LEDGER

To: December 31, 1979

From: January 1, 1979

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Electric & Water Operations

Index - 1979

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The annual meeting of stockholders is scheduled to be held April 22, 1980. A proxy form and notice of the annual meeting will be mailed to all stockholders on March 3, 1980.

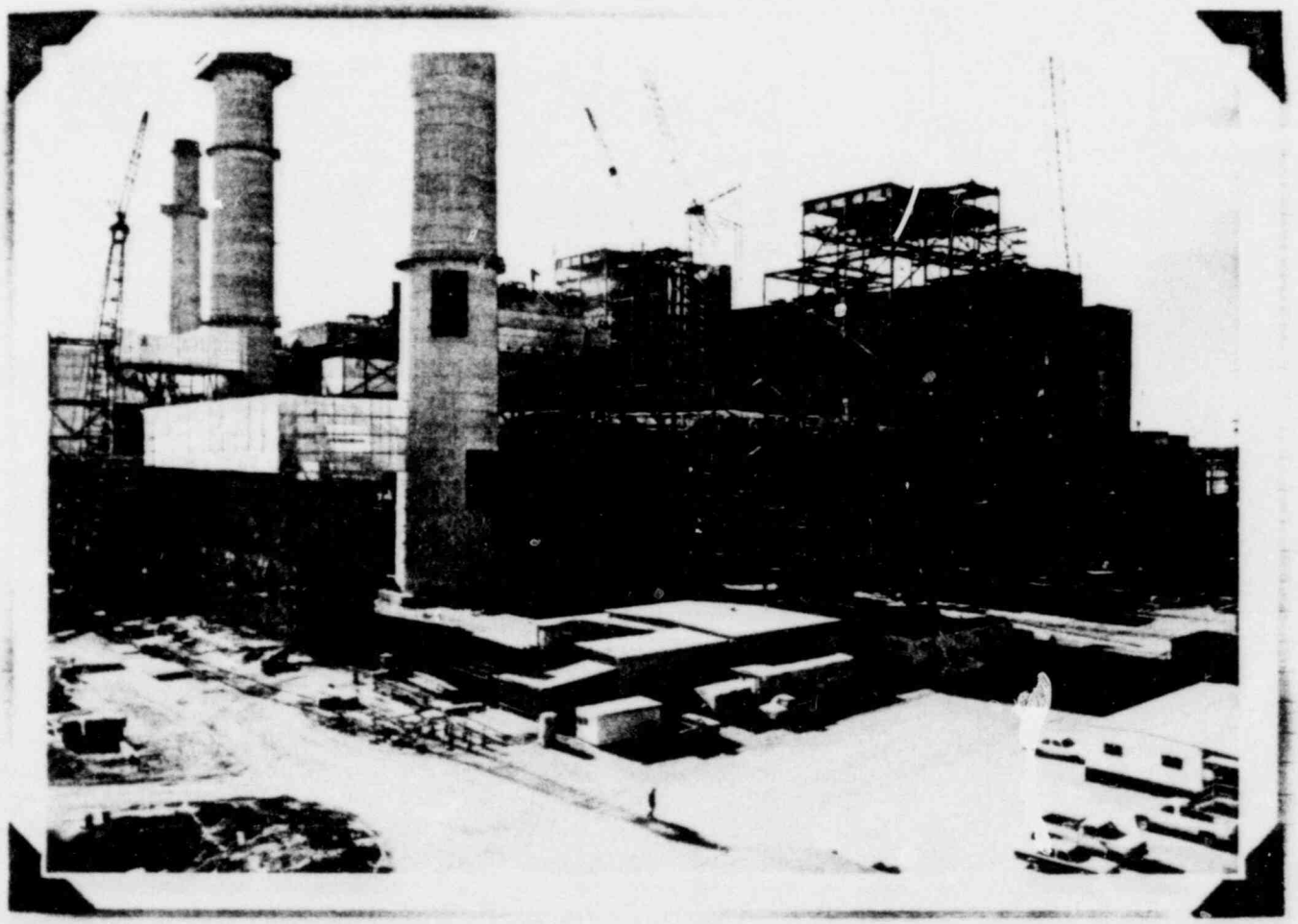
For further information and details pertaining to the information provided in this report contact D. E. Peckham, Secretary, Public Service Company of New Mexico, Post Office Box 2267, Albuquerque, New Mexico 87103.

The Common Stock of this Company is traded on the New York Stock Exchange under the symbol PNM.

This Annual Report and the financial statements contained herein are submitted for the general information of the stockholders of the Company and are not intended for use in connection with any sale or purchase of, or any offer or solicitation of offers to buy or sell, any securities of the Company.

Financial Highlights

	1979	1978	% Change
Operating revenues	$ 244,370,000	$187,205,000	30.5
Operating expenses	$ 184,554,000	$143,258,000	28.8
Operating income	$ 59,816,000	$ 43,947,000	36.1
Net earnings	$ 54,803,000	$ 37,464,000	46.3
Net earnings applicable to common stock	$ 42,607,000	$ 29,081,000	46.5
Return on average common equity	13.6%	13.0%	4.6
Average number of common shares outstanding	14,363,000	10,289,000	39.6
Net earnings per common share	$ 2.97	$ 2.83	5.0
Dividends paid per common share	$ 1.88	$ 1.72	9.3
Construction expenditures	$ 323,361,000	$198,976,000	62.5
Gross investment in utility property	$1,197,514,000	$879,893,000	36.1
Kilowatt-hour sales (thousand kWhr)	4,960,451	4,527,826	9.6
Number of electric customers served at year end	206,000	196,000	5.1
Average kWhr usage per residential customer	5,929	5,880	.8
Number of employees	2,311	2,054	12.5
Number of common stockholders	34,236	27,026	26.7



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President's Letter

J.D. Geist, President

The end of a decade has come. For our industry, as for the country in general, it was ten years of unrelenting change. The rules and the perceptions of society, the attitude of the government and the attitude toward the government seemed to shift daily. It was a strange ten years no matter who you were or how you looked at it.

It was a decade which saw the United States disengage itself from a war which it neither bothered to declare nor set realistic military goals. It was a decade in which, for the first time, an American president resigned in disgrace. It was a decade that saw "liberals" begin to militantly support the status quo under the no-growth theme and "conservatives" argue heatedly for growth and change. It was a decade that saw the nation seemingly go into shock and refuse to make decisions or take action on matters of paramount importance — energy, defense, economic policy . . . the list is endless.

Yet, through it all, our institutions did manage to survive and to keep providing the public with far more than human history could define as "basic necessities." Life went on, although polls revealed that for the first time in American history many people no longer felt confident in the future.

As it became apparent that new ideas were going to be essential, it was decided that a touchstone was needed to help us all make sure we were looking in the right direction. A statement of principle was adopted. The full statement is on page 31. As simplistic as these thoughts may seem, it is only necessary to reflect for a moment on the complexities of life and the confusion surrounding us to see why a straightforward standard was developed. If PNM can adhere to these simple thoughts, our customers will have the service they expect at a price they can afford and in a manner they can understand. Our employees will have worthwhile jobs and our owners will be repaid for making it all possible.

An astounding expansion came about during this decade, in part, as people in other states began to develop an appreciation for the way of life offered by New Mexico. It also resulted from the commitment the people of New Mexico have made to their environment. The investment in pollution control equipment at the San Juan Generating Station now exceeds the total investment of the Company just ten years ago.

Meanwhile, as the nation and the world grappled with problems, companies, including PNM, had to come up with solutions to their own problems. In light of the range and diversity of the problems encountered in the 1970's, the last ten years may well go down as a decade of solutions for PNM.

PNM initiated a shift to coal without governmental suggestion or advice more than two decades ago. The third unit at the San Juan Generating Station came on-line in 1979. During the past year, your Company acquired full ownership of the fourth unit now under construction at San Juan. By this action, we can assure our customers that they will have electricity in the 1990's. Such assurance is becoming difficult for all utilities to make in these uncertain times.

However, using coal as an energy resource is not without its problems. Stringent constraints have been established on the burning of coal. PNM is committed to building and operating facilities to meet those requirements. When new regulations were being developed, and when regulatory actions were required, we often found that the desires of environmentalists compounded our already complex business environment. However, PNM has worked hard to establish a good relationship with local organized environmental groups. As a result, we have often been able to achieve agreements with those groups that contribute to the

preservation of New Mexico's environment and maintain a balanced consideration of the customers' needs.

In addition, we continue to search for new and better ways to meet future needs without relying on natural gas and oil. As part of this search, work continued on the Palo Verde Nuclear Generating Station. As you know, your Company committed itself to a 10.2 percent share in that project in 1973. In the aftermath of Three Mile Island, extensive reviews of the engineering and construction at Palo Verde have been conducted and some are still underway. We are confident that Palo Verde will serve our customers safely and reliably. We are also confident that society will conclude that the benefits of having domestic energy resources beyond the control of international politics will outweigh the limited risks of nuclear energy.

PNM studies continue to demonstrate that nuclear power has economic, environmental, and safety advantages over other available generating alternatives. Even though this is the case, the nuclear option is currently plagued with political and regulatory uncertainties. Therefore, PNM has not made a commitment to the construction of a nuclear plant within New Mexico, but the Company does continue to include the nuclear option as a consideration in its generation planning activities. Such planning includes the examination of design options, economics, and feasible sites for any future projects.

Work will soon commence on PNM's and the country's first hot water geothermal generating facility. Though geothermal energy now provides a significant part of northern California's electricity, the hot dry steam used there is a geological rarity. Geothermal hot water is not as rare and, if the PNM project now under development with the Department of Energy and Union Oil Company is successful, the technology could lend itself to application in many areas of the country.

The decade of the 1970's was remarkable for both the nation and PNM. But changing the calendar has not changed all our problems; energy remains a critical issue; economics of uncertainty are still part of our everyday life; and the quest for understanding and solutions to these pressing issues will be the hallmark of the 1980's.

Your Company's requirements for new construction in the 1980-84 five-year period is predicted to be $1,084 million. This is less than in the 1979-83 period. Barring any unexpected circumstances, there will be little change in the real price of electricity in the foreseeable future. It is clear that in order to continue the financing required, our emphasis must be on performance for shareholders. During 1979, our common shareholders provided us with more than $57.2 million of additional equity capital, 2,959,506 additional shares, to help finance needed facilities. In return, our common shareholders earned $2.97 per share, up from $2.83 in 1978.

You, our shareholders, have taken long-term risks in order to ensure an adequate power supply. The rate structure simply must be such that the bottom line is enticing to shareholders. Stock must be selling above book value, and we will do everything reasonable to make that happer

To our employees we say thanks for a dedicated decade; your innovation and individual energy have made our Company part of the solution to our country's problems. To our directors we again express appreciation for the widsom, stability and leadership you provide.

PNM enters the 1980's confident of its ability to provide reliable service and maintain the high level of accountability to its customers and to you, our shareholders.

Sincerely,

J. D. Geist
President

G. A. Schreiber
Chairman of the Board

Economic Picture

New Mexico Economy

PNM is situated in one of the growth areas of the Rocky Mountain West, as the Company's construction budget over the past decade indicates. Projections show that during 1979-1984 population in PNM's service area will grow by 16 percent, or an average of 2.9 percent per year. The national annual growth rate is expected to be about 1 percent. In contrast, the growth rate over 1974-1979 was 14.5 percent, an annual rate of 2.5 percent. The population in PNM's service area is currently estimated to be 532,000. Total state population is about 1,241,000.

