
SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-K

ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the Fiscal Year Ended December 31, 1987

Commission File No. 1-3187H-1

HOUSTON LIGHTING & POWER COMPANY

(Exact name of registrant as specified in its charter)

Texas

(State or other jurisdiction of
incorporation or organization)

74-0694415

(L.R.S. Employer
Identification No.)

611 Walker Avenue

Houston, Texas

(Address of principal executive offices)

77002

(Zip Code)

Registrant's telephone number, including area code: (713) 228-9211

Securities registered pursuant to Section 12(b) of the Act:

Title of Each Class

Name of each exchange on
which registered

None

Securities registered pursuant to Section 12(g) of the Act:

Title of Each Class

Preferred Stock, cumulative, no par:
\$4 Series; \$6.72 Series; \$7.52 Series; \$9.52 Series; \$9.08 Series; \$8.12 Series; \$9.04 Series; Adjustable Rate,
Series A; Adjustable Rate, Series B; and \$8.50 Series.

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes No

As of March 1, 1988, 106,660,778 shares of the registrant's Common Stock, without par value, were issued and outstanding and privately held, beneficially and of record, by Houston Industries Incorporated.

Portions of the definitive proxy statement relating to the 1988 Annual Meeting of Shareholders of Houston Industries Incorporated, which will be filed within 120 days of December 31, 1987, are incorporated by reference in Item 10, Item 11, Item 12 and Item 13 of Part III of this form.

HOUSTON LIGHTING & POWER COMPANY
Form 10-K for the Year Ended December 31, 1987
TABLE OF CONTENTS

	<u>Page No.</u>
Part I	
Item 1. Business	
The Company.....	3
Certain Factors Affecting Electric Utilities and HL&P.....	3
Service Area.....	4
Peak Loads and Capability.....	4
Construction Program.....	5
Competition and Least-Cost Planning.....	12
Purchased Power and Cogeneration.....	13
Fuel.....	14
Regulatory Matters.....	16
Nuclear Insurance.....	20
Labor Matters.....	21
Operating Statistics.....	22
Officers.....	23
Item 2. Properties.....	25
Item 3. Legal Proceedings.....	25
Item 4. Submission of Matters to a Vote of Security Holders.....	25
Part II	
Item 5. Market for the Registrant's Common Stock and Related Stockholder Matters.....	26
Item 6. Selected Financial Data.....	26
Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operations.....	27
Item 8. Financial Statements.....	31
Item 9. Changes in and Disagreements with Accountants on Accounting and Financial Disclosure.....	64
Part III	
Item 10. Directors and Executive Officers of the Registrant.....	64
Item 11. Executive Compensation.....	64
Item 12. Security Ownership of Certain Beneficial Owners and Management.....	66
Item 13. Certain Relationships and Related Transactions.....	66
Part IV	
Item 14. Exhibits, Financial Statement Schedules, and Reports on Form 8-K.....	67

PART I

Item 1. Business

THE COMPANY

Houston Lighting & Power Company (HL&P) is engaged in the generation, transmission, distribution and sale of electric energy, serving an area of the Texas Gulf Coast Region, estimated at 5,000 square miles, which includes Houston (the largest city in Texas) and 156 smaller cities, villages and communities. The address of HL&P's principal executive offices is 611 Walker Avenue, Houston, Texas 77002 (telephone number 713/228-9211).

HL&P is a subsidiary of Houston Industries Incorporated (Houston Industries) which owns all of HL&P's outstanding common stock. Houston Industries is a holding company as defined in the Public Utility Holding Company Act of 1935 (1935 Act), but is exempt from regulation as a "registered" holding company under the 1935 Act except with respect to the acquisition of certain voting securities of other public utility companies and holding companies. Houston Industries also owns all of the outstanding common stock of six other subsidiaries: Primary Fuels, Inc., Utility Fuels, Inc. (Utility Fuels), Innovative Controls, Inc., KBLCOM Incorporated, Houston Industries Finance, Inc., and Development Ventures, Inc.

Certain Factors Affecting Electric Utilities and HL&P

HL&P, in common with electric utilities in general, has experienced problems in a number of areas, including difficulty and delays in securing rate increases in sufficient amounts to finance its construction program and provide an adequate return on common equity; uncertainties and delays respecting the construction and licensing of nuclear-fueled generating units; substantial increases in construction and operating costs; uncertainties regarding adequate rate treatment for costs incurred in constructing plants; negative effects on earnings due to the commencement, at commercial operation of new generating plants, of substantial charges for depreciation and other operating expenses and the cessation of the accrual of an allowance for funds used during construction (AFUDC) without offsetting rate increases; increased expenditures due to pollution control and environmental considerations; high costs in raising large amounts of capital in competition with other major users of capital; competition from unregulated suppliers of energy; controversies over the safety and uses of nuclear power; and an uncertain rate of change in energy sales due to economic conditions, self-generation and energy conservation measures undertaken by customers.

In addition, HL&P's operations have been adversely affected by depressed economic conditions in HL&P's service area. Furthermore, the problems referred to in the preceding paragraph have had and are expected to continue to have an impact on HL&P's operations. Certain of these problems could have an increased impact during 1988 in connection with the commercial operation of Unit No. 1 of the South Texas Project Electric Generating

Station (South Texas project), HL&P's request for certain interim accounting treatment with respect to Unit No. 2 of the Limestone Electric Generating Station (Limestone) and Unit No. 1 of the South Texas project and the general rate proceeding which is expected to be filed in the second quarter of 1988. See "Peak Loads and Capability", "Construction Program", "Competition and Least-Cost Planning", "Purchased Power and Cogeneration", "Regulatory Matters" (including the discussion in such section of a contemplated general rate proceeding), Item 7. "Management's Discussion and Analysis of Financial Condition and Results of Operations" and Note 9 to the Financial Statements included under Item 8 of this Report.

Service Area

HL&P's service area includes major producers of oil, gas, sulphur, refined products, chemicals, petrochemicals, oil tools and related manufacturing, processing and servicing activities. Electronics, paper, building materials, cotton, rice, cattle, salt, magnesium and other minerals are also important products of the service area. The service area is characterized by a favorable year-round climate and ready access to air, land and water transportation.

For a number of years prior to 1983, expansion of industrial activity in HL&P's service area was accompanied by a corresponding increase in the construction of industrial structures and complexes and building activity in many other fields, including multi-block office building complexes, apartment buildings, single and multi-family dwellings, hotels and motels, hospitals and other commercial structures. As a result of general recessionary conditions in the Houston area which began in 1983 and the continued weakness in the oil and gas industry and related servicing and supply industries which persisted through 1987, general economic and population growth in the service area has slowed. Since 1983, industrial and commercial construction, occupancy levels for office space and apartments, and construction of single-family homes have been at reduced levels compared to previous years. HL&P's service area has also been adversely affected by the rapid and substantial declines in world oil prices. HL&P's sales, particularly to industrial customers, have been further adversely affected by energy conservation measures, self-generation and the production of electric power from cogeneration facilities.

HL&P operates under a certificate of convenience and necessity granted by the Public Utility Commission of Texas (Utility Commission) which covers its present service area and facilities.

Peak Loads and Capability

The following table sets forth for the years indicated information with respect to the installed net capability and total net capability of HL&P at the time of peak demand, the net maximum hourly demand on its system (excluding demand which is interruptible), and the reserve margin at the time of its system net maximum hourly demand:

Year	Installed Net Capability (Megawatts)	Pur- chased Power (Mega- watts)(1)	Total Net Capability (Megawatts)	Net Maximum Hourly Demand			% Change From Prior Year	Reserve Margin (%)(1)
				Date	Megawatts	Year		
1983	12,196	1,200	13,396	August 31	10,676	0.8	25.5	
1984	12,275	925	13,200	August 23	10,851	1.6	21.6	
1985	12,318	1,595	13,913	August 19	10,618	(2.1)	31.0	
1986	11,863	1,395	13,258	July 30	10,556	(0.6)	25.6	
1987	12,460(2)	1,295	13,755	August 19	10,302(3)	(2.4)	33.5	

- (1) Reflects firm purchased power capability available through interconnections with other utilities and from cogenerators.
- (2) Capability shown is as of time of system peak and does not reflect (i) capacity changes which increased net capability by 175 megawatts but which occurred after the system peak and (ii) the uprating of a plant which had been derated by 220 megawatts during the summer.
- (3) Does not include interruptible load at time of peak of 1,016 megawatts.

For planning purposes, HL&P expects growth in peak demand for electricity to reflect the pattern of economic recovery for the Houston area. The compound annual growth rate in peak demand over the ten-year period 1988 through 1998 is estimated to be 1.1%. The current demand forecast is derived, in part, from a continuing survey of industrial customers which reflects expectations for power consumption and from assessments of the effect of additional residential and commercial customers on peak demands. Assuming facilities under construction are placed in service as presently scheduled, HL&P expects to maintain a minimum reserve margin of at least 20% in excess of its current estimate of peak load requirements through 1999, with reserve margins during the period 1988 through 1994 now projected to be in a range of 30% to 40%. See "Competition and Least-Cost Planning" and "Purchased Power and Cogeneration".

Construction Program

HL&P carries on a continuous construction program. Such construction program and the estimated construction costs set forth below are subject to periodic review and are revised from time to time in light of changes in load forecasts, fuel diversification objectives, the need to retire older plants, changing regulatory and environmental standards and other factors. With the completion of Limestone Unit No. 2 in December 1986 and the extension of the scheduled in-service dates for the Malakoff Electric Generating Station (Malakoff project) discussed below, the only active generating project in HL&P's construction program is the South Texas project. The construction program discussed below is currently estimated to cost approximately \$1.257 billion during the three-year period 1988-1990 with approximately \$477 million to be spent in 1988, \$431 million to be spent in 1989 and \$349 million to be spent in 1990, excluding nuclear fuel and AFUDC. In 1987, total construction expenditures were approximately \$643 million. These amounts do not include expenditures on projects for which HL&P was reimbursed or expects to be reimbursed by customers or

cogenerators. These amounts also do not reflect the possible acquisition by HL&P of an additional 16% interest in the South Texas project presently owned by the City of Austin (Austin) which would increase such three year construction program by \$150 million, \$62 million of which is related to the reimbursement of costs incurred by Austin prior to 1988. See Note 9 to the Financial Statements included under Item 8 of this Report.

HL&P's construction program for 1988-1990 consists of the following principal estimated expenditures:

	Amount (millions)	%
Fossil-fueled generating facilities.....	\$ 326	26
Nuclear-fueled generating facilities....	167	13
Transmission facilities.....	183	15
Distribution facilities.....	379	30
General plant facilities.....	202	16
Total.....	<u>\$1,257</u>	<u>100%</u>
	=====	=====

At December 31, 1987, HL&P owned and operated generating facilities with generating capability of 12,855 megawatts. The 1988-1990 construction program includes expenditures in connection with the following major generating projects aggregating 2,060 megawatts of estimated capability. All dollar amounts are exclusive of AFUDC and nuclear fuel payments.

Plant and Location (County)	Estimated Unit Capability (KW)	Fuel	Scheduled In-Service Date(a)	Millions of Dollars (Excluding AFUDC)		
				Through December 31, 1987	Estimated Cost	Estimated Cost Per KW
South Texas No. 1 (Matagorda)(b)	385,000	Nuclear	1988			
South Texas No. 2 (Matagorda)(b)	385,000	Nuclear	1989	\$1,546(c)	\$1,686(c)	\$2,190(c)
Malakoff No. 1 (Henderson)	645,000	Lignite	1997(d)			
Malakoff No. 2 (Henderson)	645,000	Lignite	1999(d)	137(d)	2,160(d)	1,674(d)

- (a) The scheduled in-service date indicates the year during which the unit is expected to be available to meet peak demand.
- (b) The figures shown in the table as to capability, expenditures and costs for the South Texas units represent HL&P's 30.8% share of a jointly owned 2.5 million kilowatt project for which HL&P acts as project manager. The other owners are Central Power and Light Company, Austin and the City of San Antonio (San Antonio). See "South Texas Nuclear Project", "Regulatory Matters" and Note 9

to the Financial Statements included under Item 8 of this Report. In September 1987, in an effort to settle litigation relating to the South Texas project, HL&P reached an agreement in principle (Agreement in Principle) with Austin to acquire Austin's 16% share of the South Texas project subject to the execution of definitive documentation and the satisfaction of other conditions. For a discussion of the Agreement in Principle and the related litigation, see Note 9 to the Financial Statements included under Item 8 of this Report.

- (c) The amounts shown for total expenditures and estimated completed cost represent HL&P's existing 30.8% interest in the South Texas project and reflect approximately \$65 million, or \$85 per KW, expected to be capitalized by HL&P for state and local taxes. The total expenditures through December 31, 1987 and the estimated completed cost reflect a credit of \$154.1 million (net of expenses) as a result of the settlement of certain litigation with the former architect/engineer-constructor of the South Texas project (Former Architect-Engineer) and its corporate parent. The estimated completed cost represents an increase of \$92 million with respect to HL&P's existing 30.8% interest over the previous completed cost estimate and is derived from a completion assessment adopted by the management committee for the South Texas project in December 1987 which assumed a commercial operation date for Unit No. 1 of March 1, 1988. Although no definitive estimate of additional costs has been approved, HL&P anticipates that cost increases in the range of \$100 to 150 million (of which HL&P's portion would be \$31 to \$46 million based on its 30.8% interest) may result from the delays in achieving initial criticality and the resulting delay in the anticipated date of commercial operation of Unit No. 1. See Note 9 to the Financial Statements included under Item 8 of this Report.

Based on the cost estimate approved by the management committee in December 1987, HL&P's share (based on its 30.8% interest) of the estimated completed cost for both units at the South Texas project (including AFUDC) is \$2.449 billion or \$3,181 per KW. Assuming consummation of the Agreement in Principle with Austin, which would provide HL&P with an aggregate 46.8% interest in the South Texas project, the estimated completed cost to HL&P excluding AFUDC would be approximately \$2.207 billion or \$1,886 per KW, and the estimated completed cost to HL&P including AFUDC would be \$2.976 billion or \$2,543 per KW.

- (d) In January 1987, HL&P announced the extension for five years of the scheduled in-service dates for Unit No. 1 and Unit No. 2 of the Malakoff project. See "Modified Schedule for Malakoff Project". HL&P's total investment in the Malakoff project through December 31, 1987 was \$154 million including AFUDC and land. In addition, Utility Fuels, HL&P's fuel supply affiliate, had invested \$121 million in lignite reserves and mining equipment related to the project through December 31, 1987.

Through December 31, 1987, HL&P spent approximately \$112 million excluding AFUDC for uranium concentrate and nuclear fuel processing services for its share of the fuel for the South Texas project. It expects to spend an additional \$50 million for similar purposes in connection with its 30.8% share of the project during the 1988-1990 period. These amounts do not reflect the possible acquisition by HL&P of an additional 16% interest in the South Texas project which would increase such nuclear fuel expenditures by \$56 million, \$30 million of which is related to the purchase of Austin's share of nuclear fuel. Additional nuclear fuel expenditures, which could include substantial sums for long-term storage of spent nuclear fuel, will be required after 1990. See "Fuel - Nuclear Fuel Supply".

The estimated construction expenditures set forth above do not include any amounts for the cost of decommissioning the South Texas project at the end of its estimated 40-year useful life. Based on a decommissioning study prepared in early 1987, the estimated cost of decommissioning HL&P's 30.8% ownership share of the two units at the South Texas project is \$77 million (\$117 million if HL&P's ownership interest increases to 46.8%) in 1986 dollars. However, actual costs could vary substantially from the estimates and will depend upon a number of factors including, without limitation, regulatory requirements and the method ultimately used to decommission the project. Although HL&P intends to seek to recover such costs through electric rates over the South Texas project's useful life, there can be no assurance that all of such costs will be recoverable through rates.

Actual construction expenditures will vary from the above estimates as a result of numerous factors, including changes in the rate of inflation, changes in equipment delivery schedules, construction delays and deferrals, availability of fuel, environmental protection requirements, changing U. S. Nuclear Regulatory Commission (NRC) requirements and licensing delays, changes in the construction program, the availability of adequate and timely rate relief, the ability to secure external financing, legislative changes and changes in anticipated customer demand and business conditions. The scheduled in-service dates for generating plants in the construction program may also vary as a result of similar factors. Since 1983, the nuclear industry in general has experienced significant setbacks as a result of the cancellation or deferral of several nuclear generating units under construction. In addition, the estimated completed cost and the scheduled in-service date for the South Texas project were revised during 1987 as a result of certain of the factors discussed above, and there can be no assurance that factors beyond the control of the participants will not adversely affect the South Texas project's construction schedule, schedule for commercial operation or budget. See "South Texas Nuclear Project" below, "Regulatory Matters" and Note 9 to the Financial Statements included under Item 8 of this Report.

Expenditures for environmental protection facilities for the five years ended December 31, 1987 aggregated \$939 million (excluding AFUDC), including expenditures of \$100 million in 1987. Environmental protection expenditures for 1988-1990 are estimated to be \$91 million (excluding AFUDC), of which \$48 million is expected to be expended during 1988, \$38 million during 1989 and \$5 million during 1990.

Total gross additions to the plant of HL&P during the five years ended December 31, 1987 amounted to approximately \$4.7 billion, and during the same period retirements amounted to approximately \$257 million. Gross additions during the same five-year period amounted to approximately 48% of total utility plant at December 31, 1987.

South Texas Nuclear Project. The estimated expenditures and scheduled in-service dates for the South Texas generating units presented above are based on the cost estimate provided in the September 1987 completion assessment for the entire project which was adopted in December 1987 by the project's management committee. The estimate was based on a projected commercial operation date for Unit No. 1 of March 1, 1988. However, commercial operation is not expected to occur before the summer of 1988. Although no definitive estimate of additional costs has been approved, HL&P anticipates that cost increases in the range of \$100 to \$150 million (of which HL&P's portion would be \$31 to \$46 million based on its 30.8% interest) may result from the delays in achieving initial criticality and the resulting delay in the anticipated date of commercial operation of Unit No. 1. It is anticipated that Unit No. 1 and Unit No. 2 will be available to meet peak demand in 1988 and 1989, respectively. HL&P's portion (based on its current 30.8% interest in the South Texas project) of the estimated total expenditures (excluding AFUDC and net of the proceeds received pursuant to a settlement with the Former Architect-Engineer) for the project is \$1.686 billion. Actual expenditures through December 1987 totaled \$1.546 billion (excluding AFUDC and net of such proceeds). For a discussion of the current budget and schedule for the South Texas project, the Agreement in Principle pursuant to which HL&P may acquire Austin's 16% interest in the South Texas project and the related litigation with Austin, see Note 9 to the Financial Statements included under Item 8 of this Report and Item 7, "Management's Discussion and Analysis of Financial Condition and Results of Operations".

As a result of, among other factors, the need for significant rate increases in connection with completed nuclear generating units, delays and increases in costs of building nuclear generating units, reduced energy demands and reduced need for additional electrical generating capacity, a number of other utilities have experienced difficulties in recovering through electric rates the costs expended on nuclear power plants. In some cases, action on rate increase requests has been delayed for considerable periods of time, while the utilities' earnings have deteriorated due to the cessation of accrual of AFUDC and the commencement of operating expenses and depreciation charges at commercial operation without offsetting rate relief. For a discussion of the possible impact on HL&P's earnings once Unit No. 1 of the South Texas project is placed in commercial operation and the steps HL&P has undertaken to seek to mitigate this effect, see "Regulatory Matters - Requests for Interim Accounting Treatment" and "- Contemplated General Rate Proceeding" and Item 7, "Management's Discussion and Analysis of Financial Condition and Results of Operations". In other cases, regulatory authorities have disallowed certain expenditures based upon a finding that such expenditures were imprudent. Also, a number of utilities have been required to "phase-in" the costs of nuclear generating units, while financing the costs currently and deferring recovery from customers to a subsequent date. For a discussion of certain changes in accounting standards relating to abandonment and disallowance of plant costs and

phase-in plans, see Item 7. "Management's Discussion and Analysis of Financial Condition and Results of Operations - Changes in Accounting Standards".

During 1987, there were a number of significant developments in the litigation and in various regulatory proceedings pertaining to the South Texas project. For information respecting such matters, including the pending litigation and the status of negotiations with Austin; the pending litigation with San Antonio, Central Power and Light Company and its parent corporation, Central and Southwest Corporation; the scheduled prudence review of the South Texas project by the Utility Commission; and the budget and schedule for the South Texas project, see Note 9 to the Financial Statements included under Item 8 of this Report. For information respecting a contemplated general rate proceeding and licensing proceedings before the NRC, see "Regulatory Matters - Contemplated General Rate Proceeding" and "- Nuclear Licensing".

Limestone Unit No. 2 Placed In Service. In December 1986, the second of two 720 megawatt, lignite-fired generating units at Limestone was placed into commercial operation. In January 1987, HL&P requested that the Utility Commission order an accounting treatment which would have the effect of minimizing the impact on earnings of Unit No. 2 being placed in service without being fully reflected in the rates charged customers. A similar accounting treatment was requested for Limestone Unit No. 1 but was denied by the Utility Commission. For information concerning HL&P's requests for interim accounting treatment, see "Regulatory Matters - Requests for Interim Accounting Treatment". Electric rates do not currently reflect approximately \$174 million of the project cost or any provision for operating expenses, non-reconcilable lignite mining and handling costs, taxes or depreciation related to Unit No. 2, estimated to be \$57 million annually. Operating results of HL&P have been adversely affected and will continue to be adversely affected until rate relief or other regulatory action is obtained with respect to Limestone Unit No. 2.

Modified Schedule for Malakoff Project. In January 1987, HL&P announced that the schedule for the construction of two 645 megawatt lignite units at the proposed Malakoff project in Henderson County, Texas had been modified. The scheduled in-service dates, which are the dates the units are expected to be available to meet peak demand, are now 1997 for Unit No. 1 and 1999 for Unit No. 2. The modified schedule resulted from lowered projections of future demand for electricity in the Houston area. As a result of the modified schedule, all developmental work on the two lignite units has stopped, but HL&P will resume activity, when necessary, to meet load growth requirements. HL&P's total investment in the Malakoff project through December 31, 1987, is \$154 million including AFUDC and land. This amount is included in Plant Held for Future Use and the accrual of AFUDC has been suspended until such time as construction resumes. HL&P has agreed to indemnify Utility Fuels for all necessary and actual costs incurred due to the modification of the schedule. Utility Fuels has invested \$121 million in lignite reserves and handling systems relating to the Malakoff project through December 31, 1987 and suspended capitalization of interest effective December 31, 1986. For the 1988-1990 period, Utility Fuels anticipates \$22 million of expenditures relating to the Malakoff project which are primarily associated with keeping lignite leases and other related agreements in effect.

Financing of HL&P's Construction Program. HL&P proposes to finance its construction program through the use of internally generated funds and the proceeds received from the issuance of securities including, on an interim basis, short-term debt securities. The interim financing requirements of HL&P are met through short-term bank loans under a \$650 million bank line of credit and the issuance of commercial paper. See Note 4 to the Financial Statements included under Item 8 of this Report. HL&P's ability to finance its construction program will be substantially dependent upon the availability of adequate and timely rate relief. See "Regulatory Matters - Rates and Services" and "- Contemplated General Rate Proceeding". It is presently estimated that during 1988, 10% to 20% of HL&P's construction program can be financed through internally generated funds from operations. Internally generated funds for subsequent years will be primarily dependent on the regulatory treatment of HL&P's investment in the South Texas project.

HL&P anticipates that it may utilize the sale of first mortgage bonds and/or preferred stock to fund a portion of its construction program during 1988. In this regard, HL&P has registered with the Securities and Exchange Commission (SEC) \$225 million principal amount of first mortgage bonds which it may sell during 1988, subject to favorable market conditions. The types, amounts and time of issuance of additional securities have not been determined. HL&P's Mortgage and Deed of Trust (Mortgage) and corporate charter specify earnings coverages and other conditions which must be complied with prior to the issuance by HL&P of any first mortgage bonds or additional shares of preferred stock. With respect to liquidity and financing plans of HL&P, see Item 7. "Management's Discussion and Analysis of Financial Condition and Results of Operations".

In March 1987, HL&P issued \$391 million aggregate principal amount of a new 9% series of first mortgage bonds due 2017 in exchange for an equal principal amount of outstanding high coupon first mortgage bonds. Under the terms of the exchange offers, HL&P also paid a cash premium which varied depending on the series of bonds exchanged. In March 1987, HL&P also deposited \$146 million with the bond trustee for the purpose of redeeming \$140 million principal amount of certain series of outstanding first mortgage bonds and paying accrued interest to the redemption date. These bonds were called for redemption and funds placed in trust under the replacement fund provisions of HL&P's Mortgage. The bonds were retired by the trustee in May 1987.

In June 1987, HL&P sold 1,000,000 shares of \$8.50 cumulative preferred stock which are subject to mandatory redemption. Such stock is entitled to a fixed liquidation price of \$100 per share, plus a fixed liquidation premium in the event of a voluntary liquidation before June 1, 1994, in each case together with accrued dividends. The mandatory redemption provision requires HL&P to redeem 200,000 shares annually beginning June 1, 1993. HL&P received net proceeds of \$99 million from the sale.

During 1987, HL&P also received \$128 million of the proceeds from pollution control revenue bonds issued in prior years. Approximately \$87 million (including interest earned on funds held in trust) was held in trust at December 31, 1987. Substantially all of the funds held in trust are expected to be drawn down by HL&P in 1988 and 1989 to fund qualifying construction expenditures.

In January 1988, HL&P sold \$400 million aggregate principal amount of first mortgage bonds and received net proceeds of approximately \$398 million from the sale of the bonds. These bonds will bear interest at a rate of 9-3/8% per annum and will mature in approximately equal principal amounts in each of the years 1991, 1992 and 1993.

In January 1988, HL&P deposited \$52 million with the bond trustee for purposes of redeeming all of the outstanding bonds of the 13-7/8% Series at 100% of the principal amount and paying accrued interest. The bonds of this series were called pursuant to the general redemption provisions of the Mortgage.

Competition and Least-Cost Planning

HL&P is subject to competition from a number of unregulated suppliers of energy, particularly cogenerated energy. In recent years, rising costs of electricity provided by regulated utilities have caused certain industrial and commercial customers to seek other ways to meet their energy needs, including the construction of cogeneration systems which provide electric energy both for their own needs and for sales to HL&P and other electric utilities. A relatively large number of cogeneration facilities have been built in HL&P's service area because of the relatively high concentration of process industries.

The availability of unregulated alternative energy sources increases the risk that major customers will reduce their purchases of electricity from HL&P. Should reduced purchases occur, increased electric prices to the remaining customers could occur. As costs for electricity increase, additional customers may find it economically advantageous to turn to alternative energy supplies. The existence of alternative unregulated producers of electricity has contributed to regulatory uncertainty concerning the recovery of power plant construction costs and a continued focus on "least-cost" planning for alternatives to large capital intensive generating stations.

HL&P is addressing this increased competition by, among other things, implementing new programs to reduce costs, particularly construction and fuel costs; developing a variety of rates and services and other marketing strategies to increase sales and encourage industrial expansion in its service area; and fully evaluating all low-risk, least-cost options before initiating construction of additional large central station generating facilities. Steps that have already been taken in these areas include completion of the new Limestone units ahead of schedule and under budget; development of an integrated fuel management system to provide increased fuel purchasing flexibility and assure utilization of the most economical available fuels during peak periods; modification of existing generating units to provide improved reliability, reduced maintenance costs and greater flexibility in responding to changing demand conditions; and deferral until the late 1990's of the completion of the Malakoff project.

In January 1988, HL&P filed an application with the Utility Commission and various cities in HL&P's service area that have maintained original jurisdiction requesting approval of an experimental economic redevelopment rate which would provide discounts to qualified customers. The rate has

been approved by the Utility Commission and by all of the cities. The purpose of the proposed rate is to provide an economic incentive to encourage development of and relocation to HL&P's service area and to create new jobs. The rate will be offered to certain customers in HL&P's service area including basic manufacturing industries, regional warehousing and distribution facilities, scientific and industrial research and development facilities, corporations relocating to HL&P's service area, governmental projects subject to competitive siting and facilities receiving county tax abatements.

Purchased Power and Cogeneration

The Public Utility Regulatory Policy Act of 1978 requires utilities to purchase all electricity offered to them by qualifying cogeneration facilities. HL&P is currently purchasing cogenerated energy from thirteen industrial cogeneration facilities and various small power producers which have approximately 3,200 megawatts of total generating capability. Three long-term capacity contracts cover 820 megawatts of this total amount. A fourth capacity contract for 136 megawatts has been temporarily suspended through mid 1990. During 1987, a maximum of approximately 1,800 megawatts of cogenerated power produced in HL&P's service area was wheeled or transmitted by HL&P to other utilities in Texas.

HL&P's current load forecast indicates that additional firm cogeneration capacity will not be needed during the next ten years. Certain rules of the Utility Commission specify that a utility is not required to contract for more capacity from cogenerators than is necessary to meet its approved demand forecast. Therefore, HL&P does not intend to pursue any additional long-term capacity contracts for cogenerated electric energy in the near future.

Cogenerators are not permitted under Texas law to make electric sales to parties other than electric utilities, except in the case of sales to the thermal purchaser from the cogeneration facility. Regulated electric utilities are required to provide transmission service for power under a Utility Commission rule that permits the utilities to recover their costs plus a return on investments.

Attempts have been made to secure authorization for cogenerators to sell electricity to traditional customers of regulated electric utilities, and some cogenerators have sought greater access to electric transmission facilities. HL&P believes such retail sales or such access to transmission facilities would work to the detriment of the majority of the utility's remaining customers by forcing them to bear increased costs and by reducing the overall reliability of electric service. In addition, to the extent cogenerators and other unregulated electric entities are allowed to make sales to traditional electric utility customers or to gain access to the electric transmission and distribution systems for their own purposes, HL&P's prospects may be adversely affected. HL&P intends to continue its opposition to such efforts.

HL&P's purchased power contracts with San Antonio and Austin expired in December 1987 and HL&P currently has no other long-term contracts in effect with other utilities.

Fuel

Approximately 46% of HL&P's energy requirements during 1987 was met with natural gas while 40% was met with coal and lignite. The remaining 14% was met principally with purchased power and cogenerated power. HL&P currently expects its future energy mix to be in the following proportions, with separate presentations based upon HL&P's existing 30.8% interest in the South Texas project and based upon a possible 46.8% interest in the South Texas project if the agreement in principle with Austin is consummated:

	Estimated Energy Mix (30.8% interest in South Texas project)				Estimated Energy Mix (46.8% interest in South Texas project)			
	1988	1989	1990	1996	1988	1989	1990	1996
	Gas.....	43%	35%	30%	38%	43%	35%	31%
Coal and Lignite...	39	41	41	40	38	38	37	36
Nuclear	3	7	8	8	4	10	11	12
Cogeneration.....	15	17	21	14	15	17	21	14
Total.....	100%	100%	100%	100%	100%	100%	100%	100%
	***	***	***	***	***	***	***	***

HL&P's actual energy mix in future years could vary substantially from the percentages shown in the table. Such percentages are based upon numerous estimates and assumptions relating to, among other things, environmental protection requirements, load growth, load management, cogeneration, the cost and availability of fuels and purchased electrical energy, and the actual in-service dates of HL&P's planned generating facilities.

Natural Gas Supply. HL&P purchased its natural gas fuel supplies from a large number of suppliers during 1987; however, 77% of HL&P's gas requirements were still purchased from its traditional suppliers and their affiliates. Two of these firms, Exxon Company, U.S.A. (Exxon) and United Texas Transmission Company (UTT), sell gas to HL&P under long-term contracts. The third, Houston Pipe Line Company (HPL) and its affiliates, provided 27% of HL&P's gas requirements even though no long-term contract exists between HL&P and HPL. The contract with Exxon will expire in 1996 or after delivery of a specified quantity of natural gas, whichever comes first. The UTT contract will expire on January 1, 1990, unless terminated earlier by operation of certain "economic out" provisions in the agreement or unless extended by mutual agreement of the parties.

As a result of conditions in natural gas markets, aggressive negotiations, and HL&P's strategic position in the marketplace, HL&P maintained its cost of natural gas in 1987 at approximately the same level as in 1986 despite an increase in the price of natural gas late in 1987.

Several strategic fuel projects were completed in 1987. One of these projects is the North Dayton Gas Storage Facility (owned and operated by an unaffiliated third party) which provides gas storage services exclusively to

HL&P. The purpose of this facility is to allow HL&P to reduce variations in hour to hour purchases of gas, thereby avoiding extra charges by gas suppliers and transporters. Storage capability also enables HL&P to take advantage of favorable market conditions which may permit the purchase of lower-priced gas and provides a source of gas supplies when deliveries by pipelines may be curtailed.

Another strategic project was the modification of certain segments of HL&P's existing fuel pipeline to provide dual fuel capability. This modification of the pipeline allows distribution of either oil or gas among four of HL&P's major gas/oil fueled plants, thus giving HL&P greater access to gas suppliers and/or transporters and increased gas supply flexibility without sacrificing the ability to switch fuels as economics dictate.

Coal and Lignite Supply. Coal supply services for HL&P's four coal-fired units at the W. A. Parish plant (aggregating 2,335 megawatts) are being provided by Utility Fuels. Utility Fuels purchases low-sulfur Powder River Basin coal under two long-term coal supply contracts. Substantially all of the coal requirements of the four coal-fired units at the W. A. Parish plant are expected to be met under such contracts. For information concerning a prudence review by the Utility Commission of the two contracts, the resulting litigation filed by HL&P against the two coal suppliers and the settlement of this litigation, see Note 7 to the Financial Statements included under Item 8 of this Report.

The lignite supply services for HL&P's Limestone units are also being provided by Utility Fuels. Utility Fuels has under lease or contract recoverable lignite reserves which are expected to be sufficient to meet the total projected lignite fuel requirements of 228 million tons for the remaining life of the Limestone units. It is presently contemplated that Utility Fuels will also provide the lignite supply services for HL&P's Malakoff project. See "Construction Program". Utility Fuels has purchased or leased various properties in the area of the proposed plant site containing recoverable lignite reserves which are expected to be sufficient to meet the total lignite fuel requirements of the two proposed generating units.

Nuclear Fuel Supply. The supply of fuel for nuclear generating facilities involves the acquisition of uranium concentrates, conversion to uranium hexafluoride, enrichment of the uranium hexafluoride, and fabrication of nuclear fuel assemblies. Contracts have been entered into with various suppliers to provide the two South Texas project units with uranium concentrates to allow the units to operate through 1997, conversion services through 1994, enrichment services for a period of 30 years and fuel fabrication services for the initial cores and 16 years of reloads.

A portion of the uranium inventory for the South Texas project was produced outside the United States, and it is anticipated that additional quantities of such "foreign source" uranium may be acquired from time to time in the future. Currently, such foreign source uranium is being processed, along with domestically produced uranium, by the U.S. Department of Energy (DOE) under contracts which provide for the enrichment of uranium, a process necessary to produce fuel for nuclear reactors. Litigation is currently pending under which the DOE may be restricted from continuing to

process such foreign source uranium. That litigation was initiated by certain uranium producers which contend that the DOE should not offer enrichment services for foreign source uranium "to the extent necessary to assure the maintenance of a viable domestic uranium industry." The position of the uranium producers essentially has been upheld by a federal district court and the U.S. Court of Appeals for the Tenth Circuit. The United States Supreme Court has agreed to hear an appeal from those lower court decisions. The pending litigation is not currently having an adverse effect on HL&P and the South Texas project, but if the lower courts' decisions ultimately are upheld, the cost of acquiring additional uranium over the life of the South Texas project may be increased.

Under a contract with the U. S. Department of Energy, the Department of Energy will take possession of all spent fuel generated by the plant. The Department of Energy plans to place the spent fuel in a permanent underground storage facility. The contract currently requires that a spent fuel disposal fee of one mill (\$.001) per net kilowatt-hour generated be paid. The fee may be adjusted in order to ensure full cost recovery. The South Texas project is currently designed to have on-site storage facilities with the capacity to store at least 30 years of spent fuel discharges from each unit.

Oil Supply. Fuel oil is maintained in inventory by HL&P to provide for fuel needs in emergency situations if and when sufficient supplies of natural gas are not available. In addition, HL&P uses fuel oil from time to time when oil is a more economical fuel than incremental gas supplies. HL&P has storage facilities for approximately 6,700,000 barrels of oil located at those generating plants capable of burning oil. HL&P's oil inventory will be adjusted periodically, as necessary, to accommodate changes in the availability of primary fuel supplies and to take into consideration the back-up gas fuel supply capability provided by the North Dayton Gas Storage Facility. See "Natural Gas Supply".

Recovery of Fuel Costs. For information relating to the cost of fuel over the last three years, see "Operating Statistics" and Item 8. "Financial Statements". The Utility Commission rules provide for the recovery of fuel costs through an energy component of base electric rates. The energy component is established during either a utility's general rate proceeding or an interim fuel proceeding and is to be generally effective for a minimum of twelve months, unless a substantial change in a utility's cost of fuel occurs. In that event, a utility may be authorized to appropriately revise the energy component of its base rates. The rule also provides for a reconciliation of fuel revenues, with any over- or under-recovery of fuel costs to be considered in establishing future fuel cost factors.

Regulatory Matters

Rates and Services. Pursuant to the Texas Public Utility Regulatory Act of 1975 (PURPA), the Utility Commission has original jurisdiction over electric rates and services in unincorporated areas of the State of Texas and in the cities that have relinquished original jurisdiction. In addition, the Utility Commission has appellate jurisdiction over electric rates and services within the remaining incorporated municipalities.

In September 1983, various amendments to the PURA became effective which provide for, among other things, the extension of the life of the Utility Commission to 1995, the creation of an independent Office of Public Utility Counsel to represent the interests of residential and small commercial consumers before the Utility Commission, an increase from 125 days to 185 days in the period after filing of an application before new rates may be placed into effect under bond, and a prohibition against the collection by a public utility of any rates or charges (including fuel charges) that do not have the prior approval of the Utility Commission or other proper regulatory authority. In addition, the PURA, as amended, requires the Utility Commission to treat construction work in progress (CWIP) in rate base as an exceptional form of rate relief to be granted only when necessary to maintain the financial integrity of the utility and to exclude from rate base any CWIP on major projects under construction found to have been inefficiently or imprudently planned or managed. The 1983 amendments to the PURA have resulted in more protracted rate proceedings and could delay or prevent recovery of major expenses which, in turn, could adversely affect the earnings and cash flow of HL&P.

Requests for Interim Accounting Treatment. In January 1987, HL&P requested the Utility Commission to authorize the capitalization of operating and maintenance expenses, non-reconcilable mining and handling charges, taxes and depreciation associated with Limestone Unit No. 2 and the continued recording of AFUDC from the date that Unit No. 2 was placed in commercial operation until rates reflecting the costs of such unit are placed into effect. HL&P alternatively requested that non-reconcilable mining and handling charges be allowed recovery through its fuel cost factor. Electric rates do not currently reflect approximately \$174 million of the project cost or any provision for operating expenses, non-reconcilable lignite mining and handling costs, taxes or depreciation related to Unit No. 2, estimated to be \$57 million annually. Although hearings on HL&P's request concluded in June 1987, the examiner presiding over this proceeding has not yet issued a recommendation on this matter. Until rate relief is obtained which reflects the placing of Limestone Unit No. 2 into service or the requested accounting treatment or other regulatory action is granted with respect to Limestone Unit No. 2, operating results of HL&P will be adversely affected.

In July 1987, HL&P petitioned the Utility Commission to capitalize HL&P's share of all operation and maintenance expenses, taxes, and depreciation expense of Unit No. 1 of the South Texas project which would be recorded effective with the date the unit is placed into commercial operation. The petition further requested that the Utility Commission authorize HL&P to continue recording AFUDC associated with HL&P's 30.8% share of the investment in Unit No. 1 of the South Texas project until such time as HL&P is allowed to earn a return on this invested capital. The annualized effect of such operating expenses, taxes, depreciation expense and AFUDC is estimated to be \$230 million. In November 1987, the Texas Supreme Court issued a Writ of Mandamus which stayed all action in this proceeding. The Court's action resulted from a controversy between the Utility Commission and the Texas Attorney General with respect to the Attorney General's authority both to represent the Utility Commission on dockets which are appealed to the courts and to intervene in dockets pending before the Utility Commission on behalf of the Texas state agencies. The

Writ of Mandamus will remain in effect until the Texas Supreme Court resolves this issue. Until rate relief is obtained which reflects the placing of Unit No. 1 of the South Texas project into service or the requested accounting treatment or other regulatory action is granted with respect to Unit No. 1 of the South Texas project, operating results of HL&P will be adversely affected. Because the scheduled hearings relating to the prudence review are not expected to begin before the fall of 1988, a significant lag time could occur between the commercial operation date of Unit No. 1 of the South Texas project and implementation of new rates reflecting such facility as plant in-service. See Note 9 to the Financial Statements under Item 8 of this Report for a discussion of the effect of Statement of Financial Accounting Standards (SFAS) No. 92 on HL&P's deferred accounting request for Unit No. 1 of the South Texas project.

In a related matter, the Utility Commission is reviewing its policy of not allowing post test year adjustments to rate base. In January 1988, the Utility Commission approved the publication of a proposed rule that would explicitly permit post test year adjustments to rate base. The Utility Commission has indicated that Texas consumers will benefit if post test year adjustments to rate base are allowed because such adjustments would eliminate the need for additional proceedings and regulatory expenses to handle deferred accounting treatment petitions.

Prudence Review of South Texas Project. For information concerning a prudence review of the South Texas project by the Utility Commission, see Note 9 to the Financial Statements included under Item 8 of this Report.

Contemplated General Rate Proceeding. HL&P is planning to file a petition for authority to change rates with the Utility Commission and municipalities which retain original jurisdiction during the second quarter of 1988. The amount of the requested increase has not been finalized. This filing will include a request for recovery of Limestone Unit No. 2 costs not yet in rates. In addition, due to the impending commercial operation of Unit No. 1 of the South Texas project, HL&P plans to include the costs associated with this plant in the requested relief utilizing post test year adjustments to rate base. Although the details of the requests have not been finalized, HL&P is considering the use of interim rates and deferred accounting treatment in combination with a rate moderation plan in developing a reasonable pricing plan for inclusion of these units in rates.

Appeal of 1982 Rate Order. See Note 7 of the Financial Statements included under Item 8 of this Report for information concerning the appeal of a 1982 rate order.

Environmental Quality. HL&P is subject to regulation with respect to air and water quality, solid waste disposal, and other environmental matters by various federal, state and local authorities. Environmental regulations continue to be affected by legislation, administrative actions, and judicial review and interpretation. As a result, the precise effect of existing and potential regulations upon existing and proposed facilities and operations cannot presently be determined. However, developments in these and other areas of regulation have in the past required HL&P to make substantial expenditures to modify, supplement or replace equipment and facilities and

may in the future delay or impede construction and operation of new facilities or require substantial expenditures to modify existing facilities.

The Texas Air Control Board (TACB) has jurisdiction and enforcement power to determine the level of air contaminants emitted in the State of Texas. The standards established by the Texas Clean Air Act and the rules of the TACB are subject to modification by standards promulgated by the federal Environmental Protection Agency (EPA). Compliance with such standards has resulted, and is expected to continue to result, in substantial expense to HL&P. The rate of growth in HL&P's kilowatt-hour sales to industrial customers is expected to be lower in the future than it has been in the past partially as a result of requirements imposed by the EPA, new-source performance standards, restrictions on deterioration of air quality and potential sanctions related to non-attainment regions, all as they apply to portions of HL&P's service area. In addition, expanded permit and fee systems and enforcement penalties may discourage industrial growth.

In order to ensure the control of particulate emissions and compliance with applicable clean air standards at its W. A. Parish plant, HL&P is upgrading existing pollution control equipment at the plant by installing baghouses on three of the four coal-fired generating units. The fourth coal-fired unit at the W. A. Parish plant is already equipped with a baghouse. The first unit was completed in January 1988 and the remaining two units are expected to be completed by January 1989. The total cost of all of the baghouses is approximately \$178 million excluding AFUDC. HL&P has obtained relief from certain TACB standards until the baghouse installations are completed.

The Texas Water Commission (TWC) has jurisdiction over all water discharges in the State of Texas and is empowered to set water quality standards and issue permits required for water discharges which might affect the quality of Texas water. The EPA is authorized to set such standards and issue permits with respect to discharges into navigable streams. HL&P has obtained permits from both the TWC and the EPA for all of its generating facilities currently in operation which require such permits. Applications for renewal of permits for existing facilities have been submitted as required.

HL&P is also subject to regulation by the TWC and the EPA with respect to the handling and disposal of solid waste generated on-site. The EPA has promulgated a number of regulations to protect human health and the environment from hazardous waste. Compliance with the regulations promulgated to date has not materially affected the operation of HL&P's facilities, but such compliance has increased operating costs. The promulgation of new regulations in the future or the amendment of existing regulations could result in revised solid waste handling and disposal procedures and additional costs to HL&P.

Nuclear Licensing. HL&P is subject to licensing and regulation by the NRC with respect to environmental, public health and safety aspects of the construction and operation of nuclear power plants.

In August 1987, the NRC granted a low power operating license for Unit No. 1 of the South Texas project. In 1987 the Government Accountability

Project (GAP), a citizens interest group, demanded that the NRC establish a special task force to investigate alleged safety defects at the South Texas project. The group claimed to have evidence of defects but refused to turn over the evidence to the NRC until late in 1987. The NRC has concluded an on-site investigation to review and evaluate the GAP allegations. The NRC review of all the GAP allegations has identified no substantive safety issue that would warrant delay in the NRC's consideration of a full power license for Unit No. 1 of the South Texas project.

In February 1988, the NRC imposed a civil penalty in the amount of \$75,000 for two instances in late 1987 when operations during testing at the South Texas project violated certain technical specifications. In March 1988, the NRC imposed a second civil penalty in the amount of \$50,000 for security deficiencies identified in the fall of 1987.

Initial criticality at Unit No. 1 of the South Texas project was achieved on March 8, 1988. The delay in achieving initial criticality has been principally attributable to certain equipment problems identified during the testing process which have been analyzed and corrected and the need for additional operator training undertaken to address concerns raised by the NRC. The steps remaining before Unit No. 1 can be placed into commercial operation are satisfactory completion of low power operation and the receipt of a full power license from the NRC.

The in-service date and cost estimate for Unit No. 1 of the South Texas project is subject to continuing review in light of these matters and the ongoing testing process. HL&P estimates that three to five months of additional testing will be required after initial criticality (which occurred on March 8, 1988) before Unit No. 1 can be placed in commercial operation. Although no definitive estimate of additional costs has been approved, HL&P anticipates that cost increases in the range of \$100 to \$150 million (of which HL&P's portion would be \$31 to \$46 million based on its 30.8% interest) may result from the delays in achieving initial criticality, and the resulting delay in the anticipated date of commercial operation of Unit No. 1. HL&P estimates that the carrying cost of its 30.8% interest in the South Texas project is approximately \$15 million per month.

Commercial operation of Unit No. 2 of the South Texas project is scheduled to commence in June 1989.

Viability Review. In March 1985, a Utility Commission proceeding was initiated for the purpose of gathering evidence concerning the economic viability of Unit No. 2 of the South Texas project. Initial hearings were held in January 1987 for the purpose of determining the appropriate computer model to be used for the economic study. Hearings in the final phase were held in October 1987 to consider the appropriate inputs for the study. An Examiner's report is expected to be issued in 1988. For a discussion of the Texas Supreme Court order to stay hearings on this proceeding before the Utility Commission, see Note 9 to the Financial Statements included under Item 8 of this Report.

Nuclear Insurance

See Note 9 to the Financial Statements included under Item 8 of this Report for information concerning nuclear insurance.

Labor Matters

As of December 31, 1987, HL&P had 10,910 full-time employees of which 4,485 were hourly-paid employees represented by the International Brotherhood of Electrical Workers under a collective bargaining agreement which expires on May 25, 1988.

Operating Statistics

	Year Ended December 31,		
	1987	1986	1985
Electric Energy Generated and Purchased (Mkwh):			
Generated - Net Station Output.....	48,798,146	45,507,566	49,653,222
Purchased.....	9,959,034	11,104,589	9,020,115
Net Interchange.....	(362)	737	587
Total.....	<u>58,756,818</u>	<u>56,612,892</u>	<u>58,673,924</u>
Company Use, Lost and Unaccounted for.....	2,845,491	2,605,335	2,705,208
Energy Sold.....	<u>55,911,327</u>	<u>54,007,557</u>	<u>55,968,716</u>
 Electric Sales (Mkwh):			
Residential.....	14,701,438	14,627,569	14,981,112
Commercial.....	11,188,927	11,437,464	11,490,874
Industrial.....	27,441,200	26,192,806	27,418,046
Street Lighting - Government and Municipal...	108,176	107,039	103,808
Total.....	<u>53,439,741</u>	<u>52,364,878</u>	<u>53,993,840</u>
Other Electric Utilities.....	2,471,586	1,642,679	1,974,876
Total.....	<u>55,911,327</u>	<u>54,007,557</u>	<u>55,968,716</u>
 Number of Customers (End of Period):			
Residential.....	1,147,962	1,144,165	1,156,121
Commercial.....	156,517	157,199	158,313
Industrial.....	1,764	1,755	1,800
Street Lighting - Government and Municipal...	79	80	76
Total.....	<u>1,306,322</u>	<u>1,303,199</u>	<u>1,316,310</u>
Other Electric Utilities.....	6	6	6
Total.....	<u>1,306,328</u>	<u>1,303,205</u>	<u>1,316,316</u>
 Operating Revenue (Thousands of Dollars):			
Residential.....	\$1,078,93	\$1,071,356	\$1,244,002
Commercial.....	690,078	707,386	831,277
Industrial.....	993,610	1,024,459	1,353,162
Street Lighting - Government and Municipal...	17,786	16,683	16,888
Other Electric Utilities.....	79,503	68,990	106,273
Total.....	<u>2,859,911</u>	<u>2,888,874</u>	<u>3,551,602</u>
Miscellaneous Electric Revenues.....	140,921	70,866	(18,238)
Total.....	<u>\$3,000,832</u>	<u>\$2,959,740</u>	<u>\$3,533,364</u>
 Installed Net Generating Capability (Kw) (End of Period).....			
	12,855,000	12,680,000	12,304,000
 Cost of Fuel (Cents per Million Btu):			
Gas.....	170.0	170.3	291.6
Coal.....	252.4	248.1	243.9
Lignite.....	162.7	188.5	321.9
Average.....	192.4	197.1	277.0

Officers

<u>Name</u>	<u>Age (1)</u>	<u>Officer Since(2)</u>	<u>Business Experience 1983-1987 Positions</u>	<u>Term</u>
			1983-1987 Positions	
D. D. Jordan.....	55	1971	Chairman and Chief Executive Officer and Director	1983-
D. D. Sykora.....	57	1977	President and Chief Operating Officer and Director	1983-
J. H. Goldberg...	56	1980	Group Vice President - Nuclear Vice President - Nuclear Engineering and Construction	1985- 1983-1985
H. R. Kelly.....	45	1984	Senior Vice President, General Counsel and Corporate Secretary	1984-
D. E. Simmons....	62	1972	Partner - Baker & Botts Group Vice President - Power Operations	1983-1984 1984-
			Group Vice President - Systems Engineering & Operations	1983-1984
R. J. Snokhous...	58	1983	Group Vice President - External Affairs	1983-
			Director of Public Affairs - Gulf Oil Corporation - U.S.	1983
E. A. Turner.....	60	1978	Group Vice President - Administration and Support	1985-
			Senior Vice President and Assistant to the President	1984-1985
			Group Vice President - Fossil Plant Engineering & Construction	1983-1984
A. R. Beavers....	64	1978	Vice President - Project Consultant	1987-
			Vice President - Purchasing and Materials Management	1984-1987
			Vice President - Purchasing and Services	1983-1984
L. G. Brackeen...	53	1984	Vice President - Fossil Fuel Resources	1984-
			Senior Purchasing Agent - E. I. DuPont De Nemours & Co.	1983-1984
J. S. Brian.....	40	1983	Vice President - Finance and Comptroller	1986-
			Comptroller	1983-1986
			Assistant Secretary and Assistant Treasurer	1983
R. E. Doan.....	58	1981	Vice President - Human and Information Resources	1986-
			Vice President - Human Resources	1983-1986
			Vice President - Rates, Planning & Information Systems	1983

Officers

<u>Name</u>	<u>Age (1)</u>	<u>Officer Since(2)</u>	<u>Business Experience 1983-1987 Positions</u>	<u>Term</u>
J. D. Greenwade..	48	1982	Vice President - System Operations Vice President - System Engineering and Transmission & Distribution Vice President - System Engineering	1984- 1983-1984 1983
L. B. Horrigan...	53	1981	Vice President - Purchasing and Materials Management Vice President - Fossil Plant Engineering and Construction Vice President - Fossil Plant Construction	1987- 1983-1987 1983
R. S. Letbetter..	39	1978	Vice President - Regulatory Relations Vice President & Comptroller	1983- 1983
A. D. Maddox.....	46	1982	Vice President - Customer Relations	1983-
D. G. Tees.....	43	1986	Vice President - Energy Production General Manager - Energy Production	1986- 1983-1986
G. E. Vaughn.....	45	1987	Vice President - Nuclear Operations General Manager - Nuclear Stations - Duke Power Company	1987- 1983-1987
K. W. Nabors.....	44	1986	Treasur Manager - Accounting Services Manager - Corporate Accounting	1986- 1983-1986 1983

(1) At December 31, 1987.

(2) Officers were elected May 20, 1987 to serve for one year or until their successors are duly elected and qualified.

Item 2. Properties.

All of HL&P's electric generating stations and substantially all of the other operating property of HL&P is located in the State of Texas. HL&P considers this property to be well maintained and in good operating condition.

Electric Generating Stations. As of December 31, 1987, HL&P had ten electric generating stations (60 generating units) with a combined turbine nameplate rating of 12,619,651 Kw.

Substations. As of December 31, 1987, HL&P owned 194 major substations (with capacities of at least 10.0 Mva) having a total installed rated transformer capacity of 50,294 Mva (exclusive of spare transformers).

Electric Lines-Overhead. As of December 31, 1987, HL&P operated 21,896 pole miles of overhead transmission and distribution lines, including 1,499 pole miles operated at 138,000 volts and 591 pole miles operated at 345,000 volts.

Electric Lines-Underground. As of December 31, 1987, HL&P operated 5,560 circuit miles of underground transmission and distribution lines, including 8 circuit miles operated at 138,000 volts.

General Properties. HL&P owns various properties which include a 27-story headquarters office building, division offices, service centers and other facilities used for general purposes.

Titles. The electric generating plants and other important units of property of HL&P are situated on lands owned in fee by HL&P. Transmission lines and distribution systems have been constructed in part on or across privately owned land pursuant to easements or on streets and highways and across waterways pursuant to authority granted by municipal and county permits, and by permits issued by state and federal governmental authorities. Under the laws of the State of Texas, HL&P has the right of eminent domain pursuant to which it may secure or perfect rights-of-way over private property, if necessary.

The major properties of HL&P are subject to liens securing its long-term debt, and titles to some of its properties are subject to minor encumbrances and defects, none of which impairs the use of such properties in the operation of its business.

Item 3. Legal Proceedings.

For a description of material legal and regulatory proceedings affecting HL&P, see Notes 7 through 9 to the Financial Statements included under Item 8 of this Report. See also Item 1. "Business - Regulatory Matters" for descriptions of pending regulatory proceedings.

Item 4. Submission of Matters to a Vote of Security Holders.

There were no matters submitted to a vote of security holders during the fourth quarter of 1987.

PART II

Item 5. Market for the Registrant's Common Stock and Related Stockholder Matters.

All of HL&P's Common Stock is privately held, beneficially and of record, by its parent, Houston Industries.

Item 6. Selected Financial Data.

The following table sets forth selected financial data with respect to HL&P's financial condition and results of operations and should be read in conjunction with the Financial Statements and the related notes included elsewhere herein.

	(Thousands of Dollars)				
	Year Ended December 31,				
	1987	1986	1985	1984	1983
Revenues.....	\$3,000,832	\$2,959,740	\$3,533,364	\$3,674,556	\$3,523,745
Income after preferred dividends.....	\$ 408,581	\$ 434,927	\$ 455,904	\$ 355,522	\$ 291,294
AFUDC as a percent of income after preferred dividends..	52%	52%	45%	31%	17%
Return on average common equity.....	14.0%	15.5%	17.6%	15.7%	15.0%
Ratio of earnings to fixed charges:					
Including AFUDC.....	3.35	3.36	3.76	3.55	3.50
Excluding AFUDC.....	2.41	2.42	2.84	2.99	3.22
Ratio of earnings to fixed charges and preferred dividend requirements.....	2.87	2.95	3.26	3.05	3.01
At year-end:					
Total assets.....	\$8,687,744	\$8,136,725	\$7,829,390	\$6,990,332	\$6,056,367
Long-term debt (including current maturities).....	\$2,845,877	\$2,908,277	\$2,841,399	\$2,573,602	\$2,156,000
Capitalization:					
Common stock equity.....	48%	47%	46%	46%	47%
Cumulative preferred stock.	7%	6%	6%	5%	6%
Long-term debt (including current maturities).....	45%	47%	48%	49%	47%
Construction and nuclear fuel expenditures (excluding AFUDC).....	\$ 644,580	\$ 712,418	\$ 745,972	\$ 904,076	\$ 886,892
Percent of construction expenditures financed internally from operations.	29%	35%	39%	37%	42%

ITEM 7. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION
AND RESULTS OF OPERATIONS

Results of Operations

Houston Lighting & Power Company (HL&P) reported 1987 income after preferred dividends of \$408.6 million, down \$26 million from 1986 and \$47 million from the record earnings of 1985. Allowance for funds used during construction (AFUDC) accounted for 52% of earnings in both 1987 and 1986 compared to 45% in 1985. AFUDC is a non-cash item of net income which represents the cost of funds used to finance construction projects and is capitalized as part of the cost of the assets being constructed. Decreases in AFUDC in 1987 were primarily related to a reduction in the net-of-tax AFUDC rate and the commencement of commercial operation of Unit No. 2 of the Limestone Electric Generating Station (Limestone). Increases in AFUDC in 1986 resulted from increased levels of investment in construction without corresponding increases in the amount of construction included in rate base and earning a current cash return.

The decline in HL&P's 1987 income is attributable to increased expenses principally associated with Limestone, which expenses are not yet fully reflected in electric rates, partially offset by the reduction of the federal corporate income tax rate due to the Tax Reform Act of 1986. Earnings were positively affected by base rate increases allowed by the City of Houston and the Public Utility Commission of Texas (Utility Commission) in July and December 1986, respectively.

Electric operating revenues increased 1% and declined 16% for the years 1987 and 1986, respectively. The increase in revenues in 1987 is primarily due to higher base revenues from rate increases implemented in 1986. Kilowatt hour (KWH) sales were up 3.5% during 1987 and down 3.5% in 1986. The majority of the increases was due to off-system sales and sales to industrial customers on an interruptible basis, both of which provide minimal contribution to base electric revenues. Residential KWH sales increased by .5% in 1987 and declined 2.4% in 1986. Commercial KWH sales declined by 2.2% in 1987 and .5% in 1986. Industrial KWH sales, which account for approximately half of HL&P's overall sales, were up 4.8% and down 4.5% for 1987 and 1986, respectively. However, most of the increase was due to sales made on an interruptible basis as described above.

Fuel expense increased \$47 million in 1987 and declined \$485 million in 1986. The increase in 1987 was primarily due to increased generation, partially offset by decreases in the price paid for fuel. The average cost of fuel used by HL&P during 1987 was \$1.92 per million Btu as compared with \$1.97 for 1986 and \$2.77 for 1985. The combined cost of fuel used by HL&P and the fuel portion of purchased power during 1987 was 1.86 cents per KWH as compared with 2.10 cents in 1986 and 3.02 cents in 1985. Purchased power expense decreased 10% in 1987 and 5% in 1986 due to decreases in purchases of energy from cogenerators.

Electric operating and maintenance expenses in 1987 increased 9% or \$52 million when compared to 1986. In 1986, operating and maintenance expenses decreased \$33 million or 6% when compared to 1985. The increase in 1987 was due primarily to increases in operation and maintenance expenses related to Limestone and in administrative and general expenses. The decrease in 1986 was primarily due to a reduction in transmission expenses, customer expenses and administrative and general expenses.

In January 1987, following the December 1986 commencement of commercial operation of Limestone Unit No. 2, HL&P filed a petition with the Utility Commission requesting interim accounting treatment to capitalize costs and to continue the accrual of AFUDC associated with Unit No. 2 from the time it was placed in commercial operation until rates reflecting the costs of such unit are placed in effect. Electric rates do not currently reflect approximately \$174 million of the project's cost or any provision for operating expenses, non-reconcilable lignite mining and handling costs, taxes or depreciation related to Unit No. 2, estimated to be \$57 million on an annual basis. In July 1987, a similar request was made for the first unit of the South Texas project once it goes into commercial operation. The annualized effect of operating expenses, taxes, depreciation and AFUDC related to Unit No. 1 is estimated to be \$230 million based on HL&P's 30.8% interest (\$290 million based on a 46.8% interest), none of which is reflected in electric rates. The Utility Commission has not ruled on either request. Until rate relief is obtained which reflects Limestone Unit No. 2 as plant in service or the requested accounting treatment or other regulatory action is granted with respect to Limestone Unit No. 2, operating results of HL&P will be adversely affected. Upon the commencement of commercial operation of Unit No. 1 of the South Texas project, the operating results of HL&P will be more severely impacted until similar regulatory relief is granted with respect to such unit.

In prior years, HL&P's operating results were adversely affected by the lag in recovery of increased costs through electric rates due primarily to relatively high rates of inflation. The rate of inflation, however, has moderated over the last several years, and HL&P has not been significantly impacted by the effects of inflation.

Liquidity and Capital Resources

HL&P's construction and nuclear fuel expenditures (excluding AFUDC) for the year 1987 totaled \$645 million. The approved budget for 1987 was \$638 million. Estimated expenditures for 1988, 1989, and 1990 are \$495 million, \$444 million and \$368 million, respectively. These amounts reflect the modification of the scheduled in-service dates for the two lignite units at the Malakoff Electric Generating Station as discussed in Note 10 to the Financial Statements. These amounts also reflect the cost estimate for the South Texas project adopted in December 1987 (assuming a commercial operation date for Unit No. 1 of March 1, 1988). These amounts do not reflect the possible acquisition by HL&P of an additional 16% interest in the South Texas project presently owned by the City of Austin (Austin), which would increase the estimated construction and nuclear fuel expenditures by \$205 million for the 1988-1990 period, \$92 million of which is related to the reimbursement of costs incurred by Austin prior to 1988 and the purchase of Austin's nuclear fuel. These amounts also do not include expenditures on projects for which HL&P expects to be reimbursed by customers or cogenerators.

HL&P expects to finance a portion of its construction program through funds generated internally from operations. The extent to which HL&P is able to fund its capital requirements from internal funds is dependent, to a large degree, on regulatory practices which determine the amount and timing of recovery of investments in new plant facilities, depreciation rates, recovery of operating expenses and the opportunity to earn a reasonable rate of return on its invested capital. It is presently estimated that during 1988, 10% to 20% of HL&P's construction program can be financed through internally generated funds from operations. Internally generated funds for subsequent years will be primarily dependent on the regulatory treatment of HL&P's investment in the South Texas

project. The balance of HL&P's construction program is expected to be financed through external sources, primarily sales of long-term debt, preferred stock and additional shares of common stock to Houston Industries Incorporated (Houston Industries), and, on an interim basis, the issuance of short-term debt securities. See Note 4 to the Financial Statements for a discussion of short-term financing.

In March 1987, HL&P issued \$391 million aggregate principal amount of a new 9% series of first mortgage bonds due 2017 in exchange for a like principal amount of outstanding high coupon first mortgage bonds. An additional \$140 million principal amount of high coupon first mortgage bonds was redeemed under the Replacement Fund provisions of HL&P's Mortgage and Deed of Trust and was retired by the bond trustee in May 1987. In February 1988, \$48 million principal amount of HL&P's 13 7/8% series first mortgage bonds due 1991 was redeemed at 100% of the principal amount plus accrued interest. These actions are part of a continuing program to reduce HL&P's long-term debt costs.

In June 1987, HL&P sold 1,000,000 shares of \$8.50 cumulative preferred stock which are subject to mandatory redemption. The mandatory redemption provision requires HL&P to redeem 200,000 shares annually beginning on June 1, 1993. HL&P received net proceeds of \$99 million from the sale.

During 1987, HL&P received approximately \$128 million from the proceeds of previously issued pollution control revenue bonds and first mortgage bonds, which proceeds had been held in trust. Approximately \$87 million (including interest earned on funds held in trust) was held in trust at December 31, 1987. Substantially all the funds held in trust are expected to be drawn down by HL&P in 1988 and 1989 to fund qualifying construction expenditures. On November 1, 1987, \$40 million principal amount of HL&P's 4 3/4% series first mortgage bonds matured. In January 1988, HL&P issued in a private placement \$400 million principal amount of 9 3/8% first mortgage bonds which will mature in approximately equal principal amounts in each of the years 1991, 1992, and 1993.

HL&P's capitalization ratios at December 31, 1987 consisted of 45% long-term debt, 7% preferred stock and 48% common equity, with similar ratios expected to be maintained in the future, assuming HL&P is able to obtain rate relief at levels comparable to those obtained in the past.

Houston Industries Finance, Inc., a wholly-owned subsidiary of Houston Industries, began purchasing HL&P's customer accounts receivable in January 1987.

The Tax Reform Act of 1986 (the Tax Act) includes a number of provisions that have adversely affected HL&P. Although the Tax Act reduced corporate income tax rates, it eliminated investment tax credits effective January 1, 1986 (except with respect to certain transition properties, including the South Texas project), eliminated current deductions for interest and property taxes during construction and made substantial changes to the calculation of the alternative minimum tax. This latter provision effectively provides for the inclusion of up to one half of the amount of AFUDC, a non-cash item of financial reporting income, as taxable income in determining the alternative minimum tax. These and other provisions of the Tax Act are expected to reduce the amount of cash flow generated from operations and therefore increase HL&P's reliance on external sources of funds.

Changes in Accounting Standards

In December 1986, the Financial Accounting Standards Board (FASB) issued Statement of Financial Accounting Standards (SFAS) No. 90, "Regulated Enterprises-Accounting for Abandonments and Disallowances of Plant Costs," which becomes effective for fiscal years beginning after December 15, 1987. SFAS No. 90 requires the future revenue that is expected to result from the regulator's inclusion of the cost of an abandoned plant in allowable costs for ratemaking purposes to be reported at its present value when the abandonment becomes probable. If the carrying amount of the abandoned plant exceeds that present value, a loss would be recognized. In addition, SFAS No. 90 requires any costs of a recently completed plant which are disallowed to be recognized as a loss when such a disallowance becomes probable and the amount of the disallowance is reasonably estimable. If part of the cost is disallowed indirectly (such as a disallowance of return on investment on a portion of the plant), an equivalent amount of cost shall be deducted from the reported cost of the plant and recognized as a loss. Finally, SFAS No. 90 specifies that AFUDC should be capitalized only if its subsequent inclusion in allowable costs for ratemaking purposes is probable. See Note 9 to the Financial Statements for a discussion of the prudence review of the South Texas project by the Utility Commission.

HL&P recorded a partial loss on abandonment of the Allens Creek Nuclear Project (Allens Creek) in 1982, and is currently amortizing the recoverable amount over a ten year period. HL&P believes that the application of SFAS No. 90 to Allens Creek would not materially affect the results of operations. See Notes 7 and 11 to the Financial Statements for discussions of Allens Creek.

In August 1987, the FASB issued SFAS No. 92, "Regulated Enterprises - Accounting for Phase-in Plans." SFAS No. 92 requires allowable costs deferred for future recovery under a phase-in plan related to plants completed before January 1, 1988, and plants on which substantial construction has been performed before January 1, 1988, to be capitalized as a deferred charge if each of four criteria is met. Those criteria are (a) the plan has been agreed to by the regulator, (b) the plan specifies when recovery will occur, (c) all allowable costs deferred under the plan are scheduled for recovery within ten years of the date when deferrals begin, and (d) the percentage increase in rates scheduled for each future year under the plan is not greater than the percentage increase in rates scheduled for each immediately preceding year. SFAS No. 92 does not permit the equity portion of AFUDC to be capitalized other than during construction or as part of a qualified phase-in plan. The provisions of SFAS No. 92 must be adopted for fiscal years beginning after December 15, 1987. See Note 9 to the Financial Statements for a discussion of the effect of SFAS No. 92 on HL&P's deferred accounting request for Unit No. 1 of the South Texas project.

In December 1987, the FASB issued SFAS No. 96, "Accounting for Income Taxes," which becomes effective for fiscal years beginning after December 15, 1988. SFAS No. 96 requires, among other things, the liability method of recognition for all temporary differences, requires that deferred tax liabilities and assets be adjusted for an enacted change in tax laws or rates and prohibits net-of-tax accounting and reporting. Certain provisions of SFAS No. 96 provide that regulated enterprises are permitted to recognize such adjustments as regulatory assets or liabilities if it is probable that such amounts will be recovered from or returned to customers in future rates. HL&P is currently evaluating the effects of SFAS No. 96 but does not expect the new pronouncement to have a material effect on its financial position or results of operations. HL&P presently anticipates adopting SFAS No. 96 in 1989.

Item 8. Financial Statements.

HOUSTON LIGHTING & POWER COMPANY

STATEMENTS OF INCOME
(Thousands of Dollars)

	Year Ended December 31,		
	1987	1986	1985
Operating Revenues.....	\$3,000,832	\$2,959,740	\$3,533,364
Operating Expenses:			
Fuel.....	981,922	935,169	1,420,262
Purchased power.....	379,497	421,893	442,802
Operation.....	423,789	391,873	419,086
Maintenance.....	189,566	169,533	175,490
Depreciation and amortization.....	219,501	206,262	177,099
Federal income taxes.....	195,416	222,281	262,557
Other taxes.....	151,667	146,791	140,185
Total.....	2,541,358	2,493,802	3,037,481
Operating Income.....	459,474	465,938	495,883
Other Income (Expense):			
Allowance for other funds used during construction.....	143,584	170,348	154,246
Other - net.....	(7,747)	7,236	5,023
Total.....	135,837	177,584	159,269
Income Before Interest Charges.....	595,311	643,522	655,152
Interest Charges:			
Interest on long-term debt.....	238,919	259,887	248,516
Other interest.....	25,432	24,258	16,654
Allowance for borrowed funds used during construction.....	(68,817)	(55,278)	(49,963)
Taxes applicable to the allowance for borrowed funds used during construction.....	(40,210)	(47,089)	(42,561)
Total.....	155,324	181,778	172,646
Net Income.....	439,987	461,744	482,506
Dividends on Preferred Stock.....	31,406	26,817	26,602
Income After Preferred Dividends.....	\$ 408,581	\$ 434,927	\$ 455,904

See Notes to Financial Statements.

HOUSTON LIGHTING & POWER COMPANY

STATEMENTS OF RETAINED EARNINGS
(Thousands of Dollars)

	Year Ended December 31,		
	1987	1986	1985
BALANCE AT BEGINNING OF YEAR.....	\$1,269,492	\$1,128,547	\$ 945,820
ADD - NET INCOME.....	<u>439,987</u>	<u>461,744</u>	<u>482,506</u>
Total.....	<u>1,709,479</u>	<u>1,590,291</u>	<u>1,428,326</u>
DEDUCT - CASH DIVIDENDS:			
Preferred:			
\$4.00 Series.....	390	390	390
\$6.72 Series.....	1,680	1,680	1,680
\$7.52 Series.....	3,760	3,760	3,760
\$9.52 Series.....	3,808	3,808	3,808
\$9.08 Series.....	3,632	3,632	3,632
\$8.12 Series.....	4,060	4,060	4,060
\$9.04 Series.....	2,712	2,712	2,712
"A" Series.....	3,415	3,435	4,845
"B" Series.....	3,345	3,340	1,715
\$8.50 Series.....	4,604		
Common:			
1987 \$2.86; 1986 \$2.76; 1985 \$2.60 (per share).....	<u>304,868</u>	<u>293,982</u>	<u>273,177</u>
Total.....	<u>336,274</u>	<u>320,799</u>	<u>299,779</u>
BALANCE AT END OF YEAR.....	<u>\$1,373,205</u>	<u>\$1,269,492</u>	<u>\$1,128,547</u>

See Notes to Financial Statements.

HOUSTON LIGHTING & POWER COMPANY

BALANCE SHEETS
(Thousands of Dollars)

ASSETS

	December 31,	
	1987	1986
PROPERTY, PLANT AND EQUIPMENT-AT COST:		
Electric plant:		
Production.....	\$3,894,100	\$3,747,442
Transmission.....	640,423	601,084
Distribution.....	1,845,618	1,747,216
General.....	456,232	431,048
Construction work in progress.....	2,648,682	2,170,700
Nuclear fuel.....	131,323	126,190
Held for future use.....	180,333	167,008
Electric plant acquisition adjustments.....	<u>3,166</u>	<u>3,166</u>
Total.....	9,799,877	8,993,854
Less accumulated depreciation and amortization...	<u>1,530,543</u>	<u>1,351,412</u>
Property, plant and equipment - net.....	<u>8,269,334</u>	<u>7,642,442</u>
CURRENT ASSETS:		
Cash and temporary investments.....	260	389
Working funds and special deposits.....	483	502
Accounts receivable:		
Customers.....	110,741	
Affiliated companies.....	1,208	2,628
Others.....	37,159	39,589
Inventory:		
Fuel oil and gas, at life cost.....	18,698	16,583
Materials and supplies, at average cost.....	90,946	80,044
Other.....	<u>11,661</u>	<u>11,731</u>
Total current assets.....	<u>160,415</u>	<u>262,207</u>
OTHER ASSETS:		
Recoverable cancelled project costs.....	36,129	43,382
Unamortized debt expense and premium on reacquired debt.....	67,539	47,763
Deferred debits.....	<u>154,307</u>	<u>140,931</u>
Total other assets.....	<u>257,995</u>	<u>232,076</u>
Total.....	<u>\$8,687,744</u>	<u>\$8,136,725</u>

See Notes to Financial Statements.

HOUSTON LIGHTING & POWER COMPANY

BALANCE SHEETS
(Thousands of Dollars)

CAPITALIZATION AND LIABILITIES

	December 31,	
	<u>1987</u>	<u>1986</u>
CAPITALIZATION (statements on following page):		
Common stock equity.....	\$2,975,302	\$2,866,739
Cumulative preferred stock:		
Not subject to mandatory redemption.....	341,319	341,319
Subject to mandatory redemption.....	99,055	
Long-term debt.....	<u>2,844,918</u>	<u>2,865,105</u>
Total capitalization.....	<u>6,260,594</u>	<u>6,073,163</u>
CURRENT LIABILITIES:		
Notes payable.....	551,007	65,381
Notes payable to affiliated companies.....		3,500
Accounts payable.....	202,798	229,605
Accounts payable to affiliated companies.....	22,374	17,891
Taxes accrued.....	79,224	116,126
Interest accrued.....	65,163	66,627
Accrued liabilities to municipalities.....	70,685	72,263
Current portion of long-term debt.....	959	43,172
Fuel cost over recovery.....		94,309
Other.....	<u>44,375</u>	<u>56,476</u>
Total current liabilities.....	<u>1,036,585</u>	<u>765,350</u>
DEFERRED CREDITS:		
Accumulated deferred federal income taxes.....	793,082	725,192
Unamortized investment tax credit.....	529,337	530,292
Other.....	<u>68,146</u>	<u>42,728</u>
Total deferred credits.....	<u>1,390,565</u>	<u>1,298,212</u>
COMMITMENTS AND CONTINGENCIES		
Total.....	<u>\$8,687,744</u>	<u>\$8,136,725</u>

See Notes to Financial Statements.

HOUSTON LIGHTING & POWER COMPANY

STATEMENTS OF CAPITALIZATION
(Thousands of Dollars)

	December 31,	
	<u>1987</u>	<u>1986</u>

COMMON STOCK EQUITY:

Common stock, no par; authorized 200,000,000 shares; outstanding 106,660,778 shares at December 31, 1987 and 106,515,383 shares at December 31, 1986.....	\$1,602,097	\$1,597,247
Retained earnings.....	1,373,205	1,269,492
Total common stock equity.....	<u>2,975,302</u>	<u>2,866,739</u>

CUMULATIVE PREFERRED STOCK, no par; authorized 10,000,000 shares;
outstanding 4,447,397 shares at December 31, 1987 and 3,447,397
shares at December 31, 1986 (entitled upon involuntary
liquidation to \$100 per share)

Not subject to mandatory redemption:

\$4.00 series, 97,397 shares.....	9,740	9,740
\$6.72 series, 250,000 shares.....	25,115	25,115
\$7.52 series, 500,000 shares.....	50,225	50,225
\$9.52 series, 400,000 shares.....	39,372	39,372
\$9.08 series, 400,000 shares.....	39,395	39,395
\$8.12 series, 500,000 shares.....	50,098	50,098
\$9.04 series, 300,000 shares.....	29,573	29,573
"A" series, 500,000 shares.....	48,809	48,809
"B" series, 500,000 shares.....	48,992	48,992
Total.....	<u>341,319</u>	<u>341,319</u>

Subject to mandatory redemption:

\$8.50 series, 1,000,000 shares.....	99,055	
Total cumulative preferred stock.....	<u>440,374</u>	<u>341,319</u>

LONG-TERM DEBT:

First mortgage bonds:

4 3/4% series, due 1987.....	40,000	
3% series, due 1989.....	30,000	30,000
4 7/8% series, due 1989.....	25,000	25,000
13 7/8% series, due 1991.....	48,473	65,301
15 1/8% series, due 1992.....	52,662	68,712
4 1/2% series, due 1992.....	25,000	25,000
5 1/4% series, due 1996.....	40,000	40,000
5 1/4% series, due 1997.....	40,000	40,000
6 3/4% series, due 1997.....	35,000	35,000
6 3/4% series, due 1998.....	35,000	35,000
7 1/2% series, due 1999.....	30,000	30,000
7 1/4% series, due 2001.....	50,000	50,000
7 1/2% series, due 2001.....	50,000	50,000
8 1/8% series, due 2004.....	100,000	100,000
10 1/8% series, due 2004.....	35,407	100,000
8 3/4% series, due 2005.....	125,000	125,000

(continued on next page)

HOUSTON LIGHTING & POWER COMPANY

STATEMENTS OF CAPITALIZATION
(Thousands of Dollars)

(Continued)

	December 31,	
	1987	1986
8 3/8% series, due 2006.....	125,000	125,000
8 3/8% series, due 2007.....	\$ 125,000	\$ 125,000
8 7/8% series, due 2008.....	125,000	125,000
9 1/4% series, due 2008.....	100,000	100,000
11 1/4% series, due 2009.....		125,000
12% series, due 2010.....		100,000
12 3/8% series, due 2013.....		7,944
11 5/8% series, due 2015.....		200,000
9% series, due 2017.....	390,519	
7 7/8% pollution control series, due 2016.....	68,000	68,000
7 7/8% pollution control series, due 2018.....	50,000	50,000
Funds on deposit with Trustee.....	(12,612)	(39,112)
Total first mortgage bonds.....	<u>1,692,449</u>	<u>1,845,845</u>
Pollution control revenue bonds:		
Gulf Coast 1978 series, 9 1/2%, due 1998.....	19,200	19,200
Gulf Coast 1980-T series, Floating Rate, due 1998.....	5,000	5,000
Brazos River 1983 series, 10 1/2%, due 2003.....	25,000	25,000
Gulf Coast 1974 series, 7 3/8%, due 2004.....	18,000	18,000
Brazos River 1985 A2 series, 9 3/4%, due 2005.....	10,000	10,000
Gulf Coast 1982 series, 9 7/8%, due 2012.....	12,100	12,100
Brazos River 1982 series, 9 7/8%, due 2012.....	42,800	42,800
Brazos River 1983 series, 10 5/8%, due 2013.....	75,000	75,000
Brazos River 1985 A1 series, 9 7/8%, due 2015.....	100,000	100,000
Brazos River 1985 B series, Floating Rate, due 2015.....	90,000	90,000
Matagorda County 1985 series, 10%, due 2015.....	115,000	115,000
Brazos River 1984 F series, Floating Rate, due 2016.....	68,700	68,700
Brazos River 1984 A-E series, Floating Rate, due 2019....	400,000	400,000
Matagorda County 1984 A-C series, Floating Rate, due 2019	250,000	250,000
Funds on deposit with Trustee.....	(74,126)	(167,110)
Total pollution control revenue bonds.....	<u>1,156,674</u>	<u>1,063,690</u>
Unamortized premium or (discount)-net.....	(4,427)	(5,611)
Capitalized lease obligations, average discount rate 13.8%.	<u>1,181</u>	<u>4,353</u>
Total.....	2,845,877	2,908,277
Less current maturities.....	959	43,172
Total long-term debt.....	<u>2,844,918</u>	<u>2,865,105</u>
Total capitalization.....	<u>\$6,260,594</u>	<u>\$6,073,163</u>

See Notes to Financial Statements.

HOUSTON LIGHTING & POWER COMPANY

STATEMENTS OF CHANGES IN FINANCIAL POSITION
(Thousands of Dollars)

	Year Ended December 31		
	1987	1986	1985

Sources of Funds:

Operations:

Net income.....	\$ 439,987	\$ 461,744	\$ 482,506
Items not requiring current outlay of working capital:			
Depreciation and amortization.....	229,679	218,092	184,794
Deferred federal income taxes - net.....	67,890	93,689	86,903
Investment tax credit deferred - net.....	(955)	24,332	39,788
Allowance for funds used during construction.....	(212,401)	(225,626)	(204,209)
Total.....	524,200	572,231	589,782
Dividends declared.....	(336,274)	(320,799)	(299,779)
Reinvested funds from operations.....	<u>187,926</u>	<u>251,432</u>	<u>290,003</u>

Financing:

Sale of common stock.....	4,850	136,274	
Sale of preferred stock.....	99,125	49,021	
Sale of first mortgage bonds.....			200,000
Proceeds from pollution control revenue bonds and first mortgage bonds held in trust.....	127,874	238,503	275,258
First mortgage bonds issued in exchange offer.....	390,519		
Change in notes payable and temporary cash investments.....	482,126	474,628	(281,339)
Total financing.....	<u>1,104,494</u>	<u>713,131</u>	<u>379,214</u>

Other:

Decrease (increase) in working capital (exclusive of notes payable and temporary cash investments).....	(109,099)	(59,036)	137,166
Reclassification to current maturity of long-term debt.....	(959)	(43,172)	(32,756)
Proceeds from settlement of litigation.....			177,439
Other - net.....	(7,367)	(31,113)	(90,875)
Total other.....	<u>(117,425)</u>	<u>(133,321)</u>	<u>190,974</u>
Total.....	<u>\$1,174,995</u>	<u>\$ 831,242</u>	<u>\$ 860,191</u>

Application of Funds:

Construction and nuclear fuel expenditures (net of allowance for funds used during construction).....	\$ 544,580	\$ 712,418	\$ 745,972
Reacquired long-term debt.....	530,415	118,824	114,219
Total.....	<u>\$1,174,995</u>	<u>\$ 831,242</u>	<u>\$ 860,191</u>

(continued on next page)

HOUSTON LIGHTING & POWER COMPANY

STATEMENTS OF CHANGES IN FINANCIAL POSITION
(Thousands of Dollars)

(Continued)

	Year Ended December 31		
	1987	1986	1985
Changes in Components of Working Capital (exclusive of notes payable and temporary cash investments):			
Increase (decrease) in current assets:			
Cash.....	\$ (129)	\$ (745)	\$ (4,992)
Accounts receivable.....	(113,171)	(14,228)	(27,410)
Accounts receivable from affiliated companies.....	(1,420)	2,117	(1,107)
Inventory.....	13,017	19,949	(31,836)
Other.....	(89)	(6,693)	6,265
Total.....	<u>(101,792)</u>	<u>400</u>	<u>(59,080)</u>
Increase (decrease) in current liabilities:			
Accounts payable.....	(26,807)	29,569	(45,409)
Accounts payable to affiliated companies.....	4,483	8,445	1,679
Taxes and interest accrued.....	(38,366)	(36,465)	52,587
Fuel cost over recovery.....	(94,309)	(62,290)	95,831
Current portion of long-term debt.....	(42,213)	10,416	(40,079)
Other.....	(13,679)	(8,311)	13,477
Total.....	<u>(210,891)</u>	<u>(58,636)</u>	<u>78,086</u>
Increase (Decrease) in Working Capital (exclusive of notes payable and temporary cash investments).....	<u>\$ 109,099</u>	<u>\$ 59,036</u>	<u>\$ (137,166)</u>

See Notes to Financial Statements.

HOUSTON LIGHTING & POWER COMPANY

NOTES TO FINANCIAL STATEMENTS
For the Three Years Ended December 31, 1987

(1) Summary of Significant Accounting Policies

System of Accounts

The accounting records of Houston Lighting & Power Company (HL&P) are maintained in accordance with the Federal Energy Regulatory Commission's Uniform System of Accounts which has been adopted by the Public Utility Commission of Texas (Utility Commission).

Electric Plant

Additions to electric plant, betterments to existing property and replacements of units of property are capitalized at cost. Cost includes the original cost of contracted services, direct labor and material, indirect charges for engineering supervision and similar overhead items and an allowance for funds used during construction (AFUDC). Customer advances for construction reduce additions to electric plant.

Maintenance of property and replacements and renewals of items determined to be less than units of property are charged to expense. The actual or average book cost of units of property replaced or renewed is removed from plant and such cost, plus removal cost less salvage, is charged to accumulated depreciation.

HL&P computes depreciation using the straight-line method. The depreciation provision as a percentage of the depreciable cost of plant was 3.4% for 1987, 3.6% for 1986, and 3.8% for 1985.

Allowance for Funds Used During Construction

HL&P accrues AFUDC on construction projects and nuclear fuel payments except for amounts included in the rate base by regulatory authorities. AFUDC was computed using a gross rate of 10.75% beginning in 1987 due to changes caused by the Tax Reform Act of 1986, which generally eliminates a current tax deduction for interest during construction. This gross rate is applicable to all property except certain transition property, principally the South Texas Project Electric Generating Station (South Texas project), on which interest will be permitted as a current deduction. The net-of-tax accrual rate was 9% during 1987, and such rate was 10% during 1986 and 1985.

Operating Revenues

Revenues are recognized from the sale of electricity as bills are rendered to customers. The Utility Commission provides for the recovery of fuel and the energy portion of purchased power costs

through an energy component of base electric rates. The energy component is established during a utility's general rate proceeding and is effective for a minimum of twelve months. The rules provide for a reconciliation of fuel revenues, with any over- or under-recovery of fuel costs to be considered in establishing future fuel cost recoveries. In February 1986, the Utility Commission adopted a rule that requires a monthly reduction of the fuel factor if the Utility Commission determines that a utility has materially over-recovered, or projects that it will over-recover allowable fuel costs under its existing fuel factor. The rule also provides for any fuel cost savings to be refunded as a one-time credit to customers' bills.

Federal Income Taxes

Houston Industries Incorporated (Houston Industries) and its subsidiaries file a consolidated income tax return. HL&P records as its current income tax expense an amount equal to the tax it would have to pay if it filed a separate return. HL&P follows a policy of comprehensive interperiod income tax allocation. The Tax Reform Act of 1986 eliminated investment tax credits effective January 1, 1986, except with respect to certain transition properties, principally the South Texas project. Investment tax credits are deferred and amortized over the estimated lives of the related property.

(2) Preferred Stock

HL&P's preferred stock may be redeemed at the following per share prices, plus any unpaid accrued dividends to the date of redemption:

Not subject to mandatory redemption:

\$4.00 Series: \$105.00.
\$6.72 Series: \$102.51.
\$7.52 Series: \$102.35.
\$9.52 Series: through September 30, 1990 - \$103.00;
thereafter - \$103.00 to \$101.00.
\$9.08 Series: through March 31, 1992 - \$103.00;
thereafter - \$101.00.
\$8.12 Series: through November 30, 1992 - \$104.25; thereafter -
\$102.25.
\$9.04 Series: through January 31, 1989 - \$105.00;
thereafter - \$103.00 to \$101.00.
Adjustable Rate Series "A": through March 31, 1989 - not
redeemable; thereafter - \$103.00 to \$100.00. The dividend rate
on this series, as of January 1, 1988, is 7.75%. The rate is
adjusted quarterly, based on the yield on U.S. Treasury
securities.
Adjustable Rate Series "B": through September 30, 1990 -
not redeemable; thereafter - \$103.00 to \$100.00. The dividend
rate on this series, as of January 1, 1988, is 7.50%. The rate
is adjusted quarterly, based on the yield on U.S. Treasury
securities.

Subject to mandatory redemption:

\$8.50 Series: through May 31, 1992 - \$108.50; thereafter - \$104.25 to \$100.00; provided that the \$8.50 Series may not be redeemed, directly or indirectly, prior to June 1, 1992 from the proceeds of any refunding through the incurrence of debt or through the issuance of preferred stock ranking equally with or prior to the \$8.50 Series as to dividends or liquidation, where such debt has an effective interest cost, or such preferred stock has an effective dividend cost, of less than 8.50% per annum. The mandatory redemption provision requires HL&P to redeem 200,000 shares annually beginning June 1, 1993.

(3) Long-Term Debt

At December 31, 1987, sinking or improvement fund requirements of HL&P's first mortgage bonds outstanding will be approximately \$36 million for each of the years 1988 through 1992. Of such requirements, approximately \$17 million for each of the years 1988 through 1992 may be satisfied by certification of property additions at 100% of the requirements, and the remainder through certification of such property additions at 166 2/3% of the requirements. Sinking or improvement fund requirements for 1987 and prior years have been satisfied by certification of property additions.

HL&P has agreed to expend an amount each year for replacements and improvements in respect of its depreciable mortgaged utility property equal to \$1,450,000 plus 2 1/2% of net additions to such mortgaged property made after March 31, 1948, and before July 1 of the preceding year. Such requirement may be met with cash, first mortgage bonds, gross property additions or expenditures for repairs or replacements, or by taking credit for property additions at 100% of the requirements. At the option of HL&P, but only with respect to first mortgage bonds of a series subject to special redemption, deposited cash may be used to redeem first mortgage bonds of such series at the applicable special redemption price.

Annual maturities of long-term debt and minimum capital lease payments are approximately \$1 million in 1988, \$55 million in 1989, no maturities in 1990, \$48 million in 1991 and \$78 million in 1992. See also Note 15.

The issuable amount of HL&P's first mortgage bonds is unlimited as to authorization, but limited by property, earnings, and other provisions of the Mortgage and Deed of Trust and the supplemental indentures thereto. Substantially all properties of HL&P are subject to liens securing its long-term debt.

(4) Short-Term Financing

The interim financing requirements of HL&P are met through short-term bank loans and the issuance of commercial paper. HL&P had bank lines of credit aggregating \$650 million at December 31, 1987 and 1988, which limit its total short-term borrowings and provide for interest

it rates generally less than the prime rate. Commercial paper outstanding was \$549,796,000 at December 31, 1987. Bank loans and commercial paper outstanding were \$50,000,000 and \$14,100,000, respectively, at December 31, 1986. Commitment fees are required on the undrawn portion of the lines.

Houston Industries Finance, Inc. (Houston Industries Finance), a wholly-owned subsidiary of Houston Industries, began purchasing HL&P's customer accounts receivable in January 1987.

(5) **Retirement Plan**

In 1986, HL&P adopted Statement of Financial Accounting Standards (SFAS) No. 87, "Employers' Accounting for Pensions," for its retirement plan, retroactive to January 1, 1986. Pension costs for 1987 and 1986, and related disclosures as of December 31, 1987 and 1986, are determined under the provisions of SFAS No. 87. Pension costs for the plan in 1985 are determined under the provisions of previous accounting principles.

HL&P has a noncontributory retirement plan covering substantially all employees. The plan provides retirement benefits based on years of service and the employee's highest 36 consecutive months' base compensation during the last 120 months of employment. The policy of HL&P is to fund all net pension costs, but past service costs only to the extent that the excess of plan assets over accrued benefits does not meet HL&P's funding obligations for past service costs. In 1987 and 1986, however, as a result of the change in federal income tax rates and the early retirement program, discussed below, HL&P funded the maximum amount deductible for federal income tax purposes. Plan assets consist principally of common stocks and investments in short-term, high quality, interest-bearing obligations.

In January 1987, HL&P offered employees (excluding officers) who were 55 years of age and had 15 years of service as of February 28, 1987 an incentive program to retire early. For employees electing early retirement, the program would add three years of service credit and three years in age up to 35 years of service and age 65, respectively, in determining an employee's pension. Each participating employee would also receive a supplemental benefit to age 62 (for a minimum of two years). The early retirement incentive was accepted by 430 employees.

Pension benefits are being paid out of HL&P's retirement plan assets and the supplemental benefits are being paid by HL&P. Upon the adoption of the early retirement plan, the projected benefit obligations pertaining to HL&P's retirement plan and supplemental benefits were increased by \$17.5 million and \$7.2 million, respectively. HL&P has deferred the costs associated with the increases in these projected benefit obligations and will request recovery through electric rates in its next rate proceeding before regulatory authorities. At December 31, 1987, HL&P's obligation related to the supplemental benefits was \$5.8 million.

Net pension cost includes the following components:

	<u>Year Ended December 31,</u>	
	<u>1987</u>	<u>1986</u>
	(Thousands of Dollars)	
Service cost - benefits earned during the period	\$ 12,909	\$ 10,961
Interest cost on projected benefit obligation	22,782	17,971
Return on plan assets - actual - deferred gain (loss)	(10,186)	(26,379)
Amortization of transitional asset and prior service cost	(10,096)	9,064
Net pension cost	<u>(1,455)</u>	<u>(1,915)</u>
	<u>\$ 13,954</u>	<u>\$ 9,702</u>

The funded status of the retirement plan was as follows:

	<u>December 31,</u>	
	<u>1987</u>	<u>1986</u>
	(Thousands of Dollars)	
Actuarial present value of: Vested benefit obligation	<u>\$ 180,118</u>	<u>\$ 138,747</u>
Accumulated benefit obligation	<u>\$ 207,859</u>	<u>\$ 167,116</u>
Plan assets at market value	\$ 249,403	\$ 234,843
Projected benefit obligation	<u>275,342</u>	<u>234,624</u>
Assets in excess of (less than) projected benefit obligation	(25,939)	219
Unrecognized transitional asset at January 1, 1986	(28,400)	(30,559)
Unrecognized prior service cost	6,134	
Unrecognized net loss	<u>16,034</u>	<u>11,387</u>
Accrued pension cost	<u>\$ (32,171)</u>	<u>\$ (18,953)</u>

The projected benefit obligation was determined using an assumed discount rate of 9 1/2% in 1987 and 8 1/2% in 1986 and an assumed long-term rate of compensation increase of 6 1/2% in both years. The assumed long-term rate of return on plan assets is 9%. The transitional asset at January 1, 1986 is being recognized over approximately 17 years, and the prior service cost is being recognized over approximately 15 years.

The total pension cost of HL&P's retirement plan for 1985 was \$14,405,000.

(6) Commitments and Contingencies

Significant commitments have been incurred in connection with HL&P's construction program and for nuclear fuel purchases. The construction program (exclusive of AFUDC) is presently estimated to cost \$477 million in 1988, \$431 million in 1989 and \$349 million in 1990. These amounts do not include expenditures on projects for which HL&P expects to be reimbursed by customers or cogenerators and also do not reflect the possible acquisition by HL&P of an additional 16% interest in the South Texas project. See Note 9 for discussions of such possible acquisition and the revised budget and schedule for the South Texas project. An additional \$50 million is expected to be spent during such period for uranium concentrate and nuclear fuel processing services for HL&P's portion of the South Texas project. Commitments in connection with HL&P's construction program, principally for generating plants and related facilities, are generally revocable by HL&P subject to reimbursement to manufacturers for expenditures incurred or other cancellation penalties.

HL&P also has certain leases for computer equipment that are treated as capital leases for financial accounting purposes. HL&P has no other material lease commitments.

(7) Pending Litigation

Appeal of 1982 Rate Order. On December 16, 1987, the Texas Supreme Court rendered its decision on an Application for Writ of Error filed by the Utility Commission in connection with a December 1982 rate order by the Utility Commission (Docket No. 4540). In the rate order, the Utility Commission disallowed the recovery by HL&P of approximately \$166 million of costs incurred in connection with its cancelled Allens Creek nuclear project, and ordered that any tax savings associated with the disallowed portion be passed through to customers. While the Utility Commission purported to permit \$195 million of expenditures for the project to be recovered over a ten-year period, the flow-through of tax savings on the disallowed portion reduced the recovery to approximately \$84 million. That decision was appealed by HL&P to the 201st Judicial District Court in Travis County, Texas which ruled, in December 1984, that the Utility Commission was without legal authority in imposing such punitive measures. The District Court ruled that, since the Utility Commission had found that the shareholders, and not the ratepayers, should bear the disallowed Allens Creek expenditures, the shareholders should receive any and all tax benefits associated with those expenditures. The rate order had also reduced a recommended return on common equity from 16.85% to 16.35% as "a penalty for poor management," based principally on findings that HL&P had been imprudent in the handling of its nuclear construction projects. The District Court ruled that the Utility Commission had no statutory authority for such a penalty, and that the Utility Commission's findings regarding HL&P's management of the South Texas project were "premature and presumptuous" in view of the then pending litigation on such issues against the former architect-engineer. The District

Court also ruled that the 1982 rate order had erroneously and prematurely attempted to exclude from HL&P's cost of service any of its expenses in connection with the litigation, as well as any amounts which may ultimately be assessed against HL&P in such litigation. Based on such rulings, the District Court remanded the case to the Utility Commission for further proceedings consistent with the final judgment. The Utility Commission appealed the District Court's decision to the Court of Appeals for the Third Supreme Judicial District of Texas, which essentially upheld the District Court in an opinion issued April 9, 1986 (which was modified and reissued on July 2, 1986). The Texas Supreme Court granted the Utility Commission application for Writ of Error to consider certain points of error raised by the Utility Commission, as well as certain other points raised by HL&P.

Although the Texas Supreme Court affirmed certain aspects of the lower courts' decisions, including a ruling to the effect that the Utility Commission had no statutory authority to impose a penalty on HL&P's rate of return, that court reversed the lower courts' decisions regarding allocation of certain income tax benefits associated with the disallowed costs to the benefit of shareholders and held that such income tax benefits should inure to the benefit of HL&P's ratepayers.

HL&P has filed a motion for rehearing on the issue reversed by the Texas Supreme Court. The Utility Commission has also sought rehearing on the issues affirmed by that court. Action on those motions is currently pending before the Texas Supreme Court. As a result of the Texas Supreme Court's affirmation of certain of the lower courts' decisions, the case is to be remanded to the Utility Commission for determination and implementation, subject to pending motions for rehearing and possible further appeals by HL&P. Previously reported financial results will not require restatement.

Jury Award in Condemnation Proceeding. In July 1981, HL&P filed a condemnation action against the Klein Independent School District (Klein) to take approximately 8.6 acres of Klein's property as an easement for the purpose of erecting, operating and maintaining a 345-kilovolt electric transmission line. Klein subsequently alleged in the County Civil Court at Law No. 1 of Harris County, Texas that HL&P had abused its discretion in the taking of the property. On November 27, 1985, the jury returned a verdict finding that Klein sustained actual damages of approximately \$104,000. The jury also found that HL&P's conduct in the construction, operation and maintenance of the transmission line on Klein's property was in reckless disregard of the school purposes for which the property was being used, and awarded exemplary damages in the amount of \$25 million. The jury found, further, that the value of Klein's property had been reduced to zero and that the cost of land and facilities necessary to replace or restore Klein's property and facilities was approximately \$42.1 million. On December 13, 1985, the trial judge entered judgment in favor of Klein, awarding the full amounts of actual and punitive damages, or a total of approximately \$25.1 million, plus interest, Klein having elected that form of judgment

rather than a judgment awarding condemnation damages. In addition, the court granted an injunction, pending appeal, that effectively prohibited HL&P from using the line for the transmission of energy, except during certain specified emergencies when there are no regularly conducted school or other publicly sponsored activities occurring on Klein's property.

On January 2, 1986, HL&P appealed the case to the Court of Appeals for the 14th Supreme Judicial District of Texas, and also sought, from that court, relief from the injunction against use of the line pending appeal or, in the alternative, an order increasing the bond which Klein must file in order to protect the interests of HL&P pending appeal. On February 27, 1986, the appellate court granted HL&P's requested relief from the injunction and directed the trial court to allow HL&P to post a bond that would allow continued use of the easement pending a final decision on the merits of HL&P's appeal. Klein responded on March 3, 1986, by asking the Texas Supreme Court for leave to file a mandamus petition against the 14th District Court of Appeals. On November 26, 1986, the Supreme Court conditionally granted the mandamus petition sought by Klein. Ruling that the trial court had not abused its discretion in denying HL&P's request to supersede the injunction, the Supreme Court indicated that it would grant the writ of mandamus if the Court of Appeals did not vacate its judgment, with the result of that decision being the reinstatement of the trial court's original order, which had enjoined HL&P from using the line pending the outcome of the appeal on the merits. In light of the injunction that effectively prohibited use of the line, HL&P placed a rerouted line in service in August 1987.

On November 5, 1987, the 14th District Court of Appeals issued its decision on the merits of the appeal by HL&P. The court ruled that HL&P's action pursuant to the statutory condemnation procedure could not amount to trespass and set aside the award of exemplary damages to Klein, thus relieving HL&P from liability for the \$25 million in exemplary damages awarded by the trial court. The appeals court affirmed the trial court judgment on the balance of the points raised in the appeal, leaving intact the jury's award of approximately \$104,000 in actual damages. The appeals court noted, however, that HL&P had rerouted the transmission line away from Klein's property.

Klein has filed an Application for Writ of Error with the Texas Supreme Court seeking further review of the appeals court's decision. HL&P has filed a contingent Application for Writ of Error to be considered in the event that the Texas Supreme Court grants Klein's Application. It is possible that the exemplary damages awarded by the trial court might be reinstated if the Supreme Court agrees to hear a further appeal of the decision. While HL&P can give no definitive assurance regarding the ultimate resolution of this matter, HL&P presently does not believe such resolution will have a material adverse impact on its financial position. No prediction can be made, however, of the final outcome or the timing of final judicial action in this suit.

Prudence Review of Coal Supply Agreements and Litigation with Coal Suppliers. During the course of hearing HL&P's 1986 general rate proceeding (Docket No. 6765), the Utility Commission severed into a separate docket (Docket No. 6963) certain issues related to the prudence of the two long-term contracts under which substantially all of the coal for HL&P's W. A. Parish generating units is obtained, including the degree to which the chemical characteristics of coal from one of those suppliers led to HL&P's decision to upgrade existing pollution control equipment by installing baghouses on three of those generating units. The Utility Commission staff requested that, pending the outcome of the separate docket, HL&P be at risk for all costs associated with the installation of the baghouses (estimated to total \$178 million excluding AFUDC) and for payments made for coal in excess of the equivalent of a delivered price of \$1.51 per million Btu's.

As a result of the Utility Commission's action, HL&P, Houston Industries and Utility Fuels, Inc. (Utility Fuels), a fuel supply subsidiary of Houston Industries, filed suit against the two coal suppliers in question in the United States District Court for the Northern District of Texas in Dallas. In that lawsuit, the plaintiffs requested the court to determine that performance under the contracts should be suspended or the contracts modified in the event the Utility Commission should proceed to a final determination that the maximum cost that can be included in electric rates charged to HL&P's customers is less than the amounts called for under the contracts. In addition, Utility Fuels began withholding from payments to the coal suppliers the difference between the amounts called for in the contracts and the equivalent of a delivered price of \$1.51 per million Btu's and sought to deposit that difference into the registry of the Court. In response, both coal suppliers filed counterclaims and motions for partial summary judgment on those counterclaims. On November 18, 1986, the trial court granted those motions for summary judgment in part, ruling that HL&P and Utility Fuels must pay the full contract price for coal pending the outcome of the Utility Commission proceeding and directing that the amounts previously withheld be paid to the coal companies with interest.

HL&P, Houston Industries and Utility Fuels appealed the trial court's decision to the Fifth Circuit Court of Appeals and continued to withhold the amounts in dispute pending the outcome of the appeal. On October 7, 1987, the Fifth Circuit Court of Appeals ruled that the trial court's decision was not a final, appealable order and therefore dismissed the appeal without considering the issues raised therein.

On April 20, 1987, a Utility Commission Hearings Examiner granted a motion by HL&P to suspend the procedural dates then in effect in Docket No. 6963 in order to allow HL&P, Utility Fuels and the coal companies to continue negotiations of certain modifications to the coal supply arrangements in an attempt to provide the basis for resolution of the issues in Docket No. 6963. Those negotiations were concluded on December 21, 1987, when amendments to both coal supply

contracts in question were executed. Under the amended contracts, the price paid by Utility Fuels was reduced as of January 1, 1988, and changes were made in the escalation and certain other provisions of the contracts. At the time the amended contracts were executed, Utility Fuels, pursuant to an agreed court order, paid the coal suppliers the amounts which previously had been withheld, including interest thereon.

In January 1988, HL&P and the Utility Commission staff filed testimony proposing that the amended coal supply arrangements be accepted by the Utility Commission in resolution of the issues raised in Docket No. 6963. HL&P also filed an agreed stipulation executed by HL&P, the staff and one other party to the docket. Under the stipulation, the new coal supply arrangements would be accepted by the Utility Commission and issues raised in the docket with respect to (i) prudence of amounts incurred prior to January 1, 1988 and (ii) the relationship of coal quality to the decision to install baghouses would be resolved without disallowance of amounts paid by HL&P for prior coal deliveries. However, in March 1988, the Utility Commission Hearings Examiner considering the docket issued a recommended decision in which he urged the Utility Commission to remand the matter for further evidentiary proceedings on certain points in the proposed stipulation which were questioned by the Hearings Examiner. Rather than reopening the record on his own motion, the Hearings Examiner chose to present his concerns to the Utility Commission for ruling prior to remand. A decision by the Utility Commission on the Hearings Examiner's recommendations is expected at the end of March 1988. In the event that the outstanding coal prudence issues are not resolved by the Utility Commission on a mutually acceptable basis, the parties to the new coal supply arrangements have reserved the right to terminate those arrangements and resume the litigation relating to the previous long-term agreements.

While HL&P can give no definitive assurance regarding the ultimate resolution of this matter, HL&P presently does not believe that such resolution will have a material adverse impact on its financial position. Should HL&P be unable to recover its costs, such costs may have to be charged against earnings.

Fuel Transportation Litigation. On July 31, 1986, HL&P and Utility Fuels filed suit in Federal District Court in Houston, Texas against three railroad holding companies and their railroad operating subsidiaries and two other railroads. The suit alleges that the railroads violated certain federal statutes, including the Sherman Act, in activities aimed at precluding development of coal slurry pipelines that could have delivered coal to the plaintiffs in competition with the railroads. On February 13, 1987, with the agreement of all parties, the Federal District Court in Beaumont, Texas entered its order permitting HL&P and Utility Fuels to file the same claims for alleged antitrust violations against the same railroads by intervention in an action there pending between a third party and the same railroads. HL&P and Utility Fuels have joined

with the railroads in requesting the Federal District Court in Houston to stay proceedings in the Houston litigation pending the outcome of the Beaumont litigation.

Among the defendants are the Burlington Northern Railroad Company (Burlington Northern) and the Atchison, Topeka and Santa Fe Railway Company (ATSF), which supply rail transportation services to Utility Fuels for coal purchased from mines in the Powder River Basin in Montana and Wyoming. In the litigation, Burlington Northern and ATSF have filed counterclaims based on the assertion that certain of the matters alleged to be in dispute in the litigation filed by Utility Fuels and HL&P were settled as a result of the execution of the Rail Transportation Agreement, dated March 8, 1985, among Utility Fuels and Burlington Northern and ATSF. Accordingly, the counterclaims assert that Utility Fuels is in breach of its obligation under the Rail Transportation Agreement by virtue of the filing of suit against Burlington Northern and ATSF.

In their counterclaims Burlington Northern and ATSF seek unspecified damages, including punitive damages. HL&P and Utility Fuels regard the counterclaims to be without merit, but no assessment of the ultimate outcome of the litigation can be made at this time.

See also Note 9 - Jointly-Owned Nuclear Plant.

(8) Limestone Generating Units

In December 1986, the second of two 720 megawatt, lignite-fired generating units at HL&P's Limestone Electric Generating Station (Limestone) was placed into commercial operation. In January 1987, HL&P requested that the Utility Commission order an accounting treatment which would permit HL&P to capitalize operating and maintenance expenses, non-reconcilable mining and handling charges, taxes and depreciation associated with Limestone Unit No. 2 and to continue recording AFUDC from the date Unit No. 2 was placed in commercial operation until the date when new rates are implemented that reflect Limestone Unit No. 2 as plant in service in rate base (Docket No. 7375). HL&P further requested, as an alternative, that if the mining and handling charges referred to above are not allowed to be capitalized, then those costs would be allowed recovery through the reconcilable fuel portion of base rates. Hearings in this docket concluded on June 10, 1987, and a decision by the Utility Commission is pending. A similar accounting treatment had been requested by HL&P for Limestone Unit No. 1 but was denied by the Utility Commission. Until rate relief or other regulatory action is taken with respect to Limestone Unit No. 2, operating results of HL&P will be adversely affected.

(9) Jointly-Owned Nuclear Plant

HL&P is project manager and one of four participants in the South Texas project, which consists of two 1,250 megawatt nuclear generating units. Each participant finances its own share of construction expenditures with HL&P's participating interest in the

project currently being 30.8%. As of December 31, 1987, HL&P's investments in the South Texas project and in nuclear fuel, including AFUDC, were \$2.2 billion and \$131 million, respectively.

Pending Litigation and Agreement in Principle with the City of Austin. In January 1983, the City of Austin (Austin), one of the four owners of the South Texas project, filed suit against HL&P and Houston Industries in the 98th Judicial District Court in Travis County, Texas (Cause No. 343,240), alleging that HL&P had misrepresented the capabilities of the original architect-engineer and construction manager of the project and failed to properly perform its duties as project manager. Because of such alleged misrepresentations and failures, Austin asserted it was entitled to, among other things, (a) a reformation of the participation agreement such that Austin would convey to HL&P its 16% interest in the project, (b) a refund from HL&P of the approximately \$437 million expended by Austin to that date, and of all sums expended by Austin on the project thereafter, and (c) damages in an additional unspecified amount. In December 1985, Austin filed an amended petition which again alleged that HL&P had misrepresented the capabilities of the former architect-engineer and failed to properly perform its duties as project manager for the South Texas project. In addition, the amended petition asserted claims against HL&P under the Texas Deceptive Trade Practices - Consumer Protection Act (DTPA) and sought, from HL&P and Houston Industries, either (a) an unspecified amount of damages, including treble damages to the extent proper under the DTPA, as well as pre-judgment interest costs and attorneys' fees, or (b) a reformation or rescission of the participation agreement for the South Texas project requiring HL&P to return to Austin all of the moneys expended by Austin with respect to its 16% interest in the project to the date of the judgment, with interest, relieving Austin of all future obligations with respect to such interest in the project, and providing for a concurrent transfer by Austin of such interest to HL&P.

Austin and HL&P have filed motions for partial summary judgment. On October 10, 1986, the trial judge ruled that Austin is not entitled to reformation or rescission of the participation agreement for the South Texas project. The trial judge overruled HL&P's motion for partial summary judgment directed at Austin's allegations asserting a cause of action under the DTPA and HL&P's motion for partial summary judgment directed at Austin's allegations that there was fraud in the inducement relating to Austin's entry into the participation agreement. On June 29, 1987, a newly appointed trial judge denied Austin's motion seeking to hold HL&P responsible for the actions of the former architect-engineer. The judge denied, however, HL&P's request for summary judgment on all claims relating to the participation agreement. The judge ruled that Austin must prove that HL&P breached the participation agreement by failing to report material information and must prove damages specifically related to such failure to provide information. The judge permitted Austin to maintain its claim for \$830 million under this theory of recovery if it could show that the owners would have cancelled the South Texas project in 1976 and that Austin would have built a coal plant in lieu

of the South Texas project. However, on August 10, 1987, Austin provided an updated calculation of its alleged damages under that claim, dropping its claim under this theory of recovery to \$740 million. On August 11, 1987, the judge reversed the earlier order denying HL&P's motion for summary judgment as to Austin's DTPA claims. Thus, Austin's DTPA claims have been mooted and its damage claims are no longer subject to trebling under the DTPA.

As a result, the maximum damage claim remaining in the case is an alternative claim for \$811 million relating to Austin's claim that it was fraudulently induced to enter into the South Texas project in 1973. The judge has not yet acted on HL&P's motion for summary judgment on this issue.

On September 3, 1987, HL&P announced that it had reached an agreement in principle (Agreement in Principle) with Austin to acquire Austin's 16% share of the South Texas project. Under the terms of the Agreement in Principle, HL&P and Austin would dismiss all litigation and other claims currently pending.

The Agreement in Principle provides that Austin would convey to HL&P its 400 megawatt (MW) interest in the South Texas project, together with nuclear fuel and related property, in exchange for a 400 MW interest in HL&P's Limestone station, a lignite plant having a capability of 1,440 MW which has been completed and placed in service. This conveyance would result in Austin having an undivided proportionate interest in the land, capital equipment, and fixed personal property of HL&P at Limestone. A 200 MW interest in Limestone Unit No. 1 would be conveyed on the later of June 1, 1988 or the closing of the settlement, and a 200 MW interest in Limestone Unit No. 2 would be conveyed on January 1, 1990. HL&P would operate Limestone in accordance with an operating agreement to be mutually agreed upon as part of the definitive documentation.

Under the terms of the Agreement in Principle, HL&P would (a) assume Austin's South Texas project obligations for the remaining construction and fuel costs effective September 1, 1987, as well as Austin's obligations for continuing capital improvements, decommissioning, and all other matters arising out of Austin's interest in the South Texas project; (b) pay Austin \$19.7 million for a portion of construction costs incurred during negotiations; (c) purchase Austin's nuclear fuel for \$30 million; and (d) pay certain of Austin's legal expenses. In addition, certain claims asserted by Austin under an outstanding purchased power contract would be resolved. Austin would assume responsibility for its portion of the capital improvements and fuel, operating and maintenance expenses at Limestone.

The Agreement in Principle provides that no contract obligation will come into existence until execution of the definitive contract documents and other conditions have been satisfied, including approval by the Utility Commission and the Nuclear Regulatory Commission (NRC).

In addition, the Agreement in Principle provides that it would be necessary that the order of the Utility Commission, among other things, contain no findings, conclusions, reservations, or observations by a majority of the Utility Commission that raise reasonable doubt that the transfers contemplated by the Agreement in Principle would result in rate treatment to HL&P less favorable than the rate treatment of HL&P prior to such transfers. In September 1987, HL&P filed an application with the Utility Commission (Docket No. 7725) to reflect the exchange of ownership of Limestone and the South Texas project pursuant to the Agreement in Principle. The settlement is also contingent upon the City of San Antonio (San Antonio) and Central Power and Light Company (CPL), the other participants in the South Texas project, waiving their rights of first refusal relating to acquiring part of Austin's interest.

On January 7, 1988, HL&P filed a Fourth Amended Answer, Original Third Party Petition and Original Petition for Declaratory Relief (Third Party Petition) in the pending litigation with Austin. In the Third Party Petition, HL&P requested leave of the court in which the Austin litigation is pending to make service on San Antonio and CPL and its parent corporation, Central and Southwest Corporation (CSW). The Third Party Petition makes claim against San Antonio, CPL and CSW for contribution and indemnity should HL&P be found to be liable to Austin with respect to certain claims of Austin in the pending litigation. The Third Party Petition asks for a declaratory judgment that HL&P is not liable to Austin, San Antonio, CPL or CSW with respect to its actions or inactions as project manager under the Participation Agreement among the co-owners of the South Texas project and further requests the court in the Austin litigation to implement alternative methods of dispute resolution provided by the Texas Civil Practice and Remedies Act such as non-binding arbitration. Finally, the Third Party Petition asks the court to defer or abate proceedings until completion of the second unit at the South Texas project but no later than December 31, 1990. Unit No. 2 of the South Texas project is presently scheduled for commercial operation in June 1989.

At a hearing on January 27, 1988, the court in the Austin litigation set the pending suit between Austin and HL&P for trial the first week in June 1988. The court in the Austin litigation, which has discretion whether to accept jurisdiction over the claims asserted in the Third Party Petition, allowed HL&P to serve the Third Party Petition on San Antonio, CPL and CSW without prejudice to the right of those parties to later assert that the Third Party Petition should be dismissed or severed for a separate trial in the Austin litigation or severed into a separate docket independent of the Austin litigation. The court also advised the parties that in no event would San Antonio, CPL and CSW be required to participate in the trial of the pending suit between Austin and HL&P. HL&P has also filed an original complaint in the 130th District Court of Matagorda County against San Antonio, CPL and CSW requesting substantially the same relief. If the court in the Austin litigation does not ultimately dismiss the Third Party Petition, prosecution of the action in Matagorda County will be deferred.

On March 3, 1988, San Antonio and CPL filed responses to the Third Party Petition, and each delivered letters requesting arbitration. In their responses and letters, both San Antonio and CPL asserted that HL&P has breached its duties and obligations as project manager for the South Texas project and is liable to San Antonio and CPL for resulting unspecified damages. San Antonio and CPL asked the trial judge in the Austin litigation to compel their requested arbitration and to stay further proceedings with respect to CPL and San Antonio pending the outcome of that arbitration. They further asked the trial court to enjoin HL&P from pursuing either its Third Party Petition or the separate litigation filed by HL&P in Matagorda County. No hearing has been scheduled by the court in the Austin litigation to consider these matters. CSW also responded to the Third Party Petition on March 3, 1988, asking that further proceedings be deferred pending the arbitration, and denying any liability with respect to the South Texas project.

The parties have continued settlement negotiations within the framework contemplated by the Agreement in Principle; however, no prediction can be made as to whether a settlement with Austin can be achieved. If a definitive agreement cannot be reached, any judgment entered after trial, as well as the intermediate ruling discussed above, will be subject to appeal after trial. With respect to the pending litigation, HL&P regards Austin's claims and those asserted by CPL and San Antonio to be without merit. While HL&P cannot give definitive assurance regarding the ultimate resolution of these matters, HL&P presently does not believe such resolution will have a material adverse impact on its financial position.

Assuming the Agreement in Principle is consummated, HL&P's construction and nuclear fuel expenditures would increase by \$205 million for the 1988-1990 period, \$92 million of which is related to reimbursement of costs incurred by Austin prior to 1988 and the purchase of Austin's nuclear fuel.

Order of the Texas Supreme Court. On November 4, 1987, the Texas Supreme Court entered an order which likely will delay the schedule for Docket No. 7725 and certain other dockets pending before the Utility Commission. The Court's order directed the Commissioners of the Utility Commission to stay hearings and actions in Docket No. 7725 and certain other dockets pending disposition by the Court of a Motion filed by the Attorney General of Texas for Leave to File Petition for Writ of Mandamus against the Commissioners. In addition to Docket No. 7725, the Court's order applies to Docket No. 6184, an inquiry concerning the economic viability of Unit No. 2 of the South Texas project, and Docket No. 7582, in which HL&P petitioned for deferred accounting treatment for costs related to Unit No. 1 of the South Texas project. The mandamus petition arose from action by the Utility Commission in these and certain other dockets denying the Attorney General's petitions to intervene on behalf of the Texas state agencies.

HL&P cannot be certain at this time as to the duration of the Texas Supreme Court's stay or as to the effect of the Court's action on these dockets. A hearing by the Court on the Attorney General's petition was held on December 16, 1987, and the Writ of Mandamus will remain in effect until the Texas Supreme Court resolves this issue.

Prudence Review of South Texas Project by Utility Commission. The Utility Commission has instituted a prudence review of the South Texas project for the purpose of reaching a final and binding determination for future rate base treatment of the amounts invested in the South Texas project. This proceeding (Docket No. 6668) will encompass an investigation of the prudence and efficiency of the planning, management and construction of the South Texas project, as well as the proper accounting treatment of the proceeds received from the former architect-engineer in the settlement (Settlement) of certain litigation relating to the South Texas project. There is no definitive schedule for commencement of hearings, but it is unlikely that hearings will begin before the fall of 1988.

The Utility Commission retained a consulting firm to evaluate the prudence and efficiency of the planning and management of the South Texas project and to make recommendations to the Utility Commission regarding regulatory actions based on such evaluation. In June 1986, the consulting firm presented its report (Report) to the Utility Commission, which Report covered the period through 1983. The consulting firm concluded in the Report that deficiencies in management of the project had occurred and that such deficiencies led to imprudent expenditures estimated to be in a range of \$1.1 to \$1.3 billion. According to the Report, such amounts do not include AFUDC or rate effects which the consulting firm concluded would substantially offset each other. The Report also indicated that the estimates relating to the prudence issue were preliminary, were based upon certain assumptions that should be refined and were subject to further refinement and modification.

A new consultant is expected to be retained by the Utility Commission in March 1988 to complete all work necessary for a final evaluation concerning the prudence of management and the reasonableness of costs associated with the South Texas project. Although the scope of that investigation has not been finalized, HL&P anticipates that the Report will not be sponsored by the Utility Commission staff. The manner in which the new consultant or any other party will utilize the Report in that docket, however, remains unclear.

HL&P believes that the Settlement with the former architect-engineer provided full compensation for any imprudent or inefficient planning or management during the period in question. HL&P will strongly contest any recommendation or finding that amounts invested in the South Texas project, after taking into consideration the Settlement, have been a result of inefficiency or imprudence. While no definitive assurance can be given that all amounts invested in the South Texas project will be recoverable by HL&P through electric rates or otherwise, HL&P presently believes the ultimate resolution

of the Utility Commission's prudence review will not have a material adverse effect on its financial position. Any amounts that are not recoverable would have to be charged against earnings. A substantial write-off could adversely affect HL&P's ability to finance its capital program and meet other financial obligations.

Request for Deferred Accounting Treatment. In July 1987, HL&P requested that the Utility Commission order an accounting treatment which would allow HL&P to defer its portion of all operating and maintenance expenses, taxes and depreciation that would otherwise be expensed effective with the commercial operation of Unit No. 1 of the South Texas project and to continue recording AFUDC associated with this investment until rates are placed into effect which would reflect this investment as electric plant in service in rate base (Docket No. 7582).

Because the hearings in Docket No. 6668 relating to the prudence review of the South Texas project are not currently scheduled and are unlikely to begin before the fall of 1988, a significant lag time could occur between the commercial operation date of Unit No. 1 of the South Texas project and implementation of new rates reflecting such facility as plant in service. As a result of such lag time and without the requested accounting treatment referenced above, HL&P's operating results will be adversely affected unless some other mitigative action by the Utility Commission is taken.

In October 1987, HL&P filed supplemental testimony in response to the issuance of SFAS No. 92. SFAS No. 92 precludes the capitalization of the equity portion of AFUDC for financial reporting purposes as was previously requested in Docket No. 7582. It is anticipated that the effect of such limitation would reduce earnings of HL&P by approximately \$100 million on an annualized basis. In its supplemental testimony, in lieu of the AFUDC accrual, HL&P requested the accrual of interest on the deferred costs and on the plant investment in Unit No. 1 of the South Texas project. Under this request, HL&P's 1988 financial results would be similar to those under the original deferral request.

Revised Budget and Schedule. On September 17, 1987, HL&P presented a completion estimate for the South Texas project to the management committee for the project, which estimate was adopted by the committee on December 17, 1987. Based upon its September 1987 completion assessment (which assumed a commercial operation date for Unit No. 1 of March 1, 1988), HL&P estimated that the total cost for the completed project would be \$5.28 billion, excluding AFUDC and net of the Settlement. The revised cost estimate represents an increase of \$300 million over the previous cost estimate which was \$4.98 billion, excluding AFUDC and net of the Settlement, for the entire South Texas project. HL&P's portion of such increased costs would be approximately \$92 million based on its current 30.8% interest in the South Texas project.

In August 1987, the NRC granted a low power operating license for Unit No. 1 of the South Texas project. In 1987, the Government

Accountability Project (GAP), a citizens interest group, demanded that the NRC establish a special task force to investigate alleged safety defects at the South Texas project. The group claimed to have evidence of defects but refused to turn over the evidence until late in 1987. The NRC concluded an on-site investigation to review and evaluate the GAP allegations. The NRC review of all the GAP allegations has identified no substantive safety issues that would warrant delay in the NRC's consideration of a full power license for Unit No. 1 of the South Texas project. In February 1988, the NRC imposed a civil penalty in the amount of \$75,000 for two instances in late 1987 when operations during testing at the South Texas project violated certain technical specifications. In March 1988, the NRC imposed a second civil penalty in the amount of \$50,000 for security deficiencies identified in the fall of 1987.

Initial criticality at Unit No. 1 of the South Texas project was achieved in March 1988. The delay in achieving initial criticality has been principally attributable to certain equipment problems identified during the testing process, which have been analyzed and corrected, and the need for additional operator training undertaken to address concerns raised by the NRC. The steps remaining before Unit No. 1 can be placed into commercial operation are satisfactory completion of low power operation and the receipt of a full power license from the NRC.

The in-service date and cost estimate for Unit No. 1 of the South Texas project are subject to continuing review in light of these matters and the ongoing testing process. HL&P estimates that three to five months of additional testing will be required after initial criticality before Unit No. 1 can be placed in commercial operation. Although no definitive estimate of additional costs has been approved, HL&P anticipates that cost increases in the range of \$100 to \$150 million (of which HL&P's portion would be \$31 to \$46 million based on its 30.8% interest) may result from the delays in achieving initial criticality and the resulting delay in the anticipated date of commercial operation of Unit No. 1. HL&P estimates that the carrying cost of its 30.8% interest in the South Texas project is approximately \$15 million per month.

Commercial operation of Unit No. 2 of the South Texas project is scheduled to commence in June 1989.

Nuclear Insurance. HL&P and the other owners of the South Texas project have obtained all nuclear property and nuclear liability insurance required to date, and additional insurance coverage will be purchased when the full power license for Unit No. 1 is obtained. In addition, HL&P is evaluating insurance coverage for incremental replacement power costs resulting from certain possible outages at the South Texas project. However, there can be no assurance that all potential losses or liabilities will be insurable or that the amount of insurance carried will be sufficient to cover all potential losses and liabilities. Any substantial losses not covered by insurance could have a material adverse effect on the financial condition of HL&P.

The owners of the South Texas project currently maintain property damage insurance in the amount of \$1.23 billion through American Nuclear Insurers (ANI) and Nuclear Electric Insurance Limited (NEIL) and are planning to purchase an additional \$165 million in limits from NEIL when the full power license for Unit No. 1 is obtained. The owners are also considering the purchase of an additional \$130 million in limits which has recently become available from ANI. The NEIL excess property damage insurance must be used to cover decontamination and clean-up expenses before being used to cover direct losses to property. Although there can be no assurance as to the maximum amount of property insurance available from time to time, it is anticipated that property insurance coverage will be maintained for the South Texas project in such amounts as are customary in the industry for similar nuclear generating plants. As a member insured of NEIL, HL&P will become subject to annual assessments, which could amount to approximately \$9 million for the total project, in the event that losses as a result of an accident at a nuclear plant of any NEIL insured company exceed the accumulated funds available to the insurer. HL&P and the other owners of the South Texas project have entered into an arrangement such that the total costs of insurance for the South Texas project (including premiums and assessments) are to be shared pro rata based upon the owners' respective ownership interests in the project. Under this arrangement, HL&P would ultimately bear that portion of total property damage insurance costs, including any assessment by NEIL, attributable to its ownership interest (currently 30.8%).

Effective in October 1987, the NRC amended its regulations to require nuclear power plant licensees to obtain property insurance coverage in the minimum amount of \$1.06 billion. These regulations further provide that the proceeds of this insurance shall be used to first ensure that the licensed reactor is in a safe and stable condition and can be maintained in that condition so as to prevent any significant risk to the public health or safety. Any property insurance proceeds not already expended to place the reactor in a safe and stable condition must be used first to complete decontamination operations that may be ordered by the NRC.

The owners of the South Texas project are insured against liability claims that may result from a nuclear incident to the full amount to which such claims are limited under the Price-Anderson Act (which is \$720 million as of January 18, 1988). In January 1987, HL&P and the other owners of the South Texas project executed with the NRC an indemnification agreement under the provisions of the Price-Anderson Act. This limitation on liability will increase by \$5 million for each additional operating license issued by the NRC. This insurance is provided through a combination of private insurance and a mandatory industry-wide program of self-insurance under which licensees may be assessed in the event of a nuclear incident involving any licensed facility in the United States up to \$5 million per incident for each of its licensed reactors and up to a maximum per reactor owned of \$10 million in any calendar year. HL&P and each of the other owners are subject to such assessments, which HL&P and

such owners have agreed will be borne on the basis of their respective ownership interests in the project. For purposes of such assessment, the South Texas project currently has one licensed reactor. When fuel loading begins at Unit No. 2, which is expected in December 1988, the South Texas project will have two licensed reactors.

Various proposals have been made to amend the Price-Anderson Act including amendments which would increase the limit on liability. If enacted, such amendments could result in an increase in assessments or other charges to fund the resulting increased coverage. HL&P is unable to predict what action Congress might take regarding the Price-Anderson Act or what effect such actions might have on HL&P.

(10) Modified Schedule for Malakoff Project

In January 1987, HL&P announced that the schedule for the construction of two 645 megawatt lignite units at the proposed Malakoff Electric Generating Station in Henderson County, Texas (the Malakoff project) had been modified. The scheduled in-service dates, which are the dates the units are expected to be available to meet peak demand, are now 1997 for Unit No. 1 and 1999 for Unit No. 2. The modified schedule resulted from lowered projections of future demand for electricity in the Houston area. As a result of the modified schedule, all developmental work on the two lignite units has stopped, but HL&P will resume activity when necessary to meet load growth requirements. HL&P's total investment in the Malakoff project, through December 31, 1987, is \$154 million including AFUDC and land. This amount is included in Plant Held for Future Use and the accrual of AFUDC has been suspended until such time as construction resumes. HL&P has agreed to indemnify Utility Fuels for all necessary and actual costs incurred due to the modification of the schedule. See Note 14 for such costs indemnified in 1987. Utility Fuels has invested \$121 million in lignite reserves and handling systems relating to the Malakoff project through December 31, 1987 and suspended capitalization of interest effective December 31, 1986. For the 1988 - 1990 period, Utility Fuels anticipates \$22 million of expenditures relating to the Malakoff project which are primarily associated with keeping lignite leases and other related agreements in effect.

(11) Unrecovered Costs

The Utility Commission has allowed recovery of certain costs over a period of time by amortizing those costs for rate making purposes. However, unrecovered amounts have not been included in rate base and, as a result, no return on investment is being earned during the recovery period. The amounts of such assets and the remaining recovery period applicable to each are listed below:

	<u>Unrecovered Amount at December 31, 1987</u> (Thousands of Dollars)	<u>Remaining Recovery Period at December 31, 1987</u>
Allens Creek		
Project.....	\$36,129	60 months
Other.....	4,525	11-106 months

(12) Federal Income Taxes

The current and deferred components of tax expenses are as follows:

	Year Ended December 31,		
	1987	1986	1985
	(Thousands of Dollars)		
Current - charged to operations.....	\$ 88,201	\$ 53,471	\$101,509
Deferred - charged to operations:			
Liberalized depreciation.....	64,615	73,207	60,472
Investment tax credit - net.....	(885)	28,033	31,584
Applicable to AFUDC.....	40,210	47,089	42,561
Other - net.....	<u>3,275</u>	<u>20,481</u>	<u>26,431</u>
Federal income taxes charged to operations.....	195,416	222,281	262,557
Current - charged to other income (expense).....			48
Total federal income taxes.....	<u>\$195,416</u>	<u>\$222,281</u>	<u>\$262,605</u>

Effective federal income tax rates are lower than statutory corporate rates for each year as follows:

	Year Ended December 31,		
	1987	1986	1985
	(Thousands of Dollars)		
Federal income taxes at statutory corporate rate.....	\$254,161	\$314,651	\$342,751
Reduction in taxes resulting from:			
AFUDC - other included in income.....	57,434	78,360	70,953
Other - net.....	1,311	14,010	9,193
Total.....	58,745	92,370	80,146
Federal income taxes.....	\$195,416	\$222,281	\$262,605
Effective rate.....	30.8%	32.5%	35.2%

(13) Supplementary Expense Information

Taxes, other than federal income taxes, were charged to expense as follows:

	Year Ended December 31,		
	1987	1986	1985
	(Thousands of Dollars)		
Ad valorem.....	\$ 76,686	\$ 73,366	\$ 62,806
State gross receipts.....	35,177	31,630	38,349
Payroll.....	15,222	18,788	17,712
PUC assessment.....	4,758	4,709	5,717
Miscellaneous.....	19,824	18,298	15,601
Total.....	\$151,667	\$146,791	\$140,185
Research and development costs charged to expense.....	\$ 15,317	\$ 14,462	\$ 14,038

(14) Principal Transactions Between HL&P, Its Parent and Other Related Companies

Pursuant to the corporate restructuring in 1977, Houston Industries assumed joint and several liability with HL&P for payment of principal and interest on the \$40,000,000 of 5 1/2% Convertible Debentures due 1985 issued by HL&P. In consideration thereof, HL&P issued Houston Industries a \$40,000,000 5 1/2% debenture which matured February 1, 1985. Included in Interest on Long-Term Debt in the accompanying Statements of Income for the year ended December 31, 1985 is \$183,000 related to this debenture.

HL&P issued 145,395 shares of common stock to Houston Industries in 1987 for a total consideration of \$4,850,000. No common stock of HL&P was issued to Houston Industries in 1986. In 1985, HL&P issued 5,844,416 shares of common stock to Houston Industries for a total consideration of \$136,274,000. Common stock dividends paid to Houston Industries by HL&P totaled \$304,868,000, \$293,982,000 and \$273,177,000 in 1987, 1986 and 1985, respectively.

Operating Expenses-Fuel in the accompanying Statements of Income for the years ended December 31, 1987, 1986 and 1985 includes \$509,739,000, \$468,274,000 and \$417,700,000, respectively, of coal and lignite purchased from Utility Fuels.

Operating Expenses-Operation in the accompanying Statements of Income for the years ended December 31, 1987, 1986 and 1985 includes \$15,382,000, \$9,139,000 and \$3,455,000, respectively, of service fees, reimbursable direct costs and shared costs charged by Houston Industries. In addition, such operating expenses include \$3,594,000 and \$2,408,000 of limestone purchased from Utility Fuels in 1987 and 1986, respectively. Also reflected in 1987 is \$26,313,000 of discount expense charged by Houston Industries Finance for the purchase of HL&P's accounts receivable.

Other Income (Expense) in the accompanying Statements of Income for the year ended December 31, 1987 includes \$8,931,000 of lignite holding expenses charged by Utility Fuels.

As part of the consolidated financing program, Houston Industries has established a money fund through which subsidiaries can borrow or invest on a short-term basis. Other Income (Expense) in the accompanying Statements of Income for the years ended December 31, 1987 and 1986 includes \$133,810 and \$3,634,000, respectively, of interest income from Houston Industries through such money fund transactions.

(15) Subsequent Events

In January 1988, HL&P sold \$400 million aggregate principal amount of 9 3/8% first mortgage bonds which will mature in approximately equal principal amounts in each of the years 1991, 1992 and 1993.

In January 1988, HL&P deposited \$52 million with the bond trustee to redeem all of the outstanding bonds of the 13 7/8% series at 100% of the principal amount and to pay accrued interest. The bonds were redeemed pursuant to the general redemption provisions of HL&P's Mortgage and Deed of Trust.

(16) Unaudited Quarterly Information

The following unaudited quarterly financial information includes, in the opinion of management, all adjustments (which comprise only normal recurring accruals) necessary for a fair presentation. Quarterly results are not necessarily indicative of expectations for a full year's operations because of seasonal and other factors, including rate increases and variations in operating expense patterns.

	Revenues	Operating Income	Income After Preferred Dividends
(Thousands of Dollars)			
March 31,			
1986.....	\$658,555	\$ 86,060	\$ 69,970
June 30,			
1986.....	713,022	99,158	85,655
September 30,			
1986.....	937,279	191,836	184,440
December 31,			
1986.....	650,884	88,884	94,862
March 31,			
1987.....	638,353	67,783	51,788
June 30,			
1987.....	737,853	108,383	93,534
September 30,			
1987.....	954,238	202,357	194,319
December 31,			
1987.....	670,388	80,951	68,940

(17) Reclassification

Certain amounts from the previous years have been reclassified to conform to the 1987 presentation of financial statements. Such reclassifications do not affect earnings.

AUDITORS' OPINION

Houston Lighting & Power Company:

We have examined the balance sheets and the statements of capitalization of Houston Lighting & Power Company as of December 31, 1987 and 1986 and the related statements of income, retained earnings and changes in financial position for each of the three years in the period ended December 31, 1987. Our examinations were made in accordance with generally accepted auditing standards and, accordingly, included such tests of the accounting records and such other auditing procedures as we considered necessary in the circumstances.

In our opinion, the accompanying financial statements present fairly the financial position of Houston Lighting & Power Company at December 31, 1987 and 1986 and the results of its operations and the changes in its financial position for each of the three years in the period ended December 31, 1987, in conformity with generally accepted accounting principles applied on a consistent basis.

Our examinations also comprehended the supplemental schedules V, VI, VIII and IX for each of the three years in the period ended December 31, 1987. In our opinion, such supplemental schedules, when considered in relation to the basic financial statements, present fairly in all material respects the information shown therein.

DELOITTE HASKINS & SELLS

Houston, Texas
March 3, 1988

Item 9. Changes in and Disagreements with Accountants on Accounting and Financial Disclosure.

None

PART III

Item 10. Directors and Executive Officers of the Registrant.(*)

Item 11. Executive Compensation.(*)

The following table shows, for the fiscal year ended December 31, 1987, compensation data for the five most highly compensated executive officers of HL&P whose cash compensation exceeded \$60,000 in 1987 and all executive officers of HL&P as a group.

<u>Name</u>	<u>Principal Capacity In Which Served</u>	<u>Cash Compensation</u>	
		<u>Salary</u>	<u>Other(1)</u>
D. D. Jordan	Chairman of the Board and Chief Executive Officer	\$513,333	\$130,600
D. D. Sykora	President and Chief Operating Officer	329,583	76,575
J. H. Goldberg	Group Vice President - Nuclear	237,500	36,093
H. R. Kelly	Senior Vice President, General Counsel and Corporate Secretary	213,750	33,632
E. A. Turner	Group Vice President - Administration and Support	175,833	27,890
All executive officers of HL&P as a group (7 persons, including those named above)		\$1,821,665	\$364,290

(1) Other Cash Compensation includes vested portions of amounts earned under the Executive Incentive Compensation Plan, as described below, and Board of Director and committee fees, whether received in cash or deferred.

The information related to Mr. Jordan also includes compensation earned in his capacity as President and Chief Executive Officer of Houston Industries.

A description of the benefit plans of HL&P and Houston Industries, pursuant to which cash or non-cash compensation was paid or distributed during 1987 to the named executive officers and the executive officers of HL&P as a group, is set forth in the definitive Proxy Statement relating to

the 1988 Annual Meeting of Shareholders of Houston Industries. During 1987, HL&P contributed \$501 each to the accounts of Mr. Jordan, Mr. Sykora, Mr. Goldberg, Mr. Kelly and Mr. Turner; and \$3,507 to the accounts of all executive officers as a group (7 persons) under the Employee Stock Ownership Plan of Houston Industries. Such amounts are not included in the Cash Compensation Table. Also during 1987, certain officers of HL&P, including those named in the Compensation Table above, received awards under Houston Industries Executive Incentive Compensation Plan (EICP). One half of each award to each participant is contingent and not vested and will be converted into a number of share equivalent units determined by reference to the market price of Houston Industries Common Stock. Amounts equal to dividends paid on the Houston Industries Common Stock are credited to a participant's account in the form of additional share equivalent units. The contingent portion of a participant's account will be payable at the earlier of (a) completion of four years of employment after the award was granted, (b) death or disability, or (c) the expiration of four years after the award was granted if the participant retired after attaining the age of 60 during such four-year period. If a participant is 50 years of age or older and owns 5,000 shares or more of Houston Industries Common Stock, he may elect, with the approval of the Personnel Committee and in lieu of receiving share equivalent units as described above, to have the amount of his annual awards credited to an adjustable account which will be adjusted as if it had been invested in the Deferred Compensation Plan or in Funds B, C or D of the Savings Plan of Houston Industries. A participant may elect to defer distribution of the contingent portion of his account after expiration of the periods described above by electing to have the contingent portion remain invested in contingent share equivalent units and continue to earn contingent share equivalent units equal to the dividends paid on the Houston Industries Common Stock or the participant may elect to have the contingent portion annually adjusted as if it were invested in Funds B, C or D of the Savings Plan of Houston Industries. In either event, the participant may elect to receive such deferred distribution in annual installments or in a lump sum payment. The remaining one-half is vested at the date of the award. The vested portions of such awards made pursuant to the EICP are included in the Cash Compensation Table. The non-vested portions of such awards have been excluded from the table and are as follows: \$122,500 for Mr. Jordan; \$70,875 for Mr. Sykora; \$36,093 for Mr. Goldberg; \$33,632 for Mr. Kelly; \$27,890 for Mr. Turner; and \$350,490 for all executive officers as a group (7 officers of HL&P). During 1987, HL&P made contributions under the Savings Plan of Houston Industries to the accounts of its executive officers. The vested portions of such contributions are as follows: Mr. Jordan, \$11,415; Mr. Sykora, \$7,720; Mr. Goldberg, \$5,565; Mr. Kelly, \$1,680; Mr. Turner, \$5,145; and all executive officers as a group (7 persons), \$39,188. Such amounts are not included in the Cash Compensation Table.

Messrs. Jordan, Sykora, Goldberg, Kelly, and Turner have credited years of service of 32, 32, 7, 3, and 33 years respectively, under the Retirement Plan described in the Houston Industries Proxy Statement. Mr. Goldberg and Mr. Kelly are entitled to an additional ten years of credit for service pursuant to the terms of supplemental agreements with HL&P.

Other compensation paid or distributed during 1987 to the executive officers listed in the Cash Compensation Table above did not exceed, with respect to any individual, the lesser of \$25,000 or 10% of the compensation reported in the table, or, with respect to all executive officers as a group, the lesser of \$175,000 or 10% of the compensation of the group reported in the table.

Item 12. Security Ownership of Certain Beneficial Owners and Management.(*)

As of March 1, 1988 all directors and officers of HL&P as a group beneficially owned 152,277 shares of Houston Industries Common Stock. Such ownership constitutes .13% of the outstanding Common Stock of Houston Industries.

Item 13. Certain Relationships and Related Transactions.(*)

* The information called for by Items 10, 11, 12 and 13, to the extent not set forth under Item 1. "Business - Officers", is set forth in the definitive proxy statement relating to the 1988 Annual Meeting of Shareholders of Houston Industries, which will be filed by Houston Industries (Commission File No. 1-7629) within 120 days of December 31, 1987 pursuant to Regulation 14A. Such definitive proxy statement relates to a meeting of shareholders involving the election of directors and the portions thereof called for by Items 10, 11, 12 and 13 are incorporated herein by reference pursuant to Instruction G to Form 10-K. Each member of the Board of Directors of Houston Industries is a member of the Board of Directors of the registrant.

PART IV

Item 14. Exhibits, Financial Statement Schedules, and Reports on Form 8-K

(a) (1) Financial Statements.

	<u>Page</u>
Statements of Income for the Three Years Ended December 31, 1987.....	31
Statements of Retained Earnings for the Three Years Ended December 31, 1987.....	32
Balance Sheets at December 31, 1987 and 1986.....	33
Statements of Capitalization at December 31, 1987 and 1986.....	35
Statements of Changes in Financial Position for the Three Years Ended December 31, 1987.....	37
Notes to Financial Statements.....	39
Auditors' Opinion.....	63

(a) (2) Financial Statement Schedules.

Schedules for the Three Years Ended December 31, 1987:	
V -- Property, Plant and Equipment.....	68
VI -- Accumulated Provision for Depreciation, Depletion and Amortization of Property, Plant and Equipment.....	69
VIII -- Reserves.....	70
IX -- Short-Term Borrowings.....	71

The following schedules are omitted because of the absence of the conditions under which they are required or because the required information is included in the financial statements:

I, II, III, IV, VII, X, XI, XII and XIII.

(a) (3) Exhibits.

See Index of Exhibits on page 73.

(b) Reports on Form 8-K.

The registrant filed a report on Form 8-K dated December 9, 1987.

Item 5. Other Events.

Status of Agreement in Principle with City of Austin.

SCHEDULE V - PROPERTY, PLANT AND EQUIPMENT
 For the Three Years Ended December 31, 1987
 (Thousands of Dollars)

Col. A Classification	Col. B Balance Beginning of Year	Col. C Additions at Cost	Col. D Retire- ments	Col. E Other Change) - Add (Deduct)	Col. F Balance End of Year
For the Year Ended December 31, 1987:					
Production Plant.....	\$3,747,442	\$ 146,974	\$ 316		\$3,894,100
Transmission Plant.....	601,084	41,211	1,872		640,423
Distribution Plant.....	1,747,216	119,045	20,642		1,845,618
General Plant.....	431,048	44,913	16,557	\$ (3,172)	456,232
Plant Acquisition Adjustments.....	3,166				3,166
Plant Held for Future Use.....	167,008	13,396		(71)	180,333
Total Plant.....	6,696,964	365,539	39,385	(3,243)	7,019,872
Construction Work in Progress.....	2,170,700	486,373		(8,391)	2,648,682
Nuclear Fuel.....	126,196	5,133			131,323
Total.....	\$8,993,854	\$ 857,045	\$ 39,388	\$ (11,634)	\$9,799,877
For the Year Ended December 31, 1986:					
Production Plant.....	\$3,238,785	\$ 534,122	\$ 25,665		\$3,747,442
Transmission Plant.....	187,317	14,564	1,387		601,084
Distribution Plant.....	1,611,637	105,296	22,767		1,747,216
General Plant.....	414,617	27,357	8,170	\$ (2,756)	431,048
Plant Acquisition Adjustments.....	3,166				3,166
Plant Held for Future Use.....	26,537	140,502		(31)	167,008
Total Plant.....	5,935,699	822,041	37,943	(2,787)	6,696,964
Construction Work in Progress.....	2,083,650	108,029		(20,075)	2,170,700
Nuclear Fuel.....	118,181	8,009			126,196
Total.....	\$8,137,530	\$ 938,073	\$ 37,943	\$ (20,075)	\$8,993,854
For the Year Ended December 31, 1985:					
Production Plant.....	\$2,370,568	\$ 921,177	\$ 52,960		\$3,238,785
Transmission Plant.....	549,491	40,307	1,895		587,907
Distribution Plant.....	1,523,575	168,507	27,451		1,664,687
General Plant.....	373,544	9,963	6,215	\$ (2,845)	414,617
Plant Acquisition Adjustments.....	3,166				3,166
Plant Held for Future Use.....	30,114	(3,577)			26,537
Total Plant.....	4,850,678	1,176,377	88,521	(2,835)	5,935,699
Construction Work in Progress.....	2,486,944	(231,282)		(174,012)	2,083,650
Nuclear Fuel.....	113,035	5,146			118,181
Total.....	\$7,452,657	\$ 950,241	\$ 88,521	\$ (176,847)	\$8,137,530

Notes:

- (A) Substantially all additions are originally charged to Construction Work in Progress and transferred to electric utility plant accounts upon completion. Additions at cost give effect to such transfers.
- (B) Additions at cost include non-cash charges for an allowance for funds used during construction.
- (C) NL&P computes depreciation using the straight-line method. The depreciation provisions as a percentage of the average depreciable cost of plant were 3.4% for 1987, 3.6% for 1986, and 3.8% for 1985.
- (D) Other changes in Plant Accounts include certain reclassification of amounts at December 31, 1984, which do not affect total Plant. Also included are changes in capital leases.
- (E) Construction Work in Progress was reduced by the amount of capitalized interest earned on funds held in trust in 1987, 1986, and 1985 and by the proceeds from the settlement of litigation in 1985.
- (F) Additions to Construction Work in Progress in 1987 include the transfer of \$510 million in December 1986 for the completed Limestone Unit No. 2 project to production plant. Additions to Construction Work in Progress in 1985 include the transfer of \$893 million in December 1985 for the completed Limestone Unit No. 1 project to production plant.
- (G) Additions to Plant Held for Future Use in 1987 reflect the transfer of \$14 million in December 1986 for the Malakoff project.

SCHEDULE VI - ACCUMULATED PROVISION FOR DEPRECIATION, DEPLETION
AND AMORTIZATION OF PROPERTY, PLANT AND EQUIPMENT

For the Three Years Ended December 31, 1987
(Thousands of Dollars)

Description	Col. A Balance at Beginning of Period	Col. B		Col. C		Col. D Additions Charged to Income	Deductions from Reserve Retirements, Renewals and Replacements	Col. E Balance at Close of Period
		Charged to Other Accounts	Charged to Other Accounts					
Year Ended December 31, 1987 -								
Depreciation, depletion and amortization of property, plant and equipment.....	\$1,351,412	\$214,501	\$10,178		\$0,548			\$1,530,543
Year Ended December 31, 1986 -								
Depreciation, depletion and amortization of property, plant and equipment.....	\$1,203,039	\$206,262	\$11,830		\$69,719			\$1,351,412
Year Ended December 31, 1985 -								
Depreciation, depletion and amortization of property, plant and equipment.....	\$1,113,412	\$177,099	\$ 7,695		\$95,167			\$1,203,039

SCHEDULE VIII - RESERVES

For the Three Years Ended December 31, 1987
(Thousands of Dollars)

Col. A	Col. B	Col. C	Col. D	Col. E	
Description		Additions	Deductions		
	Balance at Beginning of Period	Charged to Income	Charged to Other Accounts	from Reserves (A)	Balance at Close of Period
Year Ended December 31, 1987:					
Accumulated provisions deducted from related assets on balance sheet:					
Uncollectible accounts.....	\$4,300			\$ 4,300	
Reserves other than those deducted from assets on balance sheet:					
Property insurance.....	43	\$ 28		119	(48)
Injuries and damages.....	4,723	2,611		5,467	1,867
Year Ended December 31, 1986:					
Accumulated provisions deducted from related assets on balance sheet:					
Uncollectible accounts.....	\$5,707	\$11,493		\$12,900	\$4,300
Reserves other than those deducted from assets on balance sheet:					
Property insurance.....	(1,429)	238	\$ 1,234		43
Injuries and damages.....	5,597	3,658		4,532	4,723
Year Ended December 31, 1985:					
Accumulated provisions deducted from related assets on balance sheet:					
Uncollectible accounts.....	\$8,061	\$14,419		\$16,753	\$5,707
Reserves other than those deducted from assets on balance sheet:					
Property insurance.....		372		1,801	(1,429)
Injuries and damages.....	353	8,131		2,887	5,597

NOTES:

(A) Deductions from reserves represent losses or expenses for which the respective reserves were created. In the case of uncollectible accounts reserve, such deductions are net of recoveries of amounts previously written off.

SCHEDULE IX - SHORT-TERM BORROWINGS

For the Three Years Ended December 31, 1987
 (Thousands of Dollars)

Col. A	Col. B	Col. C	Col. D	Col. E	Col. F
Description	Category of Aggregate Short-term Borrowings	Balance at End of Period (A)	Weighted Average Interest Rate at End of Period (A)	Maximum Outstanding During the Period	Average Outstanding During the Period
Year Ended:					
December 31, 1987...Bank Loans					
Commercial Paper	\$ 549,796	8.15%	\$ 549,796	357,883	7.14%
Year Ended:					
December 31, 1986...Bank Loans	\$ 50,000	7.50%	\$ 119,067	\$ 1,093	7.91%
Commercial Paper	14,100	6.35%	247,381	79,589	6.57%
Year Ended:					
December 31, 1985...Commercial Paper				\$ 60,000	\$ 10,096
					8.12%

Note:

- (A) The Balance at End of Period excludes land and other notes (in thousands of dollars) of \$1,211, \$4,781, and \$1,457 as of December 31, 1987, 1986, and 1985, respectively.

SIGNATURES

Pursuant to the requirements of Section 13 or 15(d) of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized, in the City of Houston and State of Texas, on the 16th day of March, 1988.

HOUSTON LIGHTING & POWER COMPANY
(Registrant)

D. D. JORDAN

(D. D. Jordan, Chairman)

Pursuant to the requirements of the Securities Exchange Act of 1934, this report has been signed below by the following persons on behalf of the registrant and in the capacities and on the date indicated.

<u>Signature</u>	<u>Title</u>	<u>Date</u>
D. D. JORDAN (D. D. Jordan, Chairman)	Principal Executive Officer and Director	
J. S. BRIAN (J. S. Brian, Vice President—Finance and Comptroller)	Principal Financial and Accounting Officer	
CHARLES E. BISHOP (Charles E. Bishop)	Director	
SEARCY BRACEWELL (Searcy Bracewell)	Director	
JOHN T. CATER (John T. Cater)	Director	
H. R. DEAN (H. R. Dean)	Director	
JOSEPH M. HENDRIE (Joseph M. Hendrie)	Director	March 16, 1988
HOWARD W. HORNE (Howard W. Horne)	Director	
JAMES R. LESCH (James R. Lesch)	Director	
THOMAS B. McDADE (Thomas B. McDade)	Director	
I. A. NAMAN (I. A. Naman)	Director	
KENNETH L. SCHNITZER, SR. (Kenneth L. Schnitzer, Sr.)	Director	
D. D. SYKORA (D. D. Sykora)	Director	
JACK T. TROTTER (Jack T. Trotter)	Director	
JOE C. WESSENDORFF (Joe C. Wessendorff)	Director	

HOUSTON LIGHTING & POWER COMPANY

Exhibits to the Annual Report on Form 10-K
For the Fiscal Year Ended December 31, 1987

INDEX OF EXHIBITS

Exhibits not incorporated by reference to a prior filing are designated by an asterisk all exhibits not so designated are incorporated herein by reference to a prior filing as indicated.

- 3(a) - Restated Articles of Incorporation of HL&P, as amended and supplemented through August 8, 1985 (Exhibit T3A to HL&P's Form T-3 for Applications for Qualification of Indentures Under the Trust Indenture Act of 1939, as filed with the SEC on February 2, 1987 ("Form T-3"); Registration No. 22-16489).
- 3(b) - Amended and Restated Bylaws of HL&P, as adopted by resolution of the Board of Directors on July 2, 1986 (Exhibit T3B to HL&P's Form T-3; Registration No. 22-16489).
- 4(a)(1) - Mortgage and Deed of Trust, dated as of November 1, 1944, between HL&P and South Texas Commercial National Bank of Houston (Texas Commerce Bank National Association, as successor trustee), as trustee, as amended and supplemented by 20 Supplemental Indentures thereto (Exhibit 2(b) to HL&P's Registration Statement on Form S-7, as filed with the SEC on August 25, 1977; Registration No. 2-59748).
- 4(a)(2) - Twenty-First Supplemental Indenture to Exhibit 4(a)(1) (Exhibit 2 to HL&P's Annual Report on Form 10-K for the year ended December 31, 1977; File No. 1-3187H-1).
- 4(a)(3) - Twenty-Second Supplemental Indenture to Exhibit 4(a)(1) (Exhibit 2(d), File No. 2-62879).
- 4(a)(4) - Twenty-Third Supplemental Indenture to Exhibit 4(a)(1) (Exhibit 1 to HL&P's Annual Report on Form 10-K for the year ended December 31, 1978; File No. 1-3187H-1).
- 4(a)(5) - Twenty-Fourth Supplemental Indenture to Exhibit 4(a)(1) (Exhibit 1 to HL&P's Annual Report on Form 10-K for the year ended December 31, 1979; File No. 1-3187H-1).
- 4(a)(6) - Twenty-Fifth Supplemental Indenture to Exhibit 4(a)(1) (Exhibit 4.6, File No. 2-69854).
- 4(a)(7) - Twenty-Sixth Supplemental Indenture to Exhibit 4(a)(1) (Exhibit 4(b)(27) to HL&P's Annual Report on Form 10-K for the year ended December 31, 1980; File No. 1-3187H-1).

INDEX OF EXHIBITS (CONT'D)

- 4(a)(8) - Twenty-Seventh Supplemental Indenture to Exhibit 4(a)(1) (Exhibit (4)(b)(8) to HL&P's Annual Report on Form 10-K for the year ended December 31, 1981; File No. 1-3187H-1).
- 4(a)(9) - Twenty-Eighth Supplemental Indenture to Exhibit 4(a)(1) (Exhibit (4)(b)(9) to HL&P's Annual Report on Form 10-K for the year ended December 31, 1982; File No. 1-3187H-1).
- 4(a)(10) - Twenty-Ninth Supplemental Indenture to Exhibit 4(a)(1) (Exhibit 4(b)(10) to Houston Industries' Annual Report on Form 10-K for the year ended December 31, 1985; File No. 1-7629).
- 4(a)(11) - Thirtieth Supplemental Indenture to Exhibit 4(a)(1) (Exhibit T3C(11) to HL&P's Form T-3 For Applications for Qualification of Indentures Under the Trust Indenture Act of 1939, as filed with the SEC on February 2, 1987 ("Form T-3"); Registration No. 22-16489).
- 4(a)(12) - Thirty-First Supplemental Indenture to Exhibit 4(a)(1) (Exhibit T3C(12) to HL&P's Form T-3; Registration No. 22-16489).
- 4(a)(13) - Thirty-Second Supplemental Indenture to Exhibit 4(a)(1) (Exhibit 4(b)(13) to Houston Industries' Annual Report on Form 10-K for the year ended December 31, 1986; File No. 1-7629).
- 4(a)(14) - Thirty-Third Supplemental Indenture to Exhibit 4(a)(1) (Exhibit 4(a)(14) to Houston Industries' Annual Report on Form 10-K for the year ended December 31, 1987; File No. 1-7629).
- 4(a)(15) - Thirty-Fourth Supplemental Indenture to Exhibit 4(a)(1) (Exhibit 4(a)(15) to Houston Industries' Annual Report on Form 10-K for the year ended December 31, 1987; File No. 1-7629).
- 4(a)(16) - Thirty-Fifth Supplemental Indenture to Exhibit 4(a)(1) (Exhibit 4(a)(16) to Houston Industries' Annual Report on Form 10-K for the year ended December 31, 1987; File No. 1-7629).
- *12 - Computation of Ratio of Earnings to Fixed Charges and Earnings to Fixed Charges and Preferred Dividends.
- *24(a) - Consent of Independent Certified Public Accountants.

HL&P will furnish to the Securities and Exchange Commission upon request all constituent instruments defining the rights of holders of long-term debt of HL&P not filed herewith as permitted by paragraph (b)4(iii)(A) of Item 601 of Regulation S-K.

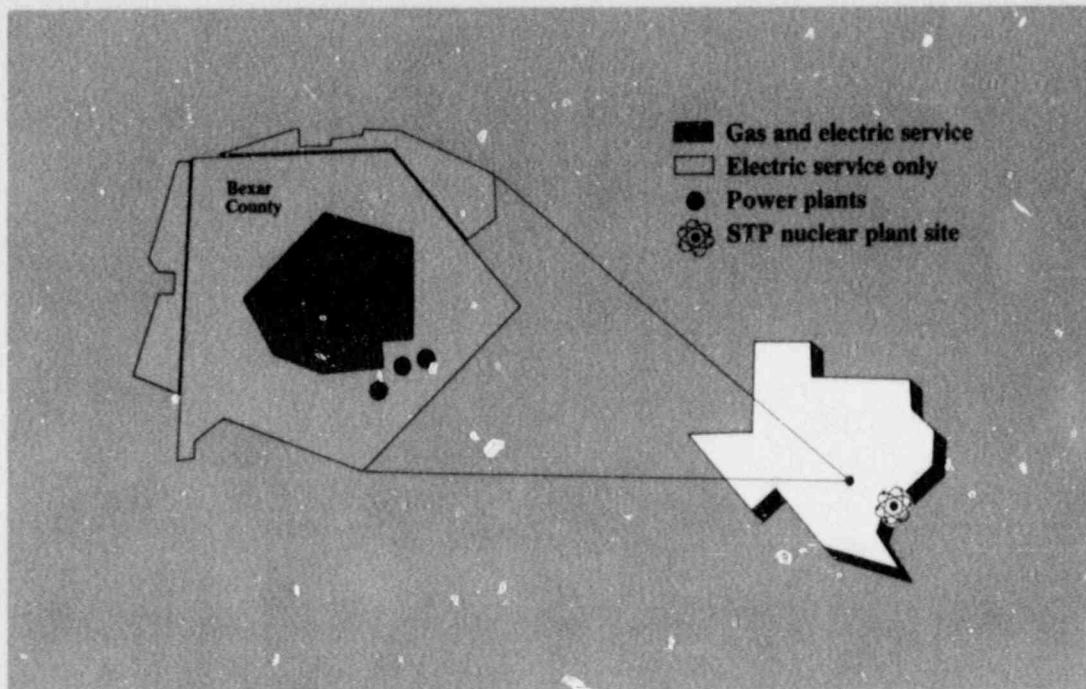


City Public Service
San Antonio's Natural Gas and Electric Utility

Annual Report - Fiscal Year Ended January 31, 1997



City Public Service



In San Antonio, the outlook remains optimistic, despite a regional economic slowdown attributed to declines in the petroleum industry. Although growth has been somewhat slower than a few years ago, the Alamo City continues to achieve steady economic progress and appears ready for further development as this decade draws to a close and the 1990s appear on the horizon.

The traditional mainstays of the San Antonio economy — services, the military and tourism — have been stabilizing influences while the community looks to diversify into areas such as biomedical technology. Meanwhile, multi-million-dollar projects under construction such as the Sea World of Texas marine life theme park, downtown's Rivercenter Mall (a large retail complex on the San Antonio River) and three new major hotels will steadily strengthen San Antonio's attractiveness as a tourist and convention center.

One of the keys to past and future progress is an adequate, reliable, cost-competitive energy supply. The job of providing vital day-to-day natural gas and electric service in San Antonio is readily accepted by City Public Service (CPS).

CPS meets the energy needs each day of historic, yet dynamically modern San Antonio.

Highlights of the Year

• Assets increased by \$485,154,000 to	\$3,639,018,000	
• City equity increased \$183,579,000 to	\$1,296,005,000	
• City payments were down \$7,781,000 to	\$ 96,191,000	
• Gross revenues decreased \$64,615,000 to	\$ 804,218,000	
• Maximum electric system load increased 246,000 KW to	2,596,000	
• 11,464 electric customers were added to total	458,037	
• 821 gas customers were added to total	285,697	
• 167 miles of electric transmission and distribution lines were added to total	8,262	
• 51 miles of gas mains were added to total	3,696	
• Amount of gas (MCF) saved through use of coal for generation	39,706,538	
• Purchase of fuel, power and gas declined \$81,163,000 to total	\$ 316,251,000	

Summary of Application of Revenue

Gross revenue for 1986-87 \$ 804,218,000

Application of Revenue:

Fuel, purchased power and resale gas	\$ 316,251,000
Other operating and general expenses	69,003,000
Maintenance of the systems	32,761,000
Operating fund	-
For debt requirements	\$218,407,000
Less interest charged to construction	<u>101,402,000</u>
Payments to the City of San Antonio	117,005,000
Balance from operations available for construction	<u>96,191,000</u>
Total	<u>173,007,000</u>
	\$ <u>804,218,000</u>

Amount spent for replacements, improvements and expansion of gas and electric systems	\$ 430,610,000
Amount provided for future construction	<u>57,853,000</u>
	\$ <u>488,463,000</u>

Funds obtained from:

Bond Funds	\$ 200,159,000
Operations	173,007,000
Contributions and advances in aid of construction	7,018,000
Sale of property	5,000
Tax Exempt Commercial Paper	78,274,000
Litigation Settlement Proceeds	<u>30,000,000</u>
Total	\$ <u>488,463,000</u>



City Public Service

ELECTRIC CUSTOMERS

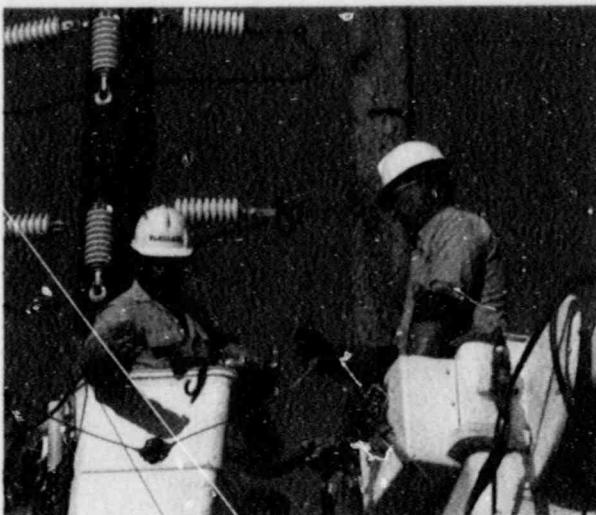
Thousands



CPS serves the nation's 10th largest city and outlying areas electrically with facilities throughout Bexar County and portions of seven adjoining counties — 1,566 square miles in all. Natural gas service is available in the San Antonio urban area.

The City of San Antonio has owned CPS since 1942 when it purchased the gas and electric systems by issuing \$33.9 million in revenue bonds. Almost a half-century later, CPS stands as one of the largest municipally-owned utilities in the country.

San Antonio's push forward is reflected both in installation of new electric and gas facilities and in increasing customer demand. The fiscal year which ended January 31 proved to be another solid year of progress in CPS operations.



Sea World of Texas is expected to draw more than three million visitors in the park's first year of operation. Above, CPS Linemen help prepare the site for construction.

The number of new electric customers was up 2.6% over the previous year as CPS made 11,464 additional connections to the electric system. While this figure is less than increases in each of the past two years, it is still a major influence on overall generation.

Total power generated and purchased in 1986-87 reached the 11 billion kilowatt-hour (KWH) mark, an increase of 3.8% over 1985-86. Summer temperatures in San Antonio helped produce a record peak demand of 2,596,000 kilowatts and a 24-hour consumption record of 46,048,300 KWH. The new peak represents an increase of 10.5% over the previous year.

The increase in new electric customers and their demand on the system, plus preparations for future development, required the installation of 167 miles of electric transmission and distribution lines. The total number of gas customers rose by 821 to 285,697, while gas main additions amounted to 51 miles, increasing the system total to 3,696 miles.

During San Antonio's recent growth, CPS has provided an adequate, reasonably-priced electric supply through fuels diversification. To continue this successful program, CPS has determined the electric system will need to add 1,000 megawatts (MW) of generating capacity by the late 1990s.

A combination of conservation and steady expansion of CPS' fuels base to include nuclear, additional Western coal and lignite is seen as the best approach for meeting future electric needs.

Coal, already a steady performer in CPS' fuels mix, satisfied 36.9% of San Antonio's 1986-87 electric requirements, a lesser percentage than in previous years. This is due to availability of less-expensive gas for generation, CPS purchase of 398.4 million KWH this year at a very favorable rate, and year-end modifications to CPS' coal-fired power plant which caused one unit to be unavailable during that time. Total fuel savings by burning coal as compared to higher-priced natural gas since Deely Plant went on line in 1978 have amounted to \$720.7 million. Reduced coal-hauling costs also saved ratepayers \$31 million compared to rates paid prior to a new transportation agreement with Western Railroad Properties Inc. and the Union Pacific System in 1985.

Furthermore, in January, the CPS Board of Trustees accepted a \$111.5 million settlement offer from former coal-haulers Burlington Northern (BN) and Southern Pacific (SP) railroads which ended a 10-year-old dispute over the transportation fees BN and SP charged CPS for moving coal from Gillette, Wyo., to San Antonio.

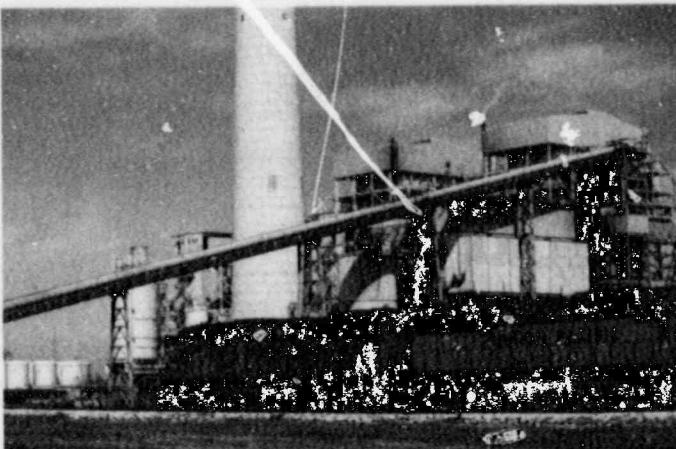
In March 1986, the Interstate Commerce Commission had ruled BN and SP violated a price provision in the Loeffler Amendment to the Staggers Rail Act of 1980 and thus overcharged CPS customers \$40 million. With interest, the ICC decision amounted to \$59 million. This decision covered only the period from October 1980 to March 1984 and CPS had filed with the ICC to cover a greater period of time. The railroads first appealed the ICC finding; however, after negotiating with CPS, the parties decided to settle the entire matter out of court. The \$111.5 million settlement is believed to be the largest of its kind in railroad transportation history.

An initial installment of \$31 million was used to reimburse CPS for an earlier payment to the railroads, plus interest, which had been required by a U.S. Supreme Court decision. That first installment also included certain legal fees relating to the railroad tariff case. The remaining \$80.5 million will be received in seven annual installments.



The price of a kilowatt-hour fell further in 1986-87 as natural gas prices for generation fuel declined to levels not seen since the mid-1970s. CPS was quick to take advantage of lower fuel costs by purchasing maximum permissible quantities of low-priced gas in accordance with its contractual agreement at prices as low as \$1.44 per thousand cubic feet (MCF). Also, due to competitive oil prices and availability of lower-cost energy on the interconnected electric grid system, CPS was able to obtain lower-cost gas for generation from subsidiary companies of Valero Energy Corporation, San Antonio's principal gas supplier. With the lower cost of natural gas, electric production from this fuel source accounted for 62.5% of total generation at a price competitive with coal. The lower overall fuel cost resulted in an 11.5% reduction in the residential cost per kilowatt-hour. Savings dependent on abundant, relatively low-priced gas may be short-lived as reports from energy industry analysts point to a probable turnaround and rising prices for natural gas in the future.

GROWTH IN PEAK DEMAND
Megawatt Hours



Reduced coal-hauling rates and a substantial settlement with CPS' former coal-hauler produced savings to customers.



Coal has proven to be a wise investment for San Antonio. At CPS' Environmental Lab near the utility's coal plant, constant tests help assure coal is environmentally sound for the city.



City Public Service



Despite possible increases in gas costs, CPS should be able to maintain stable electric rates by burning coal and again expanding its fuel mix to include nuclear energy from the South Texas Project (STP) power plant near Bay City on the Texas coast. CPS and three other utilities — Houston Lighting & Power, Central Power and Light of Corpus Christi and the City of Austin — are co-owners of the Project.

San Antonio also is counting on kilowatts from STP to help meet the projected increase in electric demand. At year's end, the Project was within budget and ahead of schedule, with Unit 1 at 97.9% complete, Unit 2 at 71.4% complete and the overall plant at 86.8% complete. Good construction progress during the year plus favorable Nuclear Regulatory Commission (NRC) findings helped prepare the Project for expected final licensing review in summer 1987.

In the first half of 1986, the NRC issued favorable inspection reports dealing with STP construction, safety and environmental impact. All of the voluminous studies found the Project can operate "without endangering the health and safety of the public."



Meeting and surpassing construction schedules brought favorable reports from STP in 1986.

In August, STP took a giant step closer to an operating license as the Atomic Safety and Licensing Board (ASLB) issued a 300-page report stating STP can be completed properly and operated safely. The ASLB document also brought STP licensing hearings to a close.

Major testing of Unit 1 is scheduled for the first quarter of 1987. Fuel load and further testing is then slated for the summer, and commercial operation of the first of STP's twin 1,250-MW units should commence in December. Unit 2 is still on track for commercial operation by mid-1989.

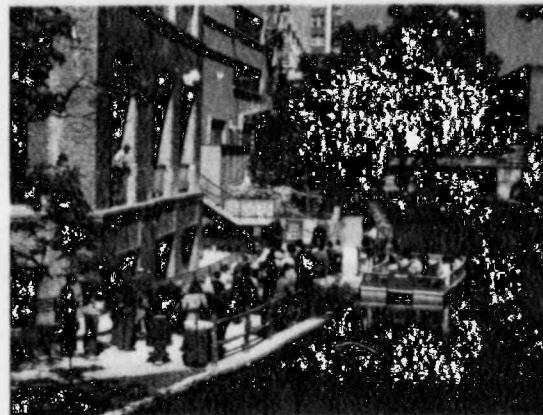
In conjunction with the 700 MW of power from the South Texas Project, CPS planners have identified the need for additional generation capacity by 1992 to keep pace with growing electric demand. In the last five years, CPS has added almost 103,000 new electric customers and 685,000 KW to its peak load. New customer projections for the next five years are in the 15,000 to 18,000 per year range and represent a steadily increasing need for more electric energy.

The CPS staff recommendation for a new 500-MW coal unit to help meet capacity requirements came after many months of study comparing numerous alternatives such as lignite and cogeneration as well as factoring in the effects of conservation. The coal option became the clear choice because of projected reductions in rail transportation costs with increased tonnage, lower market cost for Western coal, plus the fact that coal-handling facilities, water and a site already exist at CPS' present coal-fired plant.

CPS has not abandoned lignite and cogeneration possibilities, but revised their priority for consideration into the longer-range energy plan. Lignite reserves, which will continue to be acquired as they become available near current holdings in the Bastrop-Elgin area 100 miles northeast of San Antonio, are expected to be needed around the turn of the century. Cogeneration available to CPS, most of it natural gas-produced, likely will not be counted on in any large measure so long as other forms of energy continue to be less expensive.



CPS' Main Office renovation added necessary office space for utility operation and attractive enhancement to the famed San Antonio Riverwalk.



CPS and City of San Antonio Public Works staff members continued to study another possibility — a refuse-to-electricity project. Although the incineration of garbage would reduce the need for expensive city landfill sites, only slightly more than 1% of CPS' needs, or 36 MW of power, would be generated. The utility and the city are continuing to study whether the \$150 million project can benefit both CPS ratepayers and the community.

As part of its ongoing effort to improve service to customers, City Public Service upgraded and added to current facilities during the year.

The CPS Main Office renovation concluded after two years of construction. CPS' 59-year-old headquarters now has two new floors and a lower floor at river level of additional office space. In addition to providing a more productive work atmosphere, the renovation features energy efficiency enhancements and an overall reorientation of the building toward the scenic downtown River Walk along the San Antonio River.

Upgrading of CPS' downtown facilities will continue, as Trustees authorized the purchase of the Navarro Parking Garage across from the Main Office. A ground level section beneath the garage currently houses CPS' main Customer Service Center, which will be renovated. In addition, three new floors of office space atop



the garage will be added along with customer parking and a skybridge connecting the garage to the Main Office. With this new addition, current lease space in an adjoining building will be eliminated.

During the year, CPS opened its third neighborhood Customer Service Center to provide for greater customer convenience. In its first year of operation, the new Westside Center posted the second-highest number of customer transactions, surpassed only by the downtown Center.

Customer convenience also took on a new look as CPS developed a new design for gas and electric bills. The improved bill format allows room for more customer information which provides a better understanding of daily energy use. A team of CPS employees researched, designed and implemented the new blue and white bill form.



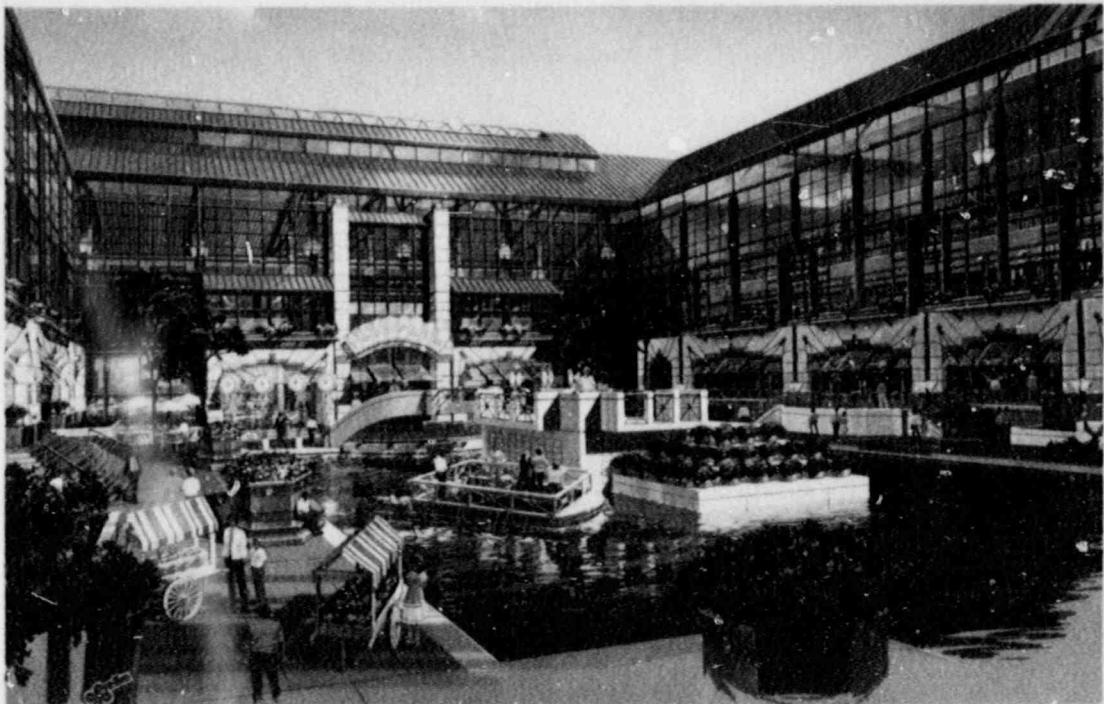
City Public Service

Three other projects begun in 1986-87 will mean major improvements to the electric and gas systems.

At the coal-fired Deely Power Plant located in southeast Bexar County, a \$24-million precipitator conversion project got underway. The electrostatic precipitators, which collect fly ash after coal combustion, will become more efficient and better able to meet environmental standards set forth by local, state and federal agencies. Furthermore, the conversion will eliminate costly plant shutdowns to remove accumulated ash. These shutdowns in the past have necessitated the substitution of more expensive fuels in electric production.

In the downtown area, the upgrading of the 10th Street Substation neared completion to handle power requirements of central San Antonio's growth. 10th Street serves about four and one-half square miles of the downtown area including Rivercenter Mall, new hotels and Hemisfair Plaza. CPS personnel designed, engineered and constructed all phases of the 10th Street project.

To the north in CPS' service area, the gas distribution system is in the process of obtaining a third major supply point. A 12.9-mile, 24-inch diameter pipeline will be constructed to tie into Valero Energy's pipeline in northern Bexar County. The \$8.5 million project should be completed next year and will bolster the gas system's reliability.



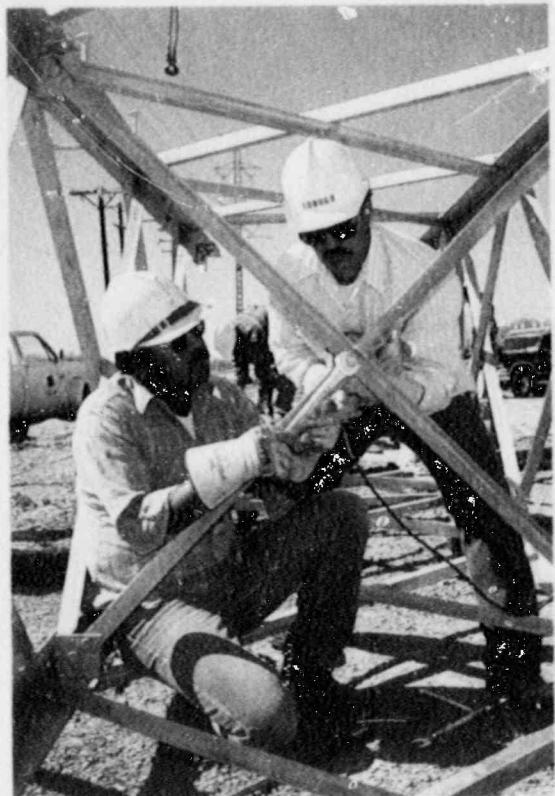
Just as these three major construction jobs will provide greater operating efficiency, other CPS initiatives this past year saved customers millions of dollars.

Two advance refunding bond issues totaling \$712.4 million will save \$130.0 million in interest for CPS customers over the next two and a half decades. During the early 1980s, capital improvements bonds were sold at various, higher-interest rates to pay for ongoing construction. CPS took advantage of favorable market conditions to refund bonds with rates as high as 11.25% and substantially reduced interest

payments over the life of the bonds. The two refunding issues accomplished in 1986-87 plus an additional refunding in the previous fiscal year will mean total interest savings of \$139.4 million by the year 2014.

Saving energy dollars for San Antonio is an important objective in CPS' day-to-day activities, and that conservation message is relayed to customers through numerous programs.

City Public Service's Consumer Information Division made more than 95,000 contacts in the community this past year emphasizing the safe and efficient use of gas and electricity. The contacts included Home Energy Surveys; school, business and community service presentations; and more than 50,000 telephone inquiries.



On the opposite page, Rivercenter Mall is a healthy economic addition for downtown San Antonio. Scenes for various construction projects on this page demonstrate the Alamo City's continued outer-city growth.



ELECTRIC REVENUE PER KWH

Cents Per KWH





City Public Service

A new type of energy survey was also initiated in 1986 to help area farmers and ranchers manage their energy consumption more efficiently. The Rural and Agricultural Audit Program (RAAP) is designed to assess the specialized energy usage patterns of farms and ranches and suggest methods for controlling energy costs. CPS' agribusiness energy audit program was the first of its kind in Texas.

Wise use of natural gas and electricity applies not only to energy efficiency but also to safety. CPS' Public Safety Awareness programs were presented to schools, civic and social organizations, as well as City of San Antonio and area fire departments.

CPS employees not only demonstrated their technical competence but also their community support by contributing more than a quarter of a million dollars to the 1986 United Way campaign. Per capita giving was up 8.8% as both active and retired employees helped make 1986 the most successful year of United Way giving in CPS history. Without the cooperation and dedication of its work force, CPS would be unable to accomplish its essential mission of service.





CPS Trustees and management staff also distinguished themselves both locally and nationally.

Board member Mayor Henry Cisneros completed a productive term as National League of Cities (NLC) president. San Antonio hosted the NLC National convention which brought together municipal leaders from around the nation.

CPS Board Chairman Glenn Biggs concluded the second longest tenure as a Trustee in CPS' 44-year history. Biggs, a member of the Board for almost 13 years and Chairman the past seven years, was instrumental in helping guide CPS during the stormy aftermath of the 1970s energy crisis.

Board Vice Chairman Earl C. Hill succeeded Biggs as Chairman, and Trustee Mrs. Lila Cockrell moved up to the post Hill vacated. Mrs. Cockrell also was elected to her second five-year term on the Board.

CPS' commitment to gas and electric safety brings utility personnel in contact with thousands of San Antonians every year.

At the staff level, Assistant General Manager for Operations Jesse B. Poston retired after 38 years of service with CPS. Poston led an engineering team which introduced many technological improvements to CPS and also served as San Antonio's principal representative to the South Texas Project.

CPS General Manager J.K. Spruce, a past president of the American Public Power Association (APPA), was named local arrangements chairman for the organization's 1987 National Conference in San Antonio. More than 2,000 utility officials from the U.S. and Canada discussed the challenges and consumer benefits of public power. City Public Service was honored to be the host utility and serves as a good example of a city-owned utility working for community progress. For, as the record indicates, CPS met the 1986-87 energy challenges of this growing metropolitan area and kept consumer costs among the lowest in the state and nation. As for the future, CPS' outlook continues to be optimistic.

Sincerely,

Glenn Biggs
Chairman, Board of Trustees

J.K. Spruce
General Manager

ANNUAL RESIDENTIAL ELECTRIC USE

Kilowatt Hours





City Public Service

1986-87 Financial Review

The cost of fuel for electric generation continued to decline in fiscal year 1986-87. The average cost of coal fell 6% to \$29.38 per ton compared to \$31.23 last January. With the purchase of more than 22% of generation gas at spot market prices, the average cost of gas declined 38% to \$2.17 per MCF, as compared to \$3.48 last year. Overall, electric generation fuel costs dropped 27% when all fuel sources are considered.

A CPS record was set on August 19, 1986, when a system hourly peak of 2,596 MW was reached, eclipsing the 1985-86 mark of 2,350 MW. Electric generation totaled 10.6 million MWH, about the same as the previous fiscal year. However, an additional 398 million KWH was purchased, and when combined with generation, power available for sale rose 3.8%. Natural gas provided fuel for 62.5% of the electric generation due to the availability of low priced spot gas. This is the largest percentage of electricity fueled by natural gas since 1977-78. Electric generation from CPS' coal-fuel power plants provided 36.9% of requirements, with the balance of 0.6% from fuel oil.

CPS customers will realize \$130.0 million in interest savings from the \$320.6 million in refunding bonds delivered in March 1986, and \$391.8 million which were priced in January and delivered in February 1987. These bonds, which were sold at interest rates of 7.835% and 6.837% respectively, replace bonds bearing interest costs of 8.9% to 11.25%. In addition, \$185 million in AA rated bonds were issued in July 1986, at an average rate of 8.765% to finance ongoing construction.

At the end of fiscal year 1986-87, CPS' total assets exceeded \$3.63 billion, increasing \$485 million, or 15%, over last year. Utility plant stood at \$1.48 billion, a 7% increase over fiscal year 1985-86. Construction Work in Progress rose to \$1.78 billion, with the South Texas Project (STP) accounting for 96%, or \$1.70 billion, of this total. Outstanding revenue bonds totaled \$2.04 billion, with an average interest rate of 8.2% (excluding the 1987 Refunding Bonds). The City of San Antonio equity in CPS increased to \$1.3 billion, growing 17% in fiscal year 1986-87.

CPS had record electric sales of nearly 10.4 billion KWH in fiscal year 1986-87. This was up 326.8 million KWH, or 3.3%, over last year. The average use per residential customer exceeded the 10,000 KWH mark for the first time and was up 2.1% over last year; however, lower use per customer by commercial and industrial customers caused overall use per customer to decline by 1.1%. The number of electric customers stood at 458,037 at year end. Total residential electric sales rose 6.7% while commercial and industrial sales rose 3.8%. Gas sales of 25.0 million MCF decreased 4.9%, or 1.3 million MCF. Although there was a small increase in the number of gas customers, usage per customer declined 5.8%. Sales to all classes of gas customers fell, with residential sales declining 5.3%.

FUELS & PURCHASED POWER

Millions of Dollars



Gross revenues for fiscal year 1986-87 totaled \$804.2 million, and were \$64.6 million, or 7.4%, lower than the previous year. Electric revenues of \$639.6 million dropped \$60.7 million, or 8.7%, and gas revenues of \$127.8 million fell \$8.7 million, or 6.4%. A \$112.3 million decline in fuel cost recoveries was partly offset by \$25.8 million from greater sales and \$22.3 million in added revenue from the January 1986, rate increase. Interest and other non-operating income rose 15.1%, or \$4.8 million, to \$36.8 million.

Both electric and gas operating expenses declined sharply. Electric operating expenses declined \$73.1 million, or 19.4%, to \$303.3 million, as production fuel was \$83.8 million lower than last year. Partially offsetting were purchased power costs which increased \$8.1 million and electric distribution expenses which were up \$3.1 million. Gas operating expenses declined to \$113.2 million, a \$5.0 million, or a 4.2%, drop from fiscal year 1985-86. Resale gas expense decreased \$5.5 million due to 1.3% less gas being purchased at lower prices. The average price of resale gas dropped to \$3.52 per MCF from \$3.69. Depreciation expense was \$1.5 million, or 3.6%, higher than last year and totalled \$41.8 million. Net electric and gas

operating revenue advanced \$6.5 million, or 2.2%, to \$301.3 million.

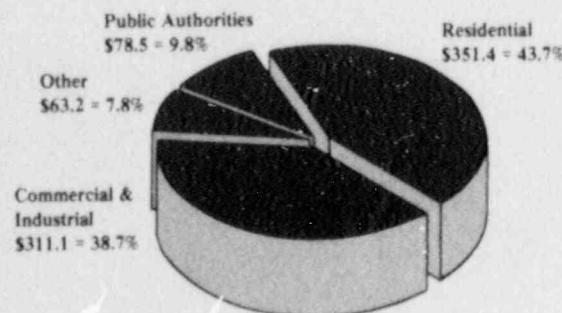
Construction expenditures of \$430.6 million were down 1% from last year, as completion of STP nears. Expenditures for San Antonio's share of STP amounted to \$322.3 million, or 75%, of the total capital expenditures. Long-term debt was used to finance 46.5% of the capital program, while 26.8% was from internally generated funds. Proceeds from the Brown and Root litigation settlement, Tax Exempt Commercial Paper Program and customer contributions provided the balance of construction funds.

Net interest and debt expense increased \$6.9 million to \$64.6 million. Interest on long-term debt climbed to \$160.8 million, up 12% over last year; however, the Allowance for Funds Used for Construction of \$101.4 million reduced interest chargeable to operations to \$59.4 million. Amortization of debt expense was \$3.3 million higher, as issue costs for the Refunding Bonds were included.

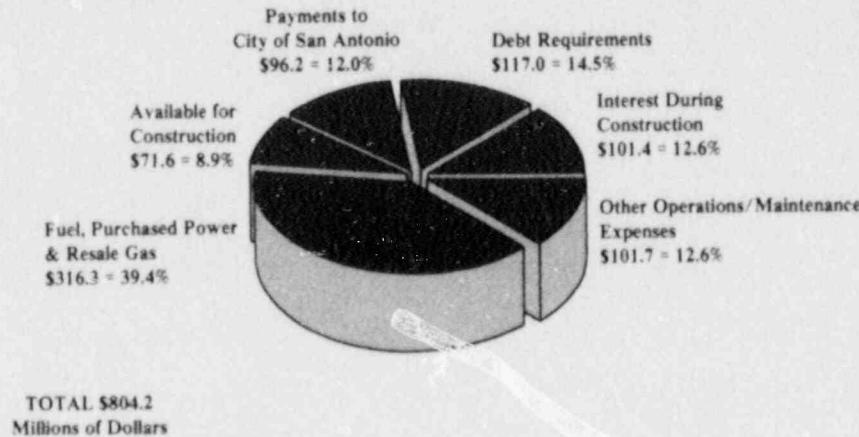
Benefits and payments to the City of San Antonio decreased \$7.8 million, or 7.5%, to \$96.2 million, and represented 12.0% of gross revenue. Reduced benefits were the direct result of lower fuel costs achieved during the year.

CPS REVENUES

Sources



Distribution





City Public Service

Balance Sheets January 31, 1987 and 1986

ASSETS

	Notes	1987	1986
		(in thousands)	
UTILITY PLANT — At cost:			
Electric	1	\$1,221,198	\$1,168,943
Gas		196,620	184,559
General		60,956	28,390
Construction work in progress	7	1,675,726	1,361,134
Nuclear fuel in process	7	100,979	95,821
Total utility plant		3,255,479	2,838,847
Less accumulated depreciation		446,913	418,743
Utility plant — net		<u>2,808,566</u>	<u>2,420,104</u>
 RESTRICTED CASH (Temporary cash investments and U.S. Government obligations — at cost which approximates market):	 2		
Bond Construction Fund		41,335	65,678
Bond Reserve — Old Series Bonds	3	17,353	17,437
Bond Reserve — New Series Bonds	3	173,786	147,715
Improvements and Contingencies Fund		131,439	73,586
Other	1	5,150	8,123
Total restricted cash		<u>369,063</u>	<u>312,539</u>
 CURRENT ASSETS:			
Cash, including temporary cash investments		19,045	22,362
Short-term investments	4	-	51,724
Customer accounts receivable, less allowance for doubtful accounts of \$1,222,000 in 1987 and \$1,151,000 in 1986		54,947	51,233
Other receivables	8	42,352	33,337
Inventories and supplies — at average cost:			
Materials and supplies		20,642	18,647
Fuel stock		42,089	33,644
Prepayments and other	8	1,859	27,964
Total current assets		<u>180,934</u>	<u>238,911</u>
 LITIGATION SETTLEMENTS BENEFITS RECEIVABLE	 7,8	 <u>205,500</u>	 <u>165,000</u>
 DEFERRED DEBITS	 1	 <u>74,955</u>	 <u>17,310</u>
 TOTAL		 <u>\$3,639,018</u>	 <u>\$3,153,864</u>

See notes to financial statements.

LIABILITIES

	Notes	1987	1986
		<i>(in thousands)</i>	

LONG-TERM DEBT — Revenue Improvement Bonds:	2,3		
Old Series		\$ 105,785	\$ 115,220
New Series		1,903,425	1,676,500
Less: Unamortized discount on New Series Bonds		<u>(20,812)</u>	<u>(11,530)</u>
Net long-term debt		<u>1,988,398</u>	<u>1,780,190</u>

EQUITY:

Appropriated retained earnings:	2		
Bond Reserve — Old Series Bonds		17,353	17,437
Bond Reserve — New Series Bonds		121,328	101,216
Improvements and Contingencies Fund		<u>131,439</u>	<u>73,586</u>
Total		<u>270,120</u>	<u>192,239</u>
Reinvested earnings		<u>1,025,885</u>	<u>920,187</u>
Total equity		<u>1,296,005</u>	<u>1,112,426</u>

CURRENT LIABILITIES:

Current maturities of long-term debt	3	34,820	32,350
Short-term debt	4	100,000	100,000
Accounts payable and accrued liabilities		<u>61,610</u>	<u>55,492</u>
Litigation settlement benefits payable to customers	8	<u>834</u>	<u>-</u>
Customer service deposits		<u>14,079</u>	<u>10,984</u>
Total current liabilities		<u>211,343</u>	<u>198,826</u>

DEFERRED CREDITS:

Customer advances for construction		14,751	12,976
Other		<u>1,965</u>	<u>6,340</u>
Total deferred credits		<u>16,716</u>	<u>19,316</u>

LITIGATION SETTLEMENT BENEFITS PAYABLE	8	79,666	-
--	---	--------	---

CONTRIBUTIONS IN AID OF CONSTRUCTION	1	46,890	43,106
--	---	--------	--------

COMMITMENTS AND CONTINGENCIES	5,7,8	-	-
-------------------------------------	-------	---	---

TOTAL		<u>\$3,639,018</u>	<u>\$3,153,864</u>
-------------	--	--------------------	--------------------

See notes to financial statements.



City Public Service

Statements of Earnings and Application of Earnings

	Notes	Years ended January 31,	
		1987	1986
		(in thousands)	
REVENUE:		1	
Electric		\$639,626	\$700,371
Gas		127,814	136,500
Interest and other income		36,778	31,962
Gross revenue		<u>804,218</u>	<u>868,833</u>
EXPENSES:		1	
Fuel, purchased power and resale gas		316,251	397,414
Other operating and general		68,998	65,035
Maintenance		32,761	33,379
Depreciation		41,811	40,351
Interest and debt expense		166,029	144,989
Allowance for interest used during construction		(101,402)	(87,296)
Payments to the City of San Antonio	6	<u>96,191</u>	<u>103,972</u>
Total expenses		<u>620,639</u>	<u>697,844</u>
NET EARNINGS:		183,579	170,989
Add:			
Depreciation		41,811	40,351
Interest requirements on New Series Bonds (payable from Improvements and Contingencies Fund)		153,411	135,235
AVAILABLE FOR APPLICATION		<u>\$378,801</u>	<u>\$346,575</u>
APPLICATION:			
To pay long-term debt requirements —			
Old Series Bonds:			
Principal payments		\$ 9,000	\$ 8,600
Bond reserve		(84)	(46)
To reinvested earnings — Net gain on sale of assets		5	4
To Improvements and Contingencies Fund:			
Minimum requirement (12½% of gross revenue)	2	100,527	108,604
Balance of available revenue		269,353	229,413
APPLICATION		<u>\$378,801</u>	<u>\$346,575</u>

See notes to financial statements.

Statements of Changes in Equity

	Years ended January 31,	
	1987	1986
	(in thousands)	
BOND RESERVE — OLD SERIES BONDS:		
Balance, beginning of year	\$ 17,437	\$ 17,483
Deductions — transfer of earnings	(84)	(46)
Balance, end of year	<u>\$ 17,353</u>	<u>\$ 17,437</u>
BOND RESERVE — NEW SERIES BONDS:		
Balance, beginning of year	\$ 101,216	\$ 89,713
Additions — from Improvements and Contingencies Fund	20,112	11,503
Balance, end of year	<u>\$ 121,328</u>	<u>\$101,216</u>
IMPROVEMENTS AND CONTINGENCIES FUND:		
Balance, beginning of year	\$ 73,586	\$ 80,068
Additions — from application of earnings:		
Minimum requirement (12½% of gross revenue)	100,527	108,604
Balance of available revenue	269,353	229,413
Total	<u>443,466</u>	<u>418,085</u>
Deductions:		
New Series Bonds:		
Additions to reserve	20,112	11,503
Payment of bond interest	153,411	135,235
Payment of bond principal	23,350	21,440
Construction expenditures	115,154	173,821
For working capital	-	2,500
Total	<u>312,027</u>	<u>344,499</u>
Balance, end of year	<u>\$ 131,439</u>	<u>\$ 73,586</u>
REINVESTED EARNINGS:		
Balance, beginning of year	\$ 920,187	\$754,173
Additions:		
From Improvements and Contingencies Fund:		
For construction	115,154	173,821
For New Series Bonds principal payments	23,350	21,440
For working capital	-	2,500
From application of earnings:		
Old Series Bonds principal payments	9,000	8,600
Net gain on sale of assets	5	4
Total	<u>147,509</u>	<u>206,365</u>
Deduction — Depreciation	<u>41,811</u>	<u>40,351</u>
Balance, end of year	<u>\$1,025,885</u>	<u>\$920,187</u>

See notes to financial statements.



City Public Service

Statements of Changes in Financial Position

Years ended January 31,
1987 1986
(in thousands)

SOURCES OF FUNDS:

	\$ 183,579	\$ 170,989
Net earnings.....	<u>183,579</u>	<u>170,989</u>
Add (deduct) amounts not affecting working capital:		
Amortization of New Series Bond discount.....	1,081	536
Amortization of deferred debts.....	4,140	1,461
Depreciation.....	41,811	40,351
Allowance for interest used during construction.....	<u>(101,402)</u>	<u>(87,296)</u>
Working capital provided from operations.....	129,209	126,041
Contributions in aid and customer advances for construction.....	7,018	7,735
Sale of revenue improvement bonds.....	181,772	270,202
Sale of refunding bonds.....	310,242	113,301
Litigation settlement.....	111,500	210,000
Other.....	<u>-</u>	<u>1,281</u>
Total.....	<u>739,741</u>	<u>728,560</u>

APPLICATION OF FUNDS:

Acquisition of utility plant — net of allowance for interest used during construction.....	329,208	347,764
Increase in other receivable.....	40,500	165,000
Retirement of bonds.....	32,350	30,040
Defeasance of bonds refunded.....	253,350	97,130
Increase in current maturities of long-term debt.....	2,470	2,310
Increase in restricted cash.....	56,524	59,821
Litigation settlement received.....	31,000	-
Excess of reacquisition amount over principal of bonds refunded in advance.....	57,649	15,978
Other.....	<u>7,184</u>	<u>498</u>
Total.....	<u>810,235</u>	<u>718,541</u>

INCREASE (DECREASE) IN WORKING CAPITAL

\$ (70,494) \$ 10,019

CHANGES IN WORKING CAPITAL COMPONENTS:

Increase (decrease) in current assets:		
Cash and temporary investments.....	\$ (3,317)	\$ (7,569)
Short-term investments.....	(51,724)	(21,874)
Customer accounts receivable.....	3,714	(4,405)
Other receivables.....	9,015	28,458
Inventories and supplies.....	10,441	679
Prepayments and other.....	(26,106)	222
Decrease (increase) in current liabilities:		
Current maturities of long-term debt.....	(2,470)	(2,310)
Accounts payable and accrued liabilities.....	(6,118)	10,894
Litigation settlement benefits payable to customers.....	(834)	7,660
Customer service deposits.....	(3,095)	(1,736)
INCREASE (DECREASE) IN WORKING CAPITAL	<u>(70,494)</u>	<u>10,019</u>
WORKING CAPITAL, BEGINNING OF YEAR	<u>40,085</u>	<u>30,066</u>
WORKING CAPITAL (DEFICIT), END OF YEAR	<u>\$ (30,409)</u>	<u>\$ 40,085</u>

See notes to financial statements.

Notes to Financial Statements — January 31, 1987 and 1986

1. Summary of Significant Accounting Policies

Basis of Accounting — City Public Service (CPS) uses the accrual method of accounting based upon the Uniform System of Accounts for Gas and Electric Utilities issued by the National Association of Regulatory Utility Commissioners.

Fiscal Year — The fiscal year ended January 31, 1987, is referred to herein as 1987 and the year ended January 31, 1986, as 1986.

Revenues and Expenses — Revenue is recognized as billed on a cycle basis. Rate schedules include fuel and gas cost adjustment clauses that permit recovery of fuel and gas costs in the month incurred. CPS charges to expense the cost of electric production fuel as it is consumed and the cost of resale gas at the time of purchase.

Utility Plant — These assets are stated at the cost of construction, including costs of contracted services, direct material and labor, indirect costs, including general engineering, labor and material overhead, and an allowance for interest used during construction ("AIUDC"). CPS computes AIUDC using rates representing the cost of borrowed funds on projects estimated to cost in excess of one million dollars and expected to require more than one year to complete. Retirements of utility plant, together with removal cost less salvage, are charged to accumulated depreciation. The maintenance of property, and replacement and renewals of items determined to be less than a unit of property, are charged to maintenance expense. General utility plant assets consist of land, buildings and equipment for general and administrative purposes that are used commonly in electric and gas operations.

CPS computes depreciation principally using the straight-line method over the estimated service lives of the assets as determined by periodic engineering studies. Depreciation as a percentage of average depreciable plant was 3.07% in 1987 and 3.16% in 1986.

Contributions in aid of construction are amortized over a period equal to the lives of the related assets.

Other Restricted Cash — These amounts consist primarily of funds being held in escrow as required under a contract with a gas supplier.

Deferred Debits — These amounts consist of the unamortized balance of bond issue expense, and the unamortized excess of the reacquisition amount over the revenue bond principal refunded in advance. Amounts are being amortized over the period during which the bonds will be outstanding.

2. Revenue Bond Indenture Requirements

The Trust Indenture executed by the City of San Antonio (the "City") in conjunction with the issuance of the revenue bonds dated February 1, 1951 through August 1, 1974, "Old Series Bonds," contains, among others, the following provisions:

- 1) All of the assets of the gas and electric systems, together with the net revenues of the systems, as defined, are pledged with the Harris Trust and Savings Bank of Chicago, Illinois, as Corporate Trustee, to secure the payment of the "Old Series Bonds."
- 2) Gross revenues of the gas and electric systems shall be applied to: (a) expenses of operating and maintaining the systems; (b) debt service and reserve requirements on the "Old Series Bonds"; (c) payment of an "in lieu of tax" amount to the City; (d) an amount equal to 12½% of gross revenues to the Improvements and Contingencies Fund; (e) additional benefits and payments to the City to bring City benefits and payments to 14% of gross revenues; (f) additional payments to the Improvements and Contingencies Fund until such fund equals 20% of the value of fixed capital assets; and (g) balance to a surplus fund.
- 3) The following funds are established: (a) General Fund; (b) Improvements and Contingencies Fund; (c) Bond Construction Fund (containing the proceeds of revenue bonds); (d) Principal and Interest Current Requirements (containing the monthly payments of annual debt requirements); and (e) Bond Reserve Fund (containing an amount equal to the next fiscal year's principal and interest requirements). These funds may be invested with authorized depository banks or in U.S. Government securities.

Beginning with the year ended January 31, 1976, New Series Electric and Gas Systems Revenue Improvement Bonds ("New Series Bonds") were issued. These bonds are junior and subordinate to the "Old Series Bonds." The bond ordinances authorizing these issues provide that no further bonds or obligations will be authorized or issued under the terms of the Trust Indenture for "Old Series Bonds" and, at such time as the Trust Indenture becomes inoperative, the Trust Estate will revert to the City. While any of the "Old Series Bonds" are outstanding, the "New Series Bonds" are payable solely from the net revenues of the systems (1) deposited and available for deposit in the Improvements and Contingencies Fund and (2) from funds payable to the City. At such time as the Trust Indenture covering the "Old Series Bonds" becomes inoperative, revenues will be applied as follows: (a) for maintenance and operating expenses of the systems; (b) for payments of the "New Series Bonds"; (c) for the payment of any obligations inferior in lien to the "New Series Bonds" which may be



City Public Service

Notes to Financial Statements

issued; (d) for an amount equal to 6% of the gross revenues of the systems to be deposited in a Repair and Replacement Fund; (e) for cash payments and benefits to the City not to exceed 14% of the gross revenues of the systems; and (f) any remaining revenues to the Repair and Replacement Fund. The funds created by the "New Series Bonds" ordinance are similar to those set forth under the "Old Series Bonds" Trust Indenture.

3. Long-Term Debt

A summary of long-term debt is as follows:

	Final Maturity	Weighted-Average Interest Rate On Outstanding Bonds	Unpaid Principal	
			1987	1986 (in thousands)
Old Series, 1962-1974	1988-1997	6.33%	\$ 115,220	\$ 124,220
New Series, 1975-1986	1998-2014	8.24%	1,928,810	1,699,850
Total		8.20%	2,044,030	1,824,070
Less current maturities			34,820	32,350
Amounts due after one year			\$2,009,210	\$1,791,720

Principal due (in thousands) for the next five years are:

	Principal Due	
	Old Series Bonds	New Series Bonds
1988	\$ 9,435	\$25,385
1989	9,905	27,535
1990	10,375	38,725
1991	10,945	42,120
1992	11,500	45,850

As of January 31, 1987, bond reserve requirements for the Old Series Bonds and New Series Bonds have been met. Additional bond reserve requirements of \$6.0 million for the New Series 1986-A Bonds, were included in the amount borrowed and were deposited in the Bond Reserve restricted cash fund in a lump sum in 1987. Similarly, additional bond requirements of approximately \$18.8 million for the New Series 1985-A and 1985-B Bonds were deposited in the Bond Reserve restricted cash fund in a lump sum in 1986. Prior to the 1983-A Bonds, reserve requirements were generated from earnings and deposited over a 61-month period as previously allowed; beginning with the 1983-A Bonds, Bond Reserve requirements have been funded from bond proceeds.

During the fiscal year ended January 31, 1987, New Series 1983-A Bonds at coupon rates of 10.4% to 10.5%, New Series 1984-A Bonds at coupon rates of 11.0% to 11.25% and New Series 1984-B Bonds at coupon rates of 10.75% to 11.125% in the principal amounts of \$79,350,000, \$91,400,000 and \$82,600,000, respectively, were advance refunded by issuance of \$320,660,000

New Series 1986 Revenue Refunding Bonds. Although the advance refunding resulted in reacquisition amounts in excess of the bond principal amounts refunded of approximately \$61,358,000, the issuance of refunding debt at interest rates lower than the previous rates will cause aggregate debt service payments to be reduced by approximately \$56,283,000. United States Government securities were purchased with the net proceeds of the 1986 issue and deposited in an irrevocable trust to satisfy scheduled principal and interest payments of the refunded issues. The refunded bond issues and trust accounts of the New Series 1986 Refunding Bonds as well as previous refundings are not included in CPS financial statements. At January 31, 1987, the following portions of each respective bond series are considered defeased:

New Series 1984-A	\$91,400,000
New Series 1984-B	82,600,000
New Series 1983-A	79,350,000
New Series 1982	48,145,000
New Series 1981-A	48,985,000

During January 1987, the City of San Antonio approved the issuance of New Series 1987 Refunding Bonds in an amount of \$391,780,000 to be delivered on or about February 19, 1987. The proceeds from the bonds will be used to advance refund \$48,025,000 principal amount of New Series 1980 Bonds, \$34,825,000 principal amount of New Series 1980-A Bonds, \$32,675,000 principal amount of New Series 1981 Bonds, \$44,620,000 principal amount of New Series 1982-A Bonds, \$8,300,000 principal amount of New Series 1984-A Bonds, \$12,500,000 principal amount of New Series 1984-B Bonds, \$109,800,000 principal amount of New Series 1985-A Bonds, and \$38,125,000 principal amount of New Series 1985-B Bonds and to pay costs and expenses related to the issuance of the New Series 1987 Bonds. Although the advance refunding resulted in reacquisition amounts in excess of the bond principal amounts refunded of approximately \$59,489,000, the issuance of refunding debt at interest rates lower than the previous rates will cause aggregate debt service payments to be reduced by approximately \$73,698,000. Also during January 1987 the City of San Antonio gave notice of its intention to issue New Series 1987-A Bonds in an amount of \$160,000,000 to be delivered on or about March 26, 1987. The proceeds from the bonds will provide funds for the purposes of improving and extending the electric and gas systems of the City.

4. Short-Term Debt

In November, 1983, the City Council of the City of San Antonio authorized the issuance of \$100 million in tax-exempt commercial paper (the "Commercial Paper") to assist in the financing of eligible projects, including fuel acquisition and capital improve-

ments to the utility systems (the "Systems"). As of January 31, 1987, \$100 million in principal amount was outstanding, with a weighted average interest rate of approximately 3.85% and an average life outstanding of about 65 days. When available, proceeds remaining from the Commercial Paper have been placed in short-term investments consisting of U.S. Government obligations at cost, which approximates market. During 1987, all remaining proceeds were used for construction purposes.

The Commercial Paper is equally and ratably payable from and is secured by (i) the Net Revenues of the systems and (ii) a lien on the sale and pledge of the proceeds from the sale of other Commercial Paper, the subsequent sale of bonds, and borrowings under the Credit Agreement (as defined herein). Such pledge on Net Revenues is subordinate and inferior to the pledge securing payment of (i) the Old Series Bonds (ii) the New Series Bonds and (iii) any New Series Bonds to be issued in the future. The City and Texas Commerce Bank National Association have entered into a revolving credit agreement (the "Credit Agreement") pursuant to which such bank is obligated under the Credit Agreement to loan to the City an aggregate amount not to exceed \$100 million for the purpose of paying amounts due on the Commercial Paper. Any borrowings under the Credit Agreement are equally and ratably secured by and payable from the above described sources pledged for payment of the Commercial Paper. There have been no borrowings under the Credit Agreement as of January 31, 1987.

5. Pension Plan

Prior to 1983, CPS had an insured pension plan under which insurance was purchased for each participating employee in an amount calculated to yield cash value at retirement sufficient to provide an annuity equal to prescribed benefits. To the extent benefits represented amounts attributable to wage increases received after an employee reached age 60½, CPS assumed all of the incremental cost. The incremental costs for these individuals are paid directly to retirees by CPS.

In 1983, CPS adopted a self-administered, defined-benefit contributory pension plan covering substantially all employees. The total employer pension cost (all funded), which includes amortization of past service costs over 30 years using the Unit Credit Cost actuarial method, is summarized as follows:

	1987	1986
	(in thousands)	(in thousands)
Paid directly to retired employees	\$ 711	\$ 712
Amounts deposited in the CPS Employees' Pension Trust	9,136	8,500
Total	<u>\$9,847</u>	<u>\$9,212</u>

A comparison of accumulated plan benefits and plan net assets for CPS' defined-benefit plan is as follows:

Actuarial present value of accumulated plan benefits as of the end of the plan year:

	December 31, 1986	December 31, 1985
	(in thousands)	(in thousands)
Vested benefits	\$104,751	\$ 8,572
Nonvested benefits	33,105	26,351
Total	<u>\$137,856</u>	<u>\$115,923</u>
Net assets available for plan benefits	<u>\$132,075</u>	<u>\$109,118</u>

An assumed rate of return of 8% was used in determining the actuarial present value of accumulated plan benefits.

In addition to providing pension benefits, CPS provides certain health care and life insurance benefits for retired employees. All of CPS' employees are eligible for these benefits upon retirement from CPS. The cost of retiree health care and life insurance benefits, funded by CPS and retired employee contributions, is recognized as an expense of CPS as employer contributions are made to the programs. These costs approximated \$734,000 and \$731,000 for 1987 and 1986, respectively.

6. Payments to the City of San Antonio

The Trust Indenture provides for benefits and services totaling 14% of CPS gross revenues, as defined, to be paid or provided to the City. The City has elected to accept benefits at no less than 14% of gross revenue. The reduction of City benefits has no effect on financial operations.

Payments to the City of San Antonio for 1987 and 1986 were as follows:

	1987	1986
In lieu of taxes	\$ 7,799	\$ 7,096
Refund gas and electric services	15,286	17,009
Additional payments	73,106	79,867
	<u>\$96,191</u>	<u>\$103,972</u>

7. South Texas Project

CPS is one of four participants in the South Texas Project ("STP"), which consists of two 1,250 megawatt nuclear generating units under construction at a site in Matagorda County, Texas. The other participants in the project are Houston Lighting & Power Company ("HLP"), the project manager; Central Power and Light Company ("CPL") and the City of Austin ("Austin"). Under the terms of the STP participation agreement, each participant provides financing for its share of construction expenditures with CPS' participating interest in the project being 28% or 700 megawatts. Projected commercial operation dates are December 1987 and June 1989 for Units 1 and 2, respectively.



Notes to Financial Statements

In 1986, a suit involving the project was settled on the agreement of Brown & Root, the former architect/engineer and constructor for STP, to pay the plaintiffs, CPS and the other participants, \$750 million. CPS commenced receipt of its \$210 million share of the settlement with receipt of approximately \$15 million on January 1, 1986, and \$30 million in 1987. The remainder, with interest, will be received in a \$7.5 million quarterly installment over six years pursuant to an unqualified contractual obligation of Aetna Life Insurance Company. The remaining payments have been recorded as both current receivables and as Litigation Settlement Benefits Receivable.

The estimated total direct cost of the project is \$5.45 billion before consideration of the Brown & Root settlement. CPS' portion of the total costs for STP would be \$2.2 billion for construction and interest during construction and \$110 million for fuel to be purchased prior to commercial operation. CPS' share of remaining costs is estimated to be \$183.7 million for plant construction over the next three years, exclusive of interest, nuclear fuel and other costs. These costs may vary from the estimated amount due to inflation, changes in equipment delivery and construction schedule and regulatory charges.

As of January 31, 1987, CPS has expended approximately \$1.699 billion in the project (net of the \$210 million settlement with Brown & Root), including interest during construction of \$381 million and advance payment on fuel of \$101 million.

Prior to the initial loading of nuclear fuel and operation of STP, an operating license must be issued by the Nuclear Regulatory Commission. In order to meet the scheduled in-service date for Unit 1, a license for fuel loading and off power testing must be obtained by July 1987. Hearings before the Nuclear Regulatory Commission's Atomic Safety and Licensing Board have been favorably completed and CPS anticipates that the license will be issued by June 1987.

5. Commitments and Contingencies

Coal Freight Rate Dispute — For the past ten years, CPS has been engaged in continuous litigation with certain railroads (Burlington Northern, Inc. and Southern Pacific) which, prior to August 1985, transported subbituminous coal to the J.T. Deed Station. The question involved the proper or lawful freight rate that CPS was legally required to pay these railroads for coal transportation services during the period 1978 through August 1985.

In December of 1984, the Federal District Court issued an order authorizing the railroads to collect the principal sum of \$19.8 million, plus interest of \$6.6 million from a subsidiary dispute involving ten months in 1980 and 1981 during which CPS paid

railroads \$19.8 million less for their services than the railroads claimed was due under their tariffs. This amount (\$26.4 million) was paid and classified with Prepayments and Other in the 1986 balance sheet pending final ruling in related matters.

In December 1986, CPS approved a settlement offer from the involved railroad, for all disputed issues. Both parties sought dismissal of actions pending before the ICC and in two Federal District Courts. As a result, CPS received a \$1 million payment from the railroads in January 1987, most of which will be used to replace utility funds used to make the \$26.4 million court-ordered rail tariff payments and to offset legal expenses incurred during the dispute. In addition, CPS will receive annual payments ranging from \$10 to \$13 million, totaling \$80.5 million, over the next seven years from the railroads, which is expected to be returned to customers as payment are received. The remaining amounts due have been recorded as both current receivables and Litigation Settlement Benefits Receivable.

Other — CPS is involved in various legal proceedings related to alleged personal and property damages, breach of contract, environmental matters, condemnation appeals and discrimination cases. In the opinion of management of CPS, the outcome of such proceedings will not have a material adverse effect on the financial position or results of operations of CPS.

Other purchase and construction commitments amounted to approximately \$65.1 million at January 31, 1987. As of January 31, 1987, CPS has no significant lease commitments.

9. Segment Information

Segment information is as follows:

	1987 (in thousands)			1986 (in thousands)		
	Electric	Gas	Total	Electric	Gas	Total
REVENUE	\$ 639,626	\$127,814	\$ 767,440	\$ 700,371	\$ 36,500	\$ 836,871
EXPENSES:						
Operating and maintenance expenses	104	113,194	418,010	377,654	118,74	495,828
Depreciation	36,501	5,310	41,811	35,435	4,916	40,351
Total	341,317	118,504	459,821	413,089	123,090	536,179
EARNINGS BEFORE INTEREST AND DEBT EXPENSE, ALLOWANCE FOR INTEREST CHARGED TO CONSTRUCTION, AND PAYMENTS TO THE CITY OF SAN ANTONIO	\$ 298,309	\$ 9,310	\$ 307,619	\$ 287,282	\$ 13,410	\$ 300,692
CAPITAL EXPENDITURES	\$ 409,090	\$ 21,520	\$ 430,610	\$ 416,071	\$ 18,989	\$ 435,060
UTILITY ASSETS	\$1,617,023	\$245,290	\$1,862,313	\$1,476,729	\$220,180	\$1,696,909
CONSTRUCTION WORK IN PROGRESS	1,769,801	6,904	1,776,705	1,446,519	10,471	1,456,955
TOTAL ASSETS	\$3,386,824	\$252,194	\$3,639,018	\$2,923,248	\$230,616	\$3,153,864

Report of Certified Public Accountants

Board of Trustees
City Public Service

We have examined the balance sheets of City Public Service at January 31, 1987 and 1986, and the related statements of earnings and application of earnings, changes in equity and changes in financial position for the years then ended. Our examinations were made in accordance with generally accepted auditing standards and, accordingly, included such tests of the accounting records and such other auditing procedures as we considered necessary in the circumstances.

In our opinion, the statements mentioned above present fairly the financial position of City Public Service at January 31, 1987 and 1986, and the results of operations and changes in financial position for the years then ended, in conformity with generally accepted accounting principles applied on a consistent basis during the period.

Arthur Young & Company

March 2, 1987

Five-Year Financial Review

	<u>1987</u>	1986	1985	1984	1983	Years ended January 31,
						(dollars in thousands)
REVENUE AND APPLICATION						
Revenues:						
Electric sales	\$ 639,623	\$ 700,371	\$ 636,364	\$ 544,125	\$ 521,435	
Gas sales	127,814	136,500	133,301	147,890	140,283	
Other income	36,778	31,962	34,589	23,452	25,975	
Total revenues	<u>\$ 804,218</u>	<u>\$ 868,833</u>	<u>\$ 804,254</u>	<u>\$ 715,467</u>	<u>\$ 687,693</u>	
Revenues applied:						
Cost of operating systems:						
Gas, electricity and fuel purchased	\$ 316,251	\$ 397,414	\$ 394,321	\$ 390,004	\$ 379,470	
Other operating expenses	69,003	65,039	57,392	50,861	49,085	
Maintenance	32,761	33,379	28,164	25,432	25,423	
Total	<u>\$ 418,015</u>	<u>\$ 495,832</u>	<u>\$ 479,877</u>	<u>\$ 466,297</u>	<u>\$ 453,978</u>	
Operating Fund	<u>\$ -0-</u>	<u>\$ 2,500</u>	<u>\$ -0-</u>	<u>\$ -0-</u>	<u>\$ -0-</u>	
Debt requirements for Old Series Bonds:						
Interest	\$ 7,426	\$ 7,875	\$ 8,303	\$ 8,696	\$ 9,018	
Principal requirements	9,000	8,600	8,195	7,835	7,540	
Reserve requirements	(84)	(46)	(17)	25	26	
Debt expense	14	12	12	13	13	
Total	<u>\$ 16,356</u>	<u>\$ 16,441</u>	<u>\$ 16,493</u>	<u>\$ 16,569</u>	<u>\$ 16,597</u>	
Payments and services to City:						
Payment in lieu of taxes	\$ 7,799	\$ 7,096	\$ 6,401	\$ 6,028	\$ 5,673	
Refunds for services	15,286	17,009	16,351	14,163	13,453	
Additional payment	73,106	79,867	72,755	61,502	59,696	
Total	<u>\$ 96,191</u>	<u>\$ 103,972</u>	<u>\$ 95,507</u>	<u>\$ 81,693</u>	<u>\$ 78,822</u>	
Debt requirements for New Series Bonds:						
Interest expense	\$ 153,411	\$ 135,235	\$ 110,165	\$ 86,645	\$ 73,504	
Principal requirements	23,350	21,440	19,730	18,120	14,825	
Reserve requirements	20,112	11,503	6,049	15,298	20,378	
Debt expense	5,178	1,867	229	119	113	
Total	<u>\$ 202,051</u>	<u>\$ 170,045</u>	<u>\$ 136,173</u>	<u>\$ 120,182</u>	<u>\$ 108,820</u>	
Allowance for funds used during construction:						
	<u>(101,402)</u>	<u>(87,296)</u>	<u>(64,467)</u>	<u>(48,439)</u>	<u>(40,871)</u>	
Additions to plant:						
Total expenditures for year	\$ 430,610	\$ 435,060	\$ 390,035	\$ 259,083	\$ 184,712	
Less construction funds provided by sources other than revenues	315,456	261,239	259,677	187,852	115,091	
Revenues used for additions to plant	115,154	173,821	130,358	71,231	69,621	
Addition to Improvements and Contingencies Fund	57,853	(6,482)	10,313	7,934	726	
Total	<u>\$ 173,307</u>	<u>\$ 167,339</u>	<u>\$ 140,671</u>	<u>\$ 79,165</u>	<u>\$ 70,347</u>	
Total revenues applied	<u>\$ 804,218</u>	<u>\$ 868,833</u>	<u>\$ 804,254</u>	<u>\$ 715,467</u>	<u>\$ 687,693</u>	
BALANCE SHEET DATA						
Utility plant at cost	\$ 3,255,479	\$ 2,838,847	\$ 2,620,511	\$ 2,236,613	\$ 1,983,694	
Annual construction additions	4,0,610	435,060	390,035	259,083	184,712	
Accumulated depreciation	446,914	418,743	384,084	350,654	319,898	
Annual depreciation allowance	41,811	40,351	37,837	35,918	34,953	
Principal and interest coverage	2.00x	2.15x	2.22x	2.05x	2.23x	

Five-Year Operations Review

	<u>1987</u>	<u>1986</u>	<u>1985</u>	<u>1984</u>	<u>1983</u>	Years ended January 31, (dollars in thousands)
OPERATING REVENUES						
Electric:						
Residential	\$ 276,307	\$ 292,216	\$ 263,217	\$ 219,067	\$ 208,969	
Commercial and industrial	266,747	295,158	268,950	230,528	214,096	
Street lighting	7,781	8,241	7,990	6,864	6,637	
Public authorities	71,073	80,007	75,491	65,032	61,271	
Other utilities	13,982	20,638	15,836	18,928	26,917	
Miscellaneous	3,736	4,111	4,880	3,706	3,545	
Total electric	\$ 639,626	\$ 700,371	\$ 636,364	\$ 544,125	\$ 521,435	
Gas:						
Residential	\$ 75,091	\$ 79,346	\$ 75,803	\$ 85,716	\$ 79,293	
Commercial and industrial	44,357	47,957	48,452	52,388	50,955	
Public authorities	7,442	8,153	8,031	9,324	8,923	
Miscellaneous	924	1,044	1,015	462	1,112	
Total gas	\$ 127,814	\$ 136,500	\$ 133,301	\$ 147,890	\$ 140,283	
SALES (000 OMITTED)						
Electric — KWH:						
Residential	4,036,562	3,782,693	3,1219	3,139,333	3,084,901	
Commercial and industrial	4,636,308	4,465,682	4,107,615	3,839,434	3,715,362	
Street lighting	78,732	78,445	76,565	78,034	78,508	
Public authorities	1,358,027	1,300,515	1,246,417	1,197,944	1,175,742	
Other utilities	257,848	413,381	181,741	194,636	332,730	
Total	10,367,477	10,040,716	9,103,557	8,449,381	8,387,243	
Gas — MCF:						
Residential	13,576	14,332	13,643	15,493	14,847	
Commercial and industrial	9,770	10,206	10,152	10,677	10,752	
Public authorities	1,657	1,764	1,708	1,925	1,895	
Total	25,003	26,302	25,503	28,095	27,494	
PURCHASE FOR RESALE:						
Electric (1,000) KWH	398,401	-0-	842	-0-	-0-	
Gas (1,000) MCF	25,701	26,040	26,367	29,398	28,322	
ELECTRIC GENERATION —						
(1,000) KWH	10,617,859	10,607,972	9,774,125	8,992,120	8,913,801	
Electric Gen. Capacity, KW (Gas)*	2,400,000	2,400,000	2,400,000	2,400,000	2,400,000	
Electric Gen. Capacity, KW (Coal)	836,000	836,000	836,000	836,000	836,000	
ELECTRIC PEAK DEMAND — KW	2,596,000	2,350,000	2,210,000	2,148,000	1,984,000	
NUMBER OF CUSTOMERS:						
Electric	458,037	446,573	425,316	398,983	372,235	
Gas	285,697	284,876	280,575	279,116	272,331	
RESIDENTIAL AVERAGES:						
Electric:						
Revenue per customer	\$ 692.51	\$ 765.21	\$ 724.92	\$ 647.97	\$ 654.37	
KWH per customer	10,117	9,906	9,615	9,285	9,660	
Revenue per KWH	6.84¢	7.73¢	7.54¢	6.98¢	6.77¢	
Gas:						
Revenue per customer	\$ 284.45	\$ 303.34	\$ 293.06	\$ 337.11	\$ 317.26	
MCF per customer	51.4	54.8	52.7	60.9	59.4	
Revenue per MCF	\$ 5.53	\$ 5.54	\$ 5.56	\$ 5.53	\$ 5.34	

* Oil rating for the gas units is 2,198,000 KW for the five-year period.



City Public Service

CPS Board of Trustees



Glenn Biogs
Chairman

Vice Chairman of the
Board, InterFirst Bank of
San Antonio, N.A.



Earl C. Hill
Vice Chairman

Attorney-at-Law



Ruben M. Escobedo
Trustee

Certified Public Accountant, President, Atkins Travel
Ruben Escobedo and
Company



Lila Cockrell
Trustee



Henry G. Cisneros
Ex-Officio Trustee

Mayor of San Antonio, Texas

Management Staff



J.K. Spruce
General Manager



**Howard L.
Freeman**
Assistant General
Manager for
Administration
and Finance



Kenneth Harz
Assistant General
Manager for
Planning and
Development



**Arthur von
Rosenborg**
Assistant General
Manager for
Planning and
Development

Department Managers

Jannie E. Axtell
Generation and
Environmental Planning

John J. Leah
Personnel Administration

L.E. Boulden
Materials and Transportation

John G. Mack
Production and Power
Plant Engineering

Stephen Braimer
Administrative Services

Bob McCullough
Public Relations

Robert J. Costello
Transmission and
Distribution Engineering

Robert C. Mecke
Construction

Franklin D. Haegelin
Personnel Services

James W. Pettinos
Operations

Cecil J. Henne
Customer Services

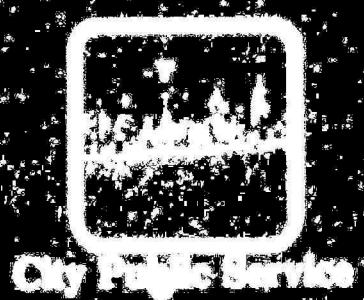
Donald R. Schnitz
Gas Engineering and Fuels

Cy Hutchinson
Data Processing Services

Stewart Schooler
Legal and Benefit Services

Donald S. Thomas
Financial Services

If you would like more information about City Public Service or energy availability, please contact Charles Scott at (513) 227-3211, or write City Public Service, P.O. Box 1771, Springfield, Ohio 45561.



P.O. Box 1771, Milwaukee, Wisconsin

PROSPECTUS SUPPLEMENT

(To Prospectus dated May 21, 1987)

1,000,000 Shares

Houston Lighting & Power Company

\$8.50 Cumulative Preferred Stock

(Fixed Liquidation Price \$100 Per Share)

Dividends on the \$8.50 Cumulative Preferred Stock, without par value (\$8.50 Preferred Stock), are cumulative from the date of original issue and are payable quarterly on January 1, April 1, July 1 and October 1 of each year, beginning October 1, 1987.

The \$8.50 Preferred Stock will be redeemable at any time at the option of the Company, in whole or in part, at a redemption price of \$108.50 per share prior to June 1, 1992; at \$104.25 per share on or after June 1, 1992 and prior to June 1, 1993; at \$102.13 per share on or after June 1, 1993 and prior to June 1, 1994; and at \$100.00 per share on June 1, 1994 or thereafter; plus in each case accrued and unpaid dividends. Any redemption of the \$8.50 Preferred Stock prior to June 1, 1992 will be subject to certain restrictions on refunding. See "Description of \$8.50 Preferred Stock — Redemption Provisions".

The \$8.50 Preferred Stock will be entitled to a mandatory sinking fund sufficient to retire on each June 1, beginning in 1993, 200,000 shares at \$100.00 per share plus accrued and unpaid dividends. In addition, the Company has the noncumulative right to redeem through the sinking fund up to 200,000 additional shares on the same terms and dates applicable to the mandatory sinking fund redemptions. The Company will have the option to satisfy the mandatory sinking fund requirement, in whole or in part, by crediting shares of the \$8.50 Preferred Stock redeemed (other than through the sinking fund) or otherwise purchased or acquired. See "Description of \$8.50 Preferred Stock — Sinking Fund Provisions".

THESE SECURITIES HAVE NOT BEEN APPROVED OR DISAPPROVED BY THE SECURITIES AND EXCHANGE COMMISSION NOR HAS THE COMMISSION PASSED UPON THE ACCURACY OR ADEQUACY OF THIS PROSPECTUS SUPPLEMENT OR THE PROSPECTUS. ANY REPRESENTATION TO THE CONTRARY IS A CRIMINAL OFFENSE.

	Price to Public(1)	Underwriting Discount	Proceeds to Company(2)
Per Share	\$100.00	.875	\$99.125
Total	\$100,000,000	\$875,000	\$99,125,000

(1) Plus accrued dividends, if any, from the date of original issue.

(2) Before deducting expenses payable by the Company estimated to be \$165,000.

The shares of \$8.50 Preferred Stock are offered by the several Underwriters when, as and if issued by the Company and accepted by the Underwriters and subject to their right to reject orders in whole or in part. It is expected that delivery of the certificates representing shares of \$8.50 Preferred Stock will be made in New York City on or about June 16, 1987.

The First Boston Corporation

Kidder, Peabody & Co.
Incorporated

The date of this Prospectus Supplement is June 9, 1987.

IN CONNECTION WITH THIS OFFERING, THE UNDERWRITERS MAY OVER-ALLOT OR EFFECT TRANSACTIONS WHICH STABILIZE OR MAINTAIN THE MARKET PRICE OF THE \$8.50 PREFERRED STOCK OFFERED HEREBY OR ANY OTHER SERIES OF THE PREFERRED STOCK OF THE COMPANY AT LEVELS ABOVE THOSE WHICH MIGHT OTHERWISE PREVAIL IN THE OPEN MARKET. SUCH STABILIZING, IF COMMENCED, MAY BE DISCONTINUED AT ANY TIME.

DESCRIPTION OF \$8.50 PREFERRED STOCK

The description of the particular terms of the \$8.50 Preferred Stock, as set forth herein and on the cover page of this Prospectus Supplement, supplements the description of the general terms and provisions of the New Preferred Stock in the accompanying Prospectus under "Description of New Preferred Stock", to which reference is hereby made.

Fixed Dividend Rate

The fixed dividend rate of the \$8.50 Preferred Stock will be \$8.50 per share per annum. Dividends on the \$8.50 Preferred Stock will accrue from the date of issuance and will be payable on January 1, April 1, July 1 and October 1 of each year, beginning October 1, 1987.

Fixed Liquidation Price and Premium

The fixed liquidation price of the \$8.50 Preferred Stock will be \$100 per share. There will be a fixed liquidation premium for the \$8.50 Preferred Stock of \$8.50 per share until June 1, 1992; of \$4.25 per share on June 1, 1992 and thereafter prior to June 1, 1993; of \$2.13 per share on June 1, 1993 and thereafter prior to June 1, 1994; and of \$0.00 per share on June 1, 1994 and thereafter.

Redemption Provisions

The \$8.50 Preferred Stock is not redeemable, directly or indirectly, prior to June 1, 1992 from the proceeds of any refunding through the incurring of debt, or through the issuance of preferred stock ranking equally with or prior to the \$8.50 Preferred Stock as to dividends or liquidation, where such debt has an effective interest cost, or such preferred stock has an effective dividend cost, to the Company of less than 8.50% per annum. The \$8.50 Preferred Stock will otherwise be subject to redemption at any time at the option of the Company, in whole or in part, at \$108.50 per share prior to June 1, 1992; at \$104.25 per share on or after June 1, 1992 and prior to June 1, 1993; at \$102.13 per share on or after June 1, 1993 and prior to June 1, 1994; and at \$100 per share on June 1, 1994 or thereafter; plus in each case dividends accrued and unpaid to the date of redemption.

Sinking Fund Provisions

On June 1, 1993 and on each June 1 thereafter so long as any shares of the \$8.50 Preferred Stock remain outstanding, the Company will redeem from funds legally available therefor 200,000 shares of the \$8.50 Preferred Stock, or such lesser number as is then outstanding, pursuant to a mandatory sinking fund at \$100 per share plus dividends accrued thereon to the date of redemption. If the required number of shares is not redeemed on any such June 1, the unsatisfied sinking fund obligation will be cumulative until such obligation is discharged. In addition, the Company has the option to redeem pursuant to the sinking fund on each mandatory sinking fund redemption date, on a noncumulative basis, an additional 200,000 shares of \$8.50 Preferred Stock at \$100 per share plus dividends accrued thereon to the date of redemption. The Company may apply as a credit against the number of shares of \$8.50 Preferred Stock required to be redeemed pursuant to the mandatory sinking fund obligation shares of such series that have been redeemed (other than through the operation of the sinking fund) or otherwise purchased or acquired and that have not previously been used for any

such credit. Unless the Company has satisfied its mandatory sinking fund obligations, (a) no dividends may be declared or paid on any Common Stock or any other stock ranking junior to the \$8.50 Preferred Stock and (b) no shares of such stock, or any other series of Preferred Stock, may be redeemed, purchased or otherwise acquired, nor may moneys be paid or set aside for a sinking fund for the redemption, purchase or other acquisition thereof.

Other

The \$8.50 Preferred Stock will have no exchange or conversion rights.

UNDERWRITING

The underwriters named below have severally agreed to purchase from the Company the following respective number of shares of \$8.50 Preferred Stock:

<u>Name</u>	<u>Number of Shares</u>
The First Boston Corporation.....	390,000
Kidder, Peabody & Co. Incorporated.....	390,000
Goldman, Sachs & Co.	40,000
Merrill Lynch, Pierce, Fenner & Smith Incorporated.....	40,000
Morgan Stanley & Co. Incorporated.....	40,000
Printon, Kane & Co.	20,000
Salomon Brothers Inc.....	40,000
Shearson Lehman Brothers Inc.	40,000
Total.....	<u>1,000,000</u>

The Underwriting Agreement provides that the obligations of the several Underwriters are subject to certain conditions precedent, and that the several Underwriters will be obligated to purchase all of the shares of \$8.50 Preferred Stock if any are purchased. The Company has agreed to indemnify the Underwriters against certain civil liabilities, including liabilities under the Securities Act of 1933, as amended.

The Company has been advised by The First Boston Corporation and Kidder, Peabody & Co. Incorporated, as Representatives of the Underwriters, that the Underwriters propose to offer the shares of \$8.50 Preferred Stock to the public initially at the offering price set forth on the cover page of this Prospectus Supplement and, through the Representatives, to certain dealers at such price less a concession of \$.50 per share; that the Underwriters and such dealers may allow a discount of \$.375 per share on sales to certain other dealers; and that the public offering price and concession and discount to dealers may be changed by the Representatives after the initial public offering.

PROSPECTUS

Houston Lighting & Power Company
Cumulative Preferred Stock
(without par value)

Houston Lighting & Power Company (Company) may offer from time to time, in one or more series, shares of its Cumulative Preferred Stock, without par value (New Preferred Stock), having an aggregate fixed liquidation price of not more than \$100 million, at prices and on terms to be determined when an agreement to sell is made or at the time of the sale, as the case may be. This Prospectus will be supplemented by one or more prospectus supplements (Prospectus Supplement) which will reflect any agreement entered into by the Company for the sale of shares of New Preferred Stock and will set forth the series designation, number of shares, proceeds to the Company, the initial public offering price, dividend rate (or method of calculation thereof), redemption provisions, sinking fund or purchase fund provisions, if any, and other specific terms of the series of New Preferred Stock in respect of which this Prospectus is being delivered (Offered Stock).

THESE SECURITIES HAVE NOT BEEN APPROVED OR DISAPPROVED BY THE SECURITIES AND EXCHANGE COMMISSION NOR HAS THE COMMISSION PASSED UPON THE ACCURACY OR ADEQUACY OF THIS PROSPECTUS. ANY REPRESENTATION TO THE CONTRARY IS A CRIMINAL OFFENSE.

The New Preferred Stock will be sold through the underwriters named below or an underwriting syndicate including and represented by such firms. The names of any other underwriters, the net proceeds to the Company from the sale of each series of New Preferred Stock and any applicable underwriting commissions or discounts will be set forth in the Prospectus Supplement relating to such series. See "Plan of Distribution" for indemnification arrangements with underwriters.

The First Boston Corporation

Kidder, Peabody & Co.
Incorporated

The date of this Prospectus is May 21, 1987.

AVAILABLE INFORMATION

The Company is subject to the informational requirements of the Securities Exchange Act of 1934, as amended (Exchange Act), and, in accordance therewith, files reports and other information with the Securities and Exchange Commission (Commission). Information as of particular dates concerning directors and officers, their remuneration, the principal holders of securities of the Company and any material interest of such persons in transactions with the Company is disclosed in reports and other information of the Company filed with the Commission. Such reports and other information can be inspected and copied at the public reference facilities maintained by the Commission at 450 Fifth Street, N.W., Judiciary Plaza, Washington, D.C. 20549; and at the Commission's regional offices at the Everett McKinley Dirksen Building, 219 South Dearborn Street, Chicago, Illinois 60604 and at the Jacob K. Javits Building, 26 Federal Plaza, New York, New York 10007. Copies of such material can also be obtained at prescribed rates from the Public Reference Section of the Commission at its principal office at 450 Fifth Street, N.W., Judiciary Plaza, Washington, D.C. 20549.

INCORPORATION OF CERTAIN DOCUMENTS BY REFERENCE

The following documents, which have been filed by the Company with the Commission pursuant to the Exchange Act (File No. 1-3187H-1), are incorporated by reference in this Prospectus and shall be deemed to be a part hereof:

- (1) The Company's Annual Report on Form 10-K for the year ended December 31, 1986;
- (2) The Company's Quarterly Report on Form 10-Q for the quarter ended March 31, 1987.

All documents subsequently filed by the Company with the Commission pursuant to Section 13(a), 13(c), 14 or 15(d) of the Exchange Act prior to the termination of the offering made by this Prospectus shall be deemed to be incorporated herein by reference and to be a part hereof from the date of filing such documents. Any statement contained in a document incorporated or deemed to be incorporated by reference herein shall be deemed to be modified or superseded for purposes of this Prospectus to the extent that a statement contained herein or in any other subsequently filed document that also is or is deemed to be incorporated by reference herein modifies or supersedes such statement. Any such statement so modified or superseded shall not be deemed, except as so modified or superseded, to constitute a part of this Prospectus.

The Company hereby undertakes to provide without charge to each person to whom a copy of this Prospectus has been delivered, upon written or oral request of any such person, a copy of any or all of the documents referred to above that have been incorporated by reference in this Prospectus (not including exhibits to the documents that are incorporated by reference unless such exhibits are specifically incorporated by reference into such documents). Written or oral requests for such copies should be directed to the Investor Relations Department, P. O. Box 4505, Houston, Texas 77210, telephone (800) 231-6406 (if calling from outside Texas) or (800) 392-4641 (if calling from inside Texas) (toll free in either case).

IN CONNECTION WITH THIS OFFERING, THE UNDERWRITERS MAY OVER-ALLOT OR EFFECT TRANSACTIONS WHICH STABILIZE OR MAINTAIN THE MARKET PRICE OF THE NEW PREFERRED STOCK OFFERED HEREBY OR ANY OTHER SERIES OF THE PREFERRED STOCK OF THE COMPANY AT LEVELS ABOVE THOSE WHICH MIGHT OTHERWISE PREVAIL IN THE OPEN MARKET. SUCH STABILIZING, IF COMMENCED, MAY BE DISCONTINUED AT ANY TIME.

SUMMARY INFORMATION

The following summary information is qualified in its entirety by, and should be read in conjunction with, the information appearing elsewhere in this Prospectus, or in any accompanying Prospectus Supplement, and in the documents incorporated herein by reference.

THE OFFERING

Issuer	Houston Lighting & Power Company.
Securities Offered.....	Cumulative Preferred Stock, without par value, in the amount, not to exceed \$100 million aggregate fixed liquidation price, and having the designation, dividend rate, redemption provisions, sinking fund or purchase fund provisions, if any, and other specific terms to be set forth in a Prospectus Supplement hereto.

THE COMPANY

Business and Service Area	Electric utility serving approximately 5,000 square miles of the Texas Gulf Coast Region, including Houston.
Property, Plant and Equipment — Net (March 31, 1987)	\$7,796,208,000
Fuel for Electric Generation (Twelve months ended March 31, 1987)	Gas and Oil 56%; Coal and Lignite 44%

	Twelve Months Ended		
	<u>March 31, 1987</u>	<u>December 31, 1986</u>	<u>December 31, 1985</u>
	(Unaudited)	(Amounts in Thousands except Ratios)	
Income Summary:			
Operating Revenues	\$2,939,538	\$2,959,740	\$3,533,364
Operating Income	\$ 447,660	\$ 465,938	\$ 495,883
Allowance for Funds Used During Construction	\$ 226,394	\$ 225,626	\$ 204,209
Net Income Before Preferred Dividends	\$ 443,001	\$ 461,744	\$ 482,506
Ratio of Earnings to Fixed Charges and Preferred Dividend Requirements	2.93	2.95	3.26
 Capitalization Summary:			
Long-Term Debt (including current maturities)	\$2,798,510	\$3,023,510	47.9%
Cumulative Preferred Stock	341,319	441,319	7.0
Common Stock Equity	2,843,966	2,843,966	45.1
Total Capitalization	<u>\$5,983,795</u>	<u>\$6,308,795</u>	<u>100.0%</u>
March 31, 1987	As Adjusted*	Percent of Adjusted Capitalization*	
(Unaudited)	(Thousands)		

Long-Term Debt (including current maturities)	\$2,798,510	\$3,023,510	47.9%
Cumulative Preferred Stock	341,319	441,319	7.0
Common Stock Equity	2,843,966	2,843,966	45.1
Total Capitalization	<u>\$5,983,795</u>	<u>\$6,308,795</u>	<u>100.0%</u>

* Adjusted to give effect to (i) the expected issuance in 1987 of the New Preferred Stock having an aggregate fixed liquidation price of \$100 million, and (ii) the anticipated issuance in 1987 of \$225 million principal amount of First Mortgage Bonds for which a registration statement has been filed with the Commission.

THE COMPANY

Houston Lighting & Power Company (Company) is engaged in the generation, transmission, distribution and sale of electric energy, serving an area of the Texas Gulf Coast Region, estimated at 5,000 square miles, which includes Houston (the largest city in Texas) and 156 smaller cities, villages and communities. The address of the Company's principal executive offices is 611 Walker Avenue, Houston, Texas 77002 (telephone number (713) 228-9211).

The Company is a subsidiary of Houston Industries Incorporated (Houston Industries) which owns all of the Company's outstanding common stock. Houston Industries is a holding company as defined in the Public Utility Holding Company Act of 1935, but is exempt from regulation as a "registered" holding company under the Act except with respect to the acquisition of securities of other public utility companies. Houston Industries owns all of the outstanding common stock of two other principal operating subsidiary companies: Primary Fuels, Inc. and Utility Fuels, Inc. Houston Industries also owns all of the outstanding common stock of four other subsidiaries: Innovative Controls, Inc., KBLCOM Incorporated, Houston Industries Finance, Inc. and Development Ventures, Inc.

APPLICATION OF PROCEEDS

The net proceeds from the sale of any New Preferred Stock offered hereby will be used to pay expenditures relating to the Company's construction program (as discussed in the documents incorporated by reference herein), including the repayment of short-term indebtedness incurred in connection therewith. Such short-term indebtedness bears or will bear interest at fluctuating rates generally lower than the prime rate. Any proceeds not so used will be used for general corporate purposes. The Company has registered with the Commission \$225 million of its First Mortgage Bonds. The proceeds from the sale of such First Mortgage Bonds may be used to fund the Company's construction program or for other general corporate purposes. The amounts, nature and timing of sales of the New Preferred Stock and any such First Mortgage Bonds have not been determined. Pending future sales of such securities or sales of other securities, financing of that portion of the construction program not provided by funds internally generated will be obtained by the Company from short-term bank borrowings and sales of commercial paper.

DESCRIPTION OF NEW PREFERRED STOCK

The information set forth below is summarized from the Restated Articles of Incorporation of the Company, as amended, which are an exhibit to the Registration Statement of which this Prospectus is a part. The statements and descriptions hereinafter contained do not purport to be complete, and are qualified in their entirety by reference to such document. All cumulative preferred stock issued or to be issued by the Company under the Restated Articles of Incorporation is referred to herein as "Preferred Stock."

The Offered Stock

The Prospectus Supplement relating to the Offered Stock will describe the following terms thereof:

- (1) the series designation;
- (2) the number of shares of such series;
- (3) the dividend rate or method of calculation thereof applicable to the series;
- (4) applicable redemption provisions;
- (5) sinking fund or purchase fund provisions, if any;

- (6) the fixed liquidation price and fixed liquidation premium applicable to the series; and
- (7) the rate or basis of exchange or conversion into other securities or method of determination thereof applicable to the series, if any.

Issuance in Series

Preferred Stock of the Company may be issued in series which may vary as to distinctive serial designations, rates of dividends, redemption prices, liquidation prices, liquidation premiums, conversion rights and requirements as to any sinking or purchase fund. The Board of Directors may fix such terms of any new series of Preferred Stock from time to time. The Company is authorized by its Restated Articles of Incorporation to issue 10,000,000 shares of Preferred Stock, without par value. A total of 3,447,397 shares of such stock other than the New Preferred Stock, represented by nine different series having an aggregate fixed liquidation price of \$344,739,700, are currently outstanding. None of such nine outstanding series is entitled to the benefit of any sinking or purchase fund.

Dividend Rights

The holders of each series of Preferred Stock, including the New Preferred Stock, shall be entitled to receive, if and when declared by the Board of Directors, cumulative quarterly dividends at the rates per annum fixed for such series, respectively, payable on January 1, April 1, July 1 and October 1 in each year (except for the \$4 Preferred Stock, the dividend payment dates for which are February 1, May 1, August 1 and November 1), before any dividends, other than a dividend payable in Common Stock of the Company, may be paid or set apart for the Common Stock. In the event that more than one series of Preferred Stock is outstanding and dividends are paid in an amount less than full cumulative dividends in arrears on all Preferred Stock, then the dividends shall be divided between the different series in proportion to the aggregate amounts which would be distributable to the Preferred Stock of each series if full cumulative dividends were declared and paid thereon.

Voting Rights

No voting rights are conferred on any series of Preferred Stock except as set forth below and under "Restrictions on Corporate Action" and except as provided by the laws of the State of Texas. The holders of Preferred Stock of any series, in cases where they have a right to vote, are entitled to one vote for each share held.

Whenever dividends on Preferred Stock are in arrears in an amount equal to four quarterly dividends, the holders of Preferred Stock of all series shall have the right to elect one-third of the Board of Directors until such arrearages are cured, and whenever such dividends are in arrears in an amount equal to eight quarterly dividends, such holders shall have the right to elect a majority of the Board of Directors. No dividends on Preferred Stock are in arrears.

Liquidation Rights

In the event of any liquidation, dissolution or winding up of the Company, or any reduction or decrease of its capital stock resulting in a distribution of assets to the holder or holders of its Common Stock other than by way of dividends out of the net profits or out of the surplus of the Company, the holders of the Preferred Stock shall be entitled to receive, from the assets of the Company available for distribution to shareholders, the fixed liquidation price established for the respective series plus, in case such liquidation, dissolution, winding up, reduction or decrease shall have been voluntary, the fixed liquidation premium for such series, if any, together in all cases with a sum equal to all accrued and unpaid dividends to the date payment is made available. If the assets distributable among the holders of the Preferred Stock should be insufficient to permit the payment in full of the preferential amounts fixed for all series, then the distribution shall be made among the holders of each series ratably in proportion to the full preferential amounts to which they are respectively entitled.

Redemption and Repurchase Provisions

Subject to restrictions on refunding applicable to certain of the Company's outstanding series of Preferred Stock and restrictions on any redemptions of the New Preferred Stock set forth in the Prospectus Supplement, the Company may at any time redeem the whole or any part of the Preferred Stock, or of any series thereof, upon notice mailed to the holders of the stock to be redeemed not less than twenty nor more than fifty days prior to the date fixed for redemption. The price at which the shares shall be redeemed is the fixed redemption price of the series of such shares together with the amount of any dividends accrued or in arrears to the date of redemption. If less than all of any one series of the Preferred Stock is to be redeemed, then the shares to be redeemed are to be selected ratably or by lot. The Company may also repurchase any of its capital stock of any class so long as it is not in arrears in the payment of any dividends on the Preferred Stock, and, if it is so in arrears, may repurchase Preferred Stock (but not Common Stock) only pursuant to an offer made to all holders of Preferred Stock. All shares of Preferred Stock redeemed or repurchased assume the status of authorized but unissued shares.

Sinking Fund or Purchase Fund

The Company may determine to include sinking fund or purchase fund provisions for any series of the New Preferred Stock.

Restrictions on Corporate Action

The Restated Articles of Incorporation provide that the affirmative vote of two-thirds of the outstanding shares of Preferred Stock will be required: (a) to create, authorize or issue any additional stock, or securities convertible into stock, ranking prior to the Preferred Stock as to dividends or liquidation rights; (b) to alter or amend the Restated Articles of Incorporation in any manner prejudicial to the Preferred Stock; or (c) to issue additional Preferred Stock or stock of equal rank unless (i) the total fixed liquidation price of all such stock and any stock of prior rank to be outstanding shall be equaled or exceeded by the capital represented by junior stock and (ii) for a period of twelve consecutive months within the fifteen months immediately prior to such issuance the net earnings of the Company available for dividends shall be at least 2½ times the annual dividend requirements on all such stock and any stock of prior rank to be outstanding after such issuance, and the earnings available for interest, amortization and dividends (after taxes and depreciation) shall be at least 1½ times the sum of such dividend requirements and the annual interest requirements on all indebtedness of the Company.

Miscellaneous

None of the Preferred Stock that is currently outstanding has any preemptive or conversion rights. The New Preferred Stock when issued will be fully paid and nonassessable.

Transfer Agent and Registrar

The transfer agent and registrar for the New Preferred Stock will be Houston Industries.

RATIOS

The ratios of earnings to fixed charges and preferred dividend requirements for each of the Company's fiscal years 1982 through 1986 were 1.94, 3.01, 3.05, 3.26 and 2.95, respectively. The ratio of earnings to fixed charges and preferred dividend requirements for the twelve months ended March 31, 1987 was 2.93. The Company's earnings used in the calculation of such ratios include the allowance for funds used during construction. The ratio for 1982 reflects an after-tax charge against income of \$168 million as a result of regulatory treatment of the cancellation of a nuclear generating project. Without such charge, the ratio for 1982 would have been 3.27. The pro forma effect of the issuance of the New Preferred Stock on the 1986 ratio would be less than 10%.

PLAN OF DISTRIBUTION

The Company will sell the New Preferred Stock to The First Boston Corporation and Kidder, Peabody & Co. Incorporated or to an underwriting syndicate including and represented by such firms. The underwriters will be named in the Prospectus Supplement by which each series of New Preferred Stock is to be offered.

Each Prospectus Supplement with respect to a series of the New Preferred Stock will set forth the terms of the offering of such series and the proceeds to the Company from such sale, any underwriting discounts and other items constituting underwriters' compensation, the initial public offering price and the discounts or concessions allowed or reallocated or paid to dealers. The initial public offering price and any discounts or concessions allowed or reallocated or paid to dealers may be changed from time to time.

Shares of New Preferred Stock will be acquired by the underwriters for their own account and may be resold from time to time in one or more transactions, including negotiated transactions, at a fixed public offering price or at varying prices determined at the time of sale. The Company has agreed to indemnify the underwriters against certain civil liabilities, including liabilities under the Securities Act of 1933. The underwriting agreement will provide that the obligations of the underwriters are subject to certain conditions precedent and that the underwriters will be obligated to purchase all of the shares of New Preferred Stock covered by the Prospectus Supplement if any are purchased.

EXPERTS

The financial statements and supplemental schedules of the Company included in the Company's Annual Report on Form 10-K for the year ended December 31, 1986, which is incorporated in this Prospectus by reference, have been examined by Deloitte Haskins & Sells, Independent Certified Public Accountants, as stated in their opinion appearing therein. Such financial statements and supplemental schedules are incorporated by reference in this Prospectus in reliance upon such opinion, given upon the authority of that firm as experts in accounting and auditing.

LEGAL OPINIONS

Certain legal matters in connection with the New Preferred Stock are being passed upon for the Company by Baker & Botts, Houston, Texas, and for the underwriters by Reid & Priest, New York, New York. Reid & Priest will not pass upon the incorporation of the Company and will rely as to all matters covered by their opinion governed by Texas law upon the opinion of Baker & Botts.

No dealer, salesman or other person has been authorized to give any information or to make any representations in connection with this offering other than those contained in this Prospectus Supplement or in the Prospectus, and, if given or made, such information or representations must not be relied upon as having been authorized by the Company or any Underwriter. This Prospectus Supplement and the Prospectus do not constitute an offer to sell, or a solicitation of an offer to buy, any of the securities offered hereby in any jurisdiction to any person to whom it is unlawful to make such offer or solicitation in such jurisdiction. Neither the delivery of this Prospectus Supplement and the Prospectus nor any sale made hereunder shall, under any circumstances, create any implication that there has been no change in the affairs of the Company since the date of this Prospectus Supplement or that the information set forth herein is correct as of any time subsequent to the date hereof or the date of filing of any documents incorporated by reference herein.

Houston Lighting & Power Company

The Light company

1,000,000 Shares

\$8.50 Cumulative

Preferred Stock

(Fixed Liquidation Price \$100 Per Share)

TABLE OF CONTENTS

	<u>Page</u>
Prospectus Supplement	
Description of \$8.50 Preferred Stock	S-2
Underwriting	S-3
 Prospectus	
Available Information	2
Incorporation of Certain Documents by Reference	2
Summary Information	3
The Company	4
Application of Proceeds	4
Description of New Preferred Stock	4
Ratios	7
Plan of Distribution	7
Experts	7
Legal Opinions	7

PROSPECTUS SUPPLEMENT

The First Boston Corporation

Kidder, Peabody & Co.
Incorporated

**\$160,000,000
CITY OF SAN ANTONIO, TEXAS
ELECTRIC AND GAS SYSTEMS
REVENUE IMPROVEMENT BONDS,
NEW SERIES 1988**

MUNICIPAL BOND NEW ISSUE INSURANCE POLICY

FGIC.

Service mark used by Financial Guaranty Insurance Company.
A private company not affiliated with any U.S. government agency.

Bond Insurance

Concurrently with the issuance of the Bonds, Financial Guaranty Insurance Company ("Financial Guaranty") will issue its Municipal Bond New Issue Insurance Policy (the "Policy") for the Bonds maturing in the year 2016 (the "Insured Bonds"). The Policy unconditionally guarantees the payment of that portion of the principal of and interest on the Insured Bonds which has become due for payment, but shall be unpaid by reason of nonpayment by the City. Financial Guaranty will make such payments to Citibank, N.A., or its successor as its agent (the "Fiscal Agent"), on the later of the date on which such principal and interest is due or on the business day next following the day on which Financial Guaranty shall have received telephonic or telegraphic notice, subsequently confirmed in writing, or written notice by registered or certified mail, from an owner of Insured Bonds or the Paying Agent of the nonpayment of such amount by the City. The Fiscal Agent will disburse such amount due on any Insured Bond to its owner upon receipt by the Fiscal Agent of evidence satisfactory to the Fiscal Agent of the owner's right to receive payment of the principal and interest due for payment and evidence, including any appropriate instruments of assignment, that all of such owner's rights to payment of such principal and interest shall be vested in Financial Guaranty. The term "nonpayment" in respect of an Insured Bond includes any payment of principal or interest made to an owner of an Insured Bond which has been recovered from such owner pursuant to the United States Bankruptcy Code by a trustee in bankruptcy in accordance with a final, nonappealable order of a court having competent jurisdiction.

The Policy is non-cancellable and the premium will be fully paid at the time of delivery of the Bonds. The Policy covers failure to pay principal of the Insured Bonds on their respective stated maturity dates, or dates on which the same shall have been called for mandatory sinking fund redemption, and not on any other date on which the Insured Bonds may have been accelerated, and covers the failure to pay an installment of interest on the stated date for its payment.

Financial Guaranty is a wholly-owned subsidiary of FGIC Corporation (the "Corporation"), a Delaware holding company. The following investors or affiliates thereof own approximately 85% of the stock of the Corporation: General Electric Capital Corporation, General Re Corporation, Lumbermens Mutual Casualty Company (affiliated with the Kemper Group), Shearson Lehman Hutton Inc., J.P. Morgan & Co. Incorporated and Gerald L. Friedman. The investors of the Corporation are not obligated to pay the debts of or the claims against Financial Guaranty. Financial Guaranty is domiciled in the State of New York and is subject to regulation by the State of New York Insurance Department. As of December 31, 1987, the total capital and surplus of Financial Guaranty was approximately \$350,500,000.

Municipal Bond New Issue Insurance Policy

Issuer: _____ Policy Number: _____

Control Number: _____

Bonds: _____ Premium: _____

Financial Guaranty Insurance Company ("Financial Guaranty"), a New York stock insurance company, in consideration of the payment of the premium and subject to the terms of this Policy, hereby unconditionally and irrevocably agrees to pay to Citibank N.A., or its successor, as its agent (the "Fiscal Agent"), for the benefit of Bondholders, that portion of the principal and interest on the above described debt obligations (the "Bonds") which shall become Due for Payment but shall be unpaid by reason of Nonpayment by the Issuer.

Financial Guaranty will make such payments to the Fiscal Agent on the date such principal or interest becomes Due for Payment or on the business Day next following the day on which Financial Guaranty shall have received Notice of Nonpayment, whichever is later. The Fiscal Agent will disburse to the Bondholder the face amount of principal and interest which is then Due for Payment but is unpaid by reason of Nonpayment by the Issuer but only upon receipt by the Fiscal Agent in form reasonably satisfactory to it, of (i) evidence of the Bondholder's right to receive payment of the principal or interest Due for Payment and (ii) evidence, including any appropriate instruments of assignment, that all of the Bondholder's rights to payment of such principal or interest Due for Payment shall thenceforth vest in Financial Guaranty. Upon such disbursement, Financial Guaranty shall become the owner of the Bond, appurtenant coupon or right to payment of principal or interest on such Bond and shall be fully subrogated to all of the Bondholder's rights thereunder, including the Bondholder's right to payment thereof.

This Policy is non-cancellable for any reason. The premium on this Policy is not refundable for any reason, including the payment of the Bonds prior to their maturity. This Policy does not insure against loss of any prepayment premium which may at any time be payable with respect to any Bond.

As used herein, the term "Bondholder" means, as to a particular Bond, the person other than the Issuer who, at the time of Nonpayment, is entitled under the terms of such Bond to payment thereof. "Due for Payment" means, when referring to the principal of a Bond, the stated maturity date thereof or the date on which the same shall have been duly called for mandatory sinking fund redemption and does not refer to any earlier date on which payment is due by reason of call for redemption (other than by mandatory sinking fund redemption), acceleration or other advancement of maturity and means, when referring to

Financial Guaranty Insurance
Company
175 Water Street
New York, New York 10038
(212) 607-3000

FGICSM

Municipal Bond New Issue Insurance Policy

interest on a Bond, the stated date for payment of interest. "Nonpayment" in respect of a Bond means the failure of the Issuer to have provided sufficient funds to the paying agent for payment in full of all principal and interest Due for Payment on such Bond. "Notice" means telephonic or telegraphic notice, subsequently confirmed in writing, or written notice by registered or certified mail, from a Bondholder or a paying agent for the Bond to Financial Guaranty. "Business Day" means any day other than a Saturday, Sunday or a day on which the Fiscal Agent is authorized by law to remain closed.

In Witness Whereof, Financial Guaranty has caused this Policy to be affixed with its corporate seal and to be signed by its duly authorized officers in facsimile to become effective and binding upon Financial Guaranty by virtue of the countersignature of its authorized representative.

Gerald L. Friedman

President

Roger F. Doyle

Executive Vice President

USPDI
Effective Date:

Authorized Representative

Citibank, N.A. acknowledges that it has agreed to perform the duties of Fiscal Agent under this Policy.

[Signature]

Authorized Officer

ADDENDUM TO OFFICIAL NOTICE OF SALE
AND OFFICIAL STATEMENT

\$160,000,000

CITY OF SAN ANTONIO, TEXAS
ELECTRIC AND GAS SYSTEMS
REVENUE IMPROVEMENT BONDS, NEW SERIES 1988

The following information updates the Official Statement:

1. At page 34 of the Official Statement, in the discussion of the South Texas Project, reference is made to a January, 1988, forecast by HL&P projecting that Unit I would reach its initial criticality by mid-February. That deadline was not met due to certain problems which included the need to repair an auxiliary feed water pump. This correction will result in the delay of criticality into March, 1988. CPS cannot predict what other problems might be encountered or the effect they may have on the Project cost and schedule.
2. In the litigation section on pp. 38-39, regarding the actions filed by HL&P against CPS and CP&L in Dallas County and Matagorda County State district courts, CPS and CP&L have responded by submitting to HL&P on March 3, 1988, a call for arbitration, as permitted by the South Texas Project Participation Agreement. The arbitration call names one arbitrator each on behalf of San Antonio and CP&L, and lists as the disputes to be arbitrated issues concerning (1) the extent to which HL&P has breached its obligations under the Participation Agreement to the City of San Antonio and CP&L and the amount of damages caused by such breach, and (2) that neither San Antonio nor CP&L is liable to HL&P for any portion of the damages alleged against HL&P by the City of Austin. The call for arbitration is binding upon the three Project Participants and should supersede HL&P's Matagorda and Dallas County actions against CPS and CP&L. HL&P has the right to name a third arbitrator, after which the arbitration may proceed, as governed by the provisions of applicable State and Federal statutes. The decision of a majority of the arbitrators so appointed is binding on all the Participants, and judgment may be entered in a court of competent jurisdiction confirming and implementing the final decision of the arbitrators. CPS has filed a pleading in the Dallas County case denying HL&P's allegations, seeking an order enforcing the arbitration, and, subject thereto, a counterclaim for damages. CPS cannot predict the outcome of these proceedings.
3. CPS's retail electric service area includes 26 incorporated cities within Bexar County in addition to the City of San Antonio. CPS also provides retail gas distribution service to residents of fifteen of these cities. CPS's electric and gas distribution facilities utilize streets, alleys, and public ways within these cities pursuant to franchise agreements with each city which provide for payment by CPS to the cities of franchise fees equal to two percent of the gross revenues derived by CPS from the sale of electric and gas service within the cities' boundaries. Most of these agreements were negotiated in the early 1960's with 25-year terms, and despite ongoing renewal discussions, fourteen of the agreements have recently expired. New agreements have been negotiated with two of the cities on terms similar to those of the prior agreements. CPS is continuing to pay franchise fees at the two-percent rate, and is continuing discussions toward

negotiation of new agreements with uniform provisions. The cities with whom franchise agreements have not been renegotiated account for approximately 5.6 percent of the total billing revenues of the systems. These cities have formed a coalition for purposes of negotiating jointly with CPS and the City of San Antonio. The cities' primary interests appear to be in obtaining higher franchise fees and in negotiating with the City of San Antonio to share in the city payment which San Antonio receives as owner from the operation of the gas and electric systems. Although some of these cities have mentioned the possibility of purchasing those portions of the CPS distribution system within their boundaries and the possible assertion of independent rate-making authority, CPS cannot predict whether these issues will be pressed if satisfactory franchise agreements can be negotiated. CPS will continue to pursue the negotiation of franchise agreements which are fair and equitable to ratepayers of the entire system, but cannot predict what provisions will be contained in final agreements.

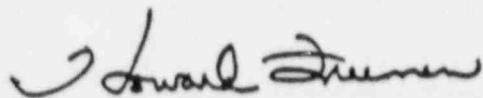
4. At its monthly meeting held on February 22, 1988, the CPS Board of Trustees unanimously elected Dr. Frank Bryant, M.D., to fill the trustee vacancy left by the departure of Mr. Earl Hill, the former chairman, whose term expired at the end of January.

5. City Public Service has been notified that the following ratings have been assigned to this issue:

Moody's Investor Services, Inc.	Aa
Standard & Poor's Corporation	AA

Dated: March 4, 1988

CITY PUBLIC SERVICE BOARD
OF SAN ANTONIO, TEXAS



Howard Freeman, Secretary

OFFICIAL STATEMENT

**\$160,000,000
CITY OF SAN ANTONIO, TEXAS
ELECTRIC AND GAS SYSTEMS
REVENUE IMPROVEMENT BONDS.
NEW SERIES 1988**

Bids to be Opened
Thursday, March 10, 1988, at 11:00 A.M., C.S.T.

CITY OF SAN ANTONIO, TEXAS

CITY COUNCIL

Henry G. Cisneros, Mayor

Maria Antonietta Berriozabal
Helen Dutmer
James C. Hasslocher
Weir Labatt

Walter Martinez
Robert Thompson

Yolanda Vera
Joe Webb
Frank D. Wing
Nelson Wolff

Louis Fox - City Manager
Carl L. White, Jr. - City Finance Director
Norma Rodriguez - City Clerk

CITY PUBLIC SERVICE BOARD OF SAN ANTONIO

Lila Cockrell, Chair
Ruben M. Escobedo

(Vacancy)

Pat Legan, Vice Chair
Henry G. Cisneros, Mayor

A. J. von Rosenberg - General Manager
Howard Freeman - Assistant General Manager
for Finance & Secretary/Treasurer

CONSULTANTS

Matthews & Branscomb
Legal Advisors

Arthur Young & Company
Auditors

Rotan Mosle Inc. and
Southwestern Capital Markets Inc.
Financial Consultants

McCall, Parkhurst & Norton
Bond Counsel

The date of this Official Statement is February 4, 1988.

TABLE OF CONTENTS

	Page
THE BONDS	
Description of Bonds	1
Summary Statement	2
Authority and Purpose	2
Historical Net Revenues and Coverage	2
Principal and Interest Requirements	3
Fund Balances	4
Outstanding Indebtedness	4
Revenue Bond Indebtedness and Utility Plants	5
Commercial Paper Program	6
Bond Ordinance Provisions	6
Security	7
Rate Covenant	8
Application of Revenues	9
Issuance of Additional Parity Bonds	10
	13
SAN ANTONIO ELECTRIC AND GAS SYSTEMS	
History and Management	20
Administration and Operating Personnel	20
Electric and Gas Sales by Customer Category	21
Description of Physical Property	22
Territory Served	27
Thirty Largest Gas and Electric Customers	27
Statement of Revenues, Expenses, and Net Income	28
Condensed Statements of Assets and Liabilities	29
Comparative Analysis of Electric and Gas Utility Operations	30
Record of Growth - Production of Electric Power	31
Five-Year Forecast of Electric and Gas Operating Data	31
1989 - 1993 Construction Program	32
South Texas Project	34
Environmental Matters	35
Fuel Supply	35
Energy Conservation Program	38
Litigation	38
Rates	40
Electric Customer Statistics	43
Typical Gas and Electric Bills of Six Texas Cities	43
Ten Year Record of City Benefits from Systems	43
TAX EXEMPTION	44
APPENDIX A - City of San Antonio - General Information	A-1
APPENDIX B - Financial Statements and Auditors' Report	B-1
APPENDIX C - CPSB Interim Financial Statements (Unaudited)	C-1
APPENDIX D - Text of Certain Indenture Provisions	D-1
APPENDIX E - CPSB Resolution Approving Bond Ordinance	E-1

This Official Statement does not constitute an offer to sell Bonds in any jurisdiction to any person to whom it is unlawful to make such offer in such jurisdiction. No dealer, salesman, or any other person has been authorized to give any information or make any representation, other than those contained herein, in connection with the offering of these Bonds, and if given or made, such information or representation must not be relied upon. The information and expressions of opinion herein are subject to change without notice except as provided herein, and neither the delivery of this Official Statement nor any sale made hereunder shall, under any circumstances, create any implication that there has been no change in the affairs of the City since the date hereof.

In the opinion of Bond Counsel, under existing statutes, regulations, published rulings and court decisions, interest on the Bonds is not includable in the gross income of the owners of the Bonds for federal income tax purposes. For a discussion of Bond Counsel's opinion and a description of certain collateral tax matters, including the application of the alternative minimum tax to the Bonds, see "Tax Exemption."

**OFFICIAL STATEMENT
\$160,000,000
CITY OF SAN ANTONIO, TEXAS
ELECTRIC AND GAS SYSTEMS REVENUE IMPROVEMENT BONDS,
NEW SERIES 1988**

Dated: March 1, 1988

Denomination: Multiples of \$5,000

Interest on the \$160,000,000 City of San Antonio, Texas Electric and Gas Systems Revenue Improvement Bonds, New Series 1988 (the "Bonds"), is payable on February 1 and August 1 of each year commencing August 1, 1988. The Bonds will be issued only as fully registered bonds in the denomination of \$5,000 or any integral multiple thereof. Principal of the Bonds will be payable at the principal corporate trust office of The Frost National Bank of San Antonio, San Antonio, Texas, the paying agent/registrar (the "Paying Agent/Registrar"). Interest on the Bonds will be payable by check dated as of the interest payment date, and mailed on each interest payment date by the Paying Agent/Registrar to registered holders. Registered holders are those shown on the records of the Paying Agent/Registrar on the 15th calendar day of the month next preceding each interest payment date.

**AMOUNTS, MATURITIES, INTEREST RATES, AND PRICES OR YIELDS
SERIAL BONDS**

Amount	Due Feb. 1	Interest Rate	Price or Yield *	Amount	Due Feb. 1	Interest Rate	Price or Yield
\$ 555,000	1990	5.30%	5.30%	\$1,170,000	2000	7.50%	7.50%
580,000	1991	5.70	5.70	1,255,000	2001	7.60	7.60
705,000	1992	6.00	6.00	1,350,000	2002	7.70	7.70
750,000	1993	6.25	6.25	1,435,000	2003	7.75	7.75
775,000	1994	6.50	6.50	6,510,000	2004	7.80	7.80
835,000	1995	6.70	6.70	7,045,000	2005	7.80	7.85
885,000	1996	6.90	6.90	7,630,000	2006	7.90	7.90
970,000	1997	7.10	7.10	8,255,000	2007	7.90	7.95
1,025,000	1998	7.20	7.20	8,940,000	2008	8.00	8.00
1,080,000	1999	7.40	7.40	9,675,000	2009	8.00	8.00

\$98,575,000 8.00% Term Bonds due February 1, 2016-Price 100%
(Accrued Interest to be Added)

* Initial offering yields as furnished by Bear, Stearns & Co. Inc., for the Underwriters.

REDEMPTION PROVISIONS

Mandatory Redemption

As previously indicated, bidders have the option to determine the maturity of term bonds, if any. If term bonds are designated by bidders they will be subject to mandatory redemption prior to maturity on February 1 in each of the years and in the respective principal amounts as set forth in paragraph B page (ii) in the Notice of Sale and Bidding Instructions (the particular bonds to be redeemed to be selected by the City by lot), in each case as a redemption price equal to 100% of their principal amount plus accrued interest to date of redemption.

Optional Redemption

Bonds maturing on and after February 1, 1999, will be redeemable, as a whole or in part on February 1, 1998, or on any interest payment date thereafter, at par and accrued interest, plus the following premium:

February 1, 1998 through January 31, 1999 at 102.0%;
February 1, 1999 through January 31, 2000 at 101.0%;
February 1, 2000 and thereafter at 100.0%.

SUMMARY STATEMENT

The following material is qualified in its entirety by the more complete information and financial statements contained elsewhere in this Official Statement.

THE ISSUER..... City of San Antonio, Texas, a political subdivision of the state of Texas, located in Bexar County.

THE BONDS..... \$160,000,000 Electric and Gas Systems Revenue Improvement Bonds, New Series 1988 (the "Bonds") which will mature on the dates and in the amounts set forth in this or the "New Series 1988 Bonds" Official Statement.

AUTHORITY FOR ISSUANCE..... The Bonds will be issued under and in conformity with the Constitution and Laws of Texas, particularly Articles 1111 et seq., and Article 2368a of Vernon's Texas Revised Civil Statutes Annotated, and pursuant to a Bond Ordinance to be adopted by the City Council of the City of San Antonio, Texas.

PURPOSE OF THIS FINANCING..... The proceeds of the Bonds will be used to pay certain of the costs of a program of improvements to and extensions of the City's electric and gas systems (the "Systems") and to fund the required reserve fund increase applicable to the Bonds. The overall improvement program includes site development, construction of electrical generating units, construction of distribution and transmission lines, additions and improvements to the gas system and miscellaneous project costs. These improvements, extensions and additions are in accord with the City's long-range development and improvement plans.

SECURITY..... The City currently has outstanding four series totalling \$105,785,000 of Old Series Bonds which are of a senior rank and are secured by a first mortgage against all real property, a security interest in all personal property, and a pledge of all revenues of the City's electric and gas systems. In addition, the City has outstanding 26 series totalling \$2,126,335,000 of New Series Bonds. The Bonds offered herein will constitute special obligations of the City on a parity with the aforementioned \$2,126,335,000 New Series Bonds, payable solely from and secured by a lien on and pledge of the net revenues of the City's electric and gas systems, subject to the prior lien of the pledge to the Old Series Bonds, all as fully set forth in the ordinance authorizing the Bonds.

ADDITIONAL BONDS..... Additional bonds on a parity with the Bonds may be issued, when among other requirements, Net Revenues of the Electric and Gas Systems during the past year were at least 150% of the maximum annual debt service on all bonds to be outstanding. Said Net Revenues may be adjusted to reflect rate changes. The senior lien of the Old Series Bonds is closed.

RATE COVENANT..... The City has covenanted to maintain Electric and Gas rates and charges sufficient to pay all expenses of maintenance and operation of the Systems, and to pay debt service requirements on all bonds and to establish and maintain the required reserves.

PAYMENT RECORD..... The City of San Antonio has never defaulted on any of its bonds.

LEGALITY..... The Attorney General of Texas and McCall, Parkhurst & Norton, San Antonio, Texas.

DELIVERY..... Anticipated on or about April 7, 1988.

BOND RATINGS..... The following ratings have been assigned to the Bonds: Moody's Investors Service, Inc., "Aa" and Standard & Poor's Corporation "AA". An explanation of the significance of such ratings may be obtained upon request from Moody's Investors Service, Inc. or Standard & Poor's Corporation. Only the opinions of Moody's Investors Service, Inc. and Standard & Poor's Corporation are represented by such ratings and the City makes no representation as to (1) the appropriateness of such ratings or (2) its ability or intent to maintain such ratings.

No assurance is given by the City that ratings will be maintained for any specified period of time, or that they will not change or be suspended or withdrawn by Moody's Investors Service, Inc. or Standard & Poor's Corporation if, in the opinion of the rating agencies, changes in the circumstances of the City should so warrant. Any such change, suspension or withdrawal of the bond ratings may have an adverse effect on the market price of the Bonds.

MUNICIPAL BOND INSURANCE..... FGIC has agreed to provide municipal bond insurance on the 2016 Term Bond. A statement of their policy is included as a separate enclosure.

GENERATING FACILITIES..... The City's major generating facilities include 12 units which have a dependable combined capability on natural gas of 2,400 MW and two 418 MW coal-fired generating units. All of these units are capable of being operated on fuel oil.

CURRENT FUEL SUPPLY..... The City's electric and gas system is supplied with 82% of its natural gas by subsidiary companies of Valero Energy Corp. with the balance from other suppliers. The City has received all of the natural gas it has required to meet its needs, except in rare instances, during the past ten years. Fuel oil may be burned as required during curtailment periods, and current fuel oil inventories are equal to total fuel requirements for about 13 days. Coal is purchased under a long-term contract recently renegotiated as to price and present coal on hand in stockpile is approximately 3.8 months supply. The current gas contracts are being renegotiated at present (see Fuel Supply).

HISTORICAL NET REVENUES AND COVERAGE

Fiscal Years Ended 1-31:

	1984	1985	1986	1987	1987 ²
Gross Revenues	\$715,466,537	\$804,254,379	\$868,833,321	\$804,218,205	\$792,393,299
Maintenance & Operating Expenses ³	<u>466,297,794</u>	<u>479,875,730</u>	<u>495,832,215</u>	<u>418,015,977</u>	<u>393,028,550</u>
Net Revenues	\$249,168,743	\$324,378,649	\$373,001,106	\$386,202,228	\$399,364,749
Actual Principal and Interest Requirements:					
Old Series Bonds ¹	\$ 16,531,220	\$ 16,498,031	\$ 16,475,985	\$ 16,425,945	\$ 16,391,826
New Series Bonds ¹	\$104,765,394	\$129,894,634	\$156,675,078	\$176,761,411	\$187,093,178
Total All Bonds	\$121,296,614	\$146,392,665	\$173,151,063	\$193,187,356	\$203,485,004
ACTUAL COVERAGE	2.05x	2.22x	2.15x	2.00x	1.96x

Maximum Principal and Interest Requirements on all Bonds, including the New Series 1988 Bonds.....\$231,524,266 in 2003

COVERAGE 1.08x 1.40x 1.61x 1.67x 1.72x

¹ Net of accrued interest and premium received on bond issues sold.

² 12 months ending December 31, 1987.

³ Includes interest on short term obligations.

PRINCIPAL AND INTEREST REQUIREMENTS*

The following schedule reflects total principal and interest requirements on all Old Series Bonds and New Series Bonds, including the New Series 1988 Bonds.

Year Ending 2-1:	New Series Bonds						% of Principal Retired	
	\$160,000,000 New Series 1988 Bonds							
	Old Series Bonds	Presently Outstanding	Principa...	Interest	Total New Series	Total All Bonds		
1988	16,388,725	191,372,571			191,372,571	207,761,296		
1989	16,358,893	189,245,399			200,820,444	217,179,299		
1990	16,312,100	201,874,004	555,000	11,575,046	215,056,326	231,368,426		
1991	16,281,750	201,925,584	580,000	12,627,323	215,103,491	231,385,241		
1992	16,219,875	201,910,251	705,000	12,597,908	215,180,099	231,399,974		
1993	16,156,975	201,986,361	750,000	12,564,848	215,258,909	231,415,884	10.108%	
1994	16,109,700	202,066,919	775,000	12,475,673	215,317,591	231,427,291		
1995	14,677,500	203,502,766	835,000	12,425,298	216,763,064	231,440,564		
1996	14,587,500	203,612,881	885,000	12,369,353	216,867,234	231,454,734		
1997	14,445,000	203,745,881	970,000	12,308,288	217,024,169	231,469,169	26.229%	
1998		218,213,019	1,025,000	12,239,418	231,477,436	231,477,436		
1999		218,244,371	1,080,000	12,165,618	231,489,989	231,489,989		
2000		218,244,799	1,170,000	12,085,698	231,500,496	231,500,496		
2001		218,254,321	1,255,000	11,997,948	231,507,269	231,507,269		
2002		218,262,176	1,350,000	11,902,568	231,514,744	231,514,744	49.391%	
2003		218,290,649	1,435,000	11,798,618	231,524,266	231,524,266		
2004		189,157,759	6,510,000	11,687,405	207,355,164	207,355,164		
2005		164,498,346	7,045,000	11,179,625	182,722,971	182,722,971		
2006		116,729,116	7,630,000	10,630,115	134,989,231	134,989,231		
2007		116,681,269	8,255,000	10,027,345	134,963,614	134,963,614	70.551%	
2008		116,612,544	8,940,000	9,375,200	134,927,744	134,927,744		
2009		116,589,069	9,675,000	8,660,000	134,924,069	134,924,069		
2010		116,468,563	10,475,000	7,886,000	134,829,563	134,829,563		
2011		116,419,806	11,340,000	7,048,000	134,807,806	134,807,806		
2012		116,339,744	12,275,000	6,140,800	134,755,544	134,755,544	89.825%	
2013		116,248,619	13,285,000	5,158,800	134,692,419	134,692,419		
2014		85,654,294	14,385,000	4,096,000	104,135,294	104,135,294		
2015			17,680,000	2,945,200	20,625,200	20,625,200		
2016			19,135,000	1,530,800	20,665,800	20,665,800	100.000%	

* Actual requirements. Cents omitted, figures ending with \$0.50 have been rounded up to the next dollar, all other figures have been rounded to the nearest dollar.

FUND BALANCES
(At December 31, 1987)

Restricted Cash and Securities:

Old Series Bonds Reserve Account.....	\$ 17,165,859
Improvements and Contingencies Fund.....	\$ 161,154,460
New Series Bonds Reserve Amount.....	\$ 181,549,336

PROPERTY ADDITIONS
(At December 31, 1987)

Additions, Improvements and Extensions to Electric and Gas Systems, 1942-1987.....	\$3,923,220,910
Bonds Issued to Finance these Property Additions.....	\$2,456,560,000
Portion of Property Additions Financed by Issuance of Bonds.....	62.6%

OUTSTANDING INDEBTEDNESS

All revenue bonds of the City payable from the net revenues of the Electric and Gas Systems of the City and issued prior to 1968 have been retired. Including the New Series 1988 Bonds, the City will have outstanding Electric and Gas Systems Revenue Improvement Bonds in 31 series as follows:

	<u>Final Maturity</u>	<u>Original Average Life</u>	<u>Effective Interest Rate On Sale Date</u>	<u>20-Bond Yield Index Nearest Sale Date^a</u>	<u>Amount Outstanding^b</u>
Old Series Bonds					
Prior Lien (closed)					
Series 1968	1989	15.6 years	4.463%	4.41%	\$ 4,010,000
Series 1971	1992	14.7 years	5.166%	5.58%	14,220,000
Series 1973	1994	15.8 years	4.763%	5.03%	21,980,000
Series 1974	1997	17.3 years	6.896%	6.95%	65,575,000
Subtotal (Old Series Bonds)					\$ 105,785,000
New Series Bonds					
Series 1975	1998	16.0 years	7.390%	7.48%	\$ 36,050,000
Series 1976	1999	15.9 years	6.270%	6.98%	43,000,000
Series 1976-A	1999	16.4 years	5.179%	6.78%	44,725,000
Series 1977	2000	18.1 years	5.254%	5.78%	49,800,000
Series 1977-A	2002	23.7 years	5.718%	5.64%	75,000,000
Series 1978	2002	16.6 years	5.755%	5.65%	58,575,000
Series 1978-A	2003	16.5 years	5.978%	6.12%	59,650,000
Series 1979	2003	16.7 years	6.153%	6.50%	61,725,000
Series 1979-A	2004	18.3 years	6.048%	6.11%	87,325,000
Series 1980	2005	18.4 years	9.383%	9.20%	18,500,000 ^e
Series 1980-A	2005	17.8 years	8.823%	8.68%	42,000,000 ^e
Series 1981	2001	13.3 years	9.956%	10.40%	29,380,000 ^e
Series 1981-A	2005	16.5 years	12.675%	12.79%	5,795,000 ^c
Series 1982	2003	15.0 years	13.152%	12.71%	6,815,000 ^c
Series 1982-A	2003	15.1 years	10.350%	10.05%	26,325,000 ^e
Series 1983	2005	17.3 years	8.857%	8.86%	94,925,000
Series 1983-A	2013	21.9 years	10.451%	9.91%	35,650,000 ^d
Series 1984-A	2013	22.0 years	11.270%	10.50%	25,300,000 ^{d,e}
Series 1984-B	2014	22.0 years	10.968%	10.36%	24,900,000 ^{d,e}
Series 1985 (Refunding)	2005	14.1 years	9.875%	9.21%	116,380,000
Series 1985-A	2014	22.1 years	9.655%	9.75%	40,200,000 ^e
Series 1985-B	2014	21.9 years	9.472%	8.95%	86,875,000 ^e
Series 1986 (Refunding)	2014	21.9 years	7.835%	6.98%	320,660,000
Series 1986-A	2014	22.6 years	8.765%	8.08%	185,000,000
Series 1987 (Refunding)	2014	16.7 years	6.837%	6.54%	391,780,000
Series 1987-A	2014	22.1 years	7.013%	6.62%	160,000,000
Series 1988 ^f	2015	22.3 years			160,000,000
Subtotal (New Series Bonds)					\$2,286,335,000
Total Bonds to be Outstanding, Including the Bonds					\$2,392,120,000

^a As published by "The Bond Buyer."

^b As of February 1, 1988, and including the Bonds.

^c An additional amount of \$48,985,000 Series 1981-A Bonds and \$48,145,000 Series 1982 Bonds are outstanding but have been advance refunded by the New Series 1985 Refunding Bonds, and are fully defeased.

^d An additional amount of \$79,350,000 New Series 1983-A Bonds, \$91,400,000 New Series 1984-A Bonds and \$82,600,000 New Series 1984-B Bonds are outstanding but have been advance refunded by the New Series 1986 Refunding Bonds, and are fully defeased.

^e An additional amount of \$48,025,000 Series 1980 Bonds, \$34,825,000 Series 1980-A Bonds, \$32,675,000 Series 1981 Bonds, \$44,620,000 Series 1982-A Bonds, \$8,300,000 Series 1984-A Bonds, \$12,500,000 Series 1984-B Bonds, \$109,800,000 Series 1985-A Bonds and \$38,125,000 Series 1985-B Bonds are outstanding but have been advance refunded by the New Series 1987 Refunding Bonds, and are fully defeased.

^f Date: March 1, 1988.

REVENUE BOND INDEBTEDNESS AND UTILITY PLANTS

<u>Date 1-31:</u>	<u>Revenue Bond Indebtedness</u>	<u>Electric and Gas Plant Equipment</u>		<u>Debt as a % of Net Plant</u>
		<u>At Cost</u>	<u>Net (Depreciated)</u>	
1960	\$ 44,145,000	\$ 187,026,225	\$ 159,317,177	27.7
1965	54,190,000	279,053,625	226,794,522	23.9
1970	71,040,000	420,480,731	335,125,890	21.2
1975	201,195,000	677,114,390	542,919,917	37.1
1976	245,595,000	809,025,826	659,773,046	37.2
1977	358,110,000	954,207,395	790,395,043	45.3
1978	484,290,000	1,100,709,068	918,110,351	52.7
1979	622,975,000	1,265,232,510	1,056,105,552	59.0
1980	783,645,000	1,449,572,698	1,212,958,432	64.6
1.31	926,505,000	1,626,916,440	1,363,764,913	67.9
1982	1,041,105,000	1,804,344,072	1,515,056,423	68.7
1983	1,153,740,000	1,983,693,741	1,663,795,179	69.3
1984	1,342,785,000	2,236,612,812	1,885,959,134	71.2
1985	1,559,860,000	2,620,510,570	2,236,426,504	69.7
1986	1,824,070,000	2,838,847,230	2,420,104,511	75.4
1987	2,044,030,000	3,255,479,253	2,808,565,730	72.8
1987 ¹	2,266,940,000	3,602,808,133	3,132,662,667	72.4

¹ As of December 31, 1987.

COMMERCIAL PAPER PROGRAM

On November 10, 1983, the City Council of San Antonio authorized the issuance of \$100 million in tax-exempt commercial paper (the "Commercial Paper") to assist in the financing of capital improvements to the Systems. The marketing of such Commercial Paper commenced on December 1, 1983, and at present the City has \$58 million of its Commercial Paper outstanding. The Commercial Paper Program will expire in November, 1988, unless it is renewed or extended. The current plans are to extend the program.

The Commercial Paper is equally and ratably secured by and is payable from (i) the Net Revenues of the Systems, such pledge being subordinate and inferior to the pledge of Net Revenues securing the New Series Bonds and the Old Series Bonds, (ii) the proceeds from the sale of additional New Series Bonds or Commercial Paper, and (iii) borrowings under and pursuant to the Credit Agreement (as hereinafter defined). The City and Texas Commerce Bank National Association have entered into a revolving credit agreement (the "Credit Agreement") pursuant to which such bank is obligated under the Agreement to loan to the City an aggregate amount not to exceed \$100,000,000 for the purpose of paying amounts due on the Commercial Paper. Any borrowings under the Credit Agreement are equally and ratably secured by and payable from the above-described sources pledged for payment of the Commercial Paper.

BOND ORDINANCE PROVISIONS

Following are direct quotes of certain provisions of the Ordinance authorizing the Bonds (the "Ordinance").

SECTION 7: Definitions. Unless the context shall indicate a contrary meaning or intent, the terms below defined, for all purposes of this Ordinance or any Ordinance amendatory or supplemental thereto, shall be construed, are used, and are intended to have meanings as follows:

(a) "Additional Parity Bonds" - Bonds or other obligations authorized to be issued under the provisions of Section 18 hereof, including refunding bonds, which are secured by a lien on and pledge of the Net Revenues of the Systems on a parity with Previously Issued Parity Bonds and the New Series 1988 Bonds.

(b) "Board of Trustees," "Board," "City Public Service Board," "Public Service Board" - The City Public Service Board of San Antonio, Texas, existing and functioning pursuant to the Indenture or, subsequent to defeasance of the Indenture, existing and functioning pursuant to this Ordinance.

(c) "City" - the City of San Antonio, Texas and where appropriate, the City Council thereof.

(d) "Commercial Paper" - the presently outstanding "City of San Antonio, Texas, Electric and Gas Systems Commercial Paper Notes, Series A", the issuance of which was authorized by the City Council of the City by ordinance adopted on November 10, 1983, originally authorized in the principal amount of \$100,000,000, and the Revolving Note, as defined in said ordinance, each of which are secured by a pledge of the Net Revenues of the Systems subordinate to the pledge of the Net Revenues securing payment of the Old Series Bonds and the New Series Bonds.

(e) "Depository" - Such bank or banks at any time selected by the Board of Trustees to serve as depository of the funds hereinafter provided for with relation to the Parity Bonds.

(f) "Fiscal Year" - The twelve-month operational period of the Systems commencing on February 1 of each year and ending on the following January 31.

(g) "Indenture" - The Trust Indenture, dated February 1, 1951, together with eight supplements thereto dated August 1, 1953, February 1, 1957, February 1, 1960, August 1, 1962, February 1, 1968, February 1, 1971, February 1, 1973 and August 1, 1974, given as security for the Old Series Bonds.

(h) "Maintenance and Operating Expenses" - Those expenses required by the law (Article 1113, V.A.T.C.S.) to be a first lien on and charge against the income of the Systems, including the cost of insurance; the purchase and carrying of stores, materials and supplies; the purchase, manufacture and production of gas and electricity for distribution and resale; the payment of salaries; and the payment of all other expenses properly incurred in operating and maintaining the Systems and keeping them in good repair and operating condition (classed as a maintenance and operating expense as opposed to a capital expenditure under the Uniform System of Accounts adopted by the National Association of Regulatory Utility Commissioners). Depreciation on the properties of the Systems shall not be considered or included as Maintenance and Operating Expenses in the determination of Net Revenues of the Systems.

(i) "Net Revenues" - All income and revenues from the operation of the Systems after the deduction of Maintenance and Operating Expenses. The term "Net Revenues" shall also include any additional and further security for the payment of the Parity Bonds as may be pledged therefor consistent with the then applicable laws of the State of Texas, provided that any such additional and further security is made equally and ratably applicable as security for all outstanding Parity Bonds.

(j) "New Series 1988 Bonds" or "Bonds" - The bonds authorized by this Ordinance.

(k) "Old Series Bonds" - The presently outstanding City of San Antonio Electric and Gas Systems Revenue Improvement Bonds, Series 1968, Series 1971, Series 1973 and Series 1974.

(l) "Parity Bonds" or "New Series Bonds" - The Previously Issued Parity Bonds, the New Series 1988 Bonds and any Additional Parity Bonds.

(m) "Paying Agent/Registrar" - The bank, trust company, or other duly qualified and legally authorized entity named from time to time as Paying Agent/Registrar for the New Series 1988 Bonds, and any Additional Parity Bonds hereafter issued in registered form.

(n) "Previously Issued Parity Bonds" - The outstanding and unpaid bonds of the following series, to wit: "CITY OF SAN ANTONIO, TEXAS, ELECTRIC AND GAS SYSTEMS REVENUE IMPROVEMENT BONDS, NEW SERIES 1975", dated August 1, 1975, and originally issued in the total principal amount of \$50,000,000; "CITY OF SAN ANTONIO, TEXAS, ELECTRIC AND GAS SYSTEMS REVENUE IMPROVEMENT BONDS, NEW SERIES 1976", dated February 1, 1976, and originally issued in the total principal amount of \$60,000,000; "CITY OF SAN ANTONIO, TEXAS, ELECTRIC AND GAS SYSTEMS REVENUE IMPROVEMENT BONDS, NEW SERIES 1976-A", dated August 1, 1976 and originally issued in the total

principal amount of \$60,000,000; "CITY OF SAN ANTONIO, TEXAS, ELECTRIC AND GAS SYSTEMS REVENUE IMPROVEMENT BONDS, NEW SERIES 1977", dated February 1, 1977, and originally issued in the total principal amount of \$60,000,000; "CITY OF SAN ANTONIO, TEXAS, ELECTRIC AND GAS SYSTEMS REVENUE IMPROVEMENT BONDS, NEW SERIES 1977-A", dated August 1, 1977, and originally issued in the total principal amount of \$75,000,000; "CITY OF SAN ANTONIO, TEXAS, ELECTRIC AND GAS SYSTEMS REVENUE IMPROVEMENT BONDS, NEW SERIES 1978", dated February 1, 1978, and originally issued in the total principal amount of \$75,000,000; "CITY OF SAN ANTONIO, TEXAS, ELECTRIC AND GAS SYSTEMS REVENUE IMPROVEMENT BONDS, NEW SERIES 1978-A", dated August 1, 1978, and originally issued in the total principal amount of \$75,000,000; "CITY OF SAN ANTONIO, TEXAS, ELECTRIC AND GAS SYSTEMS REVENUE IMPROVEMENT BONDS, NEW SERIES 1979", dated February 1, 1979, and originally issued in the total principal amount of \$75,000,000; "CITY OF SAN ANTONIO, TEXAS, ELECTRIC AND GAS SYSTEMS REVENUE IMPROVEMENT BONDS, NEW SERIES 1979-A", dated August 1, 1979, and originally issued in the total principal amount of \$100,000,000; "CITY OF SAN ANTONIO, TEXAS, ELECTRIC AND GAS SYSTEMS REVENUE IMPROVEMENT BONDS, NEW SERIES 1980", dated February 1, 1980, and originally issued in the total principal amount of \$75,000,000; "CITY OF SAN ANTONIO, TEXAS, ELECTRIC AND GAS SYSTEMS REVENUE IMPROVEMENT BONDS, NEW SERIES 1980-A", dated August 1, 1980, and originally issued in the total principal amount of \$85,000,000; "CITY OF SAN ANTONIO, TEXAS, ELECTRIC AND GAS SYSTEMS REVENUE IMPROVEMENT BONDS, NEW SERIES 1981", dated February 1, 1981, and originally issued in the total principal amount of \$75,000,000; "CITY OF SAN ANTONIO, TEXAS, ELECTRIC AND GAS SYSTEMS REVENUE IMPROVEMENT BONDS, NEW SERIES 1981-A", dated October 1, 1981, and originally issued in the total principal amount of \$60,000,000; "CITY OF SAN ANTONIO, TEXAS, ELECTRIC AND GAS SYSTEMS REVENUE IMPROVEMENT BONDS, NEW SERIES 1982", dated February 1, 1982, and originally issued in the total principal amount of \$60,000,000; "CITY OF SAN ANTONIO, TEXAS, ELECTRIC AND GAS SYSTEMS REVENUE IMPROVEMENT BONDS, NEW SERIES 1982-A", dated August 1, 1982, and originally issued in the total principal amount of \$75,000,000; "CITY OF SAN ANTONIO, TEXAS, ELECTRIC AND GAS SYSTEMS REVENUE IMPROVEMENT BONDS, NEW SERIES 1983", dated April 1, 1983, and originally issued in the total principal amount of \$100,000,000; "CITY OF SAN ANTONIO, TEXAS, ELECTRIC AND GAS SYSTEMS REVENUE IMPROVEMENT BONDS, NEW SERIES 1983-A", dated November 1, 1983, and originally issued in the total principal amount of \$115,000,000; "CITY OF SAN ANTONIO, TEXAS, ELECTRIC AND GAS SYSTEMS REVENUE IMPROVEMENT BONDS, NEW SERIES 1984-A", dated June 1, 1984, and originally issued in the total principal amount of \$125,000,000; "CITY OF SAN ANTONIO, TEXAS, ELECTRIC AND GAS SYSTEMS REVENUE IMPROVEMENT BONDS, NEW SERIES 1984-B", dated October 1, 1984, and originally issued in the total principal amount of \$120,000,000; "CITY OF SAN ANTONIO, TEXAS, ELECTRIC AND GAS SYSTEMS REVENUE REFUNDING BONDS, NEW SERIES 1985", dated January 15, 1985, and originally issued in the total principal amount of \$116,380,000; "CITY OF SAN ANTONIO, TEXAS, ELECTRIC AND GAS SYSTEMS REVENUE IMPROVEMENT BONDS, NEW SERIES 1985-A", dated April 1, 1985, and originally issued in the total principal amount of \$150,000,000; "CITY OF SAN ANTONIO, TEXAS, ELECTRIC AND GAS SYSTEMS REVENUE IMPROVEMENT BONDS, NEW SERIES 1985-B", dated October 1, 1985, and originally issued in the total principal amount of \$125,000,000; "CITY OF SAN ANTONIO, TEXAS, ELECTRIC AND GAS SYSTEMS REVENUE REFUNDING BONDS, NEW SERIES 1986", dated February 1, 1986, and originally issued in the total principal amount of \$320,660,000; "CITY OF SAN ANTONIO, TEXAS, ELECTRIC AND GAS SYSTEMS REVENUE IMPROVEMENT BONDS, NEW SERIES 1986-A", dated April 1, 1986, and originally issued in the total principal amount of \$185,000,000; "CITY OF SAN ANTONIO, TEXAS, ELECTRIC AND GAS SYSTEMS REVENUE REFUNDING BONDS, NEW SERIES 1987", dated January 1, 1987, and originally issued in the total principal amount of \$391,780,000; and "CITY OF SAN ANTONIO, TEXAS ELECTRIC AND GAS SYSTEMS REVENUE IMPROVEMENT BONDS, NEW SERIES 1987-A", dated February 1, 1987, and originally issued in the total principal amount of \$160,000,000.

* * *

(o) "Systems" - The entire electric light and power plants and systems and gas distribution system and all property of every kind appurtenant to and used or acquired in connection with said electric light and power plant and systems and gas distribution system owned by the City and described in and covered by the Indenture, together with all property of every kind now and hereafter owned or acquired by the City as a part of or for use in the operation of the City's electric light and power plants and systems and gas distribution system.

* * *

SECTION 8: Pledge. The City hereby covenants and agrees with the holders of the Parity Bonds that:

(a) Until such time as the terms, conditions and provisions of the Indenture become inoperative and the "Trust Estate" conveyed by the Indenture reverts to the City free and clear of the encumbrance created thereby, the Parity Bonds shall be and are hereby declared to be payable solely from and equally secured by an irrevocable pledge of and lien on that portion of the Net Revenues of the Systems deposited and available for deposit in (i) the "Electric and Gas Systems Improvements and Contingencies Fund" established pursuant to Section 6 of Article V of the Indenture and (ii) the General Fund of the City pursuant to Sections 5 and 6 of Article V of the Indenture.

(b) At such time as the terms, conditions and provisions of the Indenture become inoperative and the "Trust Estate" conveyed by the Indenture reverts to the City free and clear of the encumbrance created thereby, the Net Revenues shall be and are hereby irrevocably pledged to the payment of principal of and interest on (including the establishment and maintenance of a reserve, as provided in Sections 12 and 18 (e) of this Ordinance) the Parity Bonds, and it is hereby ordained that at such time all Parity Bonds and the interest thereon shall constitute a first lien upon the Net Revenues of the Systems.

SECTION 9: Rates and Charges. The City hereby agrees and reaffirms its covenants to the holders of the Parity Bonds that it will at all times maintain rates and charges for the sale of electric energy, gas or other services furnished, provided, and supplied by the Systems to the City and all other consumers which shall be reasonable and nondiscriminatory and which will produce income and revenues sufficient to pay:

- (a) All Maintenance and Operating Expenses; depreciation, replacement, and betterment expenses; and other costs as may be required by law (Article 1113, V.A.T.C.S.);
- (b) The interest on and principal of all Old Series Bonds, as and when the same shall become due, and maintain the Funds and Accounts created and established for the payment and security of the Old Series Bonds;
- (c) The interest on and principal of all Parity Bonds, as and when the same shall become due, and provide for the establishment and maintenance of the Funds and Accounts created for the payment and security of the Parity Bonds;
- (d) To the extent the same are reasonably anticipated to be paid with "Available Revenues" as defined in the ordinance authorizing the Commercial Paper, the interest on and principal of all "Notes", as defined in said ordinance, and the "Agreement", as defined in said ordinance; and
- (e) Any legal debt or obligation of the Systems as and when the same shall become due.

SECTION 10: General Account. The City, acting through the Board of Trustees, hereby reaffirms its covenant to holders of the Old Series Bonds and hereby covenants with respect to the holders of the Parity Bonds, that all revenues of every nature received through the operation of the Systems shall be deposited as received in the "CITY OF SAN ANTONIO ELECTRIC AND GAS SYSTEMS GENERAL ACCOUNT" (hereinafter referred to as "General Account"), which shall be kept separate and apart from all other funds of the City. Revenues received for the General Account shall be deposited from time to time as received in such bank or banks as may be selected by the Board of Trustees in accordance with applicable laws relating to the selection of City depositories.

SECTION 11: Flow of Funds. The City, acting through the Board of Trustees, hereby agrees and reaffirms its covenant to the holders of the Parity Bonds that:

(a) Until such time as all the terms, conditions and provisions of the Indenture shall become inoperative and the "Trust Estate" conveyed by the Indenture reverts to the City free and clear of the encumbrance created thereby, funds in the General Account shall be pledged and appropriated to the following uses in the order of precedence shown:

FIRST: For the payment of operation, maintenance, repairs, and extensions of the Systems provided for in Article 1113, V.A.T.C.S., and Section 3 of Article V of the Indenture;

SECOND: To the payment of the principal of and interest on the Old Series Bonds, and to the "San Antonio Electric and Gas Systems Bond Reserve Account" for the benefit of the Old Series Bonds in the manner and to the extent required in Section 4 of Article V of the Indenture;

THIRD: To the payment of the annual sum to be deposited in the General Fund of the City in accordance with and to the extent set out in Section 5 of Article V of the Indenture;

FOURTH: To the payment of the annual sum (equal to not less than 12-1/2% of the gross revenues of the Systems) to be deposited in the "Electric and Gas Systems Improvements and Contingencies Fund" in accordance with Section 6 (as amended) of Article V of the Indenture;

FIFTH: To the payment of the annual sum to the General Fund of the City for reimbursement of gas and electric services of the Systems used by the City for municipal purposes and amounts expended for additions to the street and traffic lighting system (such payment, together with the annual sum to be deposited in the General Fund of the City, in accordance with Section 5 of Article V of the Indenture, to total an amount equal to 14% of the gross revenues of the Systems for the current Fiscal Year), as provided in Section 6 (as amended) of Article V of the Indenture;

SIXTH: To the "Electric and Gas Systems Improvements and Contingencies Fund" until there is on deposit therein an amount equal to 20% of the value of fixed capital assets as shown by the audited statement as of the end of a Fiscal Year, as provided in Section 6 (as amended) of Article V of the Indenture; and

SEVENTH: To the "Electric and Gas Systems Surplus Fund" in the manner and to the extent funds are available, as required by Section 6 (as amended) of Article V of the Indenture.

In further explanation of said flow of funds as to the payment and security of the Parity Bonds, the Net Revenues deposited in the "Electric and Gas Systems Improvements and Contingencies Fund" shall be first appropriated and pledged to the "City of San Antonio Electric and Gas Systems Parity Bond Retirement Account" (heretofore created for the payment of principal of and interest on Parity Bonds and reaffirmed in Section 12 of this Ordinance); and to the extent necessary, all sums payable to the General Fund of the City from the Net Revenues pursuant to Sections 5 and 6 (as amended) of Article V of the Indenture shall be first appropriated and pledged to said "City of San Antonio Electric and Gas Systems Parity Bond Retirement Account."

(Note: The following schedule is not a part of the Ordinance)

**ACTUAL APPLICATION OF REVENUES UNDER
TRUST INDENTURE AND SECTION 11 (a) OF NEW SERIES BOND ORDINANCE
(Flow of Funds)**

	Fiscal Year Ended January 31:				
	1984	1985	1986	1987	1987 ⁴
OPERATING REVENUES					
Electric	\$544,125,191	\$636,364,073	\$700,371,599	\$639,625,682	\$623,670,233
Gas	<u>147,890,056</u>	<u>133,301,552</u>	<u>136,499,691</u>	<u>127,814,360</u>	<u>128,922,984</u>
Total	<u>692,015,247</u>	<u>769,665,625</u>	<u>836,871,290</u>	<u>767,440,042</u>	<u>752,593,217</u>
OPERATING EXPENSES					
Electric	325,642,247	357,235,968	376,396,173	303,302,679	281,925,086
Gas	<u>140,381,157</u>	<u>122,222,706</u>	<u>115,173,906</u>	<u>113,193,837</u>	<u>107,621,282</u>
Total	<u>466,023,404</u>	<u>479,458,674</u>	<u>494,570,079</u>	<u>416,496,516</u>	<u>389,546,368</u>
Net Operating Income	225,991,843	290,206,951	342,301,211	350,943,526	363,046,849
Non Operating Income (Net)	<u>23,045,003</u>	<u>33,930,519</u>	<u>28,821,710</u>	<u>36,778,162</u>	<u>39,800,080</u>
Net Revenues	<u>\$249,036,846</u>	<u>\$324,137,470</u>	<u>\$371,122,921</u>	<u>\$387,721,688</u>	<u>\$402,846,929</u>
Interest During Construction	<u>48,439,378</u>	<u>64,467,070</u>	<u>87,295,643</u>	<u>101,402,372</u>	<u>106,491,190</u>
Revenues Available for Application	<u>\$297,476,224</u>	<u>\$388,604,540</u>	<u>\$458,418,564</u>	<u>\$489,124,060</u>	<u>\$509,338,119</u>
ALLOCATION OF AVAILABLE REVENUES					
1. Operating Funds (To increase working capital), and Payment of debt	\$ -0-	\$ -0-	\$ 2,500,000	\$ -0-	\$ -0-
Principal & Interest ¹	16,531,219	16,498,031	16,475,985	16,425,945	16,391,826
Reserve Fund Reqs. ¹	<u>24,615</u>	<u>(16,249)</u>	<u>(46,276)</u>	<u>(83,983)</u>	<u>(51,992)</u>
Total Payment of Debt ¹	<u>16,555,634</u>	<u>16,481,782</u>	<u>18,929,709</u>	<u>16,341,962</u>	<u>16,339,834</u>
2. Payments to General Fund of City in lieu of taxes	6,028,200	6,400,800	7,095,600	7,798,800	8,850,400
3. To Improvements and Contingencies Fund- Minimum Requirements	89,433,317	100,531,797	108,604,165	100,527,276	99,049,162
4. Payment to General Fund of City as reimbursement for electric and gas services used by City during year	14,162,624	16,351,404	17,009,419	15,286,097	15,549,451
5. Additional payment to City to bring benefits to 14% of Gross Revenues ³	61,501,705	72,755,528	79,867,247	73,105,722	72,834,416
6. Balance transferred to Improvements and Contingencies Fund ²	<u>109,796,746</u>	<u>176,083,229</u>	<u>226,912,424</u>	<u>276,064,203</u>	<u>296,714,856</u>
Total Allocations	<u>\$297,476,224</u>	<u>\$388,604,540</u>	<u>\$458,418,564</u>	<u>\$489,124,060</u>	<u>\$509,338,119</u>

Footnotes:

¹ Old Series Bonds.

² New Series Bonds principal interest and New Series Reserve payments made from the Improvements and Contingency Fund for the years as shown above were as follows:

Principal	18,120,000	19,730,000	21,440,000	23,350,000	25,215,616
Interest	86,645,393	110,164,634	135,235,078	153,411,411	161,877,762
Reserve	15,298,928	6,048,979	11,502,666	20,112,307	10,492,360

³ Annual amounts shown are less than 14% because of voluntary reduction by the City.

⁴ 12 months ending December 31, 1987.

The following continues quotations from the Ordinance.

SECTION 11: Flow of Funds

(b) At such time as all the terms, conditions, and provisions of the Indenture shall become inoperative and the "Trust Estate" conveyed by the Indenture reverts to the City free and clear of the encumbrance created thereby, funds in the General Account shall be pledged and appropriated to the following uses and in the order of precedence shown:

FIRST: To the payment of reasonable and proper Maintenance and Operating Expenses of the Systems upon approval by the Board of Trustees;

SECOND: To the payment of Parity Bonds, including the establishment and maintenance of the reserve therefor;

THIRD: To the payment of "Prior Lien Bonds" (as defined in the ordinance authorizing the Commercial Paper), if any, including the establishment and maintenance of a reserve therefor;

FOURTH: To the payment and security of the "Notes" and the "Agreement" (as defined in the ordinance authorizing the Commercial Paper);

FIFTH: To the payment and security of obligations hereinafter issued which are inferior in lien to the Parity Bonds and the Notes;

SIXTH: To the payment of an annual amount equal to six percent (6%) of the gross revenues of the Systems to be deposited in the Repair and Replacement Account, hereinafter provided for in Section 13 of this Ordinance;

SEVENTH: To the payment of the annual amount due the General Fund of the City of San Antonio, as provided in Section 14 of this Ordinance; and

EIGHTH: Any remaining Net Revenues of the Systems in the General Account, to the Repair and Replacement Account, in accordance with Section 13 of this Ordinance.

SECTION 12: Parity Bond Retirement Account. For purposes of paying the principal of and interest on the Parity Bonds, when and as the same shall become due, and providing a reserve to prevent a default in the payment of such principal and interest on Parity Bonds, the City, acting through the Board of Trustees, hereby reaffirms the creation and establishment of a special account known as the "City of San Antonio Electric and Gas Systems Parity Bond Retirement Account" (hereinafter referred to as "Retirement Account"), which account shall continue to be kept separate and apart from all other funds or accounts of the Systems or of the City. The City hereby reaffirms its covenant that the Retirement Account shall be established and kept at such Depository as the Board of Trustees shall designate and funds deposited therein shall be used only for the purpose of paying the principal of and interest on the Parity Bonds.

From the Net Revenues pledged to the payment and security of the Parity Bonds (identified in Section 7 of this Ordinance), the Board of Trustees shall cause to be paid in the Retirement Account such amounts as will be fully sufficient to (i) promptly pay, when due, all principal of and interest on the Parity Bonds (hereinafter sometimes referred to as the "interest and sinking fund portion" of the Retirement Account) and (ii) establish and maintain in the Retirement Account a reserve amount (hereinafter sometimes referred to as the "Reserve Amount" or "reserve fund portion") equal to not less than the average annual principal and interest requirements of all outstanding Parity Bonds (calculated on a Fiscal Year basis as of the date the last series of Parity Bonds were authorized). In addition, all sums received from the purchasers of Parity Bonds constituting accrued interest and premium, if any, shall be placed in the interest and sinking fund portion of the Retirement Account.

In addition to the deposits required to be made in the interest and sinking fund portion of the Retirement Account to pay the annual debt service requirements of the Previously Issued Parity Bonds, the City Public Service Board is hereby directed to deposit in said Account the following amounts to pay the principal of and interest on the New Series 1988 Bonds, to wit:

(a) Deposits for payment of interest - on or before the 15th day of the first month to occur following the date of delivery of the New Series 1988 Bonds to the purchasers thereof and on or before the 15th day of each following month through July 15, 1988, an equal amount of money with such deposits totaling not less than the amount of the installment of interest coming due on the Bonds on August 1, 1988, and beginning on or before August 15, 1988 and on or before the 15th day of each following month, until the New Series 1988 Bonds are no longer outstanding, an amount of money equal to not less than one-sixth (1/6) of the next semiannual installment of interest to become due on the New Series 1988 Bonds; provided, that to the extent there are moneys available in the interest and sinking fund portion of the Retirement Account to pay interest on the New Series 1988 Bonds on August 1, 1988 or February 1, 1989, such deposits may be reduced by the amount of the aforesaid moneys available to pay said interest on the New Series 1988 Bonds.

(b) Deposits for payment of principal - on or before February 15, 1989, and on or before the 15th day of each following month, until the New Series 1988 Bonds are no longer outstanding, an amount of money equal to not less than one-twelfth (1/12) of the next annual principal payment to become due on said New Series 1988 Bonds (exclusive of Term Bonds), and during each of the 12 month periods preceding the dates the Term Bonds mature or are required to be redeemed prior to maturity not less than one-twelfth (1/12) of the principal amount required herein to be paid at maturity or to be redeemed prior to scheduled maturity. In compliance with the provisions of the ordinances authorizing the issuance of the Previously Issued Parity Bonds and this Ordinance, the Board of Trustees shall cause to be accumulated and maintained in the Retirement Account a Reserve Amount equal to not less than the average annual principal and interest requirements of the Previously Issued Parity Bonds and the New Series 1988 Bonds, such Reserve Amount to be determined on the basis of cash on deposit and the book value of securities in which moneys in the reserve fund portion of the Retirement Account are invested, and to be in addition to the amount on deposit in the Retirement Account for purposes of paying the annual debt service requirements of the outstanding Parity Bonds. The City Public Service Board shall cause to be deposited into the reserve fund portion of the Retirement Account from the proceeds of the New Series 1988 Bonds, if necessary, an amount sufficient, together with moneys accumulated in the reserve fund portion of the Retirement Account, to cause the Reserve Amount to equal not less than the average annual principal and interest requirements of the Previously Issued Parity Bonds and the New Series 1988 Bonds. Whenever the amount in the reserve fund portion of the Retirement Account equals less than the total amount required to be on deposit therein in accordance with the provisions of this Ordinance monthly deposits in an amount equal to the sum of the monthly deposits required under the provisions of the ordinances authorizing the Previously Issued Parity Bonds and this Ordinance shall be resumed and continued to be made on or before the 15th day of each month until the total amount required to be on deposit in the reserve fund portion of the Retirement Account has been fully restored.

In the event there are insufficient funds available in any month to permit the required monthly deposits in the Retirement Account for purposes of paying the annual debt service requirements on the Parity Bonds and accumulating and maintaining the Reserve Amount, either or both, amounts equivalent to such deficiencies shall be set apart and paid into the said Account from the first available and unallocated Net Revenues pledged to the payment of the Parity Bonds in the next following month or months, and such payments shall be in addition to the monthly amounts otherwise required to be paid into said Account during such month or months.

Accrued interest and premium, if any, received from purchasers of Parity Bonds which is deposited in the interest and sinking fund portion of the Retirement Account and income and profits received from the investment of funds in the Retirement Account may be taken into consideration and reduce the monthly deposits which would otherwise be required to be placed in the interest and sinking fund portion and reserve fund portion of the Retirement Account from the Net Revenues.

SECTION 13: Repair and Replacement Account. At such time as the provisions of the Indenture become inoperative, the City reaffirms its covenant with the holders of Parity Bonds that a special fund or account shall be created and established to be known as the "City of San Antonio Electric and Gas Systems Repair and Replacement Account" (hereinafter called "Repair and Replacement Account") at such Depository as may be designated by the Board of Trustees. Moneys on deposit in the Repair and Replacement Account shall be used for the following purposes, to-wit: (i) providing extensions, additions and improvements to the Systems; (ii) to meet contingencies of any nature in connection with the operations, maintenance, improvement, replacement or restoration of properties of the Systems; and (iii) the payment of bonds or other obligations for which other funds are not available, or for any or all of such purposes, as, from time to time, may be determined by the Board of Trustees.

From the Net Revenues remaining in the General Account after payment and provisions for payments and additions to the Retirement Account in accordance with the provisions of Section 12 hereof, there shall be paid into the Repair and Replacement Account an annual sum equal to 6% of the gross revenues of the Systems for the then current Fiscal Year. This annual payment to the Repair and Replacement Account shall be accumulated each Fiscal Year by monthly installments, such monthly installments to be based on each month's gross revenues to the extent funds in the General Account are available each month; provided, however, should the total annual payment to the Repair and Replacement Account in any Fiscal Year exceed 6% of the gross revenues of the Systems, as shown by the Systems' audited annual financial statement, proper year-end adjustments shall be made (on or before the March 1 following the close of each Fiscal Year) by causing any excess amount deposited therein to be transferred to the General Account.

No deposit in excess of 6% of the annual gross revenues of the Systems shall be made to the Repair and Replacement Account (as provided in the preceding paragraph of this Section) unless and until complete and full payments, or provisions for such payments, shall have been paid over or credited to the General Fund of the City in accordance with Section 14 of this Ordinance. After complete and full payments, or provisions for such payments, shall have been paid over or credited to the General Fund of the City to the full extent required in Section 14 hereof, additional deposits may be made to the Repair and Replacement Account; and at the close of each Fiscal Year, all Net Revenues remaining in the General Account after full and complete payment to the General Fund of the City has been made (except such amounts as may be required to meet unpaid accounts and obligations which have accrued or are payable during the year to insure continued operation of the Systems), shall be deposited in the Repair and Replacement Account.

SECTION 14: Payments or Credits to the General Fund of the City. In accordance with the provisions of the ordinances authorizing the issuance of the Previously Issued Parity Bonds and at such time as the provisions of the Indenture shall become inoperative and after the payments to the Retirement Account and the Repair and Replacement Account (for purposes of accumulating therein an amount equal to 6% of the annual gross revenues of the Systems) have been made in full in accordance with the provisions of Sections 12 and 13 of this Ordinance, there shall be paid over or credited to the General Fund of the City (for general purposes of the City), to the extent Net Revenues are available in the General Account and in monthly installments, an amount in cash not to exceed 14% of the gross revenues of the Systems for the month next preceding the month in which the monthly deposit is made, less the value of gas and electric services of the Systems used by the City for municipal purposes and the amount expended for additions to the street lighting system for the month for which such payment is being made. The maximum amount in cash to be transferred or credited to the General Fund of the City from the Net Revenues during any Fiscal Year shall not exceed 14% of the gross revenues of the Systems less the value of gas and electric services of the Systems used by the City for municipal purposes and the amounts expended during the Fiscal Year for additions to the street lighting system. The percentage of gross revenues of the Systems to be paid over or credited to the General Fund of the City each Fiscal Year shall be determined (within the 14% limitation) by the governing body of the City.

SECTION 15: Investments. In accordance with the provisions of the ordinances authorizing the issuance of the Previously Issued Parity Bonds and this Ordinance, funds on deposit in the Retirement Account and the Repair and Replacement Account may be, at the option of the Board of Trustees, invested in direct obligations of the United States of America; obligations which in the opinion of the Attorney General of the United States are general obligations of the United States and backed by its full faith and credit; obligations guaranteed by the United States of America; evidences of indebtedness of the Federal Land Banks, Federal Intermediate Credit Banks, Banks for Cooperatives, Federal Home Loan Banks, Federal National Mortgage Association; Participation Certificates in the Federal Assets Financing Trust; and Certificates of Deposit of any bank or trust company which are fully secured in the manner and to the fullest extent required by the laws of the State of Texas for the security of public funds. Any obligations, or evidences of ownership of said obligations, in which funds on deposit in the aforementioned Accounts are so invested shall be kept in escrow in the respective Depository for such Accounts and such investments shall be promptly sold when required and the proceeds of the sale applied to the making of payments required to be made from the Account from which the investment was made whenever such payments are necessary to be made. All income and profits received from the investment of funds in the Repair and Replacement Account shall be transferred and credited to the General Account. During the period of time the Reserve Amount in the Retirement Account totals not less than the total amount required to be on deposit therein, all income and profits received from the investment of such funds shall be transferred to the interest and sinking fund portion of the Retirement Account, thereby reducing the amount required to be deposited therein, to meet the debt service requirements of Parity Bonds; otherwise income and profits received from investments of the funds constituting the Reserve Amount shall be retained as a portion of the Reserve Amount. Income and profits received from investments of funds on deposit in the interest and sinking fund portion of the Retirement Account shall be used only for the purposes of paying the principal of and interest on the Parity Bonds, as and when the same shall become due.

SECTION 16: Transfer of Funds to the Paying Agent/Registrar. On or before an interest or principal payment date of any Parity Bonds, the Treasurer of the City Public Service Board shall make transfer of funds on deposit in the Retirement Account to the paying agent, or paying agents, (including the Paying Agent/Registrar) in the amounts calculated as fully sufficient to pay and discharge promptly, as due, each installment of interest and principal pertaining to the Parity Bonds then outstanding. In the event Parity Bonds may be called for redemption prior to maturity, the Treasurer of the City Public Service Board shall cause amounts calculated as sufficient to pay and discharge the Parity Bonds (including accrued interest and premium, if any) so called for redemption to be transferred to the paying agent, or paying agents, (including Paying Agent/Registrar), as applicable, on or before the date fixed for the redemption of such bonds.

SECTION 17: Security of Funds. All moneys on deposit in the special Funds or Accounts for which this Ordinance makes provision (except any portions thereof as may be at any time properly invested) shall be secured in the manner and to the fullest extent required by the laws of the State of Texas for the security of public funds.

SECTION 18: Issuance of Additional Parity Bonds. In addition to the right to issue obligations of inferior lien, as authorized by the laws of the State of Texas, the City reserves the right to issue additional revenue obligations payable from the same source and equally secured in the same manner as the Previously Issued Parity Bonds and the New Series 1988 Bonds and such additional revenue obligations, the Previously Issued Parity Bonds and the New Series 1988 Bonds shall in all respects be of equal dignity. The amount of additional revenue obligations for Systems' improvements and extensions to be issued from time to time shall be based upon the difference between the estimated costs of planned extensions and improvements and the total of the funds available and estimated to be available for extensions and improvements to the Systems; and it shall be the duty of the Board of Trustees to request the City Council to authorize and provide for the issuance and sale of additional revenue obligations in the amount necessary to meet the cost of such planned extensions and improvements, such request to be evidenced by resolution of the Board of Trustees; and upon receipt of such request, it shall be the duty of the City Council to review such request and to provide for the issuance and sale of such Additional Parity Bonds as the City Council may deem necessary in order that the planned extensions and improvements may be made. It is hereby covenanted and agreed that no additional revenue bonds or other obligations shall be issued or incurred on a parity with the New Series Bonds unless and until the following conditions can be satisfied and met:

(a) Until such time as the Indenture securing payment of the Old Series Bonds shall have terminated, the Board of Trustees by resolution shall have consented to the issuance of such Additional Parity Bonds and the payment thereof from the Net Revenues, and shall have further agreed to comply with all of the terms and provisions of the ordinance authorizing such Additional Parity Bonds with relation to the operation of the Systems and the disposition of revenues of the Systems.

(b) The Treasurer of the City Public Service Board shall have executed a certificate stating that the City is not in default as to any covenant, obligation or undertaking contained in any ordinance or other document relating to the issuance of any obligations then outstanding which are payable from and secured by a lien on and pledge of the Net Revenues, and that each of the Funds and Accounts created and established for the sole purpose of paying the principal of and interest on such obligations contains the amount then required to be on deposit therein.

(c) The Board of Trustees shall have secured from an independent certified public accountant a certificate evidencing his determination that the Net Revenues (including earnings from the investment of Systems' funds) were, during the last completed Fiscal Year or for any consecutive 12 month period during the last 15 consecutive months prior to the month of adoption of the ordinance authorizing the issuance of the additional obligations, equal to at least one and one-half times the maximum annual principal and interest requirements on the then outstanding Old Series Bonds and Parity Bonds and the Parity Bonds then proposed to be issued. For the purpose of making such determination, the certified public accountant may adjust the Net Revenues to include a proper allowance for revenues arising from any increase in electric and gas rates which has become effective prior to the issuance of the proposed Additional Parity Bonds, but which during all or any part of the past Fiscal Year, or other 12 month period used for determining said Net Revenues was not in effect, in an amount equal to the amount by which the billings of the Systems to customers for such Fiscal Year or 12 month period would have been increased if such increase in rates had been in effect during the whole of such Fiscal Year or 12 month period.

(d) The Additional Parity Bonds are to mature on February 1 or August 1, or both, in each of the years in which they are scheduled to mature.

(e) The ordinance authorizing the issuance of the Additional Parity Bonds provides that the amount to be accumulated and maintained in the Retirement Account as the Reserve Amount shall be an amount equal to not less than the average annual requirements for the payment of principal of and interest on all Parity Bonds which will be outstanding after giving effect to the issuance of the Additional Parity Bonds then being issued; and provides that any increase to the Reserve Amount in the Retirement Account shall be accumulated within five years and one month from the date of passage of the ordinance authorizing the issuance of the Additional Parity Bonds.

Provided, however, that Parity Bonds may be issued from time to time (pursuant to any law then available) for purposes of refunding outstanding Old Series Bonds and Parity Bonds upon such terms and conditions as the governing body of the City and the Board of Trustees may deem to be in the best interest of the City and, if less than all outstanding Parity Bonds are refunded, or if Parity Bonds are issued to refund outstanding Old Series Bonds, the proposed refunding bonds shall be considered as "Additional Parity Bonds" under the provisions of this Section, but the certificate required in paragraph (c) of this Section shall give effect to the issuance of the proposed refunding bonds (and shall not give effect to the bonds being refunded following their cancellation or provision being made for their payment). Parity Bonds and Old Series Bonds shall not be considered to be "outstanding" (under the provisions of this Ordinance) when provision has been made for their payment in the manner and to the extent permitted by the laws of the State of Texas applicable at the time such provision is made.

And provided, further, that any obligations hereafter issued which are junior and subordinate in all respects to the Parity Bonds may (without impairment of the obligation of contract of the Parity Bonds) be refunded as Parity Bonds by meeting all the terms and conditions for the issuance of Additional Parity Bonds; and such junior lien obligations may achieve the status of and become, for all purposes Parity Bonds when the following conditions can be met and upon the happening of the following events, to-wit: (i) the Board of Trustees shall have caused to be filed with the City Clerk of the City a certified written report of an independent certified public accountant demonstrating that the Net Revenues, during the last completed Fiscal Year or for any 12 consecutive months during the last 15 months prior to the month of filing such report, were equal to at least one and one-half times the maximum annual requirements for the payment of principal of and interest on the then outstanding Old Series Bonds, Parity Bonds and for the bonds then proposed to achieve the status of Parity Bonds; (ii) the Treasurer of the City Public Service Board shall have filed with the City Clerk of the City a certificate stating that the City is not in default as to any covenant, obligation or undertaking contained in any ordinance or other document relating to the issuance of any obligations then outstanding which are payable from and secured by a lien on and pledge of the Net Revenues, and that each of the Funds and Accounts created and established for the sole purpose of paying the principal of and interest on such obligations contains the amount then required to be on deposit therein; (iii) the obligations proposed to achieve the status of Parity Bonds mature on February 1 or August 1, or a day in each of the years they are scheduled to mature; and (iv) the Reserve Amount required to be on deposit or then on deposit in the Retirement Account equals not less than the average annual requirement for payment of principal of and interest on all Parity Bonds which will be outstanding after giving effect to the bonds then proposed to achieve the status of Parity Bonds.

SECTION 19: No Obligation of Lien Superior to that of the Parity Bonds. The City will not hereafter issue any additional bonds on a parity with the Old Series Bonds under the terms of the Indenture or create or issue evidences of indebtedness for any purpose possessing a lien on Net Revenues superior to that to be possessed by the Parity Bonds. The City, however, retains the right to create and issue evidences of indebtedness whose lien on Net Revenues shall be subordinate to that possessed by the Parity Bonds.

SECTION 20: Management of the Systems. In accordance with the provisions of the ordinances authorizing the Previously Issued Parity Bonds and this Ordinance, the City hereby agrees, covenants and reaffirms that:

(a) Until such time as the terms, conditions and provisions of the Indenture become inoperative and the "Trust Estate" conveyed by the Indenture reverts to the City free and clear of the encumbrance created thereby, the management of the Systems and all of its properties and affairs shall be conducted, operated and controlled in the manner and to the same extent as set forth in the Indenture to which reference is hereby made for a specific description thereof.

(b) At such time as the terms, conditions and provisions of the Indenture become inoperative and the "Trust Estate" conveyed by the Indenture reverts to the City free and clear of the encumbrance created thereby and during such time as any Parity Bonds issued hereunder are outstanding and unpaid, the complete management and control of the Systems, pursuant to the authority contained in Article 1115, V.A.T.C.S., shall be vested in a Board of Trustees consisting of five citizens (one of whom shall be the Mayor of the City) of the United States of America permanently residing in Bexar County, Texas, to be known as the "City Public Service Board of San Antonio, Texas". Those persons serving as appointed members of the Board of Trustees at the time defeasance of the Indenture occurs shall continue in office until their respective terms as established under Article VI of the Indenture have expired. The Mayor of the City shall be a voting member of the Board, shall represent the City Council thereon, and shall be charged with the duty and responsibility of keeping the City Council fully advised and informed at all times of any actions, deliberations and decisions of the Board and its conduct of the management of the Systems.

All vacancies in membership on the Board (excluding the Mayor of the City), whether occasioned by failure or refusal of any person previously named to accept appointment or by expiration of term of office or otherwise, shall be filled in the following manner: a nominee to fill such vacancy shall be elected by the majority vote of the remaining members of the Board of Trustees, such majority vote to include the vote of the Mayor. The name of such nominee shall then be submitted by the Mayor to the vote of the City Council, which by a majority vote of the members thereof then in office shall, as evidenced by ordinance or resolution, either confirm or reject such nominee; provided, however, if the City Council fails to act upon such nomination within 30 days after submission to it of such nominee, such failure to do so shall be considered as a rejection of such nominee and another nominee shall be selected by the Board. If a vacancy occurs and the remaining members of the Board (including the Mayor) fail to elect a nominee to fill such vacancy within 60 days after the vacancy occurs (or fail to select another nominee within 60 days after rejection of a nominee by the City Council), the City Council, by a majority vote of the members thereof then in office, shall elect a person to fill such vacancy and shall appoint such Trustee by resolution or ordinance. In the event the City rejects or fails to confirm three consecutive nominees of the Board to fill a vacancy on the Board, the City Council shall, within 30 days after the third rejection, appoint a temporary Trustee to fill such vacancy. The appointment of a temporary Trustee by the City Council shall constitute the nomination of such appointee as the permanent Trustee to fill such vacancy. Unless the remaining members of the Board, by a majority vote, reject the nominee selected by the City Council within 30 days after his appointment as a temporary Trustee, the appointment shall become final and the temporary Trustee shall automatically become the permanent Trustee to fill such vacancy. In such vote, the vote of the Mayor shall automatically be cast as a vote in favor of the confirmation of such Trustee, whether cast by the Mayor or not.

If the nominee of the City Council is rejected by a majority vote of the remaining Trustees, the remaining Trustees shall within 30 days after such rejection elect another nominee to fill such vacancy. Such nominee shall be considered by the City Council and if approved shall become the permanent Trustee. If such nominee is rejected by a majority vote of the members of the City Council then in office, or in the event the City Council fails to act upon such nomination within 30 days after the nomination is presented to the Council, the temporary Trustee theretofore appointed by the City Council shall automatically become the permanent Trustee to fill such vacancy. The term of office of each member appointed to the Board shall be five years. A person who has served as an appointed member of the Board for a single five year term shall be eligible for reappointment for one additional five year term and one only. A member who is appointed to the Board to serve out an unexpired portion of a retired member's term shall not be considered to have served a "term" unless the unexpired portion of the term so served is three years or more. Permanent removal of residence from Bexar County by any appointed member of the Board shall vacate his office as a member of the Board, or any member (other than the Mayor of the City) who shall be continuously absent from all meetings held by the Board for a period of four consecutive months shall, unless he shall have been granted leave of absence by the unanimous vote of the remaining members of the Board, be considered to have vacated his office as a member of the Board. Any member of the Board, other than the Mayor of the City, may, by unanimous vote of the remaining members of the Board be removed from office, but only for adequate cause.

Notwithstanding any of the foregoing provisions as contained in this Section 20 (b) or in any other section of this Ordinance pertaining to the appointment or selection of Trustees to the Board upon the defeasance of the Indenture securing payment of the Old Series Bonds, the City Council reserves unto itself the absolute right at anytime upon passage of an ordinance approved by a majority vote of its members to change the method of selection of and appointment to the Board of Trustees to direct selection by the City Council, with such change of method to direct selection being at the sole option of the City Council without approval of any persons, party, holder of Parity Bond or Board.

Except as otherwise specifically provided in this Ordinance, the Board of Trustees shall have absolute and complete authority and power with reference to the control, management and operation of the Systems and the expenditure and application of the revenues of the Systems subject to the provisions contained in this Ordinance, all of which shall be binding upon and shall govern the Board of Trustees. In connection with the management and operation of the Systems and the expenditure and application of the revenues therefrom, the Board of Trustees shall be vested with all of the powers of the City with respect thereto, including all powers necessary or appropriate for the performance of all of the covenants, undertakings and agreements of the City contained in this Ordinance, and shall have full power and authority to make rules and regulations governing the furnishing of electric and gas service to customers and for the payment of the same, and for the discontinuance of such services upon failure of customers to pay therefor, and, to the extent authorized by law, shall have full authority with reference to making of extensions, improvements and additions to the Systems and the acquiring by purchase or condemnation of properties of every kind in connection therewith.

The Board of Trustees in exercising the management powers granted herein, will ensure that policies adopted affecting research, development and corporate planning will be consistent with Council policy, and policies adopted by the Board of Trustees pertaining to such matters will be subject to Council review.

The Board of Trustees shall elect one of its members as Chairman and one as Vice Chairman of the Board and shall appoint a Secretary and a Treasurer, or a Secretary-Treasurer, who may, but need not be, a member or members of the Board. If a member of the Board of Trustees is not appointed as Secretary or Treasurer, or Secretary-Treasurer, then an employee or employees of the Board whose duties in the operation of the Systems require performance of similar duties may be appointed as Secretary or Treasurer or Secretary-Treasurer. The Board of Trustees may follow and adopt such rules for the orderly handling of its affairs as it may see fit and may manage and conduct the affairs of the Systems with the same freedom and in the same manner ordinarily employed by the Board of Directors of private corporations operating properties of a similar nature. No member of the Board of Trustees, however, shall ever vote by proxy in the exercise of his duties as a Trustee.

The Board of Trustees shall appoint and employ all officers, employees and professional consultants which it may deem desirable, including without limitation, a General Manager of the Systems, attorneys, engineers, architects, and other advisors. No officer or employee of the Board of Trustees may be employed who shall be related within the second degree of consanguinity or affinity to any member of the Board of Trustees.

The Board of Trustees shall obtain and keep continually in force an employees' fidelity and indemnity bond of the so-called "blanket" type, written by a solvent and recognized indemnity company authorized to do business in the State of Texas and covering losses to the amount of not less than One-Hundred Thousand Dollars (\$100,000).

The members of the Board of Trustees, other than the Mayor of the City, shall receive annual compensation in the minimum amount of Two Thousand Dollars (\$2,000.00), except that the Chairman of the Board shall receive annual compensation in the minimum amount of Two Thousand Five Hundred Dollars (\$2,500.00). Such compensation may be increased from time to time by the majority vote of the City Council then in office.

The members of the Board of Trustees and administrative officers shall not be personally liable, either individually or collectively, for any act or omission not willfully fraudulent or in bad faith.

SECTION 21: Method of Amendment. The City hereby reserves the right to amend ordinances authorizing the issuance of Parity Bonds subject to the following terms and conditions, to-wit:

(a) The holders of Parity Bonds aggregating in principal amount sixty-six and two-thirds (66-2/3%) percent of the aggregate principal amount of then outstanding Parity Bonds shall have the right from time to time to approve any amendment to this Ordinance which may be deemed necessary or desirable by the City; provided, however, that nothing herein contained shall permit or be construed to permit amendment of the terms and conditions of this Ordinance or in the bonds so as to:

- (1) Make any change in the maturity of outstanding Parity Bonds;
- (2) Reduce the rate of interest borne by any of the outstanding Parity Bonds;
- (3) Reduce the amount of the principal of, or redemption premium, if any, payable on any outstanding Parity Bonds;
- (4) Modify the terms of payment of principal or of interest or redemption premium on outstanding Parity Bonds or any of them or impose any condition with respect to such payment;
- (5) Affect the rights of the holders of less than all of the Parity Bonds then outstanding; or
- (6) Change the minimum percentage of the principal amount of bonds necessary for consent to such amendment.

(b) If at any time the City shall desire to amend this Ordinance under this Section, the City shall cause notice of the proposed amendment to be published at least once in a financial publication published in The City of New York, New York. Such notice shall briefly set forth the nature of the proposed amendment and shall state that a copy thereof is on file at the Office of the City Clerk of the City for inspection by all holders of Parity Bonds then outstanding.

(c) Whenever at any time within one year from the date of publication of such notice the City shall receive an instrument or instruments executed by the holders of at least sixty-six and two-thirds (66-2/3%) percent in aggregate principal amount of all Parity Bonds then outstanding, which instrument or instruments shall refer to the proposed amendment described in said notice and which shall specifically consent to and approve such amendment in substantially the form of the copy thereof on file with the City Clerk of the City, the City may adopt the amendatory ordinance in substantially the same form.

(d) Upon the adoption of any amendatory ordinance pursuant to the provisions of this Section, the ordinances authorizing the Parity Bonds then outstanding shall be deemed to be modified and amended in accordance with such amendatory ordinance, and the respective rights, duties and obligations of the City and all holders of outstanding Parity Bonds shall thereafter be determined, exercised and enforced, subject in all respects to such amendment.

(e) Any consent given by the holder of a bond pursuant to the provisions of this Section shall be irrevocable for a period of six months from the date of the publication of the notice provided for in this Section, and shall be conclusive and binding upon all future holders of the same bond during such period. Such consent may be revoked at any time after six months from the date of the publication of said notice by the holder who gave such consent, or by a successor in title, by filing notice with the City Clerk of the City, but such revocation shall not be effective if the holders of sixty-six and two-thirds (66-2/3%) percent aggregate principal amount of the then outstanding Parity Bonds as in this Section defined, have, prior to the attempted revocation, consented to and approved the amendment.

(f) Except as provided in (g) below for the Registered New Series Bonds, for the purposes of establishing ownership of Parity Bonds, the fact of the holding of Parity Bonds by any bondholder, the amount and numbers of such bonds, and the dates of their holding such bonds, may be proved by the affidavit of the person claiming to be such holder, or by a certificate executed by any trust company, bank, or any other depository wherever situated showing that at the date therein mentioned such person had on deposit with such trust company, bank, or other depository the bonds described in such certificate. The City may conclusively assume that such ownership continues until notice to the contrary is served on the City.

(g) For the purposes of establishing ownership of the Registered New Series Bonds, the City shall rely solely upon the registration of the ownership of such bonds on the Registration Books kept by the appropriate Paying Agent/Registrar, as provided in the ordinances authorizing the New Series 1983-A Bonds, the New Series 1984-A Bonds, the New Series 1984-B Bonds, the New Series 1985 Bonds, the New Series 1985-A Bonds, the New Series 1985-B Bonds, the New Series 1986 Bonds, the New Series 1986-A Bonds, the New Series 1987 Bonds, the New Series 1987-A Bonds, or this ordinance.

(h) The word "Outstanding" when used in this Ordinance with respect to Parity Bonds means, as of the date of determination, all Parity Bonds theretofore issued and delivered except:

- (i) Those Parity Bonds theretofore cancelled by the Paying Agent/Registrar or delivered to the Paying Agent/Registrar for cancellation;
- (ii) those Parity Bonds for which payment has been duly provided by the City by the irrevocable deposit with the Paying Agent/Registrar of money in the amount necessary to fully pay the principal of, premium, if any, and interest thereon to maturity or redemption, as the case may be, provided that, if such Parity Bonds are to be redeemed, notice of redemption thereof shall have been duly given pursuant to the ordinance authorizing the issuance of such Parity Bonds or irrevocably provided to be given to the satisfaction of the Paying Agent/Registrar, or waived;
- (iii) those Parity Bonds that have been mutilated, destroyed, lost, or stolen and replacement Bonds have been registered and delivered in lieu thereof; and
- (iv) those Parity Bonds for which the payment for the principal of, premium, if any, and interest on has been duly provided by the City by the deposit in trust of money or Government Securities, or both.

SECTION 22: Recognition of Provisions of Indenture. It is specifically recognized and affirmed that until defeasance of the provisions of Article V of the Indenture, the pledge of revenues herein for the payment and security of the Parity Bonds is inferior to the pledge of revenues therein to the payment of principal of and interest on the Old Series Bonds and to the maintenance of the "San Antonio Electric and Gas Systems Reserve Account" thereunder. All terms, conditions, covenants, agreements, stipulations and trust provisions whatsoever of the Indenture, providing and constituting the means of securing and providing for payment of the Old Series Bonds, including, but not limited to, the provisions of Article V thereof relating to application of revenues, are hereby recognized and affirmed and shall be given full force and effect in all respects until (i) the conditions for defeasance of the Indenture (set forth in Section 1 of Article XIV) have been fulfilled in such manner and to such extent as will have caused the "Trust Estate" to revert to the City free of the encumbrance thereof; or (ii) the Indenture has been amended in such manner as would permit the Parity Bonds to occupy a position of parity with the Old Series Bonds, in which event all such bonds will become Parity Bonds; or (iii) a defeasance of the Indenture has taken place by operation or application of the law.

SECTION 23: Transition of Funds Upon Defeasance of the Indenture: In accordance with the provisions of the ordinances authorizing the issuance of the Previously Issued Parity Bonds, and at such time as the conditions, provisions and terms of the Indenture shall become inoperative and the "Trust Estate" conveyed by the Indenture reverts to the City free and clear of the encumbrance created thereby, any funds remaining in the "San Antonio Electric and Gas Systems Bond Reserve Account" (created and established in Section 4 of Article V of the Indenture) shall be transferred and credited to the Reserve Amount on deposit in the "Retirement Account," and all moneys and funds remaining on deposit in the "Electric and Gas Systems Improvements and Contingencies Fund" and the "Electric and Gas Systems Surplus Fund" (created and established in Section 6 (as amended) of Article V of the Indenture) shall be transferred and credited to the Repair and Replacement Account.

SECTION 24: Maintenance and Operation - Insurance. The City hereby agrees and reaffirms that the Systems shall be maintained in good condition and operated in an efficient manner and at reasonable cost. So long as any of the Parity Bonds are outstanding, the City, acting by and through the Board of Trustees, agrees to maintain insurance of a kind and in an amount which usually would be carried by private companies engaged in a similar type of business.

SECTION 25: Records - Accounts - Accounting Reports. The City, acting by and through the Board of Trustees, hereby agrees, covenants and reaffirms that so long as any Parity Bonds, or any interest thereon, remain outstanding and unpaid, a proper and complete set of records and accounts pertaining to the operation of the Systems shall be kept and maintained separate and apart from all other records and accounts of the City, in which complete and correct entries shall be made of all transactions relating to the Systems as provided in Article 1113, V.A.T.C.S., and that the holder or holders of any of the Parity Bonds or any duly authorized agent or agents of such holders shall have the right at all reasonable times to inspect all such records, accounts and data relating thereto and to inspect the Systems and all properties comprising the same. The Board of Trustees shall, so far as practicable and to the extent consistent with the provisions of this Ordinance, keep its books and records in the manner prescribed in the Uniform System of Accounts adopted by the National Association of Regulatory Utility Commissioners. It is further agreed that as soon after the close of each Fiscal Year as may reasonably be done, the City (acting by and through the Board of Trustees) will cause an annual audit of such books and accounts to be made by an independent firm of certified public accountants. Each such audit, in addition to whatever other matters may be thought proper by the accountants, shall reflect the revenues and expenses of the Systems for said Fiscal Year, and the assets, liabilities and financial condition of the Systems (in reasonable detail) at the close of such Fiscal Year.

Expenses incurred in making the audit above referred to are to be regarded as Maintenance and Operating Expenses and paid as such. Copies of the aforesaid annual audit shall be immediately furnished to the Executive Director of the Municipal Advisory Council of Texas at his office in Austin, Texas, and to the original purchaser of a series of Parity Bonds and any subsequent holder thereof at his written request. At the close of the first six months' period of each Fiscal Year, the Treasurer of the City Public Service Board is hereby directed to furnish a copy of an operating and income statement in reasonable detail covering such period to any holder upon his written request therefor received not more than 30 days after the close of said six months' period. Any bondholder shall have the right to discuss with the accountant making the annual audit the contents thereof and to ask for such additional information as he may reasonably require, provided such bondholder shall have offered to the Board of Trustees sufficient indemnity to pay any costs, expenses and liabilities which may or might be incurred in providing such additional information.

SECTION 26: Remedies in the Event of Default. In addition to all of the rights and remedies provided by the laws of the State of Texas, it is specifically covenanted and agreed particularly that in the event the City (i) defaults in the payments to be made to the Retirement Account as required by this Ordinance, or (ii) defaults in the observance or performance of any other of the covenants, conditions or obligations set forth in this Ordinance, the following remedies shall be available:

(a) The holder or holders of any Parity Bonds shall be entitled to a writ of mandamus issued by a court of proper jurisdiction, compelling and requiring the City, its officers, the Board of Trustees, and/or all of them, to observe and perform any covenants, conditions or obligations prescribed in this Ordinance.

(b) No delay or omission to exercise any right or power accruing upon any default shall impair any such right or power, or shall be construed to be a waiver of any such default or acquiescence therein, and every such right and power may be exercised from time to time and as often as may be deemed expedient.

The specific remedies herein provided shall be cumulative of all other existing remedies and the specifications of such remedies shall not be deemed to be exclusive.

SECTION 27: Special Covenants. The City hereby further covenants as follows:

(a) The City has secured from the Board of Trustees a resolution acknowledging its duties, responsibilities and obligations under this Ordinance and agreeing to fully comply with all its terms and provisions, including the administration and operation of the Systems and the disposition of revenues of the Systems.

(b) It has the lawful power to pledge the revenues supporting this issue of bonds and has lawfully exercised said power under the Constitution and laws of the State of Texas, including said power existing under Articles 1111 et seq., V.A.T.C.S., that the Bonds issued hereunder, the Previously Issued Parity Bonds and Additional Parity Bonds, when issued, shall be ratably secured under said pledge of income in such manner that one bond shall have no preference over any other bond of said issues.

(c) Other than for the payment of the Bonds herein authorized, the Previously Issued Parity Bonds, the previously issued Old Series Bonds, and the Commercial Paper, the rents, revenues and income of the Systems have not in any manner been pledged to the payment of any debt or obligation of the City or of the Systems.

(d) So long as any of the Parity Bonds or any interest thereon remain outstanding, the City will not sell or encumber the Systems or any substantial part thereof, provided that this shall not be construed to prohibit the sale of such machinery or other properties or equipment which has become obsolete or otherwise unsuited to the efficient operation of the Systems; and, further, with the exception of the Additional Parity Bonds expressly permitted by this Ordinance, the City will not encumber the Net Revenues unless such encumbrance is made junior and subordinate to all of the provisions of this Ordinance.

(e) No free service of the Systems shall be allowed and should the City or any of its agents or instrumentalities make use of the services or facilities of the Systems, payments for services rendered by the Systems should either be made by the City or amounts equal in value to the services rendered by the Systems shall be deducted from the annual payment due the General Fund of the City from the Net Revenues as provided in Section 14 hereof.

(f) To the extent it legally may, the City further covenants and agrees that, so long as any Parity Bonds or any interest thereon are outstanding, no franchise shall be granted for the installation or operation of any competing electric or gas system other than that owned by the City, and the operation of any such systems by anyone other than the City is hereby prohibited.

SECTION 28: Bonds are Special Obligations. The Bonds authorized by this Ordinance are special obligations of the City payable from the pledged Net Revenues and the holders thereof shall never have the right to demand payment out of funds raised or to be raised by taxation.

.....

SECTION 30: Ordinance to Constitute Contract. The provisions of this Ordinance shall constitute a contract between the City of San Antonio and the holder or holders from time to time of the New Series 1988 Bonds and after the issuance of any of said bonds, no change, variation, or alteration of any kind in the provisions of this Ordinance may be made, unless as herein otherwise provided, until all of said bonds issued hereunder shall have been paid as to both principal and interest.

SECTION 31: Approval by Attorney General and Registration by the Comptroller of Public Accounts. The Mayor of the City and Treasurer of the City Public Service Board are hereby authorized to have control and custody of the New Series 1988 Bonds and all necessary records and proceedings pertaining thereto pending the sale of the New Series 1988 Bonds and the delivery thereof to the purchasers, and the Mayor and other officers and employees of the City and the City Public Service Board are hereby authorized and instructed to make such certifications, execute such instruments and perform such acts as may be necessary to assure the proper investigation, examination and approval thereof by the Attorney General of the State of Texas, and their registration by the Comptroller of Public Accounts of the State of Texas, and to accomplish delivery of the New Series 1988 Bonds to the purchasers thereof.

(End of Ordinance excerpts from the Ordinance)

SAN ANTONIO ELECTRIC AND GAS SYSTEMS

HISTORY AND MANAGEMENT

San Antonio acquired its gas and electric utilities in 1942 from the American Light and Traction Company which had been ordered by the Federal Government to sell properties under provisions of the Holding Company Act of 1933. The total funds required for the purchase were raised by the sale of \$33,950,000 first mortgage revenue bonds. The Trust Indenture securing the Old Series Bonds establishes management requirements and provides that the complete management and control of the electric and gas systems, while the Old Series Bonds are outstanding, shall be vested in a Board of Trustees consisting of five citizens of the United States of America permanently residing in Bexar County, Texas, to be known as the "City Public Service Board of San Antonio," sometimes also referred to herein as "Board" or "CPS." The Mayor of the City of San Antonio is a permanent ex officio member of the Board. The term of Earl C. Hill expired January 31, 1988, and his replacement has not been named. The present members of the Board are:

MRS. LILA COCKRELL, CHAIR
President
Atkins Travel By Design

PAT LEGAN, VICE CHAIR
Legan Properties, Inc.

RUBEN M. ESCOBEDO
Certified
Public Accountant
Escobedo and Co.

(Vacancy)

HENRY G. CISNEROS
Mayor,
City of San Antonio
(Ex Officio Member)

While the Old Series Bonds are outstanding, vacancies in membership on the Board are filled by majority vote of the remaining members. No person who is related within the second degree of consanguinity or affinity to any Board member or any person who has been a member of the Board within a period of five years prior to the election shall be eligible for election as a member of the Board. The members of the Board are eligible for reelection at the expiration of their first five-year term of office to one additional term only.

The Board is vested with all of the powers of the City with respect to the management and operation of the systems and the expenditure and application of the revenues therefrom, including all powers necessary or appropriate for the performance of all covenants, undertakings and agreements of the City contained in the Trust Indenture, except regarding rates and issuance of bonds, notes, or commercial paper. The Board has full power and authority to make rules and regulations governing the furnishing of electric and gas service and full authority with reference to making extensions, improvements and additions to the Systems, and to adopt rules for the orderly handling of its affairs. It is empowered to appoint and employ all officers and employees and must obtain and keep in force a "blanket" type employees' fidelity and indemnity bond covering losses in the amount of not less than \$100,000.

The Ordinances which authorize the issuance of the New Series Bonds, and which will control after the Old Series Bonds are no longer outstanding, contain similar management provisions. The management provisions of this Ordinance, which are set out in full in a previous section, add, among other things, the requirement that new Board appointees must also be approved or in certain cases appointed by a majority vote of the City Council and grants the City Council authority to review Board action with respect to research, development and planning.

ADMINISTRATION AND OPERATING PERSONNEL

Long-time career service is typical of CPS employees, who presently number 3,549. All executive and supervisory positions are held by individuals who have been thoroughly schooled and trained in the utilities field.

CPS employees have a full range of fringe benefits including a pension plan augmented by Social Security, group life insurance, hospitalization and major medical and other benefits. Generally good working conditions have produced a stable, well-qualified, highly motivated work force which for the past year recorded the very low turnover rate of 0.49% per month.

Principal executive personnel are as follows: Mr. Arthur von Rosenberg, General Manager; Mr. H.L. Freeman, Assistant General Manager for Finance; Mr. J.K. Harz, Assistant General Manager for Administration; Mr. R.J. Costello, Assistant General Manager for Operations; and Ms. J.E. Axtell, Assistant General Manager for Planning and Development. Mr. von Rosenberg has been an employee of CPS since 1959 and served as Manager of Planning and Development, Assistant General Manager for Planning and Development and Associate General Manager prior to becoming General Manager in 1988. Mr. Freeman has been an employee of CPS since 1959 and served as Superintendent of Customer Accounting, Chief Accountant and Controller prior to becoming Assistant General Manager for Finance in 1976. Mr. Harz has been an employee of CPS since 1953 and served as Superintendent of Office Services, and Manager of Customer Service, Financial Services and the Personnel Group prior to becoming Assistant General Manager for Administration in 1983. Mr. Costello has been an employee of CPS since 1957 and was Superintendent of Distribution Operations and Manager of Transmission and Distribution Engineering prior to becoming Assistant General Manager for Operations in 1987. Ms. Axtell has been an employee of CPS since 1969 and was Superintendent of Generation Planning and Manager of Generation and Environmental Planning prior to becoming Assistant General Manager for Planning and Development in 1987.

ELECTRIC AND GAS SALES BY CUSTOMER CATEGORY

	Fiscal Years Ended January 31:				
	1984	1985	1986	1987	1987 ¹
ELECTRIC SYSTEM					
SALES IN KWH					
Residential	3,139,333,099	3,491,218,510	3,782,692,779	4,036,562,109	4,103,275,281
Commercial & Industrial	3,839,434,236	4,107,615,198	4,465,681,626	4,636,307,715	4,627,851,043
Street Lighting	66,907,453	65,413,345	67,305,833	67,548,785	68,394,283
Public Authorities	1,197,943,925	1,246,617,066	1,300,515,232	1,358,027,225	1,459,559,119
Other Utilities	194,636,220	181,741,040	413,380,690	257,848,431	235,088,938
ANSL	11,126,116	11,152,134	11,139,960	11,182,429	11,203,816
Total Sales in KWH	<u>8,449,381,049</u>	<u>9,103,557,293</u>	<u>10,040,716,120</u>	<u>10,367,476,694</u>	<u>10,505,372,480</u>
AVERAGE NUMBER OF CUSTOMERS					
Residential	338,092	363,100	381,878	398,992	404,122
Commercial & Industrial	37,670	40,688	43,073	44,935	44,890
Street Lighting	33	31	42	43	56
Public Authorities	2,883	2,927	2,994	3,088	3,544
Other Utilities	4	4	4	5	5
ANSL	7,162	7,092	7,012	7,039	7,068
Total Customers	<u>385,844</u>	<u>413,842</u>	<u>435,003</u>	<u>454,102</u>	<u>459,635</u>
GAS SYSTEM					
SALES IN MCF					
Residential	15,492,622	13,642,964	14,332,095	13,576,261	14,512,380
Commercial	7,616,372	7,175,096	7,462,211	7,283,761	7,372,773
Industrial	3,061,115	2,977,367	2,743,495	2,486,467	2,433,904
Public Authorities	1,924,712	1,707,871	1,764,348	1,656,517	1,891,738
Total Sales in MCF	<u>28,094,821</u>	<u>25,503,298</u>	<u>26,302,149</u>	<u>25,003,006</u>	<u>26,210,795</u>
AVERAGE NUMBER OF CUSTOMERS					
Residential	254,267	258,664	261,571	263,991	263,905
Commercial	17,977	18,130	18,183	18,361	18,205
Industrial	258	246	227	222	212
Public Authorities	1,986	1,981	1,953	1,984	2,156
Total Customers	<u>274,488</u>	<u>279,019</u>	<u>281,934</u>	<u>284,558</u>	<u>284,478</u>
KWH SALES PER CUSTOMER					
Residential	9,285	9,615	9,906	10,117	10,154
Commercial & Industrial	101,923	100,955	103,678	103,178	103,094
MCF SALES PER CUSTOMER					
Residential	61	53	55	51	55
Commercial	424	396	410	397	405

¹ 12 months ending December 31, 1987.

DESCRIPTION OF PHYSICAL PROPERTY

ELECTRIC SYSTEM

Generating Plants

The electric generating system operated by the Board consists of six steam electric generating stations with step up substation systems.

The J.T. Deely Plant, located at Calaveras Lake, southeast of the City, is equipped to burn either coal or fuel oil. Unit No. 1 was placed in service in July, 1977 and Unit No. 2 has been in commercial operation since August, 1978. These two units will carry over 50% of the system load for the near future on coal, which is less expensive and more consistently available than oil or gas.

Also located at Calaveras Lake and sharing its cooling capability is the O.W. Sommers Plant, composed of two units which are capable of operating on either natural gas or fuel oil.

The V.H. Braunig Plant is located on Braunig Lake, also southeast of the City. It has three units which operate on either natural gas or fuel oil.

Both Calaveras Lake and Braunig Lake have additional space and cooling capability for future generating units. A new 500 megawatt coal-fired unit is to be constructed at Calaveras Lake. These lakes, which cover approximately 5,000 surface acres, are man-made and utilize treated sewage effluent and runoff waters. CPS was a pioneer in the use of poorer quality water for cooling purposes, thereby saving the higher quality underground water for other uses.

While the above plants now generate most of the load, there are three older plants which are held in reserve. They are the W.B. Tuttle, Mission Road, and Leon Creek Plants. They can burn either natural gas or fuel oil and are cooled by water recirculated through cooling towers.

CPS owns 810 railroad cars which are used in unit trains to haul coal from mines in Wyoming to the Deely Plant. CPS also performs its own required car maintenance and servicing at its car maintenance shops located at the Deely Plant.

Details of installed units at CPS generating stations are as follows:

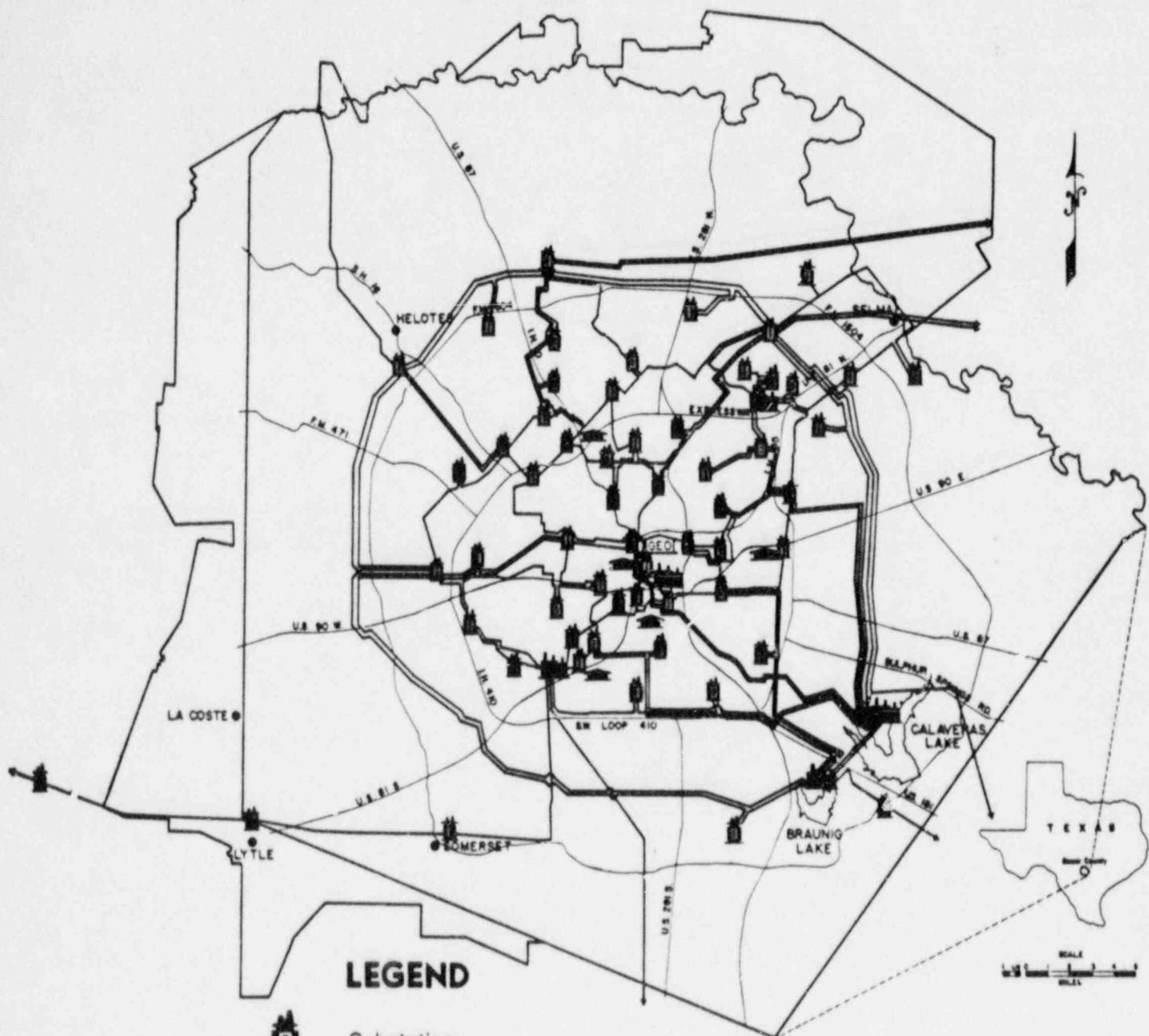
Generating Station	Fuel	Year Installed	Capability MW*
J.T. Deely Plant	Coal/Oil	1977	418
	Coal/Oil	1978	418
O.W. Sommers Plant	Gas/Oil	1974	430
	Gas/Oil	1972	430
V.H. Braunig Plant	Gas/Oil	1970	400
	Gas/Oil	1968	230
W.B. Tuttle Plant	Gas/Oil	1966	220
	Gas/Oil	1963	160
Leon Creek Plant	Gas/Oil	1961	100
	Gas/Oil	1956	100
Mission Road Plant	Gas/Oil	1954	65
	Gas/Oil	1959	100
	Gas/Oil	1953	65
	Gas/Oil	1958	100
Total Active Capability			3,236

* For the gas/oil fueled units the capability shown are the gas ratings.

Transmission System

CPS maintains a transmission line network for the movement of large blocks of electric power from the generating stations to the various parts of the service area and to or from neighboring utilities as required. This is composed of 69,000 volt, 138,000 volt and 345,000 volt lines with transformers and switching stations to provide the necessary flexibility in the movement of bulk electric power.

ELECTRIC DISTRIBUTION SYSTEM



LEGEND



Substation



Central GEO
System Control



Power Plants



Service Centers



Transmission Lines

345,000 volts

138,000 volts

69,000 volts

Interconnected System

The San Antonio System is integrated with approximately 75 other utilities, municipalities and electric cooperatives in Texas to form the Electric Reliability Council of Texas (ERCOT), which covers a large portion of Texas. CPS, along with the ten utilities listed below, form the major generating and transmission entities in Texas.

West Texas Utilities (WTU)
Houston Lighting & Power Company (HL&P)
Central Power and Light Company (CPL)
Texas Utilities Electric Company (TUEC)
Lower Colorado River Authority (LCRA)
City of Austin, Texas, Municipal Utilities (Austin)
Texas Municipal Power Agency (TMPA)
Brazos Electric Power Cooperative (BEPC)
South Texas Electric Co-op/Medina Electric Co-op (STEC/MEC)
City of Brownsville Public Utility Board (COB)

These interconnections, through operating agreements between the several utilities, provide standby power in case of outages as well as emergency firm power in the event capacity deficiencies occur at a particular locality within the area. The arrangements serve to reduce the standby capacity which each utility would otherwise need. Pursuant to a power brokerage system, these interconnections have also been utilized to transport economy energy between utilities, thereby allowing utilities to benefit from lower cost generation when available. Membership in ERCOT provides CPS with a high level of electric service reliability.

Pursuant to a 1982 Order of the Federal Energy Regulatory Commission (FERC) agreed to by all members of the Texas Interconnected Systems (TIS), and a subsequent order of FERC issued in 1987, two direct current ties connecting ERCOT with the Southwest Power Pool (SWPP), which is located to the north and east of ERCOT, are authorized. The northern tie became operational in December, 1984, and its capacity is being expanded; construction of an eastern tie is pending. The direct current nature of the ties is intended to permit scheduled energy transfers between ERCOT and SWPP while preserving the compact size of ERCOT and protecting electric utilities within Texas from power disturbances outside ERCOT. These DC ties will be owned by HL&P and by Central & Southwest Corporation ("CSW"), the parent of CPL, WTU, and affiliates, and by TUEC, Austin, and possibly others.

Distribution System

The Distribution System is supplied by 62 substations strategically located on the high voltage (69 KV and 138 KV) transmission system.

The central business section of San Antonio is served by eight underground network systems, each consisting of four primary feeders operated at 13 KV, transformers equipped with network protectors, and both a 4 wire 120/208 volt secondary grid system and a 4 wire 277/480 volt spot grid system. This system is well designed for both service and reliability.

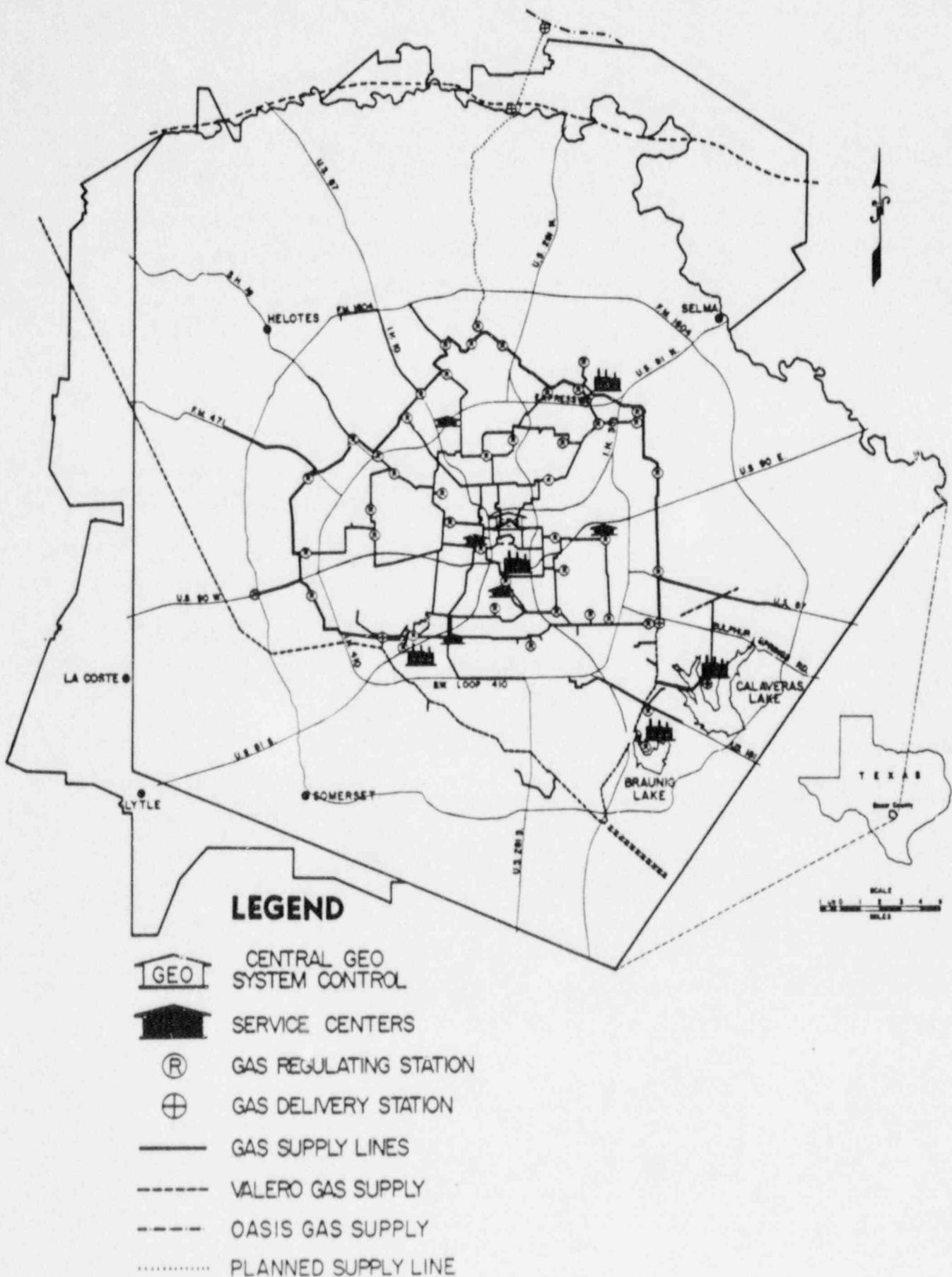
There are over 7,001 miles of pole lines and over 512 miles of underground duct lines in the distribution system. The overhead lines also carry secondary circuits and street lighting circuits. Presently there are over 48,824 street lighting units in service, with the vast majority of these being modern, high intensity units. Many of the subdivisions added in recent years have been served by underground distribution systems.

**TOTAL TRANSFORMER CAPACITY
INDICATING NET ANNUAL INCREASE
KVA**

<u>F Y Ended 1-31:</u>	<u>Overhead</u>	<u>Underground</u>	<u>Total</u>
1972	2,007,134.5	199,781.0	2,206,915.5
1973	2,183,263.5	203,781.0	2,387,046.5
1974	2,337,149.5	202,856.0	2,540,005.5
1975	2,563,716.0	204,331.0	2,768,047.0
1976	2,731,886.5	205,081.0	2,936,967.5
1977	2,915,456.0	205,581.0	3,121,037.0
1978	3,120,524.5	213,581.0	3,334,105.5
1979	3,383,280.0	214,061.0	3,597,361.0
1980	3,616,038.5	230,181.0	3,846,219.5
1981	3,863,965.5	227,656.0	4,091,621.5
1982	4,135,528.0	236,531.0	4,372,059.0
1983	4,380,618.5	245,381.0	4,625,999.5
1984	4,721,050.5	256,881.0	4,977,931.5
1985	5,185,880.0	265,725.0	5,451,605.0
1986	5,649,781.5	270,375.0	5,920,156.5
1987	6,077,171.5	311,500.0	6,388,671.5
1987 ¹	6,403,932.0	354,600.0	6,758,532.0

¹ Period ended December 31, 1987.

GAS DISTRIBUTION SYSTEM



GAS SYSTEM

Gas Delivery

Natural gas is transported to CPS by Valero Transmission Partners, L.P., successor to Valero Transmission Company, a subsidiary of Valero Energy Corporation. Gas transported by Valero is purchased and metered at two City Gate Stations and at the O.W. Sommers and V.H. Braunig Power Plants. Completion of CPS' 17.5 mile transmission line by the middle of this year will also allow gas to be delivered by Oasis Pipeline Co., a subsidiary of Enron Corp. This pipeline will provide a new delivery point through which CPS can purchase gas.

Outer Supply Line System

CPS has constructed 54.3 miles of 24 and 30-inch lines to form an outer loop supply line system between the two existing City Gate Stations. A new 17.3 mile 24" transmission line is currently under construction to connect the outer loop supply line system with Valero's West Texas 30-inch transmission line and Oasis Pipeline's 36-inch transmission line to the north of the city. Twin one-mile lengths of 20-inch line connect the V.H. Braunig Plant to Valero's transmission line. Gas is brought to O.W. Sommers Power Plant through 3.2 miles of 16-inch and 4.5 miles of 24-inch line giving that station a feed from two different Valero transmission lines.

Controlled Supply Line System

A network of approximately 140 miles of mains, ranging from 4 to 20-inch, supplies gas at high pressures to regulator installations located at strategic points throughout the distribution system. The controlled supply line system operates at pressures of from 25 to 145 psi. These pressures are maintained and controlled through the use of remote control equipment at many locations.

Distribution System

The controlled supply line system feeds into the distribution system operating at an intermediate pressure of 7 psi consisting of over 3,504 miles of 2 to 16-inch mains, together with the necessary pressure control equipment, valves, gauges, service lines, service regulators and meters. Cathodic protection for mitigation of corrosion has been completed for substantially all of the gas distribution system. A high molecular weight polyethylene pipe has been used for distribution mains and service through 4-inch sizes since 1974.

GENERAL PROPERTIES

Operation Control System

The nerve center of CPS operations is the Gas & Electric Operations (GEO) System, which is located at the Jones Avenue facility. This is a computerized monitoring and control system and was designed by CPS personnel. All substations, power plants and major gas regulating points are continually monitored and displayed on one line diagrams on video screens. Any abnormality registers an alarm and the system operator can bring up on another screen any detail of the control points and, with a light pen, operate the various switches and valves as required. In addition to the control capability, the system gathers data which is recorded on the computer for various reporting needs, such as loads, peaks, and BTU content.

Support Facilities

The operating systems are supported by modern shops for the maintenance of such items as meters, transformers, communication equipment, vehicles, railroad cars and heavy construction equipment. These shops, together with warehouses, supervisory offices, service centers and vehicle storage, are strategically located throughout the area to minimize driving time to work locations.

General Offices

The general offices are located at the intersection of Navarro and Villita Streets in the central business district of San Antonio. The administrative, financial, business data processing and engineering functions are handled at this location. The renovation of the general office was completed in 1986 with three additional floors added to provide 11 floors of modern, efficient office space with an adjacent parking garage. The CPS Customer Service Center is located across the street on the ground level of a parking garage which CPS has recently acquired. CPS is undertaking the construction of three floors of additional office space over this facility, along with beautification of the exterior areas. At the Customer Service Center, customer contacts are handled either in person or by telephone. Information concerning any customer account is available to contact personnel in a matter of seconds from the computer system by use of video data terminals. Other Customer Service Centers are located approximately one mile south of the downtown area, on the eastern edge of San Antonio, and on the west side of the service areas. These three additional centers were established to

provide the same services as the original center but more convenient to the customer's home and in a location more accessible to the freeways, without the downtown traffic congestion and with ample parking.

Assembly Building

The Villita Assembly Building is located near the General Office Building and is available for CPS sponsored meetings or may be used by civic, community and non-profit organizations to promote the growth and improvement of the city. It has a capacity of 2,000 persons as an auditorium or 1,200 for dinner.

Vehicles and Work Equipment

CPS owns a complete fleet of automobiles, trucks and work equipment. Minor maintenance is performed on the equipment at decentralized facilities and major maintenance is handled at a central garage.

TERRITORY SERVED

The electric system serves a territory consisting of substantially all of Bexar County and small portions of the adjacent counties of Comal, Guadalupe, Atascosa, Medina, Bandera, Wilson and Kendall. Certification of this service area has been approved by the Texas Public Utility Commission. In addition to the areas served at retail, electricity is sold at wholesale rates to the City of Floresville Electric Light and Power System, City of Hondo Utilities and the City of Castroville for resale. CPS has contractual arrangements for wheeling of power through the CPS system between several other electric utilities in Texas. CPS participates in the Texas Brokerage System, a computer-assisted program which facilitates interruptible economy energy purchases and sales between Texas electric utilities. The CPS gas system serves the City of San Antonio and its environs, although there is no specified certificated CPS gas service area. In Texas there is no legislative provision or procedure for certificated gas service areas.

THIRTY LARGEST CUSTOMERS Excluding Government Bases and City of San Antonio (Based on Sales for Calendar Year of 1987)

Gas Customers		Electric Customers	
<u>Customer Name</u>	<u>Annual MCF</u>	<u>Customer Name</u>	<u>Annual KWH</u>
Lone Star Energy Corporation	484,141.3	Capitol Cement Company	72,424,000
Pearl Brewing Company (Brewery)	194,048.6	Alamo Cement Company	63,652,398
The Celotex Corporation	171,590.0	United Service Auto Association	57,657,600
Roegelein Provision Co.	136,136.1	Advanced Micro Devices	46,879,000
Frito Lay Inc.	126,998.7	Southwest Research Institute	44,268,000
Sunshine Laundry	92,015.2	U.T. Health Science Center of S.A.	43,394,400
Santa Rosa Hospital	81,696.1	Pearl Brewing Company	31,698,800
SW Research Inst. 1	79,999.3	S.W. Bell Telephone Company (E. Martin)	27,856,000
Southwest Texas Methodist Hospital	75,803.4	Southwest Texas Methodist Hospital	24,566,400
H.E. Butt Grocery Company	72,869.6	Santa Rosa Hospital	23,762,400
UTSA Thermal Energy Plant	70,651.2	H.E. Butt Grocery Co. (Main Warehouse)	23,092,800
American Company Inc.	68,357.6	University of Texas San Antonio	22,019,200
Lone Star Brewing Company	65,759.2	Messer Griesheim Ind Inc.	21,203,200
Aztec Ceramics Corporation	64,709.3	City Water Board (Wurzbach Road)	20,966,400
Howell Refining Company	64,331.1	S.W. Bell Telephone Co. (N. St. Marys)	19,353,600
Gebhardt Chili	63,702.2	City Water Board (Commerce Street)	19,248,000
Baptist Memorial Hospital	60,126.5	Frost National Bank	19,186,560
Pearl Brewing Company (Can Plant)	54,862.1	North Star Mall	17,788,400
K O Steel Casting Inc.	54,757.5	Lone Star Energy Company	17,778,000
SA State Hospital	52,055.8	American Can Company Inc.	16,925,760
Colonial Cake Company	51,638.1	Ingram Park Mall (Simon Melvin Assoc.)	16,895,040
City Water Board (Commerce Street)	49,662.3	H.E. Butt Grocery Company PDC Whses	15,801,600
SA State TB Hospital	49,227.9	Trinity University	15,750,000
SW Research Inst. 2	47,698.1	Audie Murphy Veterans Hospital	15,731,100
Friedrich Refrig. Inc.	46,194.9	City Water Board (Basin St.)	15,556,800
Gaylord Container Company.	44,825.9	Bexar County Hospital District	14,889,600
Advanced Micro Devices	42,112.7	H.E. Butt Grocery Co. (Ice Cream Plnt)	14,547,840
SW Foundation Res Ed	37,256.7	Roegelein Company	13,795,600
Treasure Chest Advertising	36,885.7	Saint Marys University	13,288,000
Martin Linen Supply	36,299.9	Redland Worth Corporation	13,005,600

STATEMENT OF REVENUES, EXPENSES AND NET INCOME

Fiscal Years Ended January 31:

	1984	1985	1986	1987	1987¹
ELECTRIC DEPARTMENT					
BILLED REVENUES					
Residential	\$219,067,185	\$263,216,525	\$292,216,352	\$276,307,106	\$269,133,898
Commercial & Industrial	230,527,586	268,950,230	295,158,101	266,746,521	253,798,307
Street Lighting & AWNL Lights	6,863,991	7,989,675	8,240,775	7,781,649	8,005,932
Public Authorities	65,031,885	75,491,525	80,007,179	71,073,120	72,937,761
Other Utilities	18,928,471	15,835,738	20,637,782	13,981,586	15,219,034
Other	3,706,073	4,880,380	4,111,410	3,735,700	4,575,301
Total Revenues	544,125,191	636,364,073	700,371,599	639,625,682	623,670,233
OPERATION & MAINTENANCE EXPENSE					
Production	285,093,787	312,155,300	325,542,236	248,599,215	226,144,437
Transmission	1,058,589	1,077,688	1,229,398	1,420,995	1,695,618
Distribution	15,917,857	16,293,834	17,455,442	20,549,823	21,310,367
Customer Accounts	3,616,318	4,010,310	4,268,460	4,858,627	4,954,489
Customer Information	1,169,011	3,309,092	5,151,353	4,500,239	3,495,426
Administrative & General	16,400,399	17,650,825	19,625,444	20,188,706	20,219,711
Payroll Taxes	2,386,286	2,738,919	3,123,837	3,185,074	3,405,038
Total Expenses	325,642,247	357,235,968	376,396,173	303,302,679	281,925,086
Operating Income-Electric	218,482,944	279,128,105	323,975,425	336,323,003	341,745,147
GAS DEPARTMENT					
BILLED REVENUES					
Residential	85,716,379	75,803,102	79,345,810	75,090,820	77,154,196
Commercial & Industrial	52,388,583	48,452,238	47,756,577	44,357,117	42,614,059
Public Authorities	9,323,923	8,031,006	8,153,120	7,442,352	8,186,193
Other	461,371	1,015,205	1,044,184	924,071	968,536
Total Revenues	147,890,056	133,301,552	136,499,691	127,814,760	128,922,984
OPERATION & MAINTENANCE EXPENSE					
Gas Purchased	122,185,597	100,929,760	96,089,341	90,581,993	83,741,488
Distribution	7,513,133	8,216,293	8,725,825	8,497,171	9,267,396
Customer Accounts	2,618,713	2,786,825	2,966,218	3,376,334	3,442,950
Customer Information	501,005	1,386,694	594,748	662,105	671,180
Administrative & General	6,698,755	7,930,081	8,817,228	9,070,288	9,398,711
Payroll Taxes	803,954	873,053	980,546	1,005,946	1,099,557
Total Expenses	160,381,157	122,222,706	118,173,903	113,193,837	107,621,282
Operating Income-Gas	7,508,899	11,078,846	18,325,785	14,620,523	21,301,702
Combined Operating Income-Electric and Gas	225,991,843	290,206,951	342,301,211	350,943,526	363,046,849
Non Operating Income	23,451,290	34,588,754	31,962,031	36,778,162	39,800,080
Total	249,443,133	324,795,705	374,263,242	387,721,688	402,846,929
Add: Interest During Construction	48,439,378	64,467,070	87,295,643	101,402,372	106,491,190
Less: Amortization of Debt Expense and Other Interest	406,287	658,235	3,140,321	6,710,672	11,712,071
Net Revenues	297,476,224	388,604,540	458,418,564	482,413,388	497,626,048
OTHER DEDUCTIONS					
Interest on Bonds	95,341,613	118,467,669	143,111,063	160,837,356	168,870,838
Payments & Refund to City	81,692,529	95,507,732	103,972,266	96,190,619	97,234,267
Depreciation	35,917,670	37,836,603	40,351,075	41,810,589	43,266,989
Total Other Deductions	212,951,812	251,812,004	287,434,404	298,838,564	309,372,094
Net Earnings ²	\$ 84,524,412	\$136,792,536	\$170,984,160	\$183,574,824	\$188,253,954

¹ 12 months ending December 31, 1987.

² Excludes gain (loss) on sale of assets.

CONDENSED STATEMENTS OF ASSETS AND LIABILITIES
 January 31, 1977 to December 31, 1987

Assets

<u>Plant and Equipment Accounts</u>			<u>Current Assets & Construction Funds</u>	<u>Other Assets</u>	<u>Total</u>
<u>Date</u>	<u>At Cost</u>	<u>Accumulated Depreciation</u>	<u>Net</u>		
1-31-77	\$ 916,207,395	\$ 163,811,352	\$ 790,396,043	\$ 82,349,961	\$ 892,728,546
1-31-78	1,101,719,068	182,598,717	918,110,351	100,666,917	1,043,664,675
1-31-79	1,261,212,510	209,126,958	1,056,105,552	132,666,709	1,220,947,151
1-31-80	1,441,512,698	236,614,266	1,212,958,432	161,031,242	1,445,251,452
1-31-81	1,626,916,440	263,151,527	1,363,764,913	176,319,247	1,621,983,771
1-31-82	1,804,314,072	289,287,649	1,515,056,423	178,283,823	1,788,448,397
1-31-83	1,983,533,741	319,898,562	1,663,795,179	210,479,667	1,986,609,964
1-31-84	2,236,12,812	350,653,678	1,885,959,134	297,995,798	2,332,248,438
1-31-85	2,620,10,570	384,084,066	2,236,426,504	354,312,821	2,734,840,381
1-31-86	2,838,17,230	418,742,719	2,420,104,511	389,989,194	3,153,863,618
1-31-87	3,255,49,253	446,913,523	2,808,565,730	425,966,285	3,639,017,761
12-31-87	3,602,808,133	470,145,466	3,132,662,667	452,396,145	4,088,910,970

Liabilities

<u>Date</u>	<u>Revenue Bonds²</u>	<u>Current Liabilities¹</u>	<u>Deferred Credits and Reserves</u>	<u>Contributions In Aid Of Construction</u>	<u>City Equity In Plant</u>	<u>Total</u>
1-31-77	\$ 358,110,000	\$ 48,142,063	\$ 3,158,921	\$ 18,529,474	\$ 464,788,088	\$ 892,728,546
1-31-78	484,290,000	40,651,961	2,075,149	20,367,567	496,279,998	1,043,664,675
1-31-79	622,975,000	54,035,211	2,538,062	22,175,416	519,223,462	1,220,947,151
1-31-80	783,645,000	59,596,985	34,346,140	24,261,647	543,401,680	1,445,251,452
1-31-81	926,505,000	47,497,568	35,353,271	26,681,508	585,946,424	1,621,983,771
1-31-82	1,041,105,000	44,706,131	35,782,030	28,694,186	630,161,030	1,788,448,397
1-31-83	1,153,740,000	52,309,397	33,706,094	30,439,051	716,445,422	1,986,609,964
1-31-84	1,342,785,000	114,504,518	37,258,566	33,714,618	803,455,736	2,332,248,438
1-31-85	1,555,671,161	181,471,737	18,141,551	38,118,041	941,437,891	2,734,840,381
1-31-86	1,812,539,954	163,410,651	22,381,630	43,105,511	1,112,425,872	3,153,863,618
1-31-87	2,023,218,210	170,210,052	102,693,539	46,890,390	1,296,005,570	3,639,017,761
12-31-87	2,241,879,350	165,142,782	98,421,345	52,105,636	1,531,361,857	4,088,910,970

¹ Excludes current maturities of long-term debt.

² Includes unamortized premiums and discounts and current maturities of long-term debt.

COMPARATIVE ANALYSIS OF ELECTRIC AND GAS UTILITY OPERATIONS¹
 (Dollar Amounts in Thousands Provided)

Fiscal Years Ending January 31:

	1979	1980	1981	1982	1983	1984	1985	1986	1987	1987 ⁴	Increase 1979- 1987 ⁴
DOLLARS											
Revenue	\$343,257	\$367,350	\$441,030	\$525,777	\$687,691	\$715,457	\$804,254	\$868,833	\$804,218	\$792,393	131%
Operating Expense	231,685	241,253	295,906	345,787	454,104	466,429	480,117	497,710	423,207	401,258	73%
Balance Available ²											
For Debt Service	111,572	122,097	148,124	179,990	233,587	249,038	324,137	371,123	381,011	391,135	251%
Depreciation Expense	27,502	29,274	37,701	71,084	34,953	35,918	37,837	40,351	41,811	43,267	57%
Earnings Before											
Interest Expense	84,070	92,823	118,023	148,906	198,634	213,120	286,300	330,772	339,200	347,868	314%
Interest on Bonds	34,362	44,216	55,798	69,131	82,521	95,342	118,437	143,111	160,837	168,871	391%
Payments and											
Benefits To City ²	39,631	43,310	52,570	61,887	78,822	81,693	95,507	103,972	96,191	97,234	145%
Interest During											
Construction	(12,867)	(18,714)	(32,766)	(34,310)	(40,871)	(48,439)	(64,467)	(87,296)	(101,402)	(105,491)	710%
Net Income	\$ 22,944	\$ 24,081	\$ 42,421	\$ 72,193	\$ 73,162	\$ 84,574	\$ 136,793	\$ 170,985	\$ 183,574	\$ 188,254	720%
PERCENTAGES											
Revenue	100.00%	100.00%	100.00%	100.00%	100.00%	100.00%	100.00%	100.00%	100.00%	100.00%	
Operating Expense	67.50%	66.76%	66.64%	65.77%	66.03%	65.19%	59.70%	57.29%	52.52%	50.64%	
Balance Available											
For Debt Service	32.50%	33.24%	33.36%	34.23%	33.97%	34.31%	40.30%	42.71%	47.11%	49.36%	
Depreciation Expense	8.01%	7.97%	6.78%	5.91%	5.06%	5.02%	4.70%	4.64%	5.20%	5.46%	
Earnings before											
Interest Expense	24.49%	25.27%	26.58%	28.32%	28.89%	29.71%	35.60%	38.07%	42.18%	43.90%	
Interest on Bonds	10.01%	12.04%	12.57%	13.15%	12.00%	13.33%	14.73%	16.47%	20.00%	21.31%	
Payments and											
Benefits To City ²	11.55%	11.79%	11.84%	11.77%	11.46%	11.42%	11.88%	11.97%	11.96%	12.27%	
Interest During											
Construction	(3.75%)	(5.11%)	(7.38%)	(6.53%)	(5.94%)	(6.77%)	(8.02%)	(10.05%)	(12.61%)	(13.44%)	
Net Earnings ³	6.68%	6.55%	9.55%	9.73%	11.37%	11.81%	17.01%	19.68%	22.83%	23.76%	
Times Bonds Interest											
Number of Customers (Average For Year End)	3.25	2.76	2.65	2.40	2.83	2.61	2.74	2.59	2.37	2.32	
Electric	300,860	315,487	333,187	349,697	363,947	385,844	413,842	435,003	454,102	459,685	53%
Gas	245,335	252,279	259,786	266,563	269,997	274,488	270,019	281,934	284,558	284,478	161

Footnotes:

¹ The only changes in rates during the 9-year period shown were increases of 7.4% for gas in September, 1979; 5.4% for electric in October, 1979; 6.0% on the total bill in June, 1981; 5.1% in May, 1982; 7.3% in January, 1984; 4.26% in December, 1984; 2.75% in January, 1986.

² Does not include Street Light Construction.

³ Excludes gain (loss) on sale of assets.

⁴ 12 months ending December 31, 1987.

CITY PUBLIC SERVICE BOARD OF SAN ANTONIO
RECORD OF GROWTH-PRODUCTION - ELECTRIC POWER

F Y Ended 1-31:	Net KWH Generation	Percent Increase	Maximum KWH Demand	Percent Increase	Average ¹ KWH Demand	Percent Load Factor
1966	2,811,697,900	6.66	664,000	6.24	346,000	48.34
1967	3,107,039,900	10.50	759,000	14.31	562,000	46.73
1968	3,512,454,400	13.05	840,000	10.67	625,000	47.60
1969	3,930,310,100	11.90	941,100	12.02	689,000	47.55
1970	4,524,422,200	15.12	1,107,000	17.64	786,000	46.66
1971	4,827,311,000	6.69	1,144,000	3.34	834,000	48.17
1972	5,334,120,600	10.50	1,274,000	11.36	964,000	47.67
1973	5,884,186,800	10.31	1,364,000	7.06	1,060,000	49.11
1974	5,784,500,600	(1.69)	1,415,000	3.74	1,059,000	46.67
1975	5,806,029,700	.37	1,412,000	(.21)	1,031,000	46.94
1976	6,071,902,600	4.58	1,493,000	5.74	1,089,000	46.42
1977	6,211,489,100	2.30	1,560,000	4.49	1,078,000	45.33
1978	6,691,908,500	7.73	1,641,000	5.19	1,133,000	46.55
1979	7,267,236,400	8.60	1,688,000	2.86	1,203,000	49.15
1980	7,453,424,800	2.56	1,707,000	1.13	1,265,000	49.84
1981	8,079,949,500	8.40	1,950,000	14.24	1,363,000	47.17
1982	8,505,723,900	5.27	1,911,000	(2.19)	1,442,000	50.81
1983	8,913,765,200	4.80	1,984,000	3.82	1,522,000	51.29
1984	8,992,119,700	.88	2,148,000	8.27	1,572,000	47.79
1985	9,774,125,100	8.70	2,210,000	2.89	1,723,000	50.35
1986	10,607,971,800	8.53	2,350,000	6.33	1,790,000	51.53
1987	10,617,859,300	.093	2,596,000	10.47	1,894,000	46.69
1987 ²	11,141,884,800	4.94	2,551,000	(1.73)	1,881,000	49.86

¹ Average of Monthly Peak Demands.

² 12 months ending December 31, 1987.

³ 391,201,000 KWH were purchased this fiscal year; for comparability, total KWH generated and purchased of 11,009,060,300 KWH increased 3.8% over previous year. Generation for the 12 month period ended December 31, 1987, compared to generated and purchased power last year, increased 1.2%.

FIVE-YEAR FORECAST OF ELECTRIC AND GAS OPERATING DATA
(Dollars in Thousands)

	Fiscal Years Ended 1-31:				
	1989	1990	1991	1992	1993
Gross Revenues ¹	\$771,454	\$817,878	\$920,384	\$1,014,814	\$1,074,299
Total Operating Expenses	376,497	389,208	427,726	474,685	528,426
Available for Debt Service	\$394,957	\$428,670	\$492,658	\$540,129	\$ 545,873
Anticipated Bond Issues	\$160,000	\$270,000	\$185,000	\$ 95,000	\$ 105,000
Annual Debt Service Requirements	\$217,704	\$243,170	\$211,438	\$274,052	\$ 282,536
Estimated Debt Service Coverage	1.81x	1.76x	1.88x	1.97x	1.93x
Estimated KWH Sales (000,000)	10,948	11,527	12,049	12,654	13,283
Revenue per KWH					
Total (cents)	5.81	5.97	6.45	6.77	6.78
Residential (cents)	6.63	6.84	7.36	7.70	7.71
Estimated Peak (MW)	2,638	2,769	2,877	3,004	3,127

¹ The foregoing estimates assume future basic rate increases in the following fiscal years: 5.1% in 1989; 6.0% in 1990; 3.0% in 1991; 0.0% in 1992; and 0.0% in 1993. While annual rate increase requests are currently forecasted, there is no assurance that the amounts will be requested or that current and future City Councils will approve any particular rate increase requested. (See Rate Increases).

THE 1989 - 1993 CONSTRUCTION PROGRAM

A comprehensive program of planning and construction to meet current and future electric and gas needs is continually being reviewed, updated and extended. To reduce time required and maximize accuracy, CPS utilizes computer-based mathematical models for its forecasting process. CPS bases its near term construction and operating needs on a five-year forecast, which is a part of a twenty-five year development and electric generation plan that is maintained.

The CPS generation plan includes completion of the South Texas Project (the "Project" or "STP") generation units. The CPS share of this Project is 350 MW from each unit, scheduled for operation in 1988 and 1989, respectively. See "South Texas Project". The long-range plan also includes additional generating capacity for operation in 1992. In June, 1986, the CPS staff recommended to the CPS trustees that these generation needs be met by a 500 MW coal-fired generating station to be constructed by summer, 1992, at CPS's Calaveras Lake site in Bexar County near the existing coal and gas-fired generation plants at that location. The staff likewise recommended expansion of CPS's conservation program and energy management plan with the target of eliminating the need for one 400-500 MW unit by 2000, reassessment and refurbishment of CPS's older natural gas-fired units, and completion of the present acquisition program for lignite in the North Bastrop prospect, to be held for future development. The staff recommendation followed several months of study comparing power plant fuels including natural gas, western coal, lignite, municipal solid-waste, and renewable energy sources, as well as staff analysis of cogeneration proposals received and evaluated in a two-tier solicitation and evaluation process. Western coal was evaluated as the favored option based on the economic advantages provided by reduced rail transportation rates, lower capital cost compared to lignite and other options, lower life-time revenue requirements compared to other alternatives, and fuel diversification considerations. Estimated capital cost for the coal plant at the Calaveras site, including interest during construction, is \$1,160 per KW. The City Council passed a resolution in September, 1986, endorsing the CPS staff's coal plant recommendation. In connection with its review of all reasonable alternatives to CPS-built coal-fired generating capacity prior to final commitment, and in response to various unsolicited proposals received, CPS published notice of a solicitation of proposals in December, 1986, for turn-key electricity generating capacity or package units. Professional engineering consultants were hired to review the proposals submitted. In May, 1987, the consultant recommended the package unit proposal submitted by a consortium of H. B. Zachry, Combustion Engineering and Utility Engineering Corp. The CPS Board of Trustees authorized staff to enter into contract negotiations with this group, and a contract was executed in December, 1987.

Long-range plans also indicate the need for additional capacity in 1997 and 1999, which could be fueled by CPS lignite resources. CPS presently owns or leases approximately 261 million tons of lignite reserves, which could fuel 2,000 MW of generating capacity, depending upon the mineability of the lignite. (See Fuel Supply - Lignite.) Final commitment to install these units will depend on future load growth developments and economic considerations after full evaluation of the alternatives available. CPS engineers estimate that the construction costs of a lignite-fired unit, if built in 1999, would be \$1,805 per KW.

Historically, peak demand on the CPS electric system increased about 11 percent per year between 1950 and 1972. Beginning about 1972, the growth rate of peak demand declined sharply because of rising energy prices, fuel shortages, and conservation efforts. Since that time, CPS has conducted extensive reviews of changing economic, demographic, and energy supply considerations, and produced annual forecasts of electric growth. The latest forecast projects a peak demand growth rate averaging 3.9 percent per year over the 1988-2012 period. The CPS staff continually monitors growth trends in order to identify changes in time for appropriate modification of long range system plans.

CPS continues to review alternative forms of power generation which include both conventional alternatives and non-conventional, emerging technologies. Within the CPS system, the primary conventional alternatives are nuclear, coal, gas, oil and lignite. Among the non-conventional technologies are municipal solid waste, co-generation, compressed air storage and solar. Primary indications are that refuse fuel will be available in sufficient quantities to produce about 36 MW of generation. CPS, in conjunction with the City, has considered construction of a mass-burn facility at the Leon Creek Plant having an estimated cost of \$154,000,000. Currently CPS and the City are still discussing the economic benefits of such a plant. If the project provides an economic benefit, the joint project could be in operation in late 1991, to have a 25-year life and to burn an estimated 1,800 tons of waste per day. While CPS and the City intend this project to be a joint venture, the actual sharing of project costs and responsibilities for project implementation have not been established. In addition, CPS has agreed to limited participation with Basic Resources, Inc., a subsidiary of the Texas Utilities Electric Company, and purchase of power from a six MW plant to be located in Lee County and fueled by lignite gasification. Arrangements for such project are not yet final.

CPS's current five-year forecast calls for construction expenditures of \$1.668 billion. The \$160 million which will be raised by the Bonds will supply certain of the required funds, as will revenues from operations. The next sale of additional New Series Bonds is tentatively scheduled for early 1989, except for any refunding bonds which may be issued for interest savings.

Currently proposed capital expenditures for fiscal years 1989 - 1993, based upon detailed estimates which include interest during construction, are shown in the following table:

ESTIMATED CAPITAL EXPENDITURES FOR THE CONSTRUCTION PROGRAM
(Thousands of Dollars)

	Fiscal Years Ending 1-31:				
	1989	1990	1991	1992	1993
GAS	\$ 17,379	\$ 15,825	\$ 17,086	\$ 17,510	\$ 18,721
ELECTRIC:					
Distribution	51,905	67,981	71,324	70,145	74,987
Transmission	12,963	11,202	11,312	13,299	25,469
Production (Power Plants):					
South Texas Project	191,215	30,199	3,658	4,502	8,442
Acquisition of Additional Fuel Reserves	2,540	6,308	6,108	6,912	10,099
Tools and Equipment	2,750	1,125	1,174	1,233	1,429
Railroad Car Purchase and Replacement	(350)	(364)	(379)	(396)	(415)
Railroad Cars (Unit Train Additions)	0	0	0	0	11,463
Special Projects	5,751	7,335	3,449	1,146	1,208
Cycling Conversion -- J.T. Deely	1,338	0	0	0	0
1992 Generating Plant Site	781	4,939	1,470	1,559	435
Initial Lignite Mine	177	224	234	383	2,647
Lignite I, Plant Site A (1999)	0	0	0	0	7,604
Lignite I, Unit 1 (1999)	0	0	0	0	2,892
Calaveras Unit #5-Coal (1992)	85,890	199,780	171,511	96,212	20,982
Calaveras Unit #6-Coal (1997)	0	0	0	3,263	34,828
Resource Recovery Facility (1992)	2,000	33,712	59,150	51,828	4,376
Total Electric	356,960	357,441	329,011	250,086	206,446
GENERAL PROPERTY	25,375	14,790	16,520	12,392	12,420
TOTAL CONSTRUCTION BUDGET	\$ 399,714	\$ 388,056	\$ 362,617	\$ 279,988	\$ 237,587
ANTICIPATED BOND ISSUES	\$ 160,000	\$ 270,000	\$ 185,000	\$ 95,000	\$ 105,000

Total expenditures over the five year fiscal period 1989-1993 are shown in the following table:

	(\$000)	Percent of Total
STP	\$238,016	14.2%
Coal Units #5 & #6.	621,650	37.3
Resource Recovery Facility.	151,066	9.0
Lignite	46,128	2.8
All other electric.	443,084	26.6
General property.	81,497	4.9
Gas	86,521	5.2
Total.	\$1,667,962	100.0%

The electric utility industry in general is currently experiencing difficulties in a number of areas, including availability and high cost of capital, exposure to cancellation and penalty charges on new generating units under construction, fuel availability, uncertainties in predicting future load requirements, litigation and proposed legislation designed to delay or prevent construction of generating and other facilities and to limit the use of existing facilities, compliance with environmental regulations, licensing and other delays affecting the construction of new facilities and the effects of conservation on the use of electric energy. Any of these factors may require modification of facilities and in some cases delay construction with resulting increases in construction and operating costs and may require modification of the plans and estimates described above.

SOUTH TEXAS PROJECT

Approximately 14% of the scheduled 1989-93 construction program is for completing construction of the two unit nuclear generating station at the South Texas Project, (the "Project" or "STP"). In June, 1973, CPS agreed to participate in the Project, which involves the construction of two 1,250 MW units in the Palacios-Bay City area on a 12,000 acre site near the Texas Gulf Coast. Participants in the Project and their share therein are as follows:

Houston Lighting & Power Company (HL&P)	30.8%
City Public Service Board of San Antonio	28.0%
Central Power and Light Company (CPL)	25.2%
City of Austin (Austin)	<u>16.0%</u>
	100.0%

The required construction permits approving the Project were awarded by the Nuclear Regulatory Commission (NRC) in December, 1975, and extended in April, 1982, to include the currently scheduled completion dates. San Antonio's share of the two 1,250,000 KW units is 700,000 KW. HL&P is the Project Manager for design, engineering, construction, licensing, and operation of the Project.

The estimated capital expenditures for CPS' interest in the STP are based upon an estimated total direct cost of both units of the Project of approximately \$5.278 billion, or \$2,111 per kilowatt, after consideration of the Brown & Root settlement (referred to below). The above total Project cost is based upon a review concluded in September, 1987, by HL&P, Bechtel Energy Corporation (Bechtel) and Ebasco Constructors Incorporated (Ebasco) called the "Completion Assessment." The Completion Assessment was based on projected commercial operation commencing in February, 1988, and June, 1989, for Units 1 and 2, respectively. A subsidiary of Bechtel Power Corporation, Bechtel Energy Corporation, is the architect-engineer and construction manager of the Project. Bechtel was retained in September, 1981, to replace Brown & Root, Inc. (Brown & Root) following protracted engineering and construction delays. In February, 1982, Ebasco Constructors, Inc., a subsidiary of Ebasco Services Incorporated, was retained as the new constructor following Brown & Root's withdrawal as constructor in November, 1981. For a description of the settlement of litigation relating to Brown & Root see Note 8 to Financial Statement in Appendix B.

The Completion Assessment described above reflects an increase in the total cost to complete both Units of \$300 million over previous estimates and contains an allowance to cover contingencies. Based upon this estimate and a subsequent projected delay into June, 1988, for commercial operation of Unit 1, the total cost of the CPS share of the Project would be \$2.1 billion for construction and interest during construction and \$115 million for fuel purchases prior to commercial operation of each unit. In January, 1988, the Project Manager's projection for Unit 1 commercial operation was for 3 to 5 months following initial criticality forecasted for mid-February, 1988, with Unit 2 projected to remain on-schedule with commercial operation expected in June, 1989. If these estimates and projections prove incorrect, the Project cost and schedule would be adversely affected. Through December, 1987, CPS has expended approximately \$2.0 billion on the Project including interest during construction and advance payments for fuel after consideration of the Brown & Root Settlement.

An operating license authorizing the loading of fuel and operation of Unit 1 of the STP at power levels up to 5% of rated thermal power was issued by the NRC on August 21, 1987. The Project Manager loaded fuel shortly thereafter and commenced an initial startup test program. As mentioned above, a January, 1988, forecast by HL&P projected that Unit 1 would reach its initial criticality by mid-February, and HL&P expects thereafter to seek authorization from the NRC to proceed with its test program up to full power operation.

The NRC commenced an on-site investigation on January 18, 1988, to review and evaluate potential concerns regarding construction quality received from the Government Accountability Project (GAP), a citizens interest group. In 1987, GAP demanded that the NRC establish a special task force to investigate alleged safety defects at the STP. The group claimed to have evidence of defects but refused to turn over the information until late in 1987. Although no official notification has been received from the NRC regarding the details of the GAP allegations, the Project Manager believes that any concerns that might have been raised by GAP have been previously investigated and addressed. On January 26, 1988, GAP filed a Petition with the NRC claiming that the investigation of its allegations was inadequate and requesting delay in NRC voting on a full power operating license until a "through" investigation is completed and its results publicly released. While the NRC has not restricted the approach to initial criticality during investigation of the GAP allegations, CPS cannot predict whether this investigation or other activities may affect the cost and scheduled commercial operation dates of the STP Units.

In a January, 1985, order in a HL&P rate proceeding, the Public Utility Commission of Texas (the "PUC") directed that its staff "docket a proceeding to gather the best current evidence concerning the economic viability of Unit 2 of the South Texas Project." That proceeding is pending before the PUC. While CPS believes that the economic viability of Unit 2 can be supported in the proceeding, it cannot predict PUC action regarding STP rate treatment of HL&P and CPL, nor the effect which such orders might have on the Project.

By January, 1988, HL&P had been notified that the NRC was considering "potential enforcement actions" against STP as a result of operations in violation of the operating license Technical Specification and breakdowns in the STP Security Program subsequent to the issuance of the operating license. On February 12, the NRC

announced that it would impose a \$75,000 fine in connection with the two Technical Specification violations. CPS cannot predict whether further enforcement action will be taken or further civil penalties will be imposed, nor whether such actions may adversely affect the schedule for requesting authorization for full-power operation of Unit 1.

On November 3, 1981, the City of Austin, Texas, conducted a public referendum on whether its City Council should be authorized to sell all of Austin's 16% interest in the South Texas Project. A majority of those voting on the referendum voted to give the Austin City Council such authority. To date, Austin has been unable to sell all or part of its share in the Project, and has filed suit against HL&P seeking to "reform" and/or "rescind" parts of the Participation Agreement to, in effect, require HL&P to assume ownership and financial responsibility for Austin's share. While the court has granted summary judgment against the "reformation/rescission remedies", Austin has amended its petition to seek substantial damages against HL&P, including the trebling of such damages under certain circumstances, for mismanagement of the Project, and other claims. The case is presently set for trial in Dallas, Texas. In September, 1987, Austin and HL&P announced an agreement in principle to settle the litigation on terms which, among other things, would result in a transfer of Austin's interest in STP to HL&P. The settlement is contingent on negotiation of definitive documents to implement the agreement in principle, which is continuing. CPS is unable to predict if, when, to whom or upon what terms Austin's share of the South Texas Project may be sold, or transferred, the outcome of Austin's litigation with HL&P, or the effect on the Project. In January, 1988, HL&P brought suit against CPS, CPL and its parent Central and Southwest Corporation (CSW) in Matagorda County and also sought to join them as third-party defendants in the Dallas suit brought by Austin. See "Litigation" for a more detailed description of these suits.

ENVIRONMENTAL MATTERS

CPS is subject to extensive regulation with respect to air and water quality, solid waste disposal and other environmental matters by various federal, state and local authorities. Environmental standards have been established by the Texas Air Control Board, the Texas Water Commission and the Environmental Protection Agency (EPA). CPS has permits from EPA and the Texas Water Commission for liquid waste releases for all existing CPS power plants in Bexar County. Operating permits for the J.T. Deely coal plant are expected to be issued when the retrofit project referred to below is completed and following an adequate demonstration period. CPS has demonstrated compliance with all federal and state air emission standards with the exception of the 20% opacity limitation applicable at its J.T. Deely coal plant. Pursuant to a relief order issued by the Texas Air Control Board in December, 1985, CPS is authorized to operate the plant at 35% opacity so long as the existing particulate control equipment is in use. A request for similar relief has been submitted to EPA, which has in the past granted such relief to other utilities. CPS has recently completed the process of retrofitting both units with new cold-side particulate control equipment. Although compliance tests are not yet complete, these retrofits are expected to allow operation of the plant in compliance with the 20% standard on a more economical and reliable basis.

In accordance with The National Environmental Policy Act, The Clean Air Act, The Clean Water Act and their counterparts at the state level, CPS has submitted an Environmental Information Document and all applicable permit applications to the responsible authorities in conjunction with the proposed 1992 new coal unit. These permits and authorizations for construction are required to be in hand as a prerequisite to commencement of construction.

FUEL SUPPLY

COAL

In May, 1974, CPS signed a 20-year contract for the purchase of coal from the Sun Oil Company, which contract has been assigned to and is being performed by its affiliate, Cordero Mining Company. The contract provides a total 55,450,000 tons of low-sulfur coal committed to CPS from substantial reserves held in Campbell County, Wyoming. The 1986 coal cost averaged \$7.16 per ton and \$4.50 per ton for 1987. Effective January 1, 1987, CPS served a notice of termination of the contract on the supplier, as permitted by the contract, based on a significant discrepancy between contract and market price, and thereafter entered into discussions with the supplier to renegotiate the contract price. In July, 1987, the parties agreed to set the capital segment of the contract price at \$.80 per ton for a minimum three-year period, but agreed that, if in any calendar year the contract price is less than \$4.55 per ton, the capital segment will be increased for that year by one-half the difference between the contract price and \$4.55. The parties also revised contract provisions relating to the heating value of the coal as a function of contract price in order to reduce the upward effect on price of high BTU-value coal. This amendment to the 1974 agreement avoids termination of the contract and effectively lowers the base price. During the third quarter of 1983, CPS negotiated a secondary coal agreement with the supplier allowing CPS to pay a lower price for all coal purchased in excess of the contract quantity. This agreement, as currently amended, will terminate at the end of 1988, and provides for a secondary coal price of \$3.25 per ton with adjustment for BTU content as provided for in the 1987 amendment to the main coal supply agreement.

Following a solicitation of competitive bids in the Spring of 1985 for a long-term rail transportation contract for delivery of its coal, CPS awarded a 20 year term contract to Western Railroad Properties, Inc. ("WRPI"), a corporation formed by Chicago North Western Transportation Company together with the Union Pacific Railroad. The rate is presently \$20.74 per ton for CPS' current shipment volumes. CPS commenced taking

deliveries under this contract in August, 1985, following completion of trackage arrangements. These rates are significantly less than rates paid to CPS' previous carriers, Burlington Northern Inc. and Southern Pacific, which transported CPS' coal pursuant to filed Interstate Commerce Commission (I.C.C.) tariffs between 1976 and 1985.

In December, 1986, the CPS Board approved a settlement offer from its former coal carriers (Burlington Northern and Southern Pacific) which settled all disputes between CPS and the carriers arising from or relating to the transportation of coal occurring prior to December 23, 1986. The settlement provided for CPS to dismiss actions brought by it before the I.C.C. and the United States District court in San Antonio, Texas and for Burlington Northern and Southern Pacific to dismiss the law suit filed by them in the U.S. District Court in the Fort Worth, Texas. Following the entry of orders dismissing both the Commission proceeding and the United States District Court San Antonio Division action, Burlington Northern and Southern Pacific paid to CPS their respective share of \$31 million. On January 4, 1988, an additional \$10 million was received by CPS and over the next six years Burlington Northern and Southern Pacific will make additional annual payments ranging from \$10.5 million to \$13 million to CPS. Total payments to be made by Burlington Northern and Southern Pacific under the settlement agreement amount to \$111.5 million. The initial payment was applied by CPS to replace utility funds previously advanced to make court-ordered rail tariff payments and to pay legal expenses related to the dispute. Subsequent installments are being returned to customers as they are received.

For the 12 months ending December 31, 1987, CPS burned 2.75 million tons of coal at an average price of \$27.70 per ton to produce electricity from the J.T. Deely Plant. Approximately 38 percent of the electricity provided during the period was from the coal-fueled units. The CPS coal in stock as of December 31, 1987 was 884,535 tons, or approximately 3.8 months supply, and has an inventory cost of about \$19.2 million.

NATURAL GAS

CPS's primary natural gas supply has been provided under a five-year contract with Valero Transmission Partners, L.P. (Valero) successor to Valero Transmission Company, a subsidiary of Valero Energy Corporation. This current contract, which expires in June, 1988, requires Valero to provide CPS requirements for burner tip and electric generation needs at Valero's weighted average cost of gas plus a cost of service factor set by the Railroad Commission of Texas (The RR Commission), and requires CPS to purchase its requirements from Valero, with the option to buy from others, and transport through the Valero system, up to 41,500 MCF of gas per day, or approximately 16% of CPS' 1987 requirements. CPS has been generally successful in acquiring the full volume of "transport gas" delivered to San Antonio at substantially lower prices than the current Valero weighted average cost of gas plus the cost-of-service factor. In addition, because CPS may otherwise purchase energy from others at favorable prices which would result in substantially reduced natural gas usage in CPS's power plants, Valero has made available large quantities of natural gas from its affiliates at favorable prices under similar terms for use in CPS power plants.

Following solicitation of bids for a new gas supply, to commence after expiration of the current Valero contract, the CPS trustees, on December 21, 1987, accepted the bids of Valero Natural Gas Partners, L.P. for at least 80 percent of CPS's gas requirements and of Houston Pipeline Company for at least 15 percent of CPS's gas requirements, subject to negotiation of satisfactory terms and conditions, including assurance of a reliable gas supply. Negotiations toward final contracts with these suppliers are proceeding. The prices for gas under both Valero and Houston Pipe Line bids will be based on spot gas prices plus markups.

Under a 1979 order of the RR Commission, CPS pays Valero for delivery of natural gas at Valero's weighted average cost of gas plus 15 cents per MCF. Valero's estimated cost of gas for the month of December, 1987, was \$4.30 per MCF. The average estimated cost of "transport gas" during December was approximately \$2.78 per MCF. The average actual cost for all natural gas purchased by CPS during November, 1987, including additional volumes made available by Valero affiliates for power plants, was about \$2.07 per MCF.

The Valero rate is subject to review and revision by the RR Commission, and the future price of natural gas cannot be predicted accurately. Under the RR Commission's order of December 22, 1980, Valero must interrupt natural gas deliveries to its customers in periods of supply shortages in accordance with priorities set in that order. In general, delivery of natural gas for gas distribution systems is interrupted last, for electric generation next, and large industrial use first. These priorities are subject to RR Commission review and revision. Valero and its predecessor have generally been able to meet all natural gas requirements of CPS except for minor curtailments on certain peak days.

In 1987, Valero Energy Corporation formed a limited partnership to which it transferred its natural gas pipeline and other natural gas assets. Valero Energy retained a 49% interest in the partnership and it or its subsidiaries serve as the general partner to manage and operate the partnership assets. The reorganization included the transfer of Valero Energy's gas supply and sales contracts to the partnership. The reorganization has had no adverse effect on the performance of the gas contract, which is guaranteed by Valero Energy Corporation, or upon the jurisdiction of the RR Commission under current law.

As part of a 1979 settlement of CPS claims against its then natural gas supplier, predecessors of Valero, and the supplier's then parent Coastal Corporation (Coastal), Coastal undertook a gas search program requiring a minimum expenditure by Coastal of \$180 million over 15 years to develop new gas reserves to be committed to Valero's predecessor with a discount from market prices to be passed through to CPS and other settling customers. In January, 1986, Coastal filed a suit in State District Court in Hidalgo County, Texas seeking a

declaratory judgment as to Valero's predecessor, the Settlement Trustee, and the settling customers, including CPS, that Coastal's obligation under the gas search program had terminated. A settlement of this suit was approved by the required number of settling customers having an interest in the gas search program, and by a State District Court in Travis County, Texas, in June, 1987. The settlement terminated the program and substitutes the opportunity for settling customers to purchase their share of 40,000 MCF per day of gas from Coastal for six years at prices discounted from a defined fluctuating market average price. CPS' settlement interest obtains 7,550 MCF per day from Coastal, commencing September, 1987. The cost for the month of November, 1987 was \$1.52 per MCF. The supply fulfills about 3.0% of CPS' requirements.

NUCLEAR

The supply of fuel for nuclear generating facilities involves the acquisition of uranium concentrate, its conversion to uranium hexafluoride, enrichment of gaseous uranium hexafluoride, and fabrication of nuclear fuel assemblies. Following use of the nuclear fuel assemblies, they must either be disposed of or reprocessed to recover remaining fuel value.

Westinghouse Electric Corporation (Westinghouse) has contracted to provide the South Texas Project participants with at least 7,377,000 pounds of uranium concentrate, which, together with additional uranium provided by Chevron USA, Inc., is expected to support the operation of both STP units through the late 1990's. Options are held under these supply contracts to purchase additional uranium concentrate subject to the development of additional uranium reserves.

Contracts with Westinghouse and others for conversion services will support the operations of both STP units through the early 1990's. Contracts for enrichment services provide coverage for up to 30 years operation. Westinghouse has also contracted to furnish fuel fabrication services for the initial core and 16 years of reloads for both units.

LIGNITE

CPS is continuing to acquire lignite reserves sufficient to make up a mining block for possible future generation use. Lignite reserves of about 100 million tons would be required to meet the long-term, base load needs of a 500 MW generating unit. CPS presently owns approximately 174 million tons of lignite reserves located in Lee and Bastrop Counties, approximately 90 miles from San Antonio. CPS has leased reserves of approximately 87 million tons adjacent to its owned reserves, resulting in a total of 261 million tons of reserves. CPS also owns an undivided 35% interest in certain lignite leases in North Bastrop County adjacent to its other properties. CPS is continuing reserve mapping and negotiation for the acquisition of additional lignite reserves in the immediate area of its present reserves. See "Litigation" for discussion of an administrative proceeding affecting the development of CPS lignite reserves.

Pursuant to requests filed by CPS and the Lower Colorado River Authority ("LCRA"), the Bureau of Land Management ("BLM") has indicated that it will hold a competitive lease sale for lignite reserves under Camp Swift Military Reservation in Bastrop County, Texas, located near existing CPS lignite reserves. BLM has determined that a supplemental Environmental Impact Statement (EIS) is required as a prerequisite to the lease sale. LCRA is funding preparation of the Supplemental EIS, which is expected to be available in mid-1989, with a lease sale tentatively scheduled for 1990. The sale is restricted by federal statute to publicly owned power-generating entities. Pursuant to a coal exploration license application granted to CPS by BLM, CPS has conducted exploratory drilling on Camp Swift to assist it in developing an accurate bid. LCRA and Austin are other potential bidders for the Camp Swift reserves.

FUEL OIL

CPS has the capability of using fuel oil to supplement natural gas as an input fuel to generate electricity. Total fuel oil consumption by CPS amounted to 24,856 barrels (No. 2 fuel oil, used for startup and flame stabilization in the coal plant), for the 12 months ending December 31, 1987. CPS has a usable oil storage capability of 1.4 million barrels. As of December 31, 1987, the oil inventory was 786,262 barrels. Very little fuel oil is currently being burned since the replacement price of oil is higher than the natural gas equivalent.

FUEL SUPPLY SUMMARY

Periods of prolonged cold weather, during which natural gas supply may fall short of demand, may necessitate the curtailment of gas use for boiler fuel. The Natural Gas Policy Act, in addition to its pricing provisions, subjects intrastate gas, including gas intended for boiler fuel use, to Presidential emergency purchase authority and emergency allocation authority to assist in meeting interstate natural gas requirements for high priority uses.

Several years ago, CPS completed essential conversion of its existing gas-fired generating units for oil firing to provide greater input fuel flexibility. However, the current price of oil, against the price of competing natural gas supplies, makes its use for other than emergency needs impractical at the present time. In December, 1987, the price of fuel used by or available to CPS was as follows:

Valero - \$4.17 per million BTU (estimated)
Valero transport gas - \$2.78 per million BTU (estimated)
Special power plant gas from \$1.72 to \$1.85 per million BTU
Oil - \$3.61 per million BTU (0.4% No. 2 Fuel Oil --- Delivered by pipeline)
\$2.96 per million BTU (inventory)
Coal - \$1.59 per million BTU (inventory price)

For the long term, CPS plans call for diversification of the electric generating system to emphasize the use of coal, nuclear and lignite as the fuels for base load capacity. CPS plans to maintain the purchase of an adequate fuel supply for the two existing coal-fired units and its planned new coal unit at the most competitive prices. Under the terms of agreement with Westinghouse, along with other contracts entered into, several years' requirements of nuclear fuel for the South Texas Project will be fulfilled at known low costs, which confirm the economic feasibility of the City's participation in the Project.

ENERGY CONSERVATION PROGRAM

For many years, CPS has been encouraging voluntary conservation of electricity and natural gas usage. CPS continues to inform all customers of the various methods available by which customers can reduce energy consumption through the use of conservation measures and by the elimination of unnecessary waste of energy. The results of the voluntary conservation programs and the effect of increasing utility prices have been reflected in the previously mentioned decline in the growth rate of peak demand. In September, 1983, the CPS Board of Trustees authorized the establishment of three additional programs that provide direct incentives for customers who install energy conservation measures and appliances. The appliance rebate program provides for incentive rebate payments to be made to customers who purchase high-efficiency air conditioners and heat pumps. The weatherization loan program funds low cost loans to qualifying customers for the installation of energy-saving enhancements to existing homes. The weatherization materials program provides weatherization materials to residential customers based on the results of home energy audits conducted by CPS energy surveyors. The economics and energy conservation potential of existing programs as well as alternative or additional demand side management initiatives are periodically reviewed to ascertain the need and justification for such programs in the CPS service area. Conservation trends are carefully studied in the development of CPS plant expansion requirements.

CPS is subject to the provisions of the National Energy Conservation Policy Act (NECPA). This 1978 federal energy legislation established certain residential conservation standards and required all electric and/or gas utilities classified as a "covered utility" to follow a plan for implementing the standards under the Residential Conservation Service (RCS) program. CPS is one of 22 covered utilities included in the RCS plan of the State of Texas. The Texas RCS Plan was approved by the Department of Energy and was implemented on October 3, 1981. NECPA standards require utilities to offer to conduct an on-site energy audit of the residential customer's dwelling, inform customers of projected cost savings, and inform the customers of similar audit program directed at apartments and small commercial customers, called the Commercial and Apartment Conservation Service (CACS). The Conservation Service Reform Act of 1986, however, essentially amends NECPA by repealing the requirement for CACS audits and extends the requirements for RCS audits until June 30, 1989. In 1987 the Energy Management Center (EMC) of the Texas Governor's office assumed responsibility for administration of the State RCS program from the Public Utility Commission of Texas. The EMC has issued proposed wording changes to the State RCS Plan to incorporate provisions of the Conservation Service Reform Act. All proposed changes to the plan are administrative in nature and it is anticipated that procedures associated with providing CPS energy audits will not be affected.

LITIGATION

CPS is involved in various legal proceedings related to alleged personal and property damages, breach of contract, condemnation appeals and discrimination cases. In the opinion of management of CPS, the outcome of such proceedings will not have a material adverse effect on the financial position or operations of CPS.

On January 7, 1988, Houston Lighting & Power Company (HL&P), Project Manager of the South Texas Project, filed suit against CPS, Central Power and Light Company (CPL) and CPL's parent, Central and Southwest Corporation (CSW), in State District Court in Matagorda County, the site of STP. Suit was also filed by HL&P against these parties in the Dallas County District Court in which litigation by the fourth STP participant, Austin, against HL&P is presently pending, seeking to have CPS and CPL/CSW brought into the Austin litigation as third-party defendants. The causes of action asserted by HL&P against CPS and CPL/CSW are basically the same in both suits. HL&P continues to deny Austin's claims based on breach of contract, including mismanagement, in connection with HL&P's performance as Project Manager, but asserts that it is entitled to indemnity and contribution from CPS and CPL/CSW to the extent any liability is imposed on HL&P for these or Austin's other claims in the Dallas litigation, which include fraudulent inducement and breach of obligation by HL&P to furnish Project information. Austin's suit against HL&P alleges various elements of damages ranging from \$406 million to approximately \$938 million, to which could be added alleged penalties, costs and attorneys' fees. HL&P alleges that it did not act unilaterally in connection with various Project actions asserted by Austin as a basis for liability because decision making and actions were undertaken by the entire STP Management Committee, including representatives of CPS, CPL and Austin. HL&P requests in both suits that the courts defer trial of any claim arising out of STP and direct the implementation of alternate methods of

dispute resolution, including nonbinding arbitration, as authorized by Texas statutes, and also seeks the entry of declaratory judgements determining that HL&P has no liability to the other participants. The Austin suit has been set for trial the first week of June, 1988, and will not include claims among CPL, CPS and HL&P. CPS does not believe there is any basis for liability to HL&P for Austin's damages or otherwise and will timely answer opposing HL&P's causes of action and may include appropriate counterclaims against HL&P seeking recovery of damages attributable to acts and omissions of HL&P as Project Manager. CPS cannot predict which court or an alternative dispute resolution procedure will be the forum for adjudication of these claims, or the outcome of such actions.

In late 1987, CPS was added as a defendant in a suit brought by the State of Texas in a Nueces County State District Court alleging violations of the Texas Solid Waste Disposal Act and other Texas statutes in connection with certain lead and PCB-contaminated waste disposal sites and adjacent tracts in Nueces County, Texas. The suit, originally filed in 1981, names 28 defendants, including past and present owners of the tracts, entities which used the tracts for waste disposal, operators of waste disposal operations on the tracts, and three utilities, including CPS, who are alleged to have shipped PCB-contaminated electric transformers to the sites for commercial disposal, salvage or reclamation by the operators during the 1970's. CPS is also alleged to have furnished certain lead waste materials for disposal at the sites. The suit alleges that the sites are an unauthorized disposal facility to which wastes were shipped in violation of the Texas Solid Waste Disposal Act and administrative regulations and that the wastes were shipped without proper record keeping as required by State law. The suit, seeks civil penalties in amounts ranging from \$50 to \$25,000 for each act of violation and day of violation under applicable statutes, without specifying aggregate claims against any defendant, and attorneys' fees and costs on behalf of the State. The suit also seeks to have the defendants submit and implement a sampling and testing plan for the sites and a closure plan providing for removal or impoundment of all wastes. Studies done by other defendants in the litigation estimate the costs of cleanup of PCBs and closure of these sites to be approximately \$1 million, which is proposed to be allocated among CPS and other solvent defendants as part of a proposed settlement. The extent of contamination of the sites by lead wastes is presently not known, and the cost of cleanup and closure for these wastes cannot presently be estimated. CPS has answered the suit and will vigorously defend claims against it, but cannot predict the ultimate outcome or magnitude of liability to which it may be subject.

In August, 1983, two petitions to declare large areas of Bastrop and Lee Counties unsuitable for surface lignite mining were filed with the Surface Mining Division of the Railroad Commission of Texas (the RR Commission) by landowners in these areas. The petitioners claim that surface mining could have adverse or irreversible effects on several specified aquifer systems and related re-charge zones in the designated areas which encompass virtually all of CPS' lignite reserves. The RR Commission declared the petitions complete in September, 1983, and a public hearing was held in July, 1984, as to the issues raised. The examiner's report and proposal for decision based on the hearing evidence has been released and recommends designating no lands unsuitable. A final ruling by the RR Commission is expected during 1988. Under its rules, the RR Commission is required to designate lands as unsuitable based on the record developed in this proceeding, if it determines that reclamation is not technologically and economically feasible. Furthermore, it may designate lands unsuitable if it finds that mining operations (i) will be incompatible with existing local land use plans, (ii) can result in substantial loss or reduction of long-range productivity of water supply, or (iii) will have other specified adverse affects. CPS, in conjunction with other owners of lignite reserves in the area, has opposed the designation of the lands as unsuitable in this proceeding. See "San Antonio Electric and Gas Systems - Fuel Supply - Lignite".

RATES AND REGULATION

Under the Texas Public Utility Regulatory Act (Article 1446c), significant original jurisdiction over the rates, services and operations of electric "public utilities" is vested in the Texas Public Utility Commission. The Railroad Commission of Texas has parallel jurisdiction over "gas utilities" under similar provisions in the Texas Gas Utility Regulatory Act (Article 1446e). These Acts generally exclude from their coverage "municipally-owned utilities," such as CPS. CPS is subject to appellate but not original rate regulatory jurisdiction by the two regulatory entities in unincorporated areas in which it serves. Also, CPS is subject to less stringent electric certification requirements for service area and facilities expansion than are public utilities, and is not liable for the annual gross receipts fee payable by public utilities. The San Antonio City Council exercises general original rate regulatory jurisdiction over the CPS service area, including unincorporated areas served by CPS. To date, no appeal of CPS rates has been taken to either of the regulatory entities by residents outside the municipal limits.

RATE INCREASES

The City is obligated under the Trust Indenture and the New Series Bond Ordinance to establish rates and collect charges in an amount sufficient to pay all electric and gas system operation and maintenance expenses, to service all of the outstanding Bonds, and to make all other payments prescribed in the Indenture and New Series Bond Ordinance. Rate changes over the past decade have consisted of increases of 7.4% for gas in September, 1979; 5.4% for electric in October, 1979; 6.0% on the total bill, in June, 1981; a 5.1% combined gas and electric rate increase in May, 1982; a 7.3% combined gas and electric rate increase in January, 1984; a 4.26% combined gas and electric increase in December, 1984; a 2.75% combined gas and electric rate increase effective January 2, 1986; and a 4.2% combined gas and electric rate increase effective January 4, 1988.

In November, 1984, the Board approved revisions to certain miscellaneous service charges effective December 1984. In the summer of 1986, the Board approved revisions to the CPS Electric Line and Gas Main Extension Policies effective August 1, 1986. In the fall of 1987, the Board approved revisions to the CPS Rules And Regulations Applying To Gas And Electric Service, effective January 1, 1988.

ELECTRIC AND GAS RATE SCHEDULES

The principal electric rates effective January 4, 1988, are as follows:

MONTHLY RATE Residential Service

Rate \$3.70 **Service Availability Charge**

Energy Charge

\$0.0627 per KWH for all KWH

Peak Capacity Charge*

\$0.0118 Per KWH for all KWH in excess of 600 KWH

*Peak Capacity Charge is applicable only during the summer billing period (June-September)

Residential All Electric Service

\$3.70 **Service Availability Charge**

Energy Charge

Summer Billing (June-September)

\$0.0627 Per KWH for all KWH

Non-summer Billing (October-May)

\$0.0627 Per KWH for the first 600 KWH

\$0.0517 Per KWH for all KWH in excess of 600 KWH

Peak Capacity Charge*

\$0.0118 Per KWH for all KWH in excess of 600 KWH

*Peak Capacity Charge is applicable only during the summer billing period (June-September)

General Service

<u>Rate</u>	\$3.70	
		<u>Service Availability Charge</u>
		<u>Energy Charge</u>
\$0.0644		Per KWH for the first 1600 KWH*
\$0.0330		Per KWH for all additional KWH
		<u>Peak Capacity Charge</u>
		Summer Billing (June - September)
\$0.0110		Per KWH for all KWH in excess of 600 KWH
		Non-Summer Billing (October - May)
\$0.0068		Per KWH for all KWH in excess of 600 KWH
		* 200 KWH are added for each KW of Billing Demand in excess of 5 KW. Billing demand from October through May may not be less than 80% of highest measured demand from the previous June through September. Billing demand from June through September is the highest measured demand.
		<u>Large Light - w and Power</u>
\$100.00		<u>Service Availability Charge</u>
		<u>Demand Charge</u>
		Summer Billing (June - September)
\$ 6.30		Per KW for all KW of Billing Demand*
		Non-Summer Billing (October - May)
\$ 6.00		Per KW for all KW of Billing Demand*
		<u>Energy Charge</u>
		Summer Billing: (June - September)
\$0.0415		Per KWH for the first 50,000 KWH
\$0.0391		Per KWH for all additional KWH
		Non-Summer Billing: (October - May)
\$0.0387		Per KWH for the first 50,000 KWH
\$0.0373		Per KWH for all additional KWH
		* Billing demand from October through May may not be less than 80% of highest demand from the previous June through September. Billing demand may not be less than 100 KW.
		<u>Extra Large Power</u>
\$700.00		<u>Service Availability Charge</u>
		<u>Demand Charge</u>
		Summer Billing (June - September)
\$6.85		Per KW for all KW of Billing Demand*
		Non-Summer Billing (October - May)
\$6.25		Per KW for all KW of Billing Demand*
		<u>Energy Charge</u>
		Summer Billing: (June - September)
\$0.0391		Per KWH for the first 250 KWH per KW of Billing Demand
\$0.0335		Per KWH for all additional KWH
		Non-Summer Billing: (October - May)
\$0.0360		Per KWH for the first 250 KWH per KW of Billing Demand
\$0.0335		Per KWH for all additional KWH
		* Billing demand from October through May may not be less than 80% of highest demand from the previous June through September. Billing demand may not be less than 1000 KW.

The principal gas rate schedules are:

MONTHLY RATE
General Service

Rate:
\$3.35
\$0.490

Service Availability Charge
Per 100 cubic feet for all cubic feet

Industrial Class A

Rate:
\$24.00
\$0.565
\$0.480

Service Availability Charge
Per 100 cubic feet for the first 200,000 cubic feet
Per 100 cubic feet for all additional cubic feet

Industrial Class B

Rate:
\$23.00
\$0.455
\$0.428

Service Availability Charge
Per 100 cubic feet for the first 600,000 cubic feet
Per 100 cubic feet for all additional cubic feet

* Minimum Bill will be \$300.00 for any customer whose monthly billed consumption equals or exceeds 1,000,000 cubic feet in any month. This amount will be continued for eleven consecutive months.

FUEL AND GAS COST ADJUSTMENT

The foregoing rate schedules contain a fuel cost adjustment clause in the electric rates and a gas cost adjustment clause in the gas rates which allow the recovery of monthly fuel and gas costs that vary above or below the costs which are included in the basic rates. Electric basic rates are subject to an adjustment of plus or minus the amount of change in the price of fuel above or below a basic cost of \$0.02 per KWH sold except that during the summer months of June through September, residential electric usage of 300 KWH or less is exempt from positive fuel adjustment charges and residential usage of 301 KWH to 600 KWH is charged 50% of the standard fuel adjustment. The gas basic rates are subject to an adjustment of plus or minus the amount of change in the price of gas sold above or below a basic cost of \$3.00 per MCF sold.

ELECTRIC CUSTOMER STATISTICS

Fiscal Years Ended January 31:

	1979	1980	1981	1982	1983	1984	1985	1986	1987	1987 ¹
RESIDENTIAL										
Average Monthly KWH/ Customer	735	706	799	773	805	774	801	826	843	846
Average Monthly Bill/ Customer	\$ 32.53	\$ 32.29	\$ 39.60	\$ 42.68	\$ 54.53	\$ 54.00	\$ 60.41	\$ 63.77	\$ 57.71	\$ 55.50
Average Monthly Revenue/KWH	\$.0442	\$.0456	\$.0496	\$.0552	\$.0677	\$.0698	\$.0754	\$.0773	\$.0685	\$0.0656
COMMERCIAL AND INDUSTRIAL										
Average Monthly KWH/ Customer	8,675	8,610	9,092	9,021	8,928	8,494	8,413	8,640	8,598	8,591
Average Monthly Bill/ Customer	\$308.25	\$318.49	\$368.32	\$413.66	\$514.46	\$509.97	\$550.84	\$571.05	\$494.69	\$471.16
Average Monthly Revenue/KWH	\$.0355	\$.0370	\$.0405	\$.0459	\$.0576	\$.0600	\$.0655	\$.0661	\$.0575	\$0.0548
ALL CUSTOMERS										
Average Monthly KWH/ Customer	1,894	1,848	1,908	1,893	1,920	1,825	1,833	1,871	1,903	1,904
Average Monthly Bill/ Customer	\$ 70.98	\$ 72.13	\$ 83.05	\$ 92.62	\$118.58	\$116.72	\$127.16	\$133.39	\$116.69	\$112.23
Average Monthly Revenue/KWH	\$.0375	\$.0390	\$.0435	\$.0489	\$.0617	\$.0640	\$.0699	\$.0701	\$.0613	\$.0589

¹ 12 months ending December 31, 1987.

TYPICAL RESIDENTIAL GAS AND ELECTRIC BILLS OF SIX TEXAS CITIES¹
Usages: 500 Kilowatt hours for Electric, 5,000 Cubic Feet for Gas²

City	Electric Bill	Gas Bill	Total Bill
Austin	\$23.22	\$29.69	\$ 52.91
SAH ANTONIO	33.58	23.90	57.48
Corpus Christi	33.80	28.15	61.95
Houston	37.12	26.92	64.04
Dallas	38.66	28.05	66.71
Fort Worth	38.66	30.35	69.01

¹ Based upon January 1988 rate schedules including Fuel and Gas Cost Adjustments.

² San Antonio's typical residential usage for December 1987 was 666 KWH and 6,500 CF.

**TEN YEAR RECORD OF CITY OF SAN ANTONIO
BENEFITS FROM CITY'S ELECTRIC AND GAS UTILITY SYSTEMS**

Year Ending 1-31:	Payments To City ¹	Increase in City's Equity in System	Total Annual Benefits to City
1978	\$ 36,996,987	\$ 31,491,910	\$ 68,488,897
1979	39,557,154	22,943,464	62,500,618
1980	43,310,425	24,178,218	67,488,643
1981	52,569,716	42,544,744	95,114,460
1982	61,888,193	52,214,626	114,102,819
1983	78,822,089	79,746,561	158,568,650
1984	81,692,529	84,554,135	166,246,664
1985	95,507,732	140,468,334	235,976,066
1986	103,972,266	170,987,961	274,960,247
1987	96,190,619	183,579,699	279,770,317
1987 ²	97,234,267	188,980,487	286,214,754
Totals	<u>\$787,741,977</u>	<u>\$1,021,690,158</u>	<u>\$1,809,432,135</u>

¹ Payments to City include cash payments and refund of charges for furnishing City electricity and gas.

² 12 months ending December 31, 1987.

TAX EXEMPTION

In the opinion of McCall, Parkhurst & Morton, Bond Counsel, under existing statutes, regulations, published rulings and court decisions (a) interest on the Bonds is not includable in the gross income of the owners of the Bonds for federal income tax purposes and (b) none of the Bonds will be a "private activity bond" the interest on which is treated as a specific item of tax preference for purposes of the alternative minimum tax provisions of the Code. Interest on the Bonds will be included, however, in "adjusted net book income" for taxable years beginning in 1987, 1988 and 1989, and in "adjusted current earnings" for taxable years beginning thereafter for purposes of calculating the alternative minimum tax imposed on corporations.

In expressing its opinion, Bond Counsel will rely on the City's no-arbitrage certificate, and will assume compliance by the City with certain covenants contained in the Ordinance relating to the use of the Projects, the use and investment of the proceeds of the Bonds and payments to the federal government of certain amounts earned from the investment of the proceeds of the Bonds. Failure by the City to comply with its representations and covenants may cause the interest on the Bonds to become includable in the gross income of the owners of the Bonds or to become a specific item of tax preference for purposes of the alternative minimum tax retroactively to the date of issuance of the Bonds. Except as stated above, Bond Counsel expresses no opinion as to any other federal income tax consequences of acquiring, carrying, owning or disposing of the Bonds.

Although interest with respect to the Bonds is not includable in gross income, receipt or accrual of such interest may otherwise affect the tax liability of an owner of a Bond. The tax consequence of receipt or accrual of interest with respect to the Bonds will depend upon the tax status of the owner of the Bond and such owner's other items of income or deduction. Prospective purchasers of the Bonds should consult their own tax advisors with respect to the effect that ownership of the Bonds may have on their particular tax situation and other matters not specifically addressed herein.

The law upon which Bond Counsel have based its opinion is subject to change by the Congress and the Department of the Treasury and to subsequent judicial and administrative interpretation. There can be no assurance that such law or the interpretation thereof will not be changed in a manner which would adversely affect the tax treatment of ownership of the Bonds.

REGISTRATION AND QUALIFICATION OF BONDS FOR SALE

The sale of the Bonds has not been registered under the Federal Securities Act of 1933, as amended, in reliance upon the exemption provided thereunder by Section 3 (a)(2); and the Bonds have not been qualified under the Securities Act of Texas in reliance upon various exemptions contained therein; nor have the Bonds been qualified under the securities acts of any jurisdiction. The CPS Board and the City assume no responsibility for qualification of the Bonds under the securities laws of any jurisdiction in which the Bonds may be sold, assigned, pledged, hypothecated, or otherwise transferred. This disclaimer of responsibility for qualification for sale or other disposition of the Bonds shall not be construed as an interpretation of any kind with regard to the availability of any exemption from securities registration provisions.

LEGAL INVESTMENTS AND ELIGIBILITY TO SECURE PUBLIC FUNDS IN TEXAS

The Bonds constitute negotiable instruments, and are investment securities governed by Chapter 8, Texas Uniform Commercial Code, notwithstanding any provisions of law or court decision to the contrary, and are legal and authorized investments for banks, saving banks, trust companies, building and loan associations, savings and loan associations, insurance companies, fiduciaries, and trustees, and for the sinking fund of cities, towns, villages, school districts, and other political subdivisions, or public agencies of the State of Texas. The Bonds also are eligible to secure deposits of any public funds of the state or any political subdivision or public agency of the state, and are lawful and sufficient security for the deposits to the extent of their market value, when accompanied by any unmatured coupons attached to the bonds. No review by the CPS Board or the City has been made of the laws in other states to determine whether the bonds are legal investments for various institutions in those states.

LEGAL OPINIONS AND NO-LITIGATION CERTIFICATE

The City will furnish a complete transcript of proceedings had incident to the issuance and authorization of the Bonds, including the unqualified approving legal opinion of the Attorney General of the State of Texas, to the effect that the Initial Bond (for which the Bonds will be exchanged and substituted) is a valid and legally binding obligation of the City, and based upon examination of such transcript of proceedings, the unqualified legal opinion of Bond Counsel to the effect that the Initial Bond, and all Bonds, duly registered, authenticated, and delivered in accordance with the Ordinance, are valid and legally binding obligations of the City, and to the effect that the interest on the Initial Bond and such Bonds is excludable from gross income for Federal income tax purposes under existing law and that the Bonds are not private activity bonds to the extent described under Tax Exemption. The customary closing papers, including a certificate to the effect that no litigation of any nature has been filed or is then pending to restrain the issuance and delivery of the Initial Bond, or which would affect the provision made for its payment or security, or in any

manner questioning the validity of said Initial Bond will also be furnished. Bond Counsel was not requested to participate, and did not take part, in the preparation of the Notice of Sale and Bidding Instructions, the Official Bid Form and the Official Statement, and such firm has not assumed any responsibility with respect thereto or undertaken independently to verify any of the information contained therein, except that, in its capacity as Bond Counsel, such firm has reviewed the information describing the Initial Bond and the Bonds in the Official Statement to verify that such description conforms to the provisions of the Bond Ordinance. The legal fees to be paid Bond Counsel for services rendered in connection with the issuance of the Initial Bond are contingent on the sale and delivery of the Initial Bond. The legal opinion will be printed on the Bonds.

RATINGS

The following ratings have been assigned to the Bonds: Moody's Investors Service, Inc., "Aa" and Standard & Poor's Corporation "AA". An explanation of the significance of such ratings may be obtained from the company furnishing the rating. The ratings reflect only the respective views of such organizations and the CPS Board and the City make no representation as to the appropriateness of the ratings. There is no assurance that such ratings will continue for any given period of time or that they will not be revised downward or withdrawn entirely by either or both of such rating companies, if in the judgment of either or both companies, circumstances so warrant. Any such downward revision or withdrawal of such ratings or either of them, may have an adverse effect on the market price of the Bonds.

MUNICIPAL BOND INSURANCE

FGIC has agreed to provide municipal bond insurance on the 2016 Term Bond. A statement of their policy is included as a separate enclosure.

OFFICIAL STATEMENT

Preparation: Rotan Mosle Inc. and Southwestern Capital Markets, Inc. are employed as Financial Advisor to the CPS Board on a contract providing for a fee based on a percentage of the face amount of each separate issuance of bonds, such fee to be contingent upon the bonds actually being issued, sold and delivered. Although Rotan Mosle Inc. and Southwestern Capital Markets, Inc. performed an active role in the drafting of the NOTICE OF SALE and BIDDING INSTRUCTIONS and OFFICIAL STATEMENT, they have not independently verified all of the information set forth herein. The information contained in this OFFICIAL STATEMENT has been obtained primarily from CPS and the City records and from other sources which are believed to be reliable, including financial records of CPS and the City and other entities which may be subject to interpretation. No guarantee is made as to the accuracy or completeness of any information obtained from sources other than CPS and the City. No person, therefore, is permitted to rely upon the participation of the Financial Advisors as an implicit or explicit expression of opinion as to said completeness and accuracy. All of the summaries or excerpts of constitutional provisions, statutes, ordinances or other documents do not purport to be complete statements of same and are made subject to all of the provisions thereof. Reference should be made to such original sources in all respects.

Certification as to Official Statement: At the time of payment for and delivery of the Bonds, the CPS Board will furnish the successful bidder a certificate, executed by a proper officer or officers of the CPS Board acting in their official capacities, to the effect that to the best of their knowledge and belief: (a) the descriptions and statements of or pertaining to CPS contained in its OFFICIAL STATEMENT, as supplemented and amended, on the date of such OFFICIAL STATEMENT, on the date of sale of the Bonds and the acceptance of the best bid therefor, and on the date of the delivery of the Bonds, were and are true and correct in all material respects; (b) insofar as CPS and its affairs, including its financial affairs, are concerned, such OFFICIAL STATEMENT, as supplemented and amended, did not and does not contain an untrue statement of a material fact or omit to state a material fact required to be stated therein or necessary to make the statements therein, in the light of the circumstances under which they were made, not misleading; (c) insofar as the descriptions and statements, including financial data contained in such OFFICIAL STATEMENT, as supplemented and amended, of or pertaining to entities other than CPS and their activities are concerned, such statements and data have been obtained from sources which the CPS Board believes to be reliable and that the CPS Board has no reason to believe that they are untrue in any material respect; and (d) that there has been no adverse change in the financial condition of CPS since the date of the last audited financial statements of CIS.

This OFFICIAL STATEMENT has been duly approved by the City Council of the City of San Antonio, Texas, and by the CPS Board, and adopted for use in solicitation of bids on the Bonds.

CITY OF SAN ANTONIO, TEXAS

Henry Cisneros

Henry G. Cisneros
Mayor, City of San Antonio, and
Ex Officio Member, Board of Trustees

CITY PUBLIC SERVICE BOARD OF SAN ANTONIO

Lila Cockrell

Lila Cockrell
Chair, Board of Trustees

(THIS PAGE LEFT BLANK INTENTIONALLY)

APPENDIX A

CITY OF SAN ANTONIO, TEXAS - GENERAL INFORMATION

This Appendix contains a brief discussion of certain economic and demographic characteristics of the area in which the City is located. Certain information in this Appendix was obtained from sources identified with respect to the information given and is believed to be reliable, although no investigation has been made to verify the accuracy of such information.

DEMOGRAPHIC AND ECONOMIC DATA

Location and Population

The City of San Antonio is located in south central Texas approximately 75 miles south of the state capital in Austin, 140 miles northwest from the Gulf of Mexico, and 150 miles northeast from the Mexican border cities of Del Rio, Eagle Pass and Laredo. The land area of the City covers 328 square miles.

The City was founded in the early eighteenth century and was incorporated by the Republic of Texas in 1837, and is the County seat of Bexar County. The City of San Antonio Planning Department cites the City's 1980 population to be 921,693 making it the third largest city in Texas and, according to the Bureau of Census Statistics, the ninth largest in the United States.

The following table provides, at the dates shown, the population of the City, Bexar County, and the San Antonio SMSA, which includes Bexar, Comal and Guadalupe Counties.

Year	City of San Antonio	Bexar County	San Antonio SMSA
1920 ¹	161,399	202,096	238,639
1930 ¹	231,542	292,533	333,442
1940 ¹	253,854	338,176	376,093
1950 ¹	408,442	500,460	542,209
1960 ¹	587,718	687,151	736,066
1970 ¹	654,153	830,460	888,179
1980 ¹	786,023	988,800	1,071,954
1982 ²	819,021	1,047,668	1,130,100
1983 ²	821,181	1,047,668	1,130,100
1984 ²	849,500	1,111,900	1,207,700
1985 ²	897,500	1,138,600	1,223,600
1986 ²	921,693	1,166,509	1,268,809
1987 ³	936,000	1,186,000	1,292,400

¹ Source: U.S. Census of Population, 1920-1980 as of April 1 of the year shown.

² Source: City of San Antonio -- Planning Department as of December 31 of the year shown.

³ Source: City of San Antonio -- Planning Department as of October 31 of the year shown.

Economic Factors

The City of San Antonio, the County seat of Bexar County, and as indicated in the foregoing section, is included in the three-county San Antonio Standard Metropolitan Statistical Area. San Antonio has a diversified economic base which is composed of agribusiness, manufacturing, construction, tourism, the South Texas Medical Center complex, and is the site of the largest concentration of military installations in the United States. The City's proximity to Mexico provides favorable conditions for international business relations with Mexico in the areas of agriculture, tourism, manufacturing, wholesale and retail markets for citizens of Mexico. Industry ranges from the manufacturing of apparel, food products, aircraft, electronics and pharmaceuticals to iron and steel products and oil well equipment. San Antonio is also a major insurance center in the southwest, serving as the headquarters for several insurance companies, including United Services Automobile Association, the nation's 6th largest private automobile insurer and the 10th largest homeowners insurer. Educational facilities in the City include ten colleges and universities with a combined total enrollment of 54,030 for the fall semester 1987.

Military Installations

The military presence in Bexar County is a principal component of the area economy. As of October 1, 1986, approximately 43,339 active duty military personnel and 34,163 active duty civilian personnel were located in the County, according to the Greater San Antonio Chamber of Commerce, having a combined active military/civilian annual payroll of \$1,402,129,721. The major installations located in the County include Fort Sam Houston, the U.S. Army Health Services Command, Randolph Air Force Base, Brooks Air Force Base, the San Antonio Air Logistics Center, and the Air Force Military Training Center at Lackland Air Force Base.

Agricultural Receipts

The following table shows the total amount of receipts received from crops and livestock in Bexar County for the years indicated:

Year	Crops	Livestock	Total
1976	\$ 9,828,000	\$23,271,000	\$33,099,000
1977	12,232,000	22,841,000	35,073,000
1978	12,276,000	28,639,000	40,915,000
1979	17,179,000	33,968,000	51,147,000
1980	16,620,000	24,136,000	40,756,000
1981	21,971,000	26,843,000	48,814,000
1982	19,408,000	30,353,000	49,761,000
1983	30,021,000	34,801,000	64,822,000
1984	27,223,000	34,843,000	62,066,000
1985	31,075,000	28,164,000	59,239,000

Source: Texas Crop and Livestock Reporting Service.

Construction Activity

Set forth below is a table showing building permits issued for construction within the City at December 31 for the years indicated.

Year	Residential Single Family		Residential Multi-Family[1]		Other[2]	
	Permits	Valuation	Permits	Valuation	Permits	Valuation
1975	1,492	\$31,529,001	184	\$11,757,998	12,015	\$115,508,444
1976	2,025	48,568,523	149	10,298,267	10,980	104,997,735
1977	2,935	71,971,872	194	17,937,023	11,110	123,742,635
1978	2,550	68,551,313	320	31,751,780	11,405	138,132,132
1979	2,265	68,976,660	529	70,665,934	10,059	220,036,943
1980	2,376	114,756,432	535	77,102,937	13,210	252,110,675
1981	2,145	78,478,521	470	65,124,807	13,100	398,908,483
1982	2,315	84,439,470	1,012	157,979,723	12,001	319,917,718
1983	3,197	124,386,595	961	140,556,050	13,905	301,295,089
1984	3,128	117,820,951	1,018	164,277,022	15,237	580,154,298
1985	2,933	105,492,933	528	62,837,623	10,520	479,555,475
1986	1,886	81,020,617	344	36,325,227	10,023	537,422,729
1987	1,472	65,122,904	43	27,618,978	8,984	452,264,504

[1] Includes two family duplex projects.

[2] Includes commercial building permits, commercial additions, improvements and extensions, and certain residential improvements.

Source: Department of Housing and Inspections, City of San Antonio.

Convention Statistics

The City's climate and recreational facilities make San Antonio a favorable convention site in the southwest. The following convention statistics were compiled by the San Antonio Convention and Visitors Bureau:

Calendar Year	Conventions	Number of Room Nights	Estimated Dollar Value
1975	415	323,440	\$29,247,850
1976	465	308,396	27,783,600
1977	434	287,910	29,613,980
1978	488	329,816	34,129,800
1979	689	378,387	36,215,420
1980	733	432,702	41,413,908
1981	671	512,479	49,049,365
1982	721	531,142	55,913,000
1983	832	595,377	68,951,000
1984	791	614,802	73,500,000
1985	899	599,645	71,700,000
1986	954	578,392	125,400,000
1987	858	534,650	115,900,000

Medical and Research Facilities

The City continues to play a significant role in expanding medical service, research and development. Compilation of the most recent statistics at January 1, 1987, showed that in addition to the 25 hospitals serving the City, the South Texas Medical Center employed an estimated 16,000 people, and included a total of 30 major facilities plus support facilities valued at approximately \$557,332,900 and had an annual budget of \$577,871,105. At January 1, 1987, construction in progress was valued at approximately \$108,902,000 and planned new construction was estimated at \$173,960,000 for a total in excess of \$282,862,000. The Southwest Research Center is one of the largest and most respected organizations of its type. With a staff of over 2,253 and an annual budget over \$104 million, Southwest Research Center specializes in Biological Growth and Development, Reproductive Physiology, Microbiology and Infectious Diseases, Environmental Health Science, Engineering, and Applied Research.

Business Establishments With 500 or More Employees

Manufacturing

<u>Firm</u>	<u>Product/Service</u>
Advanced Micro Devices	Production of electronic components
Coca-Cola Bottling Company of San Antonio	Soft drink manufacturer
Datapoint Corporation	Computers and peripherals
Dee Howard Co.	Jet modification
Fairchild Aircraft Corporation	Aircraft manufacturer
Finesilver Manufacturing Co.	Men's, youths', and boys' clothing
Friedrich A/C and Refrigeration Co.	Air conditioning units and products
Levis Strauss & Company	Women's wear and youthwear
Miller Curtain Company	Curtains and Drapes
Motorola, Inc.	Truss Components
Pearl Brewing Company	Malt beverages
Redland Worth Corporation	Rock manufacturing
Roegelein Company	Meat processing
San Antonio Express-News Corporation	Newspaper
San Antonio Light	Newspaper
Structural Metals Inc.	Reinforcement steel bars
Tesoro Petroleum Corporation	Petroleum products
Turbine Support Division	Jet engine repair
Valero Energy Corporation	Petroleum products
West Point Pepperrell	Linens and fabrics

Wholesale

<u>Firm</u>	<u>Product/Service</u>
Fleming Co., Inc.	Groceries
Holly Farms Poultry	Poultry products

Retail

<u>Firm</u>	<u>Product/Service</u>
Albertson's Food & Drug	Supermarket
H.E. Butt Grocery Company	Supermarket
Cafeterias, Inc. (Luby's)	Cafeteria
Diamond Shamrock	Refining gasoline outlet and marketing
Dillard's Department Stores	Department store
Fox-Stanley Photo Products, Inc.	Photo processing and photographic equipment
Frontier Enterprises	Restaurant
Frost Bros., Inc.	Specialty store
Handy Andy, Inc.	Supermarket
Handy Dan Improvement Centers	Building materials
Joske's of Texas	Department store
Karcher, Carl Enterprises	Restaurant
Mervyn's	Department store
Miller, Bill, Bar-B-Que	Fast food chain
Montgomery Ward & Company	Retail merchandise
J.C. Penney & Company	Department store
Sears, Roebuck & Company	Department store

Seven-Eleven Corporation	Convenience store
Stop-n-Go Markets	Convenience store
Wendy's International	Fast food chain
Winn's Stores Inc.	Variety store

Transportation, Communication and Utilities

<u>Firm</u>	<u>Product/Service</u>
CITY Public Service Board	Municipal gas and electric utility
CITY Water Board	Water utility
Missouri Pacific Railroad	Shipments
Rogers Cablesystems of Texas, Inc.	Cablevision
Southern Pacific Transportation Company	Transportation
Southwestern Bell Telephone Company	Telephone utility
VIA Metropolitan Transit	Public transportation

Services

<u>Firm</u>	<u>Product/Service</u>
Alamo Community College District	Educational institution
ARA Living Centers	Nursing homes
Baptist Memorial Hospital System	Hospital
Bexar County Hospital District	Hospitals (Robert B. Green and Medical Center)
East Central Independent School District	Public school district
Edgewood Independent School District	Public school district
Harlandale Independent School District	Public school district
Judson Independent School District	Public school district
Humana Hospital-Metropolitan	Hospital
Humana Hospital San Antonio	Hospital
Hyatt Regency San Antonio	Hotel
Kelly Services, Inc.	Temporary help services
La Quinta Motor Inns, Inc.	Motor inn
Murphy, Audie L., Memorial V.A. Hospital	Federal hospital
North East Independent School District	Public school district
Northside Independent School District	Public school district
River Hotel Co. (Marriott Hotel)	Hotel
San Antonio Independent School District	Public school district
San Antonio State Hospital	Hospital
Santa Rosa Medical Center	Hospital
South San Antonio Independent School District	Public school district
Southwest Independent School District	Public school district
Southwest Research Institute	Nonprofit research institute
Southwest Texas Methodist Hospital	Hospital
Stanley Smith Securities, Inc.	Security service
Trinity University	Educational institution
University of Texas at San Antonio	Educational institution
University of Texas Health Science Center at San Antonio	Teaching and health care institution

Finance, Insurance and Real Estate

<u>Firm</u>	<u>Product/Service</u>
Ellison, Ray, Industries	Developer
Frost National Bank	Banking
Gill Companies	Installment finance
National Bank of Commerce	Banking
San Antonio Savings Association	Banking
United Services Automobile Association	Insurance

Contract Construction

<u>Firm</u>	<u>Product/Service</u>
H.B. Zachry Company	General contractor

Source: Largest Employers Directory, Economic Development Department of the Greater San Antonio Chamber of Commerce, July, 1985.

Employment Statistics

City of San Antonio Labor Force Statistics

	November 1986	November 1987
Total Employed	<u>384,639</u>	<u>423,195</u>
Unemployed	<u>35,959</u>	<u>38,934</u>
Total Labor Force	<u>420,598</u>	<u>462,129</u>
Percent of Unemployment	<u>8.5%</u>	<u>8.4%</u>

San Antonio SMSA¹ Average Annual Labor Force Statistics

	November 1986	November 1987
Total Employed	<u>522,300</u>	<u>579,800</u>
Unemployed	<u>45,000</u>	<u>48,900</u>
Total Labor Force	<u>567,300</u>	<u>628,700</u>
Percent of Unemployment	<u>7.9%</u>	<u>7.8%</u>
Nonagricultural Employment:		
Manufacturing	47,200	46,700
Mining	2,600	2,500
Construction	31,800	31,100
Transportation, Communication and Utilities	17,900	18,000
Retail and Wholesale Trade	127,200	132,500
Finance, Insurance and Real Estate	37,300	39,200
Service	110,300	118,700
Government	110,100	111,200
Total ²	<u>484,600</u>	<u>499,900</u>

¹ Includes Bexar, Comal, and Guadalupe Counties.

² Total job count.

Source: Texas Employment Commission.

Bank Deposits

Deposits in commercial San Antonio banks at December 31 for the past ten years are shown below.

<u>Year</u>	<u>Total Number of Banks</u>	<u>Total Deposits (000's)</u>
1977	42	3,190,248
1978	44	3,435,396
1979	44	3,812,173
1980	46	4,271,610
1981	45	4,391,160
1982	47	5,719,169
1983	59	6,545,426
1984	71	7,621,638
1985	75	8,267,343
1986	82	9,187,996
1987*	68	8,395,801

* As of September 30, 1987.

**MUNICIPAL GOVERNMENT, INDEBTEDNESS
AND RELATED INFORMATION**

CITY GOVERNMENT

The City has a Council-Manager form of government in which the Mayor and ten council members serve as the legislative body. These eleven officials are elected for two year terms. The present term of office for all elected officials expires in April, 1987. The City Manager is appointed by the City Council and serves as the chief administrative officer of the City.

**SUMMARY FINANCIAL STATEMENT RELATING TO CITY
GENERAL OBLIGATION BONDS**

1987 Assessed Valuation (100% of Actual)*	\$23,783,375,122
Less: Exemptions	1,581,122,205
1987 Net Assessed Valuation*	<u>\$22,202,252,917</u>
General Obligation Bond Debt (At 10-01-87)	420,244,819
Less: Applicable Interest & Sinking Fund	36,804,325
Net General Obligation Debt (At 10-01-87)	<u>\$ 383,440,494</u>

Source: City Controller.
At October 1, 1987

PRINCIPAL TAXPAYERS

The ten largest City of San Antonio taxpayers as of December 16, 1987 as listed on the City's tax rolls are shown below:

	<u>Assessed Value</u>
1. Southwestern Bell Telephone Company	\$390,502,590
2. United Services Automobile Association	262,740,550
3. Henry E. Butt and Company	149,602,950
4. Humana Hospital Corporation, Inc.	94,968,240
5. Ray Ellison Industries	86,660,426
6. H. B. Zachry	84,523,960
7. Melvin Simon & Associates, Inc.	81,973,100
8. North Star Mall	78,337,360
9. Quincy Lee/Joint Venture	77,042,435
10. National Bank of Commerce	68,508,700

* Assessed Valuation at 100% of Market Value.

CITY REVENUE BOND INDEBTEDNESS

Information concerning the City of San Antonio revenue bond and note indebtedness payable from electric and gas, water, sewer, and airport systems operations is shown below.

	<u>Total Outstanding</u>	<u>Fund Balances¹</u>
Electric and Gas Systems Revenue Bonds ²	\$2,266,940,000	\$198,715,195
Water Revenue Bonds and Notes ³	191,375,000	18,960,601
Sewer Revenue Bonds ³	351,825,000	19,105,957
Airport Revenue Bonds ³	97,795,000	11,043,179

¹ Includes all required interest and sinking, and reserve fund balances of each system.

² At December 31, 1987

³ At October 1, 1987

Summary statements of operations of the City's Water, Sewer and Airport Systems for the past two years, showing historical coverage of actual revenue bond and note debt service requirements are as follows:

City of San Antonio Waterworks System

	<u>Fiscal Years Ended 12-31:</u>	
	<u>1985</u>	<u>1986</u>
Gross Revenues	\$51,032,325	\$73,013,370
Current Expenses	25,622,275	26,915,510
<u>Net Revenues</u>	<u>\$25,410,050</u>	<u>\$46,097,860</u>
Actual Principal and Interest Requirements	\$15,160,349	\$14,183,113
COVERAGE	1.68x	3.25x
Maximum Principal and Interest Requirements (1987).....\$18,028,658	
COVERAGE	1.41x	2.56x

City of San Antonio Sewer System

	<u>Fiscal Years Ended 9-30:</u>	
	<u>1986</u>	<u>1987</u>
Gross Revenues	\$74,912,609*	\$76,532,396
Current Expenses	38,096,256*	30,221,775
<u>Net Revenues</u>	<u>\$36,816,353</u>	<u>\$46,310,621</u>
Actual Principal and Interest Requirements	\$23,445,057**	\$26,078,668
COVERAGE	1.57x	1.77x
Maximum Principal and Interest Requirements (1993).....\$33,618,768	
COVERAGE	1.10x	1.37x

* Includes \$8,957,943 for loss on refunding advance debt.
 ** Excludes \$48,100,000 for sewer refunding bonds.

City of San Antonio Airport System

	<u>Fiscal Years Ended 9-30:</u>	
	<u>1986</u>	<u>1987</u>
Gross Revenues	\$27,027,354*	\$26,798,922
Current Expenses	10,127,493	10,890,950
<u>Net Revenues</u>	<u>\$16,899,861</u>	<u>\$15,907,972</u>
Actual Principal and Interest Requirements	\$10,223,015	\$10,204,453
COVERAGE	1.65x	1.56x
Maximum Principal and Interest Requirements (2006).....\$10,493,113	
COVERAGE	1.61x	1.52x

* Includes \$2,036,643 for recovery of prior year cost of refunding bonds.

COMPARATIVE ANNUAL STATISTICAL DATA

Growth Indices

<u>Calendar Years</u>	<u>Main Telephones</u>	<u>Electric Customers</u>	<u>Gas Customers</u>	<u>Water Customers¹</u>
1969	243,766	232,952	199,749	146,089
1970	256,287	239,519	204,327	148,452
1971	270,337	248,739	210,632	151,200
1972	288,690	260,632	219,127	154,513
1973	301,016	267,443	224,084	159,012
1974	311,925	269,500	227,923	161,100
1975	322,607	272,586	230,042	162,627
1976	337,343	279,587	234,337	164,454
1977	353,663	290,904	240,566	167,633
1978	376,949	307,705	249,391	172,185
1979	398,860	321,130	255,042	178,707
1980	420,299	338,727	263,012	183,084
1981	442,250	353,998	264,451	188,969
1982	454,727	369,631	271,393	201,370
1983	472,053	383,615	273,922	207,908
1984	500,853	411,813	278,898	214,595
1985	525,445	433,064	281,575	222,672
1986	541,800	453,146	284,489	227,598
1987	541,815	459,685	284,478	227,946

¹ City Water Board only.

Business Indices

<u>Calendar Year</u>	<u>Bank Clearings</u>	<u>Building Permits</u>	<u>Postal Receipts</u>
1969	\$10,884,022,753	\$ 85,904,537	N/A
1970	10,014,836,330	103,210,207	N/A
1971	11,547,764,451	131,182,026	17,695,000
1972	13,312,759,105	223,749,000	18,681,000
1973	16,304,437,765	226,710,152	22,702,000
1974	17,475,520,274	183,520,814	23,914,000
1975	18,249,836,385	158,795,443	26,407,000
1976	20,323,429,838	163,864,525	29,818,000
1977	22,537,211,921	213,651,530	38,062,000
1978	25,745,461,776	238,435,225	43,000,000
1979	29,443,679,652	359,679,537	50,187,000
1980	33,863,636,207	443,970,044	54,906,088
1981	35,027,132,517	499,420,910	63,167,802
1982	40,291,709,241	607,140,132	79,465,772
1983	42,355,874,732	566,237,734	90,417,238
1984	46,955,097,401	862,261,221	101,815,579
1985	46,113,193,838	647,886,931	113,883,976
1986	45,096,118,659	654,768,573	125,694,443
1987	43,571,644,019	521,332,564	121,627,504

¹ On fiscal year basis, ending September 30.

Municipal Sales Tax Collections

The following statistics show a comparative record of municipal sales tax collections for the ten largest Texas cities based upon the 1980 Census.

	Sales Taxes - Net				
	1983	1984	1985	1986	1987
Arlington	\$11,471,417	\$14,452,554	\$17,141,794	\$17,055,624	\$17,153,924
Amarillo	10,508,862	11,234,589	11,730,239	11,996,168	11,440,833
Lubbock	11,561,552	12,450,682	13,283,933	12,959,730	12,602,790
Corpus Christi	15,146,788	15,977,496	17,081,745	16,161,843	15,381,555
El Paso	15,944,125	18,295,666	21,059,510	22,545,811	22,600,731
Austin	28,625,014	37,271,562	44,014,004	41,797,456	38,120,152
Fort Worth	26,571,867	30,579,368	34,154,412	34,602,039	32,193,724
SAN ANTONIO	42,591,152	49,467,890	56,242,528	56,504,214	54,043,662
Dallas	85,655,818	99,227,785	112,475,312	106,444,284	99,681,108
Houston	138,142,189	144,953,635	150,395,557	141,375,017	134,762,363

(THIS PAGE LEFT BLANK INTENTIONALLY)

APPENDIX B
CITY PUBLIC SERVICE
FINANCIAL STATEMENTS FOR THE YEARS
ENDED JANUARY 31, 1987 and 1986
AND AUDITORS' REPORT



A MEMBER OF ARTHUR YOUNG INTERNATIONAL

Arthur Young

601 N.W. Loop 410, Suite 500
San Antonio, Texas 78216
Telephone: (512) 340-1000

REPORT OF CERTIFIED PUBLIC ACCOUNTANTS

The Board of Trustees
City Public Service

We have examined the balance sheets of City Public Service at January 31, 1987 and 1986, and the related statements of earnings and application of earnings, changes in equity and changes in financial position for the years then ended. Our examinations were made in accordance with generally accepted auditing standards and, accordingly, included such tests of the accounting records and such other auditing procedures as we considered necessary in the circumstances.

In our opinion, the statements mentioned above present fairly the financial position of City Public Service at January 31, 1987 and 1986, and the results of operations and changes in financial position for the years then ended, in conformity with generally accepted accounting principles applied on a consistent basis during the period.

Arthur Young & Company

March 2, 1987

CITY PUBLIC SERVICE

BALANCE SHEETS, JANUARY 31, 1987 and 1986

<u>ASSETS</u>	<u>NOTES</u>	<u>1987</u>	<u>1986</u>
		(in thousands)	
UTILITY PLANT - At cost:			
Electric	1	\$1,221,198	\$1,168,943
Gas		196,620	184,559
General		60,956	28,390
Construction work in progress	7	1,675,726	1,361,134
Nuclear fuel in process	7	100,979	95,821
Total utility plant		<u>3,255,479</u>	<u>2,838,847</u>
Less accumulated depreciation		<u>446,913</u>	<u>418,743</u>
Utility plant - net		<u>2,808,566</u>	<u>2,420,104</u>
RESTRICTED CASH (Temporary cash investments and U. S. Government obligations - at cost which approximates market):			
Bond Construction Fund	2	41,335	65,678
Bond Reserve - Old Series Bonds	3	17,353	17,437
Bond Reserve - New Series Bonds	3	173,786	147,715
Improvements and Contingencies Fund		131,439	73,586
Other	1	5,150	8,123
Total restricted cash		<u>369,063</u>	<u>312,539</u>
CURRENT ASSETS:			
Cash, including temporary cash investments		19,045	22,362
Short-term investments	4	-	51,724
Customer accounts receivable, less allowance for doubtful accounts of \$1,222,000 in 1987 and \$1,151,000 in 1986		54,947	51,233
Other receivables	8	42,352	35,337
Inventories and supplies - at average cost:			
Materials and supplies		20,642	18,647
Fuel stock		42,089	33,644
Prepayments and other	8	1,859	27,964
Total current assets		<u>180,934</u>	<u>238,911</u>
LITIGATION SETTLEMENTS BENEFITS RECEIVABLE	7,8	205,500	165,000
DEFERRED DEBITS	1	<u>74,955</u>	<u>17,310</u>
TOTAL		<u>\$3,639,018</u>	<u>\$3,153,864</u>

<u>LIABILITIES</u>	<u>NOTES</u>	<u>1987</u>	<u>1986</u>
		<u>(in thousands)</u>	
LONG-TERM DEBT - Revenue Improvement Bonds:	2,3		
Old Series		\$ 105,785	\$ 115,220
New Series		1,903,425	1,676,500
Less: Unamortized discount on New Series Bonds		(20,812)	(11,530)
Net long-term debt		<u>1,988,398</u>	<u>1,780,190</u>
EQUITY:			
Appropriated retained earnings:	?		
Bond Reserve - Old Series Bonds		17,353	17,437
Bond Reserve - New Series Bonds		121,328	101,216
Improvements and Contingencies Fund		<u>131,439</u>	<u>73,586</u>
Total		270,120	192,239
Reinvested earnings		<u>1,025,885</u>	<u>920,187</u>
Total equity		<u>1,296,005</u>	<u>1,112,426</u>
CURRENT LIABILITIES:			
Current maturities of long-term debt	3	34,820	32,350
Short-term debt	4	100,000	100,000
Accounts payable and accrued liabilities		61,610	55,492
Litigation settlement benefits payable to customers	8	834	-
Customer service deposits		<u>14,079</u>	<u>10,984</u>
Total current liabilities		<u>211,343</u>	<u>198,826</u>
DEFERRED CREDITS:			
Customer advances for construction		14,751	12,976
Other		<u>1,985</u>	<u>6,340</u>
Total deferred credits		<u>16,716</u>	<u>19,316</u>
LITIGATION SETTLEMENT BENEFITS PAYABLE	8	79,666	-
CONTRIBUTIONS IN AID OF CONSTRUCTION	1	46,890	33,106
COMMITMENTS AND CONTINGENCIES	5,7,8	<u>-</u>	<u>-</u>
TOTAL		<u>\$3,639,018</u>	<u>\$3,153,864</u>

See notes to financial statements.

CITY PUBLIC SERVICE

STATEMENTS OF EARNINGS AND APPLICATION OF EARNINGS
FOR THE YEARS ENDED JANUARY 31, 1987 and 1986

	<u>NOTES</u>	<u>1987</u>	<u>1986</u>
		(in thousands)	
REVENUE:	1		
Electric		\$639,626	\$700,371
Gas		127,814	136,500
Interest and other income		36,778	31,962
Gross revenue		<u>804,218</u>	<u>868,833</u>
EXPENSES:	1		
Fuel, purchased power and resale gas		316,251	397,414
Other operating and general		68,998	65,035
Maintenance		32,761	33,379
Depreciation		41,811	40,351
Interest and debt expense		166,029	144,989
Allowance for interest used during construction		(101,402)	(87,296)
Payments to the City of San Antonio	6	<u>96,191</u>	<u>103,972</u>
Total expenses		<u>520,639</u>	<u>697,844</u>
NET EARNINGS		183,579	170,989
ADD:			
Depreciation		41,811	40,351
Interest requirements on New Series Bonds (payable from Improvements and Contingencies Fund)		<u>153,411</u>	<u>135,235</u>
AVAILABLE FOR APPLICATION		<u>\$378,801</u>	<u>\$346,575</u>
APPLICATION:			
To pay long-term debt requirements -			
Old Series Bonds:			
Principal payments		\$ 9,000	\$ 8,600
Bond reserve		(84)	(46)
To reinvested earnings - Net gain on sale of assets		5	4
To Improvements and Contingencies Fund:			
Minimum requirement (12-1/2% of gross revenue)	2	100,527	108,604
Balance of available revenue		<u>269,353</u>	<u>229,413</u>
APPLICATION		<u>\$378,801</u>	<u>\$346,575</u>

See notes to financial statements.

CITY PUBLIC SERVICE

STATEMENTS OF CHANGES IN EQUITY
FOR THE YEARS ENDED JANUARY 31, 1987 and 1986

	1987	1986
	(in thousands)	
BOND RESERVE - OLD SERIES BONDS:		
Balance, beginning of year	\$ 17,437	\$ 17,483
Deductions - transfer of earnings	(84)	(46)
Balance, end of year	<u>\$ 17,353</u>	<u>\$ 17,437</u>
BOND RESERVE - NEW SERIES BONDS:		
Balance, beginning of year	\$ 101,216	\$ 89,713
Additions - from Improvements and Contingencies Fund	20,112	11,503
Balance, end of year	<u>\$ 121,328</u>	<u>\$101,216</u>
IMPROVEMENTS AND CONTINGENCIES FUND:		
Balance, beginning of year	\$ 73,586	\$ 80,068
Additions - from application of earnings:		
Minimum requirement (12-1/2% of gross revenue)	100,527	108,604
Balance of available revenue	269,353	229,413
Total	<u>443,466</u>	<u>418,085</u>
Deductions:		
New Series Bonds:		
Additions to reserve	20,112	11,503
Payment of bond interest	153,411	135,235
Payment of bond principal	23,350	21,440
Construction expenditures	115,154	173,821
For working capital	-	2,500
Total	<u>312,027</u>	<u>344,499</u>
Balance, end of year	<u>\$ 131,439</u>	<u>\$ 73,586</u>
REINVESTED EARNINGS:		
Balance, beginning of year	\$ 920,187	\$754,173
Additions:		
From Improvements and Contingencies Fund:		
For construction	115,154	173,821
For New Series Bonds principal payments	23,350	21,440
For working capital	-	2,500
From application of earnings:		
Old Series Bonds principal payments	9,000	8,600
Net gain on sale of assets	5	4
Total	<u>147,509</u>	<u>206,365</u>
Deduction - Depreciation	<u>41,811</u>	<u>40,351</u>
Balance, end of year	<u>\$1,025,885</u>	<u>\$920,187</u>

See notes to financial statements.

CITY PUBLIC SERVICE

STATEMENTS OF CHANGES IN FINANCIAL POSITION
FOR THE YEARS ENDED JANUARY 31, 1987 and 1986

	1987	1986
	(in thousands)	
SOURCES OF FUNDS:		
Net earnings	\$ 183,579	\$170,989
Add (deduct) amounts not affecting working capital:		
Amortization of New Series Bond discount	1,081	536
Amortization of deferred debits	4,140	1,461
Depreciation	41,811	40,351
Allowance for interest used during construction	(101,402)	(87,296)
Working capital provided from operations	<u>129,209</u>	<u>126,041</u>
Contributions in aid and customer advances for construction	7,018	7,735
Sale of revenue improvement bonds	181,772	270,202
Sale of refunding bonds	310,242	113,301
Litigation settlement	111,500	210,000
Other	-	1,281
Total	<u>739,741</u>	<u>728,560</u>
APPLICATION OF FUNDS:		
Acquisition of utility plant - net of allowance for interest used during construction	329,208	347,764
Increase in other receivable	40,500	165,000
Retirement of bonds	32,350	30,040
Defeasance of bonds refunded	253, 50	97,130
Increase in current maturities of long-term debt	2,470	2,310
Increase in restricted cash	56,524	59,821
Litigation settlement received	31,000	-
Excess of reacquisition amount over principal of bonds refunded in advance	57,649	15,978
Other	<u>7,184</u>	<u>498</u>
Total	<u>810,235</u>	<u>718,541</u>
INCREASE (DECREASE) IN WORKING CAPITAL	<u>\$ (70,494)</u>	<u>\$ 10,019</u>

CITY PUBLIC SERVICE

STATEMENTS OF CHANGES IN FINANCIAL POSITION
FOR THE YEARS ENDED JANUARY 31, 1987 and 1986

	1987	1986
	(in thousands)	
CHANGES IN WORKING CAPITAL COMPONENTS:		
Increase (decrease) in current assets:		
Cash and temporary investments	\$ (3,317)	\$ (7,569)
Short-term investments	(51,724)	(21,874)
Customer accounts receivable	3,714	(4,405)
Other receivables	9,015	28,458
Inventories and supplies	10,441	679
Prepayments and other	(26,106)	222
Decrease (increase) in current liabilities:		
Current maturities of long-term debt	(2,470)	(2,310)
Accounts payable and accrued liabilities	(6,118)	10,894
Litigation settlement benefits payable to customers	(834)	7,660
Customer service deposits	<u>(3,095)</u>	<u>(1,736)</u>
INCREASE (DECREASE) IN WORKING CAPITAL	(70,494)	10,019
WORKING CAPITAL, BEGINNING OF YEAR	<u>40,085</u>	<u>30,066</u>
WORKING CAPITAL (DEFICIT), END OF YEAR	<u><u>\$ (30,409)</u></u>	<u><u>\$ 40,085</u></u>

See notes to financial statements.

CITY PUBLIC SERVICE

NOTES TO FINANCIAL STATEMENTS JANUARY 31, 1987 and 1986

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Basis of Accounting - City Public Service ("CPS") uses the accrual method of accounting based upon the Uniform System of Accounts for Gas and Electric Utilities issued by the National Association of Regulatory Utility Commissioners.

Fiscal Year - The fiscal year ended January 31, 1987 is referred to herein as 1987 and the year ended January 31, 1986 as 1986.

Revenues and Expenses - Revenue is recognized as billed on a cycle basis. Rate schedules include fuel and gas cost adjustment clauses that permit recovery of fuel and gas costs in the month incurred. CPS charges to expense the cost of electric production fuel as it is consumed and the cost of resale gas at the time of purchase.

Utility Plant - These assets are stated at the cost of construction, including costs of contracted services, direct material and labor, indirect costs, including general engineering, labor and material overhead, and an allowance for interest used during construction ("AIUDC"). CPS computes AIUDC using rates representing the cost of borrowed funds on projects estimated to cost in excess of one million dollars and expected to require more than one year to complete. Retirements of utility plant, together with removal cost less salvage, are charged to accumulated depreciation. The maintenance of property, and replacement and renewals of items determined to be less than a unit of property, are charged to maintenance expense. General utility plant assets consist of land, buildings and equipment for general and administrative purposes that are used commonly in electric and gas operations.

CPS computes depreciation principally using the straight-line method over the estimated service lives of the assets as determined by periodic engineering studies. Depreciation as a percentage of average depreciable plant was 3.07% in 1987 and 3.16% in 1986.

Contributions in aid of construction are amortized over a period equal to the lives of the related assets.

Other Restricted Cash - These amounts consist primarily of funds being held in escrow as required under a contract with a gas supplier.

CITY PUBLIC SERVICE

NOTES TO FINANCIAL STATEMENTS JANUARY 31, 1987 and 1986

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Deferred Debits - These amounts consist of the unamortized balance of bond issue expense, and the unamortized excess of the reacquisition amount over the revenue bond principal refunded in advance. Amounts are being amortized over the period during which the bonds will be outstanding.

2. REVENUE BOND INDENTURE REQUIREMENTS

The Trust Indenture executed by the City of San Antonio (the "City") in conjunction with the issuance of the revenue bonds dated February 1, 1951 through August 1, 1974, "Old Series Bonds," contains, among others, the following provisions:

- 1) All of the assets of the gas and electric systems, together with the net revenues of the systems, as defined, are pledged with the Harris Trust and Savings Bank of Chicago, Illinois, as Corporate Trustee, to secure the payment of the "Old Series Bonds."
- 2) Gross revenues of the gas and electric system shall be applied to: (a) expenses of operating and maintaining the systems; (b) debt service and reserve requirements on the "Old Series Bonds"; (c) payment of an "in lieu of tax" amount to the City; (d) an amount equal to 12-1/2% of gross revenues to the Improvements and Contingencies Fund; (e) additional benefits and payments to the City to bring City benefits and payments to 14% of gross revenues; (f) additional payments to the Improvements and Contingencies Fund until such fund equals 20% of the value of fixed capital assets; and (g) balance to a surplus fund.
- 3) The following funds are established: (a) General Fund; (b) Improvements and Contingencies Fund; (c) Bond Construction Fund (containing the proceeds of revenue bonds); (d) Principal and Interest Current Requirements (containing the monthly payments of annual debt requirements), and (e) Bond Reserve Fund (containing an amount equal to the next fiscal year's principal and interest requirements). These funds may be invested with authorized depository banks or in U. S. Government securities.

Beginning with the year ended January 31, 1976, New Series Electric and Gás Systems Revenue Improvement Bonds ("New Series Bonds") were issued. These bonds are junior and subordinate to the "Old Series Bonds." The bond ordinances authorizing these

CITY PUBLIC SERVICE

NOTES TO FINANCIAL STATEMENTS JANUARY 31, 1987 and 1986

2. REVENUE BOND INDENTURE REQUIREMENTS (continued)

issues provide that no further bonds or obligations will be authorized or issued under the terms of the Trust Indenture for "Old Series Bonds" and, at such time as the Trust Indenture becomes inoperative, the Trust Estate will revert to the City. While any of the "Old Series Bonds" are outstanding, the "New Series Bonds" are payable solely from the net revenues of the systems (1) deposited and available for deposit in the Improvements and Contingencies Fund and (2) from funds payable to the City. At such time as the Trust Indenture covering the "Old Series Bonds" becomes inoperative, revenues will be applied as follows: (a) for maintenance and operating expenses of the systems; (b) for payments of the "New Series Bonds"; (c) for the payment of any obligations inferior in lien to the "New Series Bonds" which may be issued; (d) for an amount equal to 6% of the gross revenues of the systems to be deposited in a Repair and Replacement Fund; (e) for cash payments and benefits to the City not to exceed 14% of the gross revenues of the systems; and (f) any remaining revenues to the Repair and Replacement Fund. The funds created by the "New Series Bonds" ordinance are similar to those set forth under the "Old Series Bonds" Trust Indenture.

3. LONG-TERM DEBT

A summary of long-term debt is as follows:

Final Maturity		Weighted- Average Interest	Unpaid Principal	
			1987	1986
Old Series, 1962-1974	1988-1997	6.33%	\$ 115,220	\$ 124,220
New Series, 1975-1986	1998-2014	8.24%	1,928,810	1,699,850
Total		8.20%	2,044,030	1,824,070
Less current maturities			34,820	32,350
Amounts due after one year			\$2,009,210	\$1,791,720

CITY PUBLIC SERVICE

NOTES TO FINANCIAL STATEMENTS
JANUARY 31, 1987 and 1986

3. LONG-TERM DEBT (continued)

Principal due (in thousands) for the next five years are:

	Principal Due	
	Old Series Bonds	New Series Bonds
1988	\$ 9,435	\$25,385
1989	9,905	27,535
1990	10,375	38,725
1991	10,945	42,120
1992	11,500	45,850

As of January 31, 1987, bond reserve requirements for the Old Series Bonds and New Series Bonds have been met. Additional bond reserve requirements of \$6.0 million for the New Series 1986-A Bonds were included in the amount borrowed and were deposited in the Bond Reserve restricted cash fund in a lump sum in 1987. Similarly, additional bond requirements of approximately \$18.8 million for the New Series 1985-A and 1985-B Bonds were deposited in the Bond Reserve restricted cash fund in a lump sum in 1986. Prior to the 1983-A Bonds, reserve requirements were generated from earnings and deposited over a 61 month period as previously allowed; beginning with the 1983-A Bonds, Bond Reserve requirements have been funded from bond proceeds.

During the fiscal year ended January 31, 1987, New Series 1983-A Bonds at coupon rates of 10.4% to 10.5%, New Series 1984-A Bonds at coupon rates of 11.0% to 11.25% and New Series 1984-B Bonds at coupon rates of 10.75% to 11.125% in the principal amounts of \$79,350,000, \$91,400,000 and \$82,600,000, respectively, were advance refunded by issuance of \$320,660,000 New Series 1986 Revenue Refunding Bonds. Although the advance refunding resulted in reacquisition amounts in excess of the bond principal amounts refunded of approximately \$61,358,000, the issuance of refunding debt at interest rates lower than the previous rates will cause aggregate debt service payments to be reduced by approximately \$56,283,000. United States Government securities were purchased with the net proceeds of the 1986 issue and deposited in an irrevocable trust to satisfy scheduled principal and interest payments of the refunded issues. The refunded bond issues and trust accounts of the New Series 1986 Refunding Bonds as well as previous refundings are not included in CPS financial statements. At January 31, 1987, the following portions of each respective bond series are considered defeased:

CITY PUBLIC SERVICE

NOTES TO FINANCIAL STATEMENTS JANUARY 31, 1987 and 1986

3. LONG-TERM DEBT (continued)

New Series 1984-A	\$91,400,000
New Series 1984-B	82,600,000
New Series 1983-A	79,350,000
New Series 1982	48,145,000
New Series 1981-A	48,985,000

During January 1987, the City of San Antonio approved the issuance of New Series 1987 Refunding bonds in an amount of \$391,780,000 to be delivered on or about February 19, 1987. The proceeds from the bonds will be used to advance refund \$48,025,000 principal amount of New Series 1980 Bonds, \$34,825,000 principal amount of New Series 1980-A Bonds, \$32,675,000 principal amount of New Series 1981 Bonds, \$44,620,000 principal amount of New Series 1982-A Bonds, \$8,300,000 principal amount of New Series 1984-A Bonds, \$12,500,000 principal amount of New Series 1984-B Bonds, \$109,800,000 principal amount of New Series 1985-A Bonds, and \$38,125,000 principal amount of New Series 1985-B Bonds and to pay costs and expenses related to the issuance of the New Series 1987 Bonds. Although the advance refunding resulted in reacquisition amounts in excess of the bond principal amounts refunded of approximately \$59,489,000, the issuance of refunding debt at interest rates lower than the previous rates will cause aggregate debt service payments to be reduced by approximately \$73,698,000. Also during January 1987 the City of San Antonio gave notice of its intention to issue New Series 1987-A Bonds in an amount of \$160,000,000 to be delivered on or about March 26, 1987. The proceeds from the bonds will provide funds for the purposes of improving and extending the electric and gas systems of the City.

4. SHORT-TERM DEBT

In November 1983, the City Council of the City of San Antonio authorized the issuance of \$100 million in tax-exempt commercial paper (the "Commercial Paper") to assist in the financing of eligible projects, including fuel acquisition and capital improvements to the utility systems (the "Systems"). As of January 31, 1987, \$100 million in principal amount was outstanding, with a weighted average interest rate of approximately 3.85% and an average life outstanding of about 65 days. When available, proceeds remaining from the commercial paper have been placed in short-term investments consisting of U. S. Government obligations at cost, which approximates market. During 1987, all remaining proceeds were used for construction purposes.

CITY PUBLIC SERVICE

NOTES TO FINANCIAL STATEMENTS
JANUARY 31, 1987 and 1986

4. SHORT-TERM DEBT (continued)

The Commercial Paper is equally and ratably payable from and is secured by (i) the Net Revenues of the systems and (ii) a lien on the sale and pledge of the proceeds from the sale of other Commercial Paper, the subsequent sale of bonds, and borrowings under the Credit Agreement (as defined herein). Such pledge on Net Revenues is subordinate and inferior to the pledge securing payment of (i) the Old Series Bonds (ii) the New Series Bonds and (iii) any New Series Bonds to be issued in the future. The City and Texas Commerce Bank National Association have entered into a revolving credit agreement (the "Credit Agreement") pursuant to which such bank is obligated under the Credit Agreement to loan to the City an aggregate amount not to exceed \$100 million for the purpose of paying amounts due on the Commercial Paper. Any borrowings under the Credit Agreement are equally and ratably secured by and payable from the above-described sources pledged for payment of the Commercial Paper. There have been no borrowings under the Credit Agreement as of January 31, 1987.

5. PENSION PLAN

Prior to 1983, CPS had an insured pension plan under which insurance was purchased for each participating employee in an amount calculated to yield cash value at retirement sufficient to provide an annuity equal to prescribed benefits. To the extent benefits represented amounts attributable to wage increases received after an employee reached age 60-1/2, CPS assumed all of the incremental cost. The incremental costs for these individuals are paid directly to retirees by CPS.

In 1983, CPS adopted a self-administered, defined-benefit contributory pension plan covering substantially all employees. The total employer pension cost (all funded), which includes amortization of past service costs over 30 years using the Unit Credit Cost actuarial method, is summarized as follows:

	1987	1986
	(in thousands)	
Paid directly to retired employees	\$ 711	\$ 712
Amounts deposited in the CPS Employees' Pension Trust	<u>9,136</u>	<u>8,500</u>
Total	<u>\$ 9,847</u>	<u>\$ 9,212</u>

CITY PUBLIC SERVICE

NOTES TO FINANCIAL STATEMENTS JANUARY 31, 1987 and 1986

5. PENSION PLAN (continued)

A comparison of accumulated plan benefits and plan net assets for CPS' defined-benefit plan is as follows:

Actuarial present value of accumulated plan benefits as of the end of the plan year:

	December 31, 1986	December 31, 1985
	(in thousands)	
Vested benefits	\$104,751	\$ 89,572
Nonvested benefits	<u>33,105</u>	<u>26,351</u>
Total	<u>\$137,856</u>	<u>\$115,923</u>
Net assets available for plan benefits	<u>\$132,075</u>	<u>\$109,118</u>

An assumed rate of return of 8% was used in determining the actuarial present value of accumulated plan benefits.

In addition to providing pension benefits, CPS provides certain health care and life insurance benefits for retired employees. All of CPS' employees are eligible for these benefits upon retirement from CPS. The cost of retiree health care and life insurance benefits, funded by CPS and retired employee contributions, is recognized as an expense of CPS as employer contributions are made to the programs. These costs approximated \$734,000 and \$731,000 for 1987 and 1986, respectively.

6. PAYMENTS TO THE CITY OF SAN ANTONIO

The Trust Indenture provides for benefits and services totaling 14% of CPS gross revenues, as defined, to be paid or provided to the City. The City has elected to accept benefits that are less than 14% of gross revenue. The reduction of City benefits has no effect on financial operations.

Payments to the City of San Antonio for 1987 and 1986 were as follows:

	1987	1986
In lieu of taxes	\$ 7,799	\$ 7,096
Refund gas and electric services	15,286	17,009
Additional payments	<u>73,106</u>	<u>79,867</u>
	<u>\$ 96,191</u>	<u>\$103,972</u>

CITY PUBLIC SERVICE

NOTES TO FINANCIAL STATEMENTS
JANUARY 31, 1987 and 1986

7. SOUTH TEXAS PROJECT

CPS is one of four participants in the South Texas Project ("STP"), which consists of two 1,250 megawatt nuclear generating units under construction at a site in Matagorda County, Texas. The other participants in the project are Houston Lighting & Power Company ("HLP"), the project manager, Central Power and Light Company ("CPL") and the City of Austin ("Austin"). Under the terms of the STP participation agreement, each participant provides financing for its share of construction expenditures with CPS' participating interest in the project being 28% or 700 megawatts. Projected commercial operation dates are December 1987 and June 1989 for Units 1 and 2, respectively.

In 1986, a suit involving the project was settled on the agreement of Brown & Root, the former architect/engineer and constructor for STP, to pay the plaintiffs, CPS and the other participants, \$750 million. CPS commenced receipt of its \$210 million share of the settlement with receipt of approximately \$15 million on January 1, 1986, and \$30 million in 1987. The remainder, without interest, will be received in \$7.5 million quarterly installments over six years pursuant to an unqualified contractual obligation of Aetna Life Insurance Company. The remaining payments have been recorded as both current receivables and as Litigation Settlements Benefits Receivable.

The estimated total direct cost of the project is \$5.495 billion before consideration of the Brown & Root settlement. CPS' portion of the total costs for STP would be \$2.2 billion for construction and interest during construction and \$110 million for fuel to be purchased prior to commercial operation. CPS' share of remaining costs is estimated to be \$183.7 million for plant construction over the next three years, exclusive of interest, nuclear fuel and other costs. These costs may vary from the estimated amount due to inflation, changes in equipment delivery and construction schedules, and regulatory changes.

As of January 31, 1987, CPS has expended approximately \$1.699 billion in the project (net of the \$210 million settlement with Brown & Root), including interest during construction of \$381 million and advance payment on fuel of \$101 million.

Prior to the initial loading of nuclear fuel and operation of STP, an operating license must be issued by the Nuclear Regulatory Commission. In order to meet the scheduled

CITY PUBLIC SERVICE

NOTES TO FINANCIAL STATEMENTS JANUARY 31, 1987 and 1986

7. SOUTH TEXAS PROJECT (continued)

In-service date for Unit 1, a license for fuel loading and low power testing must be obtained by June 1987. Hearings before the Nuclear Regulatory Commission's Atomic Safety and Licensing Board have been favorably completed and CPS anticipates that the license will be issued by June 1987.

8. COMMITMENTS AND CONTINGENCIES

Coal Freight Rate Dispute - For the past ten years, CPS has been engaged in continuous litigation with certain railroads (Burlington Northern, Inc. and Southern Pacific) which, prior to August 1985, transported subbituminous coal to the J. T. Deely Station. The question involved the proper or lawful freight rate that CPS was legally required to pay these railroads for coal transportation services during the period 1978 through August 1985.

In December of 1984, the Federal District Court issued an order authorizing the railroads to collect the principal sum of \$19.8 million, plus interest of \$6.6 million from a subsidiary dispute involving ten months in 1980 and 1981 during which CPS paid the railroads \$19.8 million less for their services than the railroads claimed was due under their tariffs. This amount (\$26.4 million) was paid and classified with Prepayments and Other in the 1986 balance sheet pending final ruling in related matters.

In December 1986, CPS approved a settlement offer from the involved railroads for all disputed issues. Both parties sought dismissal of actions pending before the ICC and in two Federal District Courts. As a result, CPS received a \$31 million payment from the railroads in January 1987, most of which will be used to replace utility funds used to make the \$26.4 million court-ordered rail tariff payments and to offset legal expenses incurred during the dispute. In addition, CPS will receive annual payments ranging from \$10 to \$13 million, totaling \$80.5 million, over the next seven years from the railroads, which is expected to be returned to customers as payments are received. The remaining amounts due have been recorded as both current receivables and Litigation Settlements Benefits Receivable.

CITY PUBLIC SERVICE

NOTES TO FINANCIAL STATEMENTS JANUARY 31, 1987 and 1986

8. COMMITMENTS AND CONTINGENCIES (continued)

Other - CPS is involved in various legal proceedings related to alleged personal and property damages, breach of contract, environmental matters, condemnation appeals, and discrimination cases. In the opinion of management of CPS, the outcome of such proceedings will not have a material adverse effect on the financial position or results of operations of CPS.

Other purchase and construction commitments amounted to approximately \$65.1 million at January 31, 1987. As of January 31, 1987, CPS has no significant lease commitments.

9. SEGMENT INFORMATION

Segment information is as follows:

	1987 (in thousands)			1986 (in thousands)		
	Electric	Gas	Total	Electric	Gas	Total
REVENUE	\$ 639,626	\$127,814	\$ 767,440	\$ 700,371	\$136,500	\$ 836,871
EXPENSES:						
Operating and maintenance expenses	304,816	113,194	418,010	377,654	118,174	495,828
Depreciation	36,501	5,310	41,811	35,435	4,916	40,351
Total	341,317	118,504	459,821	413,089	123,090	536,179
EARNINGS BEFORE INTEREST AND DEBT EXPENSE, ALLOWANCE FOR INTEREST CHARGED TO CONSTRUCTION, AND PAYMENTS TO THE CITY OF SAN ANTONIO	\$ 298,309	\$ 9,310	\$ 307,619	\$ 287,282	\$ 13,410	\$ 300,692
CAPITAL EXPENDITURES	\$ 409,090	\$ 21,520	\$ 430,610	\$ 416,071	\$ 18,989	\$ 435,060
UTILITY ASSETS	\$1,617,023	\$245,290	\$1,862,313	\$1,476,729	\$220,180	\$1,696,909
CONSTRUCTION WORK IN PROGRESS	1,769,801	6,904	1,776,705	1,446,519	10,436	1,456,955
TOTAL ASSETS	\$3,386,824	\$252,194	\$3,639,018	\$2,923,248	\$230,616	\$3,153,864

APPENDIX C

CPSB INTERIM FINANCIAL STATEMENTS

Comparative Balance Sheets at October 31 (In Thousands)

Unaudited

	Assets	1987	1986
Net Utility Plant		\$ 3,077,606	\$ 2,696,876
Restricted Cash:			
Bond Construction Fund	\$ -0-	\$ 97,480	
Bond Reserve Fund	196,703	183,254	
Bond Fund Current Requirements	71,507	71,334	
Improvement and Contingencies Fund	201,176	128,014	
Other	10,894	9,109	
Total	\$ 480,280	\$ 489,201	
Litigation Settlement Benefits Receivable (Net of Current Maturities)		\$ 183,000	\$ 142,500
Current Assets:			
Cash and Temporary Investments	\$ 41,232	\$ 14,626	
Customer Accounts Receivable (Net)	42,436	43,056	
Note and Other Receivables	66,120	33,133	
Materials and Supplies	20,640	19,730	
Fuel Stock	21,964	36,665	
Prepayments and Other	(162)	101,102	
Total	\$ 172,230	\$ 248,312	
Deferred Debits	\$ 126,830	\$ 2,773	
TOTAL ASSETS	\$ 4,039,946	\$ 3,579,662	
	Liabilities		
Long-Term Debt:			
Old Series	\$ 115,220	\$ 124,220	
New Series	2,151,720	1,952,160	
Unamortized Premium/(Discount)	(25,317)	(21,090)	
Less Current Maturities	34,820	32,350	
Total	\$ 2,206,803	\$ 2,022,940	
Earnings Reinvested in Plant		\$ 1,485,647	\$ 1,298,400
Current Liabilities:			
Current Maturities of Long-term Debt	\$ 34,820	\$ 32,350	
Short-term Debt	98,000	100,000	
Accounts Payable and Accrued Liabilities	57,806	43,493	
Customers' Service Deposits	16,010	13,436	
Total	\$ 206,636	\$ 189,277	
Deferred Credits:			
Customer Advances for Construction	\$ 14,976	\$ 14,308	
Other	2,389	7,337	
Total	\$ 17,365	\$ 21,645	
Litigation Settlement Benefits Payable		\$ 72,160	\$ -0-
Contributions in Aid of Construction		\$ 51,335	\$ 47,400
TOTAL LIABILITIES	\$ 4,039,946	\$ 3,579,662	

CITY PUBLIC SERVICE BOARD OF SAN ANTONIO
Statement of Revenue and Application of Revenue
(In Thousands)

Unaudited

	Period Ending 10-31-87	
	Quarter Ended	Twelve Months
THE REVENUE FROM OPERATION WAS:		
Electric Sales	\$ 188,140	\$ 620,535
Gas Sales	16,829	131,754
Interest and Other	8,639	42,284
TOT/L REVENUE	\$ 213,608	\$ 794,573

THE REVENUE WAS APPLIED AS FOLLOWS:

FOR OPERATIONS AND MAINTENANCE:

Fuel, Gas, and Purchased Power	\$ 65,678	\$ 292,258
Operating and General Expenses	19,505	70,839
Maintenance	9,629	35,816
Subtotal	\$ 94,812	\$ 398,913

FOR OPERATING FUND ADDITIONS:

FOR DEBT REQUIREMENTS:		
Interest and Debt Expense	\$ 44,913	\$ 176,623
Retirement of Bonds	8,705	34,202
Additions to Bond Reserve Fund	2,963	13,449
Allowance for Funds Used During Construction	(26,282)	(105,665)
Subtotal	\$ 30,299	\$ 118,609

**FOR PAYMENTS AND SERVICES TO
THE CITY OF SAN ANTONIO:**

FOR ADDITIONS TO UTILITY PLANT:		
Total Expenditures	\$ 96,915	\$ 422,650

Additions to Improvements and Contingencies Fund	34,139	73,151
Subtotal	\$ 131,054	\$ 495,801

Less Funds from Bonds, Brown & Root, TECP, Contributions, etc.	\$ 70,634	\$ 313,477
---	-----------	------------

Total Revenues Available for Plant	\$ 60,420	\$ 182,324
TOTAL REVENUE APPLIED	\$ 213,608	\$ 794,573

() Represents decrease

APPENDIX D

TEXT OF CERTAIN INDENTURE PROVISIONS

The provisions of the Old Series Bond Trust Indenture, except as pertain to the issuance of parity bonds, will continue to remain in full force and effect, and will also govern insofar as the New Series Bonds are concerned as long as any of the Old Series Bonds remain outstanding.

The Trust Indenture as amended includes among other Articles and Sections thereof the following:

ARTICLE II SPECIAL COVENANTS

SECTION 1. The City is duly authorized under the laws of the State of Texas to create and issue the bonds and to execute and deliver this Indenture and to mortgage and pledge the property conveyed and mortgaged hereunder and to pledge the revenues pledged hereunder, and all necessary action on the part of the City and its Board of Commissioners for the creation and issue of the bonds and the execution and delivery of this Indenture has been duly and effectively taken, and the bonds in the hands of the holders thereof are and will be valid and enforceable obligations of the City in accordance with their terms.

* * *

SECTION 5. The City will not, except as specifically permitted by the provisions of this Indenture, create or voluntarily permit to be created any debt, lien or charge which would be on a parity with or prior to the lien of this Indenture on the trust estate or any part thereof or on the income to be derived from the trust estate and from the operation of the City's complete electric light and power system and gas distribution system or any part thereof; and will not do or omit to do or suffer to be done or omitted to be done any matter or thing whatsoever whereby the lien of this Indenture or the priority of such lien or the bonds at any time hereby secured might or could be lost or impaired; and that it will pay or cause to be paid or will make adequate provision for satisfaction and discharge of all lawful claims and demands for labor, materials, supplies or other objects which if unpaid might by law be given precedence to or an equality with this Indenture as a lien or charge upon the trust estate or any part thereof or the income and profits thereof; provided that nothing in this section shall require the City to pay, discharge or make provision for any such lien, charge, claim or demand so long as the validity thereof shall be by it in good faith contested, unless thereby, in the opinion of the Corporate Trustee, the trust estate or some material part thereof will be lost, forfeited or materially endangered.

The provisions of this section are subject to the exception that the Board of Trustees may borrow from time to time on a purely temporary basis, such sums as would ordinarily be borrowed by private companies engaged in similar business in connection with current operations, and expected to be paid and retired from current revenues received during the fiscal year in which such sums are borrowed.

* * *

SECTION 8. The City, acting through the Board of Trustees, will maintain, preserve and keep the trust estate in a state of good repair, working order and condition and will not dispose of the trust estate in whole or in part except in the manner and upon the terms provided in Article VII hereof.

SECTION 9. The City, acting through the Board of Trustees, will duly and punctually keep, observe and perform each and every term, covenant and condition on its part to be kept, observed and performed, contained in this Indenture, and will punctually perform all duties with reference to the trust estate required by the Constitution and laws of the State of Texas, including particularly the making and collecting of such reasonable and sufficient rates and charges for electricity, gas and services supplied by its electric light and power plants and system and gas distribution system, to the City and to all other consumers, adjusting such rates and charges from time to time in such manner as will render the same reasonable but at the same time fully sufficient to meet all the requirements of this Indenture, it being expressly hereby covenanted and agreed that such rates and charges will be so fixed that the revenues derived therefrom will be sufficient at all times to pay for all operating, maintenance, depreciation and replacement costs and interest charges and principal maturities, and to maintain the Bond Reserve Account and the various funds as provided in this Indenture, and to fully carry out all of the agreements contained in this Indenture and any supplemental Indenture hereto.

SECTION 10. To the extent the City may legally so covenant, the City agrees that it will not grant a franchise for the operation of any competing electric system or gas system in the City of San Antonio until all bonds issued hereunder shall have been retired.

ARTICLE III ACCOUNTS AND RECORDS

SECTION 1. The City, acting through the Board of Trustees, shall keep full and proper books of record and account, in which full, true and proper entries will be made of all dealings, business and affairs of the City which in any way affect or pertain to the operation of the trust estate and the City's electric light and power plants and system and gas distribution system, and will furnish to the Corporate Trustee and to such bondholders as may request such statement, at least once every six months and at such other times as the Trustees may reasonably request, statements in reasonable detail showing the earnings and expenses of the City's electric light and power plants and system and gas distribution system, including the trust estate and the application of funds in the General Account hereinafter established, for the preceding six months' period. Said Board will also furnish to the Trustee from time to time such other data as to the plants, properties and equipment comprising a part of the trust estate as the Corporate Trustee shall reasonably request.

SECTION 2. As soon after the close of each fiscal year as may reasonably be done, said Board of Trustees will furnish to the Corporate Trustee and to all bondholders who may so request full audits and reports covering the operations of the Systems for the preceding fiscal year, and showing the earnings and expenses of the properties and the disposition made of all revenues for said fiscal year, the amounts available for the purposes set forth in Article V hereof, and, in such detail as the Corporate Trustee may request, the assets, liabilities and financial condition of the Systems at the close of such operating year. The Board of Trustees at the same time shall furnish to said Trustee an estimate of earnings and expenses for the ensuing year in sufficient detail to indicate the probable total net income from operations and amounts available for the several funds and accounts established herein. If any such audit discloses any discrepancies or misapplication of funds, the Board of Trustees shall be charged with the duty of rectifying such misapplications as far as possible and of remedying any deficiencies in payments hereunder from the first funds available for such purpose.

SECTION 3. The Board of Trustees will, out of revenues of the trust estate, upon written request of the governing body of the City or either of the Indenture Trustees, permit the governing body of the City and the Indenture Trustees, or either of them, at all reasonable times, by their agents, engineers, accountants and attorneys, to examine and inspect the plants, property, books of account, records, reports and other data relating to the trust estate and take copies and extracts therefrom, and will afford a reasonable opportunity to make any such examination and inspection and will furnish the Indenture Trustees and the governing body of the City any and all such other information as they may reasonably request. The Indenture Trustees shall be under no duty to make any such examination unless requested so to do by the holders of twenty-five per cent in principal amount of the bonds at the time outstanding and unless such holders shall have offered the said Trustees security and indemnity satisfactory to it against any costs, expenses and liabilities which might be incurred thereby.

SECTION 4. The Board of Trustees shall, so far as practicable and to the extent consistent with the provisions of this Trust Indenture, keep its books and records in the manner prescribed in the Uniform System of Accounts for Electric Utilities adopted by the National Association of Railroad and Utilities Commissioners on November 10, 1936, and in the Uniform System of Accounts for Gas Utilities adopted by said Association on November 10, 1936.

ARTICLE IV INSURANCE

SECTION 1. The City covenants and agrees that at all times it will insure and keep insured through the Board of Trustees all properties subject to the lien hereof which are of a character usually insured by private corporations and cities operating like properties, such insurance to be written in good and responsible insurance companies, against risks customarily insured against by private corporations and cities engaged in similar business activities, and in the same manner and to the same extent, all loss therefrom (except any single loss which does not exceed \$25,000) being payable to the Corporate Trustee by the customary mortgagee or trustee clauses to be attached to or inserted in the policies. The Board of Trustees shall furnish to the Corporate Trustee a list of such policies, showing the character of the insurance, the property and risk covered, the name of the insurance company, and other pertinent details, and shall keep said Trustee fully informed of any change in or addition to such list. Upon the written request of said Trustee such policies will be deposited with it. Said Trustee, subject to the provisions of Article IX hereof, shall be under no obligation or duty to obtain any such schedule and shall have no duty or responsibility with respect to the sufficiency or effect of any of such policies of insurance, the renewal thereof, or the responsibility of the insurers, or with respect to any such schedule or the matters shown therein, except to display any such schedule to any holder of bonds desiring to inspect the same.

In case of loss or damage to any of the insured property, the proceeds of any such insurance on any one loss amounting to not more than \$25,000 shall either be promptly applied by the Board of Trustees to the repair or replacement of the property destroyed or damaged, or otherwise to the improvement of the mortgaged property, or if not so applied within two years of the date of receipt thereof by the Board of Trustees, such proceeds shall be deposited and used for the redemption of bonds as an addition to redemption funds provided for in Section 6 of Article V hereof. In any case where the proceeds of any such insurance shall amount to a sum in excess of \$25,000 on account of any one loss, all such moneys shall be promptly deposited with the Corporate Trustee and shall be paid out from time to time to the Board of Trustees upon written request of the Board,

signed by its Chairman or Vice Chairman and its Secretary, and accompanied by a certified copy of the resolution of the Board directing such request, and specifying that certain expenditures have been made or incurred in repairing or replacing the property so impaired or destroyed, and the amount thereof, and requesting the payment by said Trustee to the Board of Trustees of an amount not in excess of the amount of such expenditures. If in the judgment of the Board of Trustees and of a licensed engineer selected by the Board of Trustees and approved by the Corporate Trustee, the interests of the City and the bondholders will be best served through the application of all or part of such insurance proceeds to improvements to the mortgaged property which do not constitute the repair or replacement of the property for the destruction or impairment of which the insurance proceeds are so paid, the amount of such proceeds, to the extent permitted by law, may be applied by the Board of Trustees to the making of such improvements, and payment thereof shall be made to the Board of Trustees by the Corporate Trustee and expended in the manner provided in the last preceding sentence hereof. The Corporate Trustee may in its discretion require such additional proof of the matters certified in such resolution as it may consider necessary or desirable. Any insurance proceeds not so paid out by said Trustee within a period of two years from the date of the receipt thereof shall be added to the redemption fund provided for in Section 6 of Article V hereof and used for the redemption of bonds as therein provided.

Any adjustment of any loss under any policy of insurance made by the Board of Trustees may be consented to by the Corporate Trustee without investigation as to the fairness thereof.

ARTICLE V APPLICATION OF REVENUES

SECTION 1. During the time any bonds issued under this Indenture remain outstanding, the properties constituting the City's electric generating, transmission and distribution system and gas distribution system (including all the properties and facilities of every kind constituting the "Trust Estate") shall be operated on the basis of a fiscal year commencing on February 1 of each year and ending on the following January 31st.

SECTION 2. All revenues of every nature received through the operation of the systems shall be deposited as received in a general fund or account to be known as the "City of San Antonio Electric and Gas System General Account," hereinafter referred to as the "General Account". Revenues received for the General Account shall be deposited from time to time as received in such bank or banks as may be selected by the Board of Trustees as the depository or depositories of funds received and administered by the Board of Trustees, such bank or banks being hereinafter collectively referred to as the "Depository". The bank or banks in which such funds are kept on deposit shall at all times be a bank or banks located in the City of San Antonio unless there is no bank in the City of San Antonio qualified and willing to serve as depository, in which case the Depository may be any bank or banks in the State of Texas selected by the Board of Trustees. The Board of Trustees shall advise the Corporate Trustee of the names of the bank or banks selected as Depository from time to time. If for any reason, in its sole discretion, the Corporate Trustee shall disapprove the appointment of any bank or banks for such purpose and shall so advise the Board of Trustees, the Board of Trustees shall promptly appoint some other bank or banks which meet with the approval of the Corporate Trustee.

SECTION 3. Funds in the General Account shall be used from day to day and month to month to pay the current expenses of operating, maintaining and repairing the systems, including the cost of insurance, the purchase and carrying of stores, material and supplies, the purchase, manufacture and production of gas and electricity for distribution and resale, the payment of salaries and the payment of all other expenses properly incurred in operating and maintaining the systems and keeping them in good repair and operating condition. The system of accounts referred to in Section 4 of Article III hereof shall govern in determining whether any particular expenditure represents an operating and maintenance expense or a capital expenditure for extensions and additions to the systems. In the event that at any time hereafter taxes of any nature shall be lawfully imposed on the systems, or any part thereof, or any income or revenues thereof, by the United States of America or any governmental body or taxing subdivision other than the City of San Antonio, and such taxes are paid under the provisions of Section 7, Article II hereof, all such payments shall be made from the General Account as an expense of operation under the provisions of this section. All funds used prior to the date of this Indenture for the carrying of stores, materials and supplies shall be permanently retained in the General Account for such purpose and additional funds shall be added thereto out of revenues from time to time to the extent necessary for carrying such stores, materials and supplies, and there shall be retained in the General Account at the end of each fiscal year funds in such an amount as may be required to meet unpaid accounts and obligations which have accrued or are payable during the year, as necessary operating funds to insure the continued operation of the systems.

SECTION 4. After providing for the cost of operations, maintenance and repairs and extensions provided for by Article 1113 Revised Civil Statutes of Texas as amended, and the retention of necessary operating funds and funds for carrying stores, materials and supplies in accordance with the provisions of Section 3 of this Article V, the next available funds in the General Account shall be used for and the same are hereby pledged to the payment of the principal and interest on bonds issued hereunder and the maintaining of a reserve for such purpose, and the Board of Trustees shall cause to be paid to the Corporate Trustee in due time in each year such amounts as will be fully sufficient to promptly pay all principal of and interest on bonds issued hereunder which will become due on August 1 of such year, and February 1 of the next succeeding fiscal year. The funds in the "San Antonio Electric and Gas Revenue Bonds Reserve Account" held by the Corporate Trustee under the Indenture dated August 1, 1942 shall become and constitute upon the effective date of the Trust Indenture the "San Antonio Electric and Gas Systems Bond Reserve Account" hereinafter referred to as the

"Reserve Account") under this Trust Indenture to be used by the Corporate Trustee solely for the payment of principal and interest on bonds secured hereby falling due at any time when there would be a default if funds in the Reserve Account were not used for such purpose. During any period of time when the total amount of funds in said Reserve Account is less than the amount which would be sufficient to pay all principal and interest on bonds theretofore issued hereunder which will become due during the fiscal year immediately succeeding the close of the current year, the Board of Trustees shall pay to the Corporate Trustee an additional amount for addition to said Reserve Account equal to twenty per cent of the total payments otherwise to be made to the Corporate Trustee to meet interest and principal accruing and payable during the fiscal year on all bonds then outstanding and unpaid. Such added payments for said Reserve Account shall cease when said fund has reached the said one fiscal year's requirements as above provided. The payments required to be made to the Corporate Trustee in this section shall be made as nearly as possible in equal monthly installments in each fiscal year on or before the tenth day of each month, provided that if the tenth day shall fall on a Sunday or holiday the payment may be made on the next succeeding secular day. The "Reserve Account" and the monthly payments to meet next maturing interest coupons and bond maturities shall be kept as separate accounts. The funds necessary to meet maturing interest coupons and bonds shall be forwarded by the Corporate Trustee to the paying agent just prior to each maturity.

SECTION 5. From the next available funds in the General Account after the payments, provisions for payments and additions to funds and accounts to the full extent required in Sections 3 and 4 of this Article V have been made, there shall be paid into the General Fund of the City of San Antonio, for general City use, the sum of \$531,000, as a reimbursement for the loss of taxes which the City would receive were the Systems privately owned, for the fiscal year ending January 31, 1952, and a like payment shall be made in each fiscal year thereafter as hereinafter provided. Said payment of \$531,000 for the first fiscal year is based upon the value of fixed capital assets of the Systems located within the city limits of the City of San Antonio as of January 31, 1951, being \$35,000,000 and the payment to be made in each fiscal year after the first fiscal year shall be in said sum of \$531,000 increased or decreased by the ratio by which the value of fixed capital assets within the city limits of the City of San Antonio is increased or decreased above or below the said \$35,000,000 as at the end of the preceding fiscal year. The term "value of fixed capital assets" as used in this Section 5 and in Section 6 of this Article V shall mean the original cost of physical plant, including real estate and equipment, constituting the electric and gas systems (but excluding all cash funds and accounts) after deducting, at original cost, all actual retirements of property and all accrued depreciation at rates established in conformity with the accounting provisions contained in Article III of this Trust Indenture, and all questions of cost, property retirements and depreciation shall be determined by the accounts and records kept by the Board of Trustees in accordance with said Article III of this Indenture.

To the extent such remaining funds as provided above are sufficient, such payments in lieu of taxes shall be made in equal monthly installments. The obligation to pay such annual sums into the General Fund of the City shall be cumulative and if in any fiscal year the money in the General Account after meeting all requirements of Sections 3 and 4 of this Article V shall be insufficient to pay in full the sums so due for such year, so much thereof as may be available shall be paid and the deficiency shall be paid from the first available funds in the succeeding fiscal year or years after meeting all prior requirements of Sections 3 and 4 of this Article V.

SECTION 6. That from the next available funds in the General Account after the payments, provisions for payments and additions to funds in full accordance with the provisions of Section 3, 4, 5 of this Article V shall be made there shall be paid into a fund to be known as the "Electric and Gas System Improvements and Contingencies Fund" (hereinafter called the "Improvements and Contingencies Fund") an annual sum equal to not less than twelve and one-half (12 1/2%) per cent of the gross revenues of the systems to be used, as permitted by Article 1113 Revised Civil Statutes of Texas, as amended, for the purposes: (a) extensions, additions and improvements to the Systems (b) to meet contingencies of any kind in connection with the operation, maintenance, improvement, replacement or restoration of property, and (c) the payment of bonds or other obligations for which other funds are not available. To the extent money in the General Account is sufficient for meeting the provisions of Paragraphs 3 to 5, inclusive, of Article V of the Indenture, the transfers or payments into said Fund shall be made in monthly installments. After setting aside and providing for said minimum amount of twelve and one-half (12 1/2%) per cent of gross revenues of the systems to be placed in said Fund as above specified, there shall be paid into the General Fund of City, to the extent available from remaining revenues in the General Account as of the end of each fiscal year: (a) a sum sufficient to reimburse the City for all amounts paid to the Board during the year for gas and electric services of the Systems used by the City for municipal purposes during such fiscal year and to the extent such remaining funds are found to be sufficient, such reimbursements may be made currently in monthly installments; and (b) commencing February 1, 1960, and during the three fiscal years ending January 31, 1961, 1962, and 1963, a sum in cash which, when added to (1) the payment in lieu of taxes for the year as provided in Section 5 of Article V of this Indenture, (2) the amount of said reimbursements for electric and gas services during the year, and (3) the amount expended during the year for additions to the street and traffic lighting system will amount to \$6,508,000 for the year, and commencing with the fiscal year beginning February 1, 1963, and for each fiscal year thereafter, a sum in cash which, when added to the payments, reimbursements and expenditures for the year mentioned in (1) to (3), inclusive, in the next preceding sentence hereof, will total an amount equal to 14% of the gross revenues of the Systems for the current fiscal year. Such fixed total payments for the first three fiscal years and such additional payments to be made thereafter based on gross revenues shall be paid in monthly installments in accordance with estimates made by the Board and shall be adjusted on or before March 15 after the close of each fiscal year.

All funds remaining in the General Account of the Board of Trustees after making such payments and reimbursements, including all allowances for depreciation, shall be placed in the said "Electric and Gas System Improvements and Contingencies Fund" until such fund, after all disbursements and charges for the purposes above specified have been made, amounts to twenty (20%) per cent of the value of fixed capital assets as shown by the audited statement of the Systems. If at the close of any fiscal year any funds falling into said Improvements and Contingencies Fund result in increasing it above twenty (20%) per cent of the value of fixed capital assets as shown by the audited statement as of the end of the fiscal year, such excess shall be retained in a fund to be known as the "Electric and Gas Systems Surplus Fund". The monies in the Surplus Fund shall be used by the Board of Trustees either (a) as an offset to permit the reduction of either electric rates or gas rates or both commencing in the next fiscal year and extending for such time as the funds will permit, or (b) for the redemption of so many of the last maturing bonds then eligible for redemption prior to maturity, as the available funds are sufficient to retire, such bond retirements to be made out of such fund only when funds available for such purpose reach the amount of \$1,000,000 or more. In the event monies in the Surplus Fund are used by the Board of Trustees as an offset to permit the reduction of rates, the Board of Trustees shall in each year transfer all or so much of the Surplus Fund to the General Account of the Board as it may deem necessary, based on the advice of rate engineers for the Board, to offset or aid in offsetting the loss of revenues during the succeeding fiscal year or years due to such rate reductions.

If at the beginning of each fiscal year the total of the funds in the Improvements and Contingencies Fund and in the Bond Construction Fund available for extensions and improvements to the systems, plus the amounts estimated by the Board of Trustees to be available from revenues for such purposes during such fiscal year, is less than the amount budgeted for extensions and improvements during such fiscal year, it shall be the duty of the Board of Trustees to request the City Council to authorize and provide for the sale of additional improvement bonds in the amount necessary with other funds, to meet the cost of budgeted improvements, and it shall be the duty of the City Council to provide for the issuance and sale of such bonds in order that the budgeted extensions and improvements may be made.

SECTION 7. All interest received by the Board of Trustees and the Corporate Trustee upon funds of the system or upon bonds or other securities in which such funds may be invested in accordance with the provisions of this Trust Indenture, except interest received on the Bond Reserve Account, shall be paid annually into the General Account and deal with as a part of the revenues of the system. Interest received on the Bond Reserve Account may, at the discretion of the Board of Trustees, be used for payment of bond interest and principal from time to time. All funds in the possession of the Board of Trustees under the Trust Indenture dated August 1, 1942 and not specifically dealt with and allocated by the provisions of this Trust Indenture shall, upon the effective date of this Trust Indenture, become funds to be administered by the Board of Trustees hereunder for the same purposes and uses to which the same have been dedicated under said prior Trust Indenture. All moneys and funds held in any of the accounts and special funds provided for in this Indenture shall be held as trust funds and accounts for the benefit of the holders of the bonds issued hereunder and moneys and funds in all of said accounts and funds shall at all times, to the extent practicable, be adequately secured by or, as to money in the Reserve Account, invested in United States government bonds or other marketable securities eligible as security for the deposit of trust funds under regulations of the Board of Governors of the Federal Reserve System, or by indemnity bonds of surety companies qualified as surety for United States government deposits. All securities and indemnity bonds taken or standing as security for such money or funds shall be subject to the approval of the Board of Trustees. The Board of Trustees shall make a monthly report to the Corporate Trustee specifying the amounts held in each of the funds on deposit in the Depository and listing the securities and indemnity bonds standing as security for such deposits, and the Corporate Trustee may, but need not, require such additions and substitutions to be made in such securities and indemnity bonds as in its opinion is necessary to protect the interest of the holders of the bonds. Moneys and funds at any time held in the Improvements and Contingencies Fund may, at the discretion of the Board of Trustees, be invested in securities which are either direct obligations of the United States of America or direct obligations of any State or municipality in the United States of America which are eligible for the investment of trust funds under the laws of either the State of Texas or the State of New York then in force, or which are direct obligations of Bexar County, Texas, the City of San Antonio, Texas, or the San Antonio Independent School District.

SECTION 8. At the close of each fiscal year all accounts and funds of the Systems shall be balanced and adjusted and such transfers, distribution and adjustments made as will cause all revenues and income for the year to be applied and held in accordance with the provisions of this Article V, and the Board of Trustees shall at the close of each operating year cause an audit of the Board's accounts and operations to be made by or under the supervision of independent certified public accounts selected by the Board of Trustees.

ARTICLE VI MANAGEMENT

SECTION 1. Pursuant to the authority contained in Article 1115, Revised Civil Statutes of Texas, 1925, as amended, the complete management and control of the systems during such time as any bonds issued hereunder are outstanding and unpaid shall be vested in a Board of Trustees consisting of five citizens of the United States of America permanently residing in Bexar County, Texas, to be known as the "City Public Service Board, of San Antonio". Said Board is referred to in this Trust Indenture as the "Board" and the "Board of Trustees". The Mayor of the City of San Antonio shall ex officio be one of the members of the Board of Trustees, and the remaining members of the Board of Trustees shall consist of Walter P. Wapier, to serve for a term ending

January 31, 1953; Willard E. Simpson, to serve for a term ending January 31, 1955; James H. Calvert, to serve for a term ending January 31, 1957; and John M. Bennett, Jr., to serve for a term ending January 31, 1959; each term of office to commence with the date of this Trust Indenture. All vacancies in membership on the Board, whether occasioned by failure or refusal of any person above named to accept appointment or by expiration of term of office or otherwise, shall be filled by the majority vote of the remaining members of the Board of Trustees. No person who is related within the second degree of consanguinity or affinity to any member of the Board of Trustees or any person who shall have been a member of the Board of Trustees within a period of five years prior to the election shall be eligible for election as a member of the Board. The term of office of each member elected to the Board, after the initial terms of the members named above, shall be five years. A person who has served as a member of the Board either for an initial term as above specified or a single five-year term by virtue of election by the Board of Trustees, shall be eligible to be re-elected for one additional five-year term, and one only. A member who is elected to the Board to serve out an unexpired portion of a retired member's term shall not be considered to have served a "term" unless the unexpired portion of the term so served is three years or more. Permanent removal of residence from Bexar County by any member of the Board shall vacate his office as a member of the Board, and any member of the Board, other than the Mayor or the City, who shall be continuously absent from all meetings held by the Board for a period of four consecutive months shall, unless he shall have been granted leave of absence by the unanimous vote of the remaining members of the Board, be considered to have vacated his office as a member of the Board. Any member of the Board other than the Mayor of the City may, by unanimous vote of the remaining members of the Board, be removed from office, but only for adequate cause.

Except as otherwise specifically provided in this Trust Indenture, the Board of Trustees shall have absolute and complete authority and power with reference to the control, management and operation of the systems and the expenditure and application of the revenues of the systems subject to the provisions contained in this Trust Indenture, all of which shall be binding upon and shall govern the Board of Trustees. In connection with the management and operation of the systems and the expenditure and application of the revenues therefrom, the Board of Trustees shall be vested with all of the powers of the City with respect thereto, including all powers necessary or appropriate for the performance of all of the covenants, undertakings and agreements of the City contained in this Trust Indenture, and shall have full power and authority to make rules and regulations governing the furnishing of electric and gas service to customers and for the payment of the same, and for the discontinuance of such services upon failure of customers to pay therefor, and, to the extent authorized by law, shall have full authority with reference to making of extensions, improvements and additions to the systems and the acquiring by purchase or condemnation of properties of every kind in connection therewith.

The Board of Trustees shall elect one of its members as Chairman and one as Vice Chairman of the Board and shall appoint a Secretary and a Treasurer, or a Secretary-Treasurer, who may, but need not be, a member or members of the Board. If a member of the Board of Trustees is not appointed as Secretary or Treasurer, or Secretary-Treasurer, then an employee or employees of the Board whose duties in the operation of the systems require performance of similar duties may be appointed as Secretary or Treasurer, or Secretary-Treasurer. The Board of Trustees may follow and adopt such rules for the orderly handling of its affairs as it may see fit and may manage and conduct the affairs of the systems with the same freedom and in the same manner ordinarily employed by the Board of Directors of private corporations operating properties of a similar nature.

The Board of Trustees shall appoint and employ all officers and employees which it may deem desirable, including a General Manager of the system and an attorney or attorneys. No officer or employee of the Board of Trustees may be employed who shall be related within the second degree of consanguinity or affinity to any member of the Board of Trustees.

The Board of Trustees shall obtain and keep continually in force an employees' fidelity and indemnity bond of the so-called "blanket" type, written by a solvent and recognized indemnity company and covering losses to the amount of not less than One Hundred Thousand Dollars (\$100,000).

The members of the Board of Trustees, other than the Mayor of the City, shall receive annual compensation in the amount of Two Thousand (\$2,000.00) Dollars, except that the Chairman of the Board shall receive annual compensation in the amount of Two Thousand Five Hundred (\$2,500.00) Dollars.

The members of the Board of Trustees shall not be personally liable, either individually or collectively, for any act or omission not willfully fraudulent or in bad faith.

ARTICLE VII POSSESSION AND RELEASE OF PROPERTY

SECTION 1. While not in default in the payment of principal of or interest on any of the bonds secured hereby, or in respect of any of the covenants, agreements or conditions in this indenture contained, the City, through the Board of Trustees, shall be permitted and suffered to possess, use and enjoy the trust estate and all property and appurtenances, franchises and rights conveyed by this Indenture (except money or property, if any, expressly required to be deposited with the Corporate Trustee) and to receive and use the revenues, rents, issues, income, produce and profits thereof with power in the ordinary course of business freely and without let or hindrance on the part of the Indenture Trustees or of the holders of the bonds, to use and consume supplies; to alter, repair, dismantle and change the position of any of its buildings and structures,

plants, mains, pipe lines, poles, wires, conduits or other property whatsoever (provided that no such change shall impair the lien of this Indenture upon any such building, structure, plant, main, pipe line, pole, wire, conduit, or other property); to replace and renew any of its equipment, machinery or other property; and to acquire any and all rights, easements and contracts in connection therewith and release any rights, easements and contracts which are abandoned.

SECTION 2. The City from time to time, through the Board es, while in possession of the trust estate shall be suffered and permitted without any release from or action by the Indenture Trustees or either of them, to sell, exchange or otherwise dispose of, free from lien of this Indenture, (1) any of its equipment, machinery, fixtures, apparatus, appliances, tools, implements, or other chattels at any time subject to the lien hereof which may have become worn out or unserviceable, disused, undesirable or unnecessary for use in the conduct of its business, replacing the same by, or substituting for the same, other property of equal value to the City, which shall forthwith become, without further action, subject to the lien of this Indenture, and (2) any materials, merchandise equipment and supplies in the ordinary course and conduct of its business; provided, however, that upon the sale or other disposition of such property to the value of \$10,000 or more in any one calendar month, the Board of Trustees shall cause to be filed with the Corporate Trustee a certificate describing such property, stating that such property has become worn out, unserviceable, undesirable or unnecessary for use in the conduct of its properties and that such disposition thereof will not impair the operating integrity of the properties, and stating also the consideration received from such sale or other disposition thereof and the use made or to be made of such consideration.

SECTION 3. So long as the City is not in default hereunder the City may sell or otherwise dispose of any real property and improvements thereon mortgaged or covered by this Trust Indenture and the Corporate Trustee shall release the lien and encumbrance of this Trust Indenture upon such property, but only upon the receipt by the Corporate Trustee of a certificate signed by a majority of the members of the Board of Trustees and by an independent licensed engineer stating in substance: (1) that the proposed sale price of the property to be released represents the then fair value of the property to be sold; (2) that the City is not, to the knowledge of the signers of the certificate, in default in the performance of any of the terms or covenants of this Trust Indenture, or any indenture supplemental thereto, or any of the bonds secured thereby; and (3) that the release of the property will not, in the opinion of the signers, be prejudicial to the interest of the bondholders and that the property to be released is not, or will not at the date of delivery or surrender of possession thereof be necessary or useful in the proper and economical operation of the systems.

The money received from the sale of such released property shall be held and used by the Board to the extent permitted by law for the purchase of additional property deemed by the Board necessary or advantageous to the system, and unless such money is used in such purchase of property within two years of the time received, the same shall be used for the redemption prior to maturity of as many of the bonds as may be redeemed with such money in the manner and as a part of the redemption fund provided for in Section 6, Article V of this Trust Indenture. All additional property purchased or acquired under the provisions of this section shall immediately upon such purchase or acquisition become subject to the lien of this Indenture.

ARTICLE VIII ISSUE OF ADDITIONAL BONDS

(This section has not been reproduced since it is no longer applicable)

ARTICLE IX DEFAULTS AND REMEDIES

SECTION 1. For the purpose of this Indenture and any indenture supplemental hereto the following events are hereby defined as and are declared to be "events of default":

- (a) Default in the due and punctual payment of any interest on any bond or bonds and the continuance thereof for a period of ninety (90) days after written notice thereof by the Corporate Trustee to each member of the governing body of the City of San Antonio and to each member of the Board of Trustees, stating that payment has been demanded and default made.
- (b) Default in the due and punctual payment of the principal of any of the bonds at maturity thereof and the continuance thereof for a period of ninety (90) days after written notice thereof by the Corporate Trustee to each member of the governing body of the City of San Antonio and to each member of the Board of Trustees, stating that payment has been demanded and default made.
- (c) Default in the performance or observance of any other of the covenants, agreements or conditions on the part of the City to be kept, observed and performed contained in this Indenture or any indenture supplemental hereto, or in the bonds, and continuation of such default for a period of ninety (90) days after written notice thereof by the Corporate Trustee to each member of the governing body of the City of San Antonio and to each member of the Board of Trustees.
- (d) The institution of bankruptcy proceedings, either voluntary or involuntary, under any State or Federal statute, whereby the City's duty to carry out all of the covenants and agreements in this Indenture or any supplemental indenture might be in anywise affected. Any notice hereinprovided to be given to a member of the governing body or the City Clerk, or to a member of or the Secretary of the Board of

Trustees shall be deemed sufficiently given if sent by registered mail with postage prepaid to the person to be notified, addressed to him at the post office in the City of San Antonio. The Corporate Trustee may give any such notice in its discretion and shall give such notice if requested so to do by the holders of not less than twenty per cent (20%) in principal amount of the bonds at the time outstanding.

Wherever the term "bonds" is used in this article and elsewhere in this Trust Indenture, unless the context clearly indicates otherwise, the same shall be taken to refer to any bonds issued under this Indenture or any indenture supplemental thereto.

SECTION 2. Upon the happening of any event of default as defined in Section 1 of this article, the Corporate Trustee shall, but only upon the written request of the holders of not less than sixty per cent (60%) in principal amount of the bonds then outstanding hereunder, and upon being indemnified to its satisfaction, by notice in writing to the Secretary of the Board of Trustees and to the City Clerk, to be sent as provided in Section 1 hereof, declare the principal of all bonds then outstanding hereunder to be due and payable immediately, and upon any such declaration the said principal shall become and be due and payable immediately, anything in this Indenture or in the said bonds to the contrary notwithstanding. This provision, however, is subject to the condition that if at any time after the principal of said bonds shall have been declared due and payable and before any sale of the trust estate shall have been made, all arrears of interest upon all such bonds, with interest upon all past due installments of interest at the rate borne by the bonds, and all past due principal of the bonds, together with the reasonable charges and expenses of the Indenture Trustees, their agents, attorneys and counsel, shall be paid by the City, and after all other defaults which may have occurred shall have been remedied or cured to the satisfaction of the Trustee, then and in every such case, the holders of sixty per cent (60%) in principal amount of the bonds then outstanding may, by notice in writing given to the Corporate Trustee, and to the City Clerk and the Secretary of the Board of Trustees in the manner provided in Section 1 of this article, waive such default and its consequences, and rescind such declaration, but no such waiver or rescission shall extend to or affect any subsequent default or impair or exhaust any right or power consequent thereon.

SECTION 3. Upon the happening of any event of default as defined in Section 1 of this article, the Indenture Trustees or either of them, personally or by their attorneys or agents, may to the extent permitted by law enter into and upon and take possession of all the trust estate and each and every part thereof and exclude the City and the Board of Trustees, or its agents, servants and employees, wholly therefrom, and have, hold, use, operate, manage and control the same, and each and every part thereof, and in the name of the City or otherwise, as they shall deem best, conduct the business thereof and exercise the franchises pertaining thereto and all the rights and powers of the City, and use all of the then existing property, materials, current supplies, stores, and other assets for that purpose, and at the expense of the trust estate from time to time maintain, restore, insure and keep insured the properties, plants, equipment and apparatus provided or required for use in connection with such business, and likewise from time to time, at the expense of the trust estate, make all such necessary or proper repairs, renewals and replacements and all such useful alterations, additions, betterments and improvements as to them may seem judicious, and collect and receive all rates, earnings, income rents, issues, profits and revenues of the same and of every part thereof, and after deducting therefrom the expenses of operation and all expenses incurred hereunder and all other proper outlays herein authorized, and all payments which may be made as just and reasonable compensation for their own services, and for the services of their attorneys, agents, and assistants, and the rest and residue of the moneys received by the Trustees, or either of them, shall be applied as follows:

- (a) In case the principal of none of the bonds shall have become due, to the payment of the interest in default, in order of the maturity of the installments of such interest, with interest on the overdue installments thereof at the same rates, respectively, as were borne by the bonds on which such interest shall be in default, such payments to be made ratably to the parties entitled thereto without discrimination or preference.
- (b) In case the principal of any of the bonds shall have become due by declaration or otherwise, first to the payment of the interest in default, in the order of the maturity of the installment thereof at the same rates, respectively, as were borne by the bonds on which such interest shall be in default, and next to the payment of the principal of all bonds then due, such payments to be made ratably to the parties entitled thereto without discrimination or preference.

In case all of such payments, and payment of whatever may be payable for any other purpose required by any provision of this Indenture, shall have been made in full and no suit to foreclose or enforce this Indenture shall have been begun or sale made as hereinafter provided, and upon compliance with all other provisions of this Indenture as to which the City shall be in default, the Indenture Trustees, after making such provision as to them may seem advisable for the payment of the next maturing installment of interest to fall due upon the bonds, shall restore the possession of the trust estate (other than any cash at the time required to be held by the Corporate Trustee hereunder) to the Board of Trustees.

SECTION 4. Upon the happening of any event of default as defined in Section 1 of this Article, if the principal of all of the bonds outstanding hereunder shall have been properly declared due and payable as provided in Section 2 of this Article, and whether or not the remedies authorized by Section 3 of this Article shall have been pursued in whole or in part, the Indenture Trustees, or either of them, may cause this Indenture to be foreclosed and the trust estate to be sold, and may proceed to protect and enforce the rights of the Indenture Trustees and the bondholders hereunder in such manner as counsel for said Trustees shall

advise, whether for the specific performance of any covenant, condition, agreement or undertaking herein contained, or in aid of the execution of any power herein granted, or for the enforcement of such other appropriate legal or equitable remedies as may in the opinion of such counsel be more effectual to protect and enforce the rights aforesaid. The Indenture Trustees shall take any such action or actions if requested so to do by the holders of at least sixty per cent (60%) in principal amount of the bonds then outstanding hereunder.

SECTION 5. Upon the happening of any event of default as defined in Section 1 of this Article, and if the principal of all of the outstanding bonds shall have been declared due and payable as provided in Section 2 of this Article, then and in every such case, and whether or not the remedies authorized by Section 3 of this Article shall have been pursued in whole or in part, the Indenture Trustees, or either of them, shall, but only upon the written request of the holders of not less than sixty per cent (60%) in principal amount of the bonds then outstanding hereunder, with or without entry, sell to the highest bidder the trust estate and all right, title, interest, claim and demand thereto and the right of redemption thereof, at any such place or places, and at such time or times and upon such notice and terms as the Trustee acting may fix and specify and as may be required by law. In case of such sale of any of the property subject to this Indenture, notice of such sale shall first be given by publication in at least one daily newspaper published in the city in which the sale is to be made at least once a week for four successive weeks next preceding such sale, and by like publication in at least one daily newspaper published in the City of New York, New York, and by the giving of any other notices which may be required by law, and upon such sale the Trustees may make and deliver to the purchaser or purchasers a good and sufficient deed or deeds for the same, which sale shall be a perpetual bar both at law and in equity against the City and all persons and corporations lawfully claiming or to claim by, through or under it. No purchaser at any such sale shall be bound to see to the application of the purchase money or to inquire as to the authorization, necessity, expediency or regularity of any such sale. Nevertheless, the City, if so requested by the acting Trustee, shall ratify and confirm any sale or sales by executing and delivering to the acting Trustee or to such purchaser or purchasers all such instruments as may be necessary or in the judgment of the acting Trustee proper for the purposes which may be designated in such request.

Such notice of sale shall state that the City has granted to the purchaser of the mortgaged property a franchise for the operation thereof for a period of twenty years dating from such purchase.

SECTION 6. In the event of any sale, whether made under the power of sale hereby granted and conferred or under or by virtue of judicial proceedings or of a judgment or decree of foreclosure and sale, the whole of the trust estate shall be sold in one lot and as an entirety, unless such sale as an entirety is impossible or impracticable by reason of some statute or otherwise.

SECTION 7. The acting Trustees may from time to time adjourn any sale to be made by them hereunder by announcement at the time and place of such adjourned sale, and without further notice or publication except as otherwise required by law may make such sale at the time and place to which the same may be so adjourned.

SECTION 8. In case an event of default as defined in Section 1 of this Article occurs, and if all of the bonds outstanding hereunder shall have been declared due and payable as provided in Section 2 hereof, and in case a bill in equity shall be filed or any other judicial proceeding commenced to enforce any right of the Indenture Trustees or of the bondholders under this Indenture or otherwise, then as a matter of right, the acting Trustee shall be entitled to the appointment of a receiver of the trust estate and of the earnings, income or revenues, rents, issues and profits thereof with such powers as the court making such appointment may confer.

SECTION 9. In case the Indenture Trustees, or either of them, shall have proceeded to enforce any rights under this Indenture by foreclosure, sale, or otherwise, and such proceedings shall have been discontinued or superseded, or shall have been determined adversely to said Trustee or Trustees, then and in every such case the City and the Indenture Trustees shall be restored to their former respective positions and rights hereunder in respect of the trust estate, and all rights, remedies and powers of the Indenture Trustees and the bondholders shall continue as though no such proceedings had been taken.

SECTION 10. In case of any such sale of the trust estate, any bondholder or bondholders or committee or bondholders or either Trustee, may bid for and purchase such property and upon compliance with the terms of sale may hold, retain possession and dispose of such property as the absolute right of the purchaser or purchasers without further accountability and shall be entitled, for the purposes of making settlement or payment for the property purchased, to use and apply any bonds hereby secured and any interest thereon due and unpaid, whether or not such interest be evidenced by coupons, by presenting such bonds and coupons in order that there may be credited thereon the sum apportionable and applicable thereto out of the net proceeds of such sale, and thereupon such purchaser or purchasers shall be credited on account of such purchase price payable by him or them with the sum apportionable and applicable out of such net proceeds to the payment of or as credit on the bonds and coupons so presented.

SECTION 11. The proceeds of any judicial or other sale of the trust estate, together with any funds at the time held by the Corporate Trustee and not otherwise appropriated, shall be applied as follows:

FIRST: To the payment of the costs, expenses, fees and other charges of such sale and a reasonable compensation to the Indenture Trustees, their agents and attorneys, and to the discharge of all expenses and liabilities incurred and advances or disbursements made by said Trustees hereunder.

SECOND: Any surplus then remaining to the payment of the whole amount then due or unpaid upon the bonds issued hereunder and then outstanding for principal and interest, with interest on overdue principal and overdue installments or interest at the same rates, respectively, as were borne by the bonds whereof the principal or installments of interest may be overdue, and in case such proceeds shall be insufficient to pay in full the whole amount so due and unpaid, then to the payment of such principal and interest ratably according to the aggregate amount due on all bonds then outstanding without preference or priority of principal over interest or of interest over principal.

THIRD: Any surplus then remaining to the City or whomsoever shall be lawfully entitled thereto.

SECTION 12. In case of a sale under any of the foregoing provisions of this Article, whether made under the power of sale herein granted or under or by virtue of judicial proceedings, the principal of all bonds issued hereunder and then outstanding, if not previously due, shall immediately thereafter become due and payable, anything in said bonds or in this Indenture, or any supplemental indenture, to the contrary notwithstanding.

SECTION 13. The remedies herein conferred upon or reserved to the Indenture Trustees or to the holders of bonds hereby secured are not intended to be exclusive of any other remedy, but each remedy herein provided shall be cumulative and shall be in addition to every other remedy given hereunder or now or hereafter existing, and every power and remedy hereby given to said Trustees or to the holders of bonds issued hereunder may be exercised from time to time as often as may be deemed expedient. No delay or omission of said Trustees or of any holder of bonds issued hereunder to exercise any power or right arising from any default hereunder shall impair any such right or power (unless the exercise of such right or power shall become barred by law) or shall be construed to be a waiver of any such default or to be acquiescence therein.

SECTION 14. Anything in this Indenture contained notwithstanding, the holders of sixty per cent (60%) in principal amount of bonds hereby secured and then outstanding shall have the right by an instrument or instruments in writing delivered to the Indenture Trustees to direct and control said Trustees as to the method of taking any and all proceedings for any sale of any or all of the trust estate, or for the foreclosure of this Indenture, or any supplemental indenture, or for the appointment of a receiver, and may at any time cause any proceedings authorized by the terms hereof to be taken or to be discontinued or delayed; provided, however, that such holders shall not be entitled to cause said Trustees to take any proceedings which in their opinion, or the opinion of the one acting, would be unjustly prejudicial to non-assenting bondholders.

SECTION 15. No holder of any bond or coupon issued hereunder shall have any right as such holder to institute any suit, action or proceeding for the foreclosure of this Indenture or for the execution of any Trust hereunder or for the appointment of a receiver, or for any other remedy hereunder, all right of action hereunder being vested exclusively in the Indenture Trustees, unless and until such holder shall have previously given to said Trustees written notice of a default hereunder and of the continuance thereof, and also unless the holders of the requisite principal amount of the bonds then outstanding shall have made written request upon said Trustees and shall have afforded a reasonable opportunity to institute such action, suit or proceeding in the name of one or both of them, and unless said Trustees shall have been offered reasonable indemnity satisfactory to them against the costs, expenses and liabilities to be incurred therein or thereby, and said Trustee for thirty (30) days after receipt of such notification, request or offer of indemnity shall have failed to institute any such action, suit or proceeding, it being understood and intended that no one or more holders of the bonds shall have the right in any manner whatever by his or their action to affect, disturb or prejudice the lien of this Indenture, or any supplement hereto, or to enforce any right thereunder except in the manner herein provided and for the equal benefit of all holders of such outstanding bonds.

SECTION 16. In any suit or action by or against the Indenture Trustees, or either of them, arising under this Indenture or on all or any of the bonds or coupons issued hereunder, said Trustee or Trustees shall not be required to produce such bonds or coupons, but shall be entitled in all things to maintain or defend any such suit or action without their production.

SECTION 17. If any covenant, agreement, waiver or part thereof in this Article or elsewhere in this Indenture, or in any supplemental indenture, contained be forbidden by any pertinent law, or under any pertinent law be effective to render this Indenture invalid or unenforceable, or to impair the lien thereof, then each such covenant, agreement, waiver or part thereof shall itself be and is hereby declared to be wholly ineffective and this Indenture and supplements thereto shall be construed as if the same were not included herein.

ARTICLE XI
FRANCHISE

In the event that any sale of the trust estate shall be made under any of the provisions of this Indenture for the enforcement of the lien of this Indenture, and any supplements thereto, the City hereby grants to the purchaser or purchasers at such sale a franchise to operate the property so purchased for a term of twenty years dating from such purchase, subject to all laws regulating same then in force. The properties so purchased, in the event they are operated by the purchaser pursuant to such franchise, shall be operated, conducted and maintained in such manner as to be a benefit to the City of San Antonio and its inhabitants, and such purchaser shall be pledged to render efficient public service.

ARTICLE XII
MODIFICATION OF THIS INDENTURE

SECTION 1. The holders of seventy-five per cent (75%) in principal amount of bonds at any time outstanding (not including in any case any bonds which may then be held or owned by or for the account of the City) shall have the right from time to time to consent to and approve the execution by the City and the Indenture Trustees of such Indenture or Indentures supplemental hereto as shall be deemed necessary or desirable by the City for the purpose of modifying or amending any of the terms or provisions contained in this Indenture or in any Indenture or Indentures supplemental thereto so contained in the ordinance authorizing bonds secured by this Indenture; provided, however, that nothing herein contained shall permit or be construed as permitting the modification or amendment of the terms and conditions contained in this Indenture or any supplemental Indenture or any ordinance or bonds so as to:

- (a) Make any change in the maturity of the bonds issued hereunder.
- (b) Reduce the rate of interest borne by any bonds.
- (c) Reduce the amount of the principal or premium, if any, payable on bonds.
- (d) Modify the terms of payment of principal or of interest or premium upon bonds or any of them or impose any conditions with respect to such payment.
- (e) Affect the rights of the holders of less than all bonds then outstanding.

If at any time the City shall request the Indenture Trustees to enter into such Supplemental Indenture, said Trustee, unless they shall deem that such proposed supplemental Indenture shall contain provisions which affect their rights or obligations and to which they are unwilling to assent, shall at the expense of the Board of Trustees, cause notice of the proposed execution of such supplemental Indenture to be published in a financial newspaper or journal published in the City of New York, New York, and in a newspaper of general circulation published in the City of San Antonio, once during each calendar week for at least four successive calendar weeks, and on or before the date of the first publication of such notice, the Corporate Trustee shall also mail a copy thereof to each registered owner of bonds at his address appearing on said Trustee's registry books, but failure to mail any such notice or any defect therein shall not affect the validity of the proceedings for obtaining consents to the execution and delivery of such supplemental Indenture. Such notice shall briefly set forth the nature of such proposed supplemental Indenture and shall state that a copy thereof is on file at the principal office of said Trustee for inspection by all holders of bonds.

Whenever at any time within one year from the date of the first publication of said notice the City shall deliver to the Corporate Trustee an instrument or instruments executed by the holders of at least seventy-five per cent (75%) in aggregate principal amount of the bonds then outstanding as in this section defined, which instrument or instruments shall refer to the proposed supplemental Indenture described in said notice and shall specifically consent to and approve the execution thereof in substantially the form of the copy thereof on file with the Corporate Trustee, thereupon, but not otherwise, the Indenture Trustees shall execute the said supplemental Indenture in substantially the said form without liability or responsibility to any holder of any bond, whether or not such holder shall have consented thereto.

If the holders of at least seventy-five per cent (75%) in aggregate principal amount of the bonds outstanding as in this section defined at the time of execution of any such supplemental Indenture, or the predecessors in title of such holders shall have consented to and approved the execution thereof as herein provided, no holder of any bond, whether or not such holder shall have consented to or shall have revoked any consent as in this section provided, shall have any right or interest to object to the execution of such supplemental Indenture or to object to any of the terms or provisions therein contained, or to the operation thereof, or to enjoin or restrain the Indenture Trustees or the City from executing the same or from taking any action pursuant to the provisions thereof.

SECTION 2. Upon the execution of any supplemental Indenture pursuant to the provisions of this section, this Indenture and any supplements thereto and the ordinances authorizing the bonds then outstanding shall be and be deemed to be modified and amended in accordance with such supplemental Indenture, and the respective

rights, duties and obligations of the City, the Trustees and all the holders of outstanding bonds shall thereafter be determined, exercised and enforced, subject in all respects to such modifications and amendments.

Any consent given by the holder of a bond pursuant to the provisions of this section shall be irrevocable for a period of six months from the date of the first publication of the notice provided for in this Article, and shall be conclusive and binding upon all future holders of the same bond during such period. Such consent may be revoked at any time after six months from the date of the first publication of such notice by the holder who gave such consent, or by a successor in title, by filing notice with the Trustees in form satisfactory to them of such revocation of consent, but such revocation shall not be effective if the holders of seventy-five per cent (75%) aggregate principal amount of the bonds outstanding as in this section defined have, prior to the attempted revocation, consented to and approved the supplemental Indenture referred to in such revocation.

For the purposes of this Article, ownership of bonds shall be established in the manner provided in Section 1 of Article XIII of this Indenture.

Any supplemental Indenture executed in accordance with the provisions of this Article shall thereafter form a part of this Indenture and all the terms and conditions in any such supplemental Indenture as to any provision authorized to be contained therein shall be and be deemed to be part of the terms and conditions of this Indenture for any and all purposes.

APPENDIX E
CPSB RESOLUTION APPROVING NEW SERIES BONDS ORDINANCE

**A RESOLUTION OF THE CITY PUBLIC SERVICE BOARD
OF SAN ANTONIO, TEXAS, RELATING TO THE ISSUANCE
AND SALE OF \$160,000,000 CITY OF SAN ANTONIO
TEXAS, ELECTRIC AND GAS SYSTEMS REVENUE
IMPROVEMENT BONDS, NEW SERIES 1988**

WHEREAS, pursuant to the authority contained in Article 1115, V.A.T.C.S., a Trust Indenture, dated February 1, 1951, and various Supplemental Indentures thereto (collectively called the "Indenture") providing security for the payment of outstanding revenue bonds known as "Old Series Bonds" and ordinances passed by the City Council of the City of San Antonio, Texas, on October 9, 1975, February 2, 1976, June 24, 1976, January 6, 1977, July 15, 1977, February 23, 1978, August 3, 1978, January 11, 1979, July 12, 1979, February 7, 1980, August 21, 1980, March 5, 1981, September 17, 1981, March 11, 1982, October 28, 1982, May 12, 1983, December 8, 1983, May 31, 1984, October 11, 1984, January 24, 1985, April 11, 1985, October 24, 1985, February 27, 1986, June 12, 1986, January 22, 1987, and February 26, 1987, (collectively called the "Ordinances"), authorizing the issuance of outstanding revenue bonds known as "New Series Bonds." The complete management and control of the electric and gas systems (the "Systems") of the City of San Antonio, Texas, is vested in a Board of Trustees known as the City Public Service Board of San Antonio, Texas (the "Board"), during the period of time any of the aforementioned "Old Series Bonds" and "New Series Bonds" are outstanding and unpaid; and

WHEREAS, in the performance of its duties and responsibilities pertaining to the management and operation of the Systems, the Board has determined that \$160,000,000 in revenue bonds should now be issued by the City to provide funds to meet the costs of improvements and extensions to the Systems currently under construction and estimated costs of planned improvements and extensions to said Systems, such amount of bonds being based upon (i) the difference between the estimated costs of such extensions and improvements and the total amount of funds available and estimated to be available to meet said estimated costs, and (ii) the current rate of expenditure of funds for such capital improvement project costs; and

WHEREAS, by virtue of the authority and power vested in the Board with reference to the expenditures and application of the revenues of the Systems and to comply with the terms and conditions prescribed in the Ordinances for the issuance of additional bonds on a parity with the heretofore issued "New Series Bonds," it is necessary and proper for the Board to formally request the City Council of San Antonio to authorize and sell such bonds, consent to the issuance of the same, approve the ordinance authorizing such bonds and agree to comply with all the terms and provisions of such ordinance with relation to the operation of the Systems, and the handling of the proceeds of such bonds.

NOW, THEREFORE, BE IT RESOLVED BY THE BOARD OF TRUSTEES OF THE CITY PUBLIC SERVICE BOARD OF SAN ANTONIO, TEXAS:

1. That the City Council of the City of San Antonio, Texas, is hereby formally requested to authorize and sell \$160,000,000 in principal amount of revenue bonds payable from the same source, secured in the same manner and on a parity with the heretofore issued "New Series Bonds"; and the Board by the adoption of this resolution doth hereby evidence its consent to the issuance and sale of such bonds and the payment thereof from the net revenues of the Systems and its approval of the ordinance authorizing the issuance of the \$160,000,000 "City of San Antonio, Texas, Electric and Gas Systems Revenue Improvement Bonds, New Series 1988" dated March 1, 1988, a copy of which ordinance is attached to this resolution; and the Board hereby agrees to comply with all of the terms and provisions of said ordinance with relation to the administration and operation of the Systems and the disposition of the revenues therefrom; and

2. That the "Official Notice of Sale" ((including abbreviated form to be published) and "Official Statement" prepared in connection with the issuance and sale of the bonds designated "City of San Antonio, Texas, Electric and Gas Systems Revenue Improvement Bonds, New Series 1988", in the principal sum of \$160,000,000, are hereby approved, and the Chairman of the Board is hereby authorized to execute the Official Statement on behalf of the Board; and

3. That the General Manager or Secretary of the Board is authorized to prepare any addenda or amendments to the "Official Notice of Sale" and "Official Statement" deemed appropriate or necessary, and cause the same to be published and/or distributed prior to the sale of the Bonds; and

4. That the Board recognizes that the ordinance authorizing the New Series 1988 Bonds (the "Bonds") contain covenants of the City of San Antonio to the effect that (i) the City will make no use of the proceeds of the Bonds directly or indirectly that would cause such Bonds to be arbitrage bonds within the meaning of Section 103 (c) of the Internal Revenue Code of 1954, as amended, (the "Code"), and (ii) the City will comply from the date of issuance of the Bonds with the amendments relating to tax-exempt Bonds included in the Tax Reform Act of 1986 (the "Amendments"); and realizing that in accordance with the terms of the ordinance the proceeds of the Bonds will be entirely within the control and disposition of the Board, the Board therefore specifically adopts such covenants made by the City Council in such ordinance and hereby covenants with the purchasers of the Bonds that it will make no use of the proceeds of the Bonds at anytime throughout the term thereof which

would cause the Bonds to be arbitrage bonds within the meaning of Section 103(c) of the Code or any Treasury regulations or income tax rulings promulgated thereunder or pertaining thereto, that it will comply with the requirements of Section 103(c) of the Code and all applicable regulations and rulings, and that it will comply with the covenants made by the City in such ordinance pertaining to the Amendments.

PASSED AND APPROVED by an affirmative vote of the Board of Trustees of the City Public Service Board of San Antonio, Texas, this the 25th day of January, 1988.

ATTEST:

/s/ HOWARD L. FREEMAN
Secretary, City Public Service Board

/s/ EARL C. HILL
Chairman, City Public Service Board

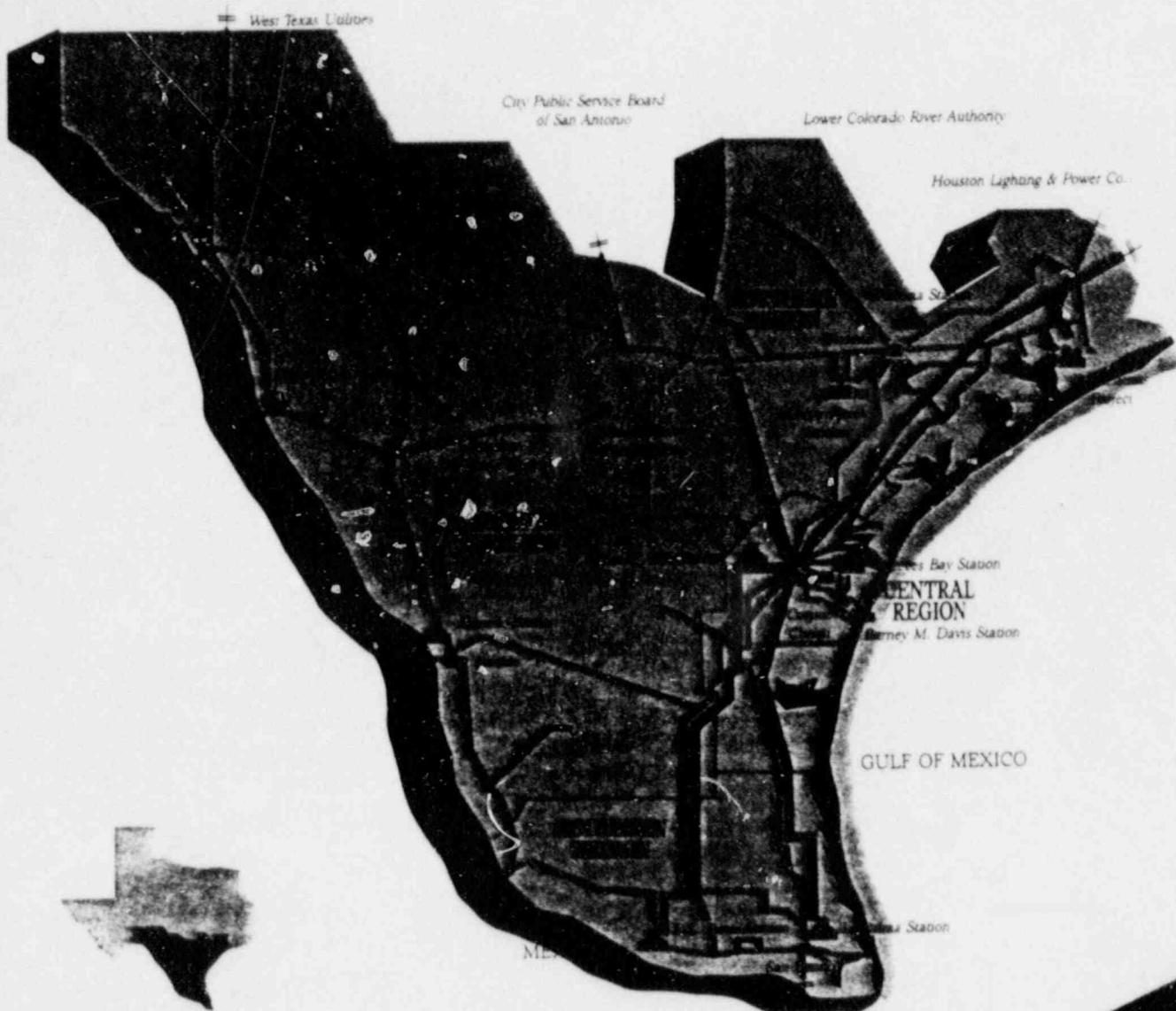
(THIS PAGE LEFT BLANK INTENTIONALLY)

Central
Power
and
Gas
Company
Annual
Report
1981

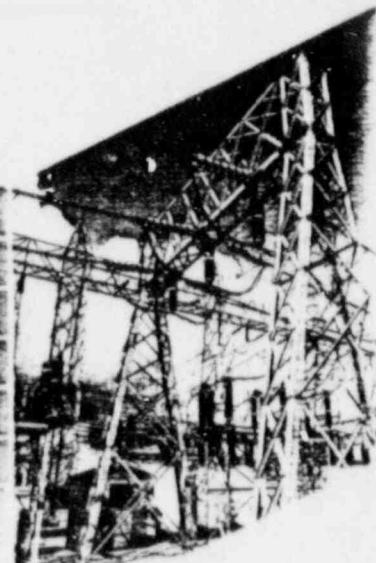




Central Power and Light Company supplies electric service to a 44,000-square-mile area which reached into 44 counties of South Texas. The Company is a subsidiary of Central and South West Corporation, a registered holding company. At the end of 1987, Central Power and Light Company served 532,546 customers in 224 communities and the surrounding area. The Company also supplies, at wholesale, a part or all of the electric requirements of five rural electric cooperatives and two municipal electric systems. The territory served by the Company has a population of approximately 1.8 million. Principal executive offices are located at 565 N. Carancahua Street, Corpus Christi, Texas. Telephone: (512) 881-5300.



TRANSMISSION LINES
— 345 KV LINES
— 115 KV LINES
— BOUNDARIES AND CONNECTIONS WITH OTHER SYSTEMS
■ REGIONAL FACTS
■ GAS-FIRED GENERATING STATIONS
■ HYDRO GENERATING STATION
■ COAL-FIRED GENERATING STATION
■ NUCLEAR PLANT UNDER CONSTRUCTION



President's Letter

During 1987, Central Power and Light Company made significant progress toward long and short term objectives that will enable us to meet current and future challenges.

Nearly two decades ago the Company initiated a plan to end its almost total dependence on natural gas as a boiler fuel. That plan, which consisted of adding both coal and nuclear capacity, will be culminated with the completion of the South Texas Project nuclear plant. Unit 1 of STP has been completed and is expected to be in service prior to our summer peak, and Unit 2 is scheduled for operation in 1989. The diversification of our fuel base will assure both price and supply stability, benefitting customers and investors.

Despite the difficulties of building and licensing nuclear plants, STP will be an asset to South Texas and will be the source of reliable power at a stable price. CPL's rates have been among the lowest in the state for a number of years, and we believe our balanced fuel mix will help us maintain a competitive position.

Preparations for a rate increase filing to include the cost of STP Unit 1 in rate base are in progress and will be filed in the coming months. The filing will propose that new rates be phased in so as to minimize the impact on customers, yet protect the Company's financial standing.

Preparing our Company for major changes that are occurring throughout the utility industry is also vital to our future. We have initiated a variety of responses to these changes. For example, we inaugurated a program in 1987 to enhance CPL's productivity. Even though the Company consistently has been among the country's most efficiently operated utilities, we made a thorough study of our organization to define the relative contributions of all functions to our operations and to identify ways of further enhancing our efficiency. We developed a reorganization plan that will reduce our total employee force by 11%. Throughout the study and planning stages, we considered it imperative that

any reductions not impair the quality of service to our customers.

Most of the reduction will be accomplished through an early retirement package that was offered to employees near the end of 1987. Of the 268 eligible employees, 236 or 88%, elected to accept it.

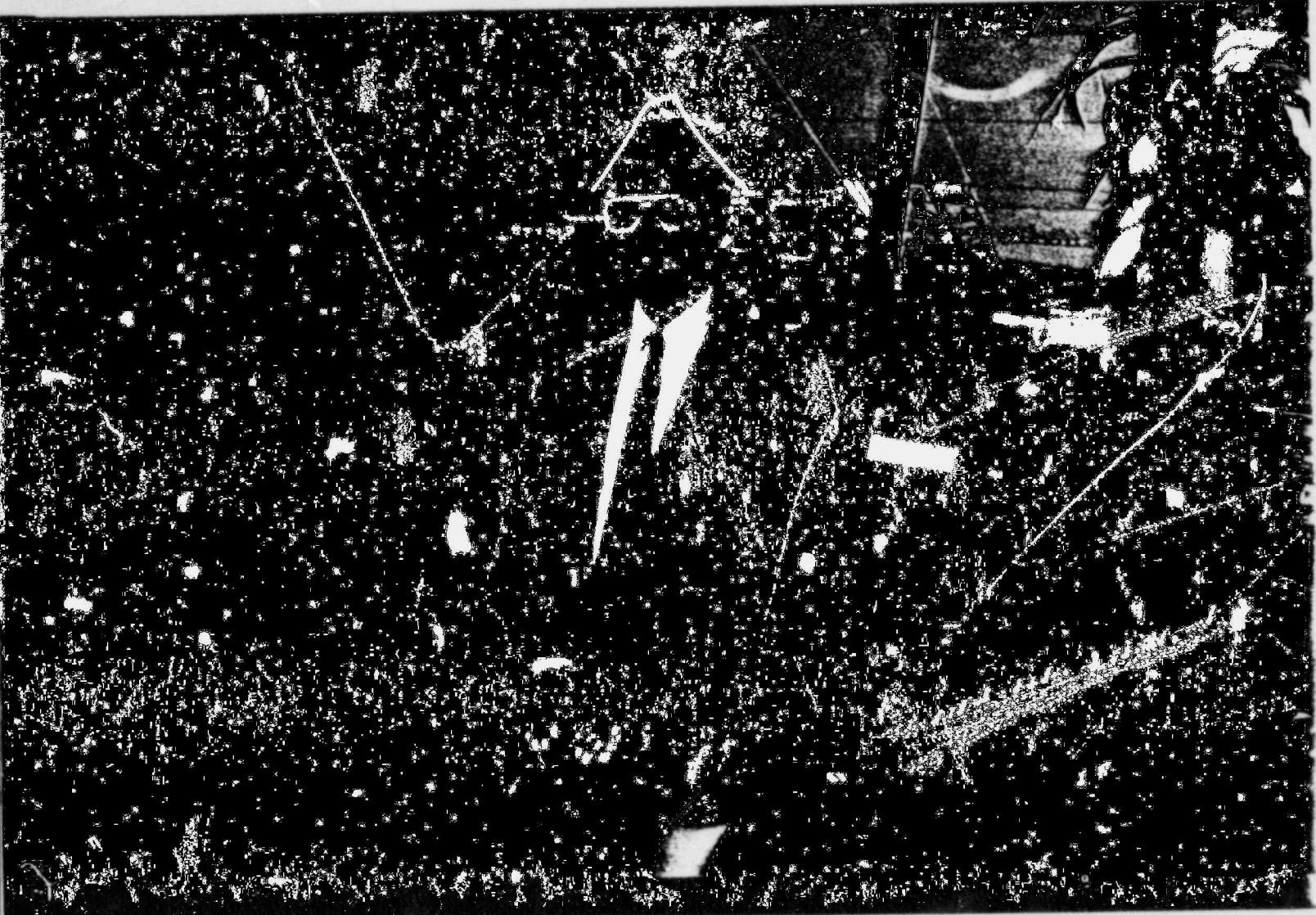
The **reorganization plan**, which affected virtually all work groups, was announced near the end of the year. Under the new structure, the Company's six distribution districts and four transmission divisions were consolidated into four operating regions. Where feasible, local manager positions were reduced by combining the responsibilities for several communities under one area manager. Likewise, power plants in reasonable proximity to each other were combined under the supervision of a single manager. The reorganization also reduced power plant personnel, cut the size of line crews and eliminated many supervisory positions throughout the organization. Several top and middle management positions were also eliminated. Overall, we reduced our senior management by 26%.

Other cost-control measures are in effect. The most significant of these is our fuel procurement strategy. CPL's fuel diversification program, aggressive contract negotiations and the creation of more competition among fuel suppliers is saving our customers millions of dollars annually. During the year we took some older, gas-fired generators out of service. Seven units will be "mothballed" to help cut costs. A major factor in the decision to take these units out of service is the low cost of nuclear fuel, which will soon be a part of our fuel mix. The procedures used to store these units will enable us to return them to operational status when they are needed to serve future load growth.

As another means of improving the results of our operations, and thereby lessen the need for higher rates, we have intensified our marketing efforts. The Company's marketing program focuses on electrical applications that improve



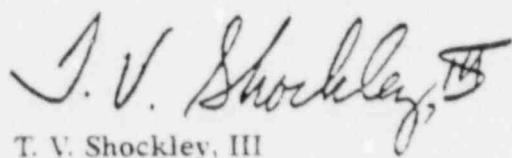
CPL employees contribute in many ways to help keep the Company efficient, competitive, and in touch with community needs.



ystem load factor, making more efficient use of our production facilities. The program also emphasizes energy conservation and encourages efficient use of electricity. With the assistance of many employees whose regular work assignments do not include marketing, the program for 1987 exceeded expectations. Our marketing successes reinforce our confidence that the Company is prepared for a more competitive future.

Operating profitably has been made difficult by current economic conditions. South Texas has suffered from the decline of the petroleum industry, and there is general agreement that the area must develop other types of industry and commerce to create a broader-based economy. We are convinced that efforts to accomplish that objective will succeed and that South Texas will be stronger for it. CPL is taking a leading role in area development efforts.

Management is grateful to CPL
employees, whose patience and loyalty during this period of transition has enabled us to continue operating in a manner that benefits all. Without their cooperation, it would have been impossible for the Company to make the changes necessary to satisfy the new requirements that are being thrust upon the utility industry.



T. V. Shockley, III
President and Chief Executive Officer
Central Power and Light Company

March 10, 1988

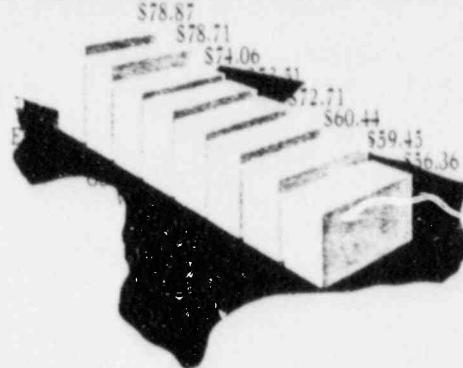


The Company's marketing program features high intensity discharge type lighting applications, the most efficient lighting technology available.

Customers Pay Lower Price, Revenues Decline

For the fourth consecutive year, reduced fuel costs resulted in lower prices for CPL's customers, keeping the Company's rates among the lowest in the state. Average revenue per kilowatt-hour from residential customers dropped from 6.22 cents to 5.90 cents during the year. In 1983 the average price of a residential kilowatt-hour was 26% higher than the present price.

TEXAS COST OF ELECTRICITY (RESIDENTIAL WINTER RATES PER 1000 KWH)



INVESTOR-OWNED ELECTRIC UTILITIES JAN. 1988

Total revenues declined by almost 11% from 1986 because of several factors. Included among them were lower fuel costs, a soft economy, a flat customer growth curve, losses of industrial load, and a reduction in economy sales to other utilities. Revenues collected under

the base rates were off by approximately 2% while fuel revenues declined 20%.

Kilowatt-hour sales were down by more than 10%.

Residential customers increased their average annual use of electricity from 10,338 kilowatt-hours to 10,369 kilowatt-hours, an increase of less than 1%. The number of customers in this category also increased slightly. Lower fuel costs, however, offset these small gains and produced a revenue reduction of almost 4%.

In the commercial category there were also slight increases in kilowatt-hour sales and in the number of customers. Revenues in this class were down by 4.5% because of the lower fuel recoveries.

Industrial revenues declined by approximately 22%, as did kilowatt-hour sales. The major reasons for these reductions are the loss of load to cogenerators and the shut down in 1986 of the Company's largest customer.

Net Income Increases. Despite the decline in revenue, the Company's net income increased from \$174.2 million in 1986 to \$191.9 million in 1987, a gain of more than 10%. The increase is attributable to a 2.7% reduction in operating expenses and taxes and a 21% increase in allowance for funds used during construction (AFUDC).

South Texas Project Unit 1 Set For Commercial Operation

Unit 1 of the South Texas

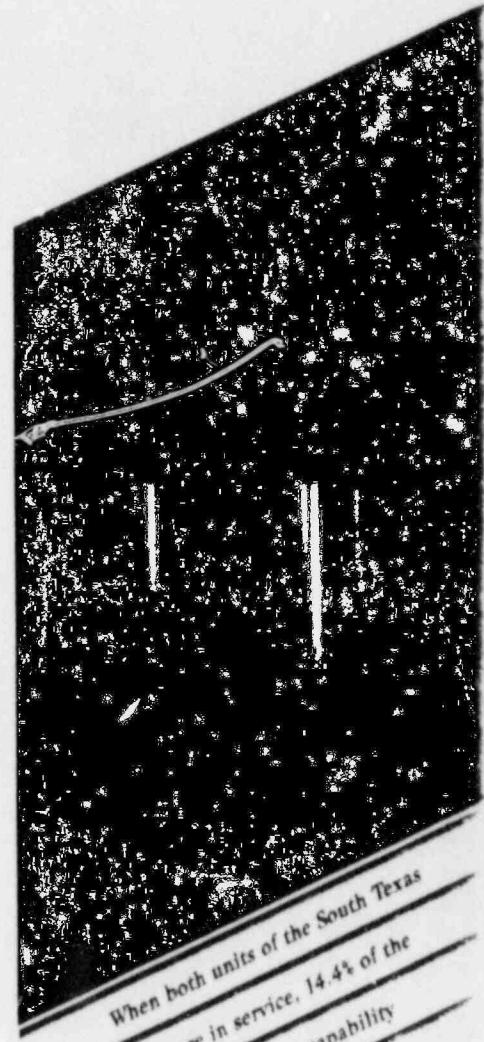
Project, a 1250-megawatt nuclear unit in which CPL has a 25.2% interest, is in the final stages of startup for commercial operation. The unit achieved initial criticality on March 8, signifying the first production of heat through the nuclear fission process. A full power license is expected to be received from the Nuclear Regulatory Commission by late March. The unit will then be put through a number of tests that gradually increase levels of power. A declaration that the unit is in commercial operation is anticipated prior to the summer peak, which normally occurs in August.

Commercial operation had been expected as early as March, but the startup schedule was delayed by design and equipment problems that were detected during startup testing. Corrective actions to resolve these problems took more than

two months to implement.

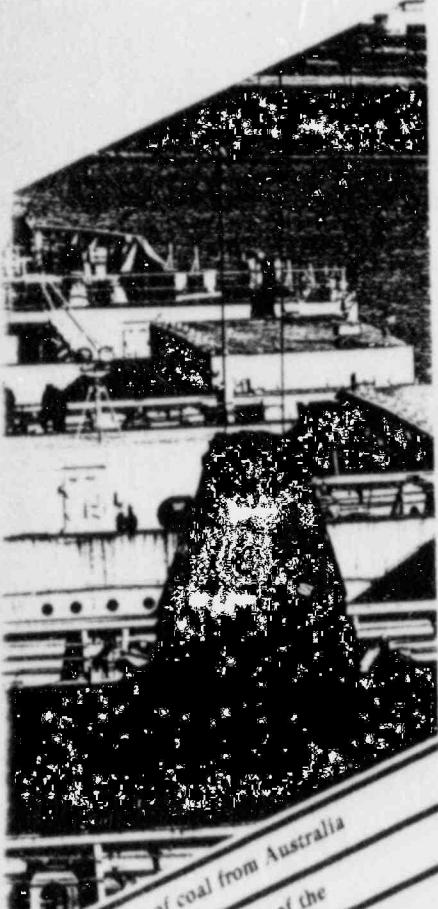
A threat of further delay resulted from a claim by an activist group that it was in possession of hundreds of allegations of safety problems at STP by current and former project employees. The group, the Government Accountability Project, in December 1987 submitted its allegations to the NRC. The NRC conducted an on-site investigation as to the substance of these allegations in January 1988. The formal report of that investigation is expected in March. It is the Project Manager's position that some of the allegations are old ones that have been previously investigated and have been corrected or dismissed, and the rest are believed to be without merit.

In September, the 1987 Completion Assessment was released. It increased the forecasted completion cost of the plant by \$300 million. Including the proceeds received from a litigation settlement with the project's former architect/engineer and constructor, the total completed cost of the plant was projected at \$5.277 billion. This total is about 4% below the total cost of \$5.495 billion estimated in 1982.



When both units of the South Texas Project are in service, 14.4% of the Company's generating capability will be nuclear.

Construction of South Texas Project Unit 1 has been completed, and Unit 2 was more than 90% complete at the end of January.



Unit 2 of STP was 90% complete and slightly ahead of schedule as of the end of January 1988. Based on the current schedule, the unit will load fuel in December 1988 and will achieve commercial operation in June 1989.

In January 1986, the Public Utility Commission of Texas opened a docket for the purpose of determining the prudence and efficiency of the planning and management of the construction of STP. In March 1988, the Texas Commission's General Counsel hired a second auditor to assist in analyzing STP prudence issues. Based on this and other factors, hearings have been suspended indefinitely by the hearings examiner. The parties are currently working together to arrive at a feasible schedule.

In 1985 a docket was instituted to gather evidence concerning the economic viability of STP Unit 2. Hearings in this docket were completed in October 1987. However, in November 1987 the Supreme Court of Texas stayed all hearings and actions in the docket pending resolution of a dispute concerning the Attorney General's right to represent other state agencies in Texas Commission proceedings.

With both units in commercial operation, STP will have the capability to

produce 2,500 megawatts of electricity. CPL's share, 630 megawatts, will account for 14.4% of the Company's total generating capacity.

Retail Rate Proposal Tied To STP Operation

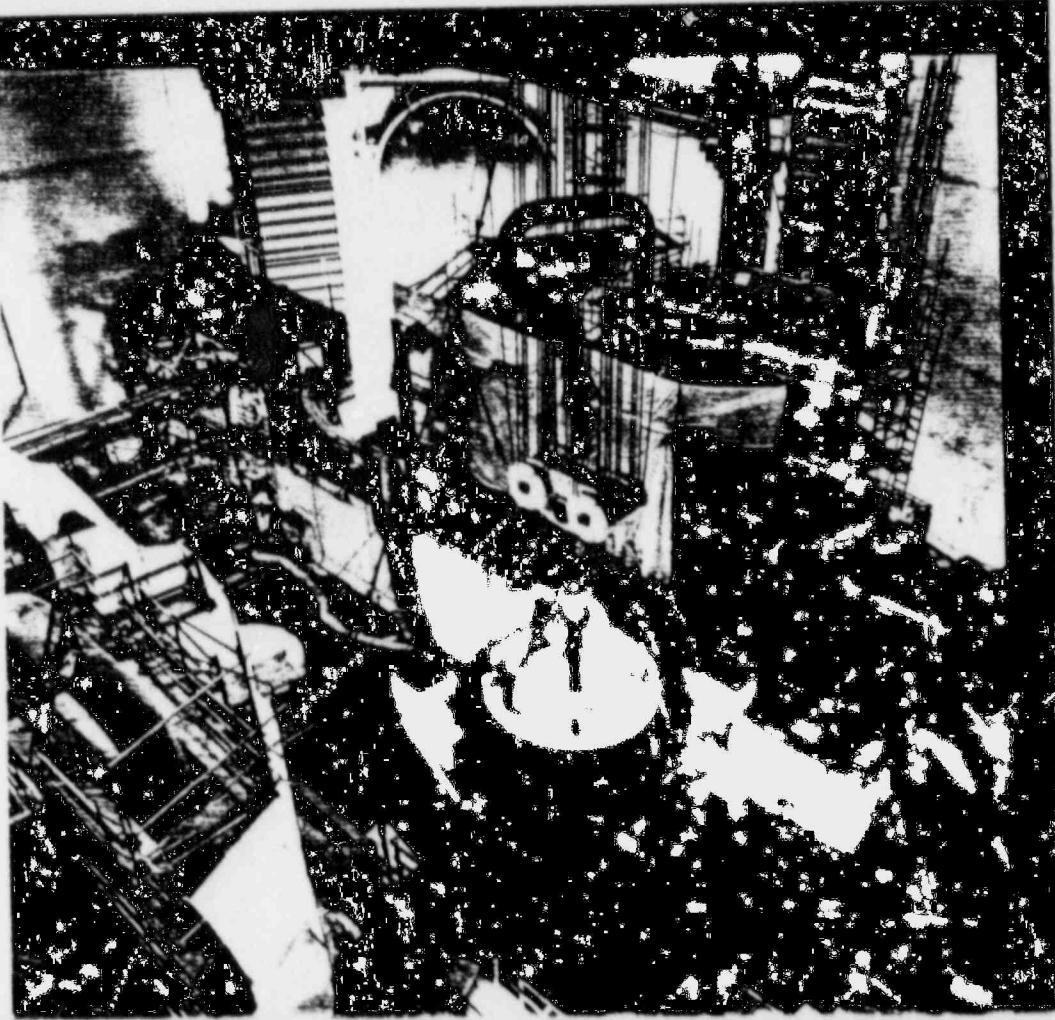
Preliminary work has been done on a rate filing primarily designed to include the first unit of STP in the Company's rate base. Actual timing of the filing is dependent on the schedule for declaring the unit in commercial operation. Present estimates are that Unit 1 will achieve that status by the summer peak.

The Company plans to file a proposal that phases in higher rates for Unit 1 over a period of several years. When Unit 2 is in commercial operation, a phase-in proposal will likewise be filed to include that unit's costs in rate base.

The phase-in approach was selected as the most practical way of meeting the needs of customers and stockholders. The phase-in cushions the impact of higher rates on customers and would gradually improve the Company's financial integrity indicators.

Trial cargos of coal from Australia and Colombia were a part of the Company's efforts during 1987 to further reduce the cost of fuel.

Inside the containment structure of STP Unit 2, work progressed on the unit's reactor head assembly.



Fuel Strategies Promote Competition, Stable Costs

For well over a decade the single most significant element in the price of electricity to CPL customers has been the cost of fuel. For many of the years since 1973 fuel costs accounted for more than half of the Company's operating expenses. Accordingly, one of our highest priorities is the continuing development of fuel procurement and utilization strategies that result in the lowest possible fuel expense compatible with future cost stability and reliability of service.

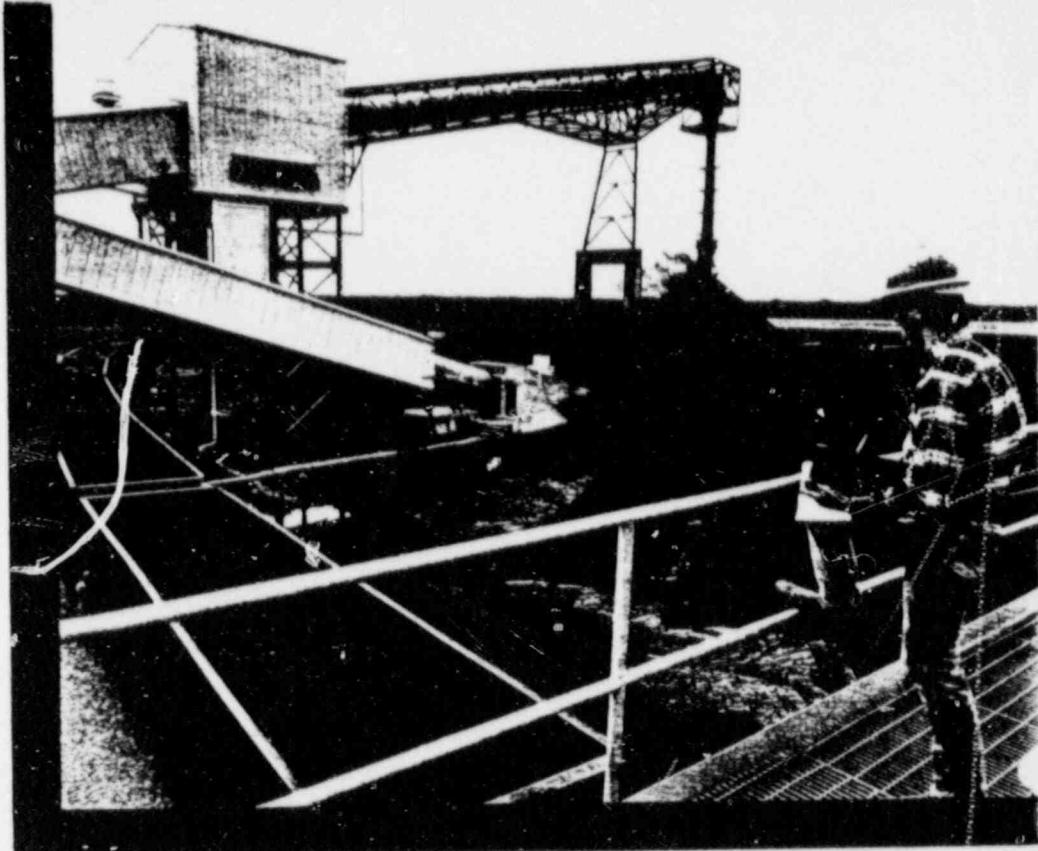
The basic elements of our strategy are 1) to diversify our fuel base as a hedge against price or supply instability, 2) to increase the number of our supply sources as a way of reducing fuel costs, and 3) to maintain a balanced mix of short term and long term procurement arrangements as a means of ensuring both market sensitivity and price stability.

The diversification of our fuel base will be complete in 1989 when the second unit of the STP nuclear plant achieves commercial operating status. In terms of generating capability, our fuel mix at that point will be approximately 71% natural gas, 15% coal, and 14% nuclear. By 1990 nuclear fuel is expected to account for approximately 21% of our fuel requirements at a unit cost of about one fifth that of natural gas.

ESTIMATED FUEL USE 1990



The Company's strategy of aggressively managing its fuel supplies has enabled it to participate heavily in the spot gas market over the past few years. This was accomplished through several contract renegotiations which reduced minimum-take commitments under our long-term arrangements. Over 30% of our gas supply is now reserved for purchase, when desirable, under short-term,



market-sensitive arrangements.

During 1987 CPL had 36 suppliers who fed through 12 direct pipelines to our power stations. Our supply sources include eight major pipeline companies, a number of large and small producers in South Texas, and suppliers acting as third-party agents to market natural gas to CPL from producers who lost their traditional market for gas.

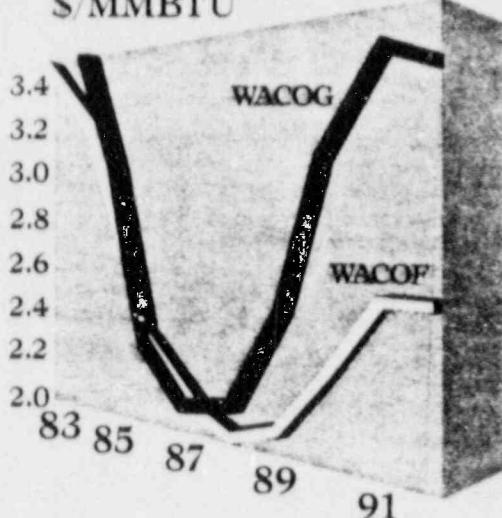
We have installed gas interchange systems at all power stations, enabling us to take advantage of this multi-supplier situation. These computerized systems, which provide operator control and state-of-the-art measurement, allow dispatchers to selectively use the most economical discretionary gas supply. The Company's purchasing strategy for natural gas has saved CPL and its customers millions of dollars during the past three years. CPL obtained its lowest level weighted average cost of gas since 1978 during the summer of 1987.

Additional millions of dollars in fuel costs have been saved during the past seven years by CPL's decision to construct Coletto Creek Power Station, a coal-fired generating unit that began commercial operation in 1980. Our efforts to increase the amount of savings from the use of coal are continuing on several fronts.

First, we have aggressively pursued the renegotiation of contracts with our principal coal supplier and the railroads that

The use of coal as a boiler fuel at Coletto Creek Power Station has saved CPL's customers millions of dollars since the station began commercial operations in 1980.

WACOF VS. WACOG \$/MMBTU



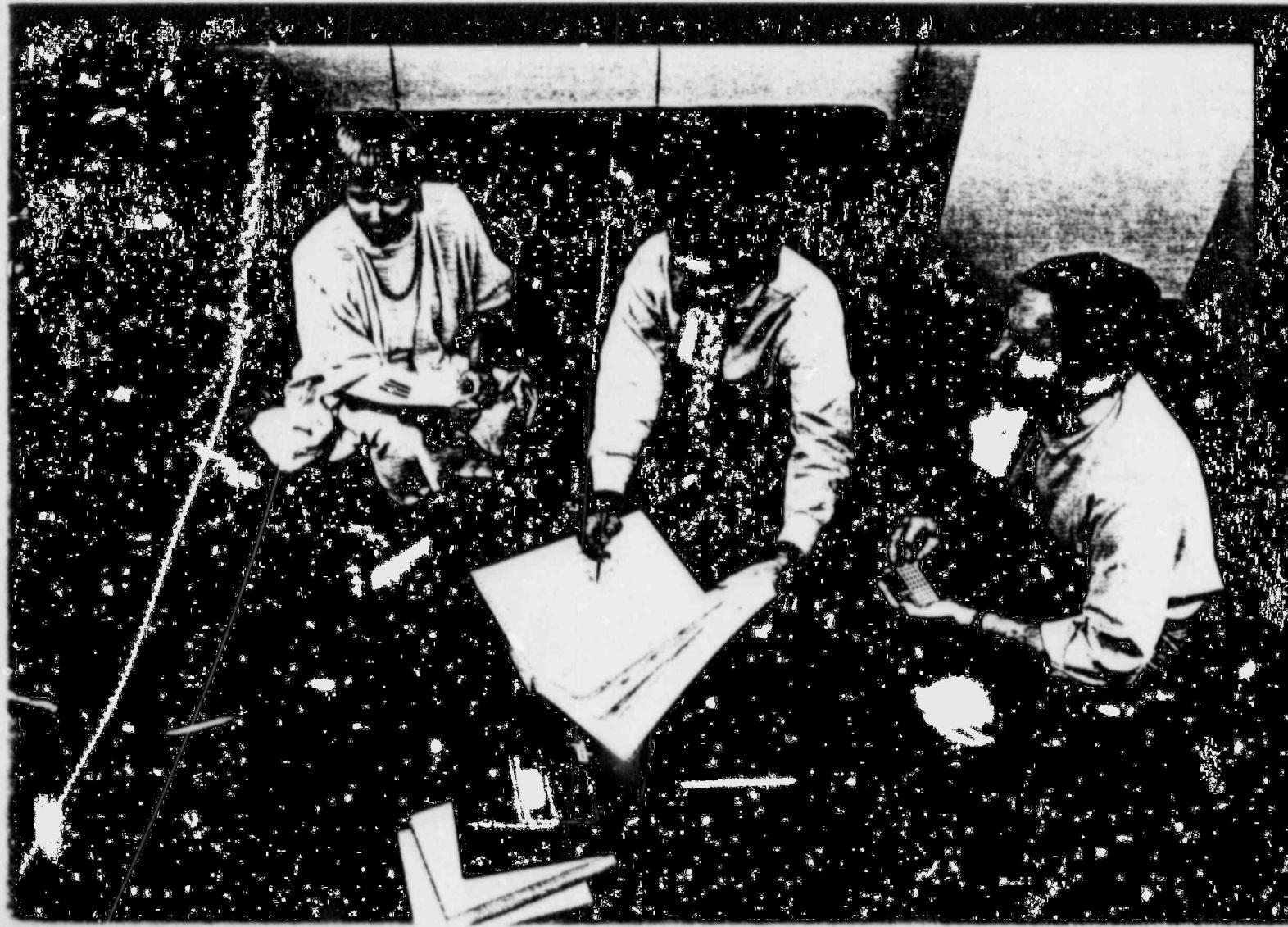
Designing rates to help CPL remain competitive was a major part of the work load for the Company's rate department during 1987.

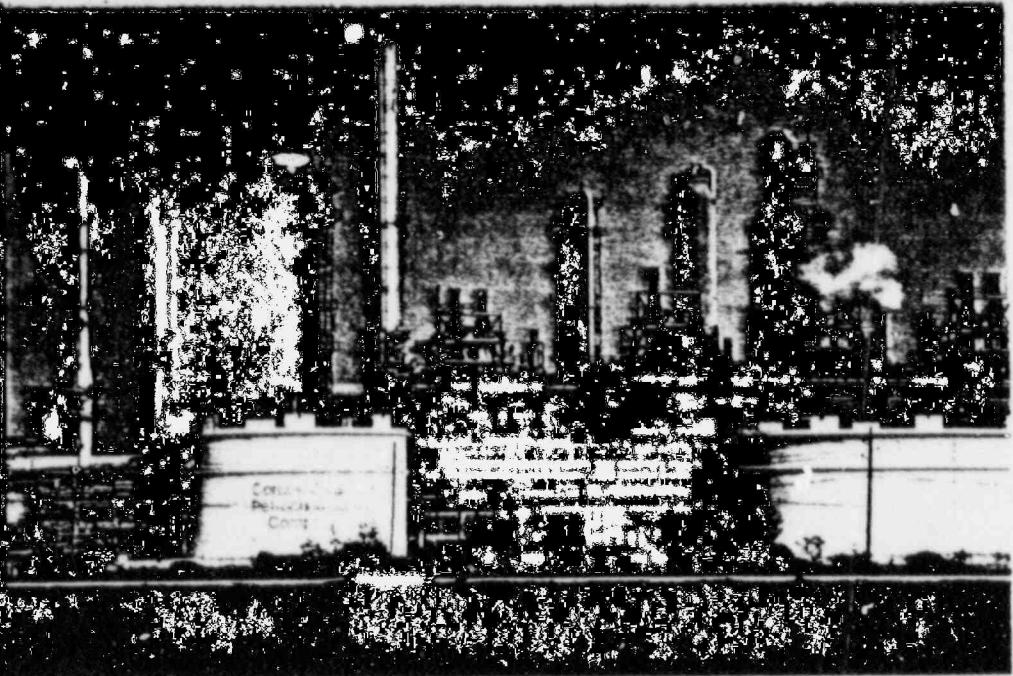
The wisdom of converting to a diversified fuel base is illustrated in this comparison and projection of CPL's weighted average cost of natural gas to the weighted average cost of all our fuel supplies.

deliver coal from Colorado. Our most recent effort produced a 25% reduction in our delivered cost.

Secondly, we have increased our activity in the open market, which now supplies approximately a quarter of our coal needs at the Coleto Creek Power Station. CPL's spot coal bidders list has approximately 100 potential suppliers, both foreign and domestic. We have explored all reasonable means of creating competition and are exploring options that will reduce the cost of our coal supplies. Our efforts included the purchase of trial cargos in 1987 from Australia and Colombia.

Our strategies to reduce the cost of fuel led to two refunds of fuel revenues in 1987. In August, we refunded \$19.4 million resulting from fuel savings during the months of January through June. Another \$21.2 million was refunded in February 1988 for fuel savings between July and December. Since 1983, the Company has refunded approximately \$197 million in fuel savings.





Large industries such as this petrochemical plant are eligible for CPL's new industrial rate.

New Rates Help CPL Meet Competition

New rates that went into effect in 1987 are keeping the Company competitive with alternative sources. In August the Public Utility Commission of Texas approved a rider that reduced the cost of power to our large industrial customers. The reduction amounted to eight-tenths of a cent per kilowatt-hour for those customers agreeing to purchase at least 12,500 kilovolt-amperes annually through 1990. We agreed that a revenue loss of \$13.2 million per year would be absorbed by our stockholders until new retail rates are put into effect. Ten of the Company's 12 existing large industrial customers have accepted the new rate. During 1988 we will apply for a rate that would allow qualifying large industrial customers to provide natural gas to CPL for the purpose of producing electricity for their use. The fuel option rate will supplant this industrial rider.

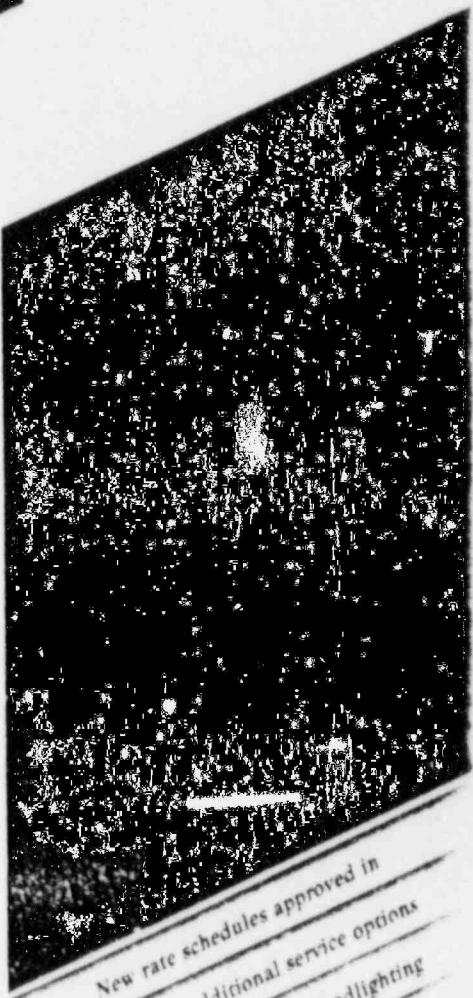
In November, the Texas Commission approved a new contract for service to Occidental Chemical Corporation's caustic chlorine facility on the north shore of Corpus Christi Bay near Ingleside. The contract provides for a combination of firm and interruptible service to the facility, which previously had been owned and operated by DuPont. The Company expects to receive more than \$25 million per year from the plant's operations. Similar pricing arrangements were approved for other new customers of the same class.

Several new rate schedules for security

lighting and floodlighting were approved in May. The tariff for a new 70-watt security light provides an additional option for residential customers. The new rates for leased floodlighting also expand the choices of services available to our commercial customers.

Also in 1987 we achieved a favorable conclusion to a rate application for our wholesale and municipal customers, whose rates are regulated by the Federal Energy Regulatory Commission. A settlement among parties was agreed upon that increased rates by \$2.2 million per year through June 1987 and \$1.3 million thereafter. The decrease reflects benefits to customers resulting from lower tax expense under the new federal income tax law. The settlement contains provisions for customers to be individually assigned the annual costs of STP Unit 1 after that unit goes into service. These costs will be repaid by the affected customers over a five-year period after rates reflecting STP Unit 1 in rate base are placed in effect. The settlement provides CPL a small amount of relief now and also assures that the wholesale and municipal customers will ultimately pay their fair share of STP costs.

Fuel revenue refunds, which have amounted to \$197 million since 1983, are expected to diminish in 1988 because of price increases on the spot market for natural gas. The price increases make it less likely that the fuel factor used to calculate fuel rates to customers can be lowered during 1988. The fuel factor will be modified to reflect the fuel savings from STP Unit 1 after that unit goes into operation.



New rate schedules approved in 1987 give additional service options to security lighting and floodlighting customers.

New Marketing Program Achieves Success

Primarily because of increasing competition and slow economic growth, marketing at CPL has taken on renewed emphasis. Greater effort is being applied to the Company's sales programs as a means of producing additional revenue and of creating greater efficiencies both for the Company and for its customers.

Satisfying our revenue requirements by means of sales, especially off-peak sales, is in the interests of all concerned. To the extent that required revenues can be attained by marketing, rate increases can be diminished.

Our marketing program focuses on efficiency — efficiency for the customer by offering options that permit maximum savings, and efficiency for the Company by helping make optimum use of our facilities. Also because of competition, effective marketing is, to a greater extent than in the past, an essential element in maintaining the Company's financial integrity.

CPL's new marketing program, inaugurated in mid-1986, experienced a full year of implementation in 1987 and achieved significant successes. Several

factors — increased competition, a sluggish economy, reduced population growth, and a depressed construction industry — made marketing especially difficult. Nevertheless, the program resulted in additional sales of more than 300 million kilowatt-hours on an annualized basis. The 1987 effort added 195.6 megawatts of connected load to the Company's lines.

The primary aims of our marketing efforts for the next decade will be strategic load growth, the retention of high-load factor customers, an increase in off-peak consumption, and the addition of new customers. Specific objectives include the following:

