Energy–Related Derivatives (Exelon, Generation, ComEd and PECO)

Generation utilizes derivatives to manage the utilization of its available generating capacity and the provision of wholesale energy to its affiliates and others. Exelon and Generation also utilize energy option contracts and energy financial swap arrangements to limit the market price risk associated with forward energy commodity contracts. Additionally, Generation enters into certain energy–related derivatives for trading or speculative purposes.

The Registrants' energy contracts are accounted for under SFAS No. 133. Economic hedges may qualify for the normal purchases and normal sales exception to SFAS No. 133 and are accounted for under the accrual method of accounting. Those that do not meet the normal purchase and normal sales exception are recorded as assets or liabilities on the balance sheet at fair value. Changes in the derivatives recorded at fair value are recognized in earnings unless specific hedge accounting criteria are met and they are designated as cash–flow hedges, in which case those changes are recorded in OCI, and gains and losses are recognized in earnings when the underlying transaction occurs or are designated as fair–value hedges, in which case those changes are recognized in current earnings offset by changes in the fair value of the hedged item in current earnings. Changes in the fair value of derivative contracts that do not meet the hedge criteria under SFAS No. 133 (or are not designated as such) and proprietary trading contracts are recognized in current earnings. Generation also has contracted for access to additional generation and sales to load–serving entities that are accounted for under the accrual method of accounting discussed in Note 18 of the Combined Notes to Consolidated Financial Statements within Exelon's 2006 Annual Report on Form 10–K.

ComEd has derivatives related to one wholesale contract and various other contracts to manage the market price exposures to several wholesale contracts that extend through 2007. The contracts that ComEd has entered into as part of the initial ComEd auction (See Note 5 — Regulatory Issues) are deemed to be derivatives that qualify for the normal purchase and normal sale exception to SFAS No. 133. ComEd does not enter into derivatives for speculative or trading purposes.

Some of PECO's gas supply agreements are derivatives under SFAS No. 133 and accounted for as such. Due to the nature of these gas contracts and market conditions, PECO's balance sheet reflected no fair value of energy derivatives at March 31, 2007 as the amounts were insignificant.

Source: EXELON CORP, 10–Q, April 25, 2007

COMBINED NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)

At March 31, 2007, Exelon, Generation and ComEd had net liabilities of $316 million, $319 million and $5 million, respectively, on their Consolidated Balance Sheets for the fair value of energy derivatives. The following table provides a summary of the fair value balances recorded by Exelon, Generation and ComEd as of March 31, 2007:

	March 31, 2007								
	Generation				ComEd				Exelon
Derivatives	Cash-Flow Hedges	Other Derivatives	Proprietary Trading	Subtotal	Cash-Flow Hedge	Other Derivatives	Subtotal	Other(a)	Energy-Related Derivatives(b)
Current assets	$ 94	$ 320	$ 83	$ 497	$ —	$ 1	$ 1	$ 8	$ 506
Noncurrent assets	67	75	9	151	—	—	—	1	152
Total mark-to-market energy contract assets	$ 161	$ 395	$ 92	$ 648	$ —	$ 1	$ 1	$ 9	$ 658
Current liabilities	$ (333)	$ (344)	$ (74)	$ (751)	$ (2)	$ (4)	$ (6)	$ —	$ (757)
Noncurrent liabilities	(114)	(93)	(9)	(216)	—	—	—	(1)	(217)
Total mark-to-market energy contract liabilities	$ (447)	$ (437)	$ (83)	$ (967)	$ (2)	$ (4)	$ (6)	$ (1)	$ (974)
Total mark-to-market energy contract net assets (liabilities)	$ (286)	$ (42)	$ 9	$ (319)	$ (2)	$ (3)	$ (5)	$ 8	$ (316)

(a) Other includes corporate operations, shared service entities, including Exelon Business Services Company (BSC), Enterprises and investments in synthetic fuel-producing facilities.

(b) Excludes Exelon's interest-rate swaps.

At December 31, 2006, Exelon, Generation and ComEd had net assets (liabilities) of $496 million, $499 million and $(11) million, respectively, on their Consolidated Balance Sheets for the fair value of energy derivatives. The following table provides a summary of the fair value balances recorded by Exelon, Generation and ComEd as of December 31, 2006:

	December 31, 2006								
	Generation				ComEd				Exelon
Derivatives	Cash-Flow Hedges	Other Derivatives	Proprietary Trading	Subtotal	Cash-Flow Hedge	Other Derivatives	Subtotal	Other(a)	Energy-Related Derivatives(b)
Current assets	$ 460	$ 751	$ 197	$ 1,408	$ —	$ —	$ —	$ 10	$ 1,418
Noncurrent assets	104	52	15	171	—	—	—	—	171
Total mark-to-market energy contract assets	$ 564	$ 803	$ 212	$ 1,579	$ —	$ —	$ —	$ 10	$ 1,589
Current liabilities	$ (119)	$ (697)	$ (187)	$ (1,003)	$ (6)	$ (5)	$ (11)	$ (1)	$ (1,015)
Noncurrent liabilities	(30)	(33)	(14)	(77)	—	—	—	(1)	(78)
Total mark-to-market energy contract liabilities	$ (149)	$ (730)	$ (201)	$ (1,080)	$ (6)	$ (5)	$ (11)	$ (2)	$ (1,093)
Total mark-to-market energy contract net assets (liabilities)	$ 415	$ 73	$ 11	$ 499	$ (6)	$ (5)	$ (11)	$ 8	$ 496

Source: EXELON CORP, 10-Q, April 25, 2007

(a) Other includes corporate operations, shared service entities, including BSC, Enterprises and investments in synthetic fuel–producing facilities.

(b) Excludes Exelon's interest–rate swaps.

Normal Operations and Hedging Activities (Generation). Electricity available from Generation's owned or contracted generation supply in excess of Generation's obligations to customers, including ComEd's contracted auction requirement and PECO's retail load, is sold into the wholesale markets. To reduce price risk caused by market fluctuations, Generation enters into physical contracts as well as derivative contracts, including forwards, futures, swaps and options, with approved counterparties to hedge anticipated exposures.

Cash–Flow Hedges (Generation and ComEd). The tables below provide details of effective cash–flow hedges under SFAS No. 133 included on Exelon's, Generation's and ComEd's Consolidated Balance Sheets as of March 31, 2007. The data in the table is indicative of the magnitude of SFAS No. 133 hedges Generation and ComEd have in place; however, since under SFAS No. 133 not all derivatives are recorded in OCI, the table does not provide an all–encompassing picture of Generation's and ComEd's derivatives. The tables also include the activity of accumulated OCI related to cash–flow hedges for the three months ended March 31, 2007 and 2006, providing information about the changes in the fair value of hedges and the reclassification from OCI into earnings.

	Total Cash–Flow Hedge OCI Activity, Net of Income Tax		
March 31, 2007	**Generation**	**ComEd**	**Exelon**
Accumulated OCI derivative gain (loss) at December 31, 2006	$ 250	$ (4)	$ 246
Changes in fair value	(411)	1	(410)
Reclassifications from OCI to net income	(13)	2	(11)
Accumulated OCI derivative gain (loss) at March 31, 2007	$ (174)	$ (1)	$ (175)

	Total Cash–Flow Hedge OCI Activity, Net of Income Tax
March 31, 2006	**Exelon and Generation**
Accumulated OCI derivative loss at December 31, 2005	$ (314)
Changes in fair value	46
Reclassifications from OCI to net income	45
Accumulated OCI derivative loss at March 31, 2006	$ (223)

At March 31, 2007, Generation and ComEd had net unrealized pre–tax losses on cash–flow hedges of $289 million and $2 million in accumulated OCI, respectively. Based on market prices at March 31, 2007, approximately $239 million and $2 million of these deferred net pre–tax unrealized losses on derivative instruments in accumulated OCI are expected to be reclassified to earnings during the next twelve months by Generation and ComEd, respectively. However, the actual amount reclassified to earnings could vary due to future changes in market prices. Amounts recorded in accumulated OCI related to changes in energy commodity cash–flow hedges are reclassified to earnings when the forecasted purchase or sale of the energy commodity occurs. The majority of Generation's cash–flow hedges are expected to settle within the next two years, while ComEd's cash flow hedge expires on May 31, 2007.

Source: EXELON CORP, 10–Q, April 25, 2007

Generation's cash–flow hedge activity impact to pre–tax earnings based on the reclassification adjustment from accumulated OCI to earnings was a $21 million pre–tax gain and a $75 million pre–tax loss for the three months ended March 31, 2007 and 2006, respectively. During the three months ended March 31, 2007 and 2006, amounts reclassified from accumulated OCI into earnings as a result of ineffectiveness were not material to the financial statements.

Other Derivatives (Exelon, Generation and ComEd). Exelon, Generation and ComEd enter into certain contracts that are derivatives, but do not qualify for hedge accounting under SFAS No. 133 or are not designated as cash–flow hedges. These contracts are also entered into to economically hedge and limit the market price risk associated with energy commodity prices. Changes in the fair value of these derivative contracts are recognized in current earnings. For the three months ended March 31, 2007 and 2006, Exelon, Generation and ComEd recognized the following net unrealized mark–to–market gains (losses), realized mark–to–market gains (losses) and total mark–to– market gains (losses) (before income taxes) relating to economic hedge mark–to–market activity of certain purchase power and sale contracts pursuant to SFAS No. 133. Generation's, ComEd's and Exelon's other economic hedge mark–to–market activity on purchase power and sale contracts are reported in fuel and purchased power, revenue and operating and maintenance expense, respectively.

	Three Months Ended March 31, 2007			
	Generation	ComEd(a)	Other(b)	Exelon
Unrealized mark–to–market gains (losses)	$ (76)	$ 1	$ (1)	$ (76)
Realized mark–to–market gains (losses)	(39)	1	—	(38)
Total net mark–to–market gains (losses)	$ (115)	$ 2	$ (1)	$ (114)

(a) See "Energy–Related Derivatives" above.
(b) Other includes corporate operations, shared service entities, including BSC, Enterprises and investments in synthetic fuel–producing facilities.

	Three Months Ended March 31, 2006			
	Generation	ComEd(a)	Other(b)	Exelon
Unrealized mark–to–market gains (losses)	$ (57)	$ (10)	$ 13	$ (54)
Realized mark–to–market gains	35	—	—	35
Total net mark–to–market gains (losses)	$ (22)	$ (10)	$ 13	$ (19)

(a) See "Energy–Related Derivatives" above.
(b) Other includes corporate operations, shared service entities, including BSC, Enterprises and investments in synthetic fuel–producing facilities.

Proprietary Trading Activities (Generation). Proprietary trading includes all contracts entered into purely to profit from market price changes as opposed to hedging an exposure and is subject to limits established by Exelon's Risk Management Committee. These contracts are recognized on the Consolidated Balance Sheets at fair value and changes in the fair value of these derivative financial instruments are recognized in earnings. The proprietary trading activities, which included volumes of 5,101 GWhs and 6,985 GWhs for the three months ended March 31, 2007 and 2006, respectively, are a complement to Generation's energy marketing portfolio but represent a very small portion of Generation's revenue from energy marketing activities. For the three months ended March 31, 2007 and 2006, Exelon and Generation recognized the following net unrealized mark–to–market gains, realized mark–to–market losses and total net mark–to–market losses (before income taxes) relating to mark–to–market activity on derivative instruments entered into for trading purposes. Gains and losses associated with financial

Source: EXELON CORP, 10–Q, April 25, 2007

trading are reported as revenue in Exelon's and Generation's Consolidated Statements of Operations and Comprehensive Income.

	Three Months Ended March 31,	
	2007	2006
Unrealized mark–to–market gains	$ —	$ 2
Realized mark–to–market losses	(3)	(2)
Total net mark–to–market losses	$ (3)	$ —

Credit Risk Associated with Derivative Instruments (Exelon and Generation)

The Registrants would be exposed to credit–related losses in the event of non–performance by counterparties that enter into derivative instruments. The credit exposure of derivatives contracts is represented by the fair value of contracts at the reporting date. For energy–related derivative instruments, Generation attempts to enter into enabling agreements that allow for payment netting with its counterparties, which reduces Generation's exposure to counterparty risk by providing for the offset of amounts payable to the counterparty against amounts receivable from the counterparty. Typically, each enabling agreement is for a specific commodity and so, with respect to each individual counterparty, netting is limited to transactions involving that specific commodity product, except where master netting agreements exist with a counterparty that allows for cross product netting. In addition to payment netting language in the enabling agreement, the credit department establishes credit limits and letter of credit requirements for each counterparty, which are defined in the derivatives contracts. Counterparty credit limits are based on an internal credit review that considers a variety of factors, including the results of a scoring model, leverage, liquidity, profitability, credit ratings and risk management capabilities. To the extent that a counterparty's credit limit and letter of credit thresholds are exceeded, the counterparty is required to post collateral with Generation as specified in each enabling agreement. Generation's credit department monitors current and forward credit exposure to counterparties and their affiliates, both on an individual and an aggregate basis.

Under the Illinois auction rules and the supplier forward contracts that Generation entered into with ComEd and Ameren, beginning in 2007, collateral postings will be one–sided from Generation only. That is, if market prices fall below ComEd's or Ameren's contracted price levels, ComEd or Ameren are not required to post collateral; however, if market prices rise above contracted price levels with ComEd or Ameren, Generation may be required to post collateral.

The notional amount of derivatives does not represent amounts that are exchanged by the parties and, thus, is not a measure of the Registrants' exposure. The amounts exchanged are calculated on the basis of the notional or contract amounts, as well as on the other terms of the derivatives, which relate to interest rates and the volatility of these rates. Exelon's and Generation's credit exposure, net of collateral, as of March 31, 2007 and December 31, 2006 were $525 million and $791 million, respectively.

As of March 31, 2007, Generation had $127 million of collateral deposit payments being held by counterparties and Generation was holding $27 million of collateral deposits received from counterparties.

9. Retirement Benefits (Exelon, Generation, ComEd and PECO)

Exelon sponsors defined benefit pension plans and postretirement benefit plans for essentially all Generation, ComEd, PECO and BSC employees, except for those employees of Generation's wholly owned subsidiary,

Source: EXELON CORP, 10–Q, April 25, 2007

AmerGen, who participate in the separate AmerGen–sponsored defined benefit pension plan and postretirement benefit plan.

Defined Benefit Pension and Other Postretirement Benefits — Consolidated Plans (Exelon, Generation, ComEd and PECO)

The following table presents the components of Exelon's net periodic benefit costs for the three months ended March 31, 2007 and 2006. The 2007 pension benefit cost is calculated using an expected long–term rate of return on plan assets of 8.75%. The 2007 other postretirement benefit cost is calculated using an expected long–term rate of return on plan assets of 7.87%. A portion of the net periodic benefit cost is capitalized within the Consolidated Balance Sheets.

Exelon calculates the expected return on pension and other postretirement benefit plan assets by multiplying the expected long–term 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. SFAS No. 87, "Employer's Accounting for Pensions" and SFAS No. 106, "Employers' Accounting for Postretirement Benefits Other than Pensions" 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. Exelon uses a calculated value when determining the MRV of the pension plan assets that adjusts for 20% 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 Exelon applies that expected return. Exelon uses fair value when determining the MRV of the other postretirement benefit plan assets.

	Pension Benefits Three Months Ended March 31,		Other Postretirement Benefits Three Months Ended March 31,	
	2007	**2006**	**2007**	**2006**
Service cost	$ 41	$ 41	$ 25	$ 25
Interest cost	151	142	49	47
Expected return on assets	(204)	(204)	(28)	(26)
Amortization of:				
Transition obligation	—	—	2	2
Prior service cost (benefit)	4	4	(14)	(23)
Actuarial loss	37	40	17	23
Net periodic benefit cost	$ 29	$ 23	$ 51	$ 48

The following approximate amounts were included in capital and operating and maintenance expense during the three months ended March 31, 2007 and 2006, respectively, for Generation's, ComEd's, PECO's and Exelon

Source: EXELON CORP, 10–Q, April 25, 2007

Corporate's allocated portion of the Exelon–sponsored and AmerGen–sponsored pension and postretirement benefit plans:

Pension and Postretirement Benefit Costs	Three Months Ended March 31, 2007	2006
Generation	$ 36	$ 31
ComEd	24	19
PECO	10	10
Exelon Corporate(a)	10	11

(a) Represents amounts billed to Exelon's subsidiaries through intercompany allocations.

Pension and Other Postretirement Benefits — AmerGen Plans (Generation)

The following table presents the components of net periodic benefit costs for the three months ended March 31, 2007 and 2006 for the AmerGen–sponsored plans. The 2007 pension benefit cost is calculated using an expected long–term rate of return on plan assets of 8.75%. A portion of the net periodic benefit cost is capitalized within the Consolidated Balance Sheets. AmerGen uses fair value for purposes of determining the MRV of the pension and other postretirement benefit plan assets.

	Pension Benefits Three Months Ended March 31,		Other Postretirement Benefits Three Months Ended March 31,	
	2007	2006	2007	2006
Service cost	$ 3	$ 3	$ 2	$ 2
Interest cost	2	2	1	1
Expected return on assets	(2)	(2)	—	—
Net periodic benefit cost	$ 3	$ 3	$ 3	$ 3

401(k) Savings Plan (Exelon, Generation, ComEd and PECO)

Exelon, Generation, ComEd and PECO participate in a 401(k) savings plan sponsored by Exelon. The plan allows employees to contribute a portion of their pre–tax income in accordance with specified guidelines. Exelon, Generation, ComEd and PECO match a percentage of the employee contribution up to certain limits. The following table presents, by registrant, the matching contribution to the savings plans during the three months ended March 31, 2007 and 2006:

Savings Plan Matching Contributions	Three Months Ended March 31, 2007	2006
Exelon	$ 16	$ 15
Generation	8	8
ComEd	4	4
PECO	2	2

Source: EXELON CORP, 10–Q, April 25, 2007

10. Income Taxes (Exelon, Generation, ComEd and PECO)

The Registrants' effective income tax rate from continuing operations for the three months ended March 31, 2007 and 2006 varied from the U.S. Federal statutory rate principally due to the following:

	Three Months Ended March 31, 2007			
	Exelon	Generation	ComEd	PECO
U.S. Federal statutory rate	35.0%	35.0%	35.0%	35.0%
Increase (decrease) due to:				
State income taxes, net of Federal income tax benefit	5.4	5.4	4.3	(0.9)
Qualified nuclear decommissioning trust fund income	0.4	0.5	—	—
Plant basis differences	—	—	—	0.4
Synthetic fuel–producing facilities credit(a)	(4.7)	—	—	—
Domestic production activities deduction	(1.4)	(1.5)	—	—
Tax exempt income	(0.3)	(0.3)	—	—
Amortization of investment tax credit	(0.3)	(0.1)	(9.6)	(0.3)
Nontaxable postretirement benefits	(0.3)	(0.1)	(8.9)	(0.2)
Allowance for funds used during construction (AFUDC), equity	—	—	(3.6)	—
Lobbying activities	0.1	—	9.7	—
Forecasted annual tax rate adjustment	(0.3)	(0.1)	11.0	—
Other	(0.7)	(1.1)	(0.4)	—
Effective income tax rate	32.9%	37.7%	37.5%	34.0%

(a) See Notes 2 and 12 of the Combined Notes to Consolidated Financial Statements within Exelon's 2006 Annual Report on Form 10-K for further information regarding investments in synthetic fuel–producing facilities.

