.<br><br>In 2019 and 2020, the company deferred \$0.8 million and \$0.5 million of regulatory assets, respectively.  |
| Recoverable energy costs  | Current rate recovery of purchased gas costs.   | Continuation of current rate recovery of purchased gas costs.  |
| Negative revenue adjustments                                      | Potential charges (up to \$3.7 million in Yr. 1, \$4.7 million in Yr. 2 and \$4.9 million in Yr. 3) if certain performance targets are not met. In 2015, 2016 and 2017, the company did not record any negative revenue adjustments. In 2018, the company recorded a \$0.1 million negative revenue adjustment.     | Potential charges if performance targets relating to service, safety and other matters are not met: Yr. 1 - \$5.5 million; Yr. 2 - \$5.7 million; and Yr. 3 - \$6.0 million.<br><br>In 2019 and 2020, the company recorded a \$0.2 million and an immaterial amount of negative revenue adjustments, respectively.   |
| Cost reconciliations  | In 2015 and 2016, the company deferred \$4.5 million and \$6.6 million as net regulatory liabilities and assets, respectively. In 2017 and 2018, the company deferred \$3.5 million and \$7.4 million as net regulatory liabilities, respectively.  | Reconciliation of expenses for pension and other postretirement benefits, environmental remediation costs, property taxes (g), energy efficiency program (h), the impact of new laws and certain other costs to amounts reflected in rates. (i)<br><br>In 2019 and 2020, the company deferred \$6 million as net regulatory liabilities and \$1.8 million as net regulatory assets, respectively.  |
| Net utility plant reconciliations                                 | Target levels reflected in rates are:<br>Yr. 1 – \$492 million (c)<br>Yr. 2 – \$518 million (c)<br>Yr. 3 – \$546 million (c)<br>No deferral was recorded for 2015 and immaterial amounts were recorded as regulatory liabilities in 2016 and 2017. In 2018, the company deferred \$0.4 million as regulatory asset. | Target levels reflected in rates were:<br>Gas average net plant target excluding AMI:<br>Yr. 1 - \$593 million<br>Yr. 2 - \$611 million<br>Yr. 3 - \$632 million<br>AMI (j):<br>Yr. 1 - \$20 million<br>Yr. 2 - \$24 million<br>Yr. 3 - \$25 million<br><br>In 2019 and 2020, the company deferred immaterial amounts as regulatory assets.  |
| Average rate base   | Yr. 1 – \$366 million<br>Yr. 2 – \$391 million<br>Yr. 3 – \$417 million   | Yr. 1 – \$454 million<br>Yr. 2 – \$476 million<br>Yr. 3 – \$498 million  |
| Weighted average cost of capital (after-tax)                      | Yr. 1 – 7.10 percent<br>Yr. 2 – 7.06 percent<br>Yr. 3 – 7.06 percent  | Yr. 1 – 6.97 percent<br>Yr. 2 – 6.96 percent<br>Yr. 3 – 6.96 percent   |
| Authorized return on common equity                                | 9.0 percent   | 9.0 percent  |
| Actual return on common equity (k)                                | Yr. 1 – 11.2 percent<br>Yr. 2 – 9.7 percent<br>Yr. 3 – 8.1 percent  | Yr. 1 – 8.90 percent<br>Yr. 2 – 9.58 percent   |

## Notes to the Consolidated Financial Statements - continued

|                        |   |   |
|------------------------|---|---|
| Earnings sharing       | Most earnings above an annual earnings threshold of 9.6 percent are to be applied to reduce regulatory assets. In 2015, earnings did not exceed the earnings threshold. Actual earnings were \$4 million, \$0.2 million above the threshold for 2016 and 2017, respectively. In 2018, earnings did not exceed the earnings threshold. | Most earnings above an annual earnings threshold of 9.6 percent are to be applied to reduce regulatory assets for environmental remediation and other costs accumulated in the rate year. In 2019 and 2020, earnings did not exceed the earnings threshold. |
| Cost of long-term debt | Yr. 1 – 5.42 percent<br>Yr. 2 – 5.35 percent<br>Yr. 3 – 5.35 percent  | Yr. 1 – 5.17 percent<br>Yr. 2 – 5.14 percent<br>Yr. 3 – 5.14 percent  |
| Common equity ratio    | 48 percent  | 48 percent  |

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

In January 2021, O&R filed a request with the NYSPSC for an increase in the rates it charges for gas service rendered in New York, effective January 1, 2022, of \$9.8 million. The filing reflects a return on common equity of 9.5 percent and a common equity ratio of 50 percent. The filing proposes continuation of the provisions with respect to recovery from customers of the cost of purchased gas, and the reconciliation of actual expenses allocable to the gas business to the amounts for such costs reflected in gas rates for pension and other postretirement benefit costs, environmental remediation and property taxes.



## Notes to the Consolidated Financial Statements - continued

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

| <b>RECO</b>   |  |   |
|---|--|---|
| Effective period  | March 2017 – January 2020  | February 2020                                   |
| Base rate changes   | Yr. 1 – \$1.7 million  | Yr. 1 – \$12 million                            |
| Amortization to income of net regulatory (assets) and liabilities | \$0.2 million over three years and continuation of \$(25.6) million of deferred storm costs over four years which expired on July 31, 2018 (a) | \$4.8 million over four years.                  |
| Recoverable energy costs  | Current rate recovery of purchased power costs.  | Current rate recovery of purchased power costs. |
| Cost reconciliations  | None   | None  |
| Average rate base   | Yr. 1 – \$178.7 million  | Yr. 1 – \$229.9 million                         |
| Weighted average cost of capital (after-tax)                      | 7.47 percent   | 7.11 percent                                    |
| Authorized return on common equity                                | 9.6 percent  | 9.5 percent                                     |
| Actual return on common equity                                    | Yr. 1 – 7.5 percent<br>Yr. 2 – 5.7 percent   | Yr. 1 – 5.4 percent                             |
| Cost of long-term debt  | 5.37 percent   | 4.88 percent                                    |
| Common equity ratio   | 49.7 percent   | 48.32 percent                                   |

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

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

### COVID-19 Regulatory Matters

Governors, public utility commissions and other regulatory agencies in the states in which O&R and RECO operate have issued orders related to the COVID-19 pandemic that impact the companies as described below.

### New York State Regulation

In March 2020, New York State Governor Cuomo declared a State Disaster Emergency for the State of New York, due to the COVID-19 pandemic and signed the "New York State on PAUSE" executive order that closed all non-essential businesses statewide. New York State designated utilities, including O&R, as essential businesses that were able to continue a portion of their work during the effectiveness of the PAUSE order. In May 2020, the "New York Forward" plan went into effect. New York Forward is a phased plan to reopen businesses in geographic areas of New York State that meet metrics established by various public health organizations. In October 2020, Governor Cuomo announced a new cluster action initiative to address COVID-19 hotspots that have arisen in various areas of New York within the Company's service territory and to impose new rules and restrictions targeted to areas with the highest concentration of COVID-19 cases and the surrounding communities. As a result of these COVID-19 clusters, the Company has limited its work in customer premises in the impacted areas to only address emergency, safety-related and selected service connections requested by customers. Since the emergency declaration, and due to economic conditions, the NYSPSC and O&R have worked to mitigate the potential impact of the COVID-19 pandemic on the Company, their customers and other stakeholders.

## Notes to the Consolidated Financial Statements - continued

In March 2020, the Company began suspending service disconnections, certain collection notices, final bill collection agency activity, new late payment charges and certain other fees for all customers. The Company also began providing payment extensions for all customers that were scheduled to be disconnected prior to the start of the COVID-19 pandemic. In June 2020, the state of New York enacted a law prohibiting New York utilities, including O&R, from disconnecting residential customers during the COVID-19 state of emergency. In addition, such prohibition will apply for an additional 180 days after the state of emergency ends for residential customers who have experienced a change in financial circumstances due to the COVID-19 pandemic. The law expires on March 31, 2021, although legislation has been introduced to extend the expiration date until December 31, 2021 or later. For the year ended December 31, 2020, the estimated foregone revenues that were not collected by O&R were \$3.4 million (see Note J). Also in March 2020, the Company requested and the NYS PSC granted an extension to file its 2019 Earnings Adjustment Mechanisms (EAMs) report, which was filed in July 2020. The earned EAM incentives of approximately \$3 million are being recovered from customers over a twelve-month period that began September 2020.

The Company's New York rate plans allow it to defer costs resulting from a change in legislation, regulation and related actions that have taken effect during the term of the rate plans once the costs exceed a specified threshold. For the year ended December 31, 2020, the reserve increases to the allowance for uncollectible accounts associated with the COVID-19 pandemic for O&R electric operations were \$2 million and were deferred pursuant to the legislative, regulatory and related actions provisions of the New York electric rate plan as a result of the New York State on PAUSE and related executive orders. The reserve increase to the allowance for uncollectible accounts associated with the COVID-19 pandemic for O&R's gas operations of \$1 million did not meet the deferral threshold at December 31, 2020. The Company's New York rate plans also provide for an allowance for write-offs of customer accounts receivable balances. The above amount deferred pursuant to the legislative, regulatory and related actions provisions were reduced by the amount that the actual write-offs of customer accounts receivable balances were below the allowance reflected in rates (due to the New York State on PAUSE and related executive orders), which difference was \$1 million for O&R for the year ended December 31, 2020.

In June 2020, the NYS PSC established a generic proceeding on the impacts of the COVID-19 pandemic and sought comment on a variety of COVID-19 related issues. In July 2020, the Company submitted joint comments with other large utilities in New York State that included a formal request to defer all COVID-19 related costs and for a surcharge mechanism to collect such deferrals based upon the individual utility's need. In January 2021, NYS PSC staff provided guidance to New York utilities that no additional mechanisms are required because there are already established mechanisms for utility recovery of unexpected material expenses through rate plan change in legislation, regulation and related actions provisions and the filing of individual deferral petitions. The guidance further provided that utilities deferring COVID-19 related costs pursuant to the provisions that allow deferral of costs resulting from a change in legislation, regulation and related actions must comply with the provisions of their rate plans, be able to demonstrate the nexus between the changes in law or regulation and the specific revenue and expense items, and consider any offsetting cost savings due to the pandemic.

