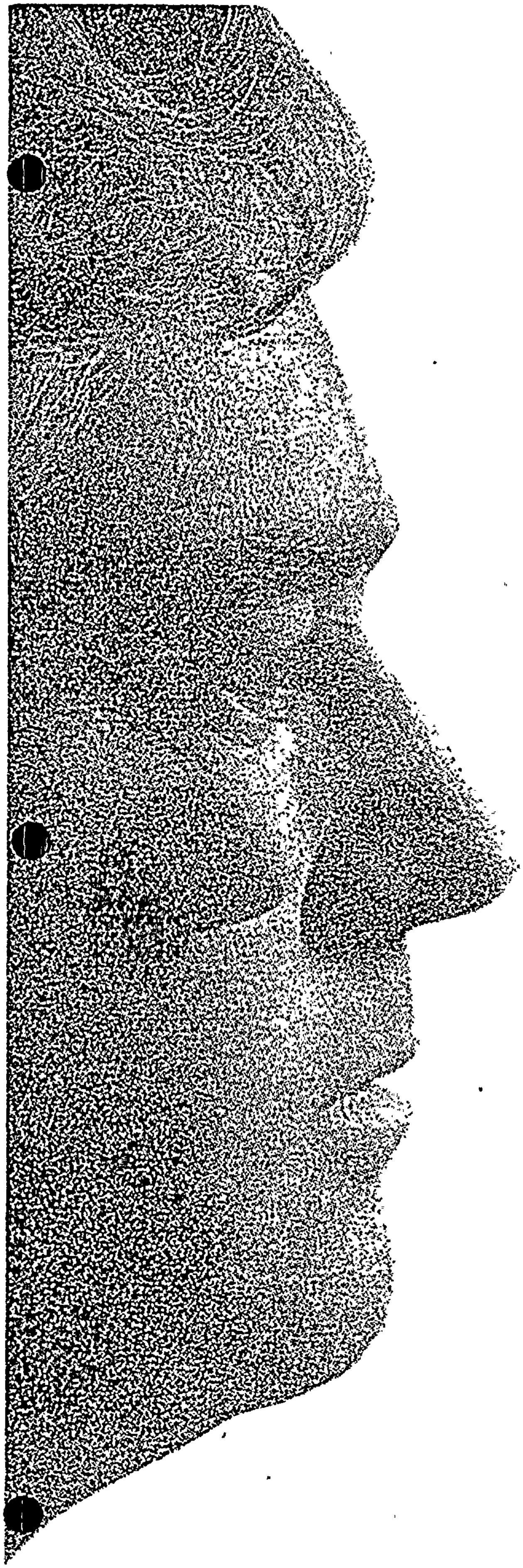
CENTRAL HUDSON GAS & ELECTRIC CORPORATION

ANNUAL REPORT 1978



"a private enterprise succeeds when all three of its constituencies— investors, customers, and employees— receive benefits."

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SHAREHOLDERS MEETING

The annual meeting of holders of common shares will be held on Tuesday, April 3, at 10:30 a.m., at the South Avenue office of the Company in Poughkeepsie, New York. Notice of this meeting, together with the proxy statement and proxy, will be mailed to shareholders about March 12. The management welcomes the personal attendance of shareholders at the meeting.

ADDITIONAL INFORMATION

Shareholders may obtain, without charge, a copy of Central Hudson's annual report to the Securities and Exchange Commission, on Form 10-K, by writing to Mr. Joseph F. Furlong, Secretary, Central Hudson Gas & Electric Corporation, 284 South Avenue, Poughkeepsie, New York 12602. A comprehensive statistical supplement to the Company's 1978 Annual Report, containing key financial and operating results for a ten-year period, will shortly be available on request to Mr. Furlong.

CENTRAL HUDSON GAS & ELECTRIC CORPORATION

General Office

284 South Avenue, Poughkeepsie, New York 12602
Telephone (914) 452-2000

Five-Year Summary of Operations*
(Thousands of Dollars)

	1978	1977	1976	1975	1974
Operating Revenues:					
Electric	$186,264	$184,391	$149,884	$138,414	$114,482
Gas	24,738	23,449	20,831	19,897	17,007
Total	211,002	207,840	170,715	158,311	131,489
Operating Expenses:					
Operations	132,554	133,688	100,917	92,604	82,327
Maintenance	8,151	8,098	6,794	6,611	5,250
Depreciation	13,393	13,279	12,859	12,569	10,312
Operating taxes	18,779	18,560	16,975	16,003	14,529
Federal income tax	9,891	7,099	6,392	4,453	(1,011)
Total	182,768	180,724	143,937	132,240	111,407
Operating Income	28,234	27,116	26,778	26,071	20,082
Other Income and Deductions:					
Allowance for equity funds used during construction	2,388	1,560	796	324	1,754
Federal income tax—credit	859	703	439	734	1,040
Other—net	(348)	(90)	(84)	17	(63)
Total	2,899	2,173	1,151	1,075	2,731
Income before Interest Charges	31,133	29,289	27,929	27,146	22,813
Interest Charges:					
Interest on debt	13,185	12,507	12,640	12,680	12,568
Other	328	866	376	510	254
Allowance for borrowed funds used during construction	(2,640)	(1,831)	(1,014)	(381)	(2,059)
Total	10,873	11,542	12,002	12,809	10,763
Net Income	20,260	17,747	15,927	14,337	12,050
Dividends on Preferred Stock	4,126	3,626	2,866	2,866	2,866
Income Available for Common Stock	16,134	14,121	13,061	11,471	9,184
Dividends Declared on Common Stock	10,531	8,966	8,382	7,737	7,328
Amount Retained in the Business	5,603	5,155	4,679	3,734	1,856
Retained Earnings—beginning of year	61,481	56,326	51,647	47,913	46,057
Retained Earnings—end of year	$ 67,084	$ 61,481	$ 56,326	$ 51,647	$ 47,913
Common Stock:					
Average Shares Outstanding (000's)	5,310	4,873	4,873	4,440	4,230
Earnings Per Share—on Average Shares Outstanding	$3.04	$2.90	$2.68	$2.58	$2.17
Earnings Per Share—Assuming Conversion of the Convertible Debentures	*$2.88*	*$2.70*	*$2.50*	*$2.40*	*$2.03*
Dividends Declared Per Share	$1.96	$1.84	$1.72	$1.72	$1.72
Ratio of Earnings to Fixed Charges**	3.17	2.81	2.68	2.37	1.78

*This summary should be read in conjunction with the financial statements and notes thereto included in the "Financial Section" of this Annual Report.

**For the purpose of computing the Ratio of Earnings to Fixed Charges, earnings consist of net income plus fixed charges plus all federal income tax amounts. Fixed charges consist of total interest charges, excluding the allowance for borrowed funds used during construction.

CENTRAL HUDSON GAS & ELECTRIC CORPORATION
POUGHKEEPSIE, N.Y. 12602

March 5, 1979

To Our Shareholders:

We submit our Annual Report concerning the activities of Central Hudson in 1978.

Traditionally, an annual report commences with a statement of the earnings for the prior year, and we continue that tradition by reporting the item of information which is of the most interest to you. We are pleased to report that our earnings per share for the year 1978 were $3.04 as compared with $2.90 for the previous year.

We wish also to report to you concerning the Company's activities on a broader basis, and therefore in addition to providing the usual financial information, this Annual Report serves to give an account of Central Hudson's total role which arises from its function as the supplier of electricity and gas in its franchise area.

We have said repeatedly that our business is no longer concerned solely with its own affairs, but increasingly must be concerned with the political, economic, and social forces which surround it. As never before, both federal and state statutes and regulations affecting the public utility business are continuously being adopted and while we regularly object to many facets of these legislative and regulatory programs and think they are often ill-advised and frequently ill-conceived, we recognize that they are attempts to give expression to the American people's desire to play a role in deciding how both natural and social resources are to be used.

American business will continue to be viable only so long as it justifies itself in the eyes of the American public as representing the best way of satisfying economic needs and preserving those life values which are synonymous with the American Way. If we do not satisfy the expectations and aspirations of the public, it is quite clear that negative consequences can be expected, and such consequences obviously would be of direct concern to our shareholders.

Although we are a gas and electric corporation, all the phases of our activities—like those of any other business—make us a component of the communities in which we exist. We provide employment and meet payrolls, we purchase supplies, we pay dividends and interest to our investors, and we pay large amounts of taxes in support of the general welfare. Furthermore, our activities affect both the natural and social environment.

It is our firm belief that we are truly an enterprise that confers great benefits to the public, and only as we confer such benefits will we find that acceptance which will enable us to continue in business and to make that business profitable and attractive to our present and future investors.

In this sense, the following pages relate to financial matters and also endeavor to give an account of what we are and what we do in the community generally.

This is the centennial year of Thomas Alva Edison's invention of the incandescent light. That invention sparked a century of progress unparalleled in history and we confidently anticipate that the next hundred years will bring even greater benefits for mankind.

H. Clifton Wilson
President

Theodore J. Carlson
Chairman of the Board
and Principal Officer

serving the interests of investors, customers, and employees is the reason for the existence of Central Hudson.

Central Hudson–a corporation

as such a corporation...