	Three Months Ended March 31, 2006			
	Exelon	Generation	ComEd	PECO
U.S. Federal statutory rate	35.0%	35.0%	35.0%	35.0%
Increase (decrease) due to:				
State income taxes, net of Federal income tax benefit	3.4	4.4	4.8	(0.6)
Qualified nuclear decommissioning trust fund income	0.5	0.7	—	—
Amortization of regulatory asset	0.7	—	0.7	—
Plant basis differences	0.1	—	—	0.1
Synthetic fuel–producing facilities credit(a)	(4.4)	—	—	—
Domestic production activities deduction	(0.8)	(1.1)	—	—
Tax exempt income	(0.5)	(0.7)	—	—
Amortization of investment tax credit	(0.5)	(0.3)	(0.8)	(0.4)
Nontaxable postretirement benefits	(0.4)	(0.3)	(0.7)	(0.3)
Lobbying activities	0.6	—	0.3	—
Forecasted annual tax rate adjustment	0.5	—	0.9	0.1
Other	(0.7)	(0.2)	0.5	0.1
Effective income tax rate	33.5%	37.5%	40.7%	34.0%

Source: EXELON CORP, 10–Q, April 25, 2007

(a) See Notes 2 and 12 of the Combined Notes to Consolidated Financial Statements within Exelon's 2006 Annual Report on Form 10-K for further information regarding investments in synthetic fuel-producing facilities.

Accounting for Uncertainty in Income Taxes (Exelon, Generation, ComEd and PECO)

The Registrants adopted the provisions of FIN 48 on January 1, 2007. The following table shows the effect of adopting FIN 48 on the Registrants' Consolidated Balance Sheets as of January 1, 2007.

Increase (decrease)	**Exelon**	**Generation**	**ComEd**	**PECO**
Accounts receivable, net — Other	$ 72	$ —	$ 72	$ 1
Goodwill	(53)	—	(53)	—
Other deferred debits and other assets	378	22	137	208
Accrued expenses	(211)	(2)	(186)	—
Deferred income taxes and unamortized investment tax credits	(86)	28	(299)	185
Other deferred credits and other liabilities	710	31	642	11
Retained earnings	(16)	(35)	(1)	13

As a result of the implementation of FIN 48, Exelon, Generation, ComEd, and PECO have identified unrecognized tax benefits of $1.5 billion, $311 million, $797 million and $318 million, respectively, as of January 1, 2007.

ComEd has identified $21 million of its unrecognized tax benefit at January 1, 2007 that, if recognized, would decrease the effective tax rate. Generation has identified $51 million of its unrecognized tax expense at January 1, 2007 that, if recognized, would increase the effective tax rate.

Generation and PECO have reflected in their Consolidated Balance Sheets as of January 1, 2007 a net interest receivable of $1 million and $20 million, respectively, related to their uncertain income tax positions. Exelon and ComEd have reflected in their Consolidated Balance Sheets as of January 1, 2007 a net interest liability of $134 million and $167 million related to their uncertain income tax positions. The Registrants have not accrued any penalties with respect to unrecognized tax benefits. The Registrants recognize accrued interest related to unrecognized tax benefits in interest expense or interest income and penalties, if any, in operating and maintenance expense on their Consolidated Statements of Operations. Exelon and ComEd have reflected in their Consolidated Statement of Operations as of March 31, 2007 net interest expense of $4 million and $8 million, respectively, related to their uncertain income tax positions. PECO has reflected in its Consolidated Income Statement as of March 31, 2007 net interest income of $3 million related to its uncertain income tax positions.

Exelon and its subsidiaries file a consolidated U.S. Federal income tax return as well as unitary and combined income tax returns in several state jurisdictions with Illinois being the most significant. Exelon and its subsidiaries also file separate company income tax returns in several states with Pennsylvania being the most significant. Exelon and its subsidiaries have completed examinations by the Internal Revenue Service (IRS) for taxable years prior to 1999; however several tax issues remain unresolved for tax years prior to 1999 and have been protested to IRS Appeals, the next administrative level within the IRS. In the second quarter of 2004, the IRS commenced an audit of Exelon and its subsidiaries for taxable years 1999 through 2001 and is expected to complete the audit by the end of 2007. Exelon and its subsidiaries have also completed examinations by the state of Illinois for taxable years prior to 1999 and by the Commonwealth of Pennsylvania on the separate company income tax returns for taxable years ending from 2000 to 2003. However, to the extent adjustments are made to these prior years as either part of a settlement at IRS Appeals or IRS Examination, the state taxable income may also be adjusted.

Source: EXELON CORP, 10-Q, April 25, 2007

It is reasonably possible that the amount of unrecognized tax benefits will significantly increase or decrease in the next twelve months as a result of settling several uncertain tax positions. ComEd is in the process of negotiating with IRS Appeals a settlement related to research and development refund claims filed by ComEd for taxable years 1989 through 1998. At this point, an estimate of a change, if any, to the unrecognized tax benefit amount cannot be made. A majority of the refund claim relates to ComEd's formerly owned generation property. Pursuant to the asset transfer agreement between ComEd and Generation, any current tax benefit related to this unrecognized tax benefit as well as a portion of the related interest income would be recorded to ComEd's goodwill as it relates to taxable periods prior to the PECO /Unicom merger as required under EITF 93–7. Generation would record the offsetting future deferred tax effects, which would impact future period earnings. ComEd and PECO also have several other issues at the IRS Appeals for taxable years 1996 through 1998 that, if settled, would not significantly increase or decrease the total amount of unrecognized tax benefits.

As part of the Federal examination of taxable years 1999 through 2001, the IRS has issued proposed adjustments related to ComEd's deferral of gain on the 1999 sale of its fossil plants. See "1999 Sale of Fossil Generating Assets" below for details. ComEd's management is in the process of evaluating its options with respect to the proposed tax deficiency. Those options include either protesting the disallowance to the IRS Appeals Division or possible litigation. If ComEd's management decides to litigate the matter, ComEd may be required to pay the tax and related interest due on the deficiency and file for refund. Paying the tax liability and interest with respect to the gain deferral of the fossil plant sale and its related issues may result in a decrease in the amount of unrecognized tax benefits by as much as $433 million.

The IRS has also proposed an adjustment requiring the capitalization of certain merger costs previously deducted, associated with the PECO / Unicom merger. Management is currently reviewing the proposed adjustment to determine if it agrees, but if accepted, Exelon and PECO would reduce the amount of its unrecognized tax benefits by approximately $16 million and $10 million, respectively.

Generation and ComEd filed refund claims related to taxable years 1999 through 2004 for research and development expenditures. The IRS is in the early stages of the audit of those claims. At this point, an estimate of a change, if any, to the unrecognized tax benefit amount cannot be made.

Certain of ComEd and PECO's tax positions evaluated under FIN 48 are dependent on ComEd and PECO having sufficient tax basis in its fixed assets. Should ComEd and PECO obtain any future benefit associated with the Simplified Service Cost Method (SSCM) accounting method change (discussed fully below), it will require a reduction to the tax basis of assets. As a result, the SSCM could have an effect on the unrecognized tax benefits associated with other tax positions that are dependent on tax basis.

Simplified Service Cost Method (Exelon, ComEd and PECO)

In 2001, ComEd and PECO filed a request with the IRS to change their tax method of accounting for certain capitalized overhead costs. The requested tax method of accounting, the SSCM, is expressly permitted under IRS regulations. The effect of the tax method change results in the immediate expensing of certain overhead costs that were previously capitalized to self–constructed property. During the first quarter of 2007, the IRS granted the tax method change. In April 2007, ComEd and PECO signed the consent agreements, thus making the tax method change effective as of that date. The consent agreement has terms and conditions that subject the change to certain published guidance as well as future guidelines and directives to be issued by the IRS. As a result of the uncertainty of forthcoming IRS settlement guidelines, ComEd and PECO are currently unable to estimate the tax benefit associated with the SSCM. ComEd and PECO have entered into an agreement with a tax consultant related to the filing of this tax method change request. The fee for this agreement is contingent upon receiving consent from the IRS and is based upon a percentage of the refunds recovered from the IRS, if any. The ultimate net cash impacts to

Source: EXELON CORP, 10–Q, April 25, 2007

ComEd and PECO related to this agreement will either be positive or neutral depending upon the outcome of the refund claim with the IRS. These potential tax benefits and associated fees would be recorded in accordance with FIN 48 and SFAS No. 5, "Accounting for Contingencies" (SFAS No. 5), respectively, and could be material to the financial position, results of operations and cash flows of ComEd and PECO.

1999 Sale of Fossil Generating Assets (Exelon and ComEd)

Exelon, through its ComEd subsidiary, has taken certain tax positions, which have been disclosed to the IRS, to defer the tax gain on the 1999 sale of its fossil generating assets. As of March 31, 2007 and December 31, 2006, deferred tax liabilities related to the fossil plant sale are reflected in Exelon's Consolidated Balance Sheets with the majority allocated to ComEd and the remainder to Generation. The Federal tax returns and related tax return disclosures covering the period of the 1999 sale are currently under IRS audit. Exelon's ability to continue to defer all or a portion of this liability depends on whether its treatment of the sales proceeds, as having been received in connection with an involuntary conversion is proper pursuant to applicable law. In November 2006, ComEd received from the IRS a notice of proposed adjustment disallowing the deferral of gain associated with its position that proceeds from the fossil plant sales resulted from an "involuntary conversion."

Exelon's and ComEd's ability to continue to defer the remainder of the tax liability on the fossil plant sale may depend in part on whether its tax characterization of a sale leaseback transaction into which Exelon entered in connection with the fossil plant sale is proper pursuant to applicable law. In February 2007, Exelon received from the IRS a notice of proposed adjustment disallowing the deferral of gain associated with its sale leaseback transaction. The IRS has indicated its position that the Exelon sale leaseback transaction is substantially similar to a leasing transaction, a sale–in, lease–out (SILO), the IRS is treating as a "listed transaction" pursuant to guidance it issued in 2005. A listed transaction is one which the IRS considers to be a potentially abusive tax shelter. Exelon disagrees with the IRS's characterization of its sale leaseback as a SILO and believes its position is correct and will continue to aggressively defend that position upon audit and any subsequent appeals or litigation.

In final form, both the notice for the involuntary conversion and the like kind exchange will be in the IRS' audit report expected to be issued in the second or third quarter of 2007. Upon receipt of the final IRS report, Exelon will have the opportunity to either appeal the disallowance to the IRS Appeals, the next administrative level of the IRS, or litigate the matter. If Exelon's and ComEd's management decides to litigate, the matter it may be required to pay the tax and related interest due on the deficiency and file for refund.

A successful IRS challenge to ComEd's positions would accelerate future income tax payments and increase interest expense related to the deferred tax gain that becomes currently payable. As of March 31, 2007, Exelon's and ComEd's potential cash outflow, including tax and interest (after tax), could be as much as $978 million. If the deferral were successfully challenged by the IRS, it could negatively impact Exelon's and ComEd's results of operations by as much as $146 million (after tax) related to interest expense. Exelon's and ComEd's management believe a reserve for interest has been appropriately recorded in accordance with FIN 48; however, the ultimate outcome of such matters could result in unfavorable or favorable adjustments to the results of operations, and such adjustments could be material. Final resolution of this matter is not anticipated for several years.

Investments in Synthetic Fuel–Producing Facilities (Exelon)

Exelon, through three separate wholly owned subsidiaries, owns interests in two limited liability companies and one limited partnership (the Sellers) that own synthetic fuel–producing facilities. Section 45K (formerly Section 29) of the Internal Revenue Code provides tax credits for the sale of synthetic fuel produced from coal. However, Section 45K contains a provision under which the tax credits are phased out (i.e., eliminated) in the event crude oil prices for a year exceed certain thresholds. Exelon is required to pay for tax credits based on the production

Source: EXELON CORP, 10–Q, April 25, 2007

of the facilities regardless of whether or not a phase–out of the tax credits is anticipated. However, Exelon has the legal right to recover a portion of the payments made to the Sellers related to phased–out tax credits.

In April 2007, the IRS published the 2006 oil Reference Price which resulted in a 33% phase–out of tax credits for calendar year 2006 which reduced Exelon's earned after–tax credits of $164 million to $110 million for the year ended December 31, 2006. At December 31, 2006, Exelon had estimated the 2006 phase–out to be 38% and had receivables on its Consolidated Balance Sheet from the Sellers totaling $63 million associated with the portion of the payments previously made to the Sellers related to tax credits that were anticipated to be phased out for 2006. The difference between the actual 2006 phase–out and the 2006 phase–out estimated at December 31, 2006 resulted in a $9 million increase in tax credits for 2006 and a corresponding $6 million decrease, net of the related tax benefit, in the receivables due from the Sellers as of December 31, 2006, which will be reflected in Exelon's operating results in the second quarter of 2007.

The following table (in dollars) provides the estimated phase–out range for 2007 based on the per barrel price of oil as of March 31, 2007. The table also contains the estimated 2007 annual average New York Mercantile Exchange, Inc. index (NYMEX) price per barrel at March 31, 2007 based on year–to–date and futures prices.

	Estimated 2007
Beginning of Phase–Out Range(a)	$ 62
End of Phase–Out Range(a)	78
2007 Annual Average NYMEX	66

(a) The estimated 2007 phase–out range as of March 31, 2007 is based upon the actual 2006 phase–out range. The actual 2006 phase–out range was determined using the inflation adjustment factor published by the IRS in April 2007. The actual 2006 phase–out range was increased by 2% (Exelon's estimate of inflation) to arrive at the estimated 2007 phase–out range.

At March 31, 2007, Exelon had receivables on its Consolidated Balance Sheet from the Sellers totaling $18 million associated with the portion of the payments previously made to the Sellers related to tax credits that are anticipated to be phased out in 2007. As of March 31, 2007, Exelon has estimated the 2007 phase–out to be 27%, which has reduced Exelon's earned after–tax credits of $65 million to $48 million for the three months ended March 31, 2007. These credits may be further phased out during the remainder of 2007 depending on the price of oil; however, as these tax credits are phased out, Exelon anticipates recording income through the establishment of additional receivables from the Sellers or from derivatives entered into in 2005 (as more fully described below) depending on the magnitude of the credits phased–out.

In 2005, Exelon and Generation entered into certain derivatives in the normal course of trading operations to economically hedge a portion of the exposure to a phase–out of the tax credits. One of the Sellers has security interests in these derivatives. Including the related mark–to–market gains and losses on these derivatives, interests in synthetic fuel–producing facilities increased Exelon's net income by $25 million and $12 million during the three months ended March 31, 2007 and 2006, respectively. Exelon anticipates that it will continue to record income or losses related to the mark–to–market gains or losses on its derivative instruments and changes to the tax credits earned by Exelon during the period of production as a result of volatility in oil prices.

Net income from interests in synthetic fuel–producing facilities is reflected in the Consolidated Statements of Operations and Comprehensive Income within income taxes, operating and maintenance expense, depreciation and amortization expense, interest expense, equity in losses of unconsolidated affiliates and other, net.

There are provisions in the agreements between the parties, such as low production volume, unanimous consents between the parties and defaults by the parties, which would allow or cause an early termination of the

Source: EXELON CORP, 10–Q, April 25, 2007

partnerships. If none of the parties to the agreements takes action to terminate the partnerships early, the partnerships will terminate in 2008.

The non–recourse notes payable principal balance was $74 million and $108 million at March 31, 2007 and December 31, 2006, respectively. The non–recourse notes payable can be relieved either through eventual payments or possibly through extinguishment which may occur subsequent to termination of the partnership pursuant to the agreements between the parties.

11. Asset Retirement Obligations (Exelon and Generation)

Nuclear Decommissioning Asset Retirement Obligations (ARO)

Exelon, Generation and AmerGen have legal obligations to decommission their nuclear power plants following the expiration of their operating licenses. Exelon, Generation and AmerGen will pay for their respective obligations using trust funds that have been established for this purpose.

The following table provides a rollforward of the nuclear decommissioning ARO reflected on Exelon's and Generation's Consolidated Balance Sheets, from January 1, 2007 to March 31, 2007:

	Exelon and Generation
Nuclear decommissioning AROs at January 1, 2007	$ 3,533
Accretion expense	57
Payments to decommission retired plants	(3)
Nuclear decommissioning AROs at March 31, 2007	$ 3,587

Exelon and Generation update their nuclear decommissioning AROs on a periodic basis; however, there were no changes in the underlying assumptions that would result in a significant change to the estimated future cash flows during the first quarter of 2007 or 2006.

Nuclear Decommissioning Trust Fund Investments

The trust funds that have been established to satisfy Exelon's and Generation's nuclear decommissioning obligations were originally funded with amounts collected from customers. Certain of these trust funds will continue to be funded by future collections from PECO customers.

At March 31, 2007 and December 31, 2006, Exelon and Generation had nuclear decommissioning trust fund investments totaling $6,540 million and $6,415 million, respectively.