## Notes to the Consolidated Financial Statements - continued

In February 2021, the NYSPSC staff issued its report on New York State's Energy Affordability Policy that provides recommendations to large New York utilities, including O&R. The report recommends, among other things, that residential and commercial customers' late payment fees and interest on deferred payment agreements be waived until two years after the expiration of the New York State moratorium on utility terminations (the moratorium currently expires on March 31, 2021, although legislation has been introduced to extend the expiration to December 31, 2021 or later) and each utility develop an arrears management program to mitigate the financial burdens of the COVID-19 pandemic on New York households and that program costs be shared, perhaps equally, between shareholders and customers. The NYSPSC staff has requested that the utilities and interested parties comment on the report prior to staff submitting the recommendations to the NYSPSC for consideration.

The Company's rate plans have revenue decoupling mechanisms in its New York electric and gas businesses that reconcile actual energy delivery revenues to the authorized delivery revenues approved by the NYSPSC per month and accumulate the deferred balances annually under O&R New York's electric and gas rate plans (January through December). The difference is accrued with interest each month for O&R New York's electric customers and after the annual deferral period ends for O&R New York's gas customers for refund to, or recovery from customers, as applicable. Generally, the refund to or recovery from customers begins February of each year over an ensuing twelve-month period for O&R New York's electric and gas customers.

### **New Jersey State Regulation**

In March 2020, New Jersey Governor Murphy declared a Public Health Emergency and State of Emergency for the State of New Jersey. Since that declaration, the NJBPU and RECO have worked to mitigate the potential impact of the COVID-19 pandemic on RECO, its customers and other stakeholders. In March 2020, RECO began suspending late payment charges, terminations for non-payment, and no access fees during the COVID-19 pandemic. The suspension of these fees is not expected to be material.

In July 2020, the NJBPU authorized RECO and other New Jersey utilities to create a COVID-19-related regulatory asset by deferring prudently incurred incremental costs related to the COVID-19 pandemic beginning on March 9, 2020, and through the later of September 30, 2021, or 60 days after the emergency declaration is no longer in effect. RECO deferred net incremental COVID-19 related costs of \$0.5 million through December 31, 2020.

### **Other Regulatory Matters**

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

## Notes to the Consolidated Financial Statements - continued

In January 2018, the NYSPSC issued an order initiating a focused operations audit of the income tax accounting of certain utilities, including O&R. The Company is unable to estimate the amount or range of its possible loss related to this matter. At December 31, 2020, the Company had not accrued a liability related to this matter.

In March 2018, Winter Storms Riley and Quinn caused damage to the Company's electric distribution systems and interrupted service to approximately 93,000 O&R customers and 44,000 RECO customers. At December 31, 2020, O&R and RECO costs related to 2018 storms amounted to \$43 million and \$17 million, respectively, most of which were deferred as regulatory assets pursuant to their electric rate plans. In January 2019, O&R began recovering its deferred storm costs over a six-year period in accordance with its New York electric rate plan. In February 2020, RECO began recovering its deferred storm costs over a four-year period in accordance with its New Jersey electric rate plan. The NYSPSC investigated the preparation and response to the storms by O&R, and other New York electric utilities, including all aspects of their emergency response plans. In April 2019, following the issuance of a NYSPSC staff report on the investigation, the NYSPSC ordered the utilities to show cause why the NYSPSC should not commence a penalty action against them for violating their emergency response plans. During 2020, O&R accrued \$0.85 million related to this matter. In August 2020, the NYSPSC approved a July 2020 settlement agreement that provides for the Company to set aside \$0.85 million for the benefit of its electric customers.

In August 2020, Tropical Storm Isaias caused significant damage to the Company's electric distribution systems and interrupted service to approximately 200,000 O&R electric customers. As of December 31, 2020, O&R incurred costs for Tropical Storm Isaias of \$34 million (including \$26 million of operation and maintenance expenses charged against a storm reserve pursuant to its New York electric rate plan and \$8 million of capital expenditures). The Company's electric rate plan provides for recovery of operating costs and capital expenditures under different provisions. The Company's incremental operating costs attributable to storms are to be deferred for recovery as a regulatory asset under its electric rate plan, while capital expenditures, up to specified levels, are reflected in rates under their electric rate plan. In addition, as of December 31, 2020, O&R incurred costs of \$2.9 million for food and medicine spoilage claims. The provisions of the Company's New York electric rate plan that impose negative revenue adjustments for operating performance provide for exceptions for major storms and catastrophic events beyond the control of the Company, including natural disasters such as hurricanes and floods.

In November 2020, the NYSPSC issued an order in its proceedings investigating the New York utilities' preparation for and response to Tropical Storm Isaias that ordered O&R to show cause why (i) civil penalties or appropriate injunctive relief should not be imposed against it (in the amount of up to \$19 million relating to 38 alleged violations) to remedy such noncompliance, and (ii) a prudence proceeding should not be commenced against the Company for potentially imprudent expenditures of ratepayer funds related to the matter. The order stated that given the continuing nature of the investigation of this matter by the New York State Department of Public Service (NYSDPS), the NYSPSC may amend the order to include any subsequently determined apparent violations identified by the NYSDPS. In addition, the order indicated that should the NYSPSC confirm

## Notes to the Consolidated Financial Statements - continued

some or all of the apparent violations identified in the order or other orders issued by the NYSPSC in the future in connection with this proceeding, and should such respective confirmed violations be classified as findings of repeated violations of the Public Service Law or rules or regulations adopted pursuant thereto that demonstrate a failure of O&R to continue to provide safe and adequate service, the NYSPSC would be authorized to commence a proceeding under Public Service Law Section 68(2) to revoke or modify O&R's certificate as it relates to its service territory or any portion thereof.

In December 2020, O&R filed a response to the NYSPSC order demonstrating why the NYSPSC should not commence penalty or prudence actions against it. The Company stated that the NYSPSC order misapplied Section 25-a of the Public Service Law by ignoring the reasonable compliance standard under the statute and instead, was imposing a strict liability standard. O&R also presented evidence that the order either misrepresented the applicable requirements or ignored that the Company was acting pursuant to practices approved by the NYSPSC. Finally, O&R stated that there was no basis to commence a prudence proceeding because the Company acted reasonably based on the information available and the circumstances at the time. The Company has not accrued a liability related to this matter and is unable to determine the outcome of this proceeding at this time.

In October 2020, the NYSPSC issued an order instituting a proceeding to consider requiring New York's large, investor-owned utilities, including O&R, to annually disclose what risks climate change poses to its company, investors and customers going forward. The order notes that some holding companies, including Con Edison, already disclose climate change risks at the holding company level, but states that the NYSPSC believes that climate-related risk disclosures should be issued specific to the operating companies in New York, such as O&R, and that such climate-related risk disclosures should be included annually with the utilities' financial reports. In December 2020, O&R, along with other large New York utilities, filed comments supporting climate change risk disclosures in annual reports filed with the NYSPSC and recommended the use of an industry-specific template.

In May 2020, the president of the United States issued the "Securing the United States Bulk-Power System" executive order. The executive order declares threats to the bulk-power system by foreign adversaries constitute a national emergency and prohibits the acquisition, importation, transfer or installation of certain bulk-power system electric equipment that is sourced from foreign adversaries. The Department of Energy is expected to issue regulations implementing the executive order. In January 2021, the president of the United States suspended the May 2020 executive order for 90 days. The Company is unable to predict the impact on it regulations that may be adopted regarding the bulk-power system.

## Notes to the Consolidated Financial Statements - continued

### Regulatory Assets and Liabilities

Regulatory assets and liabilities at December 31, 2020 and 2019 were comprised of the following items:

| <i>(Millions of Dollars)</i>                        | 2020  | 2019  |
|---|-------|-------|
| Regulatory assets                                   |       |       |
| Unrecognized pension and other postretirement costs | \$176 | \$138 |
| Deferred storm costs (a)                            | 112   | 77    |
| Environmental remediation costs                     | 74    | 85    |
| Pension and other postretirement benefits deferrals | 42    | 23    |
| Revenue taxes                                       | 15    | 14    |
| Property tax reconciliation                         | 2     | 8     |
| Deferred derivative losses                          | 9     | 8     |
| Recoverable energy costs                            | 4     | 5     |
| COVID - 19 Deferrals                                | 2     | —     |
| Other   | 14    | 15    |
| Regulatory assets – noncurrent                      | 450   | 373   |
| Deferred derivative losses                          | 14    | 15    |
| Recoverable energy costs                            | 9     | —     |
| Regulatory assets – current                         | 23    | 15    |
| Total Regulatory Assets                             | \$473 | \$388 |
| Regulatory liabilities                              |       |       |
| Allowance for cost of removal less salvage          | \$158 | \$146 |
| Future federal income tax (b)                       | 137   | 143   |
| Pension and other postretirement benefit deferrals  | 39    | 28    |
| Unrecognized other postretirement costs             | 11    | 9     |
| TCJA net benefits                                   | 9     | 17    |
| Carrying charges on deferred tax liability          | 7     | 11    |
| System benefit charge carrying charge               | 7     | 5     |
| Earnings sharing - electric and gas                 | 5     | 6     |
| Other   | 37    | 26    |
| Regulatory liabilities – noncurrent                 | 410   | 391   |
| Refundable energy costs                             | 24    | 32    |
| Revenue decoupling mechanism                        | —     | 7     |
| Regulatory liabilities – current                    | 24    | 39    |
| Total Regulatory Liabilities                        | \$434 | \$430 |

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

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

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

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

*COVID - 19 Deferrals* represents the amount related to the increase in the allowance for uncollectible accounts resulting from the COVID-19 pandemic and New York State on PAUSE and related executive orders, for electric operations for O&R.

In general, O&R receives or is being credited with a return at the Other Customer-Provided Capital rate for regulatory assets that have not been included in rate base, and receives or is being credited with a return at the

## Notes to the Consolidated Financial Statements - continued

pre-tax weighted average cost of capital once the asset is included in rate base. Similarly, O&R pays to or credits customers with a return at the Other Customer-Provided Capital rate for regulatory liabilities that have not been included in rate base, and pays to or credits customers with a return at the pre-tax weighted average cost of capital once the liability is included in rate base.

In general, O&R is receiving or being credited with a return on its regulatory assets for which a cash outflow has been made (\$187 million and \$130 million at December 31, 2020 and 2019, respectively). Regulatory liabilities are treated in a consistent manner. The Other Customer-Provided Capital rate for the years ended December 31, 2020 and 2019 was 2.65 percent and 4.2 percent, respectively. The recognition of the return on regulatory assets is determined by O&R's rate plans or orders issued by state regulators.