Central Hudson pays interest and dividends

During the year the Board of Directors increased the quarterly dividend rate on the common stock from 47¢ to 49¢, effective with the dividend paid on May 1, 1978. This step was taken in recognition of the effect of inflation on the shareholders and was expected to keep the amount of earnings paid out in dividends around the two-thirds proportion which has been the Company's objective over many years. The total dividend paid in 1978 amounted to $1.94 per share and it is estimated that the full amount is subject to federal income tax as ordinary income.

As of December 31, 1978, investors in Central Hudson's securities had purchased $202.6 million of long-term debt securities, $61 million of preferred stock, and approximately 5.4 million shares of common stock representing an equity of $141.3 million. In addition, the Company had $23 million of short-term debt outstanding.

During the year 1978, the Company paid $11.5 million in interest charges on long-term debt; it paid $1.7 million in interest charges on short-term debt; preferred dividend requirements amounted to $4.1 million; and $10.4 million was distributed in the form of cash dividends to holders of common stock. These payments amounted to 6.8% of the total investment shown above.

The 5,372,873 shares of common stock presently outstanding are registered in 24,990 names with holders in 50 states and 15 foreign countries. About 58% of the common shareholders are in New York State and about 30% reside in the Company's service area. Approximately one third of its employees own common stock in the Company.

About 6% of the Company's shareholders participate in the Dividend Reinvestment Plan. Their shares represent 2.7% of the total outstanding.

Central Hudson serves the customer

Customers

The population of the Company's service area is currently estimated at 540,000 persons. The Company has 205,081 electric customers and 43,298 gas customers who reside in a 2,600 square-mile area covering parts of eight counties in the Mid-Hudson Valley.

Central Hudson provides employment

Employees

At the end of 1978, Central Hudson had 1,305 employees. There were 316 supervisory and professional employees, and 989 were represented by Locals 320 and 2218 of the International Brotherhood of Electrical Workers. Approximately 30% of all employees have been with Central Hudson for 25 or more years.

Central Hudson provides essential services

Future Generating Plans

The Company is constantly reviewing its electric power needs and endeavors to adapt its construction programs to match its capacity and needs as closely as possible.

As a result of commitments made several years ago when the rate of growth of the Company's sales was substantially greater than it now is, the Company is participating in the construction of two electric generating plants. The level of its future construction is continually being reconsidered and the Company will take whatever steps are available to design its construction program to meet its needs.

At present, its future plans envision participating in the Nine Mile Point Nuclear Plant and Sterling nuclear project. The status of these projects is:

Nine Mile Point Nuclear Plant

Construction by Niagara Mohawk Power Corporation at Oswego, New York, of the Nine Mile Point Nuclear Plant is approximately 25% complete. However, manufacturing delays and a summer-long work stoppage due to labor problems resulted in a one-year extension of the in-service date to late 1984.

The estimated total cost of the 1,080-mw. plant is $1.96 billion. Central Hudson has a 9% interest in the plant and as of December 31, 1978 had invested $50.6 million in the construction of such plant.

Sterling Nuclear Project

It is anticipated that construction of the Sterling Nuclear Plant by Rochester Gas & Electric Corporation at Sterling, New York, will begin in 1980 and be completed in 1988, pending the outcome of hearings by the New York State Board on Electric Generating Siting and the Environment.

The State Board approved a certificate of Environmental Compatibility and Public Need in January 1978 but withdrew it in May 1978. The State Board will reconsider the public need for the 1,150-mw. plant in the Spring of 1979 following the conclusion of hearings being conducted by the Public Service Commission on the long-range plans of the members of the New York Power Pool.

The estimated total cost of the Plant is $1.78 billion. Central Hudson has a 17% interest in the Sterling Plant and as of December 31, 1978 had invested $11.7 million in the construction of the Plant.

Empire State Power Resources, Inc. (ESPRI)

In February 1979, after more than four years of review, the Public Service Commission voted to disapprove the formation of a state-wide generating company that would have owned, constructed and operated new generating facilities in New York State.

Central Hudson was one of seven major electric companies sponsoring ESPRI. The creation of a jointly owned generating company offered many advantages over individual companies acting separately, such as improved availability of financing, the possibility of lower cost capital, and the possibility of increased efficiencies in design and construction.

In 1974, an application was filed with the PSC seeking authority with respect to the initial issuance of stock by ESPRI. Public hearings on ESPRI were concluded in 1977 and an Administrative Law Judge recommended approval of the application, subject to certain conditions, in early 1978.

The reasons for the PSC's decision were not known at the time of printing this report because the written Order was not available. Furthermore, it is uncertain what effect the Commission's decision will have on Central Hudson's future generating plans.

Roseton Plant

In December 1978, the Company purchased an additional 10% interest, 120 mw., in the Roseton Electric

Generating Plant from Niagara Mohawk Power Corporation for $30.2 million. This purchase was made in accordance with an agreement entered into in 1968 when the project was undertaken to provide for capacity requirements based on experienced and then projected load growth. The agreement was approved by the Public Service Commission. As of December 31, 1978, the Company has a 30% undivided interest in the ownership and output of the 1,200-mw. Roseton Plant.

Construction

Budgeted expenditures for 1979 for new projects and for projects carried over from 1978 amount to $39.7 million. This represents a decrease of $24.8 million from the $64.5 million expended in 1978, which included $30.2 million for the purchase of an additional 10% interest in the Roseton Plant.

Of the $39.7 million budgeted for 1979, $24.5 million represents the Company's share of costs for the Nine Mile Point and Sterling nuclear projects, which are presently expected to supply power to the Company's customers beginning in the mid and late 1980's. The balance will be spent on projects located within the Company's service area.

Information pertaining to estimated construction expenditures for the period 1979 through 1983 is set forth in Note 8 of the Notes to Financial Statements.

Financing

The 1978 construction expenditures were financed from internal sources of funds, additional short-term borrowings, and the issuance of new securities. It is the Company's practice to meet its capital needs initially from short-term bank loans and the sale of commercial paper and then to refund this debt through the issuance of long-term debt and equity securities when appropriate.

On February 16, 1978, the Company sold 500,000 additional shares of common stock. The stock was sold through underwriters at a price to the public of $21.30 per share and the proceeds received by the Company were $20.68 per share for a total of $10,340,000. Such proceeds were immediately applied to the reduction of outstanding short-term debt. 81% of the shares were purchased by individuals with the average purchase per individual amounting to 163 shares.

On December 29, 1978, the Company issued $35 million of promissory notes under a Term Loan Agreement with three banks for whom Irving Trust Company, one of the lenders, acts as agent. Approximately $30 million was used to acquire the additional 10% in the Roseton Plant and the balance was applied to reduce outstanding short-term debt. The use of a term loan, payable over a period of three years or less, will enable the Company to smooth out its cash requirements and carry on an orderly financing program over the next several years.

The amount of outstanding short-term debt, in the form of commercial paper, increased from $17 million at December 31, 1977 to $23 million at December 31, 1978. The Company maintains lines of credit with banks totaling $43 million.

Major Construction

In order to reinforce the entire northwest portion of the Catskill area, which has shown rates of growth well above the Hudson Valley average over the past three years, Company personnel designed and are building a new 69,000-volt transmission line in the towns of Greenville and Westerlo. Work on the line, which is seven miles in length, started in December 1978 and will continue through 1979.

A major renovation involving replacement of the crest of the dam serving the hydroelectric plant at Sturgeon Pool was completed during 1978. Additional renovation is planned for 1979. The plant, in service since 1924, continues to be an important part of the Company's generating facilities.

The Company is engaged in various projects expected to cost $1.4 million in 1979 for required relocation of electric and gas lines as a result of street and highway reconstruction.

Roseton Litigation

The legal action is continuing by the owners of the Roseton Plant—Central Hudson, Niagara Mohawk Power Corporation and Consolidated Edison Company of New York, Inc.—to recover damages from certain contractors involved in the Roseton project.

It is alleged that the defendants' failure to design and construct properly the Roseton Plant led to a series of incidents, including a boiler implosion, which delayed the completion and commercial operation of the Plant.

At the present time no estimate can be made as to the duration or outcome of the litigation.

Rights-of-Way Management

In late 1976, the Company implemented a program to clear transmission rights-of-way which had become overgrown as a result of a nine-year moratorium on the use of herbicides. Dense vegetation impeded clearing efforts in 1977 and heavy snow in the first quarter of 1978 further hampered this work.

Following an extensive survey of our electric rights-of-way, a detailed report was prepared and various clearing options were selected which comprise a long-term electric and gas right-of-way management program that will balance reliability, cost, environmental, and public relations objectives.

The program will require three years for completion at a cost of approximately $2 million. When the program is completed, it is expected that the rights-of-way can be routinely maintained at a reduced cost.

Natural Gas Supply

With the passage of the National Energy Act by Congress, supplies of natural gas became available in late 1978 that previously had been available only within the producing states or that had been uneconomical to market in the Northeast.

The Company's three pipeline suppliers indicated that they were reducing the curtailments that had prevailed for several years, and there are indications that in at least one case the curtailment may be lifted entirely.

As a result of this favorable development, most customers purchasing gas on an interruptible basis were informed in early December that they could expect to have their requirements met in full through the ensuing heating season, assuming a normal winter. This is in contrast to recent years when supplies to these customers had been interrupted for as long as several months during the heating season.