Employment for the growing population in New Mexico is centered on government agencies plus trade and service businesses. Manufacturing represents a small portion of the economy with about 7 percent employment. This low percentage of manufacturing workers serves as insulation, tending to protect New Mexico from the effects of any national recession. The combined industrial segment of the economy (mining, manufacturing, and construction) provides about 20 percent of total employment.

But this industrial figure is climbing due to significant growth in coal and uranium mining. Besides the increasing development of huge coal reserves, the state currently supplies approximately 50 percent of the country's production of yellowcake. PNM supplies electricity to about 70 percent of the state's uranium mining activity.

In addition to the traditional segments of New Mexico's economy, there is also a large and active high technology research sector, including Los Alamos Scientific Laboratories and Sandia Laboratories. PNM is also recognized as a leader in energy research and development because of its work in projects such as solar and geothermal energy applications.

While the per capita income in New Mexico ranks in the bottom one-fifth of all states, the rate of increase is greater than most other states. Since 1974, personal income in New Mexico has been growing at one of the fastest rates in the Rocky Mountain region. Per capita income in the Albuquerque metro area, in which 80 percent of PNM's customers live, is currently about equal to the national average. The continuation of these trends is expected to lift New Mexico's per capita income above its current national ranking.

Construction and Financing

Nineteen seventy-nine was a significant year for PNM. The year represented the peak of our construction program in terms of annual dollars spent. In 1979, net utility plant additions totaled about $317 million, compared to about $199 million in 1978. Our current construction budget indicates a downward trend in annual construction dollars for the next several years until we begin our next major generating project. Also, the Company acquired full ownership of San Juan Unit 4 by purchasing Tucson Electric Power Company's 50 percent share of the unit. Construction of this 472-megawatt unit is scheduled for completion in 1982. The third unit at the San Juan Generating Station went into commercial service in December, bringing 240 net megawatts into the grid for PNM's customers.

New external funding for 1979 included a $40 million 8.75 percent preferred stock issue, an issue of common stock for $48 million, and $130 million in 6.5 percent pollution control revenue bonds. Common stock totaling $9.3 million was also raised through the Dividend Reinvestment Plan, the Employee Stock Purchase Plan, and the Tax Reduction Act Stock Ownership Plan (TRASOP). The Company also obtained commitments to place directly with institutional investors $45 million of 10⅛ percent first mortgage bonds, of which $17 million was received in 1979, with the remaining $28 million received in January 1980.

Revenues and Expenses

Revenues rose from $187 million in 1978 to $244 million in 1979, or 31 percent. This follows a 35 percent increase from 1977 to 1978. Of the $57 million increase in revenues, it is estimated that 26 percent resulted from increased kilowatt-hour sales, 26 percent from fuel clause adjustments and 48 percent from increases in base electric rates. Electric sales grew from about 4.5 billion to almost 5 billion kilowatt-hours, a 9.6 percent increase.

In 1979, fuel and purchased power expense was up by about 36 percent due to increased energy requirements and costs of fuel. Other operating and maintenance expenses climbed by 22 percent, compared to 26 percent in 1977-1978. Cost control programs were continued during the year and a trend toward improved cost-effectiveness is evident.

As a result of the financing for our construction program, interest expenses on short-term debt rose due to a higher level of borrowing and increases in the interest levels. Long-term debt also grew in 1979 and total interest charges were up by about $3.7 million. Preferred dividends increased by about $3.8 million.

Earnings

During 1979, PNM's net earnings available to common shares grew from about $29 million to $43 million, or about 47 percent. However, reflecting the Company's increased investment in plant, shares outstanding climbed from approximately 12.6 million shares to 15.6 million, or 23 percent. Earnings per share for 1979 were $2.97, compared to $2.83 for 1978, on average shares outstanding.

The increase in average shares outstanding was due to the sale of common stock in 1978 and 1979 to finance our construction program. Return on average common equity for 1979 was 13.6 percent, compared to 13 percent for 1978.

Rates and Regulation

As an electric and water utility operating in the State of New Mexico, PNM is subject to the jurisdiction of the New Mexico Public Service Commission (NMPSC). Activities of the Company regulated by the NMPSC include rates, quality of service, issuance of securities, and generation and transmission construction. The Federal Energy Regulatory Commission (FERC) has jurisdiction over rates charged by PNM for electricity sold to other electric utilities.

Since mid-1975, PNM has used a method of rate adjustment called Cost of Service Indexing, which allows recovery of present-day costs of generating and distributing electricity. As originally designed, the Index was applied to rates under jurisdiction of the NMPSC, and allowed a quarterly adjustment when return on average common equity fell below or exceeded a band of 13.5 to 14.5 percent.

In May of 1979, however, the NMPSC ruled that the rate adjustment method could serve its intent by allowing annual adjustments. At that time, the NMPSC allowed the "rolling-in" of the factor into the base rate charge and during the remainder of 1979 the Indexing factor was removed as a separate item. The NMPSC determined that PNM would be allowed to adjust rates in a manner designed to attain earnings of 13.5 percent on year-end common equity. The first annual Index factor was calculated on 1978 revenues and expenses, with certain adjustments. Investment in the construction work in progress relating to San Juan Unit 3, placed in service in late 1979, and all pollution control equipment at the San Juan Generating Station was included in the revised calculations. The allowance for funds used during construction rate on other construction work in progress was changed from 6.5 percent to 7.5 percent. A composite return on accumulated deferred investment tax credits was allowed. With the switch from quarterly to annual adjustment of the factor and with the additional procedural and reporting requirements, Indexing has become less automatic; however, it retains many advantages over a traditional rate filing, including significant reductions in traditional regulatory lag. The New Mexico Attorney General appealed the May 1979 Order to the Santa Fe District Court and is contending that the formula used by the NMPSC in arriving at the annual Index factor produces excessive revenues. The NMPSC and the Company are opposing the Attorney General's position.

On the basis of most measures of financial integrity, the Cost of Service Index has been successful to date. PNM's total capitalization more than tripled between 1974 and 1978, compared to an industry average increase of about 40 percent. Yet, during this period, PNM improved its position relative to the industry average. Return on average capital, return on equity, before and after tax interest coverages, and market price-to-book value ratio improved markedly. In particular, return on average common equity rose approximately 39 percent from 9.7 percent in 1974 to 13.6 percent in 1979.

As part of a review of the Indexing procedures, PNM filed a rate redesign package with the NMPSC on December 31, 1979, to assist the NMPSC in complying with the Public Utilities Regulatory Policies Act (PURPA). The federal law requires utility regulators nationally to review cost and price standards, to promote conservation by utility customers and to increase the efficiency of electric energy use.

If approved by the NMPSC, the Company's proposed rate redesign would promote energy conservation as well as provide rate incentives to high-use customers who shift electric consumption off-peak when generating costs are lowest. The proposal would offer high-use electric customers the possibility of being billed for electricity based on the times of the day and seasons the power is used. The concept, called Time-of-Day or Time-of-Use

rates, currently is not available from any utility in New Mexico.

The Company has a fuel adjustment clause which allows the direct pass-through of increased fuel costs. The adjustment is applicable to all sales. An additional part of the proposed rate redesign filed with the NMPSC would allow the Company to "zero out" the fuel adjustment factor by rolling the factor into the base rate for electrical service.

Electric Operations

The power produced by PNM comes from generating facilities as shown in the following table:

Location and Generating Station	PNM's Share of Capacity (MW)
Coal-Fired Stations	
Near Farmington	
Four Corners Units 4 & 5	208
San Juan Units 1, 2, & 3	550
Gas- and Oil-Fired Stations	
Albuquerque	
Person Station	96
Reeves Station	175
Prager Station	22
Santa Fe	
Santa Fe Station	11
Las Vegas	
Las Vegas Turbine	20
TOTAL	1,082

The Company holds a 13 percent ownership in Units 4 and 5 of the Four Corners Generating Station, a 50 percent ownership in San Juan Station Units 1, 2, and 3, and 100 percent ownership of the gas- and oil-fired stations. The Prager, Santa Fe, and Las Vegas Stations are used primarily to meet peak loads.

In 1979 PNM's generating fuel was mostly coal, accounting for about 67 percent of total kilowatt-hours produced. Natural gas provided 31.5 percent and oil 1.5 percent. With the addition of 240 megawatts of coal-fired capacity from San Juan Unit 3 in December of 1979, PNM's forecasted generation requirements from coal will rise to 83 percent, with natural gas and oil providing 15.8 percent and 1.2 percent, respectively, in 1980.

PNM through its operating divisions provides electric service to about half the people living in New Mexico. The Albuquerque Division service area includes roughly a third of the population of the entire state. The Belen and Bernalillo Divisions serve the rapidly growing areas south and north of Albuquerque, respectively. The Santa Fe Division serves the State Capital and surrounding communities. The Las Vegas Division serves Las Vegas on the eastern slopes of the Sangre de Cristo Mountains in north-central New Mexico. The Deming Division service area lies in the extreme southern portion of the state, just north of the Mexican border. The Western Division serves a portion of the uranium and coal mining areas west of Albuquerque.

In addition to the operating divisions, PNM-generated electricity is purchased by several other utilities, both publicly and privately owned, for distribution to their customers within the state.

As a regulated business, PNM operates under franchise agreements. Municipal electric franchise expiration dates are as follows: Albuquerque — 1992, Belen — 1990, Bernalillo — 1998, Deming — 1993, Las Vegas — 1996, and Santa Fe — 1999.

Water Operations

Water service in Santa Fe and Las Vegas is also provided by PNM. The water facilities were acquired along with the Santa Fe and Las Vegas electric systems many years ago.

During the year, PNM reached agreement with the City of Santa Fe resulting in a new water franchise. Resolution of conflicting points of view expressed by the City, PNM, and Santa Fe County was gained by further expansion of the duties of the Metropolitan Water Board. In an area where water is a critical resource and a key to development, the Board will serve as a way for the three parties to combine their expertise and meet the long-term needs for all concerned.

In large part, the credit for the success of the negotiations which resulted in the franchise agreement belongs to the PNM employees in Santa Fe. Their abilities and persistence turned a difficult situation into one of cooperation for the long-term future of water supply in Santa Fe. The new water franchise for Santa Fe will be in effect until the year 2004. The water franchise for Las Vegas expires in 1993.

The Future

Construction and Financing

Capital expenditures in 1980 are expected to drop to about $299 million, the major portion of which is for the construction of the fourth generating unit at San Juan and the three units at the Palo Verde Nuclear Generating Station in Arizona. To provide funds for the 1980 construction program, your company anticipates that it will offer up to $50 million of preferred stock in April and approximately $60 million of common stock during the second half of the year. PNM also expects to raise approximately $14 million through its internal stock programs.

In addition to the January receipt of the $28 million from the private placement first mortgage bond transaction, the Company's current financing plan also includes a first mortgage issue of approximately $60 million during the second half of the year. Use of approximately $77 million of low-cost pollution control revenue bonds currently held in trust is planned. Funding requirements will also be provided for by continued use of short-term debt. Additionally, your Company plans to participate with the City of Farmington in the issue of $26 million in pollution control revenue bonds for environmental control structures at the Four Corners Generating Station.