At March 31, 2007 and December 31, 2006, Exelon and Generation had gross unrealized gains of $1,353 million and $1,287 million, respectively, related to the nuclear decommissioning trust fund investments, which were included in regulatory liabilities or accumulated other comprehensive income in Exelon's Consolidated Balance Sheets and in noncurrent payables to affiliates or accumulated other comprehensive income in Generation's Consolidated Balance Sheets. Exelon and Generation consider all nuclear decommissioning trust fund investments in an unrealized loss position to be other–than–temporarily impaired. As a result of certain Nuclear Regulatory Commission restrictions, Exelon and Generation are unable to demonstrate the ability and intent to hold the nuclear decommissioning trust fund investments through a recovery period and accordingly recognizes any unrealized holding losses immediately. For the three months ended March 31, 2007, Generation recorded impairment charges totaling $8 million and $2 million associated with the nuclear decommissioning trust funds for the former ComEd and the AmerGen units, respectively. For the three months ended March 31, 2006, Generation recorded impairment charges totaling $3 million associated with the nuclear decommissioning trust funds for the former ComEd units.

Source: EXELON CORP, 10–Q, April 25, 2007

As a result of the sale of nuclear decommissioning trust fund investments, Exelon and Generation realized gains of $9 million for the three months ended March 31, 2007 and realized losses of $2 million for the three months ended March 31, 2006 on nuclear decommissioning trust funds.

Refer to Notes 9 and 13 of the Combined Notes to Consolidated Financial Statements within Exelon's 2006 Annual Report on Form 10-K for a full discussion of the accounting for nuclear decommissioning obligations, nuclear decommissioning trust funds and the corresponding accounting implications resulting from agreements entered into with ComEd and PECO at the time of the corporate restructuring effective January 1, 2001. In addition, see Note 16 — Related Party Transactions for information regarding intercompany balances between Generation, ComEd and PECO reflecting the obligation to refund to customers any decommissioning-related assets in excess of the related decommissioning obligations.

12. Earnings Per Share and Shareholders' Equity (Exelon)

Earnings per Share

Diluted earnings per share are calculated by dividing net income by the weighted average number of shares of common stock outstanding, including shares to be issued upon exercise of stock options, performance share awards and restricted stock outstanding under Exelon's long-term incentive plans considered to be common stock equivalents. The following table sets forth the components of basic and diluted earnings per share and shows the effect of these stock options, performance share awards and restricted stock on the weighted average number of shares outstanding used in calculating diluted earnings per share:

	Three Months Ended March 31,	
	2007	**2006**
Income from continuing operations	$ 681	$ 399
Income from discontinued operations	10	1
Net income	$ 691	$ 400
Average common shares outstanding — basic	672	669
Assumed exercise of stock options, performance share awards and restricted stock	5	6
Average common shares outstanding — diluted	677	675

The number of stock options not included in the calculation of diluted common shares outstanding due to their antidilutive effect was 3 million and 4 million for the three months ended March 31, 2007 and 2006, respectively.

Share Repurchases

In April 2004, Exelon's Board of Directors approved a discretionary share repurchase program that allows Exelon to repurchase shares of its common stock on a periodic basis in the open market. See Note 16 of the Combined Notes to Consolidated Financial Statements within Exelon's 2006 Annual Report on Form 10-K for further information regarding Exelon's share repurchase program. Repurchased shares are held as treasury shares and recorded at cost. As of March 31, 2007, 13 million shares of common stock have been purchased under the share repurchase program for $652 million. During the three months ended March 31, 2007 and 2006, Exelon repurchased 0.6 million shares and 0.9 million shares, respectively, of common stock under the share repurchase program for $37 million and $54 million, respectively.

Source: EXELON CORP, 10-Q, April 25, 2007

Long–Term Incentive Plans

The following table presents the stock–based compensation expense included in Exelon's Consolidated Statements of Income and Comprehensive Income during the three months ended March 31, 2007 and 2006:

	Three Months Ended March 31,	
	2007	2006
Stock options	$ 15	$ 17
Performance shares	17	21
Restricted stock units	6	1
Total stock–based compensation included in operating and maintenance expense	38	39
Income tax benefit	(15)	(15)
Total after–tax stock–based compensation expense	$ 23	$ 24

Stock Options and Performance Shares

For information regarding stock options and performance shares, see Notes 1 and 16 of the Combined Notes to Consolidated Financial Statements within Exelon's 2006 Annual Report on Form 10–K.

Restricted Stock Units

Beginning in January 2007, Exelon began granting key managers restricted stock units in lieu of stock options through its long–term incentive plans. During the three months ended March 31, 2007, Exelon granted 331,745 restricted stock units, which will vest and settle over a three–year period.

In accordance with SFAS No. 123 (revised 2004), "Share–Based Payment" (SFAS No. 123–R), the cost of services received from employees in exchange for the issuance of restricted stock units is required to be measured based on the grant–date fair value of the restricted stock unit issued. The value of the restricted stock units at the date of grant is either amortized through expense over the requisite service period using the straight–line method or capitalized. For non–retirement eligible individuals, the substantive service period was determined to be the three–year vesting period. The cost associated with restricted stock units granted to employees who are retirement eligible is recognized immediately upon the date of grant, as the employees are not required to render any further service to earn the restricted stock units. For employees who become retirement eligible during the substantive service period, the cost of the restricted stock units is recognized on a straight–line basis over the requisite service period.

The holders of the restricted stock units will be paid shares of common stock annually during the vesting period of three years. During the three months ended March 31, 2007, Exelon had costs of $5 million related to outstanding awards not yet settled.

13. Commitments and Contingencies (Exelon, Generation, ComEd and PECO)

For information regarding capital commitments and nuclear decommissioning at December 31, 2006, see Notes 13 and 18 of the Combined Notes to Consolidated Financial Statements within Exelon's 2006 Annual Report on Form 10–K. All significant contingencies are disclosed below.

Source: EXELON CORP, 10–Q, April 25, 2007

Energy Commitments

Generation's long–term commitments relating to the purchase from and sale to unaffiliated utilities and others of energy, capacity and transmission rights as of March 31, 2007 did not change significantly from December 31, 2006, except for the following:

- Generation's total commitments for future sales of energy to unaffiliated third–party utilities and others increased by approximately $149 million during the three months ended March 31, 2007, reflecting increases of approximately $578 million, $346 million and $121 million in 2008, 2009 and 2010 sales commitments, respectively, offset by the fulfillment of approximately $896 million of 2007 commitments during the three months ended March 31, 2007. The increases were primarily due to increased forward sales of energy to counterparties other than ComEd as a result of the expiration of the PPA with ComEd on December 31, 2006, as well as increased overall hedging activity in the normal course of business.

As a result of the first reverse–auction competitive bidding process, ComEd is procuring substantially all of its supply under supplier forward contracts with various suppliers. See Note 5 — Regulatory Issues for further information.

Fuel Purchase Obligations

Generation's and PECO's fuel purchase obligations as of March 31, 2007 did not change significantly from December 31, 2006, except for the following:

- Generation's total fuel purchase obligations for nuclear and fossil generation as of March 31, 2007 increased by $58 million for 2008, $89 million for 2009 and 2010, and $270 million for 2011 and beyond, as compared to December 31, 2006 due to contracts entered into in the normal course of business.
- PECO's total fuel purchase obligations increased by approximately $105 million during the three months ended March 31, 2007, reflecting an increase of $19 million, $36 million, $31 million and $19 million in 2007, 2008, 2009 and 2010, respectively, primarily related to the purchase of natural gas and related transportation services.

Commercial Commitments

Exelon's, Generation's, ComEd's and PECO's commercial commitments as of March 31, 2007, representing commitments potentially triggered by future events, did not change significantly from December 31, 2006, except for the following:

- Exelon's guarantees increased by $211 million primarily as a result of leasing activities, energy trading and performance guarantees.
- Generation's letters of credit increased by $6 million and its guarantees (outside the scope of FIN 45) increased by $175 million primarily as a result of energy trading activities and the performance guaranty agreement entered into in connection with the sale of TEG and TEP.

Environmental Liabilities

The Registrants' operations have in the past and may in the future require substantial expenditures in order to comply with environmental laws. Additionally, under Federal and state environmental laws, the Registrants are generally liable for the costs of remediating environmental contamination of property now or formerly owned by them and of property contaminated by hazardous substances generated by them. The Registrants own or lease a

Source: EXELON CORP, 10–Q, April 25, 2007

number of real estate parcels, including parcels on which their operations or the operations of others may have resulted in contamination by substances that are considered hazardous under environmental laws. ComEd and PECO have identified 42 and 27 sites, respectively, where former manufactured gas plant (MGP) activities have or may have resulted in actual site contamination. For almost all of these sites, ComEd or PECO is one of several Potentially Responsible Parties (PRPs) which may be responsible for ultimate remediation of each location. Of these 42 sites identified by ComEd, the Illinois Environmental Protection Agency has approved the clean up of nine sites and of the 27 sites identified by PECO, the Pennsylvania Department of Environmental Protection has approved the cleanup of 12 sites. Of the remaining sites identified by ComEd and PECO, 20 and 10 sites, respectively, are currently under some degree of active study and/or remediation. ComEd and PECO anticipate that the majority of the remediation at these sites will continue through at least 2015 and 2012, respectively. In addition, the Registrants are currently involved in a number of proceedings relating to sites where hazardous substances have been deposited and may be subject to additional proceedings in the future.