Although the immediate outlook is optimistic, the Company will continue to attempt to strengthen its long-term supply situation.

Newburgh District Headquarters

Customer Services and Engineering personnel serving the Newburgh area moved into new headquarters late in 1978.

The decision to purchase and renovate an existing building was made after an extensive evaluation of options to purchase existing buildings or construct a new facility and after full consideration of the productivity-related savings and improvements in service that would result from consolidating operations.

The new facility provides additional space for vehicle garaging, maintenance, and expanded material and equipment storage facilities. The telephone communication system utilizes a Computer Board Exchange that facilitates response to customer telephone calls. The system has proved to be an effective means of improving the quality of service under varying operating conditions and provides the promise of significant cost savings.

New Home Advisory Service

The Company is now offering a New Home Advisory Service to all builders, consultants, and prospective home buyers.

This service will promote the effective management of energy in the home by encouraging the use of better insulation, by recommending the installation of energy-efficient appliances and equipment, and by advising consumers how use habits can affect energy consumption.

In encouraging energy management, Central Hudson is assisting its customers in identifying the potential for conserving energy and achieving three long-term objectives: to conserve fossil fuels that are in short supply, to design and select utilization equipment—including the electric heat pump—that will improve the potential for conserving energy and the Company's load factor, and to reduce the effect of future escalations in energy costs on the homeowner.

Collection Procedure

Central Hudson has initiated a new collection procedure for residential customers during the cold weather months of November 1 through April 15.

The procedure provides that during this period residential customers whose electric service is necessary to heat the premises or operate a heating system will not have service discontinued for nonpayment until the Company has attempted to contact the customer personally during normal working hours, and in the event no contact is made, during nonbusiness hours.

In certain situations collection problems will be referred to the Department of Social Services for investigation.

The Company will continue to encourage customers to participate in the third-party notification, budget billing, and programs for those over 65, all of which are offered for the convenience and protection of our customers.

Street Lighting

Street lighting is an effective and essential service that provides both security and improved highway safety.

As a result of an extensive study of street lighting services during 1978, several steps will be taken by the Company to improve the quality of service and to reduce the energy requirements of street lighting systems.

This new program will improve the quality of these services, conserve energy, and decrease the effect of future fuel cost increases to street lighting customers.

Savenergy Fair

Early in November 1978, more than 16,000 people attended the SAVENERGY Fair at the McCann Recreation Center in Poughkeepsie.

The Fair, which was sponsored jointly by Central Hudson, Marist College, and Dutchess Community College, featured more than 75 energy exhibits, an energy stage show, a lecture series, a puppet show, a film series, a school poster contest, and a special program for builders, consulting engineers, and architects.

The four-day Fair was designed to make customers aware of the energy crisis and the need to conserve energy. In addition, the SAVENERGY Fair demonstrated to community leaders, elected officials, members of regulatory agencies, members of the news media, and, most critically, to customers, that the services provided by Central Hudson are part of the solution to the energy problem.

Central Hudson participates in the governmental process

Rate Application

On November 27, 1978, the Company announced that it was seeking to increase rates for electric and gas service in order to offset the continuing effects of inflation. It is probable that the Public Service Commission will not make a ruling on the rate application until late 1979.

At the time of the announcement, the Company reported that it would keep the proposed increases within the voluntary, anti-inflation guidelines established by President Carter.

Central Hudson is seeking an overall revenue increase of $25 million, or 12.81%. This represents an average annual increase of 5.69%, based on the two and one-quarter years which will have elapsed between rate changes and which is materially less than the increase in the rate of inflation generally.

It should be noted that approximately one half of any increase the Company receives will be paid as additional federal income and revenue taxes.

Time-of-Use Rates

Time-of-use electric rates for 37 large industrial and commercial customers were put into effect in March 1978 in compliance with an order issued by the Public Service Commission in July 1977.

The rates are intended to provide an economic incentive for customers to reduce their use of electricity during peak periods.

Prior to placing the rates in effect, the Company requested an adjustment clause to offset the revenue loss associated with the peak load reduction. The request was denied by the Commission on the ground that the loss of revenue was speculative.

Based on the first six months of actual experience with the time-of-use rates, the Company petitioned the Commission on November 8, 1978 for permission to increase rates by $609,000 per year. The Commission denied the Company's request to compensate this loss immediately and decided to consider it as part of the Company's $25 million rate proceeding.

Fuel Cost Adjustment Hearings

The Commission's state-wide investigation of the fuel adjustment clause is still in progress and no decision is expected before mid-1979.

Testimony by the Commission's staff supports a continuation of the fuel adjustment. Major staff conclusions are: the existing fuel adjustment has operated satisfactorily, the fuel adjustment has not been a disincentive to proper fuel procurement practices, and a fuel adjustment remains necessary because of the instability of fuel prices.

State and Federal Legislation

Central Hudson—in coordination with The Energy Association of New York State, the Associated Industries and the Empire State Chamber of Commerce—continues to advise legislators in the State capital about the effect proposed legislation would have on the utility industry and its customers.

During the past State legislative session Central Hudson was able, in conjunction with other utilities in the State, to promote constructive legislation which will bring benefits to utility customers. The licensing procedure for the siting of new generating facilities was improved. The responsibility for developing a State Master Energy Plan was placed with the State Energy Office. The 4% State sales tax on gas and electricity will be reduced to 2% over a two-year period effective January 1, 1979. This type of tax is regressive and compounds the rising cost of energy to customers.

Proposed legislation which would have prevented the creation of ESPRI was tabled, as was legislation which would have established a moratorium on the construction of nuclear generating facilities.

At the federal level, the Company coordinates its efforts with the Edison Electric Institute, the National Association of Manufacturers, and the Chamber of Commerce of the United States.

In April 1977, the National Energy Act was introduced and quickly passed by the House. It was hastily drawn and ill-conceived. The Senate responded to the concerns of industry by calling upon House-Senate Conference Committees to study in considerable detail the effects of the proposed Act.

The Act was finally signed into law by the President in November 1978, eighteen months after its introduction. Unfortunately, the National Energy Act does not provide a comprehensive energy policy for the nation. While energy conservation is important, the Act places too much reliance on conservation efforts to supply a significant portion of the nation's energy needs and too little on the development of new energy sources. While the Act mandates that new generating plants be fueled by coal instead of natural gas or oil, it fails to mention the role of nuclear energy. The Act also calls for the gradual decontrol of the price of natural gas between now and 1985.

The Company will continue to urge the adoption of a comprehensive and meaningful energy policy, which the public deserves and needs.

Freedom of Speech

During the year the Company continued its opposition to prohibitions and restrictions on advertising and promotional practices instituted by the Public Service Commission.

Although Central Hudson failed to obtain a favorable decision in the New York State Supreme Court and its Appellate Division, the case is being pursued in the Court of Appeals.

The Commission's "Statement of Policy on Advertising and Promotional Practices of Public Utilities" dates back to early 1977. It prohibits promotional advertising, prohibits the use of bill inserts to disseminate information on matters of public controversy, and establishes that the cost of advertising that seeks to sway public opinion on matters of public policy is not a proper cost for rate-making purposes.

The Company believes that these aspects of the Commission's order violate Central Hudson's constitutional right of free speech and are arbitrary and capricious.

Central Hudson contributes to the community

Taxes

In fulfilling their function of promoting the general welfare, governments require vast sums of money. Foremost among tax-paying entities are the private-sector utilities. In most communities and areas served by the Company, Central Hudson is the largest single taxpayer.

During 1978, Central Hudson's general taxes amounted to $19.6 million, the major part of which was paid directly to government units for general and school purposes. This sum represents 9% of our gross revenues.

On a state-wide basis, the payment of taxes by combination electric and gas utilities to local government subdivisions exceeded $880 million in 1977, the last year for which figures are available.

It is apparent that tax revenues obtained from the private-sector utilities are essential to the economic well-being of New York State.

Government Power

As a result of the increasing cost of electricity, interest has developed in establishing municipal electric systems in various locations in New York State as alternatives to investor-owned electric utilities.

In the Company's service area during 1978, government power advocates were active in Ulster and Orange counties and in the Town of Olive, located in Ulster County.

A municipal power study commission in Ulster County originally intended to make a recommendation to the Ulster County Legislature in January 1979 regarding the desirability of conducting a feasibility study. Instead, after six months of deliberation, the commission recommended that additional information on the issue be obtained during 1979 before formulating a recommendation.

Late in 1978, Orange County engaged a consulting firm to investigate ways to reduce energy costs for county residents.

In the Town of Olive, a citizens' committee recommended the funding of a feasibility study. The Town Board, however, declined to appropriate funds for that purpose.

Company personnel at all levels of the organization have been active in dealing with the government power issue. In every instance, Central Hudson personnel have presented factual information which illustrates that government power, in itself, will not reduce the true cost of providing electric service.

Central Hudson participates in research and environmental protection

Danskammer Coal Conversion

In June of 1975 the Federal Energy Agency (now part of the Department of Energy) issued an order prohibiting the use of oil for generation in Units Nos. 3 and 4 at the Danskammer Electric Generating Plant. Compliance with this order would require conversion of Units Nos. 3 and 4 to coal-firing.

The Energy Supply and Environmental Coordination Act provides that the FEA order may not become effective until the U.S. Environmental Protection Agency has determined that coal can be burned in compliance with all applicable air quality requirements and until DOE has completed an Environmental Impact Statement. At this writing neither agency has acted.

Pursuant to a preliminary determination by the EPA, the Company in April 1977 filed a coal conversion plan which included the use of flue gas desulfurization equipment. Execution of that plan would require an investment of approximately $102 million.

However, amendments to the Clean Air Act, which became law during 1977, may make it permissible to convert Units Nos. 3 and 4 to coal-burning without the requirement for flue gas desulfurization. The Company intends to file a revised coal conversion plan reflecting these amendments when the necessary implementing regulations are issued by the EPA. It is estimated that execution of the revised plan would require an investment of about $58 million.

The Company cannot predict whether or when a final Notice of Effectiveness of the conversion order will be issued by DOE.

Cooling Towers

In early 1975 the U.S. Environmental Protection Agency notified the Company that it intended to require the installation of cooling towers at the Roseton Plant, at an estimated capital cost of at least $62 million, of which Central Hudson's share would be 35% in 1983. Furthermore, an alteration of the cooling water intake and discharge facilities at the Danskammer Plant may be required.

Extensive and continuing biological studies indicate that the costs of cooling towers at the Roseton Plant and of discharge modifications at the Danskammer Plant would be grossly disproportionate to any possible environmental benefits which might be realized and that the cooling towers will cause certain adverse environmental and aesthetic effects.

Accordingly, the Company is contesting these requirements in administrative proceedings which commenced in December 1977 and are expected to continue through most of 1979.

Research and Development

The Company is supporting a vigorous and varied research and development program designed to improve existing energy technologies, and to develop new technologies for the production, distribution, and conservation of energy. The program also seeks to enhance the Company's understanding and control of the environmental effects of its operations.

Expenditures for research and development in 1978 were $1.7 million. Of this amount, $1.6 million was spent on electric projects. This amounts to 1.0% of electric revenues, which is in keeping with the PSC guideline calling for electric utilities to spend approximately 1% of electric revenues on research and development.

The 1978 electric research and development program was divided into four principal categories: projects funded nationally, including those funded under the aegis of the Electric Power Research Institute, for which the Company's expenditures were $434,000; projects funded on a state-wide basis through the Empire State Electric Energy Research Corporation for which the Company's share was $266,000; projects funded jointly with utilities using the waters of the Hudson River for cooling in their generating plants, for which Company expenditures were $205,000; and projects conducted solely by the Company, which cost $441,000.

The Company's contribution of $235,000 to the cost of research and development performed by the New York State Energy Research and Development Agency is mandated by Section 18-a of the Public Service Law and the Company has no control over the manner in which such funds were expended.

Expenditures for research and development funded jointly with other utilities on the Hudson River and for projects funded solely by the Company supported, principally, a continuation of a multi-year effort to determine the effects of these plants on the aquatic ecology of the River. Results obtained during 1978 continue to support earlier findings that these effects are insufficient to justify the expenditure of an estimated $62 million for cooling towers at the Roseton Plant.

During the year, the Company continued research projects designed to assess the effects of solar heating on electric system loads, the effects of various rate forms on customer utilization of electric energy, the potential of various technologies for controlling the time of occurrence of customer peak demands, and the efficacy of heat pumps in reducing heating costs in residential and commercial buildings.

MANAGEMENT'S DISCUSSION AND ANALYSIS OF THE SUMMARY OF OPERATIONS

The following discussion and analysis explains significant changes in the amounts of revenues and expenses between the years 1978 and 1977 and also between the years 1977 and 1976. Certain additional information relating to changes between these years is provided in the Notes to Financial Statements on pages 19 through 25 of this report.

THE YEAR 1978 AS COMPARED TO THE YEAR 1977

Earnings

Earnings per share of common stock were $3.04 for 1978 compared with $2.90 for 1977, an increase of 5%. The primary factors contributing to this growth in earnings were increased sales and a full year's effect of higher electric and gas rates which became effective during 1977. Earnings per share are shown after provision for dividends on preferred stock and are computed on the basis of the average number of common shares outstanding during the year. As a result of the sale of 500,000 shares of common stock in February 1978, the average number of shares outstanding increased from 4,872,873 in 1977 to 5,310,373 in 1978.

Operating Revenues

Total operating revenues increased $3.2 million (2%) in 1978. Details of the revenue changes are as follows:

	Increase or (Decrease) from 1977 (Thousands of Dollars)
Electric:	
Customer sales	$4,948
Rate increase	3,873
Sales to other utilities	(2,545)
Fuel cost adjustment charges	(4,407)
Miscellaneous	4
Total electric	1,873
Gas:	
Rate increase	1,042
Customer sales	338
Gas cost adjustment charges	(98)
Miscellaneous	7
Total gas	1,289
Total electric and gas	$3,162

The revenues received by the Company pursuant to the application of the electric and gas cost adjustment clauses only recover the additional costs incurred by the Company and, therefore, do not affect net income.

Total sales of electricity within the Company's service territory increased 4% in 1978 while sales of natural gas were 3% higher than last year. Sales increases by major customer classification are set forth below:

	Electric	Gas
Residential	0%	2%
Commercial	4	4
Industrial	9	11
Interruptible and Seasonal	N/A	0

The growth in sales of electricity and firm gas to industrial customers reflects an improved market for the products of the Company's major industrial customers.

Sales of electric energy to other utilities decreased 8% in 1978, primarily as a result of a reduction in the amount of energy purchased by New York State Electric and Gas Corporation.

Operating Expenses

Costs for operations decreased $1.1 million in 1978. The most significant item contributing to this decrease was an $11.0 million reduction in the cost of fuel used in electric generation. This decrease resulted from lower fuel oil prices and a 7% reduction in generation. The cost of purchased electricity increased $7.0 million, reflecting increased purchases of both capacity and energy from Niagara Mohawk Power Corporation under the Roseton Capability Sales Agreement and increased purchases of less expensive energy from member companies of the New York Power Pool when such power was available. Despite a 5% increase in the volume of gas purchased, the cost of natural gas was $6,000 less than last year; increased refunds received from the Company's pipeline suppliers more than offset the effect of increased purchases and higher rates. Other expenses of operation were $2.9 million greater than last year. The major portion of this increase resulted from higher wages and related fringe benefits together with the charge to expense of $518,000 for the cost of environmental studies for a potential generating site, which costs were previously deferred but are no longer considered acceptable for capitalization.

Maintenance expenses increased $53,000 primarily as a result of increased costs incurred in connection with the Company's tree-trimming program. Depreciation expense shows an increase of only $114,000 in 1978; however, the depreciation provisions for certain properties transferred to "Plant Held for Future Use" in December 1977 were included in the depreciation expense account in 1977 whereas they are being charged to "Other Income Deductions" in 1978. The annual amount of such depreciation is approximately $200,000.

Operating taxes increased $219,000. Payroll taxes were up $142,000 and state and local taxes levied on gross revenues increased $132,000. Partially offsetting these increases was a reduction of $134,000 in property taxes.

Federal income tax charged to "Operating Expenses" increased $2.8 million in 1978. See Note 2 of the Notes to Financial Statements for a detailed analysis and reconciliation of the federal income tax.

Other Income, Interest Charges, Preferred and Common Stock Dividends

The total amount of the Allowance for Funds used During Construction (AFDC) increased $1.6 million in 1978 primarily as a result of the Company's participation in Unit No. 2 of the Nine Mile Point Plant and the Sterling Plant. The AFDC rate for 1978 was 8½% for the first ten months and 8¾% for the last two months. During 1977 AFDC was computed at a rate of 8%. See Note 1 of the Notes to Financial Statements for additional information on this subject.

Total interest charges (excluding AFDC) increased $140,000. The $123,000 increase in interest charges on mortgage bonds is a result of a full year's interest on the $4.5 million of 6¼% bonds issued in June 1977. Short-term interest charges increased $598,000 due to higher levels of borrowings and higher rates of interest in effect during 1978. (See Note 4 of the Notes to Financial Statements for additional information.) Other interest charges decreased $538,000; 1977 interest charges included the interest on the promissory notes which matured on October 1, 1977 and the convertible debentures which matured on February 1, 1978.

The increase of $500,000 in dividends on preferred stock is the result of a full year's dividend on the $15 million of 8.40% preferred stock issued in May 1977.

The sale of 500,000 shares of common stock on February 16, 1978 and the increase in quarterly dividend rate from 47¢ to 49¢, effective May 1, 1978, accounted for the $1.6 million increase in common stock dividends.

THE YEAR 1977 AS COMPARED TO THE YEAR 1976

Earnings

Earnings per share of common stock increased from $2.68 in 1976 to $2.90 in 1977, an increase of 8%. The average number of shares of common stock outstanding was 4,872,873 in both years. The primary factors contributing to this growth in earnings were increased sales of electricity, both to the Company's own customers and to other utilities; higher electric rates which became effective during the third quarter of 1977; and higher gas rates which became effective during May 1977.