PNM's planned construction program over the next five years is estimated to be $1,084 million. Of this amount, approximately $593 million is for generation-related construction, including nuclear fuel, land and water acquisitions, with an additional $187 million for environmental control systems. The majority of this money is for continuing construction at the San Juan Generating Station, the Palo Verde Nuclear Generating Station in Arizona, a large pumped storage project, and PNM's interest in additional pollution control equipment for the Four Corners Generating Station. The balance of the $1,084 million will be spent over the next five years on transmission and distribution systems plus additional operating facilities for both electric and water customers. Additionally, PNM's wholly owned subsidiary, Paragon Resources, Inc., has a five-year capital expenditure program of $48 million, with about $15 million in 1980, primarily for developments related to future generation projects.

Sales and Rate Activities

Total system requirements in 1980, including sales to wholesale customers, are projected to increase by 15.8 percent. Total peak demand is projected to grow by 15.4 percent. The forecasted peak demand for the summer of 1980 is 987 megawatts. To supply this peak demand and maintain an adequate reserve margin for contingencies, PNM has a total installed capacity of 1,082 megawatts (11 megawatts of which is scheduled for retirement in early 1980, subject to a current review) and has contractually arranged to purchase an additional 160 megawatts of capacity from other utilities plus a projected eight megawatts from load management for resource capacity of 1,239 megawatts.

During the fourth quarter of 1979, PNM and the Los Angeles Department of Water and Power completed negotiations for the sale of firm surplus energy from San Juan Station to Los Angeles. Final contracts, signed in January 1980, provide for the sale of 700,000 megawatt-hours until April 1982.

In January 1980, your Company completed contract negotiations with San Diego Gas and Electric Company for the sale of contingent capacity from San Juan Station. This delivery of energy is contingent on the availability of the four units at San Juan and Palo Verde Unit 1. The contract specifies the sale of 236 megawatts each year over a six-year period (a total of about 8.6 million megawatt-hours of energy) commencing with the in-service date of San Juan Unit 4, anticipated to be May 1982.

As a result of the purchase of Tucson Electric Power Company's share of San Juan Unit 4, and the contingent sale of power from this unit to San Diego Gas and Electric during 1982 1987, PNM has not only assured availability of electricity to its customers into the 1990's, but additionally has been able to accomplish this at capacity costs of the 1970's rather than the late 1980's. The savings to PNM's customers will be substantial.

According to the schedule set by the NMPSC, PNM has filed a new Cost of Service Indexing factor which will be collected subject to refund beginning on March 21, 1980, while the NMPSC decides the case. The factor reflects increased costs PNM experienced during 1979.

In the near future, PNM will submit revised rates to the Federal Energy Regulatory Commission for wholesale customers based on test year 1980 budgeted operating data. Final decisions in pending cases have not yet been issued; however, the rates have been put into effect subject to refund.

The Company and Its People

Employees are PNM's most important asset. The employees work together to provide customers not only with the reliable service they expect today, but employees also test and implement new ideas and plans for dependable service in the years ahead.

During 1979 PNM added 257 additional employees. Although the Company's continued growth accounted for some of the increase, it was growing regulatory and environmental requirements which accounted for much of the increase. Effective environmental performance requires that the Company constantly monitor power plant emissions and maintain the necessary pollution control equipment. Detailed environmental studies are now required to support the construction of new generation and transmission facilities. To encourage energy conservation and to meet the requirements of the Public Utilities Regulatory Policies Act, personnel were added to provide additional assistance to customers and prepare studies for submission to appropriate agencies. The continued effect of these various activities on the total number of employees was significant.

PNM continues its tradition of attracting very talented and highly skilled new employees necessary to keep pace with customer needs. Of the 2,311 employees, almost 850 craft personnel are represented by Local Union 611 of the International Brotherhood of Electrical Workers. The PNM-IBEW contract expires April 30, 1981.

Employee Development

A total of 1,730 employees participated in Company-sponsored training programs during the 12-month period. Additional programs assisting employees wishing to further their education and job skills at local schools and universities are also offered.

Employee Benefits

As part of a continuing effort to retain skilled and trained employees as well as to attract new personnel, benefits, including life, health, and dental insurance as well as retirement plans, have been upgraded. Employee wages during 1979 stayed within the President's salary guidelines with isolated exceptions receiving prior approval by the federal government.

Promotions and Management Changes

An expressed principle of the Company is to promote from within its own ranks whenever practical. As a company operating in a growth mode, many jobs become available. During 1979, 877 employees were promoted to positions of higher responsibility.

The Company's Board of Directors elected two employees to vice president positions and promoted a third employee to Treasurer in April of 1979.

P. J. Archibeck was promoted to Treasurer from his previous position as Assistant Treasurer.

T. P. Warnke was elected District Vice President of PNM's San Juan area. Mr. Warnke, a former manager of PNM's Deming Division, previously served as manager of the San Juan area.

J. L. Wilkins was elected Vice President of Engineering and Construction. A past chairman of the National Electric Reliability Council, Mr. Wilkins previously was group manager of engineering and construction.

Subsidiaries

PNM has an interest in two subsidiaries, Paragon Resources, Inc. (formerly Public Service Land Company) and Western Coal Co. Paragon Resources, Inc. is a wholly owned subsidiary, organized to secure water rights and property for the Company's various projects and business-related needs. Chief among these needs are plant sites and water for Company water systems and for cooling purposes at generating plants.

Western Coal Co. is jointly owned by PNM and Tucson Electric Power Company. The purpose of Western Coal Co. is to secure coal leases and provide fuel for San Juan Generating Station. The San Juan Generating Station has contracted with Western Coal Co. to supply all coal required for the life of the plant.

Research, Development and Demonstration

PNM is involved in a number of research, development, and demonstration projects designed to increase Company operating efficiency, expand

knowledge in energy use and alternatives, and protect the environment.

- Because water resources are scarce in New Mexico, PNM is evaluating treatment procedures necessary for water to be recovered from uranium mining activities for use in generating station applications.

- PNM is investigating the economic recovery of deep seam Fruitland Formation coal at depths below strippable levels, using underground coal gasification technology.

- Numerous solar research projects are underway including the performance of both passive and active solar residential and commercial systems plus water heating applications. PNM is also participating with Western Energy Supply and Transmission Associates (WEST) in the nation's largest solar monitoring project which will provide an excellent data base for future solar projects.

- PNM is also studying the effect of transmission lines on birds of prey and their habitats. This nationally recognized study will be completed in early 1980.

- At San Juan, PNM is developing techniques for remote measurement of visible and invisible power plant plumes. This project is also funded by WEST. PNM is also testing the use of ceramic-lined pipe sections in an effort to find ways to increase abrasion resistance in coal-handling systems at San Juan.

- An improved computer-assisted planning tool is being developed to enhance PNM engineers' ability to evaluate system distribution plans and alternatives.

- In the area of nonconventional electric generation, PNM, along with the Department of Energy and Union Oil Co., is constructing the nation's first hot water geothermal generating facility. When completed, this demonstration plant will produce 50 megawatts. Ultimately, the geothermal field could produce about 400 megawatts. The Company is also in the beginning phase of work on a pumped storage facility which, when completed in 1989, will produce about 600 megawatts.

- In 1980, Company load management engineers will join with private individuals in the Deming area to construct a vertical wind axis generator for use in irrigation and rural homes.

- Subsynchronous resonance, hardly a household word, is very important to utilities. The problem lies in vibrations created by transmission lines which can damage the power plant turbine-generator. PNM and ten other western utilities contracted with General Electric and Westinghouse in 1978 to develop a relay that could sense the vibrations and disconnect the generator before any damage could be done. As a result of this study, two relays were installed at the San Juan Generating Station in 1979 — the first of their kind in the country. Additional equipment is scheduled to be installed in 1980.

- Another major project during 1978 and 1979 was the High Silica Control Project. This involved experimentation with a new chemical to disperse silica in the water that normally collects as scale on heat transfer surfaces of power plant equipment, thereby reducing plant efficiency and causing the plant to use more water. The experiment carried out at Albuquerque's Person Generating Station resulted in saving one million gallons of water per day on just one unit.

A test tunnel has been completed for PNM's hydroelectric pumped storage project.

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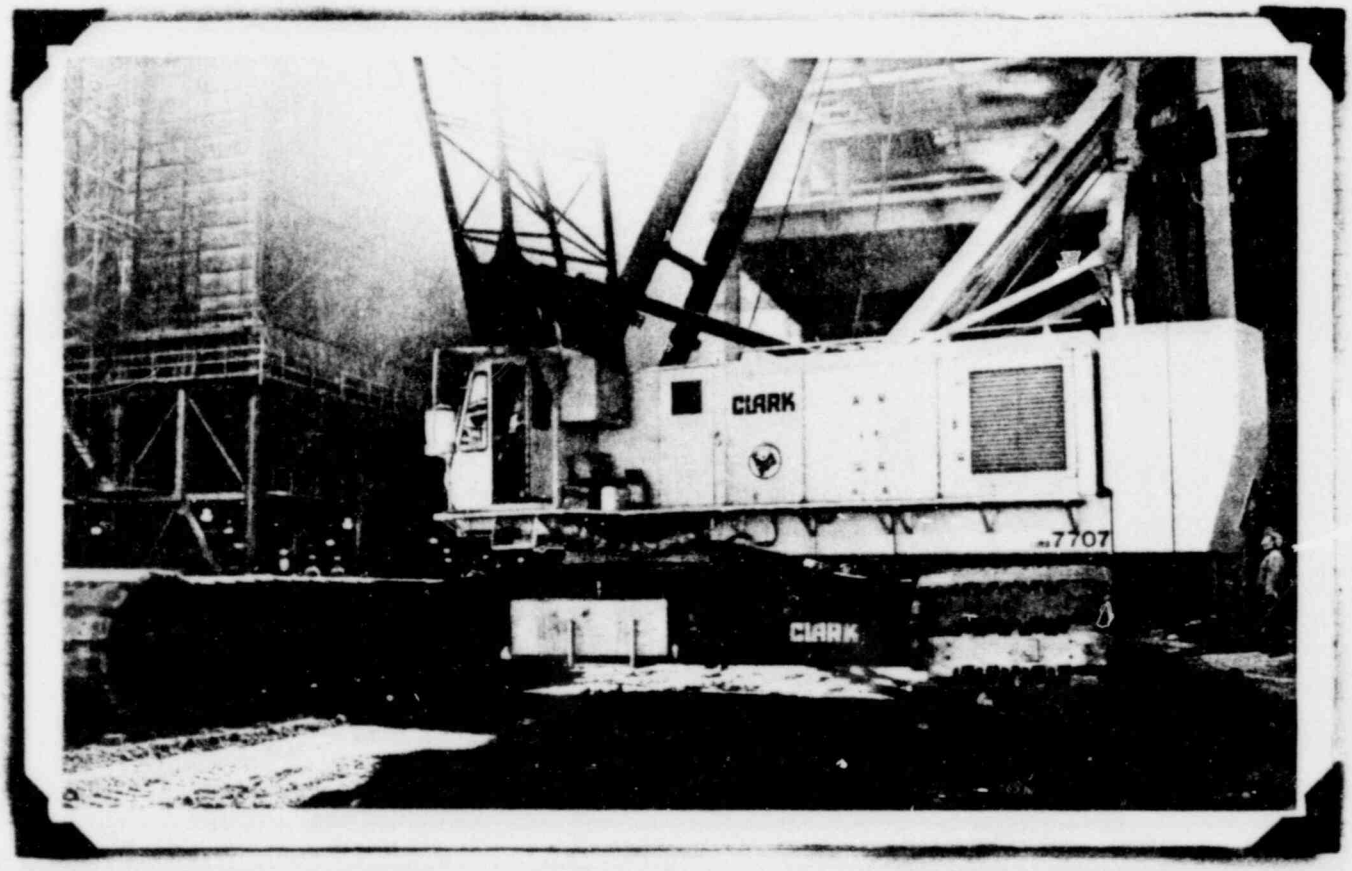


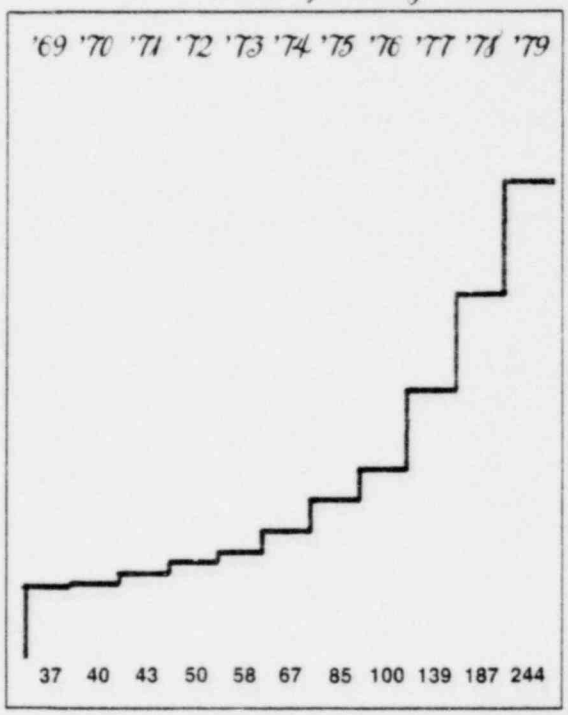
With the completion of Unit 3 in 1979, construction now centers on San Juan Unit 4.

Growth Graphs

Gross Plant Investment

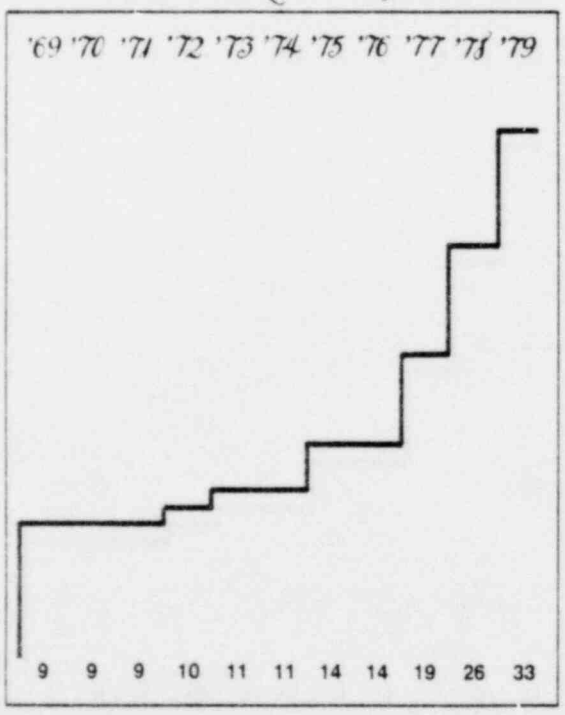
MILLIONS OF DOLLARS

Total Operating Revenues



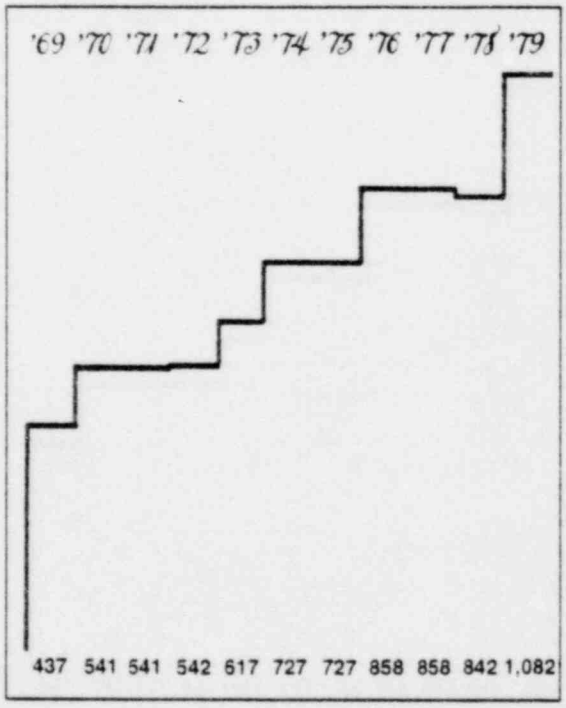
MILLIONS OF DOLLARS

Federal, State, Local and General Taxes



MILLIONS OF DOLLARS

Net Generating Capability



THOUSANDS OF KILOWATTS

Comparative Operating Statistics

	1979	1978	1977	1976
ELECTRIC SERVICE				
ENERGY SALES—kWhr (in thousands)				
Residential	1,067,755	1,000,564	957,390	916,748
Commercial	1,403,282	1,353,805	1,320,651	1,277,025
Industrial	858,533	797,314	686,845	605,559
Other ultimate customers	159,396	164,901	160,922	157,694
Total sales to ultimate customers	3,488,966	3,316,584	3,125,808	2,957,026
Sales for resale	1,471,485	1,211,242	1,241,195	638,207
Total energy sales	4,960,451	4,527,826	4,367,003	3,595,233
ELECTRIC REVENUES (in thousands)				
Residential	$ 66,262	$ 51,414	$ 39,547	$ 32,423
Commercial	77,806	60,125	45,520	36,198
Industrial	40,467	28,860	18,918	13,070
Other ultimate customers	8,704	7,052	5,215	4,168
Total revenue from ultimate customers	193,239	147,451	109,200	85,859
Sales for resale	44,000	32,568	23,219	9,340
Total revenue from energy sales	237,239	180,019	132,419	95,199
Miscellaneous electric revenues	2,532	2,581	2,605	1,935
Total electric revenue	$ 239,771	$ 182,600	$ 135,024	$ 97,134
CUSTOMERS AT YEAR END				
Residential	184,979	175,439	164,803	156,116
Commercial	20,334	19,496	18,374	17,483
Industrial	485	482	493	489
Other	264	263	265	250
Total ultimate customers	206,062	195,680	183,935	174,338
Sales for resale	5	5	5	5
Total customers	206,067	195,685	183,940	174,343
Reliable net capability — kW	1,082,000	842,000	858,000	858,000
Coincidental peak demand — kW	855,000	809,000	715,000	633,000
Average fuel cost per million BTU	120.72¢	105.52¢	92.74¢	61.83¢
BTU per kWhr of net generation	10,476	10,993	11,004	11,084
WATER SERVICE				
SALES — Gallons (in thousands)				
Customer sales	2,509,868	2,747,924	2,726,059	2,959,209
Interdepartmental sales	5,947	5,198	5,742	4,014
Total water sales	2,515,815	2,753,122	2,731,801	2,963,223
REVENUES (in thousands)				
Customer sales	$ 4,595	$ 4,599	$ 3,606	$ 2,386
Interdepartmental sales	4	6	6	3
Total water sales	$ 4,599	$ 4,605	$ 3,612	$ 2,389
Customers at year end	18,755	18,079	17,427	16,838

(1) Reclassified against expense

(2) Certain customers were reclassified from commercial to industrial during 1975. The reclassification accounted for a change of 220 customers in both categories.

1975	1974	1973	1972	1971	1970
875,361	828,243	786,108	706,973	648,626	583,136
1,177,953	1,128,576	1,110,147	985,431	885,782	792,376
530,188	549,622	616,405	653,761	618,695	552,118
136,136	137,843	128,171	123,568	116,202	107,598
2,719,638	2,644,284	2,640,831	2,469,733	2,269,305	2,035,228
578,037	250,901	122,656	114,333	106,000	98,026
3,297,675	2,895,185	2,763,487	2,584,066	2,375,305	2,133,254
$ 28,912	$ 23,314	$ 20,552	$ 17,760	$ 15,295	$ 13,910
30,851	25,403	22,283	19,421	16,309	14,784
9,993	8,349	7,210	7,229	6,549	5,963
3,361	3,004	2,613	2,204	1,994	2,056
73,117	60,070	52,658	46,614	40,147	36,713
8,241	2,782	1,074	937	857	778
81,358	62,852	53,732	47,551	41,004	37,491
1,412	2,406	2,803	795	670	621
$ 82,770	$ 65,258	$ 56,535	$ 48,346	$ 41,674	$ 38,112
151,111	147,516	143,201	136,515	127,911	120,865
16,738(2)	16,469	16,241	15,754	14,775	13,908
515(2)	298	295	303	308	300
246	231	229	221	205	201
168,610	164,514	159,966	152,793	143,199	135,274
4	4	3	3	3	3
168,614	164,518	159,969	152,796	143,202	135,277
727,000	727,000	617,000	542,000	540,700	540,700
586,000	583,400	533,000	491,700	458,700	400,600
47.23¢	39.49¢	26.16¢	24.47¢	23.55¢	23.04¢
10,848	11,054	11,017	10,841	10,870	11,058
2,859,783	3,013,508	2,855,673	2,781,854	2,563,745	2,564,580
9,195	12,568	10,710	3,638	1,707	1,782
2,868,978	3,026,076	2,866,383	2,785,492	2,565,452	2,566,362
$ 2,205	$ 2,103	$ 1,567	$ 1,530	$ 1,434	$ 1,418
3	6	3	(1)	1	1
$ 2,208	$ 2,109	$ 1,570	$ 1,530	$ 1,435	$ 1,419
16,437	16,158	15,848	15,454	15,024	14,495

Summary of Operations

	1979	1978	1977	1976	1975
		(In thousands except per share amounts)			
Total operating revenues	$244,370	$187,205	$138,636	$99,523	$84,978
Operating expenses:					
Operation and maintenance	134,539	103,864	76,524	51,535	39,785
Provision for depreciation and amortization	17,603	14,451	11,464	9,548	8,650
Taxes, other than income taxes	10,531	8,221	7,257	5,875	5,114
Income taxes	21,881	16,722	10,986	8,028	8,626
Total operating expenses	184,554	143,258	106,231	74,986	62,175
Operating income	59,816	43,947	32,405	24,537	22,803
Allowance for equity funds used during construction	15,594	10,541	6,218	4,109	1,583
Other income and deductions, net	2,401	2,257	1,435	689	530
Income before interest charges	77,811	56,745	40,058	29,335	24,916
Net interest charges	23,008	19,281	15,137	11,978	10,700
Net earnings	54,803	37,464	24,921	17,357	14,216
Preferred stock dividend requirements	12,196	8,384	6,285	4,194	2,952
Net earnings applicable to common stock	$ 42,607	$ 29,080	$ 18,636	$13,163	$11,264
Average number of shares outstanding	14,363	10,289	7,569	6,106	4,609
Per share amounts:					
Net earnings	$ 2.97	$ 2.83	$ 2.46	$ 2.16	$ 2.44
Dividends	$ 1.88	$ 1.72	$ 1.61	$ 1.42	$ 1.26

Management's Discussion and Analysis of the Summary of Operations

The following factors, which may not be indicative of future operations or earnings, have had a significant effect upon the Company's results of operations during the years 1978 and 1979.

Electric revenues increased $47.6 million in 1978 and $57.2 million in 1979. The principal factors causing these increases are as follows:

	1979	1978
Increase in electric revenues due to:	(In thousands)	
Increased kWhr sales (a)	$14,660	$ 4,584
Increased base rates (b)	27,597	29,912
Increased fuel cost adjustment factor (c)	14,963	13,104
	$57,220	$47,600

(a) kWhr sales—the number of customers increased in each period and the average use per customer decreased in 1978 but increased in 1979. Increases in kWhr sales were 3.7% in 1978 and 9.6% in 1979.

(b) Rate increases—the Company bills most customers under a Cost of Service Index order based upon the jurisdictional return on common equity. The Index order, formerly a quarterly adjustment, was revised to provide for annual adjustments to base rates effective May 15, 1979. The Company has periodically negotiated higher rates with certain customers whose rates are subject to the jurisdiction of the Federal Energy Regulatory Commission (FERC). New rates for such customers were filed with the FERC and accounted for revenues, net of recorded provisions for possible refund, of $6.7 million in 1978 and $9.9 million in 1979 which are subject to refund pending a determination by the FERC. Accumulated revenues subject to refund, net of provisions for refund, at December 31, 1979 are $18.3 million.

(c) Fuel cost adjustment—natural gas fuel costs, cost of coal per ton and purchased power have accelerated rapidly. Such costs are passed on to customers.

Water revenues increased $1.0 million in 1978 as a result of rate increases allowed by the New Mexico Public Service Commission (Commission).

Operation and maintenance expenses increased $27.3 million in 1978 and $30.7 million in 1979. Principal causes are:

(a) Production of energy from the Company's own generating units decreased by 14.3% in 1978 but increased by 16.3% in 1979. A boiler explosion, causing the shutdown of the first unit at the San Juan Generating Plant in July 1977 and the return to service of the unit in May 1978, coupled with the purchase of lower cost energy on the interchange market rather than generating from the Company's gas and oil fired units, resulted in the Company being a net purchaser of 957 million kWhr in 1978. Although generation increased in 1979, the growth in kWhr sales resulted in the Company being a net purchaser of 752 million kWhr. Increased fuel and purchased power expenses resulting from the boiler explosion were $6.9 million for the entire period of the outage. Of such expenses $6.6 million were passed on to customers through the fuel adjustment clause by approval of the Commission and are subject to refund if it is determined that the Company was responsible for the explosion.

(b) Rapidly accelerating fuel costs.

(c) Higher cost of labor and related benefits due to higher wage rates and an increase in the number of employees necessary to operate the expanded electric generating and water facilities.

(d) General inflationary factors.

(e) Maintenance and repair expenses increased by $3.0 million in 1978 and $1.9 million in 1979. Overhauls and inspections at Person Station, the Four Corners plant and the San Juan plant accounted for increased costs of $2.4 million in 1978 and $1.3 million in 1979.

The Company's gross utility plant increased by approximately 29% in 1978 and 36% in 1979 as a result of expanded operations, the need to maintain reliable service and increasing environmental protection requirements. In addition, the Company purchased the fifty-percent undivided interest of Tucson Electric Power Company in San Juan Unit 4. This increase in utility plant and the Company's construction program have been the primary causes of increases experienced in the following areas of operations:

(a) Depreciation and amortization.

(b) Taxes, other than income taxes—increases in ad valorem taxes resulted from increased plant.

(c) Allowance for funds used during construction—increased construction at the San Juan plant and the Palo Verde Nuclear Generating Station.

(d) Interest charges and preferred stock dividend requirements—from 1977 through 1979 the Company issued $112 million principal amount of first mortgage bonds, utilized $147 million of proceeds of pollution control revenue bonds and issued $86 million of preferred stock, generally at higher rates than previous issues, and had up to $96 million principal amount of short-term debt outstanding.

Other income and deductions, net, increased $.8 million in 1978 primarily because the Company's share of earnings of its fifty-percent-owned subsidiary increased due to increased coal deliveries to the San Juan plant and an increase in the price per ton delivered.

As a result of items detailed above, earnings before income taxes, income taxes, net earnings and earnings per share of common stock all increased in 1978 and 1979.

Consolidated Balance Sheet

December 31, 1979 and 1978

Assets

	1979	1978
	(In thousands)	
Utility plant, at original cost (notes 4 and 8):		
Electric plant in service	$ 712,096	$462,621
Water plant in service	31,639	30,284
Common plant in service	17,340	14,148
	761,075	507,053
Less accumulated depreciation and amortization	127,939	102,033
	633,136	405,020
Construction work in progress	435,353	371,754
Electric plant held for future use	1,086	1,086
Net utility plant	1,069,575	777,860
Other property and investments:		
Non-utility property, at cost, net of accumulated depreciation of $757,000 in 1979 and $456,000 in 1978	17,362	9,516
Investment in fifty-percent-owned company	6,111	3,895
Other, at cost	1,875	1,747
Total other property and investments	25,348	15,158
Current assets:		
Cash (note 5)	3,810	1,929
Receivables:		
Customers	23,818	18,835
Other	13,809	18,231
Allowance for doubtful receivables	(224)	(106)
Fuel, materials and supplies, at average cost	22,073	16,015
Prepaid expenses	2,040	1,116
Deferred fuel costs	11,322	11,875
Total current assets	76,648	67,895
Deferred charges:		
Construction advance	—	17,037
Unamortized debt expense	6,918	5,364
Other deferred charges	7,957	5,433
Total deferred charges	14,875	27,834
	$1,186,446	$888,747

See accompanying notes to consolidated financial statements.

Capitalization and Liabilities

	1979	1978
	(In thousands)	
Capitalization:		
Common stock equity (note 2):		
Common stock of $5 par value. Authorized 20,000,000 shares; outstanding 15,601,739 shares in 1979 and 12,642,233 shares in 1978	$ 78,009	$ 63,211
Additional paid-in capital	185,600	145,433
Retained earnings	83,719	67,645
Total common stock equity	347,328	276,289
Cumulative preferred stock. Authorized 5,000,000 shares (note 3):		
Without mandatory redemption requirements. Outstanding 860,000 shares of $100 stated value and 800,000 shares of $25 stated value	106,000	106,000
With mandatory redemption requirements. Outstanding 400,000 shares of $100 stated value in 1979.	40,000	—
Long-term debt, less current maturities (notes 4 and 11)	431,655	356,347
Total capitalization	924,983	738,636
Current liabilities:		
Short-term debt (note 5)	95,960	23,805
Accounts payable	51,695	43,072
Preferred dividends declared	2,869	1,994
Current maturities of long-term debt (note 4)	5,224	1,189
Accrued interest	5,577	4,424
Accrued taxes	9,418	7,191
Other current liabilities.	4,220	4,226
Total current liabilities	174,963	85,901
Deferred credits:		
Customer advances for construction	7,180	5,603
Accumulated deferred investment tax credits (note 6)	47,896	36,224
Accumulated deferred income taxes (note 6)	22,529	17,980
Other deferred credits	8,895	4,403
Total deferred credits	86,500	64,210
Commitments and contingencies (notes 8, 9 and 10)		
	$1,186,446	$888,747

Consolidated Statement of Earnings

Years ended December 31, 1979 and 1978

	1979	1978
	(In thousands except per share amounts)	
Operating revenues:		
Electric (note 10)	$239,771	$182,600
Water	4,599	4,605
Total operating revenues	244,370	187,205
Operating expenses:		
Fuel and purchased power	85,143	62,694
Other operation expenses	34,351	28,002
Maintenance and repairs	15,045	13,168
Provision for depreciation and amortization	17,603	14,451
Taxes, other than income taxes	10,531	8,221
Income taxes (note 6)	21,881	16,722
Total operating expenses	184,554	143,258
Operating income	59,816	43,947
Other income and deductions:		
Allowance for equity funds used during construction	15,594	10,541
Equity in earnings of fifty-percent-owned company, net of taxes (note 6)	2,151	1,498
Other, net of taxes (note 6)	250	759
Net other income and deductions	17,995	12,798
Income before interest charges	77,811	56,745
Interest charges:		
Interest on long-term debt	24,236	21,349
Amortization of debt discount, expense and premium	394	347
Other interest charges	4,302	1,668
Allowance for borrowed funds used during construction	(5,924)	(4,083)
Net interest charges	23,008	19,281
Net earnings	54,803	37,464
Preferred stock dividend requirements	12,196	8,383
Net earnings applicable to common stock	$ 42,607	$ 29,081
Average number of shares outstanding	14,363	10,289
Per share amounts:		
Net earnings	$ 2.97	$ 2.83
Dividends	$ 1.88	$ 1.72

See accompanying notes to consolidated financial statements.

Consolidated Statement of Capitalization

Years ended December 31, 1979 and 1978

	1979	1978	Percentages 1979	Percentages 1978
	(In thousands)			
Common stock equity:				
Common stock:				
Balance at beginning of year	$ 63,211	$ 44,287		
Issuance of common stock	14,798	18,924		
Balance at end of year	78,009	63,211		
Additional paid-in capital:				
Balance at beginning of year	145,433	90,947		
Premium on common stock issued	42,466	57,241		
Expenses of stock issuance	(2,299)	(2,755)		
Balance at end of year	185,600	145,433		
Retained earnings:				
Balance at beginning of year	67,645	56,213		
Net earnings	54,803	37,464		
	122,448	93,677		
Cash dividends:				
Cumulative preferred stock	12,196	8,383		
Common stock	26,533	17,649		
	38,729	26,032		
Balance at end of year	83,719	67,645		
Total common stock equity	347,328	276,289	37.5%	37.4%
Cumulative preferred stock:				
Without mandatory redemption requirements:				
Balance at beginning of year	106,000	80,000		
Issuance of preferred stock	—	26,000		
Balance at end of year	106,000	106,000	11.5	14.4
With mandatory redemption requirements:				
Balance at beginning of year	—	—		
Issuance of preferred stock	40,000	—		
Balance at end of year	40,000	—	4.3	—
Long-term debt, less current maturities:				
Balance at beginning of year	356,347	244,721		
Addition to long-term debt	82,763	114,561		
Reduction of long-term debt	(6,544)	(2,305)		
Net change in unamortized discount and premium	(911)	(630)		
Balance at end of year	431,655	356,347	46.7	48.2
Total capitalization at end of year	$924,983	$738,636	100.0%	100.0%
Number of shares issued:				
$100 stated value cumulative preferred stock	400	260		
Common stock	2,960	3,785		

See accompanying notes to consolidated financial statements.

Consolidated Statement of Changes in Financial Position

Years ended December 31, 1979 and 1978

	1979	1978
	(In thousands)	
Funds provided:		
Net earnings	$ 54,803	$ 37,464
Charges (credits) to earnings not requiring funds:		
Depreciation and amortization	19,128	15,510
Provision for noncurrent deferred income taxes, net	4,549	1,149
Investment tax credit, net	11,672	10,378
Allowance for equity funds used during construction	(15,594)	(10,541)
Undistributed earnings of fifty-percent-owned company	(2,216)	(1,621)
Funds derived from operations	72,342	52,339
Sale of first mortgage bonds	17,000	65,000
Sale of cumulative preferred stock	40,000	26,000
Proceeds from pollution control revenue bonds	62,166	48,818
Sale of common stock	57,264	76,165
Proceeds from other long-term debt	3,597	743
Proceeds from short-term debt	290,315	142,280
Decrease in deferred charges	12,405	—
Utility plant retirements, net of removal costs	14,137	809
Decrease in working capital other than short-term debt	8,154	—
Other	6,113	4,086
	$583,493	$416,240
Funds used:		
Cash dividends	$ 38,729	$ 26,032
Utility plant additions	308,526	189,307
Payment of short-term debt	218,160	168,475
Reduction of long-term debt	6,544	2,305
Additions to non-utility property	8,157	—
Increase in deferred charges	—	22,316
Increase in working capital other than short-term debt	—	4,400
Other	3,377	3,405
	$583,493	$416,240
Changes in working capital other than short-term debt:		
Cash	$ 1,881	$ (3,708)
Receivables	443	15,140
Fuel, materials and supplies	6,058	1,801
Prepaid expenses	924	(115)
Deferred fuel costs	(553)	4,747
Accounts payable	(8,623)	(9,877)
Preferred dividends declared	(875)	(572)
Current maturities of long-term debt	(4,035)	176
Accrued interest	(1,153)	(832)
Accrued taxes	(2,227)	(3,035)
Other current liabilities	6	675
Increase (decrease) in working capital other than short-term debt	$ (8,154)	$ 4,400

See accompanying notes to consolidated financial statements.

Notes to Consolidated Financial Statements

December 31, 1979 and 1978

(1) Summary of Significant Accounting Policies

System of Accounts —

The Company maintains its accounting records in accordance with the uniform system of accounts prescribed by the Federal Energy Regulatory Commission (FERC) and adopted by the New Mexico Public Service Commission (Commission). As a result of the rate-making process, the application of generally accepted accounting principles by the Company differs in certain respects from the application by nonregulated businesses. Such differences generally regard the time at which certain items enter into the determination of net earnings in order to follow the principle of matching costs and revenues.

Principles of Consolidation —

The consolidated financial statements include the accounts of the Company and its wholly-owned subsidiary, Paragon Resources, Inc. (formerly Public Service Land Company). All significant intercompany transactions have been eliminated.

Utility Plant —

Utility plant is stated at original cost, which includes payroll-related costs such as taxes, pensions and other fringe benefits, administrative costs and an allowance for funds used during construction. Contributions received from customers to meet the customers' special construction requirements are credited to utility plant.

It is Company policy to charge repairs and minor replacements of property to maintenance expense and to charge major replacements to utility plant. Gains or losses resulting from retirements or other dispositions of operating property in the normal course of business are credited or charged to the accumulated provision for depreciation.

Allowance for Funds Used During Construction (AFUDC) —

In accordance with the uniform system of accounts, AFUDC, a noncash income item, is charged to utility plant. The Commission ordered that AFUDC be limited to generating plant construction, effective April 22, 1975. The Commission further ordered, effective May 15, 1979, that the rate be increased from the previously approved 6.5% to 7.5% and allowed the Company to eliminate the recording of AFUDC on Unit 3 at the San Juan Generating Station and on pollution control plant associated with all San Juan units. The allowance for equity funds used during construction is credited to other income and deductions and the allowance for borrowed funds used during construction is credited to interest charges. The allocation of AFUDC between borrowed funds, after taxes, and equity funds is based on the method required by FERC.

Depreciation —

Provision for depreciation of utility plant is made at annual straight-line rates approved by the Commission. The average depreciation rates used were as follows:

	1979	1978
Electric plant	3.62%	3.39%
Water plant	1.88%	1.89%
Common plant	7.13%	5.89%

The provision for depreciation and amortization of certain equipment, including amortization applicable to capital leases, is charged to clearing accounts along with other costs of operation and subsequently apportioned to operating expenses and property accounts based on the use of the equipment. Depreciation of non-utility property is computed on the straight-line method.

Investment in Fifty-Percent-Owned Company —

The Company's investment in a fifty-percent-owned company is stated at equity. The co-owner, Tucson Electric Power Company, is participating with the Company in the construction and operation of a steam turbo-electric generating plant described in note (8). The generating plant utilizes coal from properties of the fifty-percent-owned company as a source of fuel.

Deferred Fuel Costs —

The Company uses the deferred method of accounting for the portion of fuel costs which is recoverable in subsequent periods under fuel adjustment clauses.

Amortization of Debt Discount, Expense and Premium —

Discount, expense and premium incurred in the issuance of the presently outstanding debt are being amortized by charges to income over the lives of the respective issues on the debt outstanding method.

Investment Tax Credits —

The Company follows the practice of deferring investment tax credits and amortizes them over the estimated useful lives of the related properties. Investment tax credit carryforwards are recorded to the extent of the sum of the investment tax credits which would have been realized if taxes payable had been based on pretax accounting income adjusted for permanent differences and the existing net deferred tax credits which would reverse during the investment tax credit carryforward period.

Income Taxes —

Certain revenue and expense items in the Consolidated Statement of Earnings are recorded in a year different from the year in which they are recorded for income tax purposes. Deferred income taxes are provided on these timing differences to the extent allowed for rate-making purposes. This normalization method is used primarily for differences attributable to deferred fuel costs, the use of liberalized depreciation methods and different lives under the asset depreciation range (ADR) than under the guideline depreciation provisions. Certain other differences result in a reduction in income tax expense in the current year. This flow-through method is used primarily for differences between tax depreciation computed under the guideline life provisions and book depreciation and certain capitalized construction costs, principally AFUDC, deducted currently for income tax purposes.

At present, rates applicable to certain customers subject to FERC control allow recovery of amounts necessary to provide additional tax normalization of the items described above which are accounted for under the flow-through method for other customers. Provision has been made for additional deferred income taxes attributable to amounts collected under these rates.

Revenues —

Revenues are recognized based on cycle billings rendered to customers monthly. The Company does not accrue revenues for services provided but not billed at the end of a fiscal period.

Pension Plan —

The Company's policy is to fund pension costs which are composed of normal costs and amortization of prior service costs over thirty years.

(2) Common Stock Equity

The Board of Directors reserved 2,000,000 shares of unissued common stock for the dividend reinvestment program, the Employee Stock Purchase Plan and the Tax Reduction Act Stock Ownership Plan, of which 1,229,413 shares remained unissued at December 31, 1979.

Charter provisions relating to the cumulative preferred stock and the indenture securing the first mortgage bonds impose certain restrictions upon the payment of cash dividends on common stock of the Company. At December 31, 1979, there were no retained earnings restricted under such provision.

(3) Cumulative Preferred Stock

The cumulative preferred stock may be redeemed by the Company, upon thirty days notice thereof, at stated redemption prices (plus accrued and unpaid dividends). Information concerning the cumulative preferred stock is as follows:

Series	*Stated Value*	*Shares Outstanding*	*Aggregate Stated Value (In thousands)*	*Stated Redemption Price (a)*
Without mandatory redemption requirements:				
1965 Series, 4.58%	$100	130,000	$ 13,000	$102.516
1974 Series, 9.2%	100	170,000	17,000	107.00
1975 Series, 10.12% (b)	100	100,000	10,000	110.12
9.16% Series (b)	25	800,000	20,000	27.29
8.48% Series (b)	100	200,000	20,000	108.48
8.80% Series (b)	100	260,000	26,000	108.80
		1,660,000	$106,000	
With mandatory redemption requirements:				
8.75% Series (b) (c)	100	400,000	$ 40,000	108.75

(a) Redemption prices are at reduced premiums in future years.

(b) Redemption may not be made through certain refunding operations prior to March 15, 1980 for the 1975 Series, or prior to June 1, 1981 for the 9.16% Series, or prior to April 1, 1982 for the 8.48% Series, or prior to April 1, 1983 for the 8.80% Series, or prior to February 1, 1984 for the 8.75% Series.

(c) On February 1, 1984 and on each February 1 thereafter, the Company shall redeem 13,000 shares of the 8.75% Series, pursuant to a mandatory sinking fund at a redemption price of $100 per share plus accrued and unpaid dividends.

(4) Long-Term Debt

The details of the Company's outstanding long-term debt including unamortized discount and premium, less current maturities, are as follows:

Issue and Maturity	*Interest Rates*	*1979*	*1978*
		(In thousands)	
First Mortgage Bonds:			
1980 through 1984	3 % to 3⅝%	$ 5,241	$ 9,012
1985 through 1989	4⅜%	8,580	8,690
1990 through 1994	4⅞%	9,880	10,002
1995 through 1999	5⅞% to 7¼%	32,197	32,602
2000 through 2004	7½% to 10⅛%	55,031	38,532
2005 through 2009	8⅛% to 9⅛%	119,073	119,290
2004 through 2009 — pollution control series, securing pollution control revenue bonds	6 % to 6⅞%	274,061	145,000
Funds held by trustee		(153,660)	(85,825)
Total first mortgage bonds		350,403	277,303
Pollution control revenue bonds, due 1984	5 % to 7.6%	77,000	77,000
Other		4,252	2,044
Total long-term debt		$431,655	$356,347

Substantially all utility plant is pledged to secure the first mortgage bonds.

Approximately 25 percent of the original principal amount of each series of first mortgage bonds will be redeemed through sinking fund requirements prior to the aforementioned due dates. The aggregate amounts (in thousands) of maturities on long-term debt outstanding at December 31, 1979 are as follows:

1980	$5 224
1981	2,314
1982	5,508
1983	2,816
1984	4,914

In August 1977 the City of Farmington, New Mexico issued and sold $77,045,000 principal amount of its 5.9% Pollution Control Revenue Refunding Bonds, Series 1977, the proceeds of which are expected to be used to retire 7.6% Pollution Control Revenue Bonds and 5% Pollution Control Revenue Bonds at their maturity in 1984. From and after such retirement, but not before, the Refunding Bonds will be payable out of revenues received by the City from the Company. Upon such retirement the Company will also guarantee the payment of the Series 1977 Bonds and secure its guaranty with an equal principal amount of its first mortgage bonds.

(5) Short-Term Debt and Compensating Balance Arrangements

The Company's interim financing requirements are met through issuance of unsecured notes payable to banks and commercial paper. The Company has agreed to maintain compensating balances with certain lending banks or to pay fees in lieu of such balances. Compensating balances are generally equal to 20% of the outstanding indebtedness or 10% of the lines of credit at such banks, whichever is greater. Details of the Company's short-term debt at December 31, 1979 and December 31, 1978 and for the years then ended were as follows:

	1979	1978
	(In thousands)	
Aggregate short-term debt outstanding:		
Notes payable to banks	$37,250	$ 4,050
Commercial paper	$58,710	$19,755
Average interest rate on outstanding debt:		
Notes payable to banks	14¾%	11¼%
Commercial paper	13⅜%	10⅛%
Maximum short-term debt outstanding during year	$95,960	$68,600
Average short-term debt outstanding during year	$38,460	$23,028
Weighted average interest rate on short-term debt outstanding during year, computed using daily outstanding balances:		
Stated interest rates	11⅞%	7¾%
Effective rate considering the effect of compensating balances and fees in lieu thereof	12⅞%	8⅛%
Unused lines of credit (subject to cancellation at the banks' option)	$60,140	$53,120
Compensating balances at end of year	$ 1,956	$ 916

Compensating balances have been reduced by the average difference between collected bank balances and book balances.

(6) Income Taxes

Income taxes consist of the following components:

	1979	1978
	(In thousands)	
Current Federal income tax	$ 3,864	$ 1,609
Current state income tax	1,467	1,048
Deferred Federal income tax	3,583	2,130
Deferred state income tax	677	657
Amount equivalent to current investment tax credit	13,611	12,413
Amortization of accumulated investment tax credit	(742)	(527)
Total income taxes	$22,460	$17,330
Charged to operating expenses	$21,881	$16,722
Charged to other income and deductions	579	608
Total income taxes	$22,460	$17,330

The Company has investment tax credit carryforwards, for tax purposes, of approximately $56,000,000 as of December 31, 1979 which will expire in 1985 and 1986. Of this amount, approximately $17,075,000 has been recorded, for financial statement purposes, as a reduction of deferred Federal income tax credits.

Deferred income taxes result from timing differences in the recognition of income and expenses for tax and accounting purposes. The major sources of these differences and the tax effects of each were as follows:

	1979	1978
	(In thousands)	
Deferred fuel costs	$ (495)	$ 2,396
Liberalized depreciation methods and asset class lives shorter than guideline lives	8,049	4,376
Other miscellaneous items	662	47
Investment tax credit carryforward	(3,956)	(4,032)
	$ 4,260	$ 2,787

The current portion of deferred income taxes (included in accrued taxes) results from timing differences on deferred fuel costs. Such balances amounted to $1,688,000 as of December 31, 1979 and $1,977,000 as of December 31, 1978 after reduction for investment tax credit carryforwards.

The Company's effective income tax rate was less than the Federal income tax statutory rate for each of the years shown. The differences are attributable to the following factors:

	1979	1978
Federal income tax statutory rate	46.0%	48.0%
Tax depreciation in excess of book depreciation caused by use of guideline depreciation provisions	(2.7%)	(1.2%)
Allowance for funds used during construction, net of depreciation adjustments	(12.1%)	(12.3%)
Certain employee benefits and taxes capitalized for financial statements, net of depreciation adjustments	(.5%)	(.7%)
Amortization of investment tax credits	(1.0%)	(1.0%)
Other miscellaneous items	(.6%)	(1.2%)
Company's effective income tax rate	29.1%	31.6%

(7) Pension Plan

The Company has a pension plan covering substantially all of its employees, including officers. The plan provides for monthly pension payments to participating employees upon their attaining the age of 65 or the age of 62 with 30 years service, the amount of such payments being dependent upon length of service and the average wage of the five most highly compensated consecutive years of employment. Early retirement is optional after age 55 or 30 years of service. Normal retirement benefits are the lesser of 65% of the participant's average annual base earnings rate minus $1,320 or 2% of the participant's average annual base earnings rate times his years of credited service. The Company made contributions to the employees' pension plan of $3,058,000 in 1979 and $2,807,000 in 1978 including normal costs and amortization of prior service costs.

Prior to May 1, 1978, the employees contributed $3 for the first $400 of monthly base salary, plus 3 percent of that part of base salary in excess of $400 during each month. The Company's funding of this portion of pension costs after such date did not have a significant effect on net earnings.

As of January 1, 1978, the most recent valuation date, the actuarially computed present value of vested benefits did not exceed the total market value of the pension fund assets and the estimated amount of the unfunded prior service liability was approximately $3,400,000.

(8) Construction Program and Jointly-Owned Plants

The Company is participating with Tucson Electric Power Company in the construction of the steam turbo-electric San Juan Generating Station. The Company owns an undivided fifty-percent interest in the first three units of the station. The Company purchased Tucson's fifty-percent undivided interest in the fourth and final unit of the San Juan Station in 1979 and now owns all of such unit.

The Company is also participating with several other utilities in the construction of the Palo Verde Nuclear Generating Station with the first unit scheduled for completion in 1983.

It is estimated that the Company's construction expenditures for 1980 will approximate $299,000,000 including expenditures on the jointly-owned projects. In connection, therewith, substantial commitments have been made. In addition to such amount, the Company's wholly-owned subsidiary forecasts construction expenditures of approximately $15,000,000.

Details of the Company's interest in jointly-owned plants at December 31, 1979 are as follows:

	Plant in Service	Accumulated Depreciation	Construction Work in Progress	Share of Total Plant
		(In thousands)		
San Juan Generating Station	$388,893	$26,788	$208,063	65 %
Palo Verde Nuclear Generating Station	—	—	$170,159	10.2%
Four Corners Generating Station Units 4 and 5	$ 26,019	$ 6,440	$ 6,087	13 %

These amounts represent the Company's share of capital costs and the Company has provided its own financing. The Company's share of direct expenses is included in the corresponding operating expenses in the Consolidated Statement of Earnings. The Company also has undivided interests in transmission facilities which are not significant.

(9) Lease Commitments

The Company leases data processing, communication, office and other equipment, office space, utility poles (joint use) and real estate. Certain leases, primarily for data processing equipment, are capital leases. All other leases are operating leases.

Certain leases provide purchase options in the approximate amount of $2,146,000 for data processing equipment and $423,000 for construction equipment. Renewal options and contingent rental provisions were not significant.

Leased property under capital leases at December 31, 1979 and 1978 is as follows:

	1979	*1978*
	(In thousands)	
Data processing equipment	$3,871	$2,310
Other	232	181
	4,103	2,491
Less accumulated amortization	1,550	970
	$2,553	$1,521

Future minimum lease payments (in thousands) under capital leases at December 31, 1979 are:

1980	$ 922
1981	927
1982	812
1983	320
1984	230
Later years	457
Total minimum lease payments	3,668
Less amount representing executory costs	142
Net minimum lease payments	3,526
Less amount representing interest	770
Present value of net minimum lease payments	$2,756

Future minimum rental payments (in thousands) required under operating leases that have initial or remaining noncancellable lease terms in excess of one year as of December 31, 1979 are:

1980	$ 670
1981	351
1982	192
1983	147
1984	146
Later years	356
Total minimum payments required	$1,862

Rents charged to operating expenses were $1,277,000 in 1979 and $1,091,000 in 1978. Such amounts exclude payments made on capital leases. Rents charged to utility plant were $236,000 in 1979 and $577,000 in 1978.

The Company has entered into an agreement, not included above, for the lease of an office building currently under construction. Lease payments will commence after construction is completed in late 1980 at a rate of 4.42% of construction cost per year for the first three years and at 9.62% per year for the remaining thirty-two years of the initial lease term. Construction costs covered by the lease are projected to be approximately $18,700,000. Such lease is an operating lease.

(10) Revenues Subject to Refund

A boiler explosion caused the shutdown of Unit 2 at the San Juan Generating Station during the period July 1977 to May 1978. The major part of increased costs for replacement energy required during the shutdown was, with the approval of the Commission, initially passed on to customers through the fuel adjustment clause; however, the Commission subsequently ruled that charges for such increased costs are subject to refund if it is determined that the Company was responsible for the explosion. Amounts collected subject to refund, based upon a formula proposed to the Commission, were approximately $2.1 million in 1978 and $4.5 million in 1977. Based on the Company's investigation the Company is of the opinion that no refunds will be due. The Company's insurance covered a major portion of the cost of replacement.

In addition, the Company has collected certain revenues and has established a provision for possible refund of a portion of those revenues that have been collected subject to refund under wholesale rate cases filed with the FERC. Information concerning such revenues and provision is as follows:

	Revenues Collected	*Provision for Possible Refund*	*Net*
		(In thousands)	
1977	$ 1,705	$ —	$ 1,705
1978	6,678	—	6,678
1979	13,177	3,292	9,885
Total	$21,560	$3,292	$18,268

(11) Subsequent Event

On October 1, 1979 the Company entered into an agreement with a group of private investors to sell $45 million principal amount of 10⅛% first mortgage bonds due 2004. On October 24, 1979 the Company received $17 million principal amount of such issue with the balance of $28 million received on January 28, 1980.

(12) Quarterly Results of Operations (Unaudited)

The results of operations (in thousands except per share amounts) by quarters for 1979 and 1978 are as follows:

Quarter Ended	*Total Operating Revenues*	*Operating Income*	*Net Earnings*	*Net Earnings per Share*
December 31, 1979	$64,335	$16,378	$16,623	$.87
September 30, 1979	$66,725	$18,998	$16,661	$.88
June 30, 1979	$56,475	$13,192	$11,504	$.61
March 31, 1979	$56,835	$11,248	$10,015	$.57(a)
December 31, 1978	$49,473	$ 9,548	$ 7,781	$.45
September 30, 1978	$50,643	$13,039	$11,725	$.90
June 30, 1978	$44,079	$11,148	$10,005	$.84
March 31, 1978	$43,010	$10,212	$ 7,953	$.71

(a) In June 1979, the Company established a provision for possible refund on certain revenues collected subject to refund since October 1977. The effect of such provision was to reduce operating revenues, net earnings and net earnings per share by approximately $1.9 million, $1.3 million and $.10, respectively, for the first quarter of 1979. The quarterly results of operations have been restated accordingly.

In the opinion of management of the Company, all adjustments (consisting of normal recurring accruals) necessary for a fair statement of the results of operations for such periods have been included.

Accountants' Report

Certified Public Accountants

Suite 500 First Plaza
Post Office Box 1027
Albuquerque, New Mexico 87103

Peat, Marwick, Mitchell & Co.

The Board of Directors and Stockholders
Public Service Company of New Mexico:

We have examined the consolidated balance sheet of Public Service Company of New Mexico and subsidiary as of December 31, 1979 and 1978 and the related consolidated statements of earnings, capitalization and changes in financial position for the years then ended. Our examinations were made in accordance with generally accepted auditing standards, and accordingly included such tests of the accounting records and such other auditing procedures as we considered necessary in the circumstances.

In our opinion, the aforementioned consolidated financial statements present fairly the financial position of Public Service Company of New Mexico and subsidiary at December 31, 1979 and 1978 and the results of their operations and changes in their financial position for the years then ended, in conformity with generally accepted accounting principles applied on a consistent basis.

Peat, Marwick, Mitchell & Co.

February 19, 1980

Stock / Dividend Data

Common Stock:

Range of sales prices of the Company's common stock, on the New York Stock Exchange (Symbol: PNM), and dividends paid on common stock for fiscal 1979 and 1978, by quarters, are as follows:

	Range of Sales Prices		Dividends
	High	Low	Per Share
Fourth Quarter, 1979	20¼	17½	$0.48
Third Quarter, 1979	21½	17⅜	0.48
Second Quarter, 1979	21¼	19	0.48
First Quarter, 1979	20⅝	19⅛	0.44
Fiscal Year	21½	17⅜	$1.88
Fourth Quarter, 1978	20½	18⅜	$0.44
Third Quarter, 1978	21¾	19⅝	0.44
Second Quarter, 1978	21⅛	19¼	0.42
First Quarter, 1978	21⅝	19⅜	0.42
Fiscal Year	21¾	18⅜	$1.72

Cumulative Preferred Stock:

While isolated sales of the Company's preferred stock have occurred in the past, the Company is not aware of any active trading market for its preferred stock.

Quarterly cash dividends were paid on each series of the Company's preferred stock at their stated rates during 1978 and 1979.

Supplementary Information on Changing Prices

The following supplementary information is supplied in accordance with the requirements of Financial Accounting Standards Board (FASB) Statement No. 33, Financial Reporting and Changing Prices, for the purpose of providing certain information about the effects of changing prices. It should be viewed as an estimate of the approximate effect of inflation, rather than as a precise measure.

Constant dollar amounts represent historical costs stated in terms of dollars of equal purchasing power, as measured by the average Consumer Price Index for All Urban Consumers (CPI-U). Current cost amounts reflect the changes in specific prices of plant from the date the plant was acquired to the present, and differ from constant dollar amounts to the extent that specific prices have increased more or less rapidly than prices in general.

The current cost of property, plant and equipment, which includes land, land rights, intangible plant, property held for future use and construction work in progress, represents the estimated cost of replacing existing plant assets and was determined by indices provided by an independent appraisal firm. These indices consist of a combination of the Handy-Whitman Index of Public Utility Construction Costs and special indices derived from actual appraisals of certain property, plant and equipment.

The accumulated provision for depreciation and amortization on the constant dollar and current cost amounts of property, plant and equipment was determined by calculating the ratio of the actual reserve to historical cost for each plant account and applying this ratio to the indexed amounts. The current year's provision for depreciation and amortization on the constant dollar and current cost amounts was determined by applying the Company's average annual depreciation and amortization rates for each plant account to the indexed amounts.

Fuel inventories, the cost of fuel used in generation, and power purchased for resale have not been restated from their historical cost. Regulation limits the recovery of fuel and purchased power through the operation of adjustment clauses or adjustments in basic rate schedules to actual costs. For this reason fuel inventories are effectively monetary assets.

As prescribed in Statement No. 33, income taxes were not adjusted. Accumulated Deferred Investment Tax Credits is treated as a monetary item, since it is returned to customers through adjustments in rates.

Under the rate making prescribed by the regulatory commissions to which the Company is subject, only the historical cost of plant is recoverable in revenues as depreciation. Therefore, the excess of the cost of plant stated in terms of constant dollars or current cost over the historical cost of plant is not presently recoverable in rates as depreciation, and is reflected as a reduction to net recoverable cost. While the rate-making process gives no recognition to the current cost of replacing property, plant and equipment, based on past practices, the Company believes it will be allowed to earn on the increased cost of its net investment when replacement of facilities actually occurs.

To properly reflect the economics of rate regulation in the Statement of Earnings from Continuing Operations, the reduction of net property, plant and equipment should be offset by the gain from the decline in purchasing power of net amounts owed. During a period of inflation, holders of monetary assets suffer a loss of general purchasing power while holders of monetary liabilities experience a gain. The gain from the decline in purchasing power of net amounts owed is primarily attributable to the substantial amount of debt which has been used to finance property, plant and equipment. Since the depreciation on this plant is limited to the recovery of historical costs, the Company does not have the opportunity to realize a holding gain on debt and is limited to recovery only of the embedded cost of debt capital.

Statement of Earnings from Continuing Operations Adjusted for Changing Prices

Year Ended December 31, 1979

	As Reported in the Primary Statement	*Adjusted for General Inflation (Constant Dollars)*	*Adjusted for Changes in Specific Prices (Current Cost)*
		(In thousands)	
Operating revenues	$244,370	$ 244,370	$ 244,370
Fuel and purchased power	85,143	85,143	85,143
Other operation expenses	34,351	34,351	34,351
Maintenance and repairs	15,045	15,045	15,045
Depreciation and amortization	17,603	27,364	28,666
Taxes, other than income taxes	10,531	10,531	10,531
Income taxes	22,460	22,460	22,460
Interest charges	23,008	23,008	23,008
Other income and deductions — net	(18,574)	(18,574)	(18,574)
	189,567	199,328	200,630
Earnings from continuing operations (excluding reduction to net recoverable cost)	$ 54,803	$ 45,042*	$ 43,740
Increase in specific prices (current cost) of property, plant and equipment held during the year			$ 67,686
Reduction to net recoverable cost		$(103,692)	(18,568)
Effect of increase in general price level			(151,580)
Excess of increase in general price level over increase in specific prices after reduction to net recoverable cost			(102,462)
Gain from decline in purchasing power of net amounts owed		62,665	62,665
Net		$ (41,027)	$ (39,797)

*Including the reduction to net recoverable cost, the earnings (loss) from continuing operations on a constant dollar basis would have been $(58,650) for 1979.

Five Year Comparison of Selected Supplementary Financial Data Adjusted For Effects of Changing Prices

	Years Ended December 31,				
	1975	1976	1977	1978	1979
	(In thousands of average 1979 dollars except per share amounts)				
Operating revenues	$114,657	$126,957	$166,134	$208,378	$244,370
Historical cost information adjusted for general inflation:					
Earnings from continuing operations					$ 45,042
Earnings from continuing operations per common share					$ 2.29
Net assets at year-end at net recoverable cost					$428,877
Current cost information:					
Earnings from continuing operations					$ 43,740
Earnings from continuing operations per common share					$ 2.20
Excess of increase in general price level over increase in specific price after reduction to net recoverable cost					$102,462
Net assets at year-end at net recoverable cost					$428,877
General information:					
Gain from decline in purchasing power of net amounts owed					$ 62,665
Cash dividends declared per common share	$ 1.70	$ 1.81	$ 1.93	$ 1.91	$ 1.88
Market price per common share at year-end	$ 24.36	$ 29.95	$ 25.13	$ 21.31	$ 17.27
Average consumer price index	161.2	170.5	181.5	195.4	217.5

PNM Statement of Principle

Public Service Company of New Mexico believes that each successive generation's quality of life will be progressively more dependent upon the availability and reliability of electric and water service.

Consistent with this belief, we recognize our obligations to:

Our Customers
An adequate and reliable source of electric and water service at the lowest reasonable cost;

Our Shareholders
A reasonable return on, with optimum security of, their investment;

Our Employees
An objective opportunity to progress and grow through productive and meaningful participation; and

Our Future Generations
A legacy of adequate electric and water service provided through free enterprise with environmental and economic compatibility.

To meet these obligations, we affirm a policy of:

Operating our Company in a responsible manner which reflects the highest corporate integrity;

Providing open communications in order to achieve a high level of understanding and acceptance of our purpose and endeavors;

Sharing our technical and administrative skills with all levels of government to assist in assuring the best decisions are made; and

Promoting, supporting and participating in worthwhile community activities and development.

J. D. Geist, President

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C. E. LEYENDECKER† — *President, Mimbres Valley Bank – Deming, New Mexico*
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R. R. REHDER† — *Professor of Management, Robert O. Anderson Graduate School of Management, University of New Mexico – Albuquerque, New Mexico*
G. A. SCHREIBER* — *Chairman of the Board of Directors, Public Service Company of New Mexico*
R. H. STEPHENS† — *President, Stephens-Irish Agency – Las Vegas, New Mexico*
E. R. WOOD — *President, Santa Fe Motor Company – Santa Fe, New Mexico*

* *Members of the Executive Committee*
† *Members of the Audit Committee*

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J. L. SMITH — *Belen Division Manager*

Executive Offices

414 Silver Avenue SW, Albuquerque, New Mexico

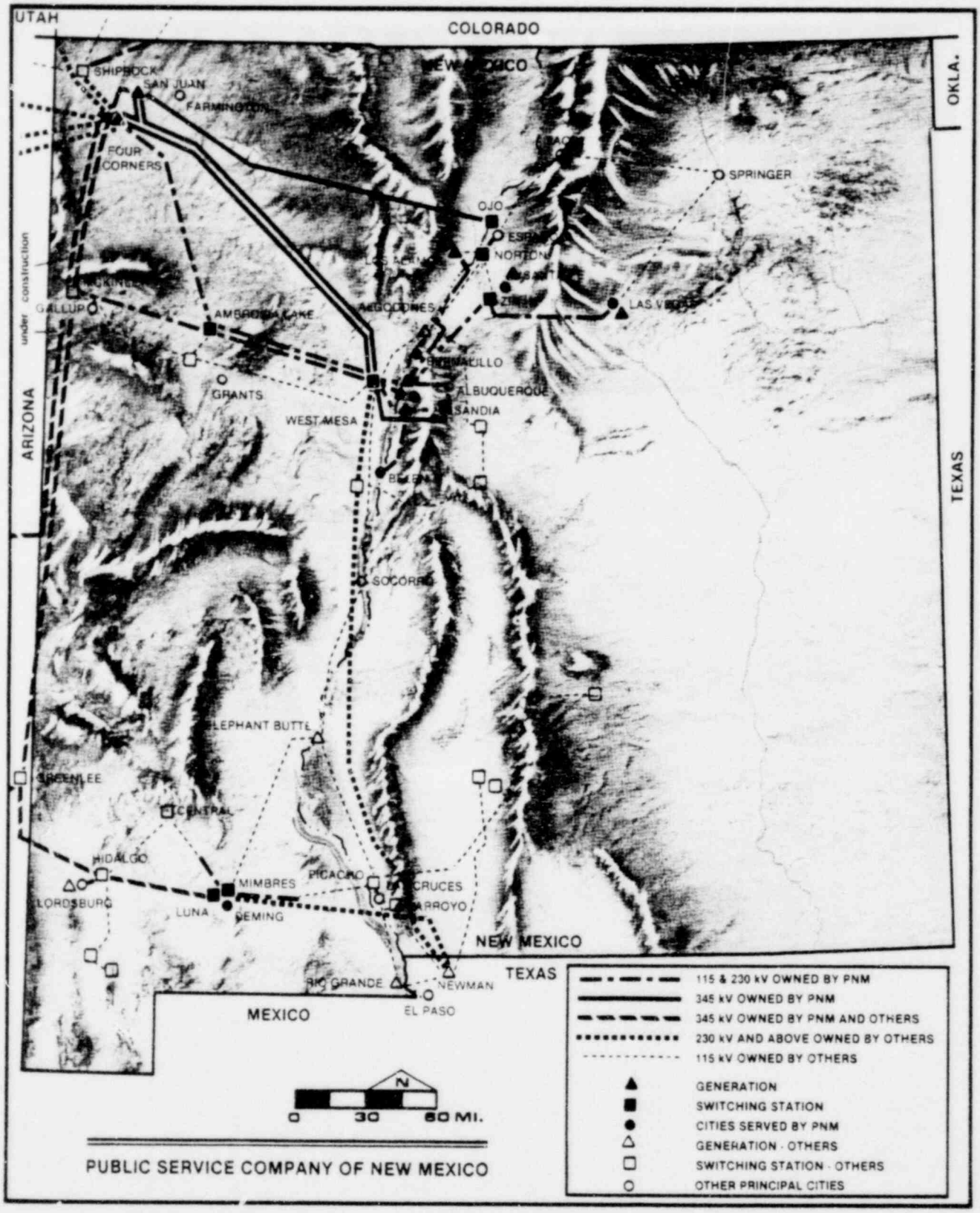
Transfer Agents

Albuquerque National Bank, Albuquerque, New Mexico
Chemical Bank, New York, New York
Irving Trust Company, New York, New York

Registrars

First National Bank in Albuquerque, Albuquerque, New Mexico
Chemical Bank, New York, New York
Irving Trust Company, New York, New York

System Map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345 kV OWNED BY PNM
345 kV OWNED BY PNM AND OTHERS
230 kV AND ABOVE OWNED BY OTHERS
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