Illinois Power Company

1987
Annual
Report

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Illinois Power Company 1987 Annual Report

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Illinois Power Company is a public utility engaged principally in the generation, transmission, distribution, and sale of electric energy and the distribution and sale of natural gas solely in the State of Illinois. The Company's territory is approximately 15,000 square miles, or one-quarter of the state. The Company serves approximately 543,000 customers.

Principal Office

Monticello, Illinois 61856

Executive Office

500 South 27th Street, Decatur, Illinois 62525
Phone (217) 424-6600

Transfer Agent and Registrar

Continental Illinois National Bank and Trust Company of Chicago
231 South LaSalle Street, Chicago, Illinois 60693

Stockholder Records and Dividend Disbursing Office

Patricia E. Perkins
Supervisor, Shareholder Services
Illinois Power Company
500 South 27th Street
Decatur, Illinois 62525
(217) 424-6609

Investor Relations

Michael R. Heneghan
Director of Investor Relations
(217) 424-8715

Annual Stockholders' Meeting

The annual stockholders' meeting will be held April 21, 1988, at the executive office of the Company at 10 a.m. A proxy statement will be mailed to stockholders about March 14, 1988.

This report and the financial statements contained herein are submitted for the general information of the stockholders of the Company as such and are not intended to induce, or to be used in connection with, any sale or purchase of securities.

Illinois Power Company

1987 Annual Report

Table of Contents

1987 Financial Highlights 2
1987 Operations Highlights 2
Letter to Stockholders 3
Directors and Officers 16
Financial Report 17
Management's Discussion and Analysis of Financial Condition and Results of Operations 17
Financial Statements 21
Electric and Gas Statistics 36

1987 Financial Highlights

	1987	1986	% Increase (Decrease)
	(Millions of Dollars except per share amounts)		
Operating revenues	**$1,220**	$1,184	3.0
Electric	**$ 911**	$ 814	11.9
Gas	**$ 309**	$ 370	(16.5)
Operating expenses and taxes	**$ 986**	$ 976	1.0
Net income	**$ 290**	$ 293	(1.0)
Average number of common shares outstanding (millions)	**67**	65	3.1
Earnings per common share	**$ 3.75**	$ 3.98	(5.8)
Dividends declared per common share	**$ 2.64**	$ 2.64	—

1987 Operations Highlights

January 23
Gas sales and deliveries peaked for the year at 625,050,000 cubic feet

February 27
Clinton power station achieved its first, self-sustaining nuclear chain reaction

April 1
Company purchased downtown Decatur building primarily for new computer center

April 10
NRC authorized full-power license for Clinton

April 24
Clinton in-service date

July 15
ICC issued order on depreciation rate and funding for decommissioning of Clinton

July 20
Peak electric demand for the year reached 3,308,000 kilowatts

August 3
Peak day energy use for the year reached 65,855,000 kilowatt-hours

August 14
Hearings concluded on the first phase of Clinton audit

September 1
New district office in Columbia opened

October 7
Gatekeeper program to keep an eye on the elderly introduced in Company

November 1
Larry Brodsky and Wilfred Connell became vice presidents

November 19
Company filed a request for rate-moderation plan

November 24
ICC approved negotiated settlement on several Clinton-related ratemaking issues

November 30
NRC issued acceptable review of Clinton's performance

Wendell J. Kelley
Chairman and President

I am confident that our plan balances the interests of our customers, our stockholders, and the economic welfare of the territory we serve.

To Our Stockholders:

In reporting to you the significant accomplishments, developments, and events of 1987, I must begin with the most important—completing construction of our nuclear generating station at Clinton and bringing it up to full-power operation. For several months now, Clinton has been fully operational, supplying about one-quarter of the electricity needs of our customers.

Next in importance, I believe, was the proposal we filed in November to recover through electric rates the owning and operating costs of the Clinton power station. I am confident that our plan balances the interests of our customers, our stockholders, and the economic welfare of the territory we serve.

Before getting into more detail about Clinton and our rate proposal, I should report to you that 1987 earnings per share decreased 5.8 percent compared to those of 1986 due to a number of factors.

Earnings per common share fell to $3.75 from $3.98 in 1986. The cash portion of our earnings increased 16¢ while the non-cash portion (allowance for funds used during construction and deferred Clinton financing costs) declined 39¢. This increase in cash earnings reflects our electric rate increase, partially offset by our plan to reduce residential electric rates during the summer of 1988 and by the resolution of various ratemaking issues associated with Clinton. The reduction in non-cash earnings reflects the inclusion of additional construction work in progress in rate base.

Clinton achieved its first, self-sustained nuclear chain reaction on February 27, 1987 following fuel loading in late 1986. A unanimous vote by the five commissioners of

the Nuclear Regulatory Commission (NRC) on April 10 gave us a license to operate Clinton up to full-power.

On April 24, the station went into commercial operation. By mid-summer, Clinton was supplying about 15 percent of our customers' monthly need for electricity.

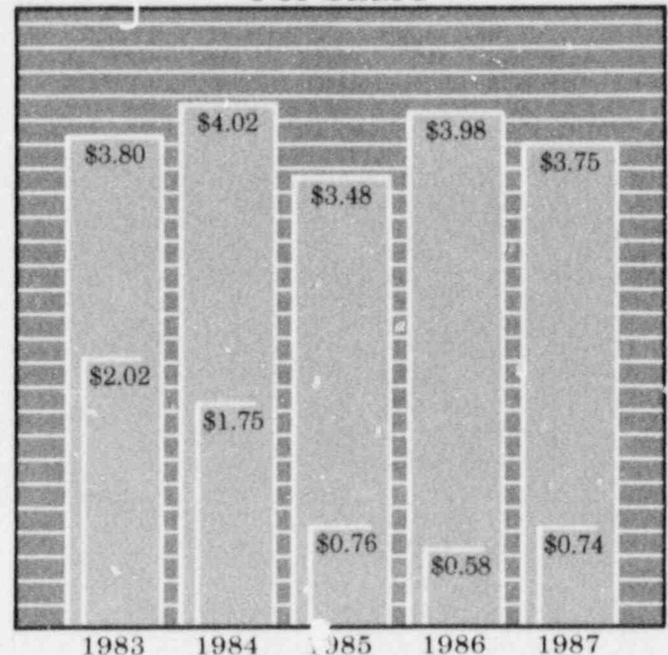
The Federal Emergency Management Agency in August approved Illinois' emergency response plan for the area surrounding the Clinton power station. The emergency response plan for the plant site was approved by the NRC in 1985.

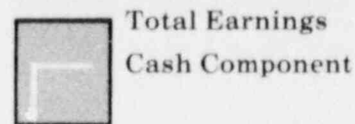
In the NRC's annual review of Clinton's performance, we received the highest achievable grade in licensing activities and in preoperational and startup testing. We received acceptable ratings in nine other areas. The NRC indicated that there were "many favorable trends" at the plant and that three areas had improved since our previous report card.

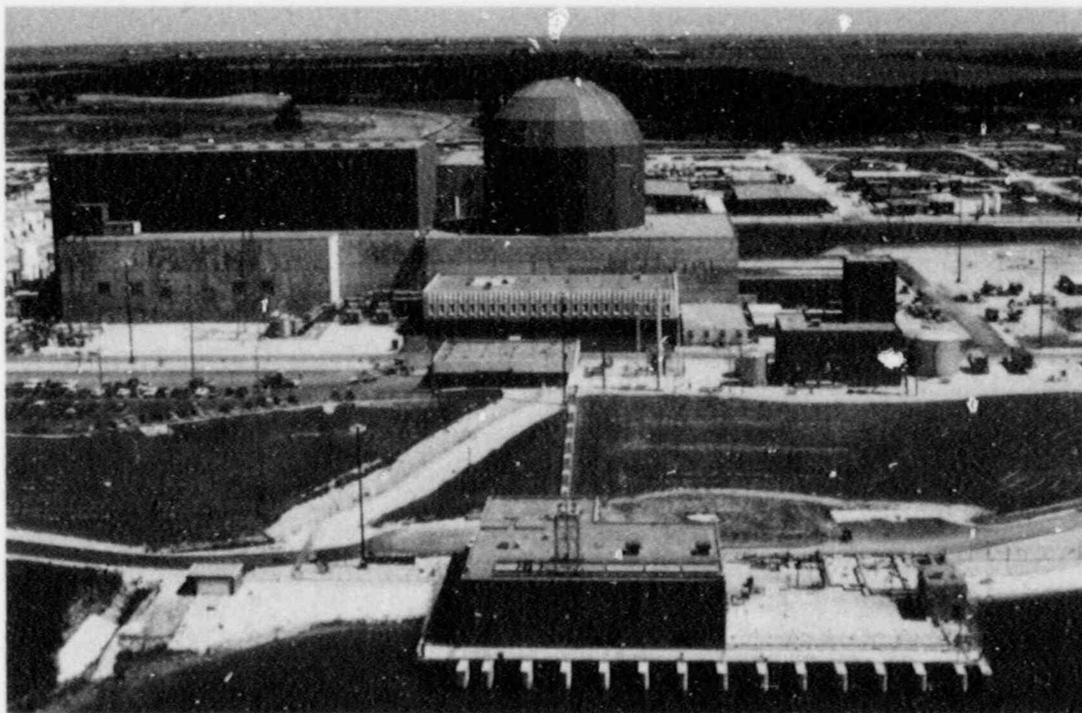
As we progressed with operation of Clinton, we also moved forward on a number of significant regulatory matters related to rates.

In July, the Illinois Commerce Commission (ICC) issued an order specifying the

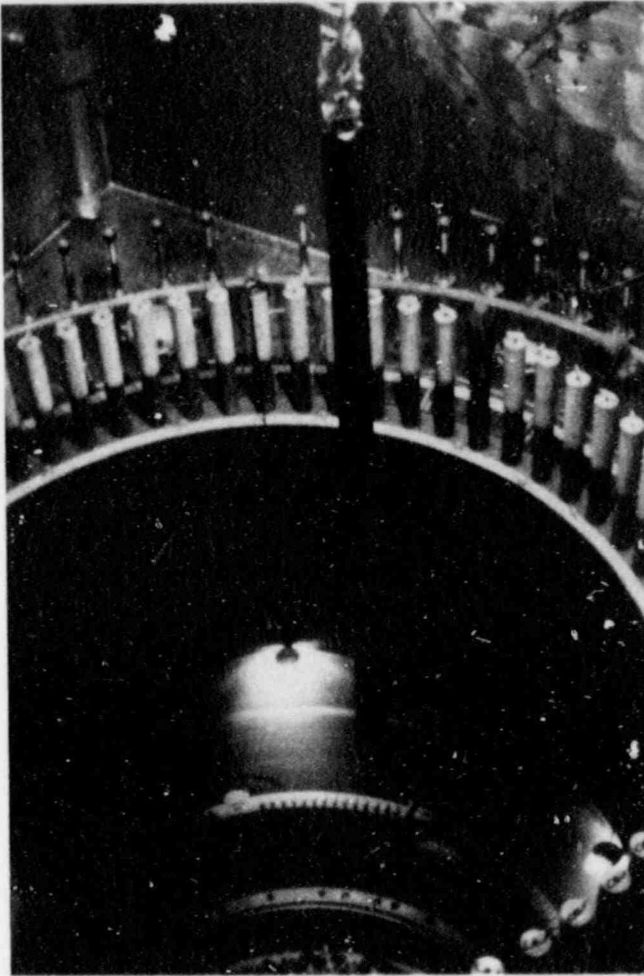
Cash Earnings vs. Total Earnings Per Share







The Clinton power station went into service April 24. The lakefront building is the screenhouse that takes in cooling water and filters it for use in the plant. The buildings to the left of the reactor dome house the turbine-generator and radwaste facilities. The 5,000-acre cooling lake and surrounding land provides recreation for more than 860,000 people during the year. In addition, about 8,000 people from 20 countries toured or used the Clinton visitors center.



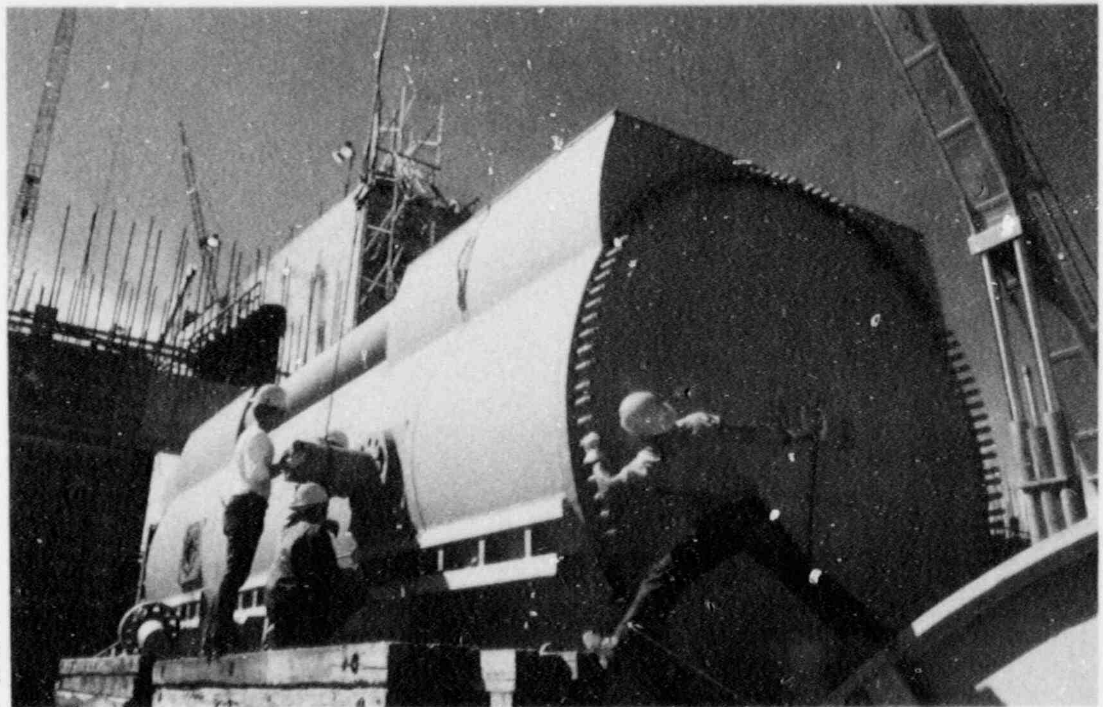
One of 624, 15-foot-long fuel bundles is lowered by crane into the reactor core at Clinton. Fuel loading began in September 1986 and was completed 22 days later.

depreciation rate for Clinton and how the decommissioning costs of the Clinton power station will be funded.

In November, the ICC approved a settlement that we had negotiated with several consumer groups and jointly proposed to the ICC. The agreement established April 24, 1987 as the in-service date of the Clinton power station and settled other related accounting issues. Our completed investment in Clinton was $3.8 billion.

The audit of the Clinton power station is nearing completion. In August, the ICC concluded hearings on the first phase of the audit to evaluate the reasonableness of the cost of the station, but the ICC did not issue an interim order. The audit firms selected by the ICC are expected to file the second phase of their report in early 1988. We expect the final order covering both phases from the ICC in late 1988.

With the successful transition from construction to operation of Clinton, it became appropriate to propose a plan for including Clinton in our electric rates. Currently $1.5 billion of Clinton's costs are included in rate base and earning a return. However, there remains the uncertainty of when and how



In 1978, workers prepared the generator to be lifted into place at Clinton.

Summer Rates

The two-part rate increase approved in 1985 officially became effective in October 1986 and April 1987. However, the approved, redesigned rates had the effect of compacting the entire 19 percent rate increase into the four summer months of 1987 and creating a dramatic difference between summer and winter rates.

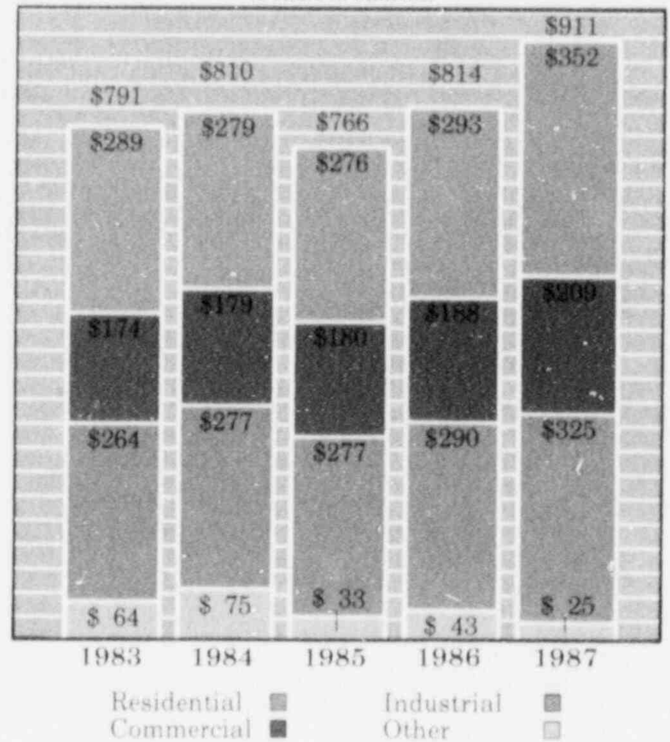
Understandably, some of our customers were angry with the electric bills they received during the summer. We had anticipated the high bill problems reflecting the electric rate increase and made extensive efforts to inform and assist customers. However, we could not have anticipated the extremely hot weather in early summer, and our efforts did not mollify some of our customers.

To help ease the burden that the dramatic difference between summer and winter rates placed on our residential customers, we asked the ICC to adjust electric rates retroactively and let us credit customers' 1987 summer bills. The ICC rejected this proposal, but approved a proposal in November that will reduce residential electric bills by $23 million in the summer of 1988. Our rate phase-in plan of November proposes a permanent solution to the dramatic difference between summer and winter rates.

Champaign-Urbana customer service representative Maxine Wrisk assisted a customer with his bill concern. During 1987, the Company's customer service representatives went the extra mile explaining the rate increase and energy conservation, and resolving bill concerns.

Electric Revenue by Customer Class

(Dollars in Millions)



much of our investment in Clinton will be recovered through electric rates. This brings me to the rate-moderation proposal I mentioned earlier.

On November 19, we asked the ICC to increase electric revenue by an average 11 percent in November 1988 and to increase rates annually by a smaller amount for six to nine years thereafter. A rate decrease would follow. Our requested increase reflects the remaining cost of constructing Clinton plus operating costs for the plant, the effect of the Tax Reform Act of 1986, and changes in other operating costs.

The annual increases after 1988 would be based on the rate of inflation for the previous year. A dollar-amount floor would assure minimum annual rate increases averaging about four percent, and a ceiling of 5.9 percent annually would shield customers from unusually high increases.

Our proposal includes a discount for senior citizens, a special rate for certain apartment dwellers, and three billing options for our residential customers. The ICC has 11 months to decide on our proposal.

We believe our proposal balances the interests of all the parties concerned. It fulfills our commitment to keep our rates competitive with those of other utilities and with the price of alternate energy sources. It minimizes the

Rate department employees, including (from left) Betty Stewart, Alan Rankin, Bob Hansen, Cheryl Miller, Todd Young, and Barb Patton, assembled the 280 copies of rate case testimony and exhibits introducing the Company's rate-moderation plan.

impact of a dramatic rate increase on our customers. And it recoups our investment in Clinton and earns for you, our shareholders, a fair return on your investment, although it somewhat delays recovery of costs compared to traditional ratemaking.

Total operating revenues were $1.22 billion, up three percent from 1986. Electric revenues increased 11.9 percent reflecting the two-part electric rate increase, partially offset by the provision to reduce electric rates during the summer of 1988. Gas revenues decreased 16.5 percent primarily because of mild winter weather and an increase in gas transported for customers.

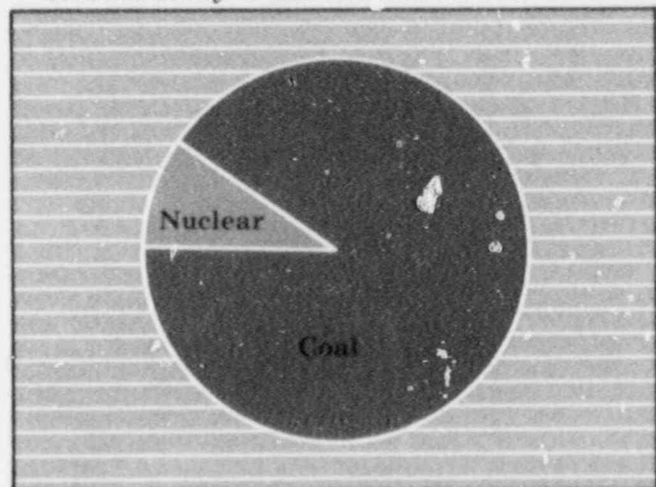
Our electricity demand in 1987 reached an hourly peak of 3,308,000 kilowatts on July 20. This includes the requirements of a power coordination agreement with two electric cooperatives. The peak was 2.6 percent lower than our all-time high peak demand set in 1986. Our 1987 peak day energy use of 65,855,000 kilowatt-hours occurred on August 3 and was 1.9 percent lower than our historic peak day energy use, also set in 1986.

Because of greater availability of our lower cost generating units and greater market demand, we sold more electricity to other utilities in 1987 than in 1986. Sales to two electric cooperatives under a power coordination agreement were $58 million. The result for the year was sales to other utilities in excess of purchases by $51 million, compared to 1986 sales in excess of purchases by $38 million.

We used 7.4 million tons of coal in our power plants in 1987, generating more than 16 billion kilowatt-hours, almost 91 percent of the total electricity we produced. We bought 85 percent of our coal from Illinois mines, reflecting our commitment to the economy of the coal industry in our state. We used nuclear fuel to generate 1.6 billion kilowatt-hours, almost nine percent of the total.

Over the next five years, we expect to generate approximately 76 percent of our electricity from coal and 23 percent from nuclear fuel.

Electricity Fuel Sources for 1987



Gas sales and deliveries in 1987 peaked at 625,050,000 cubic feet on January 23. This is 27 percent below our record peak day set in 1982.

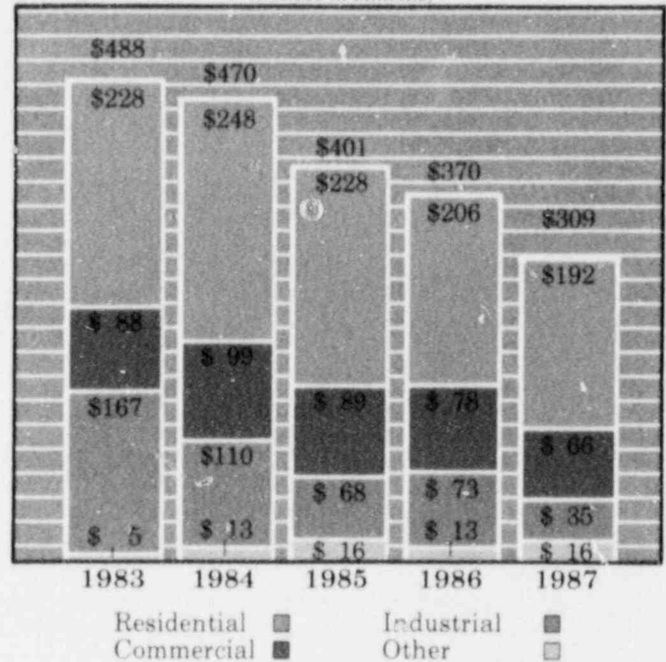
Our natural gas business has two segments—direct sales to customers and gas transported for customers. During 1987, direct sales decreased 21.1 percent, and gas transported rose 29 percent. When we transport gas, we earn about the same profit as we do when we sell gas directly. Gas consumption—gas sold directly and gas transported—decreased eight percent in 1987 compared to 1986. This reduction in gas consumption reflects mild winter weather and the impact of several industrial customers using alternate energy sources.

We drilled a new well at the Hillsboro gas storage field to increase the field's volume and to reduce gas costs. Running a new natural gas line under the Kaskaskia River to an existing subdivision of Carlyle enabled us to expand our natural gas sales into an area that was previously served by propane. We also constructed a new gas delivery station near Carlyle. This station will allow us to buy more natural gas from one of our lowest cost suppliers, Mississippi River Transmission Corporation.

Prices of natural gas to our customers have been declining since 1983, driven down

Gas Revenue by Customer Class

(Dollars in Millions)



Main and service labor foreman Ralph Ohl helped dig a trench across the Kaskaskia river bed and through adjacent woods so the Company could begin supplying natural gas to a subdivision near Carlyle.

primarily by competition among gas producers and, for a time, by lower oil prices. In the near future, gas prices may be pushed upward because of producers temporarily removing gas from spot market supplies in response to new transportation regulations.

Financing activities in 1987 were not as heavy as in 1986 because we completed constructing the Clinton power station and because we refinanced significant amounts of debt in 1986. We expect total construction expenditures to drop to $137 million in 1988, down from $264 million in 1987.

We issued $75 million of pollution control bonds in December. We refinanced $34 million of 10¾% pollution control bonds with 8.30% pollution control bonds. We also called for redemption the remaining $9.7 million of 14½% bonds and $6.8 million of 12% bonds. Our 1986 and 1987 refinancings together will reduce

Herb Downey and other senior citizens throughout our territory know they can count on Company employees such as Mt. Vernon meter changer Clarence Mays to keep their eyes open for senior citizens who may be having problems. Through the Gatekeeper program, trained Company employees refer customers who appear to need help to local social service agencies that assist the elderly.

Quality Customer Services

In 1987, we conducted many activities to maintain our high quality electric and gas service:

- In September, we completed a 9,000-square-foot building in Columbia. We established this new southern Illinois district to provide better service to this rapidly developing area.
- We began construction of a comparable building in August in Aledo to replace an older district office building.
- To add much needed work space for an expanded computer center and to demonstrate our commitment to revitalizing our communities, we purchased the vacant building of a former department store in downtown Decatur. We expect to move into the building in 1988.
- We implemented a new training program for apprentice linemen that boosts efficiency in work practices and cuts training hours and costs.
- More than 2,000 of our employees were trained to participate in the Gatekeeper and Fleetwatch programs. Respectively, these encourage employees to watch for elderly people who may be having problems and refer them to a local social service agency; and to recognize and report suspicious activities to police.
- We began performing certain electric line repairs from a helicopter to maintain hard-to-reach lines more efficiently. Repair costs were reduced by about 50 percent.

Nearly as important as sending electricity and gas to our customers is educating our customers. Approximately 40,000 schoolchildren in our service territory learned about electric energy and safety through our entertaining Starship Energy program. Another 7,800 children and adults learned about electric safety in everyday circumstances through our mechanical Safety City model. We conducted energy workshops for 130 schoolteachers. More than 1,100 students toured our fossil-fired power plants. We presented 940 programs on conservation, rates, safety, and nuclear energy to civic, church, and school groups. And we restructured our speakers' bureau, training about 150 speakers, to inform even more customers through programs in 1988.

interest and preferred stock dividend costs by approximately $15 million annually.

At year end, we had approximately $300 million of bank loans and $55 million of commercial paper outstanding with various maturities during the next six years. We also received $76 million from the automatic reinvestment and stock purchase plan during the year. At year end, we had available unused lines of bank credit of $260 million.

As we enter 1988, we see the prospect of change on the horizon particularly in regulation of our electric business. A significant amount of change already has occurred in gas regulation, especially at the federal level. We are less certain of what the changes in electric regulation will be. Some have advocated forms of deregulation, while others have suggested new forms of regulation. We believe we have developed a good strategy for facing regulatory changes, regardless of the shape they may take. Our strategy is focused on improving efficiency and service to customers while reorganizing our approach to marketing.

Efficiency in service to our customers is one of our strengths, and we plan to build on that strength. Among Illinois utilities in 1986, we had the lowest or second lowest expense per customer or megawatt-hour for meter reading, production, transmission, and distribution of electricity, and for total operating and maintenance for gas and electricity.

Keeping a tight lid on operating costs has always been a priority for us, and it is the essence of a new formal program. In February 1987, we launched a major campaign to improve the quality and productivity of service to our customers, based on suggestions solicited from employees. We expect to report some concrete results of the program next year.

At the end of the year, 6,548 customers were participating in the Illinois Residential Affordable Payment Plan. Participants must have incomes of 125 percent or less of the poverty level. They are allowed to pay only 12 percent of their income for utility service, regardless of the bill amount. During the first two years of the three-year program, we have incurred a $1.7 million shortfall between the amount billed and amount paid. The state has set aside temporary funds that we expect to be used to reimburse utilities for such shortfalls.

We favor weatherization of low-income housing to provide long-term energy assistance, and we have been a leader in this area for several years. The Energy Assistance

Jeff Morgan, left, and Craig Scroggins from the Bethalto Jaycees caulked windows at the home of a widow. This was funded with part of a $23,000 grant from the Energy Assistance Foundation. The Jaycees completed their three-year project in September 1987, weatherizing 34 homes.

In the Brake Parts Company plant of Echlin Inc. in Litchfield, manufacturing manager John Hartson, left, and Illinois Power Company industrial applications engineer Lowell Griffith discussed operations and products of the plant during a factory modernization audit. The Battelle Manufacturing Group performed the audit for three industrial customers at the request of Illinois Power Company.

Foundation, which the Company founded in 1982, issued 10 grants totaling $68,800 during the year to church and service groups. These groups, in turn, purchased materials and provided labor to weatherize homes in their communities. Our customers and other organizations donated $68,535, and we matched that amount during the year to help fund the Foundation.

In 1988, we plan to phase in a new customer assistance program that will provide a customer assistance advisor in each service area to work more actively as a liaison between customers having difficulty paying their utility bills and local social service agencies.

Our electric and gas marketing efforts to industrial and commercial customers are focused on providing better service and increasing sales to our customers. Our services for both electric and gas customers include customer seminars on energy supplies, price, conservation, audits of buildings' energy use, and technical information.

We also worked with a number of customers to objectively demonstrate that their proposed plans for considering generating their own electricity or switching from natural gas were uneconomic.

Electricity sales were significantly higher than expected and slightly higher than 1986 sales. On the other hand, total gas consumption fell below our expectations and was eight percent below 1986 sales.

Sales greater than those in 1987 look promising. One indication is that by the end of the year, 72 prospective industrial customers were considering locating in our territory, in part reflecting our efforts and customers' confidence in our territory. Our economic development efforts include contacting more international prospects, particularly in Canada, Japan, and Korea; soliciting potential aluminum casting industries; and continuing to take advantage

of such trends as automotive parts plants locating in our territory.

In the fall, a manufacturer of auto air conditioners and heaters moved into a vacant facility in Decatur. Another manufacturer of automobile accessories intends to locate in Nashville near an auto supply plant announced in 1986. The first Nashville plant and two other auto supply firms in Ottawa and Bloomington have nearly completed their facilities and expect to begin production in 1988.

The Diamond-Star Motors Corporation auto assembly plant in Bloomington-Normal is essentially complete and also will begin production in 1988. Full production with about 2,900 employees is expected in 1990. It will be one of our 10 largest industrial customers.

Separately during 1987, manufacturers of home appliances, typewriters, model toys, electronics equipment, military explosives, and cardboard containers also added or planned to add more than 1,200 employees in our service territory.

Altogether, 69 new and existing customers built or expanded facilities, creating 4,299 new jobs in 1987 in our territory. An additional 223 jobs in jeopardy were retained in our territory through state and local economic development incentive programs.

Commercial development also looks promising, especially in certain areas. The University of Illinois in Champaign-Urbana has planned about 40 high-technology or supercomputer projects. This includes a $50 million research center being constructed.

Retail and hotel businesses are booming in southwestern Illinois, and a commercial passenger and air cargo facility serving both military and civilian needs in the greater St. Louis area is being studied. Insurance, health care, and hotel businesses are expanding in the Bloomington-Normal area. These and

Bement Grain Company operations manager Steve Mechling, left, and Illinois Power Company agri-energy specialist Paul Mariman tour one of Bement Grain's elevators. Our marketing employees advised managers such as Mr. Mechling to take advantage of a new Company rate that shifted grain-drying to lower winter rates. In their year-end newsletter, Bement Grain thanked the Company for a $7,500 savings, due to the rate change, at their LaPlace and Milmine elevators during the harvest period.

other developments are due in part to our extensive work with many community and regional economic development groups.

For our agricultural customers, we introduced three options that will help them operate more competitively. Residential and commercial grain-drying customers received a shift in their billing period so that grain may be dried at the time the lower winter rates are in effect. Commercial customers' demand charges now stand alone each month, rather than being determined for the year by the highest monthly charge. Residential customers who installed a combination natural air and electric grain-drying system received rebates.

Environmental activities consumed a significant portion of our energies in 1987. A number of bills to amend the Clean Air Act are being considered in Congress but have not been passed. Those aspects affecting us the most are acid rain and toxic air pollution and national air quality standards.

We are concerned about the environmental effects of all our operations. But we want Congress to thoroughly assess the need, cost, and benefits of any additional regulations before they are imposed. We gave testimony to a congressional committee showing that one proposed tax on sulfur dioxide and nitrogen oxide emissions would cost the Company $8 billion to $11 billion over the next 40 years.

We also are concerned with keeping the Illinois coal industry a significant contributor to the economy of our territory. Along with the federal government and the state of Illinois, we are actively researching methods to develop more uses for Illinois coal. Planning began in 1987 on a clean-coal technology project at our Hennepin power station. We are one of three host utilities in this project intended to reduce sulfur dioxide and nitrogen oxide emissions that come from burning high-sulfur coal.

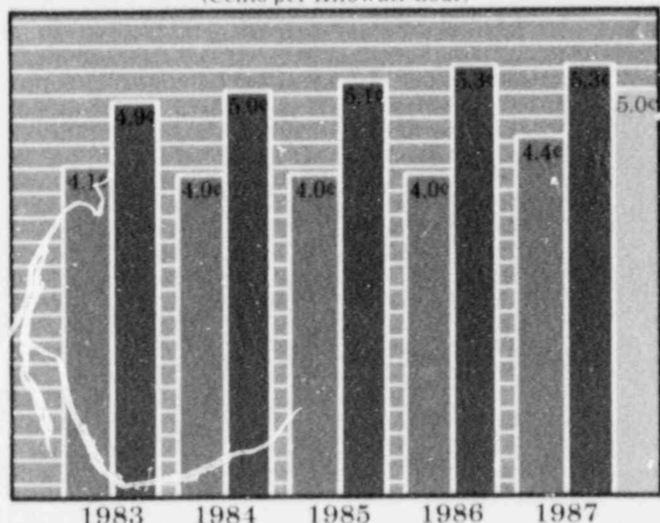
We are active supporters of and participants in several other research programs, including the Electric Power Research Institute and the Gas Research Institute. We also belong to several nuclear research groups that focus on enhancing the safety and reliability of nuclear power plant operations and maintenance.

In March 1987, the U.S. Environmental Protection Agency proposed to approve a rule change that we had pursued since 1979. The change will allow us to continue burning Illinois coal at the Baldwin power station, our largest fossil-fired generating station.

Along with 650 other organizations, we had used Martha C. Rose Chemical Company in Missouri to dispose of polychlorinated biphenyls (PCBs). In 1986, Rose abandoned its storage facilities due to lack of funds. Under federal statutes, we and other groups are responsible for cleaning up and restoring the storage site. In 1987, inventory was taken of all material at the site, and a preliminary groundwater study was conducted. We are actively involved with resolving the problem, which probably will take another two to three years.

Comparison of IP Industrial Average Electric Price to Midwest Industrial Average

(Cents per Kilowatt-hour)



IP Industrial ■ Midwest Industrial ■
IP First-Year Rate-Moderation Plan □

Committees of the Board of Directors

The current board of directors' committees, which present recommendations to the full board, and their members are as follows:

Finance Committee — This committee reviews the Company's financial forecast, financing plans, and pension fund investments; and makes recommendations to the board concerning such matters. Members of the committee are Gordon R. Worley, chairman, Richard R. Berry, William C. Gerstner, Larry D. Haab, Wendell J. Kelley, Donald E. Lasater, Keith R. Potter, Charles W. Wells, and Vernon K. Zimmerman.

Audit Committee — This committee, which consists entirely of non-management directors, recommends the appointment of the Company's independent accountants; confers with the independent accountants; and reviews the scope of audits, the results of auditors' examinations, and the activities of the Company's internal auditors. The members are Vernon K. Zimmerman, chairman, Richard R. Berry, Grover J. Hansen, Donald E. Lasater, and Eva Jane Milligan.

Compensation and Organization Committee — This committee reviews and recommends compensation of elected Company officers; reviews benefit plans; and recommends nominees to fill vacancies on the board of directors. The members are Boyd F. Schenk, chairman, Grover J. Hansen, Wendell J. Kelley, Eva Jane Milligan, and Robert M. Powers.

Corporate Activities Committee — This committee reviews corporate objectives and long-term Company plans; reviews the corporate structure appropriate to meet these objectives; and advises management and the board on such matters. The members are Keith R. Potter, chairman, Wendell J. Kelley, Robert M. Powers, Boyd F. Schenk, and Gordon R. Worley.

The first phase of a study of former gas manufacturing sites of our predecessor companies showed that residues from past activities remain at 24 sites and are not present at two other sites. Late in 1987 in Cairo, we began the first intensive, underground investigation of the sites. It will be completed in 1988. Initial findings confirmed the presence of residues. We have informed the Illinois Environmental Protection Agency about the 24 sites and about our approach to assess the potential risk to human health and welfare.

Organizational changes made this year will help strategically position us for the transitional period ahead.

First, the changes on the board of directors. On February 18, 1988, the board of directors increased the number of directors from 12 to 13 and elected Richard R. Berry to fill this vacancy. However, as of April 21, the number will be reduced, and Mr. Berry will replace Keith R. Potter, who will not stand for reelection.

Mr. Potter, of Easton, Maryland, is a consultant and retired vice chairman of International Harvester Company, a manufacturer of trucks and diesel engines. He has served on our board of directors since 1973. Although he has reached the board's mandatory retirement age of 70, Mr. Potter will continue to provide counsel as a director emeritus.

Mr. Berry is a director and executive vice president of Olin Corporation in Stamford, Connecticut. Olin Corporation is a diversified manufacturer concentrating on chemicals, metals, and aerospace/defense products.

Our management changes include the creation in May of a new investor relations section to improve communication between our Company and members of the financial community who are interested in our financial position and outlook. Michael R. Heneghan, director of investor relations, is responsible for this area.

Also in May, assistant vice president Carl

E. Mathias retired. He had served the Company nearly 45 years. Mr. Mathias' responsibilities included economic development in southwestern Illinois. He continues to be active in this area.

Vice president James O. McHood will retire later this year after 40 years of service to the Company. He has had responsibilities in many areas, including in service area operations, planning, power production, engineering, construction, the Clinton project, and energy supply.

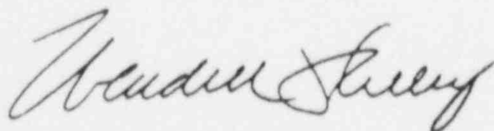
The board of directors elected Larry S. Brodsky and Wilfred Connell vice presidents of the Company, effective November 1. Mr. Brodsky is responsible for gas resources, electric dispatch, and electric interconnection agreements. He formerly was manager of energy supply. Mr. Connell is responsible for fossil power production. He formerly was manager of nuclear planning and support.

Along with electing the new vice presidents, we consolidated gas activities into the new gas resources department in November. This change will put us in a better position to maintain competitive gas prices.

The board of directors also elected Rodney A. Smith vice president effective February 1, 1988. Mr. Smith is responsible for public affairs. He formerly was manager of corporate communications at Virginia Power, a subsidiary of Dominion Resources, Inc. based in Richmond, Virginia.

These organizational changes and other activities are all part of our strategy to move forward through a period of potential political and regulatory change. From a year of progress in 1987, I am confident that we are well-positioned and well-prepared to create new opportunities for growth out of the challenges of change still to come. We are committed to earn a fair return on your investments while continuing to provide safe, reliable, and competitively priced services to all of our customers.

Sincerely yours,



Wendell J. Kelley
Chairman and President
February 18, 1988

Responsibility for Information

The financial statements and all information in this annual report are the responsibility of management. The financial statements have been prepared in conformity with generally accepted accounting principles consistently applied. In the opinion of management, the financial statements fairly reflect our financial position, results of operations, and sources of funds provided for gross property additions.

We maintain accounting and internal control systems that we believe are adequate to provide reasonable assurance that assets are safeguarded against loss from unauthorized use or disposition; and we believe that the financial records are reliable for preparing financial statements.

The financial statements have been audited by our independent accountants, Price Waterhouse, in accordance with generally accepted auditing standards. Such standards include the evaluation of internal controls to establish a basis for developing the scope of the examination of the financial statements. In addition to the use of independent accountants, we maintain a professional staff of internal auditors who conduct financial, procedural, and special audits. To assure their independence, both Price Waterhouse and the internal auditors have direct access to the audit committee of the board of directors.

Board of Directors

Richard R. Berry
Executive Vice President of Olin Corporation (diversified manufacturer concentrated in chemicals, metals, and areospace/defense products)
Stamford, Connecticut

William C. Gerstner
Executive Vice President of the Company
Decatur, Illinois

Larry D. Haab
Executive Vice President of the Company
Decatur, Illinois

Grover J. Hansen
Consultant and Retired President and Chief Operating Officer of First Federal Savings & Loan Association of Chicago
Ocean Springs, Mississippi

Wendell J. Kelley
Chairman and President of the Company
Decatur, Illinois

Donald E. Lasater
Chairman of the Board and Chief Executive Officer of Mercantile Bancorporation, Inc. (a bank holding company)
St. Louis, Missouri

Eva Jane Milligan
Retired Senior Vice President, General Personnel Manager of Marshall Field's (a retailer); President of Pro Lines, Inc. (a merchandise service organization)
Hilton Head Island, South Carolina

Keith R. Potter
Consultant and Retired Vice Chairman of International Harvester Company (a manufacturer of trucks and diesel engines)
Easton, Maryland

Robert M. Powers
President and Chief Operating Officer of A.E. Staley Manufacturing Company, a division of Staley Continental, Inc. (a processor of grain and oil seeds) and Executive Vice President of Staley Continental, Inc. (a diversified food company)
Rolling Meadows, Illinois

Boyd F. Schenk
Vice Chairman of IC Industries, Inc. (a diversified manufacturer and marketer of consumer and commercial products) and Chairman of Pet Incorporated (a processor and marketer of food products and other consumer goods)
Chicago, Illinois

Charles W. Wells
Executive Vice President of the Company
Decatur, Illinois

Gordon R. Worley
Retired Executive Vice President—Chief Financial Officer of Montgomery Ward & Co., Incorporated (a retailer)
Chicago, Illinois

Vernon K. Zimmerman
Director of the Center for International Education Research and Accounting, and Professor of Accountancy at the University of Illinois
Urbana, Illinois

Officers

Wendell J. Kelley
Chairman and President

William C. Gerstner
Executive Vice President

Larry D. Haab
Executive Vice President

Charles W. Wells
Executive Vice President

William E. Warren
Senior Vice President

Larry S. Brodsky
Vice President

Wilfred Connell
Vice President

Arthur E. Gray
Vice President and Secretary

Donald P. Hall
Vice President

Larry L. Idleman
Vice President

Paul L. Lang
Vice President

James O. McHood
Vice President

Rodney A. Smith
Vice President

Porter J. Womeldorff
Vice President

Larry F. Altenbaumer
Treasurer

Ann H. McEvoy
Assistant Secretary

Gary L. Secor
Assistant Treasurer

Note: The principal occupation of each director and officer of Illinois Power Company is that listed.

Financial Report

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

Reference is made to the Financial Statements and Electric and Gas Statistics for information concerning financial condition and results of operations. The factors having significant impact upon financial condition, changes in financial condition, and results of operations since January 1, 1985 are as follows:

Liquidity and Capital Resources

Gross Property Additions — Gross property additions for the years 1985 through 1987 were $1.9 billion, including approximately $454 million of allowance for funds used during construction (AFUDC).

Construction of the Clinton power station (Clinton) was completed in 1987. The Company owns 86.6% of Clinton and two cooperatives own the remainder. The Company's investment in the plant is $3.8 billion. The Nuclear Regulatory Commission issued a full-power operating license for Clinton on April 17, 1987. A November 1987 Illinois Commerce Commission (ICC) order established an in-service date of April 24, 1987.

We estimate that $644 million will be required for construction during the 1988-1992 period, including about $69 million for nuclear fuel. The retirement at maturity of currently outstanding long-term debt and redeemable preferred stock, and sinking fund payments on first mortgage bonds will require approximately $613 million during this five-year period.

Regulatory Matters — The audit commissioned by the ICC to evaluate the reasonableness of Clinton construction costs continues. On September 16, the ICC decided that an order would not be issued until completion of Phase II of the audit. The Company expects the audit report for Phase II to be submitted to the ICC by the end of the first quarter of 1988, and an order issued late in 1988. Should the ICC ultimately determine that a portion of Clinton construction costs not be allowed for ratemaking purposes, the disallowance would have to be recorded as a loss. Such a loss may be material in relation to earnings and financial position. Cash flow, however, would not be reduced immediately as a result of such a loss, but would be reduced over the life of the plant.

On April 22, 1987, a 9% electric rate increase became effective. An earlier 9% electric rate increase became effective in October 1986. Both increases were authorized by an August 1985 ICC rate order and increased the amount of construction work in progress (CWIP) in rate base by $384 million and $352 million, respectively. At December 31, 1987, the Company has $1.54 billion of Clinton costs in rate base. These rate increases represented additional annualized revenue of approximately $125 million.

On November 19, 1987, the Company filed an electric rate-moderation plan with the ICC. The plan would increase revenue approximately $92.7 million, net of anticipated fuel savings and a senior citizen discount, in the first year, followed by a series of up to nine annual increases indexed to inflation. Under the electric rate-moderation plan, there would be a cash flow delay of approximately $450 million over the first seven years of the plan due to its mirror CWIP provisions (representing amounts collected in rates prior to the in-service date of Clinton as a result of having CWIP in rate base). This amount would be capitalized as a part of Clinton costs for recovery over the life of the plant. In addition, under the deferred return provisions of the plan, cash flow of approximately $250 million would be delayed during the first five years for recovery during the remaining years of the plan. The plan is subject to approval or modification by the ICC. The Company expects an order in October 1988.

A November 1987 ICC order approved the provisions of a negotiated settlement reached by the Company and several intervenors. The order established April 24, 1987 as the in-service date. It also provided for the deferral of depreciation, taxes other than income taxes, and financing costs until a rate order, expected in October 1988, reflecting the inclusion of Clinton in rate base becomes effective. Such deferred costs and the related return will be recovered, to the extent that total Clinton costs are allowed in rate base, over the remaining life of Clinton. Under this agreement, Clinton operation and maintenance costs will be expensed currently. However, the electric revenues previously deferred as ordered by the ICC to reflect the lower federal income tax rates under the Tax Reform Act of 1986 were included in income and future deferrals discontinued. Earnings were decreased $19 million (28¢ per share) in 1987 due to this settlement, and future earnings will be decreased by an estimated $2 million to $3 million per month until the next electric rate order is effective. Earnings were also reduced by $11 million (16¢ per share) in 1987 to reflect the effect of excluding from the Clinton cost deferrals the portion not under jurisdiction of the ICC, because the November 1987 electric rate-moderation plan excluded that portion of the Company's operations. Amendments to generally accepted accounting principles effective in 1988, will not permit an allowance for return on shareholders' investment in post-construction cost deferrals to be capitalized for financial statement purposes. Such allowance for earnings on shareholders' investment is estimated to be approximately $11 million per month during 1988.

The cash flow associated with the deferrals under the electric rate-moderation plan and the deferrals

under the negotiated settlement will be delayed until the deferred costs are recovered in rates.

Financings — Funds provided from operations amounting to $171 million for the years 1985 through 1987 supplied working capital to meet operating requirements and a portion of the construction program. In addition, funds obtained from external sources during this three-year period totaled $1.3 billion. Funds totaling $615 million were used for debt retirements during this three-year period.

During the three-year period, temporary cash requirements were provided by short-term borrowings. At December 31, 1987, the unused portion of our total bank line of credit was $260 million.

In February 1987, the Company redeemed its $36 million, 11.66% serial preferred stock. The Company also refunded $34 million of long-term debt in July 1987 to reduce the interest rate from 10.75% to 8.3%.

The Company has had a strong capital structure, adequate short and intermediate term bank borrowing capability and flexible access to the permanent capital markets. Our future financial strength depends on a number of factors including the ultimate outcome of the pending rate request, construction audit proceedings and litigation. At December 31, 1987, based upon the most restrictive earnings test contained in our Mortgage and Deed of Trust, approximately $378 million of additional first mortgage bonds could be issued at an assumed interest rate of 9⅞%.

Tax and Accounting Developments — Many aspects of the Tax Reform Act of 1986 (Act) have affected our Company in 1987. These include the corporate income tax rate reduction, repeal of the investment tax credit, a new depreciation system for tax purposes, and a corporate alternative minimum tax. Although the statutory federal corporate income tax rate decreased from 46% to 40% for 1987, and the Company's total book tax provision correspondingly decreased, the Company's current federal income tax liability is about $33 million greater than it would have been under prior law. This results primarily from the Alternative Minimum Tax (AMT) provisions of the Act. The $33 million paid in AMT will be used as credits to offset regular income tax liabilities in future years. Although the statutory federal income tax rate decreases to 34% in 1988, the Company expects to again be affected by the AMT provisions of the Act. In accordance with Internal Revenue Service requirements, depreciation-related deferred tax balances will continue to be normalized at the weighted average tax rates at which they were provided.

Pursuant to an ICC order, the Company has recorded the benefit of the lower federal income tax rates collected from our gas utility customers as a liability subject to refund ($1.0 million at December 31, 1987). Ultimate disposition of this liability will not be determined until the ICC completes a review of the overall impact of the new tax act and the financial condition of gas operations. The Company made a filing with the ICC on February 5, 1988 requesting that this amount be included in income.

The Financial Accounting Standards Board has issued Statement of Financial Accounting Standards No. 96, "Accounting for Income Taxes" (FAS 96), dated December 1987. This new standard adopts a "liability method" of tax allocation relating to transactions that affect book and tax income in different reporting periods. The Company has not completed its evaluation of the impact that adopting this standard will have on its earnings and financial position. The impact depends in part on actions taken by the regulators. Although adopting this standard may result in a significant increase in assets and liabilities, the Company does not expect a material effect on earnings. The Statement must be adopted no later than 1989. However, depending upon the ICC's actions in the pending electric rate-moderation plan, the Company may adopt FAS 96 in 1988.

The Company faces many issues related to Clinton as well as changes in generally accepted accounting principles. See Note 13 in "Notes to Financial Statements" for information regarding these matters, which could materially affect financial liquidity, results of operations, and financial position.

Results of Operations

Electric Operations — For the three-year period 1985 through 1987, electric revenues increased 12.4%, the components of which are summarized as follows:

	1987	1986	1985
	(Millions of Dollars)		
Rate increases	$102	$ —	$ —
Volume & other	6	47	(41)
Loss on sale of nuclear fuel commitments	—	—	(8)
Fuel cost recoveries	(11)	1	5
Revenue increase (decrease)	$ 97	$ 48	$ (44)

During the above periods, kilowatt-hour sales have been affected by weather, economic conditions within our service territory, and by ongoing conservation efforts. In 1985, kilowatt-hour sales declined 6.7%, primarily due to a power coordination agreement with two cooperatives under which sales to the cooperatives were classified as power interchanged-net ($47.5 million in 1985) rather than as electric revenues ($34.6 million in 1984). See Note 3 in "Notes to Financial Statements". In 1986, we experienced a 5.6% increase in kilowatt-hour sales, primarily due to warmer summer weather. Due to the seasonal rate design, the revenue effect of the October 1986 rate increase was minimal in 1986. In 1987, we experienced an 11.9% increase in revenue primarily due to the increase in rates in October 1986 and April 1987, partially offset by a provision for rate reduction of approximately $23 million. This amount reduced electric revenues during 1987 and will be credited to residential electric customers'

1988 summer bills. This rate reduction, as approved by the ICC, provides a temporary solution to the residential electric summer/winter rate differential issue. A permanent solution has been proposed in the Company's electric rate-moderation plan.

The cost of meeting our system requirements is reflected in the cost of fuel for electric plants and power purchased and interchanged-net. Changes in these costs are summarized as follows:

	1987	1986	1985
	(Millions of Dollars)		
Fuel for electric plants	$ (2.2)	$ (8.9)	$ 20.1
Power purchased and interchanged-net	(13.4)	11.4	(65.2)
Total increase (decrease)	$ (15.6)	$ 2.5	$ (45.1)

Changes in the above costs are caused by system load requirements, availability of generating units to meet those requirements (including Clinton generation in 1987), fuel prices, purchased power prices and volumes, power interchange market conditions, a power coordination agreement with two cooperatives, and recovery of fuel costs through the fuel adjustment clause.

Kilowatt-hour generation increased 6.4%, 1.4%, and 5.1% in 1985, 1986, and 1987, respectively. During 1985 and 1986, coal-fired generation averaged more than 99% of our total generation. During 1987, coal-fired generation averaged 91% and nuclear generation 9% of our total generation. The weighted average cost per million BTU's of coal burned increased 3.2% in 1985, decreased 8.6% in 1986, and decreased 1.5% in 1987.

During 1985, fuel for electric plants increased $20.1 million. Power purchased and interchanged-net switched from a net purchase of $16.2 million in 1984 to a net sales credit of $49.0 million. These changes reflect reduced sales to our customers, increased interchange sales to other utilities, greater availability of lower cost generating units, and the power coordination agreement discussed above.

During 1986, fuel for electric plants decreased $8.9 million. The credit for power purchased and interchanged-net decreased $11.4 million. Lower fuel prices in 1986 resulted from coal contract renegotiations and a favorable spot market for coal purchases. Reduced availability of our lower cost generating units in 1986 contributed to decreased interchange sales. Increased customer requirements and increased sales under the power coordination agreement, coupled with greater availability of low-cost generation from other utilities in the interchange market, caused increased interchange purchases.

During 1987, fuel for electric plants decreased $2.2 million. The credit for power purchased and interchanged-net increased $13.4 million. Lower fuel prices in 1987 resulted from coal contract renegotiations and a favorable spot market for coal purchases. The increase in interchange sales is primarily due to greater availability of our lower cost generating units and market demand for electricity.

Gas Operations — Effective October 31, 1985, the Federal Energy Regulatory Commission (FERC) issued an order that established new rules for transportation of natural gas by interstate pipelines. One effect of the order was that pipeline companies cancelled agreements with certain of our customers to transport gas owned by such customers. As a result of this order and because of decreased gas costs for customers on our system, certain customers resumed purchasing gas directly from us, as reflected in 1986 gas sales statistics. In 1987, more liberalized interim transportation rules used by the major pipelines caused transported therms to increase again.

Gas revenues decreased 34.4% during the three-year period 1985 through 1987, the components of which are summarized as follows:

	1987	1986	1985
	(Millions of Dollars)		
Rate increase (decrease)	$ —	$ —	$ (14)
Volume & other	(60)	20	(67)
Transported gas fees	4	(3)	3
Gas cost recoveries	(5)	(48)	9
Revenue increase (decrease)	$ (61)	$ (31)	$ (69)

In 1984, the ICC approved our request to reduce gas rates and thus promote both the retention of existing customers and further industrial expansion within our service territory. This rate reduction left residential rates essentially unchanged but resulted in lower rates to industrial customers and decreased annual gas revenues of approximately $14 million in 1985.

Therm sales, which exclude therms transported, decreased 17.9% in 1985, increased 7.3% in 1986, and decreased 21.1% in 1987. The major factors affecting therm sales for the three-year period were changes in economic and weather conditions, customer conservation, and gas transportation arrangements as discussed above. In 1985, the combined therms sold and transported decreased 3.6% reflecting the milder weather experienced during the heating season. In 1986, the combination of therms sold and transported represented an increase in gas consumption of 0.5%. In 1987, the combination of therms sold and transported represented a decrease in gas consumption of 8.0%, reflecting mild winter weather and the impact of several industrial customers using alternate energy sources. Therms of gas transported for customers were 297 million in 1985, 253 million in 1986, and 327 million in 1987.

The cost of gas purchased for resale, which reflects volumes of gas delivered to customers, decreased $49.1 million, $25.0 million, and $50.2 million in 1985, 1986, and 1987, respectively. The average cost per therm delivered to customers decreased 2.0% in 1985, 12.6% in 1986, and 3.1% in 1987, reflecting declining prices and advantageous use of spot market purchases of gas.

Other Expenses and Taxes — A comparison of increases in other expenses and the credit for deferred Clinton costs for the last three years is presented in the following table:

	1987	1986	1985
	(Millions of Dollars)		
Other operating expenses	$58	$18	$15
Maintenance	22	8	3
Depreciation	76	2	1
General taxes	11	1	1
Deferred Clinton costs	(78)	—	—

The changes in other operating expenses reflect the impact of inflation, increased employee wages and benefits, greater use in 1985 of professional services relating to nuclear issues, and increased insurance costs in 1986. The increase in 1986 maintenance expenses primarily reflects power plant maintenance requirements. The main reason for the 1987 increase in other operating expenses, maintenance, depreciation, and general taxes is the beginning of Clinton operations on April 24, 1987. In addition, the Company recorded a $78.3 million reduction to expenses in 1987 to reflect the portion of Clinton depreciation and real estate taxes deferred for future recovery in accordance with the negotiated settlement.

During 1987, pension expense decreased approximately $3.9 million resulting from the adoption of Statement of Financial Accounting Standards No. 87, "Employer's Accounting for Pensions".

For a detailed analysis of income tax components, see Note 4 in "Notes to Financial Statements".

Other Income — Total AFUDC increased $43 million in 1985 and $57.3 million in 1986, and decreased $146.1 million in 1987. Changes in AFUDC relate to the amounts of CWIP not included in rate base. The amount of Clinton plant cost included in rate base, as approved by the ICC, was $733 million January through July 1985, $804 million August 1985 through September 1986, $1.156 billion October through April 1987, and $1.54 billion May through December 1987. The AFUDC effective after tax rate was 9.25% in 1985 and 1986. In 1987, the AFUDC effective rate was 9.25% after-tax for Clinton and 11% before-tax for all other construction. AFUDC on Clinton was discontinued effective with the April 24, 1987 in-service date.

In accordance with the negotiated settlement, $129.2 million was recorded as Clinton deferred financing costs for the period April 24, 1987 through December 31, 1987. Such financing costs are calculated on Clinton deferred costs and plant costs not in rate base subject to ICC jurisdiction. Clinton deferred financing costs were calculated using a 9.25% after-tax rate through October 1987 and 8.5% thereafter.

Interest Charges — Interest charges increased $28.8 million, $24.0 million, and $4.5 million in 1985, 1986, and 1987, respectively. These increases primarily reflect the $1.253 billion of long-term debt issued during the three-year period at a weighted average interest rate of 8.5%. During this period, we retired $608 million of long-term debt with a weighted average interest rate of 10.1%.

Earnings per Common Share — The changes in net income applicable to common stock in 1985 through 1987 resulted from the interaction of all the factors discussed herein, including the issuance and retirement of preferred stock. Changes in earnings per common share also reflect the increased number of common shares outstanding in each year. See Notes 8 and 9 in "Notes to Financial Statements"; and Statements of Preferred and Preference Stock.

Inflation — Inflation, as measured by the Consumer Price Index, was 3.6%, 1.9%, and 3.7% in 1985, 1986, and 1987, respectively. The primary effect of inflation on the Company is that historical plant costs are recovered in the Company's rates rather than current costs.

Report of Independent Accountants

Price Waterhouse St. Louis, Missouri

To the Board of Directors of Illinois Power Company

We have examined the financial statements of Illinois Power Company appearing on pages 21 through 34 of this report. 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.

As discussed in Note 13, the Financial Accounting Standards Board issued a statement which provides, among other things, that the costs of a plant disallowed by a regulator be recognized as a loss. This statement will be adopted, as permitted, in 1988.

As described more fully in Note 14, there are uncertainties with respect to various matters related to the Clinton power station. Management is unable to determine the effects, if any, that the resolution of these uncertainties may have on the Company's 1987 financial statements.

In our opinion, subject to the effects on the 1987 financial statements of such adjustments, if any, as might have been required had the outcome of the uncertainties referred to in the preceding paragraph been known, the financial statements examined by us present fairly the financial position of Illinois Power Company at December 31, 1987 and 1986, and the results of its operations and the sources of funds provided for gross property additions for each of the three years in the period ended December 31, 1987, in conformity with generally accepted accounting principles consistently applied.

February 11, 1988

Price Waterhouse

Statements of Income

	For the Years Ended December 31,		
	1987	1986	1985
	(Thousands of Dollars)		
Operating Revenues*			
Electric	$ 910,844	$ 814,144	$ 766,467
Gas	308,679	369,721	400,897
Total	1,219,523	1,183,865	1,167,364
Operating Expenses and Taxes			
Fuel for electric plants	262,592	264,807	273,687
Power purchased and interchanged—net	(50,975)	(37,553)	(48,975)
Gas purchased for resale	188,994	239,214	264,221
Other operating expenses	190,990	133,275	115,410
Maintenance	80,332	58,590	50,706
Depreciation	147,408	71,732	70,097
Amortization of abandoned plant costs	6,379	6,380	2,556
General taxes	115,989	105,310	104,060
Deferred Clinton costs	(78,264)	—	—
Income taxes	122,756	134,652	131,322
Total	986,201	976,407	963,084
Operating income	233,322	207,458	204,280
Other Income			
Allowance for equity funds—			
Construction	51,523	158,238	117,622
Deferred Clinton financing costs	91,726	—	—
Miscellaneous—net	57,083	64,679	48,367
Total	200,332	222,917	165,989
Income before interest charges	433,654	430,375	370,269
Interest Charges			
Interest on long-term debt	188,762	186,781	168,073
Other interest charges	14,309	11,786	6,540
Allowance for borrowed funds—			
Construction	(21,532)	(60,913)	(44,343)
Deferred Clinton financing costs	(37,441)	—	—
Total	144,098	137,654	130,270
Net income	289,556	292,721	239,999
Preferred dividend requirements	37,697	36,242	32,759
Net income applicable to common stock	$ 251,859	$ 256,479	$ 207,240
Weighted average number of common shares outstanding during the period	67,250,913	64,502,690	59,618,728
Earnings per common share	$3.75	$3.98	$3.48
Cash dividends declared per common share	$2.64	$2.64	$2.64

**Includes revenue-related taxes added to customer billings in each of the years 1987, 1986, and 1985 in the amount of $59,201,000, $58,997,000, and $61,885,000, respectively.*

Retained Earnings

	For the Years Ended December 31,		
	1987	1986	1985
	(Thousands of Dollars)		
Balance at Beginning of Year	$ 481,192	$ 398,755	$ 350,552
Net Income	289,556	292,721	239,999
	770,748	691,476	590,551
Less—			
Cash dividends—			
Preferred stock	37,440	36,845	33,070
Common stock	178,493	171,111	158,726
Reacquisition costs of preferred stock	—	2,328	—
	215 933	210,284	191,796
Balance at End of Year	$ 554,815	$ 481,192	$ 398,755

See notes to financial statements which are an integral part of these statements.

Balance Sheets

December 31,	1987	1986*
	(Thousands of Dollars)	
ASSETS		
Utility Plant, at original cost		
Electric (includes construction work in progress of $45,753,000 and $3,679,959,000, respectively)	$ 5,700,684	$ 5,494,656
Gas (includes construction work in progress of $5,591,000 and $4,701,000, respectively)	423,892	409,182
	6,124,576	5,903,838
Less-Accumulated depreciation	1,078,809	944,853
	5,045,767	4,958,985
Nuclear fuel under capital lease	200,034	191,276
Acquisition adjustment (less amortization of $3,399,000 and $3,154,000, respectively)	533	778
	5,246,334	5,151,039
Investments and Other Assets	9,697	14,934
Current Assets		
Cash and temporary cash investments	73,114	129,862
Accounts receivable (less allowance for doubtful accounts of $6,500,000 and $6,000,000, respectively)		
Service	75,480	77,077
Other	41,161	6,356
Materials and supplies, at average cost		
Fossil fuel	39,012	32,276
Gas in underground storage	17,972	21,253
Operating materials	60,743	49,357
Prepaid and refundable income taxes	72,075	60,471
Prepayments and other	7,654	10,572
	387,211	387,224
Deferred Charges		
Deferred Clinton costs	207,431	—
Unamortized deferred abandonment cost	16,581	22,960
Unamortized debt expense	52,233	43,354
Other	3,247	3,531
	279,492	69,845
	$ 5,922,734	$ 5,623,042

	1987	1986*
CAPITAL AND LIABILITIES		
Capitalization		
Common stock—		
No par value, 80,000,000 shares authorized; 68,588,901 and 65,608,876 shares outstanding, respectively, stated at	$ 1,298,207	$ 1,221,838
Retained earnings	554,815	481,192
Less—Capital stock expense	11,634	11,152
Total common stock equity	1,841,388	1,691,878
Preferred and preference stock	315,171	315,171
Redeemable preferred stock	160,000	196,000
Long-term debt	2,279,219	2,246,367
Total capitalization	4,595,778	4,449,416
Current Liabilities		
Accounts payable	109,778	122,829
Notes payable	103,170	128,863
Long-term debt and lease obligations maturing within one year	81,174	43,728
Dividends payable	54,963	52,988
General taxes accrued	34,878	35,676
Interest accrued	69,138	64,270
Provision for rate reduction	23,129	—
Other	59,955	22,514
	536,185	470,868
Other		
Accumulated deferred income taxes	443,494	356,764
Accumulated deferred investment tax credits	347,277	345,994
	790,771	702,758
Commitments and Contingencies (Notes 12 and 13)		
	$ 5,922,734	$ 5,623,042

**Restated for the effect of capitalized nuclear fuel lease (Note 1).*

See notes to financial statements which are an integral part of these statements.

Statements of Long-Term Debt

December 31,	1987	1986*
	(Thousands of Dollars)	
First mortgage bonds—		
4 % series due 1988	$ 25,000	$ 25,000
14½% series due 1990	—	9,653
4¼% series due 1993	35,000	35,000
5.85% series due 1996	40,000	40,000
6⅜% series due 1998	25,000	25,000
6¾% series due 1998	45,000	45,000
8.35% series due 1999	35,000	35,000
9 % series due 2000	35,000	35,000
7.60% series due 2001	35,000	35,000
7⅝% series due 2003	60,000	60,000
6.60% series due 2004 (Pollution Control Series A)	8,050	8,050
9⅜% series due 2004	85,000	90,000
10½% series due 2004	50,000	50,000
8⅜% series due 2006	100,000	100,000
6 % series due 2007 (Pollution Control Series B)	18,700	18,700
8¼% series due 2007	100,000	100,000
8¾% series due 2008	100,000	100,000
12 % series due 2012	—	6,827
10¾% series due 2013 (Pollution Control Series C)	125,000	125,000
11⅜% series due 2014 (Pollution Control Series D)	75,000	75,000
10¾% series due 2015 (Pollution Control Series E)	116,245	150,000
10⅜% series due 2016	125,000	125,000
9¾% series due 2016	75,000	75,000
9⅜% series due 2016	125,000	125,000
7⅜% series due 2016 (Pollution Control Series F, G, and H) *(1)*	150,000	—
8.30% series due 2017 (Pollution Control Series I)	33,755	—
Total first mortgage bonds	1,621,750	1,493,230
12¼% debentures due 1992 *(2)*	100,000	100,000
Long-term bank notes due 1987	—	17,000
Long-term bank notes due 1992	—	34,000
Revolving loan agreements *(3)*	200,000	200,000
10.75% loan agreement due 1992	8,930	8,930
Long-term loan agreement due 1992 *(4)*	60,000	—
8½% debt securities due 1994	100,000	100,000
Variable rate long-term debt due 2016 *(1)*	—	150,000
Variable rate long-term debt due 2017 *(5)*	75,000	—
Total long-term debt	2,165,680	2,103,160
Unamortized premium and discount on debt	(9,584)	(10,097)
Long-term debt maturing within one year	(33,333)	(17,006)
	2,122,763	2,076,063
Obligation under capital leases-noncurrent	156,456	170,304
	$ 2,279,219	$ 2,246,367

(1) Interest rate was adjustable daily. This debt was issued on December 31, 1986 and had an interest rate of 4.5%. This debt was replaced on February 10, 1987 with 7⅜% First Mortgage Bonds (Pollution Control Series F, G, and H) due 2016 totaling $150,000,000.

(2) The debentures, issued by IPF, are guaranteed as to payment of principal and interest by the Company.

(3) Repayment of the first $100,000,000 loan is required to begin January 31, 1991 with 10 subsequent quarterly payments. Repayment of the second $100,000,000 loan is required to begin December 10, 1988 with 11 subsequent quarterly payments. However, the first loan is subject to extension options and may also be repaid in advance at the Company's option. The interest rate is currently based on Reference Bank Certificate of Deposit Rate plus 0.5%, and at December 31, 1987 was 8.04% and 8.64%, respectively.

(4) Interest rate is adjusted semiannually and ranged from 7.687% to 8.5% at December 31, 1987.

(5) Interest rate is adjusted weekly and was 6.75% at December 31, 1987.

**Restated for the effect of capitalized nuclear fuel lease (Note 1).*

See notes to financial statements which are an integral part of these statements.

Statements of Preferred and Preference Stock

Serial Preferred Stock, cumulative, $50 par value *(1)*—Authorized 5,000,000 shares; 4,280,000 shares and 5,000,000 shares outstanding, respectively (including 720,000 shares of redeemable preferred stock at December 31, 1986)

Series	Shares	Redemption prices	December 31, 1987	December 31, 1986
			(Thousands of Dollars)	
4.08%	300,000	$51.50	**$ 15,000**	$ 15,000
4.26%	150,000	51.50	**7,500**	7,500
4.70%	200,000	51.50	**10,000**	10,000
4.42%	150,000	51.50	**7,500**	7,500
4.20%	180,000	52.00	**9,000**	9,000
8.24%	600,000	51.90	**30,000**	30,000
7.56%	700,000	51.685	**35,000**	35,000
8.94%	1,000,000	52.90 prior to March 1, 1991 51.60 thereafter	**50,000**	50,000
8.00%	1,000,000	53.29 prior to August 1, 1992 52.29 thereafter	**50,000**	50,000
Premium on preferred stock			**1,171**	1,171
Total Preferred Stock, $50 par value			**215,171**	215,171

Serial Preferred Stock, cumulative, without par value—Authorized 5,000,000 shares; 4,600,000 shares outstanding (including 2,600,000 shares of redeemable preferred stock)

Series	Shares	Redemption prices	1987	1986
A*(2)*	1,000,000	$51.50 after February 1, 1988 and prior to February 1, 1993 50.00 thereafter	**50,000**	50,000
B*(3)*	1,000,000	51.50 after May 1, 1990 and prior to May 1, 1995 50.00 thereafter	**50,000**	50,000
Total Preferred Stock, without par value			**100,000**	100,000
Preference Stock, cumulative, without par value—Authorized 5,000,000 shares; none outstanding			**—**	—
Total Preferred and Preference Stock			**$ 315,171**	$ 315,171

Redeemable Serial Preferred Stock, cumulative—

Series	Shares	Par Value	1987	1986
11.75%*(4)*	1,000,000	none	**$ 50,000**	$ 50,000
8.52%*(5)*	1,000,000	none	**50,000**	50,000
8.00%*(6)*	600,000	none	**60,000**	60,000
11.66%*(7)*	720,000	$50.00	**—**	36,000
Total Redeemable Preferred Stock			**$ 160,000**	$ 196,000

(1) Redeemable at the option of the Company in whole or in part at any time upon not less than thirty days and not more than sixty days notice by publication.

(2) Adjustable Rate Series A issued on March 3, 1983. Quarterly dividend rates are determined based on market interest rates of certain U.S. Treasury securities. See "Two-Year Dividends and Stock Prices by Quarters" on page 35 for the 1987 quarterly dividend rates. The dividend rate for any dividend period will not be less than 6% per annum nor greater than 12% per annum applied to the liquidation preference value of $50 per share.

(3) Adjustable Rate Series B issued on May 15, 1985. Quarterly dividend rates are determined based on market interest rates of certain U.S. Treasury securities. See "Two-Year Dividends and Stock Prices by Quarters" on page 35 for the 1987 quarterly dividend rates. The dividend rate for any dividend period will not be less than 7% per annum nor greater than 14½% per annum applied to the liquidation preference value of $50 per share.

(4) Subject to mandatory redemption in an amount sufficient to retire on each November 1, beginning in 1990, 200,000 shares at $50 per share plus accrued dividends. Beginning November 1, 1990, the Company may redeem up to 200,000 additional shares each year at $50 per share.

(5) Subject to mandatory redemption in an amount sufficient to retire on each February 1, beginning in 1992, 200,000 shares at $50 per share plus accrued dividends. Beginning February 1, 1992, the Company may redeem up to 200,000 additional shares each year at $50 per share.

(6) Subject to mandatory redemption in an amount sufficient to retire on each February 1, beginning in 1993, 120,000 shares at $100 per share plus accrued dividends. Beginning February 1, 1993, the Company may redeem up to 120,000 additional shares each year at $100 per share.

(7) All outstanding shares were redeemed on February 1, 1987 for $52.50 per share.

See notes to financial statements which are an integral part of these statements

Statements of Sources of Funds Provided For Gross Property Additions

	For the Years Ended December 31,		
	1987	1986*	1985*
	(Thousands of Dollars)		
Funds Provided from Operations			
Net income	$ 289,556	$ 292,721	$ 239,999
Items not requiring working capital—			
Depreciation and amortization	176,063	83,758	79,745
Deferred income taxes—net	86,730	46,313	25,932
Deferred investment tax credit—net	1,283	61,590	64,944
Deferred Clinton costs	(78,264)	—	—
Deferred Clinton financing costs	(129,167)	—	—
Allowance for funds used during construction	(73,055)	(219,151)	(161,965)
Total funds provided from operations	273,146	265,231	248,655
Dividends on—Preferred stock	(37,440)	(36,845)	(33,070)
Common stock	(178,493)	(171,111)	(158,726)
Net funds provided from operations	57,213	57,275	56,859
Funds Obtained from External Sources			
Proceeds from sales of—Common stock	76,369	71,216	155,753
Preferred stock	—	110,000	50,000
Capital stock expense	(482)	(1,061)	(1,745)
Proceeds from sales of long-term debt	338,755	575,000	358,930
Proceeds from sale of nuclear fuel	—	—	54,576
Pollution control construction funds held by trustee	—	—	16,891
Net increase (decrease) in notes payable	(25,693)	128,863	(1,000)
Retirement of long-term debt	(276,235)	(333,870)	(5,000)
Redemption of preferred stock	(36,000)	—	—
Total funds obtained from external sources	76,714	550,148	628,405
Other Funds Provided (Used)			
Net decrease (increase) in working capital**	53,577	(98,462)	13,543
Sale of investment in long-term bank notes	7,000	14,000	18,000
Miscellaneous—net	(11,281)	(35,203)	(8,764)
Increase in obligations under capital lease	7,265	18,688	57,259
Total other funds provided (used)	56,561	(100,977)	80,038
Total Funds from Above Sources	190,488	506,446	765,302
Allowance for funds used during construction	73,055	219,151	161,965
Gross Property Additions	$ 263,543	$ 725,597	$ 927,267
Decrease (Increase) in Components of Working Capital**			
Cash and temporary investments	$ 56,748	$ (80,940)	$ (12,760)
Accounts receivable	(33,208)	8,291	(6,187)
Materials and supplies	(14,841)	2,610	21,193
Accounts payable	(13,051)	(23,231)	43,533
Dividends payable	1,975	2,880	5,407
Accrued taxes	(798)	450	(8,336)
Interest accrued	4,368	2,320	8,883
Other—net	51,884	(10,842)	(38,190)
	$ 53,577	$ (98,462)	$ 13,543

Gross Property Additions and Retirements

	For the Years Ended December 31,		
	1987	1986*	1985*
	(Thousands of Dollars)		
Additions —Electric	$ 243,850	$ 700,867	$ 911,256
Gas	19,693	24,730	16,011
	$ 263,543	$ 725,597	$ 927,267
Retirements—Electric	$ 27,971	$ 10,048	$ 9,875
Gas	4,982	4,453	4,163
	$ 32,053	$ 14,501	$ 14,038

**Restated for the effect of capitalized nuclear fuel lease (Note 1).*

***Excluding notes payable, long-term debt, and lease obligations maturing within one year.*

See notes to financial statements which are an integral part of these statements.

Notes to Financial Statements

Note 1—Summary of Significant Accounting Policies:

The Company is subject to regulations of the Illinois Commerce Commission (ICC) and the Federal Energy Regulatory Commission (FERC). Because of the ratemaking process, certain differences arise in the application of generally accepted accounting principles between regulated and non-regulated businesses. Such differences concern mainly the time at which various items enter into the determination of net income in order to follow the principle of matching costs and revenues. The Company's principal accounting policies are described below.

Principles Applied in Consolidation — The Financial Statements include the accounts of IPF (Illinois Power Finance) Company N.V., a wholly-owned subsidiary. All significant intercompany transactions have been eliminated.

Utility Plant — The cost of additions to utility plant and replacements for retired property units is capitalized. Cost includes labor, material, and an allocation of general and administrative costs plus an allowance for funds used during construction (AFUDC) as described later in this note. Maintenance and repairs, including replacement of minor items of property, are charged to maintenance expense as incurred. When units of depreciable property are retired, the original cost and dismantling charges, less salvage, are charged to accumulated depreciation.

Depreciation — For financial statement purposes, the Company depreciates the various classes of depreciable property over their estimated lives by applying composite rates on a straightline basis. Provisions for depreciation of electric utility plant in 1986 and 1985 were equal to 3.4% of the average depreciable cost. In 1987, provisions for depreciation were 2.786% of the average depreciable cost for the Clinton power station (Clinton) and 3.4% of the average depreciable cost for all other electric utility plants. Provisions for depreciation of gas utility plant, as a percentage of the average depreciable cost, were equivalent to 4.0% in 1987, 1986, and 1985.

Revenue and Energy Cost — The Company records revenues as billed to its customers on a monthly cycle billing basis. At the end of each month, there is an amount of unbilled electric and gas service that has been rendered from the latest date of each cycle billing to the month end.

The electric fuel adjustment and purchased gas adjustment clauses provide that changes in allowable energy costs from the Company's filed tariffs are passed on to customers. Accordingly, allowable energy costs that are to be passed on to customers in a subsequent billing period are deferred.

Allowance for Funds Used During Construction — The FERC Uniform System of Accounts defines AFUDC as the net costs for the period of construction of borrowed funds used for construction purposes and a reasonable rate on other funds when so used. AFUDC is capitalized at a rate that is related to the approximate weighted average cost of capital. In 1986 and 1985, the rate was reduced by the income tax effect of the interest portion thereof. In 1987, AFUDC on Clinton continued to be capitalized at a net-of-tax rate, but AFUDC on all other construction was capitalized at a pre-tax rate, and the associated tax effects were deferred. The rate used in computing AFUDC was 9¼% throughout 1986 and 1985. In 1987, the rate used was 9¼% for Clinton construction and 11% for all other construction projects. While cash is not realized currently from such allowance, it is realized under the ratemaking process over the service life of the related property through increased revenues resulting from a higher rate base and higher depreciation expenses.

In accordance with ICC rate orders, the Company excluded $733 million effective January 1, 1985 and $804 million effective August 7, 1985 of electric plant construction work in progress (CWIP) from the base on which AFUDC was computed for Clinton during 1985. The amount of Clinton costs in rate base was increased to $1.156 billion effective October 4, 1986, after receiving permission from the Nuclear Regulatory Commission (NRC) to begin fuel loading. Clinton costs in rate base increased to $1.54 billion effective April 22, 1987, after receiving a full power license from the NRC for Clinton. Both of these increases were authorized in the August 1985 ICC rate order. Because these orders authorized that Clinton costs be included in the rate base upon which the Company realized revenues, there was no material effect on net income. On April 24, 1987, Clinton was placed in service and AFUDC thereon ceased.

Deferred Clinton Costs — A November 1987 ICC order specifies the deferral of certain Clinton post-construction operating costs, until rates to reflect such costs are effective. During this period a deferred financing cost is computed on Clinton plant not in rate base and the deferred costs. The deferred financing cost is capitalized at a rate that is similar to AFUDC. In 1987, the rate used to compute deferred Clinton financing costs was 9¼% through October and 8½% thereafter. These deferred costs will be recovered over the remaining life of the plant to the extent that Clinton construction costs are included in rate base.

Clinton Power Station Decommissioning — Decommissioning of Clinton will be funded by contributions to an external trust fund in accordance with an ICC order issued July 15, 1987. An annual contribution of $2.1 million over 39¼ years is

estimated to be required to decommission the Company's share of Clinton.

Amortization of Nuclear Fuel — The Company leases nuclear fuel from Illinois Power Fuel Company (Fuel Company). In accordance with the provisions of Statement of Financial Accounting Standards No. 71 "Accounting for the Effects of Certain Types of Regulation", the Company retroactively capitalized its nuclear fuel lease with the Fuel Company. This change did not affect earnings. Amortization of nuclear fuel is determined on a unit of production basis. A provision for spent fuel disposal costs is charged to fuel expense based on kilowatt-hours generated.

Unamortized Deferred Abandonment Cost — The ICC order of August 7, 1985 authorized the Company to amortize and recover through rates $31.9 million of its investment in Clinton Unit 2 over a five-year period. No return was allowed on the unamortized investment balance. Additional costs of $2.9 million were written off to Miscellaneous-net in the third quarter of 1985.

Unamortized Debt Expense — Debt issuance costs are amortized over the lives of the related issues. Costs related to refunded debt are amortized over the lives of the related new debt issues.

Income Taxes — The Company normalizes the income tax effects of transactions causing timing differences between inclusion in financial statement and taxable income. The Company computes deferred income taxes based on the statutory income tax rates in effect during the period that the timing differences originate. Deferred income taxes are amortized to income as the underlying timing differences reverse.

Principal sources of timing differences causing deferred taxes are as follows:

- Use of the most liberalized depreciable lives and methods allowed by the Internal Revenue Code,
- Capitalization of certain construction overheads, dismantling, and other costs for book purposes that are claimed as current deductions for income tax purposes,
- Revenues and energy costs recognized in different periods for financial statement purposes than for income tax purposes, and
- Alternative minimum tax payable in the current year that can be used to offset future tax liabilities.

For income tax return purposes, net depreciable utility plant does not include the allowance for funds used during construction that is capitalized for financial statement purposes.

Investment tax credits, which reduce federal income taxes, have been deferred and are being amortized to income over the life of the property which gave rise to the investment tax credits.

Federal and state income taxes are allocated between operating and non-operating income and expenses. The tax effects relating to non-operating activities are included in Other Income—Miscellaneous-net.

Note 2—Short-Term Loans and Lines of Credit:

The Company had total lines of credit represented by bank commitments amounting to $568 million of which $260 million was unused at December 31, 1987. These bank commitments support the amount of commercial paper outstanding at any time and are available to support other Company activities.

The Company has a $50 million revolving loan commitment through November 13, 1992. No borrowings were made under this agreement during 1987. The agreement is on a fee basis of .15% for the unused line of credit. In addition, the interest rate under this agreement on funds borrowed is based upon the borrowing rate of key banks in the London interbank market.

In June 1987, the Company obtained a $100 million, five-year revolving loan commitment through June 4, 1992. There was an $80 million revolving loan made under this agreement with $60 million still outstanding at year end. For the unused portion of the commitment, the Company pays a fee of 3/16% per annum on the amount of available credit. The interest rate on borrowings under this agreement is, at the Company's option, based upon the lending banks' reference rate, their Certificate of Deposit rate, the borrowing rate of key banks in the London interbank market, or a bid option.

In addition, the Company has a credit agreement entered into in 1985 that provides for a revolving loan agreement of $175 million with the provision for conversion to a three-year term loan. Fees for this agreement are primarily based on 0.3% of the unused portion of the commitment. Interest rates on borrowings are, at the Company's option, based upon the banks' prime rate, their 90-day Certificate of Deposit rate, or the borrowing rate at key banks in the London interbank market. There was a $100 million revolving loan outstanding under this agreement during 1987 (see "Statements of Long-Term Debt").

In 1984, the Company entered into a $180 million, three-year revolving loan agreement that has a provision for conversion to a three-year term loan. There was a $100 million revolving loan outstanding under this agreement during 1987 (see "Statements of Long-Term Debt"). For the unused portion of the commitment, the Company pays an annual fee of 1/4%, partially offset by a credit related to average balances maintained at the banks. The interest rate on borrowings under this agreement is, at the Company's option, based upon the lending banks' prime rate, their 90-day Certificate of Deposit rate, or the borrowing rate of key banks in the London interbank market.

The Company also has lines of credit totaling approximately $63 million with commercial banks for short-term bank borrowings. Bank borrowings under such commitments have a maximum 360-day maturity from the time of issuance and at the Company's option carry an interest rate less than or equivalent to the prime rate in effect at the time of

issuance, adjusted to the prime rate in effect on the first day of each calendar quarter thereafter. Borrowings were made under these agreements in 1987 for about $48 million. The borrowings had a weighted average interest rate of 7.9% during 1987 and were still outstanding at year end.

In December 1987, the Company obtained letter of credit agreements in the total amount of $80,547,948 from the Mitsubishi Bank in support of the issuance of $75 million Pollution Control Variable Rate Debt. The Company pays a fee of .30% per annum on the unused amount of the credit. Interest rates on unreimbursed drawings under the letters of credit are at the Federal Funds rate as defined by the bank plus .5% per annum for up to 30 days, at the bank's prime rate for 31 days through one year and at the bank's prime rate plus 1% per annum for over one year.

Notes payable at December 31, 1987 consisted of about $48 million of commercial bank borrowings as noted above and $55 million in commercial paper bearing interest at a weighted average rate of 7.8% and maturing between January 5, 1988 and January 29, 1988. At December 31, 1986, notes payable consisted of about $52 million of commercial bank borrowings and about $77 million in commercial paper, bearing interest at a weighted average interest rate of 6.0%, which matured between January 15 and January 29, 1987. There were no outstanding notes payable at December 31, 1985.

The maximum total amount of short-term borrowings at any month end during 1987, 1986, and 1985 was $124.9 million, $230.6 million, and $60.0 million, respectively. The average daily short-term borrowings during these periods approximated $104.3 million, $111.2 million, and $14.3 million, respectively with a weighted average interest rate of 7.3%, 7.3%, and 8.4%, respectively. The Company calculated the borrowings as an average of the daily borrowings outstanding. The Company calculated the interest rates by dividing the interest expense during the period for such borrowings by the average short-term borrowings indicated above.

Note 3—Facilities Agreements:

Pursuant to agreements as amended, Soyland Power Cooperative, Inc. (Soyland) and Western Illinois Power Cooperative, Inc. (WIPCO) have an investment of $450 million in the direct costs of placing Clinton in commercial operation. The Cooperatives have paid their portion of construction expenditures. This results in an ownership in Clinton of 7.02% for Soyland and 6.36% for WIPCO. The Company's ownership percentage of 86.62% is reflected in utility plant, at original cost; and accumulated depreciation on the balance sheet. Each respective participant is responsible for their share of nuclear fuel. The Company's share of Clinton operating expenses is included in the corresponding operating expenses on its income statement. See "Note 13—Clinton Power Station" for information relating to a lawsuit filed September 22, 1986 against the Company.

Each party is responsible for its portion of financing, construction, and operating expenditures. The Company's investment in Clinton including AFUDC and land at December 31, 1987 is $3.8 billion. The agreements include the provisions that the Company has control over construction and operation of the generating station, that the parties share electricity generated in proportion to their interests, and that the Company will have certain obligations to provide replacement power to the Cooperatives when the unit is out of service.

In a related agreement, the Cooperatives and the Company signed a Power Coordination Agreement in October 1984. Under the agreement, which was effective January 1, 1985, the Company will provide the Cooperatives with 10.7% (400 megawatts) of electrical capacity from its fossil-fueled generating plants through 1992, 8% in 1993 and 1994, and 4% in 1995 through 2004 and will transmit energy for the Cooperatives through the Company's transmission and subtransmission system. This will be in addition to the capacity the Cooperatives receive as part owners of Clinton. The Company is compensated with capacity charges and for energy costs and variable operating expenses.

Note 4—Income Taxes:

Income taxes included in the Statements of Income consist of the following components:

	Years Ended December 31,		
	1987	1986	1985
	(Thousands of Dollars)		
Current taxes—			
Included in Operating Expenses and Taxes	$ 42,224	$ 38,211	$ 39,939
Included in Other Income—Miscellaneous—net	(54,513)	(59,279)	(46,147)
Total current taxes	(12,289)	(21,068)	(6,208)
Deferred taxes—			
Book-tax depreciation differences—net	85,702	12,376	9,096
Certain overhead, dismantling and other costs capitalized—net	10,015	26,479	16,618
Deferred Clinton costs	24,978	—	—
Alternative minimum tax	(32,699)	—	—
Book-tax revenue and energy cost recognition differences	(5,582)	(835)	2,008
Clinton Unit 2 abandonment	(3,165)	(3,169)	(1,283)
Total deferred taxes	79,249	34,851	26,439
Deferred investment tax credit—net	1,282	61,590	64,944
	$ 68,242	$ 75,373	$ 85,175

Income taxes are less than the amount which would be computed by applying the statutory federal and state income tax rates to pre-tax income

(43.8% in 1987 and 49.5% in 1986 and 1985); the principal differences are as follows:

	Years Ended December 31,		
	1987	1986	1985
	(Thousands of Dollars)		
Computed tax expense at statutory federal and state income tax rates	$156,691	$ 182,045	$ 160,818
Reductions (increases) in income taxes resulting from—			
Allowance for funds used during construction	31,993	108,383	80,101
Deferred Clinton financing costs	56,567	—	—
Other—net	(111)	(1,711)	(4,458)
Total income taxes	$ 68,242	$ 75,373	$ 85,175

Combined federal and state effective income tax rates were 19.1%, 20.5%, and 26.2% for the years 1987, 1986, and 1985, respectively.

Statement of Financial Accounting Standards No. 96, "Accounting for Income Taxes" adopts a liability method of tax allocation relating to transactions that affect book and tax income in different reporting periods. The statement must be adopted no later than 1989. See discussion of this item in Management's Discussion and Analysis on page 18.

Note 5—Segments of Business:

The Company is a public utility engaged in the generation, transmission, distribution, and sale of electric energy and the distribution and sale of natural gas.

	1987			1986**			1985**		
	Electric	Gas	Total Company	Electric	Gas	Total Company	Electric	Gas	Total Company
	(Thousands of Dollars)			(Thousands of Dollars)			(Thousands of Dollars)		
Operation information—									
Operating revenues	$ 910,844	$ 308,679	$1,219,523	$ 814,144	$ 369,721	$ 1,183,865	$ 766,467	$ 400,897	$ 1,167,364
Operating expenses, excluding provision for income taxes and deferred Clinton costs	667,519	274,190	941,709	518,559	323,196	841,755	486,951	344,811	831,762
Deferred Clinton costs	(78,264)	—	(78,264)	—	—	—	—	—	—
Pre-tax operating income	321,589	34,489	356,078	295,585	46,525	342,110	279,516	56,086	335,602
Allowance for funds used during construction (AFUDC)	72,871	184	73,055	218,977	174	219,151	161,819	146	161,965
Deferred Clinton financing costs	129,167	—	129,167	—	—	—	—	—	—
Pre-tax operating income, including AFUDC and deferred Clinton financing costs	$ 523,627	$ 34,673	558,300	$ 514,562	$ 46,699	561,261	$ 441,335	$ 56,232	497,567
Other (income) and deductions			(57,083)			(64,679)			(48,367)
Interest charges			203,071			198,567			174,613
Provision for income taxes			122,756			134,652			131,322
Net income			$ 289,556			$ 292,721			$ 239,99[illegible]
Other information—									
Depreciation	$ 131,596	$ 15,812	$ 147,408	$ 56,507	$ 15,225	$ 71,732	$ 55,329	$ 14,768	$ 70,097
Capital expenditures	$ 243,850	$ 19,693	$ 263,543	$ 700,867	$ 24,730	$ 725,597	$ 911,256	$ 16,011	$ 927,267
Investment information—									
Identifiable assets*	$5,285,930	$ 300,265	$5,586,195	$ 4,952,694	$ 300,144	$ 5,252,838	$ 4,312,502	$ 313,847	$ 4,626,349
Nonutility plant and other investments			9,697			14,934			27,584
Assets utilized for overall Company operations			326,842			355,270			240,455
Total assets			$5,922,734			$ 5,623,042			$ 4,894,388

**Utility plant, nuclear fuel and acquisition adjustment (less accumulated depreciation and amortization), materials and supplies, unamortized deferred abandonment cost, deferred Clinton costs, prepaid gas, deferred energy costs, and deposit with pollution control authorities.*

***Restated for the effect of capitalized nuclear fuel lease (Note 1).*

Note 6—Pension and Other Post-Employment Benefit Costs:

The Company has defined benefit pension plans covering all officers and employees. Benefits are based on years of service and the employee's earnings. The Company's funding policy is to contribute annually at least the minimum amount required by government funding standards, but not more than can be deducted for federal income tax purposes. In 1987, the Company adopted Statement of Financial Accounting Standards No. 87 "Employers' Accounting for Pensions" (FAS 87). Adoption of FAS 87 decreased annual pension costs by approximately $5.6 million, a portion of which was capitalized.

Pension cost for 1987 included the following components:

	(Thousands of Dollars)
Service cost on benefits earned during the year	$ 8,911
Interest cost on projected benefit obligation	11,222
Return on plan assets	(42,713)
Net amortization and deferral	20,110
Total pension cost (benefit)	$ (2,470)

The estimated funded status of the plans at December 31, 1987, using a measurement date of September 30, 1987, a discount rate of 8½% and a rate of increase of future compensation levels of 6%, was as follows:

	(Thousands of Dollars)
Actuarial present value of:	
Vested benefit obligation	$ 95,471
Accumulated benefit obligation	$ 108,828
Projected benefit obligation	$(140,460)
Plan assets at fair value	244,336
Excess of assets over projected benefit obligation	103,876
Unamortized net gain	(40,472)
Unrecognized net asset at transition	(68,406)
Accrued pension cost included in Accounts Payable	$ (5,002)

The plan assets consisted primarily of common stocks, fixed income securities, and real estate. The actuarial present value of accumulated plan benefits at January 1, 1987 was $107,189,000 (including vested benefits of $93,825,000). Activity in the capital markets subsequent to September 30, 1987 has caused plan assets to decline by approximately 15% as of December 31, 1987.

The pension cost for 1987 was calculated using a measurement date of January 1, 1987, a discount rate of 8%, rate of increase of future compensation levels of 6%, and return on assets of 9%. The Company's pension costs prior to 1987 were accounted for in accordance with previous accounting principles. These costs were $3,136,000 and $2,059,000 in 1986 and 1985, respectively. The Company did not make any cash contributions during 1987, 1986, and 1985 for the pension plan due to its overfunded status.

In addition, the Company provides certain health care and life insurance benefits for substantially all active and retired employees. These benefits are provided through an insurance company, and premiums are based on actual claims experience. The Company recognizes the cost of these benefits as premiums are paid. Costs for 1987, 1986, and 1985, net of contributions by both active and retired employees, were $8,469,000, $8,341,000, and $7,788,000, respectively. The cost of providing those benefits for about 1,030 retirees is not separable from the cost of providing benefits for about 4,530 active employees.

Note 7—Debt Retirement Provisions:

During the five years from December 31, 1987, the amounts of debt maturing annually are $33,333,000 in 1988, 1989, and 1990, $61,364,000 in 1991, and $205,294,000 in 1992. These amounts exclude capital lease requirements. See "Note 11—Capital Leases".

In addition, certain supplemental indentures to the Mortgage and Deed of Trust require that the Company make annual deposits in cash as a sinking fund. For the 9¾% series due 2004, an annual deposit of $5,000,000 is required. For the 6.60% series due 2004 (Pollution Control Series A), an annual deposit of $125,000 in 1988, increasing $25,000 in 1989 and every two years thereafter is required. These amounts are not subject to reduction.

Certain other supplemental indentures require annual deposits, as a sinking and property fund, in amounts not to exceed $5,600,000 in 1988, $6,600,000 in 1989 and 1990, and $7,100,000 in 1991 and 1992. These amounts are subject to reduction in accordance with the mortgage, and historically have been met by pledging property additions.

The above bonds are secured by a first mortgage lien on substantially all of the fixed property, franchises, and rights of the Company with certain minor exceptions expressly provided in the mortgage securing the bonds. The remaining balance of net bondable additions at December 31, 1987 was approximately $2,099,000,000.

Note 8—Redeemable Preferred Stock:

The Company issued $50 million of 8.52% redeemable serial preferred stock and $60 million of 8.00% redeemable serial preferred stock in 1986. In 1987, the Company redeemed $36 million of 11.66% redeemable serial preferred stock.

During the five years from December 31, 1987, the amounts of redeemable preferred stock outstanding at such date, required to be redeemed at stated value are $10 million in 1990, $10 million in 1991, and $20 million in 1992. No shares are required to be redeemed in 1988 and 1989.

Note 9—Common Stock and Retained Earnings:

The Company has an Automatic Reinvestment and Stock Purchase Plan and an Employees Stock Ownership Plan (ESOP) for which at December 31, 1987, 1,820,535 and 20,761 shares, respectively, of common stock were designated for issuance.

The Company also has a Tax Reduction Act Stock Ownership Plan (TRASOP) pursuant to federal income tax laws, under which Company contributions of common stock are based on a percentage of payroll costs. Because the tax benefit for contributions to the plan was repealed under the 1986 Tax Reform Act, 1987 was the last year for contributions. Under this Plan, 216,331 shares of common stock were designated for issuance at December 31, 1987.

The Company also has an Incentive Savings Plan (Plan) for salaried employees. Under the Plan, the Company matches a portion of the employee contributions. The Company's matching contribution is used to purchase common stock. Under this Plan, 43,472 shares of common stock were designated for issuance at December 31, 1987.

Changes in common stock during 1987, 1986, and 1985 were as follows:

	1987		1986		1985	
	Shares	Amount*	Shares	Amount*	Shares	Amount*
Balance beginning of year	65,608,876	$1,221,838	62,800,583	$ 1,150,622	56,381,448	$ 994,869
Public offerings	—	—	—	—	3,000,000	78,480
Automatic Reinvestment and Stock Purchase Plan	2,723,349	69,457	2,573,622	64,854	3,160,678	71,136
ESOP	33,388	858	28,675	759	32,810	757
TRASOP	199,659	5,397	194,218	5,279	210,243	5,012
Incentive Savings Plan	23,629	657	11,778	324	15,404	368
Balance end of year	68,588,901	$1,298,207	65,608,876	$ 1,221,838	62,800,583	$ 1,150,622

**Thousands of dollars*

None of the Company's retained earnings at December 31, 1987 was restricted with respect to the declaration or payment of dividends.

Note 10—Quarterly Financial Information (Unaudited):

	First Quarter		Second Quarter		Third Quarter		Fourth Quarter	
	1987	1986	1987	1986	1987	1986	1987	1986
	(Thousands of Dollars Except Earnings Per Common Share)							
Operating revenues	$325,701	$355,900	$253,727	$245,259	$347,735	$303,818	$292,360	$278,888
Operating income	51,384	50,747	50,272	41,829	98,775	67,456	32,891	47,426
Net income	71,742	69,850	63,427	62,396	113,764	92,416	40,623	68,059
Net income applicable to common stock	62,108	61,110	54,144	53,203	104,464	83,283	31,143	58,883
Earnings per common share	$ .94	$ .96	$ .81	$ .83	$ 1.54	$ 1.28	$ .46	$ .90

Quarterly earnings per common share are based on weighted average number of shares outstanding during the quarter and the sum of the quarters may not equal annual earnings per common share.

The 1987 fourth quarter net income was reduced by $19 million (28¢ per share) due to the provisions of the negotiated settlement. See "Note 13—Clinton Power Station". Additionally, the 1987 fourth quarter net income was reduced by $11 million (16¢ per share) due to the effect of excluding from the Clinton cost deferrals the portion of the Company's electric utility business not under the jurisdiction of the ICC, because the November 1987 retail rate filing excluded that portion of the Company's operations.

Note 11—Capital Leases:

Illinois Power Fuel Company (Fuel Company), which is 50% owned by the Company, was formed in January 1981 for the purpose of financing a portion of the nuclear fuel requirements of Clinton. The Company entered into a lease agreement with the Fuel Company under which the Company leases nuclear fuel. Lease payments, which are equal to the Fuel Company's cost of fuel as consumed (including related financing costs), began in 1987 when Clinton began pre-commercial operation. Billings under the lease agreement during 1987 were $26.5 million, including $9.2 million of financing costs. The Company is obligated to make subordinated loans to the Fuel Company at any time the obligations of the Fuel Company that are due and payable exceed the funds available to the Fuel Company. The Company has an obligation for spent nuclear fuel disposal costs of leased nuclear fuel.

At December 31, 1987 and 1986 current obligations under capital lease for nuclear fuel are $46,150,000 and $25,235,000, respectively. At

December 31, 1987 and 1986 current obligations for other property under capital leases are $1,691,000 and $1,493,000, respectively.

Over the next five years projected lease payments under capital leases are as follows:

	(Thousands of Dollars)
1988	$ 48,000
1989	33,000
1990	30,000
1991	29,000
1992	40,000
Total	$180,000

Note 12—Commitments and Contingencies:

Construction Program — The 1988 construction budget is $137 million, which includes $102 million for electric facilities, $23 million for gas facilities and $12 million for nuclear fuel. The five-year construction program for 1988 through 1992 is estimated to be $644 million.

Insurance — The Company has insurance coverage for loss due to physical damage, including contamination, to Clinton. This insurance is structured through a level of primary coverage provided by nuclear insurance pools and excess coverage from a combination of nuclear insurance pools and an industry-owned mutual insurance company. The primary coverage provides limits of $500 million and the excess coverage currently provides limits of $1.025 billion, for a total available coverage of $1.525 billion. In addition, the Company has replacement power insurance coverage for the extra cost to purchase replacement power in case of a temporary accidental shutdown of the plant.

A major loss involving Clinton or other stations insured by the industry-owned mutual insurance company could result in additional annual premium assessments to the Company of up to approximately $10.2 million. In addition, while the Company has no reason to anticipate a serious nuclear incident at Clinton, if such an incident should occur, the claims for property damage, replacement power costs, and/or other costs and expenses could materially exceed the limits of insurance coverage available.

All nuclear power station operators are subject to the Price-Anderson Act (Act). Although the Act expired on August 1, 1987, all commercial reactors with construction permits or operating permits issued before August 1, 1987 remain covered under the old law. Under the Act public liability for a nuclear incident is currently limited to $720 million. Coverage of the first $160 million is provided by private insurance, with the excess coverage provided by retrospective premium assessments against each licensed nuclear reactor in the United States. The Company's maximum assessment would be $5 million per incident, but not more than $10 million per year. One of the proposals to amend the Act, under consideration in Congress, would increase the maximum retrospective assessment against each operating reactor to $63 million, limited to assessments of $10 million per year. The Company cannot predict the final outcome of the legislative proposals.

Effective January 1, 1988, a new Master Worker Policy will cover workers who claim bodily injury, sickness, or disease as a result of initial radiation exposure occurring on or after January 1, 1988. The policy will have an aggregate limit of $160 million applying to the nuclear utility industry as a whole. As claims are paid under the policy there is a provision for automatic reinstatement of policy limits up to an additional $160 million. There is also a provision for assessment of additional premium if claims exceed funds available in the insurance company reserve accounts to pay claims. The Company's maximum share of additional premium in future years for this contingency could be up to approximately $2.7 million.

Other — The Company is involved in legal or administrative proceedings before various courts and agencies with respect to matters occurring in the ordinary course of business, some of which involve substantial amounts. Management believes that the final disposition of these proceedings will not have a material adverse effect on the financial position of the Company.

Note 13—Clinton Power Station:

The Company received a full-power operating license for Clinton from the Nuclear Regulatory Commission (NRC) on April 17, 1987, and based on an order of the ICC approving a negotiated settlement, an in-service date of April 24, 1987 was established. Clinton is fully operational as a base load generating unit supplying electric service to our customers.

The Company's portion of the cost of Clinton is $3.8 billion. At December 31, 1987, $1.5 billion of Clinton costs are included in rate base and are earning a return.

Ownership of an operating nuclear generating unit exposes the Company to significant risks including increased regulatory, safety, and environmental requirements. The Company expects to be allowed to continue to operate Clinton; however, if any unforeseen or unexpected developments would prevent the Company from doing so, the Company could be materially adversely affected.

Rate & Regulatory Matters

Clinton Construction Audit — In Illinois the cost of a new electric generating plant may not be recovered in a utility's rates unless it is reasonable. Therefore, an audit is being conducted by Touche Ross & Co. and The Nielsen-Wurster Group under contract with the ICC.

A Phase I audit report filed on January 9, 1986 covered the time frame from the beginning of the project through March 31, 1985 (at which time the Company's investment in Clinton was $2.4 billion). In this audit report, Touche Ross/Nielsen-Wurster contend that a portion of Clinton costs associated with the stop work orders issued in early 1982 is

unreasonable. The report estimates that these costs are between $294 million and $464 million. Nielsen-Wurster has stated in written testimony to the ICC that $294 million is the appropriate point in this range.

Three nationally known firms, Theodore Barry & Associates, Ebasco Services Incorporated, and Burns and Roe Company, were retained on behalf of the Company to evaluate management of the Clinton project through independent audits. The independent audits are separate from the one being conducted by the two firms hired by the ICC, and Phase I audits show that construction of Clinton generally has been managed reasonably by the Company. The conclusions of these audit reports and the Touche Ross/Nielsen-Wurster Phase I audit report generally agree but differ on one point. Touche Ross/Nielsen-Wurster contend that a portion of the cost of Clinton associated with the stop work actions issued in early 1982 was unreasonable. The ICC has completed hearings on Phase I of the audit, but is deferring the issuance of an order until the audit and hearings on Phase II, which covers the period from April 1, 1985 through completion of the project, have been completed.

The Phase II audit report, which is expected to be submitted to the ICC by the end of the first quarter of 1988, could allege additional unreasonable costs. An order is expected from the ICC in late 1988. As in Phase I, independent audits to evaluate management of Clinton during this period are being performed on behalf of the Company.

In an interim order regarding the completion of Clinton, the ICC ruled that any Clinton costs expended above the amount of $2,698,361,000 for which the Company fails to present affirmative evidence of reasonableness shall not be included in rate base, even if no other party has presented any evidence challenging these costs as being unreasonable. The Company believes that the burden of proof under this order is no greater than that currently required under the Public Utilities Act generally.

Rate Request — On November 19, 1987, the Company filed with the ICC a request for an electric rate-moderation plan to incorporate Clinton into rates. The rate of return requested in the plan reflects current capital cost and is 10.25% compared to the 11.95% currently allowed. The rate plan incorporates a mirror CWIP plan, and a deferred return phase-in plan. The request includes a first-year electric revenue increase of 11.1% effective November 1988, producing approximately $92.7 million of revenue annually net of anticipated fuel savings and a senior citizen discount. This first-year increase would be followed by annual increases beginning in 1989, for six to nine years. These annual increases would be tied to the rate of inflation and would range from a minimum of about 4% to a maximum of 5.9%. Although the rate request provides the needed future rate increases to recover the Company's investment in Clinton and related operating costs, it is subject to approval or modification by the ICC. An order from the ICC is expected in October 1988.

Under the electric rate-moderation plan, there would be a cash flow delay of approximately $450 million over the first seven years of the plan due to its mirror CWIP provisions (representing amounts collected in rates prior to the in-service date of Clinton as a result of having CWIP in rate base). This amount would be capitalized as a part of Clinton costs for recovery over the life of the plant. In addition, under the deferred return provisions of the plan, cash flow of approximately $250 million would be delayed during the first five years for recovery during the remaining years of the plan.

Deferred Costs — The Company is deferring certain post-construction costs of Clinton, based on the ICC order approving the negotiated settlement, including depreciation, taxes other than income taxes, and financing costs on both the amount of plant costs not in rate base and these deferred costs from the in-service date until a rate order reflecting the inclusion of Clinton in rate base becomes effective (the regulatory lag period). As a result of the negotiated settlement, all Clinton operation and maintenance costs are being expensed. However, as a partial offset, the negotiated settlement also provided that the electric revenues previously deferred, as ordered by the ICC to reflect the lower federal income tax rates under the Tax Reform Act of 1986, be included in income and all future deferrals be discontinued. The negotiated settlement caused a net reduction in 1987 earnings of $19 million (net of income taxes) or 28¢ per share, and future earnings will be decreased by an estimated $2 million to $3 million per month until the electric rate order requested on November 19, 1987 is effective.

During 1987, the Company recorded post-construction cost deferrals of $207 million ($177 million, net of income taxes). Such deferred costs will be included in rates to the extent that Clinton costs are allowed in rates and recovered over the remaining life of the plant. Cash flow associated with these deferrals will be delayed until those costs are recovered in rates.

Decommissioning and Nuclear Fuel Disposal Costs —The Company is responsible for its ownership share of the costs of decommissioning Clinton and for spent nuclear fuel disposal costs. The establishment of an external trust fund was authorized by the ICC to invest funds for the future dismantlement and decommissioning costs of Clinton (estimated to be $87.6 million in 1987 dollars). Decommissioning costs are currently being deferred ($1.4 million during 1987) and will begin to be collected through rates upon approval of the electric rate request before the ICC.

Under the Nuclear Waste Policy Act of 1982, the U.S. Department of Energy (DOE) is responsible for the permanent storage and disposal of spent nuclear fuel. DOE currently charges one mill per kilowatt-hour generated for future disposal of spent fuel. The Company is recovering this amount through its rates.

Accounting Developments

In December 1986, the Financial Accounting Standards Board (FASB) issued Statement of Financial Accounting Standards No. 90, "Regulated Enterprises — Accounting for Abandonments and Disallowances of Plant Costs, an amendment of FASB Statement No. 71" (FAS 90), which is applicable to partial disallowances of plant costs and plant abandonments. The statement is effective for the Company in 1988 and the Company intends to adopt it on a prospective basis. This statement requires that a partial disallowance of plant costs by a regulatory commission be recorded as a loss when such a disallowance becomes probable and a reasonable estimate can be made. Under generally accepted accounting principles, as effective through 1987, a disallowance would not have required an immediate charge to income unless it resulted in a negative rate of return on the Company's investment in Clinton, but it would have been reflected as a reduction in the Company's earnings over the life of the plant. In addition, once adopted, the statement requires that AFUDC be capitalized only if its subsequent inclusion in allowable costs for ratemaking purposes is probable.

The Company did not adopt the provisions of FAS 90 prior to 1988. If the Company had adopted the new standard, the Company believes that no loss provision for a disallowance would have been required in 1987 or prior financial statements because no reasonable estimate of loss can be made and the low end of the range of possible disallowance is zero.

In August 1987, the FASB issued Statement of Financial Accounting Standards No. 92, "Regulated Enterprises — Accounting for Phase-in Plans, an amendment to FAS 71" (FAS 92), which established the criteria for financial statement purposes that must be met in order for costs to be deferred for recovery in the future. The statement is effective for the Company in 1988 and the Company intends to adopt it on a prospective basis.

The Company's proposed deferred return phase-in plan meets the criteria of FAS 92.

FAS 92 also states that an allowance for earnings on shareholders' investment may only be capitalized during construction, as AFUDC, or as part of a qualified phase-in plan. The Company's deferral of certain post-construction costs in the regulatory lag period does not meet the criteria of a phase-in plan as established by this statement. Accordingly, beginning in 1988 for financial statement purposes, the Company may not capitalize an allowance for earnings on shareholders' investment as part of post-construction cost deferrals. Such allowance for earnings on shareholders' investment would have been approximately $11 million per month during 1988. However, pursuant to the ICC order, such amounts may be recovered over the life of the plant to the extent that Clinton costs are allowed in rate base.

Legal Proceedings

On September 22, 1986, members of 22 Illinois rural electric power distribution cooperatives filed a lawsuit against the Company concerning the Company's construction management of Clinton. The action purported to be brought derivatively on behalf of the member cooperatives of WIPCO and Soyland and, in turn, on behalf of WIPCO and Soyland, and as a class action on behalf of the individual members of the distribution cooperatives. On January 7, 1988, on the motion of WIPCO and Soyland, the Circuit Court for Sangamon County, Illinois, ruling orally from the bench, dismissed the derivative claims but granted leave to WIPCO and Soyland to be realigned as plaintiffs and to file their five-count complaint against the Company (Soyland complaint). In the Soyland complaint, WIPCO and Soyland alleged that the Company breached fiduciary duties to them and was negligent in connection with the planning, construction, and licensing of Clinton. The Soyland complaint seeks recovery of an unspecified amount of compensatory damages from the Company. The Company has moved for an extension of time to respond to the Soyland complaint until after a written order detailing the Court's January 7 ruling has been entered.

In the one remaining count of the original complaint filed by the members of the distribution cooperatives, those plaintiffs seek to proceed on behalf of a class of all customers of cooperatives that obtain electrical power from Clinton. This count alleges that such customers have been and will be "injured due to drastically increased energy supply costs". The plaintiffs seek unspecified compensatory damages from the Company. On January 14, 1987, the Circuit Court for Sangamon County, Illinois denied the Company's motion to dismiss the class action count of the original complaint for lack of standing. The Court has not yet addressed other grounds asserted by the Company in support of its motion to dismiss that count.

The Company believes that it has managed the construction of Clinton prudently and efficiently and that it should be allowed to recover the full cost of that unit through its rates. Almost all recent cases of which the Company is aware in which regulatory commissions have conducted prudence audits in connection with placing new generating units in rates have resulted in some investment being disallowed or proposed to be disallowed. In many such cases, the amounts involved were significant.

Management is unable to predict the ultimate outcome of the uncertainties discussed in this note which could have a material adverse effect on the Company's earnings and/or financial position.

Two-Year Dividends and Stock Prices by Quarters

The common stock is listed on the New York Stock Exchange and the Midwest Stock Exchange. The prices below are the prices reported on the Composite Tape. The preferred stocks are listed on the New York Stock Exchange and the prices below are the prices on that Exchange.

		1987 Stock Prices								1986 Stock Prices							
		1		2		3		4		1		2		3		4	
	Dividends(1)	High	Low	High	Low	High	Low	High	Low	High	Low	High	Low	High	Low	High	Low
Common	$ .66	31½	27⅞	28⅜	25⅛	27	24⅞	27	21¼	29	23⅛	29¾	23⅞	32	25½	31¼	28½
4.08% Pfd.	.51	25½	23	24⅛	21	22½	19½	20¼	18¼	23	18¼	23¾	20	[illegible]	20⅛	25	22
4.26% Pfd.	.53¼	25⅜	24	24¾	22⅜	23½	21	22¾	20	24	18⅜	24⅜	20¾	25	21½	26¾	24
4.70% Pfd.	.58¾	28	26½	26¾	23	25⅜	22½	24⅛	21	25	20½	26⅜	22½	28⅜	23	28⅜	25⅜
4.42% Pfd.	.55¼	26½	24	25¾	21⅛	23¼	21¼	22⅛	19½	24	19	25¼	21	25¼	22½	27⅜	23¾
4.20% Pfd.	.52½	26	24½	25¾	21½	24	21⅜	23¾	19	23½	19	25	20⅛	25⅜	22	26½	23½
8.24% Pfd.	1.03	49¾	45¼	47½	42	44	39	41½	36	46½	38	47	41½	48½	41⅜	49½	44⅜
7.56% Pfd.	.94½	45¼	41¼	44¼	36⅜	40¼	35½	41	30	42¾	33	43	37	44¼	37¾	45½	40½
8.94% Pfd.	1.11⅞	51½	47⅜	48¾	41½	46½	41⅛	42¾	37	49⅜	39	50	44⅜	50½	44⅜	51½	47
8.00% Pfd.	1.00	47¼	44¾	47	39¾	41½	37⅞	38⅜	33	44½	35½	46	39⅜	45¾	39	48	44⅜
11.66% Pfd. (4)	1.45¾	54¼	52½	—	—	—	—	—	—	56	52¼	57	52¼	58½	55¼	58½	55
Adj. Rate Pfd. A	(2)	43	38¾	41	37¾	41⅛	38¾	42	38½	46⅜	37	45½	41	44⅜	40	44⅜	37
Adj. Rate Pfd. B	(3)	51¼	47	50⅜	46	51	49⅛	51	48	52	49½	52¼	49½	50½	46	51¾	47
11.75% Pfd.	1.46⅞	62	56½	58¼	55	58¾	54½	57½	55	58	52¾	58	56⅛	58	55	59½	57
8.52% Pfd.	1.065	54	54	53	50	—	—	50	47	--	—	50¼	50	51¾	50¼	52	52
8.00% Pfd.	2.00	—	—	102¼	97⅞	99⅛	96¼	96⅜	96⅜	—	—	—	—	—	—	—	—

(1) The amount declared in each quarter during 1987 and 1986.

(2) Dividend rate changes. Rates for dividends declared in 1987 were $0.75, $0.75, $0.75, and $0.8375 in the first, second, third, and fourth quarters, respectively. Rates for dividends declared in 1986 were $0.7875, $0.75, $0.75, and $0.75 in the first, second, third, and fourth quarters, respectively.

(3) Dividend rate changes quarterly. Rates for dividends declared in 1987 were $0.875, $0.875, $0.900, and $1.0688 in the first, second, third, and fourth quarters, respectively. Rates for dividends declared in 1986 were $1.0188, $0.875, $0.875, and $0.875, in the first, second, third, and fourth quarters, respectively.

(4) Shares were redeemed on February 1, 1987 at $52.50 per share.

There were 90,655 registered holders of common stock at January 11, [illegible].

*Selected Financial Data**

	1987	1986	1985	1984	1983
Total operating revenues	**$1,219,523**	$1,183,865	$1,[illegible]67,364	$1,280,537	$1,278,259
Net income	**$ 289,556**	$ 292,721	$ [illegible]39,999	$ 235,478	$ 207,736
Net income applicable to common stock	**$ 251,859**	$ 256,479	$ 207,240	$ 210,221	$ 184,096
Earnings per common share	**$ 3.75**	$ 3.98	$ 3.48	$ 4.02	$ 3.80
Cash dividends declared per common share	**$ 2.64**	$ 2.64	$ 2.64	$ 2.64	$ 2.52
Total assets**	**$5,922,734**	$5,623,042	$4,894,388	$4,083,670	$3,543,900
Long-term debt**	**$2,279,219**	$2,246,367	$2,012,672	$1,621,201	$1,398,518
Redeemable preferred stock	**$ 160,000**	$ 196,000	$ 86,000	$ 86,000	$ 36,000
Ratio of earnings to fixed charges***	**2.51**	2.57	2.66	3.15	3.56

**Thousands of dollars except earnings per common share, cash dividends declared per common share, and ratio of earnings to fixed charges.*

***Restated for the effect of capitalized nuclear fuel lease.*

****The ratio of earnings to fixed charges represents the number of times that earnings before income taxes and fixed charges cover the fixed charges. Earnings used in the calculation of the above ratios include allowance for funds used during construction and deferred Clinton financing costs and are before the deduction of income taxes and fixed charges that include interest on long-term debt, related amortization of debt discount, premium and expense, other interest, and that portion of rent expense that is estimated to be representative of the interest component.*

Electric Statistics

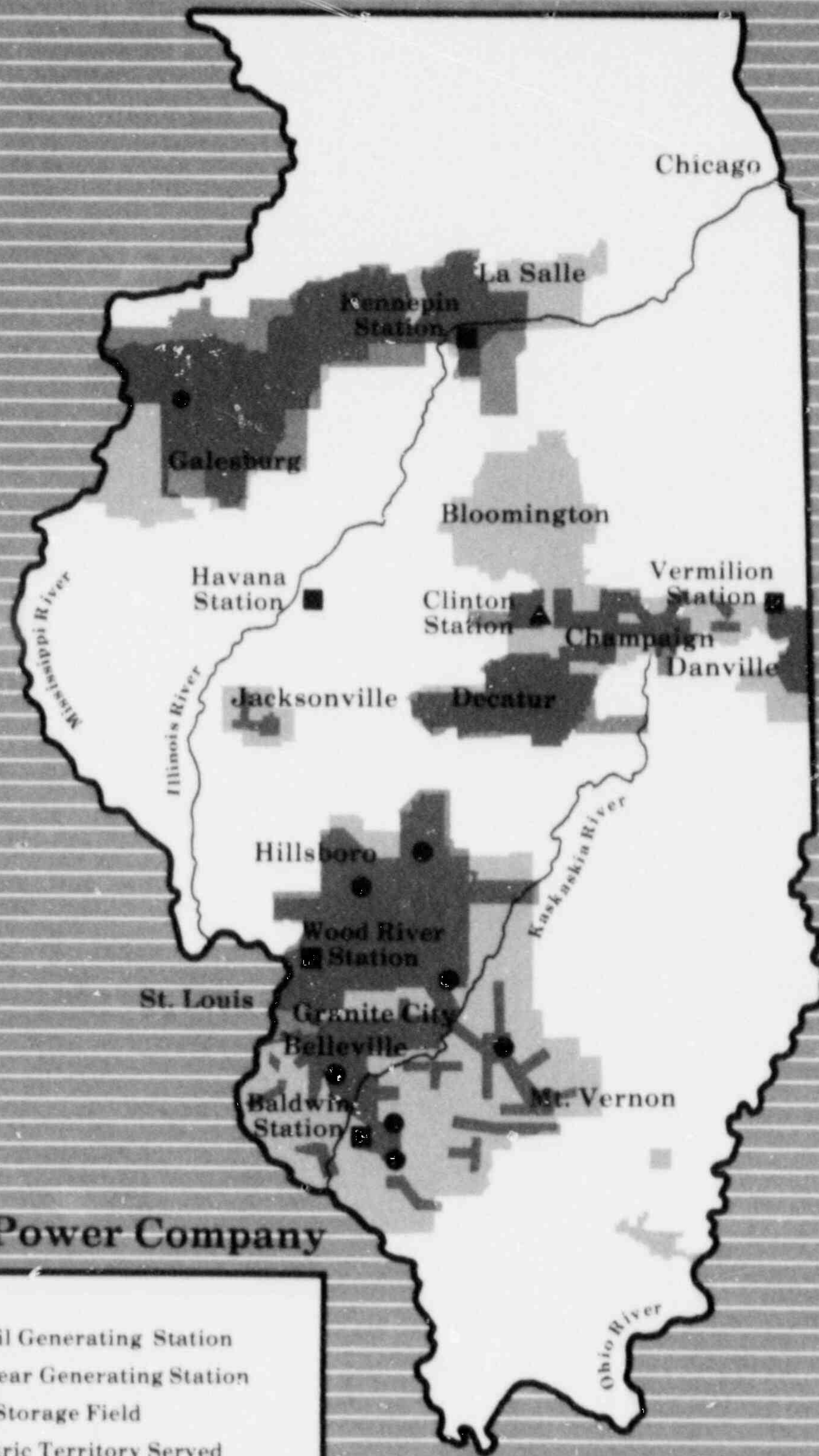
	1987	1986	1985
Revenues (Thousands of Dollars)			
Residential	$ 351,910	$ 293,041	$ 276,210
Commercial	208,527	187,592	179,665
Industrial	325,484	290,321	276,903
Other	19,895	16,601	16,057
Revenues—ultimate consumers	905,816	787,555	748,835
Rural cooperatives, municipal and other utilities	23,541	21,611	21,036
Miscellaneous	(18,513)	4,978	(3,404)
	$ 910,844	$ 814,144	$ 766,467
Customers at End of Year			
Residential	484,809	482,802	479,675
Commercial	56,958	56,734	56,315
Industrial	354	339	340
Other	715	720	717
	542,836	540,595	537,047
Sales in KWH (Thousands)			
Residential	4,240,938	4,197,687	3,926,997
Commercial	2,861,725	2,821,336	2,706,217
Industrial	7,323,167	7,341,567	6,932,903
Other	321,697	320,121	314,455
Sales—ultimate consumers	14,747,527	14,680,711	13,880,572
Rural cooperatives, municipal and other utilities	588,179	554,746	546,328
	15,335,706	15,235,457	14,426,900

Gas Statistics

	1987	1986	1985
Revenues (Thousands of Dollars)			
Residential	$ 191,555	$ 205,814	$ 228,299
Commercial	66,225	77,832	88,683
Industrial	34,506	73,163	68,100
Revenues—ultimate consumers	292,286	356,809	385,082
Interdepartmental revenues	1,272	355	316
Miscellaneous	15,121	12,557	15,499
	$ 308,679	$ 369,721	$ 400,897
Customers at End of Year			
Residential	350,334	349,691	348,994
Commercial	33,271	33,027	32,963
Industrial	486	483	485
	384,091	383,201	382,442
Sales in Therms (Thousands)			
Residential	331,640	356,965	365,082
Commercial	137,232	161,011	165,689
Industrial	95,690	197,815	136,392
Sales—ultimate consumers*	564,562	715,791	667,163
Interdepartmental sales	5,122	1,232	827
	569,684	717,023	667,990

**Excludes therms transported for others amounting to 326,801,000 in 1987, 253,280,000 in 1986, and 297,070,000 in 1985.*

Our Territory and Facilities



Illinois Power Company

Legend

- ■ Fossil Generating Station
- ▲ Nuclear Generating Station
- ● Gas Storage Field
- Electric Territory Served
- Gas Territory Served
- Gas & Electric Territory

Illinois Power Company
500 South 27th Street
Decatur, Illinois 62525

BULK RATE
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Springfield, IL
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