Operating Revenues

Total operating revenues increased $37.1 million (22%) in 1977. Details of the revenue changes are as follows:

	Increase or (Decrease) from 1976 (Thousands of Dollars)
Electric:	
Fuel cost adjustment charges	$16,674
Sales to other utilities	11,702
Customer sales	3,177
Rate increase	2,755
Miscellaneous	199
Total electric	34,507

Gas:	
Gas cost adjustment charges .	2,651
Rate increase	610
Customer sales	(660)
Miscellaneous	17
Total gas	2,618
Total electric and gas ...	$37,125

Sales of firm capacity to New York State Electric and Gas Corporation accounted for $1.2 million of the increase in revenues from other utilities.

Total sales of electricity within the Company's service territory increased 4% in 1977. Increased production by the cement manufacturers located in the Company's territory was the major factor contributing to a 10% growth in sales to industrial customers.

Sales of natural gas were 9% lower than 1976 mainly as a result of decreased sales of seasonal and interruptible gas service. Curtailments by the Company's pipeline suppliers reduced the amount of gas available for such sales. The Company, however, was able to meet the needs of all of its firm gas customers. The decreases in sales of gas to firm customers resulted primarily from the warmer weather experienced during the last quarter of 1977 and the additional efforts put forth by customers to conserve gas during the severe cold spell experienced in the first quarter of 1977.

Changes in sales by major customer classification are set forth below (parentheses denote decrease):

	Electric	Gas
Residential	0%	(3)%
Commercial	3	(5)
Industrial	10	(13)
Interruptible and Seasonal	N/A	(19)

Operating Expenses

Costs for operations increased $32.8 million in 1977. The largest increase was in the cost of fuel used in electric generation which amounted to $21.6 million more than in 1976. This increase resulted from higher fuel oil prices and a 7% increase in generation. The cost of purchased electricity increased $6.8 million, reflecting primarily the purchase of less expensive energy from member companies of the New York Power Pool when such power was available. Although the volume of natural gas purchased decreased 10%, the cost of such gas increased $2.0 million as a result of higher rates charged by the Company's pipeline suppliers. Other expenses of operation were $2.4 million over last year. Increased wages and related fringe benefits together with higher costs for research and development represent the major portion of this increase.

Maintenance expenses increased $1.3 million, or 19%. The two most significant variations were a $570,000 increase in the cost of tree trimming and a $365,000 increase in the cost of maintaining electric generating units.

Operating taxes increased $1.6 million. State and local taxes levied on gross revenues increased $1.0 million while property taxes were up $410,000 as compared to 1976.

Federal income tax charged to "Operating Expenses" increased $707,000 in 1977.

Other Income, Interest Charges, and Preferred Stock Dividends

The total amount of AFDC increased $1.6 million in 1977 primarily as a result of the Company's participation in Unit No. 2 of the Nine Mile Point Plant and the Sterling Plant. The AFDC rate used by the Company was 8% in 1977 and 8½% in 1976.

Total interest charges (excluding AFDC) increased $357,000. The $158,000 increase in interest charges on mortgage bonds reflects the interest on the $4.5 million of 6¼% bonds issued in June 1977. The decrease of $662,000 in interest charges on unsecured long-term debt and the increase of $485,000 in other interest charges resulted primarily from the charging of interest expense on long-term debt maturing within one year to other interest charges. Short-term interest charges increased $371,000 mainly due to higher levels of borrowings during the year.

The sale of the new preferred stock in May 1977 resulted in a $760,000 increase in the preferred stock dividends.

COMMON STOCK DIVIDENDS AND PRICE RANGES

Dividends have been paid by the Company and its principal predecessors for 75 years, and the common stock of the Company has been listed on the New York Stock Exchange since 1945. The price ranges and the dividends paid for each quarterly period during the Company's last two fiscal years were as follows:

1978	High	Low	Dividend
Fourth Quarter	$21⅞	$19¾	$.49
Third Quarter	22	20½	.49
Second Quarter	21¾	20⅛	.49
First Quarter	22⅛	20⅜	.47
1977			
Fourth Quarter	$22	$20⅝	$.47
Third Quarter	22½	20⅝	.45
Second Quarter	21⅞	19⅝	.45
First Quarter	21	19⅛	.43

FINANCIAL SECTION
1978 ANNUAL REPORT

Report of Independent Accountants

To the Board of Directors and Shareholders of
Central Hudson Gas & Electric Corporation

In our opinion, the accompanying balance sheet and the related statements of income, retained earnings, and changes in financial position present fairly the financial position of Central Hudson Gas & Electric Corporation at December 31, 1978 and 1977, and the results of its operations and the changes in its financial position for the years then ended, in conformity with generally accepted accounting principles consistently applied. Our examinations of these statements were made in accordance with generally accepted auditing standards and accordingly included such tests of the accounting records and such other auditing procedures as we considered necessary in the circumstances.

New York, New York
January 26, 1979

PRICE WATERHOUSE & CO.

Statement of Retained Earnings
(Thousands of Dollars)

	Year ended December 31, 1978	1977
Balance at beginning of year	$61,481	$56,326
Net Income	20,260	17,747
	81,741	74,073
Dividends declared—cash:		
On cumulative preferred stock	4,126	3,626
On common stock ($1.96 per share 1978; $1.84 per share 1977)	10,531	8,966
	14,657	12,592
Balance at end of year	$67,084*	$61,481

*Pursuant to the terms of the 4.85% promissory notes, due 1995, $58,670 is not restricted with respect to the declaration of dividends on common stock.

Statement of Income
(Thousands of Dollars)

	Year ended December 31, 1978	1977
Operating Revenues		
Electric	$158,784	$154,366
Gas	24,738	23,449
Total—own territory	183,522	177,815
Revenues from electric sales to other utilities	27,480	30,025
	211,002	207,840
Operating Expenses		
Operation:		
Fuel used in electric generation (Note 1)	66,565	77,524
Purchased electricity	27,137	20,177
Purchased natural gas	11,691	11,697
Other expenses of operation	27,161	24,290
Maintenance	8,151	8,098
Depreciation (Note 1)	13,393	13,279
Taxes, other than income tax	18,779	18,560
Federal income tax (Note 2)	6,504	4,552
Deferred income tax—net (Note 2)	3,387	2,547
	182,768	180,724
Operating Income	28,234	27,116
Other Income and Deductions		
Allowance for equity funds used during construction (Note 1)	2,388	1,560
Federal income tax—credit (Note 2)	721	628
Deferred income tax—credit (Note 2)	138	75
Other—net	(348)	(90)
	2,899	2,173
Income before Interest Charges	31,133	29,289
Interest Charges		
Interest on mortgage bonds	10,750	10,627
Interest on unsecured long-term debt	762	805
Interest on short-term debt	1,673	1,075
Other interest	272	793
Allowance for borrowed funds used during construction (Note 1)	(2,640)	(1,831)
Amortization of premium and expense on debt	56	73
	10,873	11,542
Net Income	20,260	17,747
Dividends on Preferred Stock	4,126	3,626
Income Available for Common Stock	$ 16,134	$ 14,121
Common Stock:		
Average Shares Outstanding (000's)	5,310	4,873
Earnings per Share—On Average Shares Outstanding	$3.04	$2.90
Earnings per Share—Assuming Conversion of the Convertible Debentures (Note 3)	*$2.88*	*$2.70*

Balance Sheet
(Thousands of Dollars)

Assets

	1978	1977
Utility Plant, at original cost		
Electric	$417,304	$377,753
Gas	49,335	48,726
Common	20,426	18,756
	487,065	445,235
Less accumulated depreciation	140,813	127,049
	346,252	318,186
Construction work in progress	72,546	49,337
	418,798	367,523
Investments in and Advances to Subsidiaries (Note 1)	838	837
Current Assets		
Cash	3,282	3,590
Special deposits	258	191
Accounts receivable from customers	16,962	14,824
Accrued unbilled utility revenues (Note 1)	4,547	4,769
Other receivables	1,594	1,223
Materials and supplies, at average cost:		
Fuel	9,951	8,412
Construction and operating	6,277	6,211
Prepayments	3,010	2,646
	45,881	41,866
Deferred Charges		
Deferred electric fuel costs (Note 1)	2,550	2,029
Deferred gas costs (Note 1)	834	539
Deferred environmental research and development costs	3,603	2,576
Unamortized debt expense	1,555	1,642
Unamortized project costs	616	771
Other	1,591	1,637
	10,749	9,194
	$476,266	$419,420

December 31, 1978 and 1977

Liabilities

	1978	1977
Capitalization		
Capital Stock (Note 5)		
Cumulative preferred stock	$ 61,030	$ 61,030
Premium on cumulative preferred stock	67	67
Common stock	76,371	66,031
Capital stock expense	(2,245)	(2,154)
	135,223	124,974
Retained Earnings	67,084	61,481
Long-term Debt (Note 6)	202,575	167,750
Unamortized Premium on Debt	470	501
	405,352	354,706
Current Liabilities		
Long-term debt maturing within one year	—	8,000
Sinking fund requirements	175	175
Notes payable (Note 4)	23,000	17,000
Accounts payable	12,519	10,609
Accrued taxes	5,988	4,414
Accrued interest	2,523	2,689
Customer deposits	2,698	2,543
Dividends declared	3,664	3,322
Other	3,647	2,678
	54,214	51,430
Deferred Credits and Other Liabilities		
Deferred gas refunds	1,182	1,239
Miscellaneous reserves	626	396
Other	297	302
	2,105	1,937
Accumulated Deferred Income Tax (Note 2)	14,595	11,347
	$476,266	$419,420