Regulatory assets that represent future financial obligations and were deferred in accordance with O&R's rate plans or orders issued by state regulators do not earn a return until such time as a cash outlay has been made. Regulatory liabilities are treated in a consistent manner. At December 31, 2020 and 2019, regulatory assets for O&R that did not earn a return consisted of the following items:

### Regulatory Assets Not Earning a Return

| <i>(Millions of Dollars)</i>                        | 2020  | 2019  |
|---|-------|-------|
| Regulatory assets                                   |       |       |
| Unrecognized pension and other postretirement costs | \$176 | \$138 |
| Environmental remediation costs                     | 74    | 85    |
| Revenue taxes                                       | 13    | 11    |
| Deferred derivative losses – long term              | 9     | 8     |
| Other   | 1     | 1     |
| Deferred derivative losses – current                | 13    | 15    |
| Total Regulatory Assets                             | \$286 | \$258 |

The recovery periods for regulatory assets for which a cash outflow has not been made and that do not earn a return have not yet been determined, except as noted below, and are expected to be determined pursuant to O&R's future rate plans to be filed or orders issued by the state regulators in connection therewith. O&R recovers unrecognized pension and other postretirement costs over 10 years pursuant to NYSPSC policy.

The deferral for revenue taxes represent the Metropolitan transportation business tax surcharge on the cumulative temporary differences between the book and tax basis of assets and liabilities of O&R, as well as the difference between taxes collected and paid by the Company to fund mass transportation. O&R recovers the majority of the revenue taxes over the remaining book lives of the electric and gas plant assets.

O&R recovers deferred derivative losses – current within one year, and noncurrent generally within three years.

### Note C – Capitalization

#### Common Stock

At December 31, 2020 and 2019, 1,000 shares of the Company's common stock (\$5.00 par value) were outstanding, all of which were owned by Con Edison.

## Notes to the Consolidated Financial Statements - continued

### Dividends

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

### Long-Term Debt

There are no long-term debt maturities for periods 2021-2025.

The carrying amounts and fair values of long-term debt at December 31, 2020 and 2019 are:

| <i>(Millions of Dollars)</i>                   | 2020            |            | 2019            |            |
|--|-----------------|------------|-----------------|------------|
|  | Carrying Amount | Fair Value | Carrying Amount | Fair Value |
| Long-Term Debt (including current portion) (a) | \$893           | \$1,105    | \$818           | \$934      |

(a) Amounts shown are net of unamortized debt expense and unamortized debt discount of \$7 million as of December 31, 2020 and 2019.

Fair values of long-term debt have been estimated primarily using available market information and are classified as Level 2 liabilities (see the fair value hierarchy defined in Note M).

### Significant Debt Covenants

There are no significant debt covenants under the financing arrangements for the debentures of O&R, other than obligations to pay principal and interest when due and covenants not to consolidate with or merge into any other corporation unless certain conditions are met, and no cross-default provisions. The Company was in compliance with its significant debt covenants at December 31, 2020.

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

### Note D – Short-Term Borrowing

In December 2016, O&R, along with Con Edison and Consolidated Edison Company of New York, Inc. (CECONY), entered into a credit agreement (Credit Agreement), under which banks are committed to provide loans and letters of credit on a revolving credit basis. The Credit Agreement, as amended in 2019, expires in December 2023. There is a maximum of \$200 million of credit available to O&R (subject to increase to \$250 million of credit if the necessary regulatory approvals are requested and obtained). The Credit Agreement supports the Company’s commercial paper programs. The Company has not borrowed under the Credit



## Notes to the Consolidated Financial Statements - continued

Agreement. At December 31, 2020 and 2019, O&R had \$45 million and \$17 million of commercial paper outstanding, respectively. The weighted average interest rate at December 31, 2020 and December 31, 2019 was 0.3 percent and 2.0 percent, respectively. At December 31, 2020 and 2019, an immaterial amount of letters of credit were outstanding for O&R under the Credit Agreement.

The banks' commitments under the Credit Agreement are subject to certain conditions, including that there be no event of default. The commitments are not subject to maintenance of credit rating levels or the absence of a material adverse change. Upon a change of control of, or upon an event of default by the Company, the banks may terminate their commitments with respect to the Company, declare any amounts owed by the Company under the Credit Agreement immediately due and payable and require the Company to provide cash collateral relating to the letters of credit issued for it under the Credit Agreement. Events of default include the exceeding at any time of a ratio of consolidated debt to consolidated total capital of 0.65 to 1 (at December 31, 2020 this ratio was 0.54 to 1); having liens on its assets in an aggregate amount exceeding five percent of its consolidated total capital, subject to certain exceptions; the Company or any of its material subsidiaries failing to make one or more payments in respect of material financial obligations (in excess of an aggregate \$150 million of debt or derivative obligations other than non-recourse debt) of the Company; the occurrence of an event or condition which results in the acceleration of the maturity of any material debt (in excess of an aggregate \$150 million of debt other than non-recourse debt) of the Company or enables the holders of such debt to accelerate the maturity thereof; and other customary events of default. Interest and fees charged for the revolving credit facilities and any loans made or letters of credit issued under the Credit Agreement reflect the Company's credit ratings. The Company was in compliance with its covenants at December 31, 2020.

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, Con Edison Transmission, Inc. and certain employees of Con Edison's Clean Energy Businesses, Inc. The plan is designed to comply with the Internal Revenue Code and the Employee Retirement Income Security Act of 1974. Con Edison also maintains additional non-qualified supplemental pension plans.

## Notes to the Consolidated Financial Statements - continued

### Total Periodic Benefit Cost

The components of the Company's total periodic benefit costs for 2020, 2019 and 2018 were as follows:

| <i>(Millions of Dollars)</i>                     | 2020        | 2019        | 2018        |
|--|-------------|-------------|-------------|
| Service cost – including administrative expenses | \$19        | \$16        | \$19        |
| Interest cost on projected benefit obligation    | 34          | 37          | 35          |
| Expected return on plan assets                   | (53)        | (51)        | (53)        |
| Recognition of net actuarial loss                | 37          | 27          | 36          |
| Recognition of prior service costs               | 3           | 2           | 2           |
| <b>TOTAL PERIODIC BENEFIT COST</b>               | <b>\$40</b> | <b>\$31</b> | <b>\$39</b> |
| Cost capitalized                                 | (7)         | (7)         | (8)         |
| Reconciliation to rate level                     | (11)        | (2)         | 8           |
| <b>Total expense recognized</b>                  | <b>\$22</b> | <b>\$22</b> | <b>\$39</b> |

In March 2017, the FASB issued amendments to the guidance for retirement benefits through ASU 2017-07, "Compensation-Retirement Benefits (Topic 715): Improving the Presentation of Net Periodic Pension Cost and Net Periodic Postretirement Benefit Cost." The Company adopted ASU 2017-07 beginning on January 1, 2018. The guidance requires that components of net periodic benefit cost other than service cost be presented outside of operating income on consolidated income statements, and that only the service cost component is eligible for capitalization. Accordingly, the service cost components are included in the line "Other operations and maintenance" and the non-service cost components are included in the line "Other deductions" in the Company's consolidated income statement. In August 2018, the FASB issued amendments to the guidance for retirement benefits through ASU 2018-14, "Compensation-Retirement Benefits (Subtopic 715-20): Disclosure Framework - Changes to the Disclosure Requirements for Defined Benefit Plans." The guidance requires disclosure of the weighted-average interest crediting rate used for cash balance plans for all periods presented, and a narrative description of significant changes in the benefit obligation. The Company adopted ASU 2018-14 for fiscal years ending after December 15, 2020 and the required disclosures are included below and, as applicable, in Note F.

## Notes to the Consolidated Financial Statements - continued

### Funded Status

The funded status at December 31, 2020, 2019 and 2018, as related to O&R, was as follows:

| <i>(Millions of Dollars)</i>                       | 2020           | 2019           | 2018           |
|--|----------------|----------------|----------------|
| <b>CHANGE IN PROJECTED BENEFIT OBLIGATION</b>      |                |                |                |
| Projected benefit obligation at beginning of year  | \$1,035        | \$901          | \$963          |
| Service cost – excluding administrative expenses   | 19             | 16             | 19             |
| Interest cost on projected benefit obligation      | 34             | 37             | 35             |
| Net actuarial (gain)/loss                          | 127            | 115            | (59)           |
| Plan amendments                                    | —              | 15             | —              |
| Benefits paid                                      | (78)           | (49)           | (57)           |
| <b>PROJECTED BENEFIT OBLIGATION AT END OF YEAR</b> | <b>\$1,137</b> | <b>\$1,035</b> | <b>\$901</b>   |
| <b>CHANGE IN PLAN ASSETS</b>                       |                |                |                |
| Fair value of plan assets at beginning of year     | \$810          | \$700          | \$748          |
| Actual return on plan assets                       | 96             | 130            | (28)           |
| Employer contributions                             | 41             | 32             | 39             |
| Benefits paid                                      | (78)           | (49)           | (57)           |
| Administrative expenses                            | (2)            | (3)            | (2)            |
| <b>FAIR VALUE OF PLAN ASSETS AT END OF YEAR</b>    | <b>\$867</b>   | <b>\$810</b>   | <b>\$700</b>   |
| <b>FUNDED STATUS</b>                               | <b>\$(270)</b> | <b>\$(225)</b> | <b>\$(201)</b> |
| Unrecognized net loss                              | \$185          | \$137          | \$125          |
| Unrecognized prior service costs                   | 26             | 30             | 17             |
| Accumulated benefit obligation                     | 1,085          | 998            | 863            |

The increase in the 2020 pension funded status liability at O&R of \$45 million, compared with December 31, 2019, was primarily due to an increase in the plan's projected benefit obligation as a result of a decrease in discount rate. The increase in the 2019 pension funded status liability at O&R of \$24 million compared with December 31, 2018, was primarily due to an increase in the plan's projected benefit obligation as a result of a decrease in the discount rate, partially offset by an increase in plan assets as a result of the actual return on plan assets. See below for further information on the change in the discount rate and determination of the discount rate assumption. The 2020 increase in pension funded status liability corresponds with an increase to regulatory assets of \$38 million for unrecognized net losses and unrecognized prior service costs associated with O&R's New York utility business consistent with the accounting rules for regulated operations, a debit to OCI of \$5 million (net of taxes) for the unrecognized net losses, and an immaterial change to OCI (net of taxes) for the unrecognized prior service costs associated with RECO.

At December 31, 2020 and 2019, the Company's investments included \$26 million held in external trust accounts for benefit payments pursuant to the supplemental retirement plan. See Note M. The accumulated benefit obligations for the supplemental retirement plan for O&R were \$37 million and \$35 million as of December 31, 2020 and 2019, respectively.

