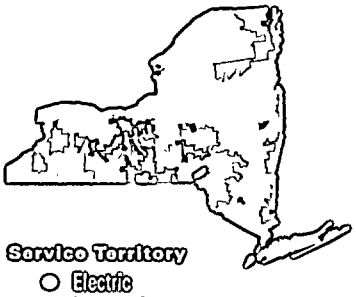
Corporate Profile

OVERVIEW

NYSEG is a market-driven energy enterprise dedicated to generating, marketing and delivering safe, reliable energy and energy-related products and services. Our expansive service territory encompasses one-third of New York State. Our priority is to achieve superior customer satisfaction and loyalty by offering customized, competitively-priced solutions to meet energy and energy-related needs.



Service Territory
- Electric
- Natural Gas
- Electric & Natural Gas

VISION

NYSEG is committed to helping companies and people shape their energy environments in ways that improve the efficiency and quality of their businesses and lives.

STRUCTURE

Electric Generation Our generation business is a low-cost electricity producer and marketer, serving wholesale and retail customers in the Northeast. Our electric generating system is consistently among the top 10 most efficient in the nation, generating 16 million megawatt-hours of electricity in 1996.

Natural Gas Our natural gas business has increased in throughput, revenues and profit since 1992. Nine new franchises added in 1996 make it the fastest growing natural gas business in New York State. Aggressive, entrepreneurial and growing, we offer some of the most competitive prices in the Northeast.

Customer Service and Energy Delivery Meeting the energy needs of 808,000 electric and 238,000 natural gas customers, we stand by our 144-year reputation for the operation of a safe, reliable energy system. Our highly-trained, responsive company representatives are also active members of the communities we serve.

Energy Services XENERGY, Inc., is an established and rapidly growing international energy services, information systems and energy consulting company. In 1996, by seizing opportunities emerging in the competitive energy services market, XENERGY won major contracts and now supplies electricity to several Fortune 500 firms.

Shaping Tomorrow

NYSEG

1996 Annual Report New York State Electric & Gas Corporation

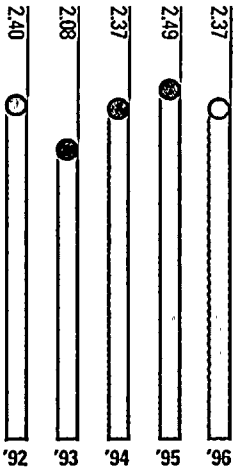
Financial Highlights

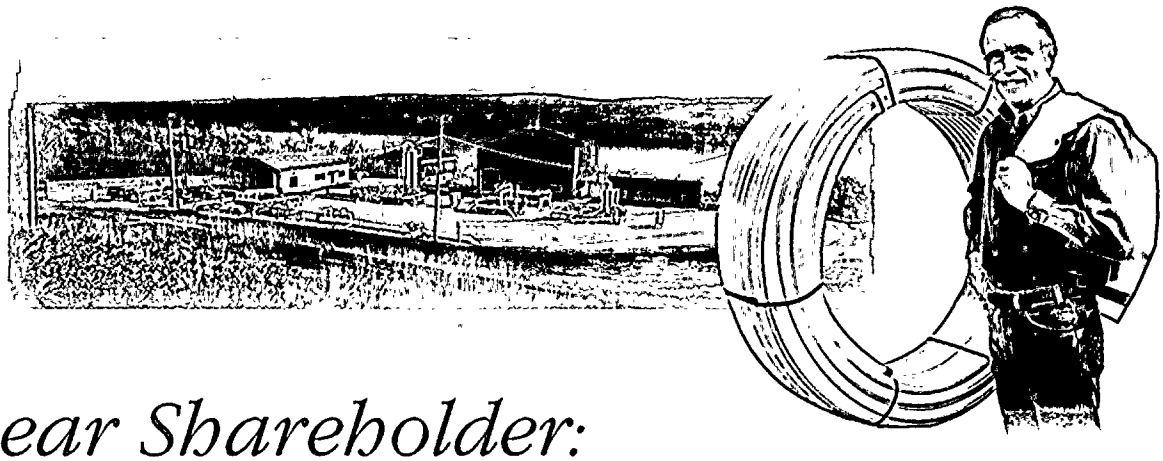
At December 31	1996	1995	% Change
Total Assets (Thousands)	$5,059,681	$5,114,331	(1)
Operating Results (Thousands)			
Total Operating Revenues	$2,059,371	$2,009,541	2
Total Operating Expenses	$1,601,828	$1,537,397	4
Net Income	$178,241	$196,690	(9)
Earnings Available for Common Stock	$168,711	$177,969	(5)
Retail Megawatt-hour Sales	13,216	13,093	1
Dekatherms of Natural Gas Delivered	61,542	58,535	5
Per Common Share			
Earnings	$2.37	$2.49	(5)
Dividends	$1.40	$1.40	–
Book Value (Year end)	$25.41	$24.38	4
Market Value (Year end)	$21.63	$25.88	(16)
Other Information			
Common Stock Price Range	$20⅜–26⅜	$19–26¾	
Return on Average Common Equity	9.6%	10.4%	(8)
Market-to-Book Ratio (Year end)	85%	106%	(20)
Average Common Shares Outstanding (Thousands)	71,127	71,503	(1)
Common Stock Shareholders of Record (Year end)	45,608	50,576	(10)

* Net income, earnings available for common stock, earnings per common share and return on average common equity for 1996 include the effect of the writedown of the investment in EnerSoft Corporation that decreased net income and earnings available for common stock by $10 million, earnings per common share by 14 cents and return on average common equity by 0.6%.

Earnings

(Dollars Per Share)





Dear Shareholder:

It is a privilege to write to you as the new chief executive officer of NYSEG. Since joining the company a few months ago, I have been quickly getting up to speed on opportunities and challenges, as well as visiting with employees, customers, shareholders and other stakeholders throughout our expansive service area. Two impressions stand out: the high caliber of our people and their commitment to our customers, and the high regard in which we are held by our customers for our reliable operations and responsiveness. It is clear that we have the resources and the determination to meet the challenges facing New York's energy industry in 1997 and beyond — and to capitalize on the opportunities this new environment presents.

The electric and natural gas utility businesses are undergoing rapid change as they react to increasing competition. At NYSEG, we have been in the forefront of change and are no stranger to competition. In fact, our natural gas business has operated in a competitive market for several years. We offer a host of supply and pricing options and services to our customers and our natural gas prices are some of the most competitive in the Northeast. We are growing the business by acquiring new franchises, building natural gas storage facilities and improving sales in traditional service areas.

The electric side of our enterprise has been preparing to compete. We are doing a good job of controlling our own costs — they have remained relatively flat since 1988. Despite our efforts, taxes and government mandated payments to nonutility generators (NUGs) together have tripled since 1988, driving up electric prices. Taxes and mandated power purchases from NUGs contribute disproportionately to New York's electric prices being among the highest in the country, making increasing competition all the more difficult and challenging. The New York State Legislature is expected to consider important legislation in 1997 that would lower the onerous gross receipts tax and provide access to low-cost financing to lessen the cost impacts of NUG contracts. Both of these actions would lead to price reductions for customers.

XENERGY, our 22-year-old energy services company with offices throughout North America, provides value-added products and services that give our customers greater control over their environments — at work and at home. This is a highly competitive field that complements our electric generating, natural gas and energy delivery expertise. XENERGY's goal is to provide customers with one-stop shopping for energy and energy management services.

New York is one of several states leading the nation toward unbundling the traditional services provided by utilities. Last September, we responded to the Public Service Commission's (PSC) restructuring proceeding with a plan that proposed an orderly transition to competition in our service area over a five-year period, with wholesale competition beginning in August 1997 and customer choice in August 1998. We further proposed to hold electric prices flat for five years and requested that we have the opportunity to fully recover investments previously approved by the PSC, and that were made in accordance with our obligation to provide safe and adequate service to our customers. We also filed to create a holding company, an organizational structure which has become quite common in our industry. We expect the PSC to rule on our restructuring proposals in 1997.

While the unpredictable electric restructuring process has created uncertainty for the company in the financial markets and for our employees, we have not lost sight of our fundamental priorities to achieve superior customer satisfaction, be price competitive and pursue growth opportunities. You will see in this report that 1996 was another good year on all three fronts. The strengths of our business — low electric production costs, low-priced natural gas and being a highly regarded provider of energy services — will position us well in the emerging competitive marketplace.

Earnings for 1996 were $2.37 per share, down from $2.49 in 1995. Excluding a charge of 14 cents per share to write down our investment in EnerSoft, the software development company that ceased operations in December, earnings in 1996 were $2.51.

We believe we are pursuing a vision that will create value for all our customers and shareholders. That is, to be an energy enterprise dedicated to achieving superior customer satisfaction by helping companies and people shape their energy environments in ways that improve the efficiency and quality of their businesses and lives.

Before closing, I would like to pay tribute to James A. Carrigg who retired last September as chairman, president and chief executive officer of NYSEG. Jim did a remarkable job to prepare us for the future and we are most fortunate to have had his outstanding leadership. Also, on a sad note, I would like to recognize board member Charles W. Stuart, who passed away in November, and whose wise counsel over 25 years will be missed.

Our people are working relentlessly to help ensure that NYSEG is our customers' energy provider of choice — tomorrow as well as today. We are grateful for their contributions, and to you, our shareholders, for your continued confidence in NYSEG.

On Behalf of the Board of Directors,

Wes von Schack

Wesley W. von Schack
Chairman, President and Chief Executive Officer
JANUARY 23, 1997

CUSTOMERS • OFFERING FLEXIBLE ENERGY PRICES

We were the first utility in the state to offer flexible electric prices to eligible businesses. This economic development tool has helped retain and create hundreds of new jobs in our service area. In addition, we offer some of the most competitive natural gas prices in the Northeast and a host of supply and pricing options to industrial and commercial customers.

SLI Corporation, a cutting-edge semiconductor laser manufacturer, is a beneficiary of our flexible electric prices. SLI brought its new jobs to Binghamton after looking at sites served by municipal electric systems and sites in other states.

CUSTOMERS • EXCEEDING CUSTOMERS' EXPECTATIONS

We helped National Pipe & Plastics, Inc., near Binghamton, install a natural gas engine to run an industrial air compressor. Heat from the engine is captured and used to heat a warehouse. We also helped Cornell University plan the move of an overhead power line and construction of a parallel circuit. We then won the bid to do the work.

CUSTOMERS • GUARANTEEING SUPERIOR CUSTOMER SATISFACTION

We now offer four service guarantees: prompt turn on/turn off of existing services, hook up of new service within five days, satisfaction with a new natural gas home heating system and timely response in an emergency. In addition to the benefits to customers, the guarantees will help us identify better ways to complete day-to-day tasks.

Our new guarantees ensure that we are meeting our customers' service needs.

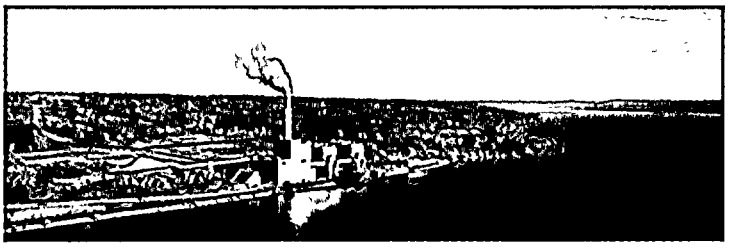
1996 HIGHLIGHTS

CUSTOMERS • PROTECTING THE ENVIRONMENT

We are vigilant in protecting the environment. NYSEG, in association with Kodak, was recently awarded U.S. Department of Energy funds to demonstrate how micronized coal reburning reduces nitrogen oxides emissions at our Milliken Generating Station and at a Kodak facility in Rochester.

Also, during planning and construction of the Seneca Lake Storage Project, which includes two new natural gas pipelines, protecting streams and controlling erosion were primary tasks.

Our Milliken Generating Station will soon be demonstrating how micronized coal reburning reduces nitrogen oxides emissions.



CUSTOMERS • BEST IN THE STATE

At the end of 1996, we had the lowest rate of customer complaints to the Public Service Commission among the state's combination electric and natural gas utilities.

Our customer call center and field employees are at the front line of our effort to achieve superior customer satisfaction.

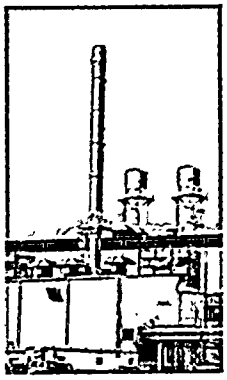
Our gas energy management system and Internet-based electronic bulletin board have made natural gas supply management and trading more efficient.

CUSTOMERS • PUTTING NATURAL GAS PRICES "ON ICE"

While the prices of most other fuels have skyrocketed this winter, natural gas prices for our residential customers are frozen through July 1998 at some of the most competitive levels in the Northeast.

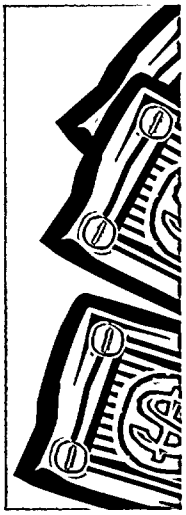
PRICE • REDUCING MANDATED NONUTILITY GENERATOR COSTS

We are mandated to buy high-priced electricity from nonutility generators (NUGs). Although we have saved customers more than $1 billion in NUG power costs through aggressive actions, more than 18 cents of every dollar we receive from our electric customers goes to pay for NUG power. We have commenced court actions and are backing legislation to further reduce NUG power costs.



The cost of power from nonutility generators, including this facility in Plattsburgh, is driving up electricity prices in New York State.

PRICE • WORKING TO LESSEN NEW YORK'S TAX HIT

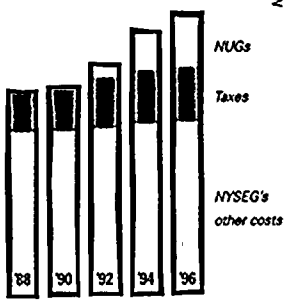


Taxes in New York State are more than double the national average. Of every dollar we receive from our electric retail customers, 19 cents goes to pay taxes. Our customers also pay local sales taxes on their purchases of NYSEG energy.

We are working diligently with legislators at the Capitol in Albany to lessen the impact of taxes on our customers' bills.

PRICE • FIGHTING THE GROSS RECEIPTS TAX

New York utilities are saddled with a 4.25% gross receipts tax while other businesses are taxed on their net income. In 1996, the gross receipts tax cost our customers $82 million. We support phasing out the gross receipts tax over five years or less, beginning in 1997. We will continue working with state legislators to make it happen.

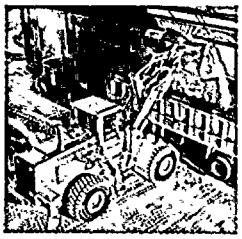


The costs we control have stayed relatively flat since 1988.

PRICE • CREATING ALTERNATIVES FOR WHAT USED TO BE WASTE

A flue gas desulfurization system, or scrubber, removes more than 90% of the sulfur dioxide produced in Milliken Generating Station's boilers. A byproduct of the process is gypsum, which is used in wallboard, cement and plaster. A Canadian wallboard manufacturer purchases most of Milliken's gypsum.

Gypsum from Milliken Generating Station's scrubber is sold to a Canadian wallboard manufacturer.



GROWTH • HELPING NEW YORK STATE'S ECONOMY REBOUND

We work with community development agencies to help new and expanding businesses select sites, negotiate real estate transactions, assess environmental requirements, obtain financial or tax incentives, and develop staffing and training programs. Our tools include flexible electric and natural gas pricing, new software to monitor and document business activity and customer contacts, research and development investment, a real estate tracking system and a statewide community database. The bottom line is jobs for New York.

We are aggressively marketing our service area — "the economic energy zone" — to potential new businesses through our economic development program.

Our seasoned electricity trading group is the link between the economical power we have available for sale and the success we have had in the wholesale power markets.

GROWTH • BOOSTING THE BOTTOM LINE WITH WHOLESALE POWER SALES

Because our generating stations are efficient, low-cost producers, we are a strong competitor in the wholesale electric markets throughout the Northeast. In recent years our wholesale business has increased more than 30%, now comprising about 37% of total electric kilowatt-hour sales. We compete successfully with other utilities, power marketers and brokers.

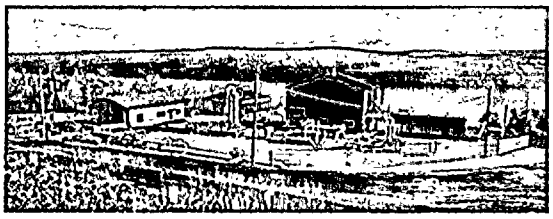
GROWTH • HITTING AN ECONOMIC DEVELOPMENT "HOME RUN"

Guardian Industries Corp., which produces flat glass for the construction and automotive industries, will employ approximately 250 workers when its new Geneva flat glass plant is up and running. The new plant will produce 600 tons of glass each day. Guardian cited our assistance in managing the site selection screening process, ensuring competitive energy rates, and helping them obtain environmental permits and emission reduction credits among the reasons it chose Geneva.

Guardian Glass chose Geneva as the site for a new plant that will employ 250 people.

GROWTH • CREATING A MORE FLEXIBLE NATURAL GAS SUPPLY

Our Seneca Lake Storage Project is the first high-deliverability natural gas storage facility in the Northeast. Two new pipelines link the storage facility with New York's Southern Tier. The project means increased supply flexibility for our growing natural gas business.



Our new natural gas storage facility and its two pipelines mean increased supply flexibility.

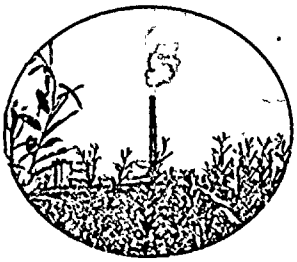
GROWTH • BUILDING OUR NATURAL GAS BUSINESS

We added nine natural gas franchises last year, representing over 1.5 million dekatherms of new load. Bringing natural gas to the Plattsburgh area makes available an economical and clean energy source for the former Plattsburgh Air Force Base, recently designated for development as an industrial park. Natural gas is particularly important in attracting businesses to the park. We also added franchises in the Towns of Carlisle, Cobleskill, Davenport and Halfmoon and the Village of Cobleskill.

XENERGY, headquartered in Burlington, Massachusetts, provides value-added products and services that give customers greater control over their environments — at work and at home.

GROWTH • PURSUING INNOVATIVE PROJECTS

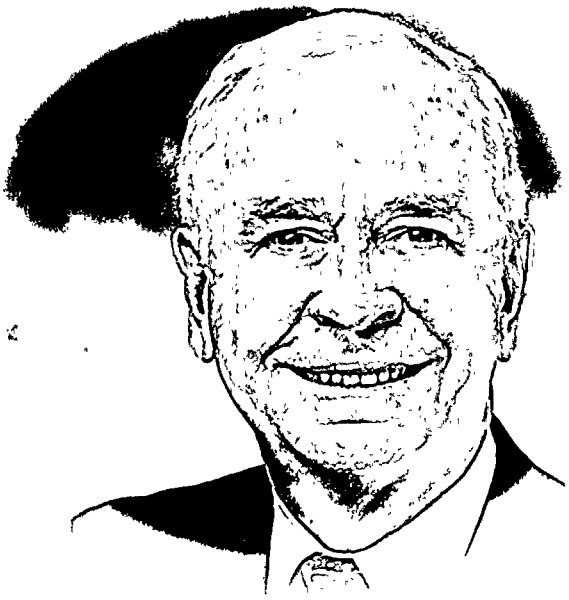
Among the innovative projects we are involved in are commercialization of fast-growing willow trees as a fuel for electric generating stations and the conversion of 10 UPS delivery vehicles to natural gas, the first such project outside a U.S. metropolitan area. UPS has the largest private fleet of natural gas-fueled vehicles in the country.



Willow, an alternative power plant fuel, is being grown on a three-acre test site at our Kintigh Generating Station.

GROWTH • GAINING VALUABLE EXPERIENCE IN RETAIL ACCESS

XENERGY Inc., is rapidly expanding its retail energy business. By winning key electricity contracts, such as one with the Massachusetts High Technology Council, XENERGY has become an industry leader. Across the nation, XENERGY is currently under contract to prepare several Fortune 500 firms for the competitive energy market.



James A. Carrigg

In Appreciation

DEDICATION AND COMMITMENT

... for his visionary leadership of and unselfish contributions to the utility industry and the community that are without parallel;
... an outstanding 38 year career with NYSEG,
... service in many important posts on utility industry councils,
... leadership in many community, civic and charitable organizations ...

New York State Senate Resolution, September 1996

We wish him well in retirement.

MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

LIQUIDITY AND CAPITAL RESOURCES

COMPETITIVE CONDITIONS

Movement toward competition was swift during 1996 for the historically regulated electric industry. The company is addressing numerous issues as it adjusts to operate under the complex and sweeping changes faced by its electric and natural gas businesses.

Electric Industry • The Public Service Commission of the State of New York (PSC), the Federal Energy Regulatory Commission (FERC) and regulators in other states are revising their policies to introduce competition and reduce rates in the electric industry. Orders were issued during 1996 in two significant proceedings: the PSC's Competitive Opportunities Proceeding and the FERC's proceeding relating to competitive wholesale electric markets.

Competitive Opportunities Proceeding: The transition to a more competitive electric industry in New York State was set in motion in August 1994 when the PSC instituted the Competitive Opportunities Proceeding. The overall objective of this proceeding is to identify regulatory and ratemaking practices that will assist in the transition to a more competitive electric industry.

On May 20, 1996, the PSC issued its Order in the Competitive Opportunities Proceeding, which calls for a competitive wholesale power market in early 1997 and the introduction of retail access for all electric customers in early 1998. The Order also calls for lowering rates for consumers, increasing customers' choice of suppliers, continuing reliability of service, continuing programs that are in the public interest, allaying concerns about market power and continuing customer protections and the utilities' obligation to serve.

The Order strongly encourages divestiture, particularly of generation assets, but does not require it. The Order states that incentives for divestiture will be worked out for each utility in conjunction with the rate and restructuring plan it was required to submit by October 1, 1996. (See Electric Rate and Restructuring Plan.) The Order also states that utilities should have a reasonable opportunity to seek recovery of strandable costs consistent with the goals of lowering rates, fostering economic development, increasing customer choices and maintaining reliable service. Certain aspects of the restructuring envisioned by the PSC — particularly its apparent determinations that it can deny a reasonable opportunity to recover prudent past investments made on behalf of the public, order retail wheeling, require divestiture of generation assets and deregulate certain sectors of the energy market — could, if implemented, have a negative effect on the operations of New York's investor-owned electric utilities, including the company.

On October 9, 1996, the PSC issued a procedural order allowing until January 7, 1997, (subsequently extended until February 14, 1997) to complete the discovery and settlement negotiations regarding the utilities' submissions (negotiation period). Any hearings as well as the submission of briefs and the closing of the record must be completed no later than 60 days after the negotiation period closes.

FINANCIAL REVIEW CONTENTS

Energy Association Lawsuit: In September 1996 the company joined with six other New York utilities and the Energy Association of New York State (Energy Association) in filing a lawsuit in the New York State Supreme Court, Albany County (Court) to annul the PSC's Order in the Competitive Opportunities Proceeding. The lawsuit seeks a declaration that the PSC's Order is unlawful, or in the alternative, that the Court clarify that the PSC's Order is simply a policy statement and can be given no binding effect by the PSC. The intent of the lawsuit is not to challenge the transition to competition, but to ensure that the transition is orderly and competition is fair to customers, shareholders and taxpayers. The lawsuit was necessary to preserve the company's shareholders' rights to have the opportunity to recover prudent investments made to serve customers and to protect the reliability of the electric system. To preserve those rights a lawsuit had to be filed within four months of the PSC's Order.

The lawsuit contends, among other things, that the PSC did not follow proper procedures in reaching its decision in the Competitive Opportunities Proceeding and lacks the statutory or legal authority to: deny a reasonable opportunity for utilities to recover past expenditures prudently incurred to fulfill their legal obligation to provide electricity service to the public, mandate retail wheeling, deregulate the rates charged by electricity generators or the energy services sector and order divestiture of the utilities' assets. On November 26, 1996, the Court issued a decision denying the relief requested.

On December 24, 1996, the seven New York utilities and the Energy Association appealed the decision to the New York State Supreme Court, Appellate Division (Third Department).

Given the uncertainties regarding the Competitive Opportunities Proceeding and the Energy Association lawsuit to annul the PSC's Order in that proceeding, the company is unable to predict the outcome of this proceeding and the ultimate effect on the company's financial position, results of operations, or its eligibility to continue applying Statement of Financial Accounting Standards No. 71 (Statement 71), Accounting for the Effects of Certain Types of Regulation. (See Accounting Issues.)

Electric Rate and Restructuring Plan: On September 27, 1996, the company submitted a five-year rate and restructuring plan (NYSEG*Plan*) in response to the PSC's Order dated May 20, 1996, in the Competitive Opportunities Proceeding. The company anticipates amending NYSEG*Plan* in the near future to provide for the formation of a holding company. If implemented with the anticipated amendments, NYSEG*Plan* would:

- Freeze the average retail price of electricity for five years, beginning August 1, 1997, and allow customers to increase their electricity use at up to half the present price.
- Allow the company to form a holding company and transfer designated fossil and hydropower generation assets to a generation company or companies within the holding company structure.
- Introduce wholesale competition on August 1, 1997, and phase in retail competition beginning August 1, 1998.
- Give investors a reasonable opportunity to fully recover past, prudently incurred costs.

In NYSEG*Plan,* the company emphasizes that lowering electric prices will take a combination of competition and a reduction of mandated costs, such as power purchases from nonutility generators (NUGs) and New York State's high taxes. Those mandated costs have resulted in excess payments to NUGs and taxes in New York State that are more than twice the national average. Such above-market costs will diminish the ability of New York State utilities to compete in the retail market with utilities in other states.

NYSEG*Plan* is contingent upon the receipt of electric price increases of 2.8% scheduled for August 1, 1996, and 2.7% a year later, as approved by the PSC in August 1995 under the company's three-year electric rate settlement agreement. The price increases are needed primarily to cover the rising cost of NUG power, higher taxes and past expenditures whose recovery has been delayed.

NYSEG*Plan* is also contingent upon the reasonable opportunity to fully recover prudently incurred investments, the outcome of the Energy Association lawsuit, FERC approval and implementation of a statewide Independent System Operator and Power Exchange, no restriction on investment and earnings by unregulated affiliates and final corporate and regulatory approvals. (See Energy Association Lawsuit and Rate Matters.)

Generation Business: The company plans to transfer designated generation assets to a generation company or companies. (See Electric Rate and Restructuring Plan.) The company has sharpened its focus on the evolving wholesale power market and is concentrating on maximizing short-term wholesale power sales and pursuing and negotiating creative medium- and long-term wholesale sales contracts to improve its competitive position.

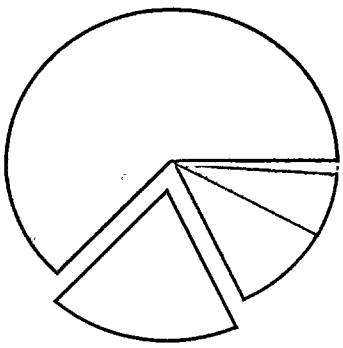
In July 1996 the company announced plans to remove three generating units from active service by mid-1997, if initiatives to improve the marketability of their output do not succeed. The three units, two at Jennison Generating Station and one at Hickling Generating Station, represent 116 megawatts (MW) of capacity and would be placed on long-term cold standby. Currently Goudey, Greenidge and Hickling generating stations each have one unit on long-term cold standby, representing a combined capacity of 133 MW. Certain of these units operated intermittently in 1996 when energy markets were favorable.

Petition to the FERC on NUGs: In February 1995 the company petitioned the FERC asking for relief from having to pay approximately $2 billion more than its avoided costs for power purchased over the lives of two NUG contracts. The FERC denied that petition in April 1995 and denied the company's subsequent request for a rehearing. The company believes that the overpayments under the two contracts violate the Public Utility Regulatory Policies Act of 1978.

In June 1995 the company filed a petition with the United States Court of Appeals for the District of Columbia to review the FERC's decision.

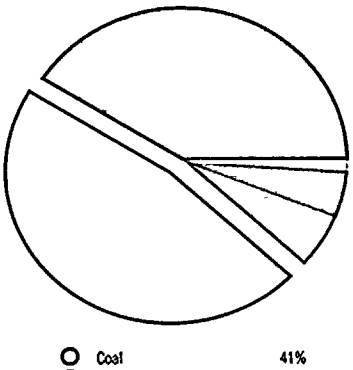
The company continues to seek cost-effective ways to terminate or renegotiate existing NUG contracts and thus reduce its overpayment burdens under such contracts.

1996 Sources of Electricity
Generation and Purchases – mwh



Coal	63%
NUG	19%
Power Authority & other	10%
Nuclear	7%
Hydro	1%

1996 Cost of Electricity
Production and Purchased Power



Coal	41%
NUG	47%
Power Authority & other	6%
Nuclear	5%
Hydro & other	1%

FERC Orders 888 and 889: In April 1996 the FERC issued Orders 888 and 889 adopting final rules to facilitate the development of competitive wholesale electric markets by opening up transmission services and to address the resulting stranded costs.

The FERC directed all public utilities to file a compliance open-access transmission tariff on or before July 9, 1996. Order 888 allows each utility to submit further modifications to its tariff, and allows customers to request modifications to the tariff. The company filed its compliance open-access transmission tariff and a modified open-access transmission tariff on July 9 and July 10, 1996, respectively. The company is required to operate under the July 9 compliance tariff until the July 10 modified tariff becomes effective.

The company's modified tariff has been accepted for filing and suspended for five months, to become effective on February 9, 1997, subject to refund and any further orders.

Under the compliance tariff, the company must offer transmission service to its wholesale customers on terms comparable to those it applies to itself, and it is also required to offer and/or provide certain ancillary services. The company's tariff and tariffs of other utilities could adversely affect the revenues received and payments made by the company in connection with its transmission and wholesale power transactions.

On December 30, 1996, the New York Power Pool (NYPP), of which the company is a member, submitted a compliance filing with the FERC in response to Order 888. This filing indicates the intention to restructure the NYPP using an Independent System Operator (ISO) structure, as endorsed by the FERC. On January 31, 1997, the NYPP submitted an additional restructuring filing, which includes proposals to establish an ISO, a Power Exchange and a New York State Reliability Council. The company is unable to predict the outcome of these filings and their ultimate effect on the company's financial position or results of operations.

Natural Gas Industry • During 1996 the company added nine natural gas franchises and gained approximately 5,000 natural gas customers in both new and existing franchise areas. The company plans to continue to increase its natural gas business through the expansion of natural gas service in existing franchise areas and an aggressive policy to acquire new franchises. The company completed two new large pipelines in December 1996. A 25-mile pipeline system was constructed, and natural gas began flowing to large industrial and public authority customers in the Plattsburgh area. A 10-mile pipeline was constructed, and natural gas began flowing to a large industrial customer in Cobleskill.

The natural gas business has experienced a number of regulatory changes, including FERC Order 636, which has been in effect for three years, and recent PSC opinions and orders.

PSC Opinions and Orders: The PSC issued an Opinion and Order in December 1994 (December Order) that set forth the policy framework to guide the transition of New York's gas distribution industry to a more competitive marketplace after the implementation of FERC Order 636. The PSC subsequently issued an Order on Reconsideration in August 1995 addressing petitions for rehearing or clarification of the December Order. In November 1995 the company and other utilities filed restructuring tariffs in compliance with the Order on Reconsideration.

Under the company's natural gas tariffs that were approved by PSC Order in March 1996 (March Order) with certain modifications, all of the company's customers — residential, small business and commercial, and industrial — may buy natural gas from other sources under a small customer aggregation program, with the company providing delivery service for a separate fee. The company has been offering unbundled transportation services for a decade. The March Order approving the company's tariffs is not expected to have a material effect on the company's natural gas operations. Consistent with the March Order, the company is implementing new services to compete more effectively for sales to larger, more sophisticated transportation customers as well as smaller customers.

Seneca Lake Natural Gas Storage Project: The company's Seneca Lake storage project was placed in service in December 1996. The project consists of a natural gas storage cavern, a compressor station and two natural gas transmission pipelines. The storage facility, located north of Watkins Glen on the west side of Seneca Lake, includes a depleted salt cavern that has a working capacity of 800 million cubic feet of natural gas.

The project's primary purposes are to ensure an adequate natural gas supply to customers and to support economic growth in southern and central New York. The project also allows the company to increase supply flexibility, retire two inefficient and expensive propane plants and reduce pipeline demand charges.

The company expects to expand the project in 1997, at an estimated cost of $10 million. The expansion will allow for growth in the company's wholesale natural gas business through the sale of storage capacity in interstate commerce. The company submitted a filing to the PSC in December 1996 for approval to expand the project, and submitted a filing to the FERC in January 1997 for approval to provide additional services related to the project expansion.

Economic and Business Climate • For the past few years the sluggish economy in New York State has limited the company's sales growth opportunities and increased the difficulty of retaining and expanding its industrial customer base. There are indications, however, that the state's economic and business climate is improving. When fully implemented, proposed tax cuts in combination with previously legislated tax cuts will reduce business and personal taxes by $5.7 billion a year, and more than 400 burdensome business regulations will have been eliminated or changed.

The company continues to focus on improving sales. The flexible rates the company has developed allow it to negotiate long-term contracts with eligible electric and natural gas customers. The contracts may cover existing or new load, or both.

ACCOUNTING ISSUES (See Note 1.)

The PSC's Competitive Opportunities Proceeding could affect the eligibility of the company to continue applying Statement 71. If the company could no longer meet the criteria of Statement 71 for all or a separable part of its business, the company may have to record as expense or revenue certain previously deferred items (regulatory assets and regulatory liabilities) and may have to record as a loss the amount for power purchase contracts with NUGs that is above the estimated price in a competitive marketplace. These items are currently recovered in rates.

At December 31, 1996 and 1995, the company had $604 million and $690 million, respectively, of regulatory assets, and $269 million and $294 million, respectively, of regulatory liabilities on its balance sheets. At December 31, 1996, the company also had power purchase contracts with NUGs that, on a present value basis, are $1.8 billion above the estimated price in a competitive marketplace. Although the company believes it will continue to meet the criteria of Statement 71 in the near future, it cannot predict what effect a competitive marketplace or future PSC actions will have on its ability to continue to do so.

The company has other costs currently being recovered in rates that may not be fully recoverable in a competitive marketplace, including operating costs for certain generating plants that may be above the market price for electricity. The inability to recover those above-market costs would have an adverse effect on the company's financial position and results of operations.

ENERGY SERVICES (See Note 10.)

The company has been making investments in energy services companies through its subsidiary, NGE Enterprises, Inc. (NGE). Those companies provide energy, financial and environmental services.

During 1996 NGE determined that EnerSoft Corporation (EnerSoft), a computer software and real-time information and trading systems company, no longer fit NGE's strategic focus. As a result, the company took a $10 million (14 cents per share) charge against earnings in 1996 to write down NGE's investment in EnerSoft, and exited that business in December 1996.

XENERGY, Inc. (XENERGY), acquired in June 1994, is an energy services, information systems and energy-consulting company serving utilities, governmental agencies and end-use energy consumers. XENERGY's revenues were slightly higher in 1996 than in 1995, and are expected to grow in 1997.

XENERGY has been successful in securing customers under pilot programs for retail electricity competition. In Massachusetts, XENERGY was chosen to supply 200 thousand megawatt-hours per year to the Massachusetts High Technology Council, a group of 13 companies participating in the pilot program. In New Hampshire, XENERGY has formed an alliance with Freedom Energy Company, L.L.C. to supply power to customers representing approximately 10% of the 50-megawatt load in the pilot program.

The company's investment as of December 31 and net loss for the year ended December 31 related to NGE are:

	1996	1995	1994
(Millions)			
Investment	$57	$54	$47
Net Loss*	$21	$12	$6

* Includes net loss from EnerSoft of $16 million, $7 million and $5 million in 1996, 1995 and 1994, respectively. EnerSoft's 1996 net loss includes $10 million related to NGE's decision to exit that business.

The company expects that NGE will continue to incur operating losses at least through 1997, but at a lower level due to the exit from EnerSoft.

RATE MATTERS

Electric Rate Settlement • The company's current three-year electric rate settlement agreement (electric agreement), approved by the PSC on August 1, 1995, is effective for the period August 1, 1995, through July 31, 1998. Effective August 1 each year, the electric agreement provides for:

	1995	1996	1997
Revenue increase (millions)	$45.1	$45.3	$45.5
Percent increase	2.9%	2.8%	2.7%
Allowed return on equity	11.1%	11.2%	11.2%

The rate increases for years two and three of the electric agreement are primarily to cover increases in the mandated purchases of power from NUGs, higher taxes and past expenditures whose recovery has been delayed to lessen previous rate increases.

NUG power purchases, including termination costs, totaled $320 million in 1996, and the company estimates that such purchases will total $338 million in 1997, $351 million in 1998 and $352 million in 1999. (See Note 8.)

At the time the electric agreement was approved by the PSC, the rate design for years two and three had yet to be determined. In May 1996 a PSC administrative law judge issued a Recommended Decision (RD) on the rate design for years two and three. In July 1996 the company submitted the draft rate design for year two to the PSC. This rate design was based on the RD and had an effective date of September 1, 1996.

The PSC issued an order in August 1996 that deferred the use of the year-two rates contained in the filing through December 30, 1996, unless otherwise ordered by the PSC. In September 1996 the company filed a petition for rehearing with the PSC requesting that the PSC vacate its August Order and place in effect a tariff containing a revenue allocation and rate design that would increase revenues $45.3 million during year two of the electric agreement. On December 18, 1996, the PSC issued an order that further deferred use of the year-two rates through June 30, 1997. On January 16, 1997, the PSC issued an order denying the petition for rehearing and stated that the petition should be considered in the context of NYSEG*Plan*. (See Electric Rate and Restructuring Plan.)

On December 23, 1996, the company filed a lawsuit in the New York State Supreme Court, Albany County. Among other things, the lawsuit asks for a judgment directing the PSC to immediately issue an order granting the company rates that include year-two rate increases.

The company is unable to predict the outcome of this matter and its ultimate effect on the company's financial position or results of operations.

Natural Gas Rate Settlement • The company's natural gas rate settlement agreement (gas agreement), which was authorized by the PSC in December 1995, freezes natural gas prices from December 15, 1995, until July 31, 1998. The natural gas rates approved in the gas agreement made permanent, until July 31, 1998, a 3.2% increase, less an adjustment of about $1 million. That increase became effective August 1, 1995, the final year of the gas portion of the previous three-year electric and natural gas rate settlement agreement.

An earnings sharing mechanism in the gas agreement provides that the average of the earned equity returns (exclusive of service quality awards or penalties) will be determined for the three years, and half of the three-year average of net earnings in excess of 14%, if any, will be shared with customers.

The gas agreement eliminated, effective August 1, 1995, the gas adjustment clause and the weather normalization clause, which were used to collect from, or refund to, customers amounts resulting from changes in the cost of purchased natural gas and the effect of unusually warm or cold weather on natural gas sales. The company uses risk management techniques such as natural gas futures and options to manage natural gas commodity prices and to fix margins on sales of natural gas.

ENVIRONMENTAL MATTERS (See Notes 8 and 9.)

The company continually assesses actions needed to comply with changing environmental laws and regulations. Any additional compliance programs will require changes in the company's operations and facilities and increase the cost of electric and natural gas service. Historically, rate recovery has been authorized for environmental compliance costs.

The Clean Air Act Amendments of 1990 (1990 Amendments) limit emissions of sulfur dioxide and nitrogen oxides and require emissions monitoring. The U.S. Environmental Protection Agency (EPA) allocates annual emissions allowances to each of the company's coal-fired generating stations based on statutory emissions limits. An emissions allowance represents an authorization to emit, during or after a specified calendar year, one ton of sulphur dioxide.

The company estimates that it will have allowances in excess of the affected coal-fired generating stations' actual emissions during Phase I, which began on January 1, 1995. The company's present strategy is to bank excess allowances for use in later years. It is estimated that the company will meet Phase II (begins January 1, 2000) emissions requirements through the year 2004, by using allowances banked during Phase I together with the company's Phase II annual emissions allowances. This strategy could be modified should market or business conditions change.

INVESTING AND FINANCING ACTIVITIES

Investing Activities • Capital expenditures for the company's electric and natural gas businesses, including nuclear fuel and the allowance for funds used during construction (AFDC), totaled $215 million in 1996, $164 million in 1995 and $248 million in 1994. Expenditures in those three years were primarily for the extension of service, necessary improvements to existing facilities and compliance with environmental requirements. In 1996 and 1995 capital expenditures were financed entirely with internally generated funds.

Capital expenditures projected for 1997, 1998 and 1999 are $141 million, $157 million and $128 million, respectively, and are expected to be financed entirely with internally generated funds. (See Note 8.)

Financing Activities • In September 1996 the company initiated a common stock repurchase program of not to exceed four million shares. As of December 31, 1996, the company had repurchased 1,832,500 shares at an average price of $21.90 per share. Common stock equity was reduced by $40 million as a result of the repurchase. The company plans to purchase shares from time to time as market and other conditions warrant.

The company's other financing activities during 1996, funded through the issuance of commercial paper, consisted of:

- The redemption, at a premium, of $100 million of 8.95% preferred stock.
- The redemption, at par, of $23 million of 9 7/8% Series first mortgage bonds, due February 1, 2020, pursuant to a sinking fund provision in the company's mortgage indenture.
- The redemption, at a premium, of the remaining $37 million of 8 5/8% Series first mortgage bonds due 2007.
- The purchase, at a discount, of $2.60 million of 4.15% preferred stock, $1.98 million of 4.40% preferred stock and $1.48 million of 4.15% (1954) preferred stock.

Since 1987 the company has reduced its debt from 62% to 45% of total capital (includes current maturities) and has raised its common stock equity from 33% to 51% of total capital at December 31, 1996.

The company reduced its embedded cost of long-term debt to 6.9% at the end of 1996, and has refinanced and/or redeemed more than $1.8 billion in long-term debt since the beginning of 1988. The embedded cost of preferred stock, which was reduced significantly due to the redemption of the 8.95% preferred stock, was 6% at December 31, 1996. Annual interest expense and preferred stock dividends have been reduced by nearly $80 million since the beginning of 1988.

The company uses short-term, unsecured notes, usually commercial paper, to finance certain refundings and for other corporate purposes. There was $129 million and $29 million of commercial paper outstanding at December 31, 1996 and 1995, respectively, at weighted average interest rates of 5.8% and 6.1%, respectively.

The company also has a revolving credit agreement with certain banks that provides for borrowing up to $200 million until December 31, 2001. There were no amounts outstanding under this agreement during 1996 or 1995.

RESULTS OF OPERATIONS

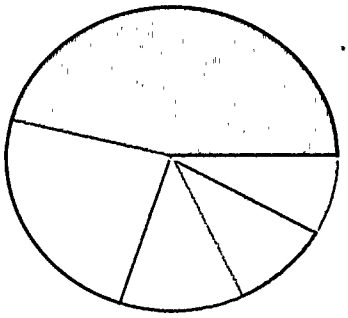
(Thousands, except per share amounts)	1996	1995	1994	1996 over 1995 Change	1995 over 1994 Change
Total Operating Revenues	**$2,059,371**	$2,009,541	$1,898,855	2%	6%
Operating Income	**$457,543**	$472,144	$438,575	(3%)	8%
Earnings Available for Common Stock	**$168,711**	$177,969	$168,698	(5%)	5%
Average Shares Outstanding	**71,127**	71,503	71,254	(1%)	–
Earnings Per Share	**$2.37**	$2.49	$2.37	(5%)	5%
Earnings Per Share Excluding Certain Charges	**$2.51**	$2.49	$2.49	1%	–
Dividends Per Share	**$1.40**	$1.40	$2.00	–	(30%)

EARNINGS PER SHARE

Earnings per share for 1996 were 12 cents lower than 1995 earnings per share. Without a charge of 14 cents per share to write down an investment in EnerSoft Corporation by NGE Enterprises, Inc., 1996 earnings per share would have been two cents higher than the prior year.

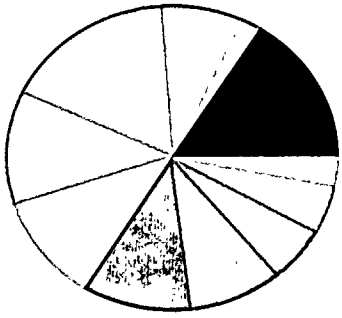
Higher electric and natural gas retail sales, mainly due to a combination of cold weather in the first quarter of 1996 and additional customers, added five cents per share to earnings. Lower interest charges in 1996 added nine cents per share to earnings and a reduction in preferred stock dividends, primarily due to the redemption of $100 million of 8.95% preferred stock, net of related interest expense on commercial paper, added 10 cents per share to earnings. Earnings per share were reduced 15 cents because of lower electric retail margins, primarily due to increases in mandated purchases of power from NUGs. (See Electric Rate Settlement.) Higher operating costs further decreased earnings six cents per share.

1996 Revenue Dollar
Where it came from



Residential	46¢
Commercial	24¢
Industrial	12¢
Street lighting & other	10¢
Other electric utilities	8¢

1996 Revenue Dollar
Where it went



Purchased electricity	
NUGs	16¢
Other	2¢
Purchased gas	8¢
Taxes	17¢
Other materials & services	12¢
Employee wages & benefits	11¢
Fuel	11¢
Depreciation & amortization	9¢
Interest to bondholders, etc.	6¢
Dividends – common stock	5¢
Retained in the business	3¢

Earnings per share in 1995 were 12 cents higher than in 1994. Excluding a charge for the 1993 production-cost penalty that lowered 1994 earnings by 12 cents per share, earnings per share were unchanged between 1995 and 1994.

Higher electric and natural gas prices added eight cents per share to 1995 earnings and higher profits on wholesale sales of electricity added five cents. The company's efforts to control operating costs increased 1995 earnings two cents per share. Lower interest charges in 1995, primarily due to the refinancing and retirement of debt, added six cents per share to earnings. Those increases were offset by an 11 cent per share decrease in other income and deductions, mostly because of higher losses incurred by NGE, and a nine cent charge to earnings per share for higher maintenance expenses, including storm-related costs.

INTEREST EXPENSE

Compared to the prior year, interest expense (before the reduction for allowance for borrowed funds used during construction) decreased $6 million and $9 million in 1996 and 1995, respectively. The decreases in both years were primarily the result of the refinancing and retirement of certain issues of long-term debt.

DIVIDENDS PER SHARE

The quarterly common stock dividend for 1996 was unchanged compared to 1995. Dividends per share for 1995 decreased 30% compared to the prior year because the board of directors reduced the quarterly common stock dividend from 55 cents per share to 35 cents per share in October 1994. Future dividend levels will depend on many factors, including the effect of industry restructuring on earnings.

OPERATING RESULTS FOR THE ELECTRIC BUSINESS SEGMENT

(Thousands)	1996	1995	1994	1996 over 1995 Change	1995 over 1994 Change
Retail Sales – Megawatt-Hours (mwh)	**13,216**	13,093	13,148	1%	–
Operating Revenues	**$1,723,147**	$1,708,297	$1,600,075	1%	7%
Operating Expenses	**$1,322,885**	$1,286,969	$1,202,328	3%	7%
Operating Income	**$400,262**	$421,328	$397,747	(5%)	6%

Electric retail sales increased in 1996 primarily because of cold weather in the first quarter of 1996 and additional customers.

The slight decrease in electric retail sales in 1995 resulted from the sluggish economy in the company's service territory. Although there were significant changes in weather during 1995 compared to 1994, the overall effect on sales was minimal.

Operating Revenues: The $15 million increase in electric operating revenues for 1996 was primarily due to higher retail sales, which added $14 million to revenues. An increase in wholesale sales of electricity added $12 million to revenues and changes in prices effective August 1995, net of the effect of eliminating the fuel adjustment clause, added $6 million to revenues. Those increases were partially offset by an increase in regulatory deferrals of $21 million.

Electric operating revenues for 1995 were $108 million higher than 1994 revenues. Revenues rose $87 million because of increases in electric prices, due to changes in rates effective August 1995 and 1994, primarily to accommodate increased mandated purchases of NUG power. An increase in wholesale sales of electricity added $9 million to 1995 revenues. Electric revenues for 1994 were reduced by $13 million because of the 1993 production-cost penalty that was recorded in the second quarter of 1994.

Operating Expenses: Electric operating expenses rose $36 million in 1996. Electricity purchases, mostly required purchases from NUGs, increased operating expenses $42 million. That increase was partially offset by an $8 million decrease in fuel used in electric generation.

The $85 million increase in electric operating expenses in 1995 is primarily attributable to an increase of $76 million in electricity purchased, mostly due to NUG purchases. Maintenance expenses, including storm-related costs, rose $10 million.

OPERATING RESULTS FOR THE NATURAL GAS BUSINESS SEGMENT

(Thousands)	1996	1995	1994	1996 over 1995 Change	1995 over 1994 Change
Deliveries – Dekatherms (dth)	61,542	58,535	58,624	5%	–
Operating Revenues	$336,224	$301,244	$298,780	12%	1%
Operating Expenses	$278,943	$250,428	$257,952	11%	(3%)
Operating Income	$57,281	$50,816	$40,828	13%	24%

Natural gas deliveries increased in 1996 due to a combination of cold weather in the first quarter of 1996 and additional customers.

Natural gas deliveries for 1995 were almost equal to 1994 deliveries. The sluggish economy in the company's service territory continued to affect sales, which were below expectations. There were significant changes in weather during 1995 compared to 1994, but the overall effect on 1995 sales was minimal.

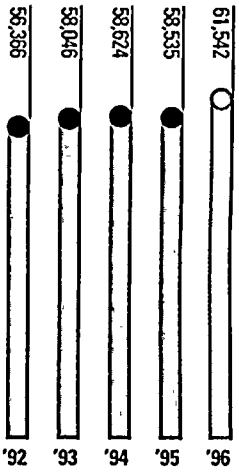
Operating Revenues: Natural gas operating revenues for 1996 increased $35 million over 1995 revenues. A change in rate structure effective December 1995 and changes in rates effective August 1995 added $20 million to revenues. Higher retail sales added $9 million to revenues and an increase in transportation of customer-owned gas added $4 million to revenues for the year.

In 1995 natural gas operating revenues increased $2 million, primarily as a result of higher natural gas prices that added $3 million to revenues. Changes in rates effective in August 1995 and 1994 were the primary reason for the higher natural gas prices.

Operating Expenses: Comparing 1996 to 1995, natural gas operating expenses rose $29 million. An increase in natural gas purchased, due to higher commodity costs and higher deliveries, added $23 million and an increase in certain operating costs added $5 million to expenses.

The $8 million reduction in natural gas operating expenses in 1995 was due to a combination of factors. Natural gas purchased decreased $12 million mainly because of lower commodity prices. That decrease was partially offset by higher depreciation and distribution operation expenses that each added $1 million to operating expenses.

Natural Gas Dekatherm Deliveries (Thousands)



Consolidated Statements of Income

Year Ended December 31	1996	1995	1994
(Thousands, except per share amounts)			
Operating Revenues			
Electric	$1,723,147	$1,708,297	$1,600,075
Natural gas	336,224	301,244	298,780
Total Operating Revenues	2,059,371	2,009,541	1,898,855
Operating Expenses			
Fuel used in electric generation	222,102	229,759	231,648
Electricity purchased	360,753	318,440	242,352
Natural gas purchased	172,705	149,789	161,627
Other operating expenses	342,455	326,922	328,961
Maintenance	107,697	116,807	106,637
Depreciation and amortization	189,401	184,770	178,326
Other taxes	206,715	210,910	210,729
Total Operating Expenses	1,601,828	1,537,397	1,460,280
Operating Income	457,543	472,144	438,575
Interest Charges, Net	122,729	129,567	136,092
Other Income and Deductions	48,630	30,023	12,377
Income Before Federal Income Taxes	286,184	312,554	290,106
Federal Income Taxes	107,943	115,864	102,461
Net Income	178,241	196,690	187,645
Preferred Stock Dividends	9,530	18,721	18,947
Earnings Available for Common Stock	$168,711	$177,969	$168,698
Earnings Per Share	$2.37	$2.49	$2.37
Average Shares Outstanding	71,127	71,503	71,254

The notes on pages 26 through 38 are an integral part of the financial statements.

Consolidated Balance Sheets

December 31	1996	1995
(Thousands)		
Assets		
Current Assets		
Cash and cash equivalents	$8,253	$11,433
Special deposits	31,364	5,785
Accounts receivable, net	189,043	195,834
Fuel, at average cost	36,472	33,682
Materials and supplies, at average cost	43,044	44,809
Prepayments	47,169	31,371
Accumulated deferred federal income tax benefits, net	3,424	7,594
Total Current Assets	358,769	330,508
Utility Plant, at Original Cost		
Electric	5,177,365	5,090,044
Natural gas	529,023	445,256
Common	151,290	140,686
	5,857,678	5,675,986
Less accumulated depreciation	1,933,599	1,791,625
Net Utility Plant in Service	3,924,079	3,884,361
Construction work in progress	58,285	79,229
Total Utility Plant	3,982,364	3,963,590
Other Property and Investments, Net	99,221	99,633
Regulatory and Other Assets		
Regulatory assets		
Unfunded future federal income taxes	269,767	323,446
Unamortized debt expense	80,745	85,023
Demand-side management program costs	71,425	74,824
Other regulatory assets	181,661	206,736
Total regulatory assets	603,598	690,029
Other assets	15,729	30,571
Total Regulatory and Other Assets	619,327	720,600
Total Assets	$5,059,681	$5,114,331

The notes on pages 26 through 38 are an integral part of the financial statements.

Consolidated Statements of Cash Flows

Year Ended December 31	1996	1995	1994
(Thousands)			
Operating Activities			
Net income	$178,241	$196,690	$187,645
Adjustments to reconcile net income to net cash provided by operating activities			
Depreciation and amortization	189,401	184,770	178,326
Deferred fuel and purchased gas	1,066	15,022	(1,944)
Federal income taxes and investment tax credits deferred, net	28,928	52,362	37,910
Changes in current operating assets and liabilities			
Accounts receivable	6,791	(40,169)	25,921
Inventory	(1,025)	19,286	5,924
Accounts payable and accrued liabilities	3,486	10,281	(4,125)
Other, net	52,144	13,589	20,721
Net Cash Provided by Operating Activities	459,032	451,831	450,378
Investing Activities			
Utility plant capital expenditures	(214,373)	(163,401)	(246,536)
Proceeds from governmental and other sources	2,977	5,621	23,915
Expenditures for other property and investments	(916)	(3,145)	(34,482)
Funds restricted for capital expenditures	–	1,324	41,113
Net Cash Used in Investing Activities	(212,312)	(159,601)	(215,990)
Financing Activities			
Issuance of pollution control notes and first mortgage bonds	–	37,000	275,000
(Repurchase) sale of common stock	(40,198)	–	23,386
Revolving credit agreement, net	–	–	(50,000)
Repayments of preferred stock, first mortgage bonds and pollution control notes, including net premiums	(171,478)	(92,395)	(497,450)
Changes in funds set aside for first mortgage bond and preferred stock repayments	(25,000)	–	95,000
Long-term notes, net	(2,581)	(5,504)	(2,290)
Commercial paper, net	100,680	(123,280)	101,700
Dividends on common and preferred stock	(111,323)	(118,940)	(161,676)
Net Cash Used in Financing Activities	(249,900)	(303,119)	(216,330)
Net (Decrease) Increase in Cash and Cash Equivalents	(3,180)	(10,889)	18,058
Cash and Cash Equivalents, Beginning of Year	11,433	22,322	4,264
Cash and Cash Equivalents, End of Year	$8,253	$11,433	$22,322

The notes on pages 26 through 38 are an integral part of the financial statements.

Consolidated Balance Sheets

December 31	1996	1995
(Thousands)		
Liabilities		
Current Liabilities		
Current portion of long-term debt	$83,488	$37,003
Commercial paper	129,300	28,620
Accounts payable and accrued liabilities	121,123	117,637
Interest accrued	22,195	24,093
Taxes accrued	–	22,231
Other	71,324	68,027
Total Current Liabilities	427,430	297,611
Regulatory and Other Liabilities		
Regulatory liabilities		
Deferred income taxes - unfunded future federal income taxes	109,065	128,643
Deferred income taxes	94,004	108,605
Other liabilities	65,471	56,729
Total regulatory liabilities	268,540	293,977
Other liabilities		
Deferred income taxes	751,553	743,484
Other postretirement benefits	95,195	75,683
Liability for environmental restoration	32,100	31,800
Other	74,627	81,288
Total other liabilities	953,475	932,255
Long-term debt	1,480,814	1,581,448
Total Liabilities	3,130,259	3,105,291
Commitments	–	–
Preferred Stock Redeemable Solely at the Option of the Company	134,440	140,500
Preferred Stock Subject to Mandatory Redemption Requirements	25,000	125,000
Common Stock Equity		
Common stock ($6.66 2/3 par value, 90,000,000 shares authorized and 69,670,327 and 71,502,827 shares issued and outstanding at December 31, 1996 and 1995, respectively)	464,469	476,686
Capital in excess of par value	816,384	842,442
Retained earnings	489,129	424,412
Total Common Stock Equity	1,769,982	1,743,540
Total Liabilities and Stockholders' Equity	$5,059,681	$5,114,331

The notes on pages 26 through 38 are an integral part of the financial statements.

Consolidated Statements of Changes in Common Stock Equity

(Thousands, except shares and per share amounts)

	Common Stock $6.66 2/3 Par Value Shares	Amount	Capital in Excess of Par Value	Retained Earnings	Total
Balance, January 1, 1994	70,595,985	$470,640	$824,943	$320,114	$1,615,697
Net income				187,645	187,645
Cash dividends declared					
Preferred stock (at serial rates)					
Redeemable - optional				(8,419)	(8,419)
- mandatory				(10,528)	(10,528)
Common stock ($2.00 per share)				(142,265)	(142,265)
Issuance of stock					
Dividend reinvestment and stock purchase plan	906,842	6,046	17,450		23,496
Amortization of capital stock issue expense			(769)		(769)
Balance, December 31, 1994	71,502,827	476,686	841,624	346,547	1,664,857
Net income				196,690	196,690
Cash dividends declared					
Preferred stock (at serial rates)					
Redeemable - optional				(8,196)	(8,196)
- mandatory				(10,525)	(10,525)
Common stock ($1.40 per share)				(100,104)	(100,104)
Amortization of capital stock issue expense			818		818
Balance, December 31, 1995	71,502,827	476,686	842,442	424,412	1,743,540
Net income				178,241	178,241
Cash dividends declared					
Preferred stock (at serial rates)					
Redeemable - optional				(7,955)	(7,955)
- mandatory				(1,575)	(1,575)
Common stock ($1.40 per share)				(99,611)	(99,611)
Common stock repurchase	(1,832,500)	(12,217)	(27,981)		(40,198)
Premium paid on preferred stock redemption, net				(4,383)	(4,383)
Amortization of capital stock issue expense			1,923		1,923
Balance, December 31, 1996	69,670,327	$464,469	$816,384	$489,129	$1,769,982

The notes on pages 26 through 38 are an integral part of the financial statements.

1 SIGNIFICANT ACCOUNTING POLICIES

Principles of consolidation • The consolidated financial statements include the company's subsidiaries, Somerset Railroad Corporation (SRC) and NGE Enterprises, Inc. (NGE).

Utility plant • The cost of repairs and minor replacements is charged to the appropriate operating expense accounts. The cost of renewals and betterments, including indirect costs, is capitalized. The original cost of utility plant retired or otherwise disposed of and the cost of removal less salvage are charged to accumulated depreciation.

Depreciation and amortization • Depreciation expense is determined using straight-line rates, based on the average service lives of groups of depreciable property in service. Depreciation accruals were equivalent to 3.5% of average depreciable property for 1996, 1995 and 1994. Amortization expense includes the amortization of certain regulatory assets authorized by the Public Service Commission of the State of New York (PSC).

Accounts receivable • The company has an agreement that expires in November 2000 to sell, with limited recourse, undivided percentage interests in certain of its accounts receivable from customers. The agreement allows the company to receive up to $152 million from the sale of such interests. At December 31, 1996 and 1995, accounts receivable on the consolidated balance sheets are shown net of $152 million of interests in accounts receivable sold. All fees associated with the program are included in other income and deductions on the consolidated statements of income and amounted to approximately $9 million, $10 million and $7 million in 1996, 1995 and 1994, respectively. Accounts receivable on the consolidated balance sheets are also shown net of an allowance for doubtful accounts of $7 million at December 31, 1996 and 1995. Bad debt expense was $19 million, $18 million and $20 million in 1996, 1995 and 1994, respectively.

In June 1996 the Financial Accounting Standards Board issued Statement of Financial Accounting Standards No. 125 (Statement 125), Accounting for the Transfer and Servicing of Financial Assets and Extinguishment of Liabilities, effective for transactions occurring after December 31, 1996. The company's accounting complies with the provisions of Statement 125.

Income taxes • The company files a consolidated federal income tax return with SRC and NGE. Deferred income taxes are provided on all temporary differences between financial statement basis and taxable income in accordance with Statement of Financial Accounting Standards No. 109 (Statement 109), Accounting for Income Taxes. Investment tax credits, which reduce federal income taxes currently payable, were deferred and are being amortized over the estimated lives of the applicable property.

Regulatory assets and liabilities • Pursuant to Statement of Financial Accounting Standards No. 71 (Statement 71), Accounting for the Effects of Certain Types of Regulation, the company capitalizes, as regulatory assets, incurred costs that are probable of recovery in future electric and natural gas rates. In accordance with the company's current electric and natural gas rate settlement agreements, the company is no longer deferring certain costs that were previously subject to deferral accounting, such as fuel and natural gas purchased. The company also records as regulatory liabilities, obligations to customers to refund previously collected revenue or to spend revenue collected from customers on future costs.

The company's regulatory assets and liabilities consisted of the following:

December 31	1996	1996	1995	1995
	Assets	Liabilities	Assets	Liabilities
(Thousands)				
Unfunded future federal income taxes	$269,767	–	$323,446	–
Deferred income taxes– unfunded future federal income taxes	–	$109,065	–	$128,643
Deferred income taxes	–	94,004	–	108,605
Unamortized debt expense	80,745	–	85,023	–
Demand-side management (DSM) program costs	71,425	–	74,824	–
Nonutility generator (NUG) termination agreements	43,991	–	43,847	–
Environmental remediation costs	32,100	–	31,763	–
Other postretirement benefits	18,417	–	21,179	–
Other	87,153	65,471	109,947	56,729
Total	$603,598	$268,540	$690,029	$293,977

Unfunded future federal income taxes and deferred income taxes are amortized as the related temporary differences reverse. Unamortized debt expense is amortized over the lives of the related debt issues. DSM program costs, other regulatory assets and other regulatory liabilities are amortized over various periods in accordance with the company's rate settlement agreements. The company is earning a return on all regulatory assets for which the company has spent funds.

If the company could no longer meet the criteria of Statement 71 for all or a separable part of its business, the company may have to record as expense or revenue all or a portion of its regulatory assets and liabilities and may have to record as a loss the amount for power purchase contracts with NUGs that is above the estimated price in a competitive marketplace.

Consolidated Statements of Cash Flows • The company considers all highly liquid investments with a maturity or put date of three months or less when acquired to be cash equivalents. Those investments are included in cash and cash equivalents on the consolidated balance sheets.

Total income taxes paid were $98 million, $55 million and $69 million for the years ended December 31, 1996, 1995 and 1994, respectively.

Interest paid, net of amounts capitalized, was $112 million, $118 million and $132 million for the years ended December 31, 1996, 1995 and 1994, respectively.

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

Reclassifications • Certain amounts have been reclassified on the consolidated financial statements to conform with the 1996 presentation.

2 INCOME TAXES

Year ended December 31	1996	1995	1994
(Thousands)			
Charged to operations			
Current	$79,015	$63,502	$64,551
Deferred, net			
Accelerated depreciation	52,572	55,493	57,564
Revenue decoupling mechanism	(2,153)	(4,608)	6,870
Alternative minimum tax (AMT) credit	310	18,009	6,076
Demand-side management	(1,267)	21	(9,048)
Miscellaneous	(14,197)	(10,339)	(17,514)
Investment tax credit (ITC)	(6,337)	(6,214)	(6,038)
Total	$107,943	$115,864	$102,461

The company's effective tax rate differed from the statutory rate of 35% due to the following:

Year ended December 31	1996	1995	1994
(Thousands)			
Tax expense at statutory rate	$100,165	$109,396	$101,537
Depreciation not normalized	20,542	19,774	18,552
ITC amortization	(6,337)	(6,214)	(6,038)
Research & Development credit	83	(5,547)	(1,352)
Cost of removal	(2,825)	(3,772)	(5,462)
Other, net	(3,685)	2,227	(4,776)
Total	$107,943	$115,864	$102,461

The company's deferred tax assets and liabilities consisted of the following:

December 31	1996	1995
(Thousands)		
Current Deferred Tax Assets	$3,424	$7,594
Noncurrent Deferred Taxes		
Depreciation	$761,794	$727,630
Unfunded future federal income taxes	109,065	128,643
Accumulated deferred ITC	119,696	126,032
Future income tax benefit – ITC	(41,847)	(44,488)
Other	4,529	40,063
Total Noncurrent Deferred Tax Liabilities	953,237	977,880
Valuation Allowance	1,385	2,852
Less amounts classified as regulatory liabilities		
Deferred income taxes – unfunded future federal income taxes	109,065	128,643
Deferred income taxes	94,004	108,605
Noncurrent Deferred Income Taxes	$751,553	$743,484

3 LONG-TERM DEBT

At December 31, 1996 and 1995, long-term debt was:

	Maturity Dates	Interest Rates	Amount 1996	Amount 1995
(Thousands)				
First mortgage bonds (1)	1997 to 2023	5 5/8% to 9 7/8%	$903,000	$963,000
Pollution control notes (2)	2006 to 2034	3.30% to 6.15%	613,000	613,000
Long-term notes	12/31/99		29,900	31,000
Various long-term notes			15,809	5,501
Obligations under capital leases			10,699	14,799
Unamortized premium and discount on debt, net			(8,106)	(8,849)
			1,564,302	1,618,451
Less debt due within one year – included in current liabilities			83,488	37,003
Total			$1,480,814	$1,581,448

At December 31, 1996, long-term debt and capital lease payments that will become due during the next five years are:

1997	1998	1999	2000	2001
(Thousands)				
$83,488	$35,634	$33,906	$1,899	$51,641

(1) The company's first mortgage bond indenture constitutes a direct first mortgage lien on substantially all utility plant. The mortgage also provides for a sinking and improvement fund. This provision requires the company to make an annual cash deposit with the Trustee equivalent to 1% of the principal amount of all bonds delivered and authenticated by the Trustee prior to January 1 of that year (excluding any bonds issued on the basis of the retirement of bonds). The company satisfied the requirement by depositing $23 million in cash in 1996 and 1997. The funds were used to redeem, at par, $23 million of 9 7/8% Series first mortgage bonds, due February 2020, in both February 1996 and February 1997.

(2) Fixed-rate pollution control notes totaling $306 million were issued to secure the same amount of tax-exempt pollution control revenue bonds issued by a governmental authority. The interest rates range from 5.70% to 6.15%.

Adjustable-rate pollution control notes totaling $132 million were issued to secure the same amount of tax-exempt adjustable-rate pollution control revenue bonds (Adjustable-rate Revenue Bonds) issued by a governmental authority. The Adjustable-rate Revenue Bonds bear interest at rates ranging from 3.30% to 3.85% through dates preceding various annual interest rate adjustment dates. On the annual interest rate adjustment dates the interest rates will be adjusted, or at the option of the company, subject to certain conditions, a fixed rate of interest may become effective. Bond owners may elect, subject to certain conditions, to have their Adjustable-rate Revenue Bonds purchased by the Trustee.

Multi-mode pollution control notes totaling $175 million were issued to secure the same amount of tax-exempt multi-mode pollution control refunding revenue bonds (Multi-mode Revenue Bonds) issued by a governmental authority. The Multi-mode Revenue Bonds have a structure that allows the interest rates to be based on a daily rate, a weekly rate, a commercial paper rate, an auction rate, a term rate or a fixed rate. Bond owners may elect, while the Multi-mode Revenue Bonds bear interest at a daily or weekly rate, to have their bonds purchased by the Registrar and Paying Agent. The maturity dates of the Multi-mode Revenue Bonds are February 1, 2029, June 1, 2029, and October 1, 2029, and can be extended subject to certain conditions. At December 31, 1996, the multi-mode pollution control notes bore interest at the daily rate. The weighted average interest rate for all three series was 3.2%, excluding letter of credit fees, for the year ended December 31, 1996.

The company has irrevocable letters of credit that support certain payments required to be made on the Adjustable-rate Revenue Bonds and Multi-mode Revenue Bonds, and that expire on various letter of credit expiration dates. If the company is unable to extend the letter of credit that is related to a particular series of Adjustable-rate Revenue Bonds, that series will have to be redeemed unless a fixed rate of interest becomes effective. Multi-mode Revenue Bonds are subject to mandatory purchase upon any change in the interest rate mode and in certain other circumstances. Payments made under the letters of credit in connection with purchases of Adjustable-rate Revenue Bonds and Multi-mode Revenue Bonds are repaid with the proceeds from the remarketing of those Bonds. To the extent the proceeds are not sufficient, the company is required to reimburse the bank that issued the letter of credit.

4 PREFERRED STOCK

At December 31, 1996 and 1995, serial cumulative preferred stock was:

Series	Par Value Per Share	Redeemable Prior to	Redeemable Per Share	Shares Authorized and Outstanding (1)	Amount 1996	Amount 1995
(Thousands)						
Redeemable solely at the option of the company:						
3.75%	$100		$104.00	150,000	$15,000	$15,000
4 1/2% (1949)	100		103.75	40,000	4,000	4,000
4.15% (2)	100		101.00	14,000	1,400	4,000
4.40% (2)	100		102.00	55,200	5,520	7,500
4.15% (1954) (2)	100		102.00	35,200	3,520	5,000
6.48%	100		102.00	300,000	30,000	30,000
7.40% (3)	25	12/1/98	26.85	1,000,000	25,000	25,000
		Thereafter	25.00			
Adjustable Rate (4)	25	12/1/98	27.50	2,000,000	50,000	50,000
		Thereafter	25.00			
Total					$134,440	$140,500
Subject to mandatory redemption requirements:						
6.30% (5)	100	1/1/98	103.78	250,000	$25,000	$25,000
8.95% (6)	25			–	–	100,000
Total					$25,000	$125,000

At December 31, 1996, there were no preferred stock redemptions or annual redeemable preferred stock sinking fund requirements for the next five years.

(1) At December 31, 1996, there were 1,610,600 shares of $100 par value preferred stock, 7,800,000 shares of $25 par value preferred stock and 1,000,000 shares of $100 par value preference stock authorized but unissued.

(2) In 1996 the company purchased the following, at a discount, through the issuance of commercial paper: $2.60 million of 4.15% preferred stock, $1.98 million of 4.40% preferred stock and $1.48 million of 4.15% (1954) preferred stock.

(3) The company is restricted in its ability to redeem this Series prior to December 1, 1998.

(4) The payment on this Series, for April 1, 1997, is at an annual rate of 5.40% and subsequent payments can vary from an annual rate of 4% to 10%, based on a formula included in the company's Certificate of Incorporation. The company is restricted in its ability to redeem this Series prior to December 1, 1998.

(5) On January 1 in each year 2004 through 2008, the company must redeem 12,500 shares at par, and on January 1, 2009, the company must redeem the balance of the shares at par. This Series is redeemable at the option of the company at $103.78 per share prior to January 1, 1998. The $103.78 price will be reduced annually by 63 cents for the years ending 1998 through 2002; thereafter, the redemption price is $100.00. The company is restricted in its ability to redeem this Series prior to January 1, 2004.

(6) Redeemed January 1, 1996.

Dividend Limitations: After dividends on all outstanding preferred stock have been paid, or declared, and funds set apart for their payment, the common stock is entitled to cash dividends as may be declared by the board of directors out of retained earnings accumulated since December 31, 1946. Common stock dividends are limited if common stock equity (52% at December 31, 1996) falls below 25% of total capitalization, as defined in the company's Certificate of Incorporation. Dividends on common stock cannot be paid unless sinking fund requirements of the preferred stock are met. The company has not been restricted in the payment of dividends on common stock by these provisions. Retained earnings accumulated since December 31, 1946, were approximately $489 million and $424 million as of December 31, 1996 and 1995, respectively.

5 BANK LOANS AND OTHER BORROWINGS

The company has a revolving credit agreement with certain banks that provides for borrowing up to $200 million to December 31, 2001. At the option of the company, the interest rate on borrowings is related to the prime rate, the London Interbank Offered Rate or the interest rate applicable to certain certificates of deposit. The agreement also provides for the payment of a commitment fee that can fluctuate from .10% to .25% depending on the credit ratings of the company's first mortgage bonds. The commitment fee was .125% at December 31, 1996 and 1995, and .1875% at December 31, 1994.

The revolving credit agreement does not require compensating balances. The company had no outstanding loans under the revolving credit agreement at December 31, 1996 or 1995.

The company uses short-term unsecured notes, usually commercial paper, to finance certain refundings and for other corporate purposes. The weighted average interest rates on commercial paper balances at December 31, 1996, 1995 and 1994 were 5.8%, 6.1% and 5.8%, respectively.

6 RETIREMENT BENEFITS

Pensions • The company has a noncontributory retirement annuity plan that covers substantially all employees. Benefits are based principally on the employee's length of service and compensation for the five highest paid consecutive years during the last 10 years of service. It is the company's policy to fund pension costs accrued each year to the extent deductible for federal income tax purposes.

Net pension benefit included the following components:

Year ended December 31	1996	1995	1994
(Thousands)			
Service cost: Benefits earned during the year	$18,593	$16,391	$17,637
Interest cost on projected benefit obligation	46,070	45,400	43,328
Actual return on plan assets	(138,957)	(185,816)	(17,409)
Net amortization and deferral	58,162	111,209	(48,824)
Net pension (benefit)	$(16,132)	$(12,816)	$(5,268)

The funded status of the plan was:

December 31	1996	1995
(Thousands)		
Actuarial present value of accumulated benefit obligation		
Vested	$472,786	$450,857
Nonvested	52,272	53,837
Total	$525,058	$504,694
Fair value of plan assets	$(995,795)	$(888,190)
Actuarial present value of projected benefit obligation (PBO)	679,778	661,138
Plan assets in excess of PBO	(316,017)	(227,052)
Unrecognized net transition asset	51,898	59,136
Unrecognized net gain	275,531	178,927
Unrecognized prior service cost	(26,464)	(9,931)
Net pension (asset) liability	$(15,052)	$1,080
Assumptions used to determine actuarial valuations		
Discount rate used to determine PBO	7.25%	7.0%
Rate of compensation increase used to determine PBO	4.75%	4.75%
Long-term rate of return on plan assets for net pension benefit	8.0%	8.0%

Plan assets primarily consist of domestic and international equity securities; U.S. agency, corporate and Treasury bonds; and cash equivalents.

Postretirement benefits other than pensions • The company has postretirement benefit plans, such as a comprehensive health insurance plan and a prescription drug plan, that provide certain benefits for retired employees and their dependents. Substantially all of the company's employees who retire under the company's pension plan may become eligible for those benefits at retirement. The postretirement benefit plans were unfunded as of December 31, 1996 and 1995.

The net periodic postretirement benefits cost other than pensions recognized on the income statements for 1996, 1995 and 1994 (below) represent the portion of costs related to Statement of Financial Accounting Standards No. 106 (Statement 106), Employers' Accounting for Postretirement Benefits Other Than Pensions, that the company has been allowed to collect from its customers. The company has deferred $18 million and $21 million of Statement 106 costs as of December 31, 1996 and 1995, respectively. The company expects to recover any deferred Statement 106 amounts by the year 2000.

Net postretirement benefits cost other than pensions included the following components:

Year ended December 31	1996	1995	1994
(Thousands)			
Service cost: Benefits accumulated during the year	$6,436	$5,412	$7,050
Interest cost on accumulated postretirement benefit obligation	15,795	15,228	15,903
Amortization of transition obligation over 20 years	10,330	10,330	10,330
Amortization of (gain) loss	(3,246)	(4,575)	2
Deferral for future recovery	(8,950)	(7,742)	(18,757)
Net periodic postretirement benefits cost	$20,365	$18,653	$14,528

The status of the plans for postretirement benefits other than pensions, as reflected in the company's consolidated balance sheets, was as follows:

December 31	1996	1995
(Thousands)		
Accumulated postretirement benefit obligation (APBO)		
Retired employees	$103,912	$114,383
Fully eligible active plan participants	15,259	15,214
Other active plan employees	107,022	106,689
Total APBO	226,193	236,286
Less unrecognized transition obligation	165,278	175,608
Less unrecognized net gain	(34,280)	(15,005)
Accrued postretirement liability	$95,195	$75,683

A 9% annual rate of increase in the per capita costs of covered health care benefits was assumed for 1997, gradually decreasing to 5% by the year 2003. Increasing the assumed health care cost trend rates by 1% in each year would increase the APBO as of January 1, 1997, by $39 million and increase the aggregate of the service cost and interest cost components of the net postretirement benefits cost for 1996 by $5 million. Discount rates of 7.25% and 7% were used to determine the APBO in 1996 and 1995, respectively.

7 JOINTLY-OWNED GENERATING STATIONS

Nine Mile Point Unit 2 • The company has an undivided 18% interest in the output and costs of the Nine Mile Point nuclear generating unit No. 2 (NMP2), which is operated by Niagara Mohawk Power Corporation (Niagara Mohawk). Ownership of NMP2 is shared with Niagara Mohawk 41%, Long Island Lighting Company 18%, Rochester Gas and Electric Corporation 14% and Central Hudson Gas & Electric Corporation 9%. The company's share of the rated capability is 206 megawatts. The company's share of net utility plant investment, excluding nuclear fuel, was approximately $610 million and $625 million, at December 31, 1996 and 1995, respectively. The accumulated provision for depreciation was approximately $144 million and $129 million, at December 31, 1996 and 1995, respectively. The company's share of operating expenses is included in the consolidated statements of income.

Nuclear insurance • Niagara Mohawk maintains public liability and property insurance for NMP2. The company reimburses Niagara Mohawk for its 18% share of those costs.

The public liability limit for a nuclear incident is approximately $8.3 billion. Should losses stemming from a nuclear incident exceed the commercially available public liability insurance, each licensee of a nuclear facility would be liable for up to $76 million per incident, payable at a rate not to exceed $10 million per year. The company's maximum liability for its 18% interest in NMP2 would be approximately $14 million per incident. The $76 million assessment is subject to periodic inflation indexing and a 5% surcharge should funds prove insufficient to pay claims associated with a nuclear incident. The Price-Anderson Act also requires indemnification for precautionary evacuations whether or not a nuclear incident actually occurs.

Niagara Mohawk has procured property insurance for NMP2 aggregating approximately $2.8 billion through the Nuclear Insurance Pools and the Nuclear Electric Insurance Limited (NEIL). In addition, the company has purchased NEIL insurance coverage for the extra expense that would be incurred by purchasing replacement power during prolonged accidental outages. Under NEIL programs, should losses resulting from an incident at a member facility exceed the accumulated reserves of NEIL, each member, including the company, would be liable for its share of the deficiency. The company's maximum liability per incident under the property damage and replacement power coverages is approximately $3 million.

Nuclear plant decommissioning costs • Based on the results of a 1995 decommissioning study, the company's 18% share of the cost to decommission NMP2 is $150 million in 1997 dollars ($422 million in 2026 when NMP2's operating license will expire). The estimated annual contribution needed to cover the company's share of costs as outlined in the study is approximately $4 million.

The company's estimated liability for decommissioning NMP2 using the Nuclear Regulatory Commission's (NRC) minimum funding requirement is approximately $82 million in 1997 dollars. The company's electric rates currently include an annual allowance for decommissioning of $2 million, which approximates the NRC's minimum funding requirement. Decommissioning costs are charged to depreciation and amortization expense and are recovered over the expected life of the plant. In its five-year electric rate and restructuring plan submitted in the PSC's Competitive Opportunities Proceeding, the company used the 1995 decommissioning study as a basis for increasing the amount proposed to be recovered in rates for decommissioning. The company believes that any increase in decommissioning costs will ultimately be recovered in rates.

The company has established a Qualified Fund under applicable provisions of the federal tax law and to comply with NRC funding regulations. The balance in the fund, including reinvested earnings, was approximately $11 million and $9 million at December 31, 1996 and 1995, respectively. Those amounts are included on the consolidated balance sheets in other property and investments, net. The related liability for decommissioning is included in other liabilities - other. At December 31, 1996, the external trust fund investments were classified as available-for-sale, and their carrying value approximated fair value.

In early 1996 the Financial Accounting Standards Board issued an exposure draft, Accounting for Certain Liabilities Related to Closure and Removal of Long-Lived Assets. The exposure draft proposes that companies recognize the present value of estimated decommissioning costs. If the final statement includes that requirement, the estimated liability the company would have to recognize on its balance sheet related to decommissioning NMP2 is approximately $61 million, based on the 1995 decommissioning study.

Homer City • The company has an undivided 50% interest in the output and costs of the Homer City Generating Station, which comprises three generating units. The station is owned with Pennsylvania Electric Company and is operated by its affiliate, GPU Generation, Inc. The company's share of the rated capability is 959 megawatts, and its net utility plant investment was approximately $269 million and $276 million at December 31, 1996 and 1995, respectively. The accumulated provision for depreciation was approximately $181 million and $168 million, at December 31, 1996 and 1995, respectively. The company's share of operating expenses is included in the consolidated statements of income.

8 COMMITMENTS

Capital expenditures • The company has substantial commitments in connection with its capital expenditure program and estimates that expenditures for 1997, 1998 and 1999 will approximate $141 million, $157 million and $128 million, respectively, and are expected to be financed entirely with internally generated funds. The program is subject to periodic review and revision. Actual capital expenditures may change to reflect additional regulatory requirements and the company's continued focus on minimizing capital expenditures. Capital expenditures will be primarily for the extension of service, necessary improvements to existing facilities and compliance with environmental requirements.

Nonutility generator power purchase contracts • During 1996, 1995 and 1994 the company expensed approximately $320 million, $284 million and $214 million, respectively, for NUG power, including termination costs. The company estimates that NUG power purchases, including termination costs, will total $338 million in 1997, $351 million in 1998 and $352 million in 1999.

9 ENVIRONMENTAL LIABILITY

The company has been notified by the U. S. Environmental Protection Agency (EPA) and the New York State Department of Environmental Conservation (NYSDEC), as appropriate, that it is among the potentially responsible parties (PRPs) who may be liable to pay for costs incurred to remediate certain hazardous substances at nine waste sites, not including the company's inactive gas manufacturing sites, which are discussed below. With respect to the nine sites, seven sites are included in the New York State Registry of Inactive Hazardous Waste Sites (New York State Registry) and two of the sites are also included on the National Priorities list.

Any liability may be joint and several for certain of those sites. The company has recorded an estimated liability of $1 million related to six of the nine sites, which is reflected in the company's consolidated balance sheets at December 31, 1996. The ultimate cost to remediate the sites may be significantly more than the estimated amount and will be dependent on such factors as the remedial action plan selected, the extent of site contamination and the portion attributed to the company.

The company has a program to investigate and perform necessary remediation at its known inactive gas manufacturing sites. In March 1994 and October 1996 the company entered into Orders on Consent with the NYSDEC requiring the company to investigate and, where necessary, remediate 34 of the company's 38 known inactive gas manufacturing sites. With respect to the 38 sites, eight sites are included in the New York State Registry.

Expenditures through the year 2009 are estimated at $31 million, including the impact of the Orders on Consent. That estimate was determined by using the company's experience and knowledge related to the sites as a result of the investigation and remediation that the company has performed to date. It could change materially, based on facts and circumstances derived from site investigations, changes in required remedial action, changes in technology relating to remedial alternatives and changes in presently enacted laws and regulations. The liability to investigate and perform remediation, as necessary, at the known inactive gas manufacturing sites, is reflected in the company's consolidated balance sheets at December 31, 1996 and 1995, in the amount of $31 million. The company has recorded a corresponding regulatory asset, since it expects to recover such expenditures in rates, as the company has previously been allowed by the PSC to recover such costs in rates. The company has notified its former and current insurance carriers that it seeks to recover from them certain of the cleanup costs. The company is unable to predict the amount of insurance recoveries, if any, that it may obtain.

10 ENERGY SERVICES

The company, pursuant to a PSC Order, is allowed to invest up to 5% of its consolidated capitalization (approximately $171 million at December 31, 1996) in one or more subsidiaries that may engage or invest in energy-related or environmental-services businesses and provide related services.

The company has been making investments in energy services companies through NGE Enterprises, Inc. (NGE). Those companies provide energy, financial and environmental services.

The company's investment as of December 31 and net loss for the year ended December 31 related to NGE are:

	1996	1995	1994
(Millions)			
Investment	$57	$54	$47
Net Loss*	$21	$12	$6

* Includes net loss from EnerSoft Corporation (EnerSoft) of $16 million, $7 million and $5 million in 1996, 1995 and 1994, respectively. EnerSoft's 1996 net loss includes $10 million related to NGE's decision to exit that business.

The majority of the company's investment is included in other property and investments, net on the consolidated balance sheets. NGE's total liabilities and capitalization at December 31, 1996 and 1995, was approximately $45 million and $48 million, respectively. NGE's net loss is included in other income and deductions on the consolidated statements of income.

11 FAIR VALUE OF FINANCIAL INSTRUMENTS

Certain of the company's financial instruments had carrying amounts and estimated fair values (based on the quoted market prices for the same or similar issues of the same remaining maturities) as follows:

December 31	1996	1996	1995	1995
	Carrying Amount	Estimated Fair Value	Carrying Amount	Estimated Fair Value
(Thousands)				
Preferred stock subject to mandatory redemption requirements	$25,000	$22,531	$125,000	$130,085
First mortgage bonds	$894,894	$938,873	$954,151	$1,025,696
Pollution control notes	$613,000	$623,666	$613,000	$617,446

The carrying amount for the following items approximates estimated fair value because of the short maturity (within one year) of those instruments: cash and cash equivalents, commercial paper and interest accrued.

Special deposits include restricted funds that are set aside for preferred stock and long-term debt redemptions. The carrying amount approximates fair value because the special deposits have been invested in securities with a short-term maturity (within one year).

12 INDUSTRY SEGMENT INFORMATION

Certain information pertaining to the electric and natural gas operations of the company follows:

	1996	1996	1995	1995	1994	1994
	Electric	Natural Gas	Electric	Natural Gas	Electric	Natural Gas
(Thousands)						
Operating						
Revenues	$1,723,147	$336,224	$1,708,297	$301,244	$1,600,075	$298,780
Income	$400,262	$57,281	$421,328	$50,816	$397,747	$40,828
Depreciation and amortization	$176,906	$12,495	$172,831	$11,939	$167,484	$10,842
Capital expenditures	$129,212	$82,625	$113,539	$45,142	$183,910	$40,396
Identifiable assets*	$4,376,814	$550,196	$4,525,541	$493,537	$4,631,511	$486,075

*Assets used in electric, natural gas and energy services operations not included above were $132,671, $95,253, and $113,099 at December 31, 1996, 1995 and 1994, respectively. They consist primarily of cash and cash equivalents, special deposits, prepayments and subsidiaries' assets.

13 QUARTERLY FINANCIAL INFORMATION (UNAUDITED)

Quarter ended	March 31	June 30	Sept. 30	Dec. 31
(Thousands, except per share amounts)				
	1996	1996	1996	1996
Operating revenues	$618,764	$452,933	$456,568	$531,106
Operating income	$196,353	$74,924	$74,285	$111,981
Net income	$98,676	$20,882	$11,052*	$47,631
Earnings available for common stock	$96,343	$18,496	$8,616	$45,256
Earnings per share	$1.35	$.26	$.12*	$.65
Dividends per share	$.35	$.35	$.35	$.35
Average shares outstanding	71,503	71,503	71,416	70,096
Common stock price**				
High	$26.38	$24.50	$24.88	$22.63
Low	$21.88	$22.00	$21.13	$20.38
	1995	1995	1995	1995
Operating revenues	$571,910	$439,916	$464,694	$533,021
Operating income	$157,323	$81,035	$106,638	$127,148
Net income	$75,584	$24,630	$43,503	$52,973
Earnings available for common stock	$70,825	$19,914	$38,878	$48,352
Earnings per share	$.99	$.28	$.54	$.68
Dividends per share	$.35	$.35	$.35	$.35
Average shares outstanding	71,503	71,503	71,503	71,503
Common stock price**				
High	$21.75	$24.00	$26.75	$26.38
Low	$19.00	$21.25	$22.50	$24.75

* Includes the effect of the writedown of the investment in EnerSoft Corporation that decreased net income and earnings available for common stock by $10 million and decreased earnings per share by 14 cents.

**The company's common stock is listed on the New York Stock Exchange. The number of shareholders of record at December 31, 1996, was 45,608.

Report of Management

The company's management is responsible for the preparation, integrity and reliability of the consolidated financial statements, notes and other information in this annual report. The consolidated financial statements have been prepared in accordance with generally accepted accounting principles and include estimates that are based upon management's judgment and the best available information. Other financial information contained in this report was prepared on a basis consistent with that of the consolidated financial statements.

The company maintains a system of internal controls designed to provide reasonable assurance to the company's management and board of directors regarding the preparation of reliable published financial statements and the safeguarding of assets against loss or unauthorized use. The system contains self-monitoring mechanisms and actions are taken to correct deficiencies as they are identified. Even an effective internal control system, no matter how well designed, has inherent limitations, including the possibility of the circumvention or overriding of controls, and therefore can provide only reasonable assurance with respect to financial statement preparation and the safeguarding of assets. Further, because of changes in conditions, internal control system effectiveness may vary over time.

The company maintains an internal audit department that independently assesses the effectiveness of the internal controls. In addition, the company's independent accountants, Coopers & Lybrand L.L.P., have considered the company's internal control structure to the extent they considered necessary in expressing an opinion on the consolidated financial statements. Management is responsive to the recommendations of its internal audit department and Coopers & Lybrand L.L.P. concerning internal controls and corrective measures are taken when considered appropriate. The board of directors oversees the company's financial reporting through its audit committee. The committee, which is comprised entirely of outside directors, meets regularly with management, the internal auditor and Coopers & Lybrand L.L.P. to discuss auditing, internal control and financial reporting matters. Both the internal auditor and independent accountants have direct access to the audit committee, independent of management.

The company assessed its internal control system as of December 31, 1996, in relation to criteria for effective internal control over financial reporting and the safeguarding of assets described in Internal Control - Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission. Based on this assessment, the company believes that, as of December 31, 1996, its system of internal control over financial reporting and over the safeguarding of assets against loss or unauthorized use met those criteria.

Wesley W. von Schack
Chairman, President and Chief Executive Officer

Sherwood J. Rafferty
Senior Vice President and Chief Financial Officer

Gary J. Turton
Vice President and Controller
Chief Accounting Officer

Report of Independent Accountants

To the Shareholders and Board of Directors,
New York State Electric & Gas Corporation and Subsidiaries
Ithaca, New York

We have audited the accompanying consolidated balance sheets of New York State Electric & Gas Corporation and subsidiaries as of December 31, 1996 and 1995, and the related consolidated statements of income, changes in common stock equity and cash flows for each of the three years in the period ended December 31, 1996. These financial statements are the responsibility of the company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with generally accepted auditing standards. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the consolidated financial position of New York State Electric & Gas Corporation and subsidiaries at December 31, 1996 and 1995, and the consolidated results of their operations and their cash flows for each of the three years in the period ended December 31, 1996, in conformity with generally accepted accounting principles.

Coopers + Lybrand L.L.P.

New York, New York
January 31, 1997

GLOSSARY

Above-market costs • costs, such as amounts for power purchase contracts with NUGs, that are greater than the market price.

Allowance for funds used during construction (AFDC) • the cost of money used to finance a project which is added to construction costs and recovered over the life of the asset.

Allowed return on common stock equity • the cost of common stock equity as determined by the PSC.

Book value per share • common stock equity divided by the number of common shares outstanding at the end of the period.

Btu (British thermal unit) • the quantity of heat required to raise the temperature of one pound of water by one degree fahrenheit at sea level.

Common stock equity • the value of common stockholders' investment in a company including retained earnings.

Dekatherm (dth) • a measure of heating value equal to one million Btu. One dekatherm equals approximately 1,000 cubic feet of natural gas (one mcf).

Demand-side management (DSM) • the planning and implementation of programs designed to help electric customers conserve energy.

Earnings available for common stock • net income less preferred stock dividends.

Earnings per share • earnings available for common stock for a given period divided by the average number of shares outstanding for the period.

Embedded cost of long-term debt • the weighted average interest rate on long-term debt outstanding.

Market-to-book ratio • the market price of common stock divided by its book value per share.

Net income • income after all revenues and expenses are recognized but before preferred dividends are recognized.

Nonutility generator (NUG) • a nontraditional power generator that is also known as an independent power producer.

Price/earnings (P/E) ratio • the market price of common stock divided by its earnings per share.

Retained earnings • the portion of earnings that has been reinvested in the business and not paid out as dividends.

Return on common stock equity • the rate of return actually earned on common stock equity calculated by dividing earnings for common stock by average common stock equity.

Transportation gas • natural gas purchased directly from a supplier by an end user and transported, for a fee, by a local distribution company, such as the company.

Unbilled revenues • the estimated revenues attributable to energy that has been delivered to the company's customers but for which the metered amount has not yet been billed to the customers.

Watt • one ampere of electric current under one volt of pressure (one kilowatt is 1,000 watts, one kilowatt-hour is one kilowatt used for one hour and one megawatt is 1,000 kilowatts or one million watts).

ACRONYMS

AFDC • Allowance for Funds used During Construction

APBO • Accumulated Postretirement Benefit Obligation

DSM • Demand-side Management

EPA • U. S. Environmental Protection Agency

FERC • Federal Energy Regulatory Commission

NEIL • Nuclear Electric Insurance Limited

NGE • NGE Enterprises, Inc.

NMP2 • Nine Mile Point nuclear generating unit No. 2

NRC • Nuclear Regulatory Commission

NUG • Nonutility Generator

NYSDEC • New York State Department of Environmental Conservation

PBO • Projected Benefit Obligation

PRP • Potentially Responsible Party

PSC • Public Service Commission of the State of New York

SRC • Somerset Railroad Corporation

Selected Financial Data

(Thousands, except per share amounts)	1996	1995	1994	1993	1992	1991	1986
Operating Revenues							
Electric	$1,723,147	$1,708,297	$1,600,075	$1,527,362	$1,451,525	$1,367,936	$1,098,[illegible]
Natural gas	336,224	301,244	298,780	272,787	240,164	187,879	179,195
Total Operating Revenues	2,059,371	2,009,541	1,898,855	1,800,149	1,691,689	1,555,815	1,277,284
Operating Expenses							
Fuel used in electric generation	222,102	229,759	231,648	245,283	262,531	274,877	238,371
Electricity purchased	360,753	318,440	242,352	161,967	95,026	45,808	29,302
Natural gas purchased	172,705	149,789	161,627	141,635	126,815	99,528	111,147
Other operating expenses	342,455	326,922	328,961	349,177	318,680	279,364	182,710
Restructuring expenses	–	–	–	26,000	–	–	–
Maintenance	107,697	116,807	106,637	111,757	102,500	110,131	88,486
Depreciation and amortization	189,401	184,770	178,326	164,568	158,977	152,380	100,796
Other taxes	206,715	210,910	210,729	204,962	200,941	178,185	122,400
Total Operating Expenses	1,601,828	1,537,397	1,460,280	1,405,349	1,265,470	1,140,273	873,212
Operating Income	457,543	472,144	438,575	394,800	426,219	415,542	404,072
Interest Charges, Net	122,729	129,567	136,092	141,099	151,831	158,528	166,328
Other Income and Deductions	48,630	30,023	12,377	1,923	1,144	5,754	(109,089)
Income Before Federal Income Taxes	286,184	312,554	290,106	251,778	273,244	251,260	346,833
Federal Income Taxes	107,943	115,864	102,461	85,750	89,276	82,617	118,339
Net Income	178,241(1)	196,690	187,645(2)	166,028(3)	183,968	168,643	228,494
Preferred Stock Dividends	9,530	18,721	18,947	20,638	20,995	20,330	20,104
Earnings Available for Common Stock	168,711(1)	177,969	168,698(2)	145,390(3)	162,973	148,313	208,390
Common Stock Dividends	99,611	100,104	142,265	152,316	144,621	131,875	140,[illegible]
Retained Earnings Increase (Decrease)	$64,717	$77,865	$26,433	$(6,926)	$18,352	$16,438	$64,52[illegible]
Average Number of Shares of Common Stock Outstanding	71,127	71,503	71,254	69,990	67,972	62,906	54,014
Earnings Per Share	$2.37(1)	$2.49	$2.37(2)	$2.08(3)	$2.40	$2.36	$3.86
Dividends Paid Per Share	$1.40	$1.40	$2.00	$2.18	$2.14	$2.10	$2.60
Book Value Per Share of Common Stock (Year End)	$25.41	$24.38	$23.28	$22.89	$22.85	$22.16	$25.86
Capital Expenditures	$211,837	$158,681	$224,306	$245,029	$245,618	$245,883	$332,896
Total Assets	$5,059,681	$5,114,331	$5,230,685	$5,287,958	$5,077,916	$4,924,836	$4,224,984
Long-term Obligations, Capital Leases and Redeemable Preferred Stock	$1,505,814	$1,606,448	$1,776,081	$1,755,629	$1,883,927	$1,897,465	$1,951,227

(1) Includes the effect of the writedown of the investment in EnerSoft Corporation that decreased net income and earnings available for common stock by $10 million and decreased earnings per share by 14 cents.

(2) Includes the effect of the 1993 production-cost penalty that decreased net income and earnings available for common stock by $8 million and decreased earnings per share by 12 cents.

(3) Includes the effect of restructuring expenses that decreased net income and earnings available for common stock by $17 million and decreased earnings per share by 25 cents.

○ FINANCIAL STATISTICS

	1996	1995	1994	1993	1992	1991	1986
Financial Statistics							
Return on average common stock equity – percent	9.6	10.4	10.3	10.1 (1)	10.6	10.7	15.3
Percentage of AFDC and non-cash return to total earnings	3.3	2.7	4.7	5.5	4.0	5.1	53.7
Mortgage bond interest – times earned	4.1	4.0	3.5	3.0	3.1	3.0	2.9
Interest charges and preferred dividends – times earned	2.3	2.2	2.1	1.9	1.9	1.8	1.9
Market value per share of common stock (year end)	$21.63	$25.88	$19.00	$30.75	$32.50	$29.00	$31.38
Dividend payout ratio (percent)	59.1	56.2	84.4	104.8	89.2	89.0	67.4
Price earnings ratio (year end)	9.1	10.4	8.0	14.8	13.5	12.3	8.1
Property, Plant and Equipment (includes construction work in progress) (Thousands)							
Electric	$5,208,307	$5,125,336	$5,027,137	$4,887,125	$4,694,073	$4,537,356	$4,129,838
Natural gas	544,898	472,056	431,202	393,945	361,630	336,199	164,426
Common	162,758	157,823	171,639	180,532	205,345	189,135	78,781
Total	$5,915,963	$5,755,215	$5,629,978	$5,461,602	$5,261,048	$5,062,690	$4,373,045
Accumulated Depreciation	$1,933,599	$1,791,625	$1,642,653	$1,541,456	$1,427,793	$1,309,829	$769,336
Number of Shareholders of Record							
Common stock	45,608	50,576	56,279	58,990	61,183	59,593	71,935
Preferred stock	1,211	1,297	1,329	3,632	3,829	3,943	6,060

(1) The return on equity for 1993 excludes restructuring expenses.

∘ Electric Sales and Natural Gas Deliveries Statistics

	1996	1995	1994	1993	1992	1991	1986
Electric Sales							
Megawatt-Hour (mwh) Sales (Thousands)							
Residential	**5,393**	5,286	5,399	5,423	5,472	5,297	4,791
Commercial	**3,430**	3,405	3,315	3,298	3,283	3,285	2,772
Industrial	**2,992**	3,010	2,997	2,950	3,082	3,068	2,899
Other	**1,401**	1,392	1,437	1,417	1,457	1,457	1,345
Total Retail	**13,216**	13,093	13,148	13,088	13,294	13,107	11,807
Other electric utilities	**7,914**	7,636	6,827	6,233	6,003	5,066	3,545
Total	**21,130**	20,729	19,975	19,321	19,297	18,173	15,352
Operating Revenues (Thousands)							
Residential	**$744,439**	$725,299	$679,124	$635,155	$601,042	$553,056	$457,132
Commercial	**400,841**	395,076	366,854	333,674	314,272	293,197	235,246
Industrial	**242,792**	247,576	245,218	228,215	225,832	207,933	187,372
Other	**158,377**	158,568	153,888	138,320	133,819	124,575	109,181
Total Retail	**1,546,449**	1,526,519	1,445,084	1,335,364	1,274,965	1,178,761	988,931
Other electric utilities	**162,232**	150,444	141,902	147,175	143,414	131,412	95,707
Unbilled revenue recognition, net	**–**	–	–	2,257	(427)	35,333	–
Other operating revenues	**14,466**	31,334	13,089	42,566	33,573	22,430	13,451
Total Operating Revenues	**$1,723,147**	$1,708,297	$1,600,075	$1,527,362	$1,451,525	$1,367,936	$1,098,089
Natural Gas Deliveries							
Dekatherm (dth) Deliveries (1) (Thousands)							
Residential	**25,470**	23,512	24,662	25,080	24,913	18,115	14,[illegible]
Commercial	**10,146**	10,540	10,611	10,640	10,796	8,054	7,343
Industrial	**2,726**	2,587	2,180	1,820	1,689	1,788	5,126
Other	**2,230**	2,463	2,038	1,805	1,959	1,917	3,373
Total Retail	**40,572**	39,102	39,491	39,345	39,357	29,874	29,981
Transportation of customer-owned natural gas	**20,970**	19,433	19,133	18,701	17,009	12,530	3,287
Total	**61,542**	58,535	58,624	58,046	56,366	42,404	33,268
Operating Revenues (1) (Thousands)							
Residential	**$198,338**	$181,697	$185,073	$170,734	$152,325	$111,106	$91,068
Commercial	**83,393**	75,178	72,360	66,648	59,939	43,969	42,711
Industrial	**14,509**	11,310	11,542	9,602	8,092	8,640	24,429
Other	**15,697**	14,584	12,997	10,943	10,762	10,243	17,783
Total Retail	**311,937**	282,769	281,972	257,927	231,118	173,958	175,991
Transportation of customer-owned natural gas	**17,476**	13,718	12,791	12,091	11,639	9,571	2,168
Unbilled revenue recognition, net	**292**	1,700	3,768	2,686	(3,626)	3,770	–
Other natural gas revenue	**6,519**	3,057	249	83	1,033	580	1,036
Subtotal	**24,287**	18,475	16,808	14,860	9,046	13,921	3,204
Total Operating Revenues	**$336,224**	$301,244	$298,780	$272,787	$240,164	$187,879	$179,195

(1) The increase in 1992 is primarily due to the acquisition of Columbia Gas of New York, Inc.

Electric Generation Statistics

	1996	1995	1994	1993	1992	1991	1986
System Capability (Megawatts)							
Coal	2,236	2,226	2,278	2,394	2,415	2,412	2,366
Nuclear	206	206	189	189	188	196	–
Hydro	62	61	69	67	70	70	68
Internal combustion	7	7	7	7	8	8	7
Total Generating Capability	2,511	2,500	2,543	2,657	2,681	2,686	2,441
Purchased – Power Authority	591	517	514	486	489	488	563
– NUG	599	595	594	362	347	110	–
Less: Firm sales	(607)	(118)	(367)	(311)	(8)	–	–
Total System Capability	3,094	3,494	3,284	3,194	3,509	3,284	3,004
System Capability (Percent)							
Coal	72	63	69	75	69	74	79
Nuclear	7	6	6	6	5	6	–
Hydro	2	2	2	2	2	2	2
Total Generating Capability	81	71	77	83	76	82	81
Purchased – Power Authority	19	15	16	15	14	15	19
– NUG	20	17	18	12	10	3	–
Less: Firm sales	(20)	(3)	(11)	(10)	–	–	–
Total System Capability	100	100	100	100	100	100	100
Megawatt-Hour (mwh) Production, Net (Thousands)							
Generated							
Coal	14,195	14,296	14,338	15,131	16,709	16,157	13,196
Nuclear	1,566	1,306	1,509	1,295	922	1,180	–
Hydro	309	240	321	309	301	258	338
Total Generated	16,070	15,842	16,168	16,735	17,932	17,595	13,534
Purchased – Power Authority	1,921	1,849	1,700	1,617	1,635	1,667	2,590
– NUG	4,235	4,413	3,601	2,472	1,260	473	26
– Other, net	465	155	14	78	(10)	(130)	438
Total	22,691	22,259	21,483	20,902	20,817	19,605	16,588
Production Expenses (Thousands)							
Generated	$322,233	$335,706	$339,546	$371,891	$375,209	$391,393	$318,885
Purchased – Power Authority	27,263	26,079	21,478	16,713	15,661	14,668	16,357
– NUG	319,958	283,913	214,010	137,791	71,260	30,028	1,454
– Other	13,532	8,448	6,864	7,463	8,105	1,112	11,491
Total	$682,986	$654,146	$581,898	$533,858	$470,235	$437,201	$348,187

Board of Directors

James A. Carrigg • a director since 1983, is Chairman of the Board of Trustees of Broome Community College in Binghamton, New York. He was Chairman, President and Chief Executive Officer of the corporation from 1991 until September 1996.

Alison P. Casarett • a director since 1979, is Dean Emeritus at Cornell University in Ithaca, New York. She is Emeritus Professor of Radiation Biology at the New York State College of Veterinary Medicine of Cornell University. She was Special Assistant to the President of Cornell University from 1993 to 1995. Prior to that time she was Dean of The Graduate School at Cornell University.

Joseph J. Castiglia • a director since 1995, is Chairman of the Center for Competitiveness and Vice Chairman of the AAA Western and Central New York Automobile Association, both in Buffalo, New York. He was Vice Chairman, President and Chief Executive Officer of Pratt & Lambert United, Inc., a paint and specialty chemicals company in Buffalo, New York.

Lois B. DeFleur • a director since 1995, is President of the State University of New York at Binghamton in Binghamton, New York. She is Vice Chairperson of the American Council on Education in Washington, D.C.

Everett A. Gilmour • a director since 1980, is Chairman of the Board of The National Bank and Trust Company of Norwich and N.B.T. Bancorp, Inc., both in Norwich, New York.

Paul L. Gioia • a director since 1991, is of counsel at LeBoeuf, Lamb, Greene & MacRae, attorneys at law in Albany, New York. He was a Senior Vice President of First Albany Corporation from 1987 to 1993 and prior to that Chairman of the Public Service Commission of the State of New York.

John M. Keeler • a director since 1989, is Managing Partner of Hinman, Howard & Kattell, attorneys at law in Binghamton, New York. He is Chairman of The Stuart and Willma Hoyt Foundation and a director of the Harriet L. Dickenson Foundation, both in Binghamton, New York.

Allen E. Kintigh • a director since 1987, is President of Royal Equipment, Inc., in Houston, Texas. He was President and Chief Operating Officer of the corporation from 1988 through 1990.

Ben E. Lynch • a director since 1987, is President of Winchester Optical Company, Elmira, New York. He was Chairman of the Arnot-Ogden Medical Center, in Elmira, New York and President of Horseheads Board of Education in Horseheads, New York.

Alton G. Marshall • a director since 1971, is President of Alton G. Marshall Associates, Inc., a real estate investment company in New York, New York. He is also Governor of The Real Estate Board of New York, Inc. in New York, New York.

Wesley W. von Schack • a director since September 1996, is Chairman, President and Chief Executive Officer of the corporation. He is a director of Mellon Bank Corporation and Mellon Bank, N.A., in Pittsburgh, Pennsylvania, and of RMI Titanium Company, in Niles, Ohio. He is also a life trustee and Vice Chairman of the Board of Trustees of Carnegie Mellon University, in Pittsburgh, Pennsylvania. He was Chairman of the Board, Chief Executive Officer and Director of DQE, Inc. from 1989 to August 1996 and Chairman from 1987 to August 1996 and Chief Executive Officer and Director from 1986 to August 1996 of Duquesne Light Company.

◦ EXECUTIVE OFFICERS

Ages and years of service as of January 1, 1997, in parentheses

Wesley W. von Schack • (52, 0) Chairman, President and Chief Executive Officer.

Jack H. Roskoz • (58, 34) Executive Vice President.

Michael I. German • (46, 2) Senior Vice President - Gas Business Unit.

Gerald E. Putman • (46, 26) Senior Vice President - Customer Service Business Unit.

Sherwood J. Rafferty • (49, 16) Senior Vice President and Chief Financial Officer.

Daniel W. Farley • (41, 15) Vice President and Secretary.

Robert D. Kump • (35, 10) Treasurer.

Jeffrey K. Smith • (48, 26) Vice President - Generation.

Ralph R. Tedesco • (43, 18) Vice President - Strategic Growth Business Unit.

Gary J. Turton • (49, 24) Vice President and Controller.

Denis E. Wickham • (47, 24) Vice President - Electric Resource Planning.

◦ XENERGY Inc.

Kellogg L. Warner • (41, 8) President and Chief Executive Officer.

Committees of the Board • Chairperson listed first
Audit: Lynch, Casarett, Castiglia, Keeler
Corporate Diversification: Gioia, Carrigg, Castiglia, Gilmour, Lynch, von Schack
Executive: Carrigg, Gilmour, Gioia, Kintigh, Marshall, von Schack
Executive Compensation and Succession: Gilmour, Casarett, Lynch, Marshall
Nominating: Marshall, Casarett, DeFleur, Gilmour

Shareholder Information

Shareholder Services
Shareholder Services representatives are available between 8 a.m. and 4:30 p.m. (Eastern Time) on regular business days at 1-800-225-5643. Or you may write to:

New York State Electric & Gas Corporation
Attention: Shareholder Services
P.O. Box 3200
Ithaca, NY 14852-3200

Please contact NYSEG Shareholder Services with questions regarding:

- dividend payments or lost dividend checks
- direct deposit of dividends
- our dividend reinvestment and stock purchase plan
- replacement of lost certificates
- a change of address
- annual report requests
- our annual meeting of shareholders

The Shareholder Connection
1-800-225-5643
NYSEG investor information at your fingertips.

This service provides quick access to timely dividend and news release information 24 hours a day, seven days a week.

Transfer Agent and Registrar
To present certificates for transfer (certified or registered mail is recommended) or for stock transfer instructions, write to:

ChaseMellon Shareholder Services
Customer Service
P.O. Box 590
Ridgefield Park, NJ 07660

Internet Address
http://www.nyseg.com
Information about NYSEG, including financial documents and news releases, are available at our world wide web site.

Shareholders may also obtain a free copy of Form 10-K, which is filed each year with the Securities and Exchange Commission, by contacting Shareholder Services at the telephone number or address above.

Trading Symbol
NGE is the trading symbol for NYSEG common stock listed on the New York Stock Exchange.

Annual Meeting
Wednesday, May 21, 1997, at 10:30 a.m.
State University of New York
College at Oneonta
Charles W. Hunt College Union
Oneonta, NY.

Formal notices of the meeting, a proxy statement and form of proxy will be mailed to shareholders in April.

We would like your comments and suggestions on this annual report.

NYSEG

Which sections of the 1996 NYSEG annual report did you find most useful? *(Check all that apply)*

- ☐ Letter to Shareholders
- ☐ Statistics
- ☐ Front Narrative Section
- ☐ Investor Information
- ☐ Management's Discussion & Analysis
- ☐ Consolidated Financial Statements and Notes

Overall, how would you rate the clarity of this report?

☐ Excellent ☐ Very Good ☐ Fair ☐ Poor

Additional comments _____

(Optional)

Name _____

Address _____ Phone _____

City _____ State _____ Zip _____

Why worry?

NYSEG

You can elect to enroll in our Direct Deposit of Common Dividends Service instead of having NYSEG mail your quarterly common stock dividends in the form of a check.

With Direct Deposit:

- Your dividend will be electronically deposited to your designated account at any financial institution that accepts direct deposits, thereby providing immediate credit.
- You eliminate lost, stolen, delayed or misplaced checks.
- You receive an acknowledgement of the deposit.

☐ Yes, I would like to receive an authorization package and more information on this service.

Name _____

Address _____ Phone _____

City _____ State _____ Zip _____

Learn why New York earned the Cato Institute's 1996 Fiscal Policy Report Card top grade.

NYSEG

Since 1995, New York added 100,000 private sector jobs and cut 15,000 state jobs. In 1996, income taxes were cut by $1.8 billion and businesses taxes by $300 million. Learn more about how your business can grow and prosper in New York – mail the card today!

☐ Yes. Please send me information about how I can expand or relocate my business in New York.

☐ Yes. Please send me information about NYSEG Economic Development services.

Name _____

Title _____

Company _____

Address _____ Phone _____

City _____ State _____ Zip _____

NO POSTAGE
NECESSARY
IF MAILED
IN THE
UNITED STATES

BUSINESS REPLY MAIL
FIRST CLASS MAIL PERMIT NO. 141 ITHACA, NY

POSTAGE WILL BE PAID BY ADDRESSEE

New York State Electric & Gas Corporation
Attn: Corporate Communications
P.O. Box 5224
Binghamton, NY 13902-7994

NO POSTAGE
NECESSARY
IF MAILED
IN THE
UNITED STATES

BUSINESS REPLY MAIL
FIRST CLASS MAIL PERMIT NO. 141 ITHACA, NY

POSTAGE WILL BE PAID BY ADDRESSEE

New York State Electric & Gas Corporation
Attn: Corporate Communications
P.O. Box 5224
Binghamton, NY 13902-7994

NO POSTAGE
NECESSARY
IF MAILED
IN THE
UNITED STATES

BUSINESS REPLY MAIL
FIRST CLASS MAIL PERMIT NO. 141 ITHACA, NY

POSTAGE WILL BE PAID BY ADDRESSEE

New York State Electric & Gas Corporation
Attn: Corporate Communications
P.O. Box 5224
Binghamton, NY 13902-7994

New York State Electric & Gas Corporation
Ithaca-Dryden Road
P.O. Box 3287
Ithaca, NY 14852-3287

BULK RATE
U.S. POSTAGE
PAID
New York State
Electric & Gas
Corporati

New York State Electric & Gas Corporation
is an equal opportunity employer.

Printed on recycled paper.

Printed with soy ink.

Printed using an infrared drying system.

Graphic Design: Sunmark, LLC

Printing: Cayuga Press

2/97 96-1769 135M CAP Corporate Communications