Statement of Changes in Financial Position
(Thousands of Dollars)

	Year ended December 31, 1978	1977
Source of Funds		
Internal sources:		
Net income	$20,260	$17,747
Income items not requiring current outlays:		
Depreciation accruals:		
Charged to depreciation expense	13,393	13,279
Charged to other income accounts	508	265
Deferred income tax—net	3,249	2,472
Equity component of AFDC*	(2,388)	(1,560)
Other—net	577	495
Net funds from internal sources	35,599	32,698
Available from financing:		
Mortgage bonds	—	4,500
Term loan notes	35,000	—
Preferred stock	—	15,000
Common stock	10,340	—
Short-term debt	6,000	—
Total funds from external sources	51,340	19,500
Total source of funds	$86,939	$52,198
Application of Funds		
Construction charges:		
Gross charges for construction	$64,513	$32,343
Less equity component of AFDC*	2,388	1,560
	62,125	30,783
Dividends:		
Preferred stock	4,126	3,626
Common stock	10,531	8,966
	14,657	12,592
Retirement of securities and short-term debt:		
Convertible debentures	8,000	—
Long-term promissory notes	175	4,375
Short-term debt	—	3,000
	8,175	7,375
Net increase (decrease) in working capital, other than short-term debt and current maturities of long-term debt.	(769)	1,240
Changes in deferred and other accounts—net	2,751	208
Total funds applied	$86,939	$52,198

*Allowance for funds used during construction (AFDC). (See Note 1.)

Notes to Financial Statements

Note 1 — Summary of Accounting Policies

General: The Company is subject to regulation by the New York State Public Service Commission (PSC) and the Federal Energy Regulatory Commission (FERC) with respect to its rates for service and the maintenance of its accounting records. The Company's accounting policies conform to generally accepted accounting principles as applied in the case of regulated public utilities and are in accordance with the accounting requirements and rate-making practices of the regulatory authorities having jurisdiction.

Utility Plant: The costs of additions to utility plant and replacements of retirement units of property are capitalized at original cost. Costs include labor, materials and supplies, indirect charges for such items as transportation, certain taxes, pension and other employee benefits, and an allowance for the cost of funds used during construction. Replacement of minor items of property is included in maintenance expenses.

The original cost of property, together with removal cost, less salvage, is charged to accumulated depreciation at such time as the property is retired and removed from service.

Allowance for Funds used During Construction (AFDC): The Company includes in plant costs an allowance for funds used during construction approximately equivalent to the cost of funds used to finance construction expenditures. The concurrent credit for the amount so capitalized is reported in the Statement of Income as follows: the portion applicable to borrowed funds is reported as a reduction of interest charges while the portion applicable to other funds (the equity component) is reported as other income. AFDC was computed at a rate of 8¾% for the last two months of 1978, 8½% for the first ten months of 1978, and 8% for 1977. The equity component of AFDC is not considered a current source of funds and therefore is not included as such in the Statement of Changes in Financial Position.

Depreciation: For financial statement purposes, the Company's depreciation provisions are computed on the straight-line method using rates based on annual studies of the estimated useful lives and estimated net salvage of properties. The provision for depreciation of transportation equipment is charged indirectly to various asset and expense accounts, while the depreciation provision for certain properties included in the account "Plant Held for Future Use" is charged to "Other Income Deductions" for accounting purposes. The Company's total provision for depreciation amounted to approximately 3.2% of the original cost of average depreciable property in both 1978 and 1977.

The ratio of the amount of accumulated depreciation to the cost of depreciable property at December 31 was 29.3% in 1978 and 29.0% in 1977.

For federal income tax purposes, the Company uses an accelerated method of depreciation and generally uses the shortest life permitted for each class of assets.

Federal Income Tax: The Company's general policy with respect to accounting for the federal income tax is to reflect in income the amount of estimated income tax currently payable. However, certain tax deductions are accounted for on a deferred basis as described in Note 2.

Rates and Revenues: Electric and gas retail rates applicable to intrastate service (other than contractually established rates for service to municipalities and governmental bodies) are regulated by the PSC. Transmission rates and rates for electricity sold for resale in interstate commerce are regulated by FERC.

Revenues are recognized on the basis of cycle billings rendered monthly or bimonthly. Estimated revenues are accrued for those bimonthly customers whose meters are not read in the current month.

The Company's tariff for retail electric service includes a fuel cost adjustment clause pursuant to which electric rates are adjusted to reflect changes in the average cost of fuels used in electric generation and certain purchased power costs from the average of such costs during a base period. The Company's tariff for gas service contains a comparable clause to adjust gas rates for changes in the price of purchased natural gas and certain costs of manufactured gas.

Deferred Electric Fuel Costs: The provisions of the electric fuel cost adjustment clause are such that changes in fuel costs incurred in the current month are not billed to customers until subsequent months. Therefore, in order to match costs and revenues, the Company defers that portion of such costs incurred in the current month which will result in a cost adjustment in subsequent months.

Deferred Gas Costs: In accordance with requirements applicable to all regulated gas utilities in the State, the Company defers each month any difference between the amount of gas costs incurred which are recoverable through the gas adjustment clause (GAC) and GAC revenues. The net deferral remaining at August 31 of each year is amortized over a subsequent twelve-month period for both billing and accounting purposes.

Subsidiaries: The subsidiaries are wholly owned land-holding companies, and they are not consolidated for financial reporting purposes since their assets, liabilities and operations are not significant in relation to those of the Company. The Company uses the equity method of accounting for its investment in subsidiaries.

Note 2 — Federal Income Tax

Depreciation: In computing depreciation for federal income tax purposes the Company uses an accelerated method as permitted under the Internal Revenue Code, and the class life system prescribed in the Revenue Act of 1971.

Investment Tax Credit: The federal income tax is reduced by the investment tax credit. The additional investment tax credit resulting from increasing the rate of such credit from 4% to 10%, as provided by the Tax Reduction Act of 1975, is being deferred and amortized over the life of the related property in accordance with a Statement of Policy of the PSC. The investment tax credit which is not deferred is allocated equally between "Utility Operating Income" and "Other Income and Deductions" in accordance with the Uniform Systems of Accounts of the PSC.

In 1977 the Company established a Tax Reduction Act Stock Ownership Plan which is funded by the use of the additional 1% investment tax credit permitted by the Tax Reduction Act of 1975. The 1% credit amounted to $275,000 for 1977 and is estimated to be $283,000 for 1978.

Deferred Income Tax: The Company is using deferred tax accounting for the following income tax deductions:

1. additional depreciation resulting from the use of the class life depreciation system, the tax effect of which is being amortized over the lives of the related assets;
2. costs of removal, the tax effect of which is being amortized over a five-year period commencing with the year such removal costs are incurred;
3. additional 6% of investment tax credit resulting from the Tax Reduction Act of 1975;
4. electric fuel costs and gas costs recoverable in subsequent periods, the tax effect of which is recognized,as related revenues are recorded; and
5. certain other deferred costs.

A summary of the amounts deferred or credited to income is as follows:

	Amounts Deferred		Amounts Credited	
	1978	1977	1978	1977
	(Thousands of Dollars)			
Operating Income:				
Class life depreciation	$1,175	$1,071	$ 64	$ 30
Cost of removal	404	371	385	378
Investment tax credit	1,699	1,676	—	—
Deferred fuel and gas costs	1,625	1,218	1,232	1,760
Other	327	541	162	162
	5,230	4,877	1,843	2,330
Other Income (Investment tax credit)	—	—	138	75
Total	$5,230	$4,877	$1,981	$2,405

Reconciliation: The following is a reconciliation of the difference between the amount of federal income tax as reported in the Statement of Income and the amount computed by multiplying the income before tax by the statutory tax rate.

	1978		1977	
	Amount ($000)	% of Pretax Income	Amount ($000)	% of Pretax Income
Net income	$20,260		$17,747	
Federal income tax	5,783		3,924	
Deferred income tax—net	3,249		2,472	
Income before tax	$29,292		$24,143	
Computed tax expense	$14,060	48.0%	$11,589	48.0%
Increases (reductions) in computed taxes resulting from:				
Investment tax credit	(2,830)	(9.7)	(2,845)	(11.8)
Allowance for funds used during construction	(2,413)	(8.2)	(1,628)	(6.7)
Excess of tax depreciation over book depreciation	(1,550)	(5.3)	(2,069)	(8.6)
Taxes and pension costs expensed on tax return and capitalized on books	(598)	(2.1)	(601)	(2.5)
Cost of removal	(505)	(1.7)	(464)	(1.9)
Deferred fuel and gas costs—net	(393)	(1.3)	542	2.2
Deferred costs	(275)	(1.0)	(461)	(1.9)
Miscellaneous items—net	287	1.0	(139)	(.5)
Federal income tax	5,783	19.7	3,924	16.3
Deferred income tax—net	3,249	11.1	2,472	10.2
Total	$ 9,032	30.8%	$ 6,396	26.5%

Note 3 — Earnings per Share and Convertible Debentures

The 5¾% convertible debentures were repaid at maturity on February 1, 1978. At December 31, 1978 the 4⅜% convertible debentures, due June 1, 1981, were convertible into common stock at the rate of $31.48 per share, and accordingly 254,130 shares of common stock authorized and unissued were reserved for such purpose. The dual presentation of earnings per share data in the Statement of Income reflects the net reduction in earnings per share which would have been realized if the debentures outstanding at the end of each period had, in fact, been converted to common stock. No debentures have been converted, and at December 31, 1978 the conversion price of $31.48 compared with a closing market price per share of $19.875.

Note 4 — Short-Term Borrowing Arrangements and Compensating Balances

At December 31, 1978 the Company maintained lines of credit with seven banks totaling $43,000,000. At that time the outstanding short-term obligations, which consisted only of commercial paper, amounted to $23,000,000. The total amount of commercial paper outstanding at December 31, 1978 was backed by the lines of credit maintained with the banks. Such commercial paper had maturities ranging from 27 days to 63 days and carried interest rates ranging from 10.375% to 10.825%. The average interest rate on such obligations was 10.5%.

The maximum amount of aggregate short-term borrowings during 1978 was $35,000,000, which occurred on February 10. The maximum amount during 1977 was $29,000,000, which occurred on each of the following three dates: February 10, April 15, and May 10. The average amount of short-term borrowings during 1978, based on the month-end figures, was $20,283,333; the approximate weighted average interest rate, on the same basis, was 8.2%. The comparable figures for 1977 were $18,492,000 and 5.6%.

Compensating balance requirements are not formalized under the lending arrangements with banks, but the Company is expected to maintain certain average balances against its lines of credit and/or the average amounts borrowed. The requirements differ from bank to bank, but in general call for the maintenance of average balances equal to 10% of the line of credit plus 10% of the average amount borrowed. Inasmuch as requirements are informal and are on an average basis, bank balances are not subject to any restrictions with respect to withdrawals. Accordingly, amounts on deposit, including float, may be greater or less than computed average balances at any given date. Substantially all cash balances were considered to represent compensating balances at December 31, 1978.

Note 5 — Capital Stock

Details of capital stock at December 31, 1978 and 1977 are shown below:

	Redemption Price			Shares Authorized	Shares Outstanding	
	Current	Through	Eventual Minimum		December 31, 1978	December 31, 1977
Common stock without par value (Note 3)				10,000,000	5,372,873	4,872,873
Cumulative preferred stock, $100 par value				1,200,000		
4½% series	$107.00	—	$107.00		70,300	70,300
4.75% series	106.75	—	106.75		20,000	20,000
4.35% series	102.00	—	102.00		60,000	60,000
4.96% series	101.00	—	101.00		60,000	60,000
7.72% series	107.00	1/31/81	101.00		130,000	130,000
7.44% series	106.80	1/31/83	101.22		120,000	120,000
8.40% series	108.40	5/31/82	101.00		150,000	150,000
Total					610,300	610,300

Expenses incurred on issuance of capital stock are accumulated and reported as a reduction in total capital stock and are not being amortized.

Note 6 — Long-Term Debt

Details of long-term debt are shown below:

	December 31, 1978	December 31, 1977
	(Thousands of Dollars)	
First mortgage bonds:		
2⅞% series, due December 1, 1980	$ 12,000	$ 12,000
3.30% series, due December 1, 1982	6,000	6,000
3.20% series, due October 1, 1984	11,000	11,000
4⅛% series, due May 15, 1988	18,000	18,000
7⅛% series, due January 15, 1999	20,000	20,000
9⅜% series, due June 1, 2000	25,000	25,000
7¾% series, due February 1, 2002	20,000	20,000
9¼% series, due April 15, 2004	15,000	15,000
10⅝% series, due November 1, 2005	20,000	20,000
6¼% series, due June 1, 2007	4,500	4,500
	151,500	151,500
Convertible debentures (Note 3): 4⅜%, due June 1, 1981	8,000	8,000
Promissory notes (net of sinking fund requirements): 4.85%, due December 1, 1995	8,075	8,250
Term loan notes (see below)	35,000	—
Total long-term debt	$202,575	$167,750

In December 1978 the Company issued term loan notes aggregating $35 million to three banks. The Loan Agreement under which these notes were issued provides that the notes shall be paid in three consecutive annual installments commencing December 31, 1979; the Company, however, has the right to prepay any installment in whole or in part without penalty and also has the right to defer, without penalty, the payment of each of the first two installments until December 31, 1981, the date on which the third installment is due. The interest rate on such notes during the first two years is the "prime" rate in effect at the Irving Trust Company and the rate during the third year is such rate plus .25%.

Expenses incurred on debt issues and any discount or premium on debt are deferred and amortized over the lives of the related issues.

Note 7—Pension and Retirement Plan

The Company has a noncontributory pension and retirement plan (Plan) available to all employees after one year's employment.

The cost of the Plan to the Company amounted to $2,694,000 for the calendar year 1978 and $2,348,000 for 1977. Of these amounts, approximately 20% in 1978 and 24% in 1977 were charged to construction. Based upon the Annual Valuation Report furnished to the Company by the independent actuary for the Plan, the unfunded liability was $5,333,587 as of September 30, 1978, the end of the last Plan year. The unfunded liability is being amortized and funded over a period of fifteen years. Current service costs are funded annually.

The independent actuary has also furnished the Company with its opinion that as of September 30, 1978 the assets of the Plan were sufficient to cover the liabilities in respect of the members of the Plan who are eligible for vested benefits.

Note 8 — Commitments and Contingencies

The Company is engaged in a construction program which is presently estimated to involve expenditures during the period 1979 through 1983 of $296.8 million. The estimates by years are as set forth below:

	1979	1980	1981	1982	1983	5-Year Total
			(Thousands of Dollars)			
Construction Expenditures:*						
Expenditures excluding future generating plants	$15,200	$17,500	$21,400	$23,000	$18,600	$ 95,700
Participation in Unit No. 2 of the Nine Mile Point Plant (9%)	21,000	24,100	19,700	17,700	24,700	107,200
Participation in the Sterling Plant (17%)	3,500	4,400	8,100	18,900	45,700	80,600
Purchase of an additional 5% interest in the Roseton Plant	—	—	—	13,300	—	13,300
Total	$39,700	$46,000	$49,200	$72,900	$89,000	$296,800

*Including AFDC (see Note 1).

The above five-year construction program does not include any provision for (1) the possible conversion from oil-firing to coal-firing of Units Nos. 3 and 4 of the Danskammer Plant; (2) the possible installation of cooling towers at the Roseton Plant and the possible alteration of the cooling water intake and discharge facilities at the Danskammer Plant; and (3) compliance with other environmental and energy conservation requirements. Estimates of construction expenditures are subject to continuous review and adjustment and actual construction expenditures may vary from such estimates as a result of the matters referred to above or other causes.

The Company's undivided interest in the ownership and output of the Roseton Plant was increased from 20% to 30% as of December 31, 1978. It is obligated to purchase a further 5% interest in 1982 and has an option to acquire the remaining interests of the other two owners in 2004. In addition, the Company is obligated to purchase specified amounts of Roseton Plant capability during the summer capability periods through 1982. The Company's share of direct operating expense for the Roseton Plant is included in the appropriate expense classification in the accompanying income statement.

The Company has long-term contracts for the supply of natural gas with three pipeline suppliers. The earliest expiration date of any of these contracts is in 1988. The Company also has a contract for the storage of gas. All such contracts are under tariffs on file with and approved by FERC.

Reference is made to the section entitled "Central Hudson Provides Essential Services" for additional information regarding the Nine Mile Point Plant, the Sterling Plant, the Roseton Plant, and Natural Gas Supply.

Commitments for minimum rentals under noncancellable leases are minor, and neither the present value of non-capitalized financing leases nor the impact on net income of capitalizing such leases is significant.

Note 9 — Departmental Information

The following presents certain information pertaining to the Company's operations for its electric and gas departments for the years ended December 31, 1978 and 1977:

	Electric		Gas		Total	
	1978	1977	1978	1977	1978	1977
	(Thousands of Dollars)					
Operating Revenues	$186,264	$184,391	$24,738	$23,449	$211,002	$207,840
Operating Expenses:						
Depreciation	11,887	11,813	1,506	1,466	13,393	13,279
Other, excluding income tax	140,689	141,875	18,795	18,471	159,484	160,346
Total	152,576	153,688	20,301	19,937	172,877	173,625
Operating Income before Income Tax	33,688	30,703	4,437	3,512	38,125	34,215
Federal Income Tax, including deferred income tax—net	8,799	6,667	1,092	432	9,891	7,099
Operating Income	$ 24,889	$ 24,036	$ 3,345	$ 3,080	$ 28,234	$ 27,116
Construction Expenditures*	$ 62,703	$ 30,648	$ 1,810	$ 1,695	$ 64,513	$ 32,343
Identifiable Assets at December 31*						
Net Utility Plant	$308,893	$280,607	$37,359	$37,579	$346,252	$318,186
Construction Work in Progress	70,734	48,214	1,812	1,123	72,546	49,337
Total Utility Plant	379,627	328,821	39,171	38,702	418,798	367,523
Materials and Supplies	15,511	14,041	717	582	16,228	14,623
Total	$395,138	$342,862	$39,888	$39,284	$435,026	$382,146

*Includes allocation of Common Utility Property.

Note 10—Selected Quarterly Financial Data (Unaudited)

Selected financial data for each quarterly period within 1977 and 1978 are shown below:

	Operating Revenues	Operating Income	Net Income	Income Available for Common Stock	Earnings Per Average Share of Common Stock Outstanding
	(Thousands of Dollars)				(Dollars)
Quarter Ended:					
March 31, 1977	$55,512	$8,660	$6,112	$5,396	$1.11
June 30, 1977	47,914	5,518	3,110	2,264	.47
September 30, 1977	53,500	6,254	3,954	2,922	.60
December 31, 1977	50,914	6,683	4,570	3,538	.72
March 31, 1978	59,449	9,437	7,242	6,210	1.21
June 30, 1978	48,398	5,850	3,881	2,850	.53
September 30, 1978	50,576	6,421	4,535	3,503	.65
December 31, 1978	52,578	6,526	4,602	3,570	.66

Note 11 — Replacement Cost Data (Unaudited)

The Company has computed replacement cost data in compliance with reporting requirements of the Securities and Exchange Commission and will include such estimated replacement cost information in its annual report on Form 10-K for the year ended December 31, 1978. The impact of inflation, particularly in recent years, is such that the cost of replacing the Company's plant in service would be significantly greater than the historical costs of such facilities being reported in the financial statements. The Company's rates are subject to regulation and, although there are no plans to undertake other than normal replacements of plant in service, the Company believes that any higher costs it may experience upon replacement of existing facilities would be recovered through the normal regulatory process.

DIRECTORS

ERNEST E. ALTHOUSE
Poughkeepsie, N.Y.
Vice Chairman of the Board and Vice Chairman of Committee on Finance; Member of Executive Committee and Committee on Compensation and Succession

WILLIAM P. ARNOLD
New York, N.Y.
President, Associated Dry Goods Corporation, a department store chain; Member of Committee on Audit

RAYMOND T. BENEDICT
Stamford, Ct.
Lawyer, of Counsel, Cummings & Lockwood; Member of Executive Committee and Committee on Finance

JAMES R. BREED, M.D.
Poughkeepsie, N.Y.
Surgeon
Member of Committee on Audit

THEODORE J. CARLSON
Poughkeepsie, N.Y.
Chairman of the Board and Principal Officer; Chairman of Executive and Retirement Committees; Member of Committees on Finance, on Audit and on Compensation and Succession

ROY C. KETCHAM
Fishkill, N.Y.
Chairman of the Board and Chief Executive Officer, Ketcham Motors, Inc., an automobile and farm equipment dealership; Chairman of the Board of The Fishkill National Bank; Chairman of Committee on Compensation and Succession; Member of Executive Committee

EDWARD J. MACK
LaGrangeville, N.Y.
Lawyer; Member of Retirement Committee and Committee on Compensation and Succession

HERBERT L. SHULTZ
Kingston, N.Y.
Vice President for Development, Vassar College; Member of Retirement Committee and Committee on Audit

JOHN WILKIE
Katonah, N.Y.
Chairman of Committees on Finance and on Audit; Member of Executive and Retirement Committees

H. CLIFTON WILSON
Poughkeepsie, N.Y.
President; Member of Executive and Retirement Committees, and Committees on Finance and on Compensation and Succession

OFFICERS OF THE BOARD

THEODORE J. CARLSON
Chairman of the Board and Principal Officer and Chairman of Executive and Retirement Committees

JOHN WILKIE
Chairman of Committees on Finance and on Audit

ERNEST E. ALTHOUSE
Vice Chairman of the Board and Committee on Finance

ROY C. KETCHAM
Chairman of Committee on Compensation and Succession

OFFICERS

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President

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Vice President-Engineering

L. WALLACE CROSS
Vice President-Finance and Accounting

WILLIAM A. KLING
Vice President-Community Affairs and Corporate Services

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Vice President-Customer Services

CHARLES E. RIDER
Vice President

HENRY L. WALKER
Vice President-Production

JOSEPH F. FURLONG
Secretary and Treasurer

NORMAN J. PAXTON
Controller

JAMES E. SMITH
Assistant Vice President

WALTER A. BOSSERT, JR.
Assistant Secretary and Assistant Treasurer

CHARLES P. KOVAR
Assistant Secretary

EMORY R. OSBORN
Assistant Treasurer

TRANSFER AGENTS

COMMON STOCK
Irving Trust Company
1 Wall Street
New York, New York 10015

PREFERRED STOCK
4.35%, 4½%, 4.75%, 4.96% Series
Charles P. Kovar, Emory R. Osborn
Central Hudson Gas & Electric Corporation
Poughkeepsie, New York 12602

7.44%, 7.72%, 8.40% Series
Marine Midland Bank
2 Broadway
New York, New York 10004

REGISTRAR

COMMON STOCK
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INDEPENDENT ACCOUNTANTS

Price Waterhouse & Co.
153 East 53rd Street
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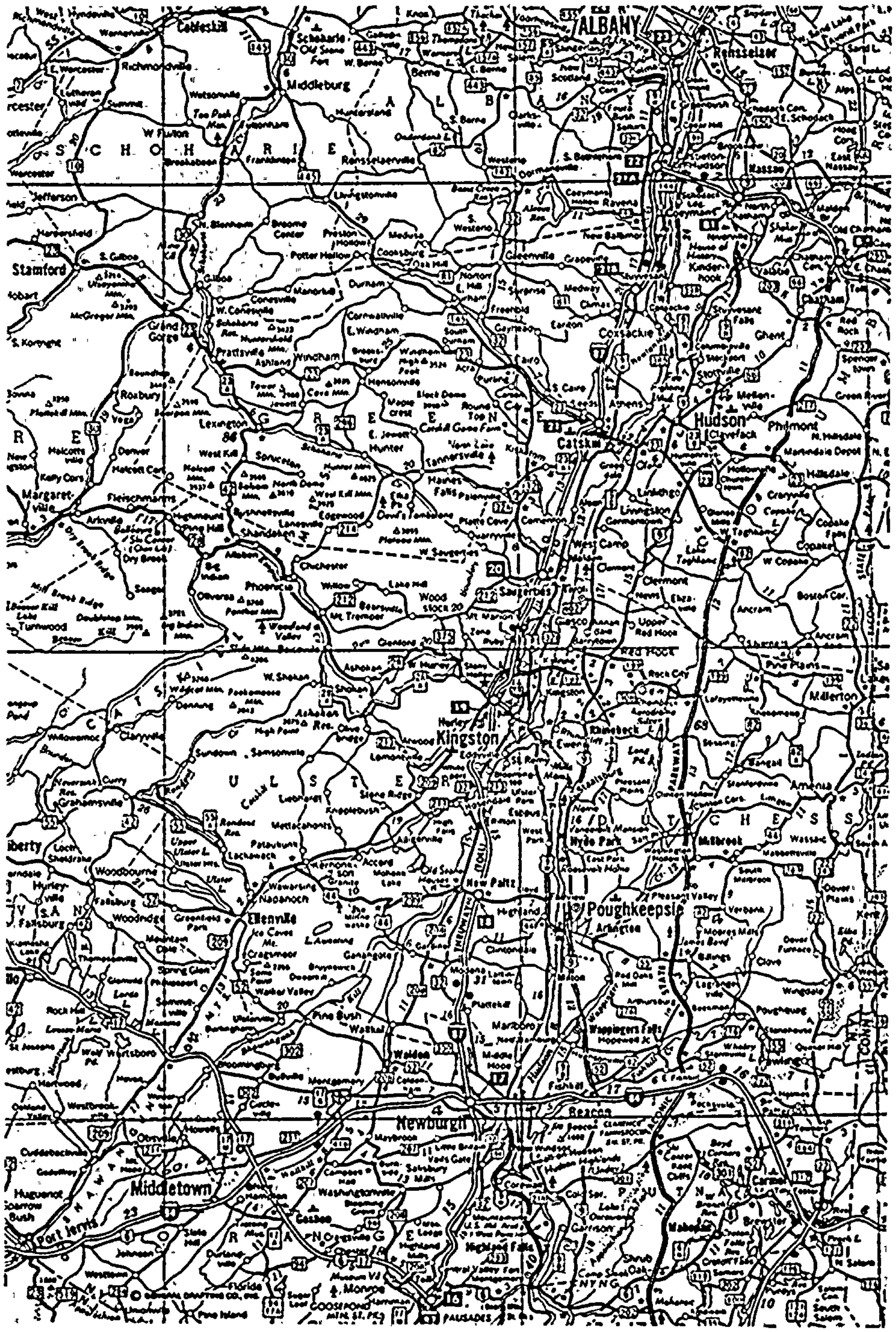

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The map depicts the
2,600 square-mile area
served by Central Hudson,
extending from 10 miles south
of Albany to 30 miles north
of New York City, and
including a population
of about 540,000.