## Notes to the Consolidated Financial Statements - continued

### Assumptions

The actuarial assumptions were as follows:

|   | 2020   | 2019   | 2018   |
|---|--------|--------|--------|
| Weighted-average assumptions used to determine benefit obligations at December 31:                        |        |        |        |
| Discount rate   | 2.55 % | 3.35 % | 4.25 % |
| Interest crediting rate for cash balance plan   | 3.00 % | 3.30 % | 4.00 % |
| Rate of compensation increase   | 3.20 % | 3.20 % | 4.00 % |
| Weighted-average assumptions used to determine net periodic benefit cost for the years ended December 31: |        |        |        |
| Discount rate   | 3.35 % | 4.25 % | 3.70 % |
| Interest crediting rate for cash balance plan   | 3.30 % | 4.00 % | 4.10 % |
| Expected return on plan assets  | 7.00 % | 7.00 % | 7.50 % |
| Rate of compensation increase   | 3.20 % | 4.00 % | 4.00 % |

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

### Discount Rate Assumption

To determine the assumed discount rate, the Company uses a model that produces a yield curve based on yields on selected highly rated (Aa or higher by either Moody's Investors Service or S&P Global Ratings) corporate bonds. Bonds with insufficient liquidity, bonds with questionable pricing information and bonds that are not representative of the overall market are excluded from consideration. For example, the bonds used in the model cannot be callable (with the exception of "make-whole" callable bonds), and the amount of the bond issue outstanding must be in excess of \$50 million. The spot rates defined by the yield curve and the plan's projected benefit payments are used to develop a weighted average discount rate.

### Expected Benefit Payments

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

| <i>(Millions of Dollars)</i> | 2021 | 2022 | 2023 | 2024 | 2025 | 2026-2030 |
|------------------------------|------|------|------|------|------|-----------|
| O&R                          | \$57 | \$58 | \$60 | \$60 | \$60 | \$301     |

### Expected Contributions

Based on estimates as of December 31, 2020, O&R expects to make contributions to the pension plan during 2021 of \$39 million. O&R's policy is to fund the total periodic benefit cost of the qualified plan to the extent tax deductible.

## Notes to the Consolidated Financial Statements - continued

### Plan Assets

The asset allocations for the pension plan at the end of 2020, 2019 and 2018, and the target allocation for 2021 are as follows:

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

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

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

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

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 2021 reflects the results of such a study conducted in 2018.

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

## Notes to the Consolidated Financial Statements - continued

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 as defined by the accounting rules for fair value measurements (see Note M).

The fair values of the pension plan assets at December 31, 2020 by asset category are as follows:

| <i>(Millions of Dollars)</i>                                       | Level 1 | Level 2 | Total    |
|--|---------|---------|----------|
| Investments within the fair value hierarchy                        |         |         |          |
| U.S. Equity (a)  | \$4,202 | \$—     | \$4,202  |
| International Equity (b)   | 3,693   | —       | 3,693    |
| U.S. Government Issued Debt (c)                                    | —       | 1,424   | 1,424    |
| Corporate Bonds Debt (d)   | —       | 3,535   | 3,535    |
| Structured Assets Debt (e)   | —       | 188     | 188      |
| Other Fixed Income Debt (f)  | —       | 1,067   | 1,067    |
| Cash and Cash Equivalents (g)                                      | 51      | 408     | 459      |
| Total investments within the fair value hierarchy                  | \$7,946 | \$6,622 | \$14,568 |
| Investments measured at NAV per share (m)                          |         |         |          |
| Private Equity (h)   |         |         | 635      |
| Real Estate (i)  |         |         | 1,880    |
| Hedge Funds (j)  |         |         | 292      |
| Total investments valued using NAV per share                       |         |         | \$2,807  |
| Funds for retiree health benefits (k)                              | (116)   | (97)    | (213)    |
| Funds for retiree health benefits measured at NAV per share (k)(m) |         |         | (41)     |
| Total funds for retiree health benefits                            |         |         | \$(254)  |
| Investments (excluding funds for retiree health benefits)          | \$7,830 | \$6,525 | \$17,121 |
| Pending activities (l)   |         |         | (99)     |
| Total fair value of plan net assets                                |         |         | \$17,022 |

- (a) U.S. Equity includes both actively- and passively-managed assets with investments in domestic equity index funds and actively-managed small-capitalization equities.
- (b) International Equity includes international equity index funds and actively-managed international equities.
- (c) U.S. Government Issued Debt includes agency and treasury securities.
- (d) Corporate Bonds Debt consists of debt issued by various corporations.
- (e) Structured Assets Debt includes commercial-mortgage-backed securities and collateralized mortgage obligations.
- (f) Other Fixed Income Debt includes municipal bonds, sovereign debt and regional governments.
- (g) Cash and Cash Equivalents include short term investments, money markets, foreign currency and cash collateral.
- (h) Private Equity consists of global equity funds that are not exchange-traded.
- (i) Real Estate investments include real estate funds based on appraised values that are broadly diversified by geography and property type.
- (j) Hedge Funds are within a commingled structure which invests in various hedge fund managers who can invest in all financial instruments.
- (k) The Company sets aside funds for retiree health benefits through a separate account within the pension trust, as permitted under Section 401(h) of the Internal Revenue Code of 1986, as amended. In accordance with the Code, the plan's investments in the 401(h) account may not be used for, or diverted to, any purpose other than providing health benefits for retirees. The net assets held in the 401(h) account are calculated based on a pro-rata percentage allocation of the net assets in the pension plan. The related obligations for health benefits are not included in the pension plan's obligations and are included in the Company's other postretirement benefit obligation. See Note F.
- (l) 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.

## Notes to the Consolidated Financial Statements - continued

(m) In accordance with ASU 2015-07, Fair Value Measurements (Topic 820): Disclosures for Investments in Certain Entities That Calculate Net Asset Value per Share (or its equivalent), certain investments that are measured at fair value using the net asset value per share (or its equivalent) practical expedient have not been classified in the fair value hierarchy.

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

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

(a) - (m) Reference is made to footnotes (a) through (m) in the above table of pension plan assets at December 31, 2020 by asset category.

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

| <i>(Millions of Dollars)</i> | For the Years Ended December 31, |      |      |
|------------------------------|----------------------------------|------|------|
|                              | 2020                             | 2019 | 2018 |
| O&R                          | \$5                              | \$4  | \$4  |

### Note F – Other Postretirement Benefits

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

## Notes to the Consolidated Financial Statements - continued

### Total Periodic Benefit Cost

The components of the Company's total periodic other postretirement benefit costs for 2020, 2019 and 2018 were as follows:

| <i>(Millions of Dollars)</i>                                       | 2020         | 2019       | 2018       |
|--|--------------|------------|------------|
| Service cost – including administrative expenses                   | \$4          | \$5        | \$6        |
| Interest cost on projected other postretirement benefit obligation | 6            | 8          | 8          |
| Expected return on plan assets                                     | (11)         | (11)       | (10)       |
| Recognition of net actuarial loss                                  | 2            | 1          | 5          |
| Recognition of prior service credit                                | (2)          | (1)        | (4)        |
| <b>TOTAL PERIODIC OTHER POSTRETIREMENT BENEFIT COST/(CREDIT)</b>   | <b>\$(1)</b> | <b>\$2</b> | <b>\$5</b> |
| Cost capitalized   | (2)          | (2)        | (2)        |
| Reconciliation to rate level                                       | 8            | 5          | (1)        |
| <b>Total expense recognized</b>                                    | <b>\$5</b>   | <b>\$5</b> | <b>\$2</b> |

For information about the adoption of ASU 2017-07, "Compensation-Retirement Benefits (Topic 715): Improving the Presentation of Net Periodic Pension Cost and Net Periodic Postretirement Benefit Cost," and ASU 2018-14, "Compensation-Retirement Benefits (Subtopic 715-20): Disclosure Framework- Changes to the Disclosure Requirements for Defined Benefit Plans", see Note E.

### Funded Status

The funded status of the programs at December 31, 2020, 2019 and 2018 were as follows:

| <i>(Millions of Dollars)</i>                                   | 2020          | 2019          | 2018          |
|--|---------------|---------------|---------------|
| <b>CHANGE IN BENEFIT OBLIGATION</b>                            |               |               |               |
| Benefit obligation at beginning of year                        | \$203         | \$201         | \$234         |
| Service cost   | 4             | 5             | 6             |
| Interest cost on accumulated postretirement benefit obligation | 6             | 8             | 8             |
| Amendments   | —             | (14)          | —             |
| Net actuarial loss/(gain)                                      | 11            | 12            | (38)          |
| Benefits paid and administrative expenses, net of subsidies    | (9)           | (10)          | (10)          |
| Participant contributions                                      | 1             | 1             | 1             |
| <b>BENEFIT OBLIGATION AT END OF YEAR</b>                       | <b>\$216</b>  | <b>\$203</b>  | <b>\$201</b>  |
| <b>CHANGE IN PLAN ASSETS</b>                                   |               |               |               |
| Fair value of plan assets at beginning of year                 | \$152         | \$125         | \$144         |
| Actual return on plan assets                                   | 24            | 32            | (12)          |
| Employer contributions   | 3             | 1             | 1             |
| Employer group waiver plan subsidies                           | 2             | 1             | 2             |
| Participant contributions                                      | 1             | 1             | 1             |
| Benefits paid  | (9)           | (8)           | (11)          |
| <b>FAIR VALUE OF PLAN ASSETS AT END OF YEAR</b>                | <b>\$173</b>  | <b>\$152</b>  | <b>\$125</b>  |
| <b>FUNDED STATUS</b>   | <b>\$(43)</b> | <b>\$(51)</b> | <b>\$(76)</b> |
| Unrecognized net loss  | \$1           | \$6           | \$16          |
| Unrecognized prior service credits                             | (15)          | (16)          | (3)           |

The decrease in the 2020 other postretirement benefits funded status liability for O&R of \$8 million, compared with December 31, 2019, was primarily due to an increase in the fair value of plan assets as a result of the actual return on plan assets. This decreased liability corresponds with an increase in regulatory liability of \$3



## Notes to the Consolidated Financial Statements - continued

million for unrecognized net losses and unrecognized prior service costs associated with O&R's New York utility business consistent with the accounting rules for regulated operations, a credit to OCI of \$2 million (net of taxes) for the unrecognized net losses and an immaterial change to OCI for the unrecognized prior service costs associated with RECO.

The decrease in the 2019 other postretirement benefits funded status liability at O&R of \$25 million, compared with December 31, 2018, was primarily due to an increase in plan assets as a result of the actual return on plan assets. This decreased liability corresponds with a decrease to regulatory assets of \$19 million for unrecognized net losses and unrecognized prior service costs associated with O&R's New York utility business consistent with the accounting rules for regulated operations, a credit to OCI of \$2 million (net of taxes) for the unrecognized net losses and a credit to OCI of \$3 million (net of taxes) for the unrecognized prior service costs associated with RECO.