ComEd and Nicor Gas Company, a subsidiary of Nicor Inc. (Nicor), are parties to an interim agreement under which they cooperate in remediation activities at 38 former MGP sites for which ComEd or Nicor, or both, may have responsibility. Under the interim agreement, costs are split evenly between ComEd and Nicor pending their final agreement on allocation of costs at each site, but either party may demand arbitration if the parties cannot agree on a final allocation of costs. For most of the sites, the interim agreement contemplates that neither party will pay less than 20%, nor more than 80% of the final costs for each site. ComEd's accrual for these environmental liabilities is based on ComEd's estimate of its 50% share of costs under the interim agreement with Nicor. On April 17, 2006, Nicor submitted a demand for arbitration of the cost allocation for 38 MGP sites. Through March 31, 2007, ComEd has incurred approximately $117 million associated with remediation of the sites in question. Although ComEd believes that the arbitration proceedings will not result in an allocation of costs materially different from ComEd's current estimate of its aggregate remediation costs for MGP sites, the outcome of the arbitration proceedings is not certain and could result in a material increase or decrease of ComEd's estimate of its share of the aggregate remediation costs.

Based on the final order received in ComEd's Rate Case, beginning in 2007, ComEd is recovering MGP remediation costs from customers for which it established a regulatory asset (see ComEd Rate Case below). Pursuant to a PAPUC order, PECO is currently recovering a provision for environmental costs annually for the remediation of former MGP facility sites, for which PECO has recorded a regulatory asset. See Note 14 — Supplemental Financial Information for further information regarding regulatory assets and liabilities.

As of March 31, 2007 and December 31, 2006, Exelon, Generation, ComEd and PECO had accrued the following amounts for environmental liabilities:

March 31, 2007	Total Environmental Investigation and Remediation Reserve	Portion of Total Related to MGP Investigation and Remediation
Exelon	$ 114	$ 86
Generation	19	—
ComEd	56	49
PECO	39	37

Source: EXELON CORP, 10-Q, April 25, 2007

December 31, 2006	Total Environmental Investigation and Remediation Reserve	Portion of Total Related to MGP Investigation and Remediation
Exelon	$ 119	$ 88
Generation	20	—
ComEd	58	49
PECO	41	39

The Registrants cannot predict the extent to which they will incur other significant liabilities for additional investigation and remediation costs at these or additional sites identified by environmental agencies or others, or whether such costs may be recoverable from third parties.

Section 316(b) of the Clean Water Act

In July 2004, the United States Environmental Protection Agency (EPA) issued the final Phase II rule implementing Section 316(b) of the Clean Water Act. The Clean Water Act requires that the cooling water intake structures at electric power plants reflect the best technology available to minimize adverse environmental impacts. The Phase II rule established national performance standards for reducing entrainment and impingement of aquatic organisms at existing power plants. The rule provided each facility with a number of compliance options and permitted site–specific variances based on a cost–benefit analysis. The requirements were intended to be implemented through state–level National Pollutant Discharge Elimination System (NPDES) permit programs. All of Generation's power generation facilities with cooling water systems are subject to the regulations. Facilities without closed–cycle recirculating systems (e.g., cooling towers) are potentially most affected. Those facilities are Clinton, Cromby, Dresden, Eddystone, Fairless Hills, Handley, Mountain Creek, New Boston, Oyster Creek, Peach Bottom, Quad Cities, Salem and Schuylkill. Since promulgation of the rule, Generation has been evaluating compliance options at each of its affected plants to achieve interim compliance deadlines.

On January 25, 2007, the U.S. Court of Appeals for the Second Circuit issued its opinion in a challenge to the final Phase II rule brought by environmental groups and several states. The court found that, with respect to a number of significant provisions of the rule, the EPA either exceeded its authority under the Clean Water Act, failed to adequately set forth its rationale for the rule, or failed to follow required procedures for public notice and comment. The court remanded the rule back to the EPA for revisions consistent with the court's opinion. By its action, the court invalidated compliance measures that the utility industry supported because they were cost–effective and provided existing plants with needed flexibility in selecting the compliance option appropriate to its location and operations. For example, the court found that environmental restoration does not qualify as a compliance option and site–specific compliance variances based on a cost–benefit analysis are impermissible.

The court's decision has created significant uncertainty about the specific nature, scope and timing of the final compliance requirements. It is not yet known whether the EPA, or any of the industry petitioners, will seek an *en banc* rehearing by the entire Second Circuit panel, or file a petition for *certiorari* seeking review by the U.S. Supreme Court. In the interim, the EPA has announced the suspension of the Phase II rule due to the uncertainty about the specific compliance requirements created by the court's remand of significant provisions of the rule. Until the EPA finalizes the rule on remand, the state permitting agencies will continue the current practice of applying their best professional judgment to address impingement and entrainment requirements at plant cooling water intake structures. Due to this uncertainty, Generation cannot estimate the effect that compliance with the Phase II rule requirements will have on the operation of its generating facilities and its future results of operations, financial condition and cash flows. If the final rule has performance standards that require the reduction of cooling

Source: EXELON CORP, 10–Q, April 25, 2007

water intake flow at the plants consistent with closed loop cooling systems, then the impact on the operation of the facilities and Exelon's and Generation's future results of operations, financial position and cash flows could be material.

In a pre–draft permit dated May 13, 2005 and a draft permit issued on July 19, 2005, as part of the NPDES permit renewal process for Oyster Creek that has been pending since 1999, the New Jersey Department of Environmental Protection (NJDEP) preliminarily determined that closed–cycle cooling and environmental restoration are the only viable compliance options for Section 316(b) compliance at Oyster Creek. The final permit has not been issued, and Oyster Creek has continued to operate under the 1999 permit. Generation cannot predict with any certainty how the NJDEP will implement its best professional judgment. AmerGen has not made a determination regarding how it will comply with the Section 316(b) regulations and must first evaluate the final regulations issued by the EPA as a result of the decision of the U.S. Court of Appeals for the Second Circuit, discussed above. In addition, the cost required to retrofit Oyster Creek with closed cycle cooling could be material and could therefore negatively impact Generation's decision to renew the plant's operating license.

In June 2001, the NJDEP issued a renewed NPDES permit for Salem, which expired in July 2006, allowing for the continued operation of Salem with its existing cooling water system. NJDEP advised Public Service Enterprise Group Incorporated (PSEG), the plant operator, in a letter dated July 12, 2004 that it strongly recommended reducing cooling water intake flow commensurate with closed–cycle cooling as a compliance option for Salem. PSEG submitted an application for a renewal of the permit on February 1, 2006. In the permit renewal application, PSEG analyzed closed–cycle cooling and other options and demonstrated that the continuation of the Estuary Enhancement Program, an extensive environmental restoration program at Salem, along with continued operation of the existing intake, is the best available technology to meet the Section 316(b) requirements. PSEG continues to operate Salem under the approved June 2001 NPDES permit while the NPDES permit renewal application is being reviewed. PSEG must evaluate the final Phase II rule after remand, particularly whether the restoration done under the Estuary Enhancement Project remains a compliance option. If application of the final Section 316(b) regulations or the NJDEP as a result of the Phase II ruling discussed above ultimately requires the retrofitting of Salem's cooling water intake structure to reduce cooling water intake flow commensurate with closed–cycle cooling, Exelon's and Generation's share of the total cost of the retrofit and any resulting interim replacement power would likely be in excess of $500 million and could result in increased depreciation expense related to the retrofit investment.

Nuclear Generating Station Groundwater

On December 16, 2005 and February 27, 2006, the Illinois EPA issued violation notices to Generation alleging violations of state groundwater standards as a result of historical discharges of liquid tritium from a line at the Braidwood Nuclear Generating Station (Braidwood). In November 2005, Generation discovered that spills from the line in 1996, 1998 and 2000 have resulted in a tritium plume in groundwater that is both on and off the plant site. Levels in portions of the plume exceed Federal limits for drinking water. However, samples from drinking water wells on property adjacent to the plant showed that, with one exception, tritium levels in these wells were at levels that naturally occur. The tritium level in one drinking water well was elevated above levels that occur naturally, but was significantly below the state and Federal drinking water standards, and Generation believes that this level posed no threat to human health. Generation has investigated the causes of the releases and has taken the necessary corrective actions to prevent another occurrence. Generation notified the owners of 14 potentially affected adjacent properties that, upon sale of their property, Generation will reimburse the owners for any diminution in property value caused by the tritium release. As of March 31, 2007, Generation has purchased four of the 14 adjacent properties.

On March 13, 2006, a class action lawsuit was filed against Exelon, Generation and ComEd (as the prior owner of Braidwood) in Federal District Court for the Northern District of Illinois on behalf of all persons who live or own

Source: EXELON CORP, 10–Q, April 25, 2007

property within 10 miles of Braidwood. Initially, the plaintiffs primarily sought compensation for diminished property values, but in February 2007, they amended their complaint to seek punitive damages. The U.S. District Court for the Northern District of Illinois denied the class action status of the lawsuit on March 19, 2007. Plaintiffs have requested reconsideration and are seeking certification of a class of approximately 200 persons whose property allegedly has tritium at levels below detection level, along with a class of adjacent property owners (unspecified in number) that have allegedly been impacted by tritium from the plant. Exelon, Generation and ComEd will oppose class certification on these bases.

