Gulf States Utilities 1981 Annual Report

Description of Business

Gulf States Utilities was incorporated in 1925 and is primarily in the business of generating, transmitting, and distributing electricity to 517,000 customers in Southeast Texas and South Louisiana. The service area extends 350 miles westward from Baton Rouge, La., to a point about 60 miles east of Austin, Tx. The service area encompasses the northern suburbs of Houston and major cities such as Conroe, Huntsville, Port Arthur, Orange and Beaumont, Tx.; Lake Charles and Baton Rouge, La.

GSU also sells electricity to municipalities and rural electrical cooperatives in both Texas and Louisiana. In Baton Rouge, GSU supplies steam and electricity to industrial customers through a cogeneration facility and the company owns and operates a natural gas retail distribution system serving 86,000 customers.

As a member of the Southwest Power Pool, the company has the ability to interchange electricity between the 41 members serving seven states in the South and Southwest. The company had a peak load of 5,542 megawatts in 1981 while it had installed capacity and firm power purchase agreements totaling 6,745 megawatts, providing a 21.7 percent margin.

The company also has a wholly-owned subsidiary, Prudential Drilling Company, engaged primarily in oil and gas exploration. Prudential is expanding its operations and has been authorized by the board of directors of Gulf States to spend about $10 million per year for the next four years in search of oil and gas. Additional funds could be made available for development and production of discoveries resulting from this search.

Financial Highlights

	1981	1980	% Change
Total Operating Revenue (000)	**$ 1,221,714**	$ 1,005,226	21.5
Operating Expenses and Taxes (000)	**$ 991,421**	$ 836,367	18.5
Net Income (000)	**$ 150,931**	$ 117,189	28.8
Income Applicable to Common Stock (000)	**$ 120,550**	$ 92,309	30.6
Earnings per Share of Common Stock			
Based on Average Shares Outstanding	**$2.24**	$2.05	9.3
Assuming Conversion of Convertible Debentures	**$2.20**	$1.96	12.2
Dividends per Share	**$1.48**	$1.39	6.5
Average Common Shares Outstanding (000)	**53,851**	44,987	19.7
Number of Electric Customers (end of year)	**516,812**	500,043	3.4
Total Kilowatt-Hour Sales (000)	**30,697,020**	30,585,482	0.4
System Peak Load — Kilowatts	**5,541,600**	5,604,400	(1.1)

*See Note 7 to the Financial Statements for the pro-forma effect of the change in accounting for fuel cost.

Contents

The Cover

A workman on the cooling tower for the nearly complete Nelson 6 coal-fired power plant is dwarfed by stack of the 540-megawatt unit.

Dear Fellow Shareholders:

Gulf States Utilities showed solid progress in a number of important areas in 1981 as well as good operating results despite the economic burdens of inflation and extraordinarily high interest rates. Unfortunately, the pleasure those results should afford us is diminished by the medical retirement of former board chairman W. Donham Crawford on March 1, 1982.

Don Crawford's career in the electric utility industry, including four years as GSU's chairman, can be characterized as one of attacking problems with intelligence and hard work. He continues that attitude as he fights a rare nerve disease that caused him to take medical leave from the company last August. Our prayers and wishes are with Don and his family as he continues treatment.

W. Donham Crawford

A measure of his character is reflected in the fact that Don Crawford developed an excellent management team during his tenure as chairman.

As board members during this period, we have participated in the fundamental decisions made by this company's management and have admiration and the utmost confidence in the management group.

Their achievements and those of 4,600 dedicated employees are chronicled in the operating results of 1981.

Earnings for the year were $2.24 per share of common stock and the dividend on common reached $1.48 per share. The regular quarterly dividend was raised again this February from 37 cents to 39 cents and that produces an annual rate of $1.56 which puts the company in a more competitive position to offer an attractive rate of return to investors who have many other investment opportunities in today's high interest rate market.

The $2.24 per common share earnings included a cash payment of $12 million to a GSU subsidiary as part of an exchange of lignite coal reserves between the subsidiary and another company. The gain from the exchange is the equivalent of 14 cents per share.

Disregarding the 14 cents contributed by the lignite sale, 1981 results were satisfactory in the face of inflation, high interest rates and a faltering economy.

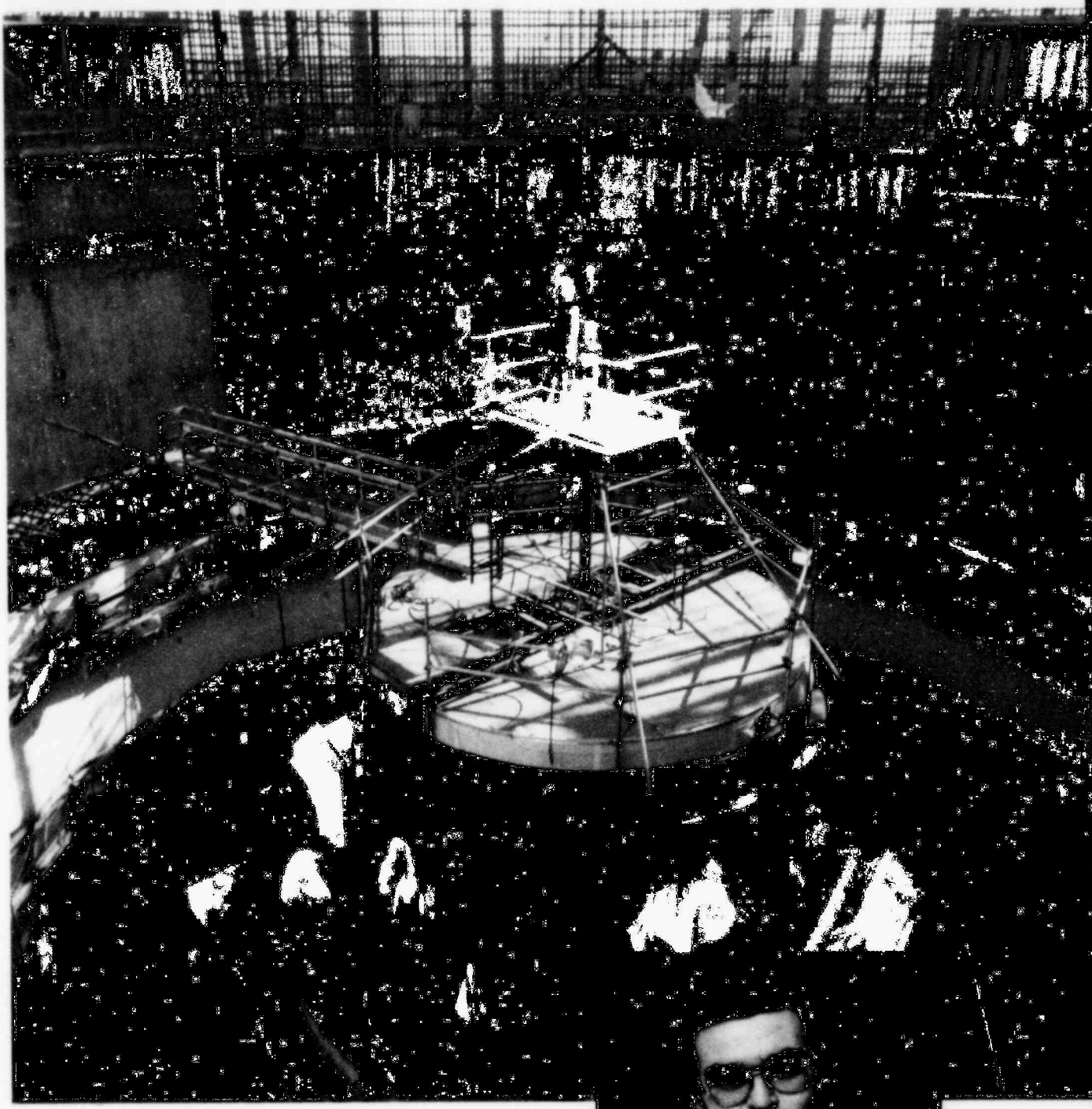
Despite the 1981 gyrations of the economy, it is gratifying that Gulf States can report major progress on our two largest construction projects. The 940-megawatt River Bend 1 nuclear generating unit under construction north of Baton Rouge, La., went from about 26 percent complete at the beginning of the year to nearly 44 percent complete by year's end. In more human terms, and considering the incredibly elaborate safety and quality control procedures that are going into River Bend, the progress in 1981 is the work equivalent of building 6,000 homes that are as close to human perfection as possible.

Equally significant were the construction gains at the 540-megawatt coal-fired Nelson 6 generating unit being built near Lake Charles, La., which went from about 47 percent to better than 92 percent complete in 1981. We have equity partners in both of these units and they are discussed in detail in the "Participation" section of this report on page 7.

The effort and dedication in both these projects have been immense and it is a tribute to the men and women of both GSU and the constructors — Bechtel Power Co. at the Nelson unit, and Stone and Webster at River Bend.

Another significant achievement was in the area of maintenance and operation of our generating units. Our goal is to have as many of our 34 generating units operating as much of the time as possible during the peak electric use months each summer. In 1981, the diligence and perseverance of our operations and maintenance employees gave us peak months' availability within a fraction of 80 percent, which is an outstanding achievement. This availability rate allowed us to sell power to other utilities and effectively lowered our customers' fuel charge for several months last fall.

Surveyor calculates distances from the top of the reactor vessel at the River Bend nuclear plant site.



"Safety and quality of construction remain our most basic objectives at River Bend."

Tom Crouse
Construction Superintendent
River Bend

In these times of economic pressure, we are forging a new partnership with our customers and we are exploring all avenues of customer assistance to help minimize increasing energy costs on the customer's budget. The benefits of energy conservation are clearly a portion of this program and conservation is being strongly endorsed by the company. This area is comprehensively explored in the "Shared Goals" portion beginning on page 13.

From the viewpoint of being able to earn on our investment, we are pursuing an aggressive program to establish rates that are fair to our investors and accurately reflect the cost of doing business. Unfortunately, this entire area is hamstrung because the data we submit to regulatory bodies, according to their own rules, is from eight to 18 months old when evaluated by the commissions. Regulators simply must respond faster and have more recent data that reflect current prices. To oversimplify, it is like trying to buy a 9-year old child shoes based on the size he wore when he was 7½.

Paul W. Murrill (left), Norman R. Lee.

In a fundamentally different vein, but still in pursuit of an attractive return for our investors, the company recorded a solid achievement in the purchase of Prudential Drilling Company last year. It is part of a continuing effort to develop earnings not regulated by utility commissions. Purchased entirely out of stockholders' equity with 588,000 shares of GSU common stock representing less than $7 million, Prudential has now embarked on an oil and gas exploration program that we intend to fund at the level of about $10 million annually in venture capital through 1985. A number of promising joint drilling projects are already underway and the potential for the new, wholly owned subsidiary looks bright. Any oil or natural gas developed by Prudential will be sold on the open market and not be used for fuel by Gulf States.

Another reflection of the solid achievement in 1981 was the virtual completion of Edison Plaza, the company's new headquarters in downtown Beaumont, Tx. Edison Plaza consolidates 1,200 employees, who have been working in five different Beaumont buildings, into a modern and highly efficient work environment.

In essence, 1981 appears to have harbored the type of events that will continue to be crucial to the company this year and next. Resourceful management in financing, construction, obtaining adequate electric service rates, providing for the most economical operation of the company and minimizing the effect of higher rates on customers will continue to hold our utmost attention. And with the skilled efforts of our 4,600 employees, we will succeed.

Sincerely,

Paul W. Murrill
Chairman of the Board
and Chief Executive Officer

Norman R. Lee
President and
Chief Operating Officer

Finance

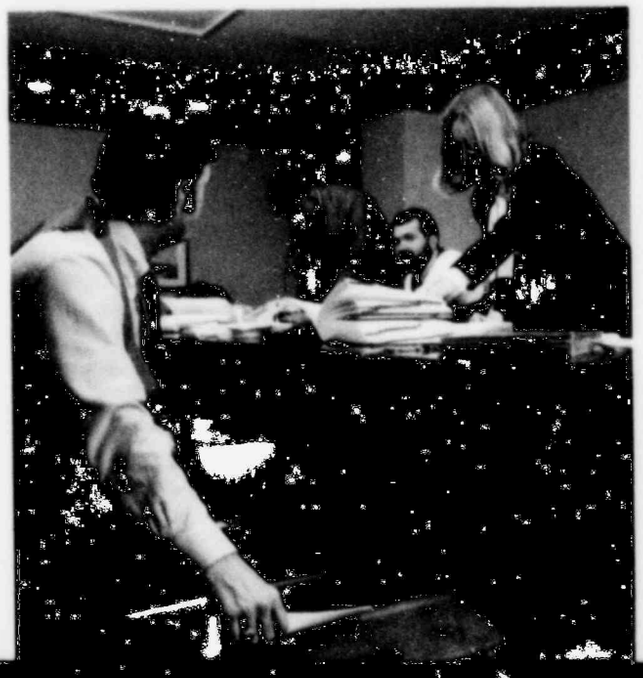
While the company continues to move away from increasingly expensive natural gas and oil as its main generating fuels by building coal-fired and nuclear fueled power plants, it was nonetheless arduous to finance this construction program in 1981.