### Assumptions

The actuarial assumptions were as follows:

|   | 2020   | 2019   | 2018   |
|---|--------|--------|--------|
| Weighted-average assumptions used to determine benefit obligations at December 31:                        |        |        |        |
| Discount Rate   | 2.55 % | 3.35 % | 4.30 % |
| Weighted-average assumptions used to determine net periodic benefit cost for the years ended December 31: |        |        |        |
| Discount Rate   | 3.35 % | 4.30 % | 3.70 % |
| Expected Return on Plan Assets  | 8.10 % | 8.10 % | 7.50 % |

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

The health care cost trend rate used to determine net periodic benefit cost for the years ended December 31, 2020, 2019 and 2018 was 5.20 percent, 5.40 percent and 5.60 percent, respectively, which was assumed to decrease gradually 4.50 percent by 2024 and remain at that level thereafter. The health care cost trend rate used to determine benefit obligations as of December 31, 2020, 2019 and 2018 was 7.04 percent, 5.20 percent and 5.40 percent, respectively, which is assumed to decrease gradually to 4.50 percent by 2034 and remain at that level thereafter.

### Expected Benefit Payments

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

| (Millions of Dollars) | 2021 | 2022 | 2023 | 2024 | 2025 | 2026-2030 |
|-----------------------|------|------|------|------|------|-----------|
| O&R                   | \$9  | \$9  | \$9  | \$9  | \$10 | \$50      |

### Expected Contributions

Based on estimates as of December 31, 2020, O&R expects to make a contribution of \$3 million to the other postretirement benefit plans in 2021.

## Notes to the Consolidated Financial Statements - continued

### Plan Assets

The asset allocations for O&R's other postretirement benefit plans at the end of 2020, 2019 and 2018 and the target allocation for 2021 are as follows:

| Asset Category    | Target Allocation Range | Plan Assets at December 31, |      |      |
|-------------------|-------------------------|-----------------------------|------|------|
|                   | 2021                    | 2020                        | 2019 | 2018 |
| Equity Securities | 75% -85%                | 82%                         | 81%  | 79%  |
| Debt Securities   | 15% -25%                | 18%                         | 19%  | 21%  |
| Total             | 100%                    | 100%                        | 100% | 100% |

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

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

The fair values of the plans' assets at December 31, 2020 by asset category as defined by the accounting rules for fair value measurements (see the fair value hierarchy defined in Note M) are as follows:

| <i>(Millions of Dollars)</i>                              | Level 1 | Level 2 | Total |
|---|---------|---------|-------|
| Equity (a)  | \$—     | \$141   | \$141 |
| Other Fixed Income Debt (b)                               | —       | 31      | 31    |
| Cash and Cash Equivalents (c)                             | —       | 1       | 1     |
| Investments (excluding funds for retiree health benefits) | \$—     | \$173   | \$173 |
| Pending activities (d)                                    | —       | —       | —     |
| Total fair value of plan net assets                       | —       | —       | \$173 |

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

The fair values of the plan assets at December 31, 2019 by asset category (see the fair value hierarchy defined in Note M) are as follows:

| <i>(Millions of Dollars)</i>                              | Level 1 | Level 2 | Total |
|---|---------|---------|-------|
| Equity (a)  | \$—     | \$123   | \$123 |
| Other Fixed Income Debt (b)                               | —       | 28      | 28    |
| Cash and Cash Equivalents (c)                             | —       | 1       | 1     |
| Investments (excluding funds for retiree health benefits) | \$—     | \$152   | \$152 |
| Pending activities (d)                                    | —       | —       | —     |
| Total fair value of plan net assets                       | —       | —       | \$152 |

- (a) - (d) Reference is made to footnotes (a) through (d) in the above table of other postretirement benefit plan assets at December 31, 2020 by asset category.

## Notes to the Consolidated Financial Statements - continued

### Note G – Environmental Matters

#### Superfund Sites

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

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

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

The accrued liabilities and regulatory assets related to Superfund Sites at December 31, 2020 and 2019 were as follows:

| <i>(Millions of Dollars)</i> | 2020 | 2019 |
|------------------------------|------|------|
| Accrued Liabilities:         |      |      |
| Manufactured gas plant sites | \$76 | \$79 |
| Other Superfund Sites        | 1    | 1    |
| Total                        | \$77 | \$80 |
| Regulatory assets            | \$74 | \$85 |

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

## Notes to the Consolidated Financial Statements - continued

Environmental remediation costs incurred related to Superfund Sites were \$1 million and \$7 million for the years ended December 31, 2020 and 2019, respectively.

Insurance and other third-party recoveries received by the Company for the year ended December 31, 2020 were immaterial. No insurance and other third-party recoveries were received by the Company for the year ended December 31, 2019.

O&R estimates that in 2021, it will incur costs for remediation of approximately \$2 million. The Company is unable to estimate the time period over which the remaining accrued liability will be incurred because, among other things, the required remediation has not been determined for some of the sites.

In 2020, O&R estimated that for its manufactured gas plant sites, each of which has been investigated, the aggregate undiscounted potential liability for the remediation of coal tar and/or other environmental contaminants could range up to \$127 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; however, the Company believes that these amounts are greatly exaggerated, based on the disposition of previous claims. At December 31, 2020 and 2019, the Company had accrued its estimated aggregate undiscounted potential liability for these suits and additional suits that may be brought over the next 15 years as shown in the following table. The estimates were based upon a combination of modeling, historical data analysis and risk factor assessment. Courts have begun, and unless otherwise determined on appeal may continue, to apply different standards for determining liability in asbestos suits than the standard that applied historically. As a result, the Company currently believes that there is a reasonable possibility of an exposure to loss in excess of the liability accrued for the suits. The Company is unable to estimate the amount or range of such loss. In addition, certain current and former employees have claimed or are claiming workers' compensation benefits based on alleged disability from exposure to asbestos. The Company defers as regulatory assets (for subsequent recovery through rates) costs incurred for asbestos claims by employees and third-party contractors relating to its divested generating plants.

## Notes to the Consolidated Financial Statements - continued

The Company's accrued liability for asbestos suits and workers' compensation proceedings (including those related to asbestos exposure) and the amounts deferred as regulatory assets for the Company at December 31, 2020 and 2019 were as follows:

| <i>(Millions of Dollars)</i>              | 2020  | 2019  |
|---|-------|-------|
| Accrued liability – asbestos suits        | \$0.4 | \$0.4 |
| Regulatory assets – asbestos suits        | 0.4   | 0.4   |
| Accrued liability – workers' compensation | \$4.2 | \$5.0 |

### Note H - Leases

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

The Company leases office buildings, equipment and access rights to support electric distribution facilities. The Company recognized lease right-of-use assets and lease liabilities on its balance sheets for virtually all of its leases (other than leases that meet the definition of a short-term lease, the expense for which was immaterial). A lease right-of-use asset represents a right to use an identifiable underlying asset and obtain substantially all of the economic benefits from the use of that asset for the lease term. A lease liability represents an obligation to make lease payments arising from the lease. Leases are classified as either operating leases or finance leases. Operating leases are included in operating lease right-of-use asset and operating lease liabilities on the Company's balance sheet. Finance leases are included in other noncurrent assets, other current liabilities and other noncurrent liabilities. The Company, as a regulated entity, is permitted to continue to recognize expense for operating leases using the timing that conforms to the regulatory rate treatment as rental payments are recovered from our customers and to account the same way for finance leases.

For new operating leases, the Company recognizes operating lease right-of-use assets and operating lease liabilities based on the present value of the future minimum lease payments over the lease term at commencement date. As most of the Company's leases do not provide an implicit rate, the Company used its collateralized incremental borrowing rate based on the information available at the commencement date to determine the present value of future payments. Most of the Company's leases have remaining lease terms of one year to 11 years and may include options to renew or extend the leases for up to five years at the fair rental value. The Company's lease terms include options to renew, extend or terminate the lease when it is reasonably certain that the Company will exercise that option. There were no leases with material variable lease payments or residual value guarantees. The Company accounts for lease and non-lease components as a single lease component.

Operating lease cost and cash paid for amounts included in the measurement of lease liabilities for the years ended December 31, 2020 and 2019, were as follows:

## Notes to the Consolidated Financial Statements - continued

| <i>(Millions of Dollars)</i> | 2020  | 2019  |
|------------------------------|-------|-------|
| Operating lease cost         | \$1.0 | \$1.0 |
| Operating lease cash flows   | \$1.0 | \$0.9 |

As of December 31, 2020 and 2019, assets recorded as finance leases for O&R were \$0.9 million and \$1.0 million, respectively, and the accumulated amortization associated with finance leases for O&R was \$1.8 million and \$1.7 million, respectively. For the years ended December 31, 2020 and 2019, finance lease costs and cash flows for O&R were immaterial.

Right-of-use assets obtained in exchange for operating lease obligations were \$0.3 million and immaterial for O&R for the years ended December 31, 2020 and 2019, respectively.

Other information related to leases for O&R at December 31, 2020 and 2019 were as follows:

|  | 2020       | 2019       |
|--|------------|------------|
| Weighted Average Remaining Lease Term: |            |            |
| Operating leases                       | 3.4 years  | 3.7 years  |
| Finance leases                         | 18.2 years | 19.2 years |
| Weighted Average Discount Rate:        |            |            |
| Operating leases                       | 3.6%       | 3.8%       |
| Finance leases                         | 3.1%       | 3.1%       |

Future minimum lease payments under non-cancellable leases at December 31, 2020 were as follows:

| <i>(Millions of Dollars)</i>             | Operating Leases | Finance Leases |
|--|------------------|----------------|
| Year Ending December 31,                 |                  |                |
| 2021                                     | \$1.0            | \$—            |
| 2022                                     | 0.5              | —              |
| 2023                                     | 0.1              | —              |
| 2024                                     | 0.1              | —              |
| 2025                                     | 0.1              | 0.1            |
| All years thereafter                     | 0.2              | 0.7            |
| Total future minimum lease payments      | \$2.0            | \$0.8          |
| Less: imputed interest                   | (0.1)            | (0.2)          |
| Total                                    | \$1.9            | \$0.6          |
| Reported as of December 31, 2020         |                  |                |
| Operating lease liabilities (current)    | \$1.0            | \$—            |
| Operating lease liabilities (noncurrent) | 0.9              | —              |
| Other current liabilities                | —                | —              |
| Other noncurrent liabilities             | —                | 0.6            |
| Total                                    | \$1.9            | \$0.6          |

At December 31, 2020, the Company did not have material obligations under operating or finance leases that had not yet commenced.