On March 14 and 23, 2006, 37 area residents filed two separate but identical lawsuits against Exelon, Generation and ComEd in the Circuit Court of Will County, Illinois alleging property contamination and seeking compensation for diminished property values. Exelon removed these cases to Federal court, and all three cases were assigned to the same District Court judge. Subsequently, seven plaintiffs withdrew from the cases, and 18 additional plaintiffs were added. On October 11, 2006, two area residents filed a lawsuit in the U.S. District Court for the Northern District of Illinois against Exelon, Generation and ComEd. The allegations in the complaint are substantially similar to the lawsuits described above, and the case has been transferred to the judge overseeing the other Federal cases.

Exelon, Generation and ComEd, have tendered the defense for all of these lawsuits described above to their insurance carrier, ANI, and ANI has agreed to defend the suits subject to a reservation of rights. Exelon, Generation and ComEd continue to believe that these lawsuits are without merit and will continue to vigorously defend them.

On March 16, 2006, the Attorney General of the State of Illinois and the State's Attorney for Will County, Illinois filed a civil enforcement action against Exelon, Generation and ComEd in the Circuit Court of Will County relating to the releases of tritium discussed above and alleging that, beginning on or before 1996, and with additional events in 1998, 2000 and 2005, there have been tritium and other non–radioactive wastes discharged from Braidwood in violation of Braidwood's NPDES permit, the Illinois Environmental Protection Act and regulations of the Illinois Pollution Control Board. The lawsuit seeks injunctive relief relating to the discontinuation of the liquid tritium discharge line until further court order, soil and groundwater testing, prevention of future releases and off–site migration and to provide potable drinking water to area residents. The action also seeks the maximum civil penalties allowed by the statute and regulations, $10,000 or $50,000 for each violation (depending on the specific violation), and $10,000 for each day during which a violation continues. On May 24, 2006, the Circuit Court of Will County, Illinois entered an order resulting in Generation commencing remediation efforts in June 2006 for tritium in groundwater off of plant property. Among other things, the May 24, 2006 order requires Generation to conduct certain studies and implement measures to ensure that tritium does not leave plant property at levels in excess of the United States EPA safe drinking water standard. Any civil penalty will not be determined until the consent decree is finalized. Furthermore, the Circuit Court of Will County may exercise its discretion in determining the final penalty, if any, taking into account a number of factors, including corrective actions taken by Generation and other mitigating circumstances.

As of March 31, 2007 and December 31, 2006, Generation had reserves of $3 million and $3 million (pre–tax), respectively, related to the matters described above, which Generation deems adequate to cover the costs of remediation and potential related corrective measures.

As a result of intensified monitoring and inspection efforts in 2006, Generation detected small underground tritium leaks at the Dresden Nuclear Generating Station (Dresden) and at the Byron Nuclear Generating Station (Byron). Neither of these discharges occurred outside the property lines of the plant, nor does Generation believe either of these matters poses health or safety threats to employees or to the public. Generation identified the source

Source: EXELON CORP, 10–Q, April 25, 2007

of the leaks and implemented repairs. On March 31, 2006 and April 12, 2006, the Illinois EPA issued a violation notice to Generation in connection with the Dresden and Byron leaks, respectively, alleging various violations, including those related to (1) Illinois groundwater standards, (2) non–permitted discharges, and (3) each station's NPDES permit. Generation has analyzed the remediation options related to these matters and submitted its response and proposed remediation plan to the Illinois EPA. On July 10, 2006, the Illinois EPA rejected the remediation plan for Dresden and on July 12, 2006, the Illinois EPA sent a Notice of Intention to Pursue Legal Action. On July 17, 2006, the Illinois EPA rejected the remediation plan for Byron and has referred the matter to the Illinois Attorney General for consideration of formal enforcement action and the imposition of penalties.

Generation is actively discussing the violation notices and Attorney General civil enforcement matters for Braidwood, Dresden and Byron, discussed above, with the Illinois EPA and the Attorneys General for Illinois and the Counties in which the plants are located. While Generation is unable to determine the amount of the civil penalties that will be included in a final consent decree, it is probable that they will exceed $100,000 in the aggregate for all three stations but will not be material to Exelon's and Generation's financial position, results of operations and cash flows. Generation expects these matters to be resolved during 2007.

Exelon, Generation or ComEd cannot determine the outcome of the above–described matters but believe their ultimate resolution should not, after consideration of reserves established, have a significant impact on Exelon's, Generation's or ComEd's financial position, results of operations or cash flows.

Cotter Corporation

The EPA has advised Cotter Corporation (Cotter), a former ComEd subsidiary, that it is potentially liable in connection with radiological contamination at a site known as the West Lake Landfill in Missouri. On February 18, 2000, ComEd sold Cotter to an unaffiliated third party. As part of the sale, ComEd agreed to indemnify Cotter for any liability incurred by Cotter as a result of any liability arising in connection with the West Lake Landfill. In connection with Exelon's 2001 corporate restructuring, this responsibility to indemnify Cotter was transferred to Generation. Cotter is alleged to have disposed of approximately 39,000 tons of soils mixed with 8,700 tons of leached barium sulfate at the site. Cotter, along with three other companies identified by the EPA as PRPs, has submitted a draft feasibility study addressing options for remediation of the site. The PRPs are also engaged in discussions with the State of Missouri and the EPA. The estimated costs of the anticipated remediation strategy for the site range up to $24 million. Once a remedy is selected, it is expected that the PRPs will agree on an allocation of responsibility for the costs. Generation has accrued what it believes to be an adequate amount to cover its anticipated share of the liability.

Greenhouse Gas Emissions Reductions

Exelon announced on May 6, 2005 that it has established a voluntary goal to reduce its greenhouse gas (GHG) emissions by 8% from 2001 levels by the end of 2008. The 8% reduction goal represents a decrease of an estimated 1.3 million metric tons of GHG emissions. Exelon will incorporate recognition of GHG emissions and their potential cost into its business analyses as a means to promote internal investment in activities that result in the reduction or avoidance of GHG emissions. Exelon made this pledge under the United States EPA's Climate Leaders program, a voluntary industry–government partnership addressing climate change. Exelon believes that its planned GHG management efforts, including increased use of renewable energy, its current energy and process efficiency initiatives and its efforts in the areas of carbon sequestration, will allow it to achieve this goal. The anticipated cost of achieving the voluntary GHG emissions reduction goal will not have a material effect on Exelon's future results of operations, financial condition or cash flows.

Source: EXELON CORP, 10–Q, April 25, 2007

On April 2, 2007, the U.S. Supreme Court issued a decision in the case of Massachusetts v. U.S. Environmental Protection Agency holding that carbon dioxide and other GHGs are pollutants subject to regulation under the new motor vehicle provisions of the Clean Air Act. The case was remanded to the EPA for further rulemaking to determine whether GHGs may reasonably be anticipated to endanger public health or welfare, or in the alternative provide a reasonable explanation why GHGs should not be regulated. Possible outcomes from this decision include regulation of GHGs from manufacturing plants, including electric generation, transmission and distribution facilities, under a new EPA rule, and Federal or state legislation. Due to the uncertainty as to any of these potential outcomes, Exelon cannot estimate the effect of the decision on its operations and its future results of operations, financial condition and cash flows.

Leases

The Registrants' lease commitments as of March 31, 2007 did not change significantly from December 31, 2006. See Note 18 of the Combined Notes to Consolidated Financial Statements within Exelon's 2006 Annual Report on Form 10-K for information regarding leases.

Litigation and Regulatory Matters

Exelon, Generation and PECO

PJM Billing Dispute. In December 2004, Exelon filed a complaint with FERC against PJM and PPL Electric (PPL) alleging that PJM had overcharged Exelon from April 1998 through May 2003 as a result of a billing error. Specifically, the complaint alleges that PJM mistakenly identified PPL's Elroy substation transformer as belonging to Exelon and that, as a consequence, during times of congestion, Exelon's bills for transmission congestion from PJM erroneously reflected energy that PPL took from the Elroy substation and used to serve PPL load.

Beginning in September of 2005 and throughout 2006, Exelon and PPL filed multiple settlement proposals with FERC, with each new proposal superceding the prior, in attempts to resolve this matter. On March 20, 2007, FERC issued an order accepting the settlement in which PPL agreed to directly pay Exelon approximately $43 million in a lump-sum payment (comprised of $38 million of erroneous charges, plus interest of $5 million). At that time, Exelon established a receivable due from PPL and recognized the corresponding gain in current earnings. Approximately $32 million and $11 million of the settlement amount will be received by Generation and PECO, respectively, and recorded as a reduction to purchased power expense and interest income. In April 2007, this receivable amount was paid in full, including interest.

Real Estate Tax Appeals. Generation and PECO each have been challenging real estate taxes assessed on certain nuclear plants. PECO has been involved in litigation in which it has contested taxes assessed in 1997 under the Pennsylvania Public Utility Realty Tax Act of March 4, 1971, as amended (PURTA), and has appealed local real estate assessments for 1998 and 1999 on the Peach Bottom Atomic Power Station (York County, PA) (Peach Bottom). On March 27, 2007, PECO prevailed in a unanimous decision by the Pennsylvania Supreme Court in its contesting of taxes assessed in 1997 under PURTA. The Commonwealth of Pennsylvania (Commonwealth) had contended that PECO owed more in real estate taxes in 1997 than had previously been remitted by PECO, while PECO contended that it owed less than what it had previously remitted. PECO received a favorable ruling in this case, which is expected to result in the eventual refunding or credit to PECO of approximately $38 million of real estate taxes previously remitted plus approximately $17 million in interest. PECO has recorded a receivable for the $55 million expected to be received from the Commonwealth. PECO had previously reserved approximately $17 million for the difference between the Commonwealth's assessment and the amount previously remitted by PECO. PECO is in the process of determining the ultimate use and ratemaking treatment of these amounts and has recorded the total of these amounts of $72 million as a regulatory liability. See Note 14 — Supplemental Financial

Source: EXELON CORP, 10-Q, April 25, 2007

Information for a listing of PECO's regulatory assets and liabilities. As of March 31, 2007, Generation was involved in real estate tax appeals for 2006 and 2005 for the valuation of its Byron plant and is involved in appeals regarding the 2006 valuation of its Braidwood, Clinton and Dresden plants. The ultimate outcome of these matters remains uncertain and could result in unfavorable or favorable impacts to the consolidated financial statements of Exelon, Generation and PECO. Generation and PECO believe their reserve balances for exposures associated with real estate taxes as of March 31, 2007 reflect the probable expected outcome of these appeals proceedings in accordance with SFAS No. 5.

Exelon and Generation

Asbestos Personal Injury Claims. In the second quarter of 2005, Generation engaged independent actuaries to determine if, based on historical claims data and other available information, a reasonable estimate of future losses could be calculated associated with asbestos–related personal injury actions in certain facilities that are currently owned by Generation or were previously owned by ComEd and PECO. Based on the actuaries' analyses, management's review of current and expected losses, and the view of counsel regarding the assumptions used in estimating the future losses, Generation recorded an undiscounted $43 million pre–tax charge for its estimated portion of all estimated future asbestos–related personal injury claims estimated to be presented through 2030. This amount did not include estimated legal costs associated with handling these matters, which could be material. Generation's management determined that it was not reasonable to estimate future asbestos–related personal injury claims past 2030 based on only three years of historical claims data and the significant amount of judgment required to estimate this liability. The $43 million pre–tax charge was recorded as part of operating and maintenance expense in Generation's Consolidated Statements of Operations and Comprehensive Income in 2005 and reduced net income by $27 million after tax.

At March 31, 2007 and December 31, 2006, Generation had reserved approximately $48 and $48 million, respectively, in total for asbestos–related bodily injury claims. As of March 31, 2007, approximately $12 million of this amount relates to 138 open claims presented to Generation, while the remaining $36 million of the reserve is for estimated future asbestos–related bodily injury claims anticipated to arise through 2030 based on actuarial assumptions and analysis. Generation plans to obtain annual updates of the estimate of future losses. On a quarterly basis, Generation monitors actual experience against the number of forecasted claims to be received and expected claim payments. During 2006 and the first quarter of 2007, Generation performed a periodic update to this reserve, which did not result in a material adjustment.

Oil Spill Liability Trust Fund Claim. In December 2004, the two Salem nuclear generation units were taken offline due to an oil spill from a tanker in the Delaware River near the facilities. The units, which draw water from the river for cooling purposes, were taken offline for approximately two weeks to avoid intake of the spilled oil and for an additional two weeks relating to start up issues arising from the oil spill shutdown. The total shutdown period resulted in lost sales from the plant. Generation and PSEG subsequently filed a joint claim for losses and damages with the Oil Spill Liability Trust Fund. In January 2007, Exelon and PSEG submitted a revised damages calculation to the Oil Spill Liability Trust Fund identifying approximately $46 million in total damages and losses, of which approximately $20 million would be paid to Exelon. As this matter represents a contingent gain, Generation has not recorded any income. Generation expects this matter to be resolved in 2007.

Exelon

Pension Claim. On July 11, 2006, a former employee of ComEd filed a purported class action lawsuit against the Exelon Corporation Cash Balance Pension Plan (Plan) in the Federal District Court for the Northern District of Illinois. The complaint alleges that the Plan, which covers certain management employees of Exelon's subsidiaries,

Source: EXELON CORP, 10–Q, April 25, 2007

calculated lump sum distributions in a manner that does not comply with the Employee Retirement Income Security Act (ERISA). The plaintiff seeks compensatory relief from the Plan on behalf of participants who received lump sum distributions since 2001 and injunctive relief with respect to future lump sum distributions. It remains to be determined whether this case will proceed as a class action and how many Plan participants may be part of the proposed class, if a class is certified. However, the lawsuit is not expected to have a material financial impact on Exelon.

Savings Plan Claim. On September 11, 2006, five individuals claiming to be participants in the Exelon Corporation Employee Savings Plan, Plan #003 (Savings Plan), filed a putative class action lawsuit in the United States District Court for the Northern District of Illinois. The complaint names as defendants Exelon, its Director of Employee Benefit Plans and Programs, the Employee Savings Plan Investment Committee, the Compensation and the Risk Oversight Committees of Exelon's Board of Directors and members of those committees. The complaint alleges that the defendants breached fiduciary duties under ERISA by, among other things, permitting fees and expenses to be incurred by the Savings Plan that allegedly were unreasonable and for purposes other than to benefit the Savings Plan and participants, and failing to disclose purported "revenue sharing" arrangements among the Savings Plan's service providers. The plaintiffs seek declaratory, equitable and monetary relief on behalf of the Savings Plan and participants, including alleged investment losses. On February 21, 2007 the district court granted the defendants' motion to strike the plaintiffs' claim for investment losses.

Exelon, Generation, ComEd and PECO

General. The Registrants are involved in various other litigation matters that are being defended and handled in the ordinary course of business. The Registrants maintain accruals for such costs that are probable of being incurred and subject to reasonable estimation. The ultimate outcomes of such matters, as well as the matters discussed above, are uncertain and may have a material adverse effect on the Registrants' financial condition, results of operations or cash flows.

Fund Transfer Restrictions

The Federal Power Act declares it to be unlawful for any officer or director of any public utility "to participate in the making or paying of any dividends of such public utility from any funds properly included in capital account." What constitutes "funds properly included in capital account" is undefined in the Federal Power Act or the related regulations; however, the FERC has consistently interpreted the provision to allow dividends to be paid as long as (i) the source of the dividends is clearly disclosed, (ii) the dividend is not excessive and (iii) there is no self–dealing on the part of corporate officials. While these restrictions may limit the absolute amount of dividends that a particular subsidiary may pay, Exelon does not believe these limitations are materially limiting because, under these limitations, the subsidiaries are allowed to pay dividends sufficient to meet Exelon's actual cash needs. See Note 18 of the Combined Notes to Consolidated Financial Statements within Exelon's 2006 Annual Report on Form 10–K for additional information regarding fund transfer restrictions.

Income Taxes

ComEd and PECO have entered into several agreements with a tax consultant related to the filing of refund claims with the IRS. The fees for these agreements are contingent upon a successful outcome of the claims and are based upon a percentage of the refunds recovered from the IRS, if any. The ultimate net cash impacts to ComEd and PECO related to these agreements will either be positive or neutral depending upon the outcome of the refund claim with the IRS. These potential tax benefits and associated fees could be material to the financial position, results of operations and cash flows of ComEd and PECO. If a settlement is reached, a portion of ComEd's tax benefits,

Source: EXELON CORP, 10–Q, April 25, 2007

including any associated interest for periods prior to the PECO/Unicom Merger, would be recorded as a reduction of goodwill under the provisions of EITF 93–7. Exelon cannot predict the timing of the final resolution of these refund claims.

See Note 10 — Income Taxes for information regarding the Registrants' income tax refund claims and certain tax positions, including the 1999 sale of fossil generating assets.

14. Supplemental Financial Information (Exelon, Generation, ComEd and PECO)

Supplemental Statement of Operations Information

The following tables provide additional information regarding the components of other, net within the Consolidated Statements of Operations and Comprehensive Income of Exelon, Generation, ComEd and PECO for the three months ended March 31, 2007 and 2006:

	Three Months Ended March 31, 2007			
	Exelon	Generation	ComEd	PECO
Investment income	$ 2	$ —	$ 1	$ 1
Gain on sale of investments, net	15	15	—	—
Decommissioning–related activities:				
Decommissioning trust fund income(a)	46	46	—	—
Decommissioning trust fund income — AmerGen(a)	11	11	—	—
Other–than–temporary impairment of decommissioning trust funds(b)	(8)	(8)	—	—
Other–than–temporary impairment of decommissioning trust funds — AmerGen	(2)	(2)	—	—
Regulatory offset to non–operating decommissioning–related activities(c)	(37)	(37)	—	—
Net direct financing lease income	6	—	—	—
AFUDC, equity	1	—	1	—
Recovery of tax credits related to Exelon's investments in synthetic fuel–producing facilities(d)	20	—	—	—
Interest income related to settlement of PJM billing dispute(e)	5	4	—	1
Interest income related to uncertain income tax positions under FIN 48(f)	1	—	—	3
Other	3	3	—	—
Other, net	$ 63	$ 32	$ 2	$ 5

(a) Includes investment income and realized gains and losses.

(b) For the three months ended March 31, 2007, includes other–than–temporary impairments totaling $8 million on nuclear decommissioning trust funds for the former ComEd units.

(c) Includes the elimination of non–operating decommissioning–related activity for those units that are subject to regulatory accounting, including the elimination of decommissioning trust fund income and other–than–temporary impairments. See

Source: EXELON CORP, 10–Q, April 25, 2007