The company was obligated to finance during periods of extraordinary interest rates with the vast majority of these funds being devoted to cash requirements of construction financing of the 940-megawatt, $2.5 billion, River Bend 1 nuclear unit; the 540 megawatt, $438 million, Nelson 6 coal unit; and GSU's 42 percent interest in Cajun Electric Power Cooperative's $430 million Big Cajun 2, Unit 3, a 540-megawatt coal-fired unit planned to be in operation in 1983.

The capital markets provided about $391 million in funds to the company in 1981 including about $109 million through the sale of equity securities, $24 million through the conversion of debentures and $258 million in debt financing.

In summary, the 1981 financing program was as follows:

- April and May, first mortgage bonds, $75 million, at 14.75 percent interest.
- July, common stock, five million shares worth $53,275,000.
- September, first mortgage bonds, $60 million at 16.8 percent interest. GSU drew $33 million of the total in September and $27 million in January, 1982.
- October, Euro debentures, $60 million, at 17.5 percent interest.
- December, common stock, three million shares, $35,385,000.



- December, first mortgage bonds, $100 million, at 17.5 percent interest. GSU drew $60 million of the total in December and the remainder in January, 1982.

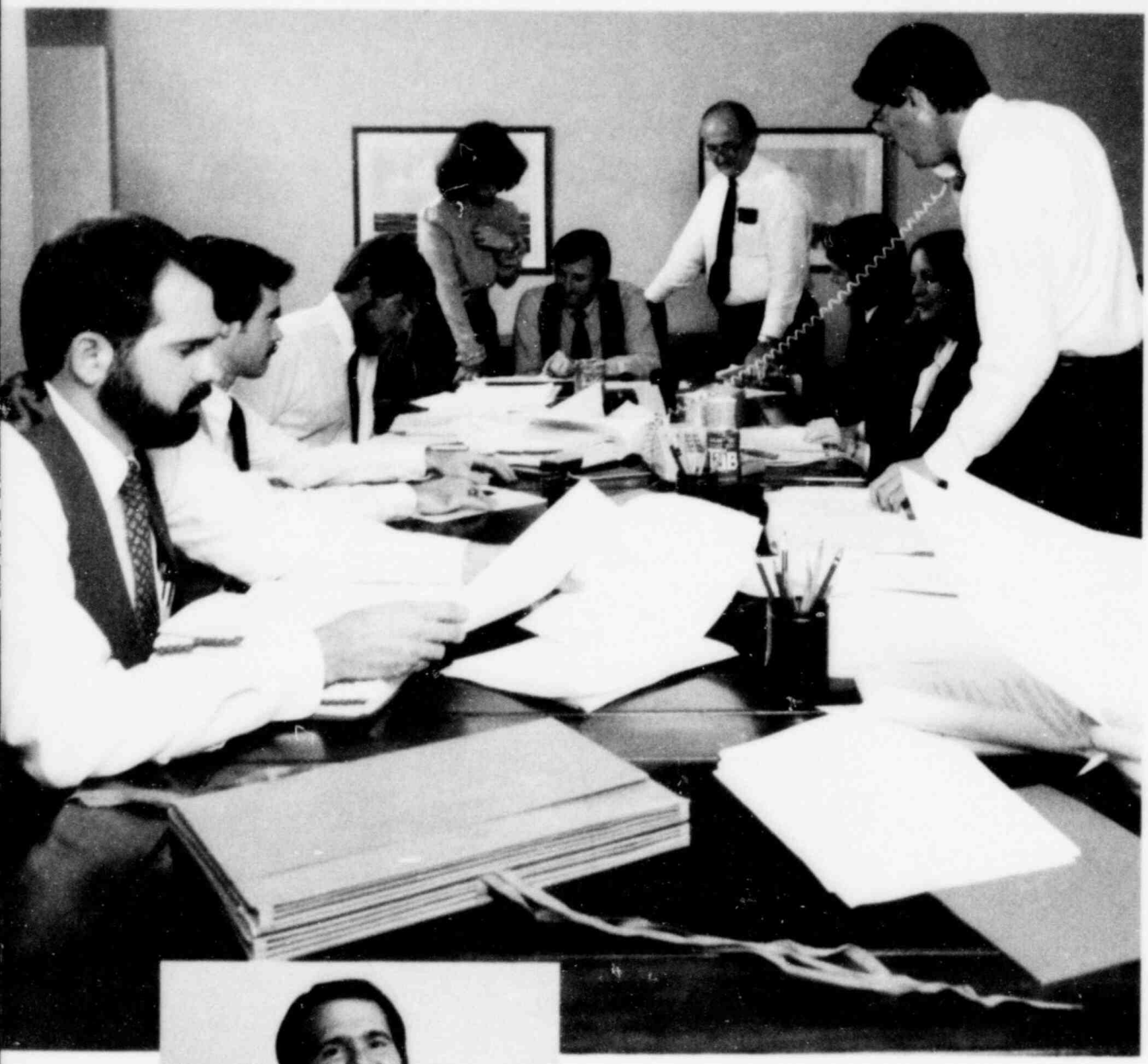
An additional financing vehicle used in 1981 was the $200 million revolving credit agreement between GSU and a consortium of nearly two dozen major American and international banks. This intermediate-term agreement, under which GSU borrowed $30 million in 1981 had a year-end outstanding balance of $190 million. Negotiations are presently underway with several of the participating banks to create a larger revolving credit facility of $800 million which will include the $190 million outstanding balance.

To maintain the company's flexibility in financing, GSU sought and received consent by holders of the company's 7¼ percent convertible debentures to modify the trust indenture under which they were issued. The modification was to eliminate the indenture's interest coverage covenant and increase GSU's financing flexibility. To encourage the modification, the company agreed to reduce the price at which the debentures can be converted into common stock. The conversion rate was lowered from $14.85 per share to $13.25.

A financing of a different nature took place in 1981, when the company began an aggressive program to diversify into potentially profitable areas that are not under the jurisdiction of utility regulatory authorities. GSU exchanged 588,000 shares of Gulf States common stock for all the outstanding shares of Prudential Drilling Co. of Houston. After Prudential became a wholly-owned subsidiary of GSU, Gulf States began carrying out a plan made last year to fund the subsidiary with about $10 million annually over the next four years in the exploration and development of oil and natural gas properties.

A number of joint venture agreements between Prudential and other oil and gas exploration companies have been signed, drilling has commenced, and some preliminary results should be available by the end of 1982.

A portion of the new tax laws enacted by Congress in 1981 has direct benefit to Gulf States' stockholders. It is a tax relief program that allows stockholders to reinvest their common stock dividends in additional common shares of Gulf States and to defer income taxes on the reinvested dividends until the stock is sold. An individual can defer up to $750 each year in reinvested dividends ($1,500 on a joint return) from 1982 to 1985. The gains derived from the sale of shares received from dividend reinvestment during this period will be taxed as a capital gain if the shares are held more than one year before being sold.



"Financing at the lowest cost possible is an absolute obligation to customers and stockholders."

Greg Copeland
Director — Long Term Finance

Rates

Even though the GSU management is dedicated to the most economic operation of the company possible and is actively seeking new ways to cut costs, it is only through rate increases that the company can cope with the effects of high construction costs, high interest rates and inflation.

The company recognizes that higher electric service rates place additional burdens on customers, but it is equally clear that if customers are to have adequate supplies of electricity in the future the company must maintain a rate of return that will hold existing investors and attract new ones during a period that requires an extensive construction program. Toward that end the company pursued rate increases in both Texas and Louisiana last year.

In May, the company filed for a $131.5 million rate increase in its Texas jurisdiction. Two weeks of mid-summer hearings before the Public Utility Commission of Texas led to a commission decision to grant GSU a $63.7 million annual increase in revenue. The decision, which was put into effect in October but is under appeal by several municipalities, allows the company to earn 16.5 percent on equity and includes 76 percent of Construction Work in Progress (CWIP) in rate base. CWIP is money the company has invested in new plant that has not begun operating.

At the end of October, the company filed for a $217.8 million rate increase in Louisiana. In that filing the company included a request for interim rate relief from the Louisiana Public Service Commission (LPSC). However, the LPSC denied the company's request for $46 million in interim relief. The company is providing updated data on the total request to the LPSC as early in 1982 as possible to give the LPSC an opportunity to hold prompt hearings on the total request.

The company is completing a case for filing with the Federal Energy Regulatory Commission to increase rates for the company's wholesale and transmission service customers in both Texas and Louisiana.

Participation

The extraordinary capital demands of new power plant construction have led many companies, including Gulf States, to consider joint ownership in such projects. In fact, it will probably hold true for years in the future that expensive coal and nuclear power plants will be funded by consortiums of utilities that are geographic neighbors and share similar needs for added generating capacity.

In GSU's case the company is sharing the construction cost and output of three power plants with other utilities.

These major projects are:

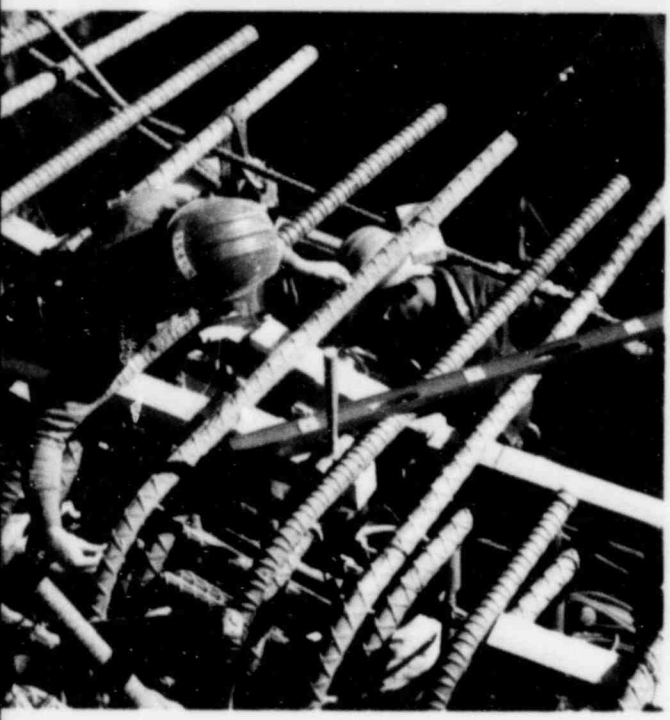
- River Bend 1, a 940-megawatt nuclear powered generator being built about 30 miles north of Baton Rouge, La. Cajun Electric Power Cooperative (CEPCO) began funding its 30 percent ownership portion of that plant in early 1981. During the year CEPCO brought its ownership portion to parity by funding $388 million and now GSU and the co-op fund at the 70/30 percent rate monthly. Another utility operation, the Texas based Sam Rayburn G&T (SRG&T), had planned to begin funding a seven percent portion of the River Bend unit in 1981. However, SRG&T's participation must be approved by the Rural Electrification Administration (REA) and the company understands the REA presently does not intend to approve SRG&T's participation. Efforts continue to be made to get the approval. The upshot of that is that if the company does not get SRG&T participation, it will have to bear additional construction financing until completion of the unit.
- Nelson 6, a 540-megawatt coal-fired generator being built a few miles west of Lake Charles, La. Sam Rayburn Municipal Power Authority (SRMPA) and SRG&T will become 20 and 10 percent owners respectively of the nearly-completed unit. Both SRMPA and SRG&T are affiliates of Sam Rayburn Dam Electric Cooperative, which serves a number of East Texas cooperatives, communities, and the town of Vinton, La. Both participants have reached parity with GSU on funding. The unit was within eight percent of completion at year's end and is scheduled for commercial operation in May of 1982.
- Big Cajun 2, Unit 3, a 540-megawatt coal fired generator being built by Cajun Electric Power Cooperative near New Roads, La. GSU began funding its 42 percent ownership in early 1981. The company is scheduled to have funded the unit to parity by early 1982 and then will fund its 42 percent of the construction outlays. The unit is scheduled for completion in 1983.

GSU specialists, underwriters and attorneys complete stock sale closing in New York.

Construction

Construction progress on Gulf States' new power plants was massive, sustained and highly successful in 1981.

Most visible was the progress on the 540-megawatt Nelson 6 coal-fired generator under construction near Lake Charles, La. It is the company's first coal-fired facility, and, at the beginning of the year, was nearly half complete as a massive steel framework stood surrounded by mounds of excavated earth. At year's end the land was returning to normal and the entire project was within a few percentage points of completion.



To fuel the unit, one train after another, each carrying about 11,000 tons of coal, began arriving in October in preparation for the start-up. By December, the 18-story-high boiler was test-fired with oil. Plans called for test operations and de-bugging to continue through the spring with commercial operation expected in May.

When Nelson 6 is in full operation the unit will devour more than 300 tons of coal an hour which will be supplied by five 110-car trains in a constant shuttle between the Gillette, Wyo., mine and the Nelson unit.

Almost in the shadow of the giant coal-fired generator is the much smaller, but significant, Nelson 7 gas-fired turbine generator.

The 90-megawatt unit, capable of running on natural gas and light oil, was 65 percent complete as the year ended and will be used beginning this summer to provide peaking power when hot weather air conditioning demands begin cutting into the company's reserve margin of generating capacity.

Work on River Bend 1, the 940-megawatt nuclear generator now under construction near Baton Rouge, La., progressed excellently in 1981 not only from the standpoint of actual construction completed, but also from the quality standpoint that is under constant review by Gulf States, the prime contractor Stone & Webster, and the Nuclear Regulatory Commission (NRC).

Highlighting the year's construction, which went from 26 percent complete to nearly 44 percent complete, was the placement of the reactor vessel in mid-year. The reactor vessel serves as the boiler in a nuclear power plant and is a key point in construction.

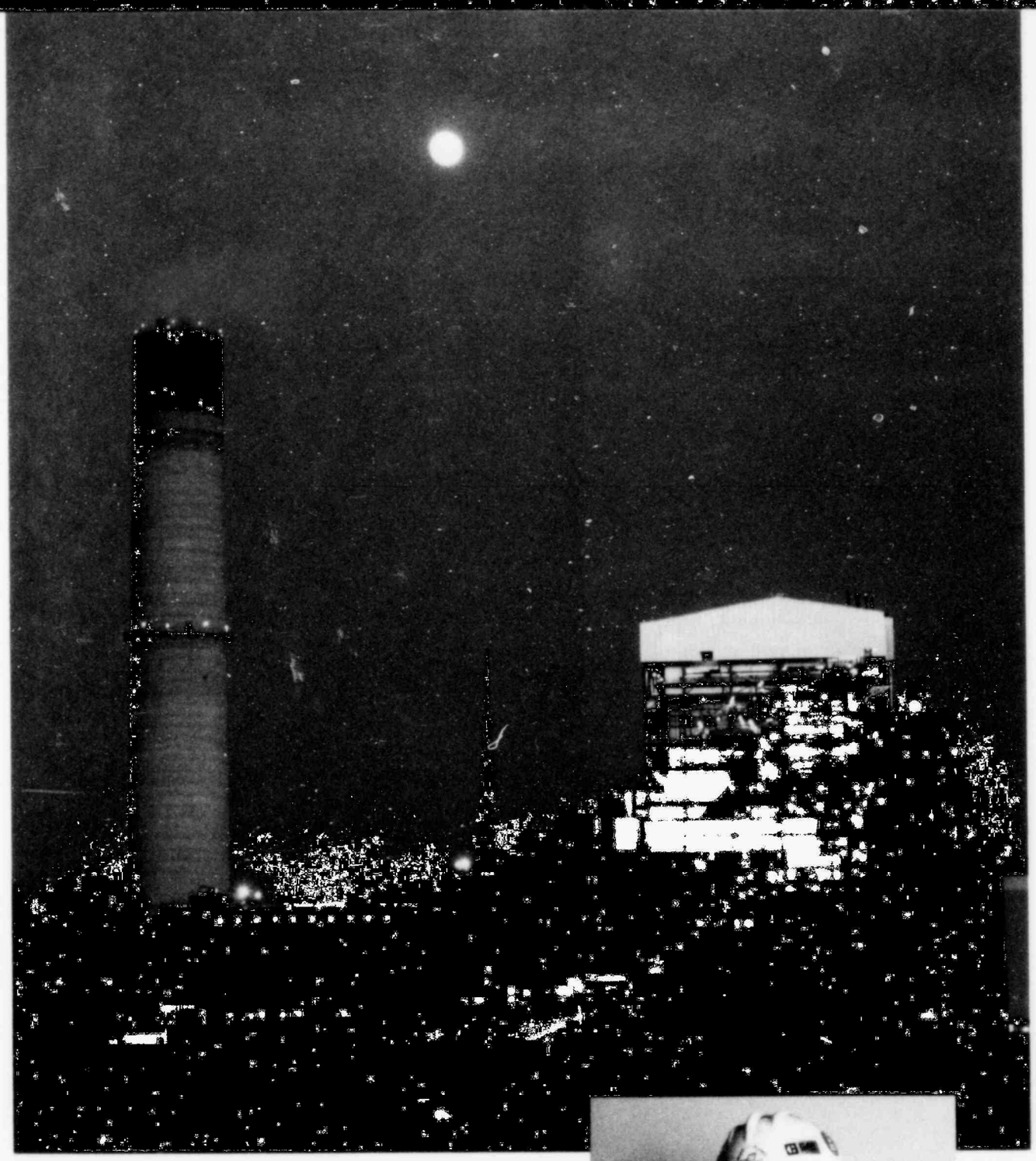
As for quality, the Nuclear Regulatory Commission's on-site resident inspector and other NRC inspectors, who made periodic visits to the site, turned up no major violations of construction quality or operational safety during the year.

Since August, 1979, the NRC has issued 30 inspection reports on River Bend representing 2100 man hours of review. Only 23 violations have been noted in those reports. The most serious was a Level IV. The NRC ranks violations from I to VI, I being the most serious.

In that regard, the NRC unconditionally rejected a request by the Union of Concerned Scientists (UCS) to halt construction at River Bend. The anti-nuclear UCS cited anonymous sources claiming "dangerous practices" at River Bend. A 10-month NRC investigation concluded that all UCS allegations had already been discovered and remedied by GSU and Stone & Webster.

Another extremely complex facet of River Bend is the licensing procedure that is required by the NRC. Last year the company filed a 20-volume, 9,000-page application for a River Bend operating license. After a four-month review by the NRC to establish if the application was sufficiently complete, the NRC said there was enough documentation to docket the application and begin the safety review. In all, the licensing procedure can take as much as two and one-half years to complete.

The moon hovers above the nearly complete Nelson 6 coal-fired power plant.



"The relatively inexpensive cost of using coal as a fuel at Nelson will benefit customers for decades to come."

Glenn T. Miller
Fuel Handling Operator
Nelson Station

Work continued at River Bend under the innovative Nuclear Construction Stabilization Agreement. It is a labor agreement that calls for no strikes or slowdowns and provides streamlined methods for settling craft disputes. An agreement under this concept calls for one 1700 member shift to work four consecutive 10-hour days and then be replaced by a second 1700 member work force for the next four days. Now in its third year of use, the "Rolling 4-10's" continue to provide excellent productivity and an amicable work climate.

While the construction and administrative aspects of River Bend continue in excellent fashion, present economic conditions are hampering our very aggressive completion schedule. The company notified the NRC in November that funding limitations of the project will control the rate of completion. High interest rates and inflation have forced the company to finance River Bend at a rate that will complete the project as quickly as possible, yet not jeopardize the company's financial integrity. Based on that management decision and updated construction cost estimates that have raised the projected cost from $1.7 billion to $2.5 billion, the company will fund the project at a rate that moves the commercial operation date back from mid-1984 to late 1985. A factor in this decision is the Rural Electrification Administration's indication that it will not support the application of the Sam Rayburn G&T to become a seven percent partner in the project. If that is the case, GSU will have to provide additional financing in 1982.

Despite this setback, the percentage-complete figure after 24 months of construction compares favorably to current industry patterns and the company anticipates bringing River Bend on line faster than most similar nuclear power plants.

One construction project that is in the final phases of completion is the company's new 17-storied headquarters in downtown Beaumont, Tx. Known as Edison Plaza, the spacious 462,000 square foot building is more than three times as large as the converted hotel which GSU has been using as a headquarters for about

25 years. The new building, owned by New York-based Statmont, Inc., and leased by Gulf States will house about 1,200 employees who have been scattered through five downtown buildings. The glass and aggregate-paneled building adds a fitting addition to the downtown area that is going through a period of revitalization.

Operations

Operationally, the company achieved marked success in 1981, moved forward on a series of programs to give customers superior service, and recorded a decrease in peak load for the first time in more than a decade. However, that drop was more of a statistical aberration than a trend.

For several years the company had been supplying more than 250 megawatts of energy to a Louisiana cooperative. In late June, responsibility for this load was assumed by the co-op when a new generating unit

was brought into operation. On June 22, just before the load was dropped, GSU hit a peak of 5542 megawatts which left a 21.7 percent reserve margin and turned out to be the generating peak in 1981. It was 62 megawatts less than the 5604 megawatt-peak recorded during the heat wave of 1980.

Electric sales in 1981 showed modest but stable growth. The company recorded one percent kilowatt-hour sales increases in residential and industrial classes of customers and a five percent increase for commercial customers.

While the residential customer group grew by four percent, a much cooler summer in 1981 compared to 1980 caused sales to grow by only one percent. The five percent growth in commercial sales was created primarily by the addition of new customers, and the modest increase of one percent among industrial customers is credited to a strong economy in the first half of 1981 that started turning sour in the second half.

Having as many power plants as possible operating during the summer months — when load is highest — is important if GSU is to avoid having to buy expensive power from neighboring utilities to meet customer demand. A 1981 commitment of money and manpower to increasing peak months' availability paid off last summer when availability reached a very respectable 79 percent compared to 73 percent the previous year.

At the same time availability was going up, GSU's use of its most expensive generating fuel — oil — was going down. Only two percent of the primary energy GSU used to make electricity in 1981 was oil; the rest was cheaper natural gas.

Both availability of generating units and the efforts to use cheaper fuel are part of a major program to give customers the best possible service. In a period when customers will inevitably see their electric bills increase, it is important to continue to provide top-notch service and find areas for improvement in the economy of company operation. Toward that end a number of programs were established to maintain quality and improve economics.

A major improvement in 1981 was the completion of a 345-kilovolt transmission line that now links GSU with Southwestern Electric Power Co. This tie, at the west end of the GSU system, allows power to be interchanged between the companies and improves reliability for both. On the eastern end of the Gulf States system, work is beginning on a 500-kilovolt intertie between GSU and the Southern Company. A unique advantage to this transmission line is a commitment by the Southern Company to sell coal-fired electric power over it to Gulf States at rates which will benefit all GSU customers.

A management reporting program was started in which line crews and service crews are measured for productivity against a base standard. If needed, time saving techniques or specialized training may be suggested to improve a particular crew's efficiency.

In a parallel effort, some crews have been relocated to areas that are closer to where the work is actually needed and that minimizes travel time.

More supervision is being given by GSU management to contractors that are doing work for the company to assure efficiency of operation.

New concepts in tree trimming are being explored to minimize cost as well as getting the most out of each dollar spent.

Increased emphasis is being placed on keeping delinquent bills from becoming uncollectible bad debts. Despite higher electric rates and a faltering economy, bad debts comprised less than .4 percent of 1981 revenues and attention in that area continues.

"As energy costs increase, we have a duty to help our customers use electricity as efficiently as possible."

Judith Moses
Superintendent Consumer
Services — Beaumont Division

Shared Goals

Energy — its use, its cost, its availability, its politics — has been the focal point of international debate for nearly a decade. And for the most energy intensive country in the world, it has become a national obsession.

Since 1974, energy cost and availability have changed the way we live, the cars we drive, how warm we are in the summer and how cold we are in the winter. Energy costs make pink panthers walk across our television screens telling us to insulate and television announcers breathlessly try to squeeze in the line that "these estimates will vary depending on how you drive. Mileage will be lower in California."

Energy cost and availability have direct consequences to Gulf States Utilities and its more than 517,000 customers. Simply put: Electricity takes an increasing share of the customer's budget. It is true for a chemical plant or a neighborhood grocery or a family.

Because electricity is such an integral and important part of our social fabric, Gulf States is committed to a single goal we share with our customers.

The goal is to have affordable electricity provided by an efficient and reliable company. It certainly is not new, and it does not sound particularly profound, but it is a goal that becomes elusive as primary energy costs increase.

We are developing programs in many areas to meet this goal. Several have been discussed in prior sections of this report and they relate to fuel diversity, financial integrity and operational efficiency. But there is more that needs attention and we are moving rapidly to fulfill our responsibility to customers and stockholders.

These programs include:

- Conservation
- Public Awareness
- Alternate Energy Sources
- Rates and Rate Design

Adding attic insulation becomes commonplace as energy costs increase.

Conservation

The simplest way to keep electric bills down is to use less, and that is the way conservation is viewed by many of our customers. Gulf States, primarily through our division offices and Consumer Services department and advertising, is actively showing customers how to conserve in many different areas.

We have classroom demonstrations on energy conservation. We work with city governments developing energy efficient building codes. We sponsor workshops and classes for electrical contractors and builders on efficient operations of equipment and weatherizing homes.

Trained GSU employees visit customers' homes on request and go over the home from top to bottom to point out ways to save electricity. Last year we expanded the program to include mobile homes which are a growing segment of our service area housing.

Energy Stores are operated by the company in shopping malls in both Baton Rouge and Beaumont. The stores provide a convenient location where customers can stop by, talk with qualified GSU representatives, and learn in minutes ways to cut their electric bill. Energy Information Centers, with wide ranging information kits, are operating in most company business offices.

Public Awareness

Even though the need for conservation is obvious, many customers do not realize that for little cost they can conserve without changing their lifestyle drastically. To demonstrate cost savings through conservation, GSU division offices across the company's 28,000 square mile service area are actively working with civic clubs and social service agencies to show the simplicity of energy conservaton. Also, weatherization demonstrations in workshops or educational programs are going on almost daily.

The company's advertising in 1981 stressed conservation and the many conservaton services the company offered. Additionally, a series of commercials were developed and aired showing low cost or no cost conservation practices.

Alternate Energy Sources

Gulf States' interest in alternate energy sources is aimed at practical applications of technology that could be cost competitive with existing fuels. The focal point is on several new uses of coal that could be compatible with existing natural gas-fired power plants, but expands into several applications.

Two forms of coal use are under study including gasification and micronization. In a joint project with Westinghouse and funded by the Department of Energy (DOE), the company is completing the preliminary engineering on a project that would take low sulfur Western coal and process it into a form of natural gas that would be used to power existing boilers. If this proves to be successful and economic, such a coal gasification plant could be in operation by 1986.

A second gasification project, in conjunction with Combustion Engineering and, again, funded by DOE, has fallen victim to government cost cutting. This project was to develop a gasification plant that would use higher sulfur Eastern coal. Preliminary engineering was about 50 percent complete when the funding was curtailed.

Micronization of coal is a process in which chunks of coal are reduced to nearly microscopic size and potentially can be burned in existing boilers now fueled by natural gas. Gulf States and several industries are pioneering this attempt, and if test results in 1982 are encouraging, a demonstration project using an existing industrial boiler could be attempted next year.

The company's solar applications are moving beyond the experimental stage in one area. A demonstration project was authorized in 1981 which has the goal of selling 100 solar water heaters in the Beaumont, Tx., area in 1982-83. The units will be sold and guaranteed by GSU. Gulf States employees will check construction installation for quality. Later the project will be evaluated by a team to determine if there is a future business opportunity for GSU.

Wind power, an indirect form of solar energy, has been under study for nearly a year by GSU. A 25-kilowatt wind generator was installed at a beachfront location on the Texas coast last year to accumulate data on wind potential. While the initial results tend to show that it is not economical in this area, tests will continue and other locations may be explored.

Rates and Rate Design

Rates that offer customers the chance to save money by shifting their use of electricity to "off-peak" hours show promise for the future. The idea is to offer lower costs per kilowatt-hour for late night and very early morning use of electricity. The incentive to the customer is obvious — a lower electric bill. The advantage to the company is that if customer demand for late summer afternoon electricity can be avoided, GSU will not have to construct very expensive new generating capacity to meet that peak demand.

The concept appears simple, but it is a complex process to reduce peak demand and create cost incentives to customers that are effective while not damaging the company's cash flow. Preliminary results of a year-long study conducted with the aid of about 100 customers in the Beaumont, and Port Arthur, Tx., area indicate 85 percent of these customers are willing to shift their energy use if the cost incentives are great enough. While this is encouraging, more research is necessary before the company can seek authorization to institute such rates.

Financial Section

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Management Responsibility for Financial Statements

Management is responsible for the preparation, integrity, and objectivity of the financial statements of Gulf States Utilities Company. The statements have been prepared in conformity with generally accepted accounting principles applied on a consistent basis, except for the change to deferred fuel accounting (see Note 7 to the Financial Statements) and, in some cases, reflect amounts based on estimates and judgment of management, giving due consideration to materiality.

The Company maintains a system of internal controls designed to help give reasonable assurance that the books and records properly reflect the transactions of the Company and that established policies and procedures are followed. Internal control systems are subject to inherent limits in recognition of the need to balance their costs with the benefits they produce. The Company's management strives to maintain this balance.

Coopers & Lybrand, independent certified public accountants, are engaged to examine, in accordance with generally accepted auditing standards, the financial statements of the Company and issue a report thereon, which appears on page 32. Such auditing standards include a review of internal accounting controls, tests of transactions, and other procedures sufficient to provide reasonable assurance that the financial statements are neither materially misleading nor contain material errors.

The Board of Directors, through the Audit Committee of the Board, has general oversight of management's preparation of the financial statements and is responsible for engaging, subject to shareholder approval, the independent accountants. The Committee reviews with the independent accountants the scope of their audits and the accounting principles applied in financial reporting. The Audit Committee meets regularly, both separately and jointly, with independent accountants, representatives of management, and the internal auditors, to review activities in connection with financial reporting. The independent accountants have full and free access to meet with the Audit Committee, without management representatives present, to discuss the results of their examination and their opinion on the adequacy of internal accounting controls and the quality of financial reporting.

Selected Financial Data

For the years ended December 31
(in thousands except per share amounts, ratios and KWH sales)

	1981	1980	1979	1978	1977
Electric Sales (millions of KWH)	**30,697**	30,585	29,742	28,892	26,537
Operating Revenue	**$1,221,714**	$1,005,226	$ 864,338	$ 717,958	$ 587,760
Net Income*	**150,931**	117,189	84,181	70,146	65,650
Income Applicable to Common Stock	**120,550**	92,309	68,559	59,156	55,074
Earnings Per Share of Common Stock:					
Based on average shares outstanding	**2.24**	2.05	1.74	1.73	1.69
Assuming conversion of convertible debentures	**2.20**	1.96	1.65	1.62	1.65
Dividends Per Share of Common Stock	**1.48**	1.39	1.36	1.24	1.15
Total Assets	**3,343,419**	2,925,701	2,439,345	2,059,425	1,758,574
Long-Term Debt and Preferred Stock Subject to Mandatory Redemption	**1,642,894**	1,444,505	1,066,938	877,097	805,656
Capitalization Ratios:					
Common Shareholders' Equity	**34.4%**	32.6%	35.6%	37.4%	33.4
Preferred Stock (not subject to mandatory redemption)	**5.0**	5.8	7.3	7.4	11.5
Preferred Stock (subject to mandatory redemption)	**6.5**	7.5	4.0	1.9	—
Long-Term Debt	**54.1**	54.1	53.1	53.3	55.1
Return on Average Common Equity	**14.21**	12.94	10.91	10.93	11.53
Book Value Per Share, end of year	**$ 15.41**	$ 15.60	$ 15.53	$ 15.50	$ 14.89

*See Note 7 to the Financial Statements for the pro-forma effect of the change in accounting for fuel cost.

Common Stock Prices and Cash Dividends Per Share

For years ended December 31, 1981 and 1980

1981	High	Low	Cash Dividends Paid Per Share	1980	High	Low	Cash Dividends Paid Per Share
Fourth Quarter	$12¾	$10⅞	$.37	Fourth Quarter	$11⅞	$10⅛	$.37
Third Quarter	12¼	10¾	.37	Third Quarter	12¼	10¾	.34
Second Quarter	12⅞	10¾	.37	Second Quarter	13⅝	9¾	.34
First Quarter	12	10⅜	.37	First Quarter	11¾	9	.34

The Common Stock of the Company is listed on the New York, Midwest and Pacific Stock Exchanges. The approximate number of common shareholders on December 31, 1981 was 81,000.

Management's Discussion and Analysis of Results of Operations and Financial Condition

Results of Operations

Net income increased $33,742,000 or 29% during 1981, as compared to 1980, while earnings per share of common stock increased 9% despite the dilutive effect of having 20% additional average shares outstanding. The increase in net income was primarily the result of increased rates placed into effect in 1981, and the latter part of 1980, as well as increased subsidiary earnings during 1981. The increase in subsidiary earnings resulted primarily from a gain realized by Varibus Corporation (Varibus) on an exchange of lignite leases and a change by Varibus in the method used to account for its oil and gas operations (see Note 8 to the Financial Statements). See Note 7 to the Financial Statements for the effect on income of a change in the Company's method of accounting for fuel and purchased power costs.

Operating Revenue

Operating revenue, of which approximately 90% was derived from sales of electricity, increased 22%, 16%, and 20% during 1981, 1980, and 1979, respectively. The primary causes of these increases were increased rates, increased fuel costs which are billed through revenue, and increased sales volume, as detailed below:

	1981	1980	1979
	(in thousands)		
General Rate Increases	**$120,036**	$ 61,771	$ 31,804
Net Changes in Fuel Cost Recovery	**77,519**	57,536	79,167
Sales Volume	**18,933**	21,581	35,409
	$216,488	$140,888	$146,380

The major rate increases granted to the Company have been in electric retail rates. In October, 1981, the Company placed into effect a $63.7 million increase granted by the Public Utility Commission of Texas (PUCT). The PUCT approved and the Company placed into effect a $44 million increase in retail rates in October, 1980, and a $24.9 million increase in November, 1979.

The Company currently has a petition before the Louisiana Public Service Commission (LPSC) requesting an increase in retail rates of approximately $218 million. An order from the LPSC is expected in 1982. The LPSC ordered an electric rate increase of $77.3 million in November, 1980. Of this amount, $27.1 million was placed into effect as an interim rate increase in March, 1980, while the remaining $50.2 million was placed in effect in November, 1980. A $22.9 million increase approved by the Commission was placed in effect in January, 1979.

On a kilowatt hour basis, sales volume increased less than 1% in 1981, and approximately 3% in both 1980 and 1979, when compared with the previous years. Increases in commercial and industrial sales of 5% and 1%, respectively during 1981, were offset by an 11% decrease in sales for resale. The increase in kilowatt hour sales during 1980, was attributable to a 10% increase in sales to residential customers, which was partially offset by a 1% decline in sales to industrial customers. The increased demand of the industrial customers in 1979, was the major cause of the increase in sales volume in that year.

Operating Expenses

The Company's primary operating expenses are fuel for power generation and purchased power. During the three year period from 1979 to 1981, these two expense items amounted to approximately 58% of electric operating revenue. Increases in the unit costs of fuel used for generation was the primary reason for the 27% increase in fuel costs during 1981, as compared to 1980. The increase in purchased power expense during 1981 as compared to 1980, is primarily attributable to increases in the unit price paid for energy purchased. Delays experienced by the Company in the construction of generating units have also resulted in the Company having to purchase additional amounts of power.

The increased availability of lower cost natural gas and the Company's own generating units, including the Company's Sabine Unit 5 which became operational in December, 1979, resulted in a 15% decrease in purchased power costs during 1980 as compared to 1979. Increased Company-owned generation, along with an increase in the unit cost of fuel for generation resulted in a 19% increase in fuel costs during 1980 as compared to 1979.

Operating and maintenance expenses have increased steadily over the past five years. Operating expenses have risen primarily due to increases in gas purchased for resale, labor and material costs, and general administrative costs resulting from inflationary pressures and increased demand for energy services. Maintenance expenses have increased primarily due to the performance of scheduled maintenance of generating units to improve their availability and unscheduled outages of certain generating units.

Depreciation expense has increased primarily due to increases in utility plant in service.

The decrease in federal income taxes during 1981 was primarily the result of recording certain adjustments in accordance with regulatory agency instructions.

Other taxes, primarily property and revenue-related taxes, have increased in the past several years and are expected to continue to rise in the future as a result of growth and inflation.

Non-Operating Items

Increases in allowance for funds used during construction (AFUDC) are primarily due to the increases in the rate used to compute AFUDC, such increases in turn being due to continuing increases in the Company's cost of capital. These increases have been offset in part by increased amounts of construction work in progress included in the rate base, as allowed by the LPSC and the PUCT.

In 1981, the increase in "Non-utility subsidiary operations" resulted primarily from the gain realized by Varibus Corporation on an exchange of lignite leases and a change by Varibus in the method used to account for its oil and gas operations. (See Note 8 to the Financial Statements).

Increases in interest charges on long-term debt are attributable to increased borrowings at substantially higher interest rates.

Financings and Capital Resources

Since 1976, the total assets of the Company have doubled as a result of the extensive on-going construction program, which is expected to continue into the near future. In addition to funding the construction program, the Company must also periodically retire maturing securities (debentures, bonds, and trust obligations) and pay dividends to holders of shares of its outstanding preferred stock.

The Company's construction expenditures for 1981, and as estimated for 1982 and 1983, are as follows:

	1981	1982	1983
	(in thousands)		
Construction expenditures (including AFUDC)	$427,000	$517,000	$602,000
Nuclear fuel and nonutility plant	10,000	6,000	28,000
	$437,000	$523,000	$630,000

Funding of construction expenditures by the participants in jointly-owned facilities (see Note 6 to the Financial Statements) totaled approximately $517 million during 1981, and helped reduce the Company's cash outlay for construction during the year.

The Company's ability to obtain adequate amounts of cash for its operational and construction needs is directly related to (1) revenues generated by sales and the subsequent collection of such amounts, (2) the incurring of additional short-term indebtedness, and (3) the issuance of debt and equity securities.

During 1981, the Company generated 33% of its construction expenditures (including AFUDC) from operations. It is currently estimated that approximately 35% of construction expenditures (including AFUDC) will be generated from operations during 1982 and 1983. The remaining requirements have been and will continue to be obtained through external financing. During 1981, the Company raised approximately $367 million through the issuances of long-term debt and equity securities. The Company repaid $45 million of long-term debt, including the Tur-Gen Trust obligation, during 1981. Additionally, the Company liquidated the Gideon Trust obligation on January 4, 1982 (see Note 4 to the Financial Statements). Average daily short-term borrowings for construction and general corporate purposes totaled approximately $82 million during 1981, down 27% from last year. (For information regarding bank lines of credit and short-term borrowings of the Company, see Note 5 to the Financial Statements).

The Company's Mortgage Indenture places limitations on the amount of first mortgage bonds which the Company is allowed to issue. Based on the results of operations at December 31, 1981, adjusted to give effects to the issuance of $27 million, 16.8% Series, First Mortgage Bonds and $40 million, 17.5% Series, First Mortgage Bonds issued by private placement in January, 1982, (see Note 12 to the Financial Statements) such indenture would allow the Company to issue approximately $177 million of additional first mortgage bonds (assuming a 17.5% rate for such bonds).

During January, 1982, the Company completed modification of the Trust Indenture under which its 7¼% Convertible Debentures due 1992 were issued (see Note 12 to the Financial Statements). The modification eliminates the Indenture's interest coverage covenant thereby increasing the Company's financial flexibility. Prior to the modification, the amount of first mortgage bonds and other funded debt which the Company could issue was limited by the more restrictive Trust Indenture. With the completion of the modification, the issuable amount of first mortgage bonds is limited by the less restrictive Mortgage Indenture, while indenture limitations on the issuable amount of other funded debt have been removed.

Limitations are placed upon the issuance of additional preferred stock by the Company's Restated Articles of Incorporation. Based on the results of operations of the Company as of December 31, 1981, and adjusted for the issuances detailed above, the Company would not be able to issue any additional preferred stock, due to the current high dividend and interest rates.

Statement of Income

For the three years ended December 31
(in thousands except per share amounts)

	1981	1980	1979
Operating Revenue			
Electric	**$1,106,522**	$ 904,871	$769,415
Steam	**77,624**	69,346	68,278
Gas	**37,568**	31,009	26,645
	1,221,714	1,005,226	864,338
Operating Expenses and Taxes			
Fuel (Note 7)	**481,285**	378,794	318,494
Purchased power (Note 7)	**150,463**	136,261	160,882
Other operations	**133,647**	111,928	92,631
Maintenance	**70,867**	57,155	46,700
Depreciation and amortization	**78,194**	73,422	62,887
Taxes			
Income (Note 10)			
Current	**9,343**	8,199	(7,163)
Deferred — net	**(6,252)**	16,000	16,911
Investment tax credits — net	**32,029**	19,972	28,446
Other	**41,845**	34,636	29,240
	991,421	836,367	749,028
Operating Income	**230,293**	168,859	115,310
Other Income and Deductions			
Allowance for equity funds used during construction	**40,741**	40,590	27,260
Non-utility subsidiary operations (Note 8)	**11,498**	(1,398)	(1,283)
Other — net	**1,996**	(3,621)	3,088
Income Before Interest Charges	**284,528**	204,430	144,375
Interest Charges			
Long-term debt	**151,427**	99,198	68,784
Other	**17,698**	20,954	17,539
Allowance for borrowed funds used during construction	**(35,528)**	(32,911)	(26,129)
	133,597	87,241	60,194
Net Income (Note 7)	**150,931**	117,189	84,181
Dividends on Preferred Stock	**30,381**	24,880	15,622
Income Applicable to Common Stock	**$ 120,550**	$ 92,309	$ 68,559
Average Shares of Common Stock Outstanding	**53,851**	44,987	39,310
Earnings Per Share of Common Stock (Note 7)			
Based on average shares outstanding	**$ 2.24**	$ 2.05	$ 1.74
Assuming conversion of convertible debentures	**2.20**	1.96	1.65

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

Statement of Sources of Funds Invested In Utility and Other Plant

For the years ended December 31
(in thousands)

	1981	1980	1979
Provided From Operations			
Net income	**$150,931**	$117,189	$ 84,181
Principal income items not requiring current funds			
Depreciation and amortization	**78,194**	73,422	62,887
Deferred income taxes — net	**(6,252)**	16,000	16,911
Investment tax credits — net	**32,029**	19,972	28,446
Equity component of allowance for funds used during construction	**(40,741)**	(40,590)	(27,260)
Total provided from operations	**214,161**	185,993	165,165
Dividends			
Preferred dividends	**(30,381)**	(24,880)	(15,622)
Common dividends	**(79,379)**	(62,299)	(53,846)
Reinvested funds provided from operations	**104,401**	98,814	95,697
Provided From Financing			
Sales of securities			
Common stock	**132,762**	71,422	50,103
Preferred stock not subject to mandatory redemption	—	—	35,000
Preferred stock subject to mandatory redemption	—	100,000	35,000
First mortgage bonds (principal amount)	**168,000**	175,000	150,000
Guaranteed debentures	**60,000**	—	—
Net change in short-term borrowings	**(20,433)**	(39,579)	8,162
Reduction of long-term debt	**(41,970)**	(17,133)	(11,992)
Equipment purchase obligations	**(16,181)**	8,811	9,784
Revolving credit agreement	**30,000**	160,000	—
Total provided from financing	**312,178**	458,521	276,057
Other Sources and Uses			
Provided from sales of nuclear fuel and other property	**2,823**	6,379	10,818
Temporary cash investments	**(3,300)**	—	33,000
Other — net (including changes in working capital)	**(20,158)**	39,844	(25,419)
Total provided from other sources and uses	**(20,635)**	46,223	18,399
Expenditures for Utility and Other Plant	**395,944**	603,558	390,153
Equity component of allowance for funds used during construction	**40,741**	40,590	27,260
Invested in Utility and Other Plant	**$436,685**	$644,148	$417,413

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

Balance Sheet

December 31
(in thousands)

	1981	1980
Assets		
Utility and Other Plant, at original cost		
Plant in service	**$2,140,180**	$1,978,622
Less: Accumulated provision for depreciation	**743,730**	674,450
	1,396,450	1,304,172
Construction work in progress (Notes 6 and 9)	**1,595,005**	1,335,237
Nuclear fuel (Note 9)	**98,259**	87,934
	3,089,714	2,727,343
Other Property and Investments		
Non-utility subsidiary companies (Note 8)	**32,474**	22,099
Other	**1,960**	1,655
	34,434	23,754
Current Assets		
Cash (Note 5)	**1,208**	1,153
Temporary cash investments	**3,300**	—
Receivables		
Customers	**73,794**	68,519
Notes	**13,333**	8,300
Other	**14,967**	5,087
Materials and supplies, at average cost	**17,545**	15,574
Fuel stock, at average cost	**39,127**	34,677
Prepayments and other	**11,425**	5,379
	174,699	138,689
Deferred Charges		
Unamortized debt expense	**6,716**	5,463
Unamortized project cancellation costs	**17,307**	21,158
Other	**20,549**	9,294
	44,572	35,915
	$3,343,419	$2,925,701
Capitalization and Liabilities		
Capitalization		
(See Statement of Capitalization)		
Common shareholders' equity	**$ 933,383**	$ 763,196
Preferred stock		
Not subject to mandatory redemption	**136,444**	136,444
Subject to mandatory redemption	**175,553**	175,553
Long-term debt	**1,467,341**	1,268,952
	2,712,721	2,344,145
Current Liabilities		
Long-term debt due within one year (Note 4)	**63,691**	61,948
Notes payable (Note 5)		
Banks	**—**	20,000
Commercial paper	**34,745**	35,178
Accounts payable		
Trade	**65,384**	56,213
Subsidiaries	**761**	2,984
Taxes accrued	**16,770**	13,789
Interest accrued	**33,127**	27,484
Other	**57,134**	47,397
	271,612	264,993
Deferred Credits		
Investment tax credits	**145,389**	113,354
Accumulated deferred income taxes	**175,444**	163,521
Other	**11,037**	15,295
	331,870	292,170
Proceeds from Sale of Nuclear Fuel (Note 9)	**27,216**	24,393
Commitments and Contingencies (Note 9)	**—**	—
	$3,343,419	$2,925,701

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

Statement of Capitalization

December 31
(in thousands)

	1981	%	1980	%
Common Shareholders' Equity (Note 2)				
Common stock				
Authorized 100,000,000 shares without par value				
Outstanding 60,574,877 and 48,907,824 shares, respectively	**$ 602,305**		$ 469,543	
Premium and expense on capital stock	**(2,088)**		(2,169)	
Other paid-in capital	**25,876**		25,847	
Retained earnings	**307,290**		269,975	
	933,383	34.4	763,196	32.6
Preferred Stock (Notes 2 and 3)				
Authorized 6,000,000 shares, $100 par, cumulative				
Outstanding 3,119,970 shares.				
Dividend Series / **Shares Outstanding** / **Current Redemption Price**				
Not subject to mandatory redemption				
$ 4.40 — 51,173 — $108.00	**5,117**		5,117	
4.50 — 5,830 — 105.00	**583**		583	
4.40-1949 — 1,655 — 103.00	**166**		166	
4.20 — 9,745 — 102.818	**975**		975	
4.44 — 14,804 — 103.75	**1,480**		1,480	
5.00 — 10,993 — 104.25	**1,099**		1,099	
5.08 — 26,845 — 104.63	**2,685**		2,685	
4.52 — 10,564 — 103.57	**1,056**		1,056	
6.08 — 32,829 — 103.34	**3,283**		3,283	
7.56 — 350,000 — 106.80	**35,000**		35,000	
8.52 — 500,000 — 109.95	**50,000**		50,000	
9.96 — 350,000 — 111.60	**35,000**		35,000	
	136,444	5.0	136,444	5.8
Subject to mandatory redemption				
8.80 — 371,835 — 107.00	**37,183**		37,183	
9.75 — 33,697 — 107.00	**3,370**		3,370	
8.64 — 350,000 — 108.64	**35,000**		35,000	
11.48 — 500,000 — 111.48	**50,000**		50,000	
13.64 — 500,000 — 113.64	**50,000**		50,000	
	175,553	6.5	175,553	7.5
Long-Term Debt (Note 4)				
First mortgage bonds				
Maturing 1982 through 1986 —				
3⅛% due December 1, 1982	**—**		10,000	
3⅛% due December 1, 1983	**10,000**		10,000	
4¼% due September 1, 1986	**15,000**		15,000	
Maturing 1987 through 1996 —				
4% to 17½%	**385,000**		217,000	
Maturing 1997 through 2006 —				
5⅜% to 10.15%	**455,000**		455,000	
Maturing 2007 through 2011 —				
8⅜% to 12.3%	**285,000**		285,000	
Pollution control and industrial development bonds — due 2006 and 2007 — 5.9% to 7%	**48,000**		48,000	
Convertible debentures — due 1992 — 7¼%	**20,483**		44,623	
Guaranteed debentures — due 1988 — 17½%	**60,000**		—	
Equipment purchase obligations	**—**		25,754	
Revolving credit agreement	**190,000**		160,000	
	1,468,483		1,270,377	
Unamortized premium and discount on debt — net	**(1,142)**		(1,425)	
	1,467,341	**54.1**	**1,268,952**	**54.1**
	$2,712,721	100.0	$2,344,145	100.0

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

Statement of Changes in Capital Stock and Retained Earnings

For the years ended December 31, 1979, 1980, and 1981
(in thousands of dollars)

	Preferred Stock					
	Not Subject to Mandatory Redemption	Subject to Mandatory Redemption	Common Stock	Premium (Less Expense)	Other Paid-In Capital	Retained Earnings
Balance: January 1, 1979	$117,936	$ 30,534	$348,018	$ 350	$ 19,297	$226,038
Net income — 1979						84,181
Preferred stock:						
Public offerings (700,000 shares)	35,000	35,000		(1,431)		
Preferred stock recapitalization	(16,492)	10,019			6,550	
Common stock sold:						
Public offerings (3,500,000 shares)			38,546			
Other issuances (919,454 shares)			11,557	(13)		
Dividends declared:						
Preferred stock						(15,622)
Common stock						(53,846)
Balance: December 31, 1979	136,444	75,553	398,121	(1,094)	25,847	240,751
Net income — 1980						117,189
Preferred stock sold (1,000,000 shares)		100,000		(1,045)		
Common stock sold:						
Public offerings (5,000,000 shares)			57,400			
Other issuances (506,868 shares)			14,022	(30)		
Dividends declared:						
Preferred stock						(24,880)
Common stock						(62,299)
Capital stock expense						(786)
Balance: December 31, 1980	136,444	175,553	469,543	(2,169)	25,847	269,975
Net income — 1981						150,931
Common stock sold:						
Public offering (8,000,000 shares)			92,375			
Other issuances (2,041,481 shares)			16,596	81	29	
Conversion of Debentures (1,625,572 shares)			23,791			
Dividends declared:						
Preferred stock						(30,381)
Common stock						(79,379)
Capital stock expense						(3,856)
Balance: December 31, 1981	$136,444	$175,553	$602,305	$(2,088)	$ 25,876	$307,290

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

Notes to Financial Statements

1. Summary of Significant Accounting Policies

System of Accounts. The accounting records of the Company are maintained in accordance with the Uniform System of Accounts as prescribed by the Federal Energy Regulatory Commission (FERC) and adopted by the Louisiana Public Service Commission (LPSC) and the Public Utility Commission of Texas (PUCT).

Utility and Other Plant. Utility and other plant is stated at original cost when first dedicated to public service and the amounts shown do not represent reproduction costs or current values. Costs of repairs and minor replacements are charged to expense as incurred. The original cost of depreciable utility plant retired and cost of removal, less salvage, are charged to accumulated provision for depreciation. The provision for depreciation is computed using the straight-line method at rates which will amortize the unrecovered cost of depreciable plant over the estimated remaining service life.

Composite depreciation rates were as follows:

	1981	1980	1979
Electric	**3.70%**	3.72%	3.76%
Steam	**2.80**	2.77	2.79
Gas	**3.50**	3.57	3.49
Total Company	**3.68**	3.69	3.74

Allowance for Funds Used During Construction and Capitalization of Interest. Allowance for funds used during construction (AFUDC) is a non-cash item which is calculated under guidelines prescribed by the FERC and is capitalized as part of the cost of utility plant representing the cost of servicing the capital invested in Construction Work in Progress (CWIP). Effective April 1, 1981, the rate used to compute AFUDC was increased to a 9% net rate compounded semi-annually from the 8.5% net rate in effect since January 1, 1981. The rate used in 1980, was 8.0% (net) compounded semi-annually and 7.6% (net) compounded effective July 1, 1979. Prior to July, 1979, the Company used a net rate of 7.5% (simple). In January, 1982, the rate used to compute AFUDC was increased to 9.5%.

Such AFUDC has been segregated into two component parts — borrowed and equity funds. That portion allocated to borrowed funds is reflected as an adjustment to interest charges. Interest incurred by certain trusts (see Notes 4 and 9) is included in interest expense in the statement of income and a corresponding amount is included as part of the borrowed funds component of AFUDC.

Revenue, Fuel and Purchased Power. The Company records revenue as billed to its customers on a cycle billing basis. Revenue is not recorded for energy delivered and unbilled at the end of each fiscal period. Rate schedules of the Company provide for adjustments to substantially all rates for increases or decreases in the costs of fuel for generation, purchased power, and gas distributed. Fuel and purchased power costs in excess of those included in base rates are deferred until such costs are billed to customers. If costs fall below the levels included in base rates, the difference is accrued and subsequently credited to customers.

Income Taxes. The Company and its subsidiaries file a consolidated federal income tax return. Income taxes are allocated to the individual companies based on their respective taxable income or loss and investment tax credits.

The Company follows a policy of comprehensive interperiod income tax allocation where such treatment is permitted for ratemaking purposes by regulatory bodies. Deferred federal income taxes result from timing differences in the recognition of revenue and expenses for tax and accounting purposes. These deferred income taxes are charged to income and concurrently credited to accumulated deferred income taxes.

Investment tax credits have been deferred and are being amortized ratably over the useful lives of the related property. The Company claims the additional 1½% investment tax credit, as provided by the Internal Revenue Code, under the provisions of the Employee Stock Ownership Plan (ESOP).

Non-Utility Subsidiary Companies. The Company has made investments in and advances to non-utility subsidiary companies and accounts for its investments on the equity basis.

Employee Benefits. The Company has a contributory pension plan covering all employees meeting certain age and service requirements. The accrued cost of this plan is being funded. Past and prior service costs are being funded and amortized by the Company over a thirty-year period.

Earnings Per Share. Earnings per share are based on the weighted average number of common shares outstanding during the period. Earnings per share assuming conversion of convertible debentures are based on the weighted average number of common shares outstanding plus the shares which would have been issued if the outstanding convertible debentures had been converted on the date of original issue, after giving effect to the elimination of related interest expense, amortization of bond discount, and expense of issue (net of related income taxes). The number of shares for the latter computation was approximately 55,231,000, 47,992,000 and 42,600,000, for the years 1981, 1980 and 1979, respectively.

2. Capital Stock and Retained Earnings

At December 31, 1981, the Company had authorized 10,000,000 shares of no par preferred stock (none issued) and 20,000,000 shares of no par preference stock (none issued). The Company's Restated Articles of Incorporation places limitations on the issuance of additional preferred stock. For information with respect to the amount of preferred stock currently issuable subject to this limitation, see "Management's Discussion and Analysis of Results of Operations and Financial Condition." There are no limitations on the issuance of preference stock.

At December 31, 1981, the Company had reserved 2,398,097 shares of common stock to be issued in connection with its employee benefit plans and dividend reinvestment plan.

Certain limitations on the payment of cash dividends on common stock are contained in the Company's Restated Articles of Incorporation and indentures. The most restrictive limitation is contained in the Trust Indenture, dated as of September 1, 1977. Based on such limitations, the retained earnings available for payment of dividends as of December 31, 1981 and 1980, amounted to approximately $212 million and $171 million, respectively (see Note 3 for restrictions on common dividends under the sinking fund provisions for preferred stock).

3. Preferred Stock Subject to Mandatory Redemption

The Company consummated, in January, 1979, an exchange of certain series of its preferred stock not subject to mandatory redemption for shares of its $8.80 and $9.75 Dividend Preferred Stock subject to mandatory redemption, with the result of an increase in other paid in capital. The $8.80 and $9.75 Dividend Preferred Stock are entitled to mandatory sinking funds sufficient to retire 3% of the shares of each series beginning in 1984. The $8.64, $11.48, and $13.64 Dividend Preferred Stock are entitled to mandatory sinking funds sufficient to retire 4% of the shares of each series beginning in the sixth year after the date of issuance. The aggregate sinking fund requirements are approximately $1,217,000, $2,617,000, and $6,617,000 in 1984, 1985, and 1986, respectively. Preferred stock sinking fund provisions restrict the payment of common stock dividends and the purchase of such stock by the Company unless the sinking fund requirements are met.

4. Long-Term Debt

The Company's Mortgage contains sinking fund provisions which require, generally, that the Company make annual cash deposits equal to 1.2% of the greatest aggregate principal amount of first mortgage bonds subsequently authenticated and delivered or, in lieu thereof, to apply property additions or reacquired first mortgage bonds for that purpose. The Company has satisfied the mortgage requirements in past years by certifying "available net additions" to the trustee. Sinking fund requirements on the first mortgage bonds which the Company currently plans to meet by certifying "available net additions" to the trustee for each of the five years subsequent to December 31, 1981, are as follows:

1982 — $10,704,000
1983 — $10,584,000
1984 — $10,464,000
1985 — $10,464,000
1986 — $10,284,000

The Company's Mortgage Indenture contains an interest coverage covenant which limits the amount of first mortgage bonds which the Company may issue. For information with respect to the additional amount of first mortgage bonds which the Company is currently able to issue subject to this limitation, see "Management's Discussion and Analysis of Results of Operations and Financial Conditions."

At December 31, 1981, the 7¼% Convertible Debentures could be converted into the Company's common stock at a price of $14.85 per share (see Note 12 for information concerning indenture modification). The closing market price of the Company's common stock at December 31, 1981 was $11⅞.

During 1978, the Company entered into two agreements whereby the Company assigned its right to purchase turbine generators to certain trusts (the Gideon Trust and the Tur-Gen Trust). The agreements provided that the trusts would make required payments to the turbine generator's manufacturers and the Company would purchase such generators from the trusts for an amount equal to the payments made plus certain carrying costs, including interest which varied with the prime interest rate.

During March, 1981, and January, 1982, respectively, the Company liquidated the Tur-Gen and Gideon Trust obligations upon payment of $27,583,000 and $53,760,000, respectively. Interest on the trusts totaled approximately $10,212,000, $8,013,000, and $6,126,000 during 1981, 1980, and 1979, respectively.

During March, 1980, the Company entered into a revolving credit agreement which bears interest at the prime rate (15¾% at December 31, 1981). Under the terms of the agreement, the Company can borrow up to $200,000,000 in principal amounts of $5,000,000 or more until September, 1982. Such borrowings are payable over a five-year period beginning in 1982.

5. Short-Term Borrowings

As of December 31, 1981, the Company had agreements with banks and banking institutions which provided for committed lines of credit totaling approximately $250,000,000. Interest rates associated with these lines range from the prime rate to 108% of the prime rate; London Interbank Offering Rate (LIBOR) + ⅜% to LIBOR + ⅝% or a mutually agreeable rate to be determined at the time of borrowing. Commitment fees range from ⅛ of 1% to ½ of 1% of amount of available credit. In lieu of commitment fees, certain banks require a cash balance be maintained equal to 5% to 10% of the commitment.

Information regarding short-term debt outstanding is as follows:

	1981	1980
	(In thousands)	
Maximum amount outstanding at any one time	**$159,035**	$168,225
Average daily outstanding	**81,712**	111,984
Weighted average interest rate for amount outstanding at year-end	**13.28%**	16.75%
Weighted average annual interest rate(a)	**17.74%**	13.69%

(a) Calculated by dividing the sum of the effective interest for the year by the average daily short-term debt outstanding.

6. Jointly-Owned Facilities

The Company owns undivided interests in certain generating units currently under construction as detailed below:

Generating Station	Scheduled In-Service Date	Company Share	Company's Pro Rata Share of Expenditures
			(In thousands)
Roy S. Nelson Unit 6 (Coal — 540 MW)	1982	70%	$348,865
Big Cajun 2 Unit 3 (Coal — 540 MW)	1983	42	102,595
River Bend Unit 1 (Nuclear — 940 MW)	1985	70	892,400

Participants in Nelson Unit 6 are Sam Rayburn Municipal Power Agency (SRMPA) with a 20% ownership share and Sam Rayburn G&T (SRG&T) with a 10% interest. SRG&T funded total construction expenditures from June, 1980 through September, 1980, and have since funded their proportionate share of the costs. SRMPA began funding all construction costs, except those funded by SRG&T, in July, 1981, and continued to do so until November, 1981, when such funding reached its proportionate share. SRMPA has since funded its 20% ownership share.

The Company began funding total costs of Cajun Electric Power Cooperative's (CEPCO) Big Cajun 2 Unit 3 in April, 1981, and will continue to do so until its cumulative contributions reach its proportionate share of the costs of the unit. The Company will then fund its share of the costs. CEPCO is the project manager and will operate this unit.

Participants in River Bend Unit 1 are CEPCO with a 30% ownership share and SRG&T with a proposed 7% ownership share. CEPCO began funding total construction costs in January, 1981, and continued to do so until November, 1981, when such funding reached CEPCO's proportionate share of total construction costs. CEPCO then began funding its proportionate share.

SRG&T's participation in River Bend Unit 1 is subject to approval by the Rural Electrification Administration (REA). The Company has been advised that the REA presently does not intend to approve SRG&T's pending application for participation in River Bend Unit 1. Therefore, the Company intends to seek further consideration by the REA relative to such participation. No assurance can be given to if and when the actual approval might be granted. If SRG&T does not participate in the unit and the Company is unable to obtain other participants, the Company would assume SRG&T's ownership share.

The Company expects to utilize all of the energy generated by its share of the capacity of Big Cajun 2 Unit 3 at the time this unit is placed in service. In addition, the Company has various agreements with the participants in Nelson Unit 6 and River Bend Unit 1 whereby, after each unit goes into commercial operation, the Company will be obligated to purchase a portion of each participant's share of capacity of each unit. In the first year of commercial operation of the units, the Company has agreed to purchase 100% of the participants' share of the unit's capacity. Thereafter, the Company is obligated to purchase declining amounts for periods ranging from three to 14 years. The fixed costs applicable to the buy-backs of power are based in part on final unit costs and other variable factors and are not determinable at this time. The variable costs associated with such buy-backs will be composed of fuel costs and operations and maintenance expenses.

7. Change in Accounting for Fuel

In June, 1981, at the urging and authorization of the LPSC, the Company changed its method of accounting for fuel and purchased power costs in Louisiana. The change, effective January 1, 1981, results in the Company deferring or accruing on its books any under or over recovered fuel and purchased power costs in excess of those included in base rates until such costs are reflected in billings to customers pursuant to its Louisiana fuel adjustment clause. The cumulative effect of the

change on prior years is immaterial and included in income for 1981. The effect of the change for the year 1981 was to decrease net income by $4.8 million ($.09 per share). The pro forma effects of the change in accounting for fuel, assuming the new method were applied retroactively, are shown below.

	1981	1980	1979
	(in thousands except per share amounts)		
Net Income	**$150,931**	$117,189	$84,181
Earnings per share based on average shares outstanding	**2.24**	2.05	1.74
Earnings per share — assuming conversion of convertible debentures	**2.20**	1.96	1.65
Pro forma amounts assuming change in accounting for fuel costs applied retroactively:			
Net Income	**$150,931**	$113,571	$87,696
Earnings per share — based on average shares outstanding	**2.24**	1.97	1.84
Earnings per share — assuming conversion of convertible debentures	**2.20**	1.88	1.74

8. Non-Utility Subsidiary Companies

On July 28, 1981, the Company acquired Prudential Drilling Company (Prudential), through an exchange of 588,000 shares of Gulf States common stock for all of the common stock of Prudential. The Company accounted for this transaction as a pooling-of-interests. Both Prudential and Varibus Corporation (Varibus), the Company's other wholly-owned non-utility subsidiary, are engaged primarily in the exploration, development, and operation of oil and gas properties.

During 1981, in order to conform to the method used by Prudential, Varibus changed its method of accounting for oil and gas operations to the full cost method of accounting. Due to the immaterial effect on prior periods, the cumulative effect of the change is included in income for 1981. Earnings per share of common stock based on average shares outstanding and earnings per share of common stock assuming the conversion of convertible debentures were increased $.07 due to the change in accounting method.

On September 11, 1981, Varibus and Northwestern Resources Company exchanged certain lignite holdings in Central and East Texas. Varibus acquired lignite property in East Texas and received cash consideration of approximately $14 million (of which $2 million was received in 1980) in exchange for lignite properties in Central Texas. For 1981, the exchange transaction had the effect of increasing net income and income applicable to common stock by approximately $7.6 million and both earnings per share of common stock based on average shares outstanding and assuming the conversion of convertible debentures by $.14.

9. Commitments and Contingencies

In 1978, the Company sold a portion of its uranium inventory to the Uranox Trust for approximately $55,836,000 (the Company's book value). The Company may repurchase the uranium inventory for an amount equal to the trust's cost plus interest and other costs incurred to the date the options are exercised. The balance sheet at December 31, 1981 and 1980, included $27,216,000 and $24,393,000, respectively, recorded in "Utility and Other Plant, at original cost — Nuclear Fuel" and "Proceeds from Sale of Nuclear Fuel." Interest costs for the years ended December 31, 1981, 1980, and 1979, were $2,823,000, $5,994,000, and $8,320,000, respectively.

In 1980, the Company sold a portion of the uranium oxide inventory previously held by the trust. These sales reduced the level of "Proceeds from Sale of Nuclear Fuel" in 1980 approximately $47,100,000. A total of 927,000 pounds and 216,000 pounds of the inventory was sold to participants in River Bend Unit 1, CEPCO and SRG&T, respectively (see Note 6). SRG&T purchased the uranium oxide using funds from a $70 million interim financing. If SRG&T does not obtain, by mid-1982, a long-term loan guaranteed by REA sufficient in amount to pay all of its cost of purchasing such concentrates, the Company has agreed to purchase the concentrates owned by SRG&T at the cost to SRG&T plus its carrying charges.

Since June, 1980, SRG&T has been using the balance of the funds from the interim financing to pay construction costs of Nelson Unit 6 in order to earn its co-ownership interest in the unit (see Note 6). If SRG&T does not secure the necessary loan guarantees, the Company would be required to purchase SRG&T's ownership interest in Nelson Unit 6.

The 1982 construction program is currently estimated to be $523,000,000, including approximately $83,000,000 of AFUDC. This amount has been reduced by the participants' funding of their interests in the units under construction (see Note 6). In connection with the construction program, the Company has incurred substantial commitments, some of which are related to 1983 and subsequent years.

Various state and federal laws require governmental permits prior to construction and operation of certain facilities. Substantial expenditures and commitments are made prior to obtaining such permits. Unless and until events occur making such permits unobtainable, no provision is made in the financial statements for possible losses which could occur if such permits should not be obtained.

Construction of River Bend Unit 2, a 940 MW boiling water nuclear reactor unit has been deferred pending the completion of River Bend Unit 1. Total Company expenditures on this unit through December 31, 1981 were $63.9 million excluding $20 million of AFUDC.

10. Income Taxes

The provisions for federal income tax were less than the amounts computed by applying the federal income statutory tax rate to pre-tax income. The reasons for these differences are as follows:

	1981	1980	1979
Statutory Rate	**46.0%**	46.0%	46.0%
Increases (decreases) resulting from:			
Exclusions from taxable income of AFUDC	**(17.3)**	(15.9)	(17.4)
Items capitalized for book purposes, but expensed for tax purposes	**(1.6)**	(2.4)	(2.0)
Effect of excess book depreciation over straight-line tax depreciation	**3.5**	4.0	6.5
Adjustment for prior years taxes and other regulatory adjustments	**(7.2)**	(1.3)	—
Equity in earnings of non-utility subsidiaries	**(2.9)**	.4	(.1)
Other items	**(2.1)**	(.6)	(2.1)
Effective Tax Rate	**18.4%**	30.2%	30.9%

Deferred income tax expense results from timing differences in the recognition of revenue and expenses for tax and accounting purposes. The sources of the differences between book and tax income which were used to reduce the Company's current tax liability for the respective years were:

	1981	1980	1979
		(in thousands)	
Excess of accelerated tax depreciation over straight-line depreciation	**$ 7,231**	$10,865	$ 8,955
Items expensed for tax purposes, but capitalized as depreciable plant for book purposes	**(4,634)**	4,891	5,762
Excess of accelerated amortization of pollution control facilities over straight-line tax depreciation	**2,373**	2,371	2,377
Cancellation costs of proposed nuclear units expensed for tax purposes in 1978, to be amortized for book purposes	**(1,659)**	(1,594)	(136)
Fuel and purchased power expense deferred (accrued) for book purposes	**(7,270)**	—	—
Items expensed for book purposes but deferred for tax purposes	**(2,300)**	—	—
Other	**7**	(533)	(47)
	$ (6,252)	**$16,000**	**$16,911**

The Company was able to reduce its income tax liability for the years 1981, 1980, and 1979 by utilizing investment tax credits. At December 31, 1981, the Company had accumulated carryforwards of investment tax credit of $40,800,000. These carryforwards expire through 1996, and will be used to reduce income taxes in future years. The investment tax credit utilization limit is increasing progressively, from a maximum of 70% of the income tax liability (before application of the investment tax credit) in 1980 to 80% in 1981 and 90% in 1982 and subsequent years.

11. Employee Benefits

The total costs of the Company's contributory pension plan for the years ended December 31, 1981, 1980, and 1979, were $6,696,000, $5,393,000, and $3,730,000, respectively. Of such amounts, $4,245,000, $3,506,000, and $2,447,000, respectively, were charged to income and the balance of such costs for each period were charged to construction and other accounts.

The valuation date of the latest pension information is January 1 of the subsequent years for each plan year ended December 31. The information for the plan years 1980 and 1979, is shown below. Such valuation information is not yet available with respect to plan year 1981.

	1980	1979
	(in thousands except percents)	
Actuarial present value of accumulated plan benefits:		
Vested	**$41,742**	$38,798
Nonvested	**2,573**	2,531
Present value of accumulated plan benefits	**$44,315**	$41,329
Net assets available for benefits	**$59,008**	$50,027
Assumed rate of return in determining actuarial present values of plan benefits	**9%**	8%

12. Subsequent Events — Financings

In accordance with prior commitments, the Company sold $40,000,000 principal amount of First Mortgage Bonds, 17½% Series, and $27,000,000 principal amount of First Mortgage Bonds, 16.8% Series, by private placement on January 13, 1982 and January 14, 1982, respectively. The proceeds from both issuances were used to reduce outstanding loans under the Company's $200 million revolving credit facility and short-term debt incurred primarily in connection with the Company's construction program.

During January, 1982, the Company completed modification of the Trust Indenture under which its 7½% Convertible Debentures due 1992 were issued. The modification eliminates the Indenture's interest coverage covenant thereby increasing the Company's financial flexibility. In return for the necessary consents of two-thirds of the debenture holders, the Company reduced the price at which the debentures could be converted into common stock from $14.85 to $13.25 per share.

13. Quarterly Financial Information (Unaudited)

(In thousands except per share amounts)

				Earnings Per Share of Common Stock*	
	Operating Revenue	Operating Income	Net Income	Based On Average Shares Outstanding	Assuming Conversion of Convertible Debentures
1981					
First Quarter	**$266,123**	**$47,986**	**$27,333**	**$.40**	**$.39**
Second Quarter	**320,607**	**53,023**	**32,994**	**.50**	**.49**
Third Quarter	**373,116**	**74,724**	**61,415**	**.97**	**.95**
Fourth Quarter	**261,868**	**54,560**	**29,189**	**.37**	**.37**
1980					
First Quarter	227,873	27,685	20,279	.34	.33
Second Quarter	242,539	42,125	29,424	.54	.52
Third Quarter	297,511	54,378	45,292	.85	.81
Fourth Quarter	237,303	44,671	22,194	.31	.30

* Individual quarterly amounts may not add to annual amounts since the per share amounts are based upon the average number of shares outstanding during each quarter.

In June, 1981, the Company changed its method of accounting for fuel and purchased power costs effective January 1, 1981 (see Note 7). The effect of the change on the first quarter of 1981, had the new method been in effect, would have been to increase net income by $6,824,000 ($.14 per share). The financial information presented for the first quarter of 1981, has been restated to reflect this change in accounting method.

See Note 8 for details concerning the exchange of lignite leases between Varibus and a third party during the third quarter of 1981.

14. Supplemental Information on Changing Prices (Unaudited)

The following supplementary information is supplied in accordance with the requirements of the Statement of Financial Accounting Standards (SFAS) No. 33 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 Consumers Price Index for all Urban Consumers. 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 utility and other plant, which includes land, land rights, nuclear fuel, plant held for future use, and construction work in progress, represents the estimated cost of replacing existing plant assets and was determined by indexing surviving plant by the Handy-Whitman Index of Public Utility Construction Costs. The current year's provision for depreciation on the constant dollar and current cost amounts of utility and other plant was determined by applying the Company's depreciation rates to the indexed plant amounts.

Fuel inventories, the cost of fuel used in generation, and gas purchased for resale have not been restated from their historical cost in nominal dollars. Regulation limits the recovery of fuel and purchased costs 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 SFAS No. 33, income taxes were not adjusted.

Under the rate-making prescribed by the regulatory commissions to which the Company is subject, only the historical cost of plant is recoverable in revenue 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 utility and other plant, 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 reflect properly the economics of rate regulation in the statement of income adjusted for changing prices, the reduction of net utility and other plant 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 utility and other plant. 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 Income Adjusted for Changing Prices (Unaudited)

For the year ended December 31, 1981	Conventional Historical Cost	Constant Dollar Average 1981 Dollars	Current Cost Average 1981 Dollars
		(in thousands)	
Operating revenue	$1,221,714	$1,221,714	$1,221,714
Fuel	481,285	481,285	481,285
Purchased power	150,463	150,463	150,463
Other operations, maintenance, and gas for resale	204,514	204,514	204,514
Depreciation and amortization	78,194	171,516	184,691
Taxes	76,965	76,965	76,965
Other — net	(54,235)	(54,235)	(54,235)
Interest charges	133,597	133,597	133,597
	1,070,783	1,164,105	1,177,280
Net Income (excluding reduction to net recoverable cost)	$ 150,931	$ 57,609*	$ 44,434
Increase in specific prices (current cost) of utility and other plant held during the year**			$ 145,274
Reduction to net recoverable cost		$ (154,325)	107,835
Effect of increase in general price level			(394,259)
Excess of increase in general price level over increase in specific prices after reduction to net recoverable cost			(141,150)
Gain from decline in purchasing power of net amounts owed		164,547	164,547
Net		$ 10,222	$ 23,397

* Including the reduction to net recoverable cost, the loss on a constant dollar basis would have been $96,716 for 1981.

** At December 31, 1981 current cost of utility and other plant, net of accumulated depreciation was $4,808,815 while historical cost or net cost recoverable through depreciation was $3,089,714.

Five Year Comparison of Selected Supplementary Financial Data Adjusted for Effects of Changing Prices (Unaudited)

	Years Ended December 31,				
	1981	1980	1979	1978	1977
	(in thousands of average 1981 dollars)				
Operating revenue	$1,221,714	$1,109,496	$1,083,007	$1,000,879	$882,126
Historical cost information adjusted for general inflation:					
Net income (excluding reduction to net recoverable cost)	57,609	41,603	27,078		
Net income per common share (after dividend requirements on preferred stock)	.51	.31	.19		
Net assets at year-end at net recoverable cost	1,029,054	947,987	947,856		
Current Cost Information:					
Net income (excluding reduction to net recoverable cost)	44,434	22,179	6,888		
Income (Loss) per common share (after dividend requirements on preferred stock and excluding reduction to net recoverable cost)	.26	(.12)	(.32)		
Excess of increase in general price level over increase in specific prices after reduction to net recoverable cost	(141,150)	(227,198)	(214,379)		
Net assets at year-end at net recoverable cost	1,029,054	947,987	947,856		
General Information:					
Gain from decline in purchasing power of net amounts owed	164,547	207,132	198,790		
Cash dividends declared per common share	$ 1.48	$ 1.53	$ 1.70	$ 1.73	$ 1.73
Market price per common share at year-end	11.49	12.25	13.03	15.77	20.31
Average consumer price index	272.4	246.8	217.4	195.4	181.5

To the Shareholders of Gulf States Utilities Company:

We have examined the balance sheet and statement of capitalization of GULF STATES UTILITIES COMPANY as of December 31, 1981 and 1980, and the related statements of income, sources of funds invested in utility and other plant and changes in capital stock and retained earnings for each of the three years in the period ended December 31, 1981. 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 financial statements referred to above present fairly the financial position of GULF STATES UTILITIES COMPANY as of December 31, 1981, and 1980, and the results of its operations and sources of its funds invested in utility and other plant and changes in capital stock and retained earnings for each of the three years in the period ended December 31, 1981, in conformity with generally accepted accounting principles applied on a consistent basis except for the change, with which we concur, in the method of accounting for fuel costs as described in Note 7 to the financial statements.

COOPERS & LYBRAND

Houston, Texas
February 2, 1982

Statistical Summary

For the years ended December 31	1981	1980	1979	1978	1977
Electric Department					
Number of Customers —					
End of Year					
Residential	**455,160**	438,560	423,850	407,761	391,031
Commercial	**52,955**	52,731	50,807	48,892	47,352
Industrial	**3,852**	3,414	3,386	3,392	3,379
Temporary construction	**2,871**	3,354	3,279	4,304	4,389
Other	**1,974**	1,984	1,873	1,790	1,690
	516,812	500,043	483,195	466,139	447,841
Sales —					
Thousands of KWH					
Residential	**5,717,715**	5,682,016	5,147,436	5,198,421	4,789,630
Commercial	**4,178,126**	3,969,390	3,759,289	3,738,114	3,486,193
Industrial	**15,066,330**	14,870,419	14,961,211	14,447,417	13,216,824
Temporary construction	**50,306**	37,691	44,059	42,358	23,017
Other	**2,797,761**	3,098,910	2,638,490	2,452,228	2,025,933
	27,810,238	27,658,426	26,550,485	25,878,538	23,541,597
Steam	**2,886,782**	2,927,056	3,191,464	3,012,993	2,995,619
	30,697,020	30,585,482	29,741,949	28,891,531	26,537,216
Average Annual KWH Use					
Per Customer					
Residential	**12,786**	13,173	12,374	13,009	12,480
Commercial	**79,558**	76,529	75,291	77,472	74,875
Industrial	**4,095,224**	4,340,461	4,402,946	4,221,922	3,858,927
Electric Energy					
Output — Thousands of KWH					
Net Generated	**28,115,700**	27,775,374	25,381,996	28,299,011	26,295,869
Net Purchased and Interchanged	**4,411,795**	4,507,245	5,871,615	1,985,508	1,603,807
	32,527,495	32,282,619	31,253,611	30,284,519	27,899,676
Peak Load, Including Interruptible Load — Kilowatts	**5,541,600**	5,604,400	5,229,300	5,137,700	4,656,800
Total Capability, Including Contract Purchases at Time of Peak Load — Kilowatts	**6,745,000**	6,602,000	6,169,000	5,737,000	5,734,000
Annual Load Factor	**67.0%**	65.2%	68.2%	67.3%	68.4%
Steam Department					
Steam Sales — Millions of Pounds	**12,209**	14,906	14,796	15,787	16,987
Gas Department					
Number of Customers — End of Year	**85,664**	85,218	83,910	82,391	80,116
Sales — MCF	**8,598,822**	9,097,207	9,891,822	10,207,194	9,865,995

Directors

*John W. Barton
President-Jack's Cookie Company
Baton Rouge, La. (1970)

W. Donham Crawford
Honorary Chairman of the Board and
former Chief Executive Officer
Beaumont, Tx. (1977)

Edwin Hiam
Investment Adviser
Boston, Mass. (1959)

Dr. Frederic A. Holloway
Consultant
Retired Exxon Vice President — Science and Technology
Baton Rouge, La. (1979)

William H. LeBlanc, Jr.
President — Baton Rouge Supply Co., Inc.
Baton Rouge, La. (1974)

Norman R. Lee
President and Chief Operating Officer
Beaumont, Tx. (1967)

*Paul W. Murrill
Chairman of the Board and
Chief Executive Officer
Beaumont, Tx. (1978)

Alvin T. Raetzsch, Sr.
Retired Assistant to the Vice President and
General Manager — U.S. Chemical Division of
PPG Industries, Inc.
Lake Charles, La. (1975)

Monroe J. Rathbone, Jr.
Medical doctor and partner — The Surgical Clinic
Baton Rouge, La. (1975)

Lorene L. Rogers
President Emeritus, The University of
Texas at Austin
Austin, Tx. (1976)

*Nathaniel S. Rogers
President — First City Bancorporation of
Texas, Inc.; Chairman of the Board —
First City National Bank of Houston
Houston, Tx. (1978)

*Bismark A. Steinhagen
Partner — Steinhagen Oil Co.
Beaumont, Tx. (1974)

James E. Taussig II
Real Estate Development
Lake Charles, La. (1975)

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* Executive Committee
( ) Year Elected

Officers

Chairman
Paul W. Murrill (0) [47]
Chairman of the Board and Chief Executive Officer

President
Norman R. Lee (33) [57]
President and Chief Operating Officer

Executive Vice Presidents
Joseph E. Bondurant (24) [52]
Executive Vice President — Operations

Joseph L. Donnelly (3) [52]
Executive Vice President — Finance

Edward M. Loggins (23) [51]
Executive Vice President — Administration and Technical Services

Senior Vice Presidents
Thomas H. Burbank (3) [60]
Senior Vice President — Accounting Services and Rates

William J. Cahill, Jr. (2) [58]
Senior Vice President — River Bend Nuclear Group

E. Linn Draper (3) [40]
Senior Vice President — Engineering and Technical Services

Vice Presidents
James R. Aldridge (2) [51]
Vice President — Human Resources

William H. Barksdale (24) [50]
Vice President — Technical Services

Philip T. Boerger (3) [57]
Vice President — Fossil Projects

James H. Derr, Jr. (41) [61]
Vice President — Power Plant Engineering and Design

Anthony F. Gabrielle (2) [54]
Vice President — Computer Applications

Charles D. Glass (32) [53]
Vice President — Texas Operations

Calvin J. Hebert (19) [47]
Vice President — Financial Services

William J. Jefferson (2) [52]
Vice President — Rates and Regulatory Affairs

Fred C. Repper (3) [54]
Vice President — Public Affairs

Edward J. Serwan (3) [60]
Vice President — Production

Aubrey D. Sprawls (32) [53]
Vice President — Consumer Services

Summa L. Stelly (33) [56]
Vice President — Louisiana Operations

J. Gary Weigand (4) [46]
Vice President — Nuclear Operations

Jasper F. Worthy (26) [53]
Vice President — General Services

Division Vice Presidents
John W. Conley (24) [50]
Division Vice President — Western

James E. Moss (23) [46]
Division Vice President — Baton Rouge

Arden D. Loughmiller (21) [44]
Division Vice President — Beaumont

J. Ted Meinscher (31) [49]
Division Vice President — Lake Charles

Ronald M. McKenzie (14) [41]
Division Vice President — Port Arthur

Other Officers
Leslie D. Cobb (26) [47]
Secretary

Bobby J. Willis (20) [46]
Controller

Jack L. Schenck (1) [43]
Treasurer

Roy E. Eyler (23) [57]
Assistant Secretary

Jon P. Trevelise (1) [36]
Assistant Controller

Clyde W. McBride (4) [30]
Assistant Treasurer

( ) years of service [ ] age

Principal Offices

350 Pine Street
Beaumont, Texas 77701

Divisions

285 Liberty Avenue
Beaumont, Texas 77701

1540 Ninth Avenue
Port Arthur, Texas 77640

Highway 75 North
Conroe, Texas 77301

446 North Boulevard
Baton Rouge, Louisiana 70802

314 Broad Street
Lake Charles, Louisiana 70601

Stockholder Information

Stock Listing

Gulf States Utilities Company is traded under the symbol GSU on New York, Midwest, Philadelphia and Pacific Stock Exchanges.

Stock Transfer Agents

Texas Commerce Bank Beaumont, N.A.
Beaumont, Texas

Morgan Guaranty Trust Company
New York, New York

First National Bank of Chicago
Chicago, Illinois

Registrars

First Security Bank of Beaumont, N.A.
Beaumont, Texas

Morgan Guaranty Trust Company
New York, New York

Northern Trust Company
Chicago, Illinois

Dividend Reinvestment Agent

Gulf States Utilities Company
P. O. Box 1671
Beaumont, Texas 77704

Form 10-K

The Form 10-K Annual Report to the Securities and Exchange Commission will be available March 31, 1982. Copies of Form 10-K and GSU's 1981 Financial and Statistical Report can be obtained without charge from Leslie D. Cobb, Secretary, P. O. Box 2951, Beaumont, Texas 77704.

Notice of Annual Meeting

The 1982 annual meeting of shareholders will be held at 2 p.m., Thursday, May 13, 1982, in the company headquarters, 350 Pine Street, Beaumont, Texas. Formal notices of the meeting, proxy statements and proxies will be mailed to the common shareholders about April 2, 1982. Shareholders are invited to attend, but if they cannot, they are urged to fill out and return their proxies.

Gulf States Utilities
P. O. Box 2951
Beaumont, Texas 77704