## Notes to the Consolidated Financial Statements - continued

The Company is a lessor under certain leases whereby the Company owns real estate and leases portions of it to others. Revenue under such leases was immaterial for O&R for the years ended December 31, 2020 and 2019.

### Note I – Income Tax

In response to the economic impacts of the COVID-19 pandemic, the Coronavirus Aid, Relief, and Economic Security Act (CARES Act) was signed into law on March 27, 2020. The CARES Act provides relief to corporate taxpayers by permitting a five-year carryback of net operating losses (NOLs) for tax years 2018, 2019 and 2020, temporarily removing the 80 percent limitation when applying the NOLs to carryback years, increasing the 30 percent limitation on interest deductibility to 50 percent of adjusted taxable income for tax years 2019 and 2020, and provides for certain employee retention tax credits and refunds for eligible employers. There is no material impact from the CARES Act on the income tax expense of the Company for the year ended December 31, 2020.

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

| <i>(Millions of Dollars)</i> | 2020 | 2019 | 2018 |
|------------------------------|------|------|------|
| State                        |      |      |      |
| Current                      | \$1  | \$2  | \$—  |
| Deferred                     | 7    | 4    | 4    |
| Federal                      |      |      |      |
| Current                      | 1    | 15   | (2)  |
| Deferred                     | 12   | (4)  | 13   |
| Total income tax expense     | \$21 | \$17 | \$15 |

## Notes to the Consolidated Financial Statements - continued

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

| <i>(Millions of Dollars)</i>   | 2020         | 2019         |
|--|--------------|--------------|
| Deferred tax liabilities:  |              |              |
| Property basis differences   | \$440        | \$426        |
| Regulatory assets:   |              |              |
| Unrecognized pension and other postretirement costs                        | 49           | 39           |
| Environmental remediation costs  | 21           | 24           |
| Deferred storm costs   | 31           | 21           |
| Other regulatory assets  | 28           | 21           |
| Operating lease right-of-use asset   | 1            | 1            |
| <b>Total deferred tax liabilities</b>                                      | <b>570</b>   | <b>532</b>   |
| Deferred tax assets:   |              |              |
| Accrued pension and other postretirement costs                             | \$77         | \$68         |
| Regulatory liabilities:  |              |              |
| Future income tax  | 38           | 40           |
| Other regulatory liabilities   | 83           | 78           |
| Superfund and other environmental costs                                    | 22           | 22           |
| Asset retirement obligations   | 1            | 1            |
| Loss carryforwards   | 3            | 1            |
| Operating lease liabilities  | 1            | 1            |
| Other  | 5            | 6            |
| <b>Total deferred tax assets</b>   | <b>\$230</b> | <b>\$217</b> |
| <b>Net deferred tax liabilities</b>  | <b>340</b>   | <b>315</b>   |
| Unamortized investment tax credits   | —            | 1            |
| <b>Net deferred tax liabilities and unamortized investment tax credits</b> | <b>\$340</b> | <b>\$316</b> |

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

| <i>(% of Pre-tax income)</i>                         | 2020       | 2019       | 2018       |
|--|------------|------------|------------|
| STATUTORY TAX RATE                                   |            |            |            |
| Federal  | 21%        | 21%        | 21%        |
| Changes in computed taxes resulting from:            |            |            |            |
| State income tax, net of federal income tax benefit  | 6          | 6          | 6          |
| Cost of removal                                      | 3          | 2          | 2          |
| Amortization of excess deferred federal income taxes | (8)        | (7)        | (7)        |
| Reversal of uncertain tax positions                  | —          | —          | (1)        |
| Research and development credits                     | —          | (1)        | —          |
| Other  | 1          | (1)        | —          |
| <b>Effective tax rate</b>                            | <b>23%</b> | <b>20%</b> | <b>21%</b> |

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

At December 31, 2020, O&R has a New York State net operating loss of approximately \$24 million, due primarily to storm related costs and higher accelerated state tax depreciation. A deferred tax asset has been



## Notes to the Consolidated Financial Statements - continued

recognized for this New York State net operating loss carryforward, which will begin to expire, if unused, in 2040, and no valuation allowance was provided; as it is more likely than not that the deferred tax asset will be realized.

At December 31, 2020, RECO has a New Jersey State net operating loss carryforward of approximately \$24 million, due primarily to storm related costs and higher accelerated state tax depreciation. A deferred tax asset has been recognized for the New Jersey State NOL carryforward that will begin to expire, if unused, in 2038, and no valuation allowance has 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, O&R is not permitted to recognize the tax benefit attributable to a tax position unless such position is more likely than not to be sustained upon examination by taxing authorities, including resolution of any related appeals and litigation processes, based solely on the technical merits of the position.

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

| <i>(Millions of Dollars)</i>                         | 2020 | 2019 | 2018 |
|--|------|------|------|
| Balance at January 1,                                | \$—  | \$2  | \$3  |
| Additions based on tax positions of prior years      | —    | —    | —    |
| Reductions for tax positions of prior years          | —    | (2)  | —    |
| Reductions from expiration of statute of limitations | —    | —    | (1)  |
| Balance at December 31,                              | \$—  | \$—  | \$2  |

At December 31, 2020, the estimated liability for uncertain tax positions for O&R was an immaterial amount. O&R recognizes interest on liabilities for uncertain tax positions in interest expense and would recognize penalties, if any, in operating expenses in O&R's consolidated income statement. In 2020, 2019 and 2018, O&R recognized no interest or penalties for uncertain tax positions in its consolidated income statement.

Con Edison and its subsidiaries' federal tax return for 2019 remains under examination. State income tax returns remain open for examination in New York for tax years 2010 through 2019 and in New Jersey for tax years 2016 through 2019.

### Note J - Revenue Recognition

The following table presents, for the years ended December 31, 2020, 2019 and 2018, revenue from contracts with customers as defined in ASC Topic 606, "Revenue from Contracts with Customers," as well as additional revenue from sources other than contracts with customers, disaggregated by major source.

## Notes to the Consolidated Financial Statements - continued

|                              | 2020   |                          |                                | 2019   |                          |                                | 2018   |                          |                                |
|------------------------------|--|--------------------------|--------------------------------|--|--------------------------|--------------------------------|--|--------------------------|--------------------------------|
| <i>(Millions of Dollars)</i> | Revenues<br>from<br>contracts<br>with<br>customers | Other<br>revenues<br>(a) | Total<br>operating<br>revenues | Revenues<br>from<br>contracts<br>with<br>customers | Other<br>revenues<br>(a) | Total<br>operating<br>revenues | Revenues<br>from<br>contracts<br>with<br>customers | Other<br>revenues<br>(a) | Total<br>operating<br>revenues |
| O&R                          |  |                          |                                |  |                          |                                |  |                          |                                |
| Electric                     | \$619  | \$10                     | \$629                          | \$627  | \$7                      | \$634                          | \$647  | \$(5)                    | \$642                          |
| Gas                          | 224  | 9                        | 233                            | 247  | 12                       | 259                            | 256  | (7)                      | 249                            |
| Total O&R                    | \$843  | \$19                     | \$862                          | \$874  | \$19                     | \$893                          | \$903  | \$(12)                   | \$891                          |

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

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

O&R has the obligation to deliver electricity and gas to its customers. As the energy is immediately available for use upon delivery to the customer, the energy and its delivery are identifiable as a single performance obligation. The Company recognizes revenues as this performance obligation is satisfied over time as the Company delivers, and the customers simultaneously receive and consume, the energy. The amount of revenues recognized reflects the consideration the Company expects to receive in exchange for delivering the energy. Under its tariffs, the transaction price for full-service customers includes the Company's energy cost and for all customers includes delivery charges determined based on customer class and in accordance with established tariffs and guidelines of the NYSPSC or the NJBPU, as applicable. Accordingly, there is no unsatisfied performance obligation associated with these customers. The transaction price is applied to the Company's revenue generating activities through the customer billing process. Because energy is delivered over time, the Company uses output methods that recognize revenue based on direct measurement of the value transferred, such as units delivered, which provides an accurate measure of value for the energy delivered. The Company accrues revenues at the end of each month for estimated energy delivered but not yet billed to customers. The Company defers over a 12-month period net interruptible gas revenues, other than those authorized by the NYSPSC to be retained by the Company, for refund to firm gas sales and transportation customers.

In March 2020, the Company began suspending new late payment charges and certain other fees for all customers. The estimated amount of these foregone revenues for the year ended December 31, 2020 was \$3.4 million. The Company also began providing payment extensions for all customers that were scheduled to be disconnected prior to the start of the COVID-19 pandemic. See "COVID-19 Regulatory Matters" in Note B.

## Notes to the Consolidated Financial Statements - continued

### Note K - Stock-Based Compensation

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

Shares of Con Edison common stock used to satisfy O&R's obligations with respect to stock-based compensation may be new shares (authorized, but unissued) or treasury shares (existing treasury shares or shares purchased in the open market). The shares used during the year ended December 31, 2020 were new shares. Con Edison intends to use new shares to fulfill its stock-based compensation obligations for 2021.

The Company has recognized stock-based compensation expense using a fair value measurement method. The following table summarizes stock-based compensation expense recognized by the Company in the years ended December 31, 2020, 2019 and 2018:

| <i>(Millions of Dollars)</i>       | 2020  | 2019  | 2018  |
|------------------------------------|-------|-------|-------|
| Performance-based restricted stock | \$1.1 | \$2.9 | \$0.1 |
| Time-based restricted stock        | 0.1   | 0.2   | 0.1   |
| Stock purchase plan                | 0.5   | 0.4   | 0.4   |
| Total                              | \$1.7 | \$3.5 | \$0.6 |
| Income tax benefit                 | \$0.5 | \$1.0 | \$0.2 |

### Restricted Stock Units

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

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

## Notes to the Consolidated Financial Statements - continued

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

|                                     | 2020            | 2019            | 2018            |
|-------------------------------------|-----------------|-----------------|-----------------|
| Risk-free interest rate (a)         | 0.10% - 0.13%   | 1.58% - 1.59%   | 2.48% - 2.63%   |
| Expected term (b)                   | 3 years         | 3 years         | 3 years         |
| Expected share price volatility (c) | 30.16% - 40.95% | 12.89% - 15.51% | 14.76% - 17.71% |

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

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

(c) Based on historical experience.

A summary of changes in the status of the Performance RSUs’ TSR and non-TSR portions during the year ended December 31, 2020 is as follows:

|                                 | Weighted Average Grant Date Fair Value (a) |                    |                        |
|---------------------------------|--|--------------------|------------------------|
|                                 | Units                                      | TSR<br>Portion (b) | Non-TSR<br>Portion (c) |
| Non-vested at December 31, 2019 | 84,706                                     | \$67.93            | \$77.18                |
| Granted                         | 28,704                                     | 80.18              | 91.07                  |
| Vested                          | (25,141)                                   | 73.06              | 74.56                  |
| Forfeited                       | (6,569)                                    | 74.03              | 88.33                  |
| Non-vested at December 31, 2020 | 81,700                                     | \$70.17            | \$81.97                |

(a) The TSR and non-TSR Portions each account for 50 percent of the awards’ value.

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

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

The total expense to be recognized by the Company in future periods for unvested Performance RSUs outstanding at December 31, 2020 is \$2 million and is expected to be recognized over a weighted average period of one year. The Company paid cash of \$2 million in 2020 and 2019, and \$1 million in 2018 to settle vested Performance RSUs.

In accordance with the accounting rules for stock compensation, for time-based awards, the Company is accruing a liability and recognizing compensation expense based on the market value of a common share throughout the vesting period. The vesting period for awards is three years and is based on the employee’s continuous service to O&R. Prior to vesting, the awards are subject to forfeiture in whole or in part under certain circumstances. The awards are “liability awards” because each restricted stock unit represents the right to receive, upon vesting, one share of Con Edison common stock, the cash value of a share or a combination thereof. As such, prior to vesting, changes in the fair value of the units are reflected in net income. A summary of changes in the status of time-based awards during the year ended December 31, 2020 is as follows:

## Notes to the Consolidated Financial Statements - continued

|                                 | Units   | Weighted Average<br>Grant Date<br>Fair Value |
|---------------------------------|---------|--|
| Non-vested at December 31, 2019 | 4,150   | \$80.35                                      |
| Granted                         | 1,550   | 78.00  |
| Vested                          | (1,100) | 77.66  |
| Non-vested at December 31, 2020 | 4,600   | \$80.20                                      |

The total expense to be recognized by the Company in future periods for unvested time-based awards outstanding at December 31, 2020 was immaterial and is expected to be recognized over a weighted average period of one year. The Company paid an immaterial amount of cash in 2020, 2019 and 2018 to settle vested time-based awards.

### Stock Purchase Plan

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

Participants in the plan immediately vest in shares purchased by them under the plan. Prior to September 1, 2020, 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 2020, the plan was amended and as a result of the amendment, the fair value of the shares of Con Edison common stock purchased after September 1, 2020 under the plan was calculated using the closing price at which shares were traded on the New York Stock Exchange on the last business day of the month for all shares purchased during the month. During 2020, 2019 and 2018, 836,984, 747,899 and 786,385 shares were purchased under the Stock Purchase Plan, including those purchased by employees of other subsidiaries of Con Edison, at a weighted average price of \$79.82, \$85.45 and \$78.27 per share, respectively.

### Note L – Derivative Instruments and Hedging Activities

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

In August 2017, the FASB issued amendments to the guidance for derivatives and hedging through ASU 2017-12, "Derivatives and Hedging (Topic 815): Targeted Improvements to Accounting for Hedging Activities." The amendments in this update provide greater clarification on hedge accounting for risk components,

## Notes to the Consolidated Financial Statements - continued

presentation and disclosure of hedging instruments, and overall targeted improvements to simplify hedge accounting. The amendments were effective for reporting periods beginning after December 15, 2019. The application of the guidance did not have a material impact on the Company's financial position, results of operations and liquidity because the Company does not elect hedge accounting for its derivative instruments and hedging activities.

The fair values of the Company's commodity derivatives, including the offsetting of assets and liabilities, on the consolidated balance sheet at December 31, 2020 and 2019 were:

| <i>(Millions of Dollars)</i>                          | 2020   |                             |   | 2019   |                             |   |
|---|--|-----------------------------|---|--|-----------------------------|---|
| <b>Balance Sheet Location</b>                         | <b>Gross Amounts of Recognized Assets/ (Liabilities)</b> | <b>Gross Amounts Offset</b> | <b>Net Amounts of Assets/ (Liabilities) (a)</b> | <b>Gross Amounts of Recognized Assets/ (Liabilities)</b> | <b>Gross Amounts Offset</b> | <b>Net Amounts of Assets/ (Liabilities) (a)</b> |
| <b>Fair value of derivative assets</b>                |  |                             |   |  |                             |   |
| Current   | \$1  | (\$1)                       | \$— (b)   | \$—  | \$—                         | \$— (b)   |
| Noncurrent  | 1  | —                           | 1   | —  | —                           | —   |
| <b>Total fair value of derivative assets</b>          | <b>\$2</b>   | <b>(\$1)</b>                | <b>\$1</b>                                      | <b>\$—</b>   | <b>\$—</b>                  | <b>\$—</b>                                      |
| <b>Fair value of derivative liabilities</b>           |  |                             |   |  |                             |   |
| Current   | \$(13)   | \$—                         | \$(13)  | \$(13)   | \$1                         | \$(12)  |
| Noncurrent  | (9)  | —                           | (9)   | (8)  | 1                           | (7)   |
| <b>Total fair value of derivative liabilities</b>     | <b>\$(22)</b>  | <b>\$—</b>                  | <b>\$(22)</b>                                   | <b>\$(21)</b>  | <b>\$2</b>                  | <b>\$(19)</b>                                   |
| <b>Net fair value derivative assets/(liabilities)</b> | <b>\$(20)</b>  | <b>\$(1)</b>                | <b>\$(21)</b>                                   | <b>\$(21)</b>  | <b>\$2</b>                  | <b>\$(19)</b>                                   |

- (a) Derivative instruments and collateral were offset on the consolidated balance sheet as applicable under the accounting rules. The Company enters into master agreements for its commodity derivatives. These agreements typically provide offset in the event of contract termination. In such case, generally the non-defaulting party's payable will be offset by the defaulting party's payable. The non-defaulting party will customarily notify the defaulting party within a specific time period and come to an agreement on the early termination amount.
- (b) At December 31, 2020 and 2019, margin deposits of \$1 million were classified as derivative assets on the consolidated balance sheet, but not included in the table. Margin is collateral, typically cash, that the holder of a derivative instrument is required to deposit in order to transact on an exchange and to cover its potential losses with its broker or the exchange

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

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

## Notes to the Consolidated Financial Statements - continued

The following table presents the realized and unrealized gains or losses on commodity derivatives that have been deferred for the years ended December 31, 2020 and 2019:

| <i>(Millions of Dollars)</i>  | <b>Balance Sheet Location</b> | <b>2020</b> | <b>2019</b> |
|---|-------------------------------|-------------|-------------|
| Pre-tax gains/(losses) deferred in accordance with accounting rules for regulated operations: |                               |             |             |
| Current   | Deferred derivative gains     | \$—         | \$(1)       |
| Noncurrent  | Deferred derivative gains     | —           | (2)         |
| Total deferred gains/(losses)   |                               | \$—         | \$(3)       |
| Current   | Deferred derivative losses    | \$2         | \$(8)       |
| Current   | Recoverable energy costs      | (24)        | (18)        |
| Noncurrent  | Deferred derivative losses    | (1)         | (2)         |
| Total deferred gains/(losses)   |                               | \$(23)      | \$(28)      |
| Net deferred gains/(losses)   |                               | \$(23)      | \$(31)      |

The following table presents the hedged volume of the Company's commodity derivative transactions at December 31, 2020:

| <b>Electric Energy (MWh) (a)</b> | <b>Capacity (MW) (a)</b> | <b>Natural Gas (Dt) (a)</b> |
|----------------------------------|--------------------------|-----------------------------|
| 1,908,430                        | 5,550                    | 14,900,000                  |

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

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

At December 31, 2020, the Company had \$2 million of credit exposure in connection with open energy supply net receivables and hedging activities, net of collateral, related to investment-grade counterparties and exchange brokers.

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

The following table presents the aggregate fair value of the Company's derivative instruments with credit-risk-related contingent features that are in a net liability position, the collateral posted for such positions and the additional collateral that would have been required to be posted had the lowest applicable credit rating been reduced one level and to below investment grade at December 31, 2020:

## Notes to the Consolidated Financial Statements - continued

### (Millions of Dollars)

|  |        |
|--|--------|
| Aggregate fair value – net liabilities (a)   | \$21   |
| Collateral posted  | 12     |
| Additional collateral (b) (downgrade one level from current ratings)                 | —      |
| Additional collateral (b) (downgrade to below investment grade from current ratings) | 12 (c) |

- (a) Non-derivative transactions for the purchase and sale of electricity, gas and qualifying derivative instruments, which have been designated as normal purchases or normal sales, are excluded from the table. These transactions primarily include purchases of electricity from independent system operators. In the event the Company was no longer extended unsecured credit for such purchases, the Company would not be required to post additional collateral at December 31, 2020. For certain other such non-derivative transactions, the Company could be required to post collateral under certain circumstances, including in the event counterparties had reasonable grounds for insecurity.
- (b) The additional collateral amounts shown above are based upon the estimated O&R allocation of the Utilities' collateral requirements. The Utilities measure the collateral requirements by taking into consideration the fair value amounts of derivative instruments that contain credit-risk-related contingent features that are in a net 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 Company has a legally enforceable right of offset.
- (c) Derivative instruments that are net assets have been excluded from the table. At December 31, 2020, if the Company had been downgraded to below investment grade, it would have been required to post an immaterial amount of additional collateral.

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

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



## Notes to the Consolidated Financial Statements - continued

- Level 2 – Consists of assets or liabilities valued using industry standard models and based on prices, other than quoted prices within Level 1, that are either directly or indirectly observable as of the measurement date. The industry standard models consider observable assumptions including time value, volatility factors, and current market and contractual prices for the underlying commodities, in addition to other economic measures. This category includes contracts traded on active exchanges or in over-the-counter markets priced with industry standard models.
  
- Level 3 – Consists of assets or liabilities whose fair value is estimated based on internally developed models or methodologies using inputs that are generally less readily observable and supported by little, if any, market activity at the measurement date. Unobservable inputs are developed based on the best available information and subject to cost benefit constraints. This category includes contracts priced using models that are internally developed and contracts placed in illiquid markets. It also includes contracts that expire after the period of time for which quoted prices are available and internal models are used to determine a significant portion of the value.

Assets and liabilities measured at fair value on a recurring basis as of December 31, 2020 and 2019 are summarized below.

| <i>(Millions of Dollars)</i> | 2020        |            |            |                           |             | 2019        |            |            |                           |             |
|------------------------------|-------------|------------|------------|---------------------------|-------------|-------------|------------|------------|---------------------------|-------------|
|                              | Level 1     | Level 2    | Level 3    | Netting<br>Adjustment (e) | Total       | Level 1     | Level 2    | Level 3    | Netting<br>Adjustment (e) | Total       |
| Derivative assets:           |             |            |            |                           |             |             |            |            |                           |             |
| Commodity (a)(b)(c)          | \$—         | \$2        | \$—        | \$—                       | \$2         | \$—         | \$—        | \$—        | \$1                       | \$1         |
| Other (a)(b)(d)              | 20          | 6          | —          | —                         | 26          | 20          | 6          | —          | —                         | 26          |
| <b>Total assets</b>          | <b>\$20</b> | <b>\$8</b> | <b>\$—</b> | <b>\$—</b>                | <b>\$28</b> | <b>\$20</b> | <b>\$6</b> | <b>\$—</b> | <b>\$1</b>                | <b>\$27</b> |
| Derivative liabilities:      |             |            |            |                           |             |             |            |            |                           |             |
| Commodity (a)(b)(c)          | \$—         | \$11       | \$11       | \$—                       | \$22        | \$1         | \$11       | \$9        | (\$2)                     | \$19        |

- (a) The Company's policy is to review the fair value hierarchy and recognize transfers into and transfers out of the levels at the end of each reporting period. There were no transfers of commodity derivative liabilities transferred from level 3 to level 2 during the year ended December 31, 2020. There were \$2 million of commodity derivative liabilities transferred from level 3 to level 2 during the year ended December 31, 2019 because of availability of observable market data due to the decrease in the terms of certain contracts from beyond three years as of September 30, 2019 to less than three years as of December 31, 2019.
- (b) Level 2 assets and liabilities include investments held in the deferred compensation plan and/or non-qualified retirement plans, exchange-traded contracts where there is insufficient market liquidity to warrant inclusion in Level 1, and certain over-the-counter derivative instruments for electricity and natural gas. Derivative instruments classified as Level 2 are valued using industry standard models that incorporate corroborated observable inputs; such as pricing services or prices from similar instruments that trade in liquid markets, time value and volatility factors.
- (c) The accounting rules for fair value measurements and disclosures require consideration of the impact of nonperformance risk (including credit risk) from a market participant perspective in the measurement of the fair value of assets and liabilities. At December 31, 2020 and 2019, the Company determined that nonperformance risk would have no material impact on its financial position or results of operation.
- (d) Other assets are comprised of assets such as life insurance contracts within the non-qualified retirement plan.
- (e) Amounts represent the impact of legally-enforceable master netting agreements that allow the Company to net gain and loss positions and cash collateral held or placed with the same counterparties.

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

## Notes to the Consolidated Financial Statements - continued

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

| Commodity   | Fair Value of Level 3 at<br>December 31, 2020<br>(Millions of Dollars) | Valuation<br>Techniques | Unobservable Inputs            | Range                          |
|-------------|--|-------------------------|--------------------------------|--------------------------------|
| Electricity | \$(11)   | Discounted Cash Flow    | Forward capacity<br>prices (a) | \$0.08-\$6.26 per kW-<br>month |

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

The table listed below provides a reconciliation of the beginning and ending net balances for assets and liabilities measured at fair value for the years ended December 31, 2020 and 2019 and classified as Level 3 in the fair value hierarchy:

| <i>(Millions of Dollars)</i>                  | 2020   | 2019  |
|---|--------|-------|
| Beginning balance as of January 1,            | \$(9)  | \$(9) |
| Included in earnings                          | (8)    | (7)   |
| Included in regulatory assets and liabilities | (3)    | 1     |
| Settlements                                   | 9      | 8     |
| Transfer out of level 3                       | —      | (2)   |
| Ending balance as of December 31,             | \$(11) | \$(9) |

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

### Note N - Asset Retirement Obligations

The Company recognizes a liability at fair value for legal obligations associated with the retirement of long-lived assets in the period in which they are incurred, or when sufficient information becomes available to reasonably estimate the fair value of such legal obligations. When the liability is initially recorded, asset retirement costs are capitalized by increasing the carrying amount of the related asset. The liability is accreted to its present value each period and the capitalized cost is depreciated over the useful life of the related asset. The fair value of the asset retirement obligation liability is measured using expected future cash flows discounted at credit-adjusted risk-free rates, historical information, and where available, quoted prices from outside contractors. The Company evaluates these assumptions underlying the asset retirement obligation liability on an annual basis or as frequently as needed. The Company recorded asset retirement obligations associated with the removal of asbestos and asbestos-containing material in its substations and electric equipment. At December 31, 2020, the liabilities for asset retirement obligations of the Company were \$1 million. At December 31, 2019, the liabilities for asset retirement obligations of the Company were \$3 million.

## Notes to the Consolidated Financial Statements - continued

The Company includes in depreciation rates the estimated removal costs, less salvage, for utility plant assets. The amounts related to removal costs that are associated with asset retirement obligations are classified as an asset retirement liability. Pursuant to accounting rules for regulated operations, future removal costs that do not represent legal asset retirement obligations are recorded as regulatory liabilities. Accretion and depreciation expenses related to removal costs that represent legal asset retirement obligations are applied against the Company's regulatory liabilities. Asset retirement costs that are recoverable from customers are recorded as regulatory liabilities to reflect the timing difference between costs recovered through the rate-making process and recognition of costs. The related net regulatory liabilities recorded for the Company were \$158 million and \$146 million at December 31, 2020 and 2019, respectively.

### Note O – Related Party Transactions

The NYSPSC generally requires that the Company and Con Edison's other subsidiaries be operated as separate entities. The Company and Con Edison's unregulated subsidiaries are required to have separate operating employees and operating officers of the Company may not be operating officers of Con Edison's unregulated subsidiaries. The Company may provide and receive administrative and other services to and from Con Edison and its subsidiaries only pursuant to cost allocation procedures approved by the NYSPSC and/or other regulatory authorities, as applicable. Transfers of assets between the Company and Con Edison or its other subsidiaries may be made only as approved by the NYSPSC. The debt of the Company is to be raised directly by the Company and not derived from Con Edison. Without the prior permission of the NYSPSC, the Company may not make loans to, guarantee the obligations of, or pledge assets as security for the indebtedness of Con Edison or its other subsidiaries. The NYSPSC limits the dividends that the Company may pay Con Edison. See "Common Stock" in Note C. As a result, substantially all of the net assets of O&R (\$807 million) at December 31, 2020 are considered restricted net assets. The NYSPSC may impose additional measures to separate, or "ring fence," the Company from Con Edison and its other subsidiaries. See "Rate Plans" in Note B.

The services received include substantial administrative support operations, such as corporate secretarial and associated managerial duties, accounting, treasury, investor relations, information resources, legal, human resources, fuel supply and energy management services. The costs of administrative and other services provided by the Company, and received from Con Edison and its other subsidiaries for the years ended December 31, 2020, 2019 and 2018 were as follows:

| <i>(Millions of Dollars)</i> | 2020 | 2019 | 2018 |
|------------------------------|------|------|------|
| Cost of services provided    | \$18 | \$19 | \$28 |
| Cost of services received    | \$62 | \$57 | \$55 |

At December 31, 2020 and 2019, O&R's payable to Con Edison and its other subsidiaries associated with these services was \$2 million and \$4 million, respectively.

## Notes to the Consolidated Financial Statements - continued

In addition, CECONY and O&R have joint gas supply arrangements, in connection with which O&R purchased from CECONY \$59 million and \$71 million of natural gas for the years ended December 31, 2020 and 2019, respectively. These amounts are net of the effect of related hedging transactions. At December 31, 2020 and 2019, O&R's net payable to CECONY associated with these gas purchases were \$8 million.

At December 31, 2020 and 2019, the Company's net payable to Con Edison for income taxes was \$1 million and \$12 million, respectively.

FERC has authorized CECONY to lend funds to O&R for periods of not more than 12 months, in an amount not to exceed \$250 million, at prevailing market rates. At December 31, 2020 and 2019, there were no outstanding loans to O&R.

### Note P – New Financial Accounting Standards

In December 2019, the FASB issued amendments to the guidance for income taxes through ASU 2019-12, "Income Taxes (Topic 740): Simplifying the Accounting for Income Taxes." The amendments in this update simplify the accounting for income taxes by removing certain exceptions such as: 1) the incremental approach for intraperiod tax allocation when there is a loss from continuing operations and income or a gain from other items, 2) the requirement to recognize a deferred tax liability for equity method investments when a foreign subsidiary becomes an equity method investment, 3) the ability not to recognize a deferred tax liability for a foreign subsidiary when a foreign equity method investment becomes a subsidiary, and 4) the general methodology for calculating income taxes in an interim period when a year-to-date loss exceeds the anticipated loss for the year. The amendments are effective for fiscal years beginning after December 15, 2021 and interim periods within fiscal years beginning after December 15, 2022, with early adoption permitted. The application of this guidance will not have a material impact on the Company's financial position, results of operations and liquidity.

In March 2020, the FASB issued ASU 2020-04, Reference Rate Reform (Topic 848): Facilitation of the Effects of Reference Rate Reform on Financial Reporting (ASU 2020-04). In 2017, the United Kingdom's Financial Conduct Authority announced that it intends to stop persuading or compelling banks to submit the London Interbank Offered Rate (LIBOR), a benchmark interest rate referenced in a variety of agreements, after 2021. In November 2020, LIBOR's administrator announced it plans to consult on its intention to cease publication of one-week and two-month U.S. Dollar LIBOR immediately after the LIBOR publication on December 31, 2021, and the remaining U.S. Dollar LIBOR tenors immediately after publication on June 30, 2023. ASU 2020-04 provides entities with optional expedients and exceptions for applying generally accepted accounting principles to contract modifications and hedging relationships, subject to meeting certain criteria, that reference LIBOR or another reference rate expected to be discontinued. In January 2021, the FASB issued amendments to the guidance through ASU 2021-01 to include all contract modifications and hedging relationships affected by reference rate reform, including those that do not directly reference LIBOR or another reference rate expected to be discontinued, and clarify which optional expedients may be applied to them. The guidance can be applied prospectively from any date beginning March 12, 2020. The optional relief is temporary and generally cannot be applied to contract modifications and hedging relationships entered into or evaluated after, December 31, 2022. The Company does not expect the new guidance to have a material impact on its financial position, results of operations or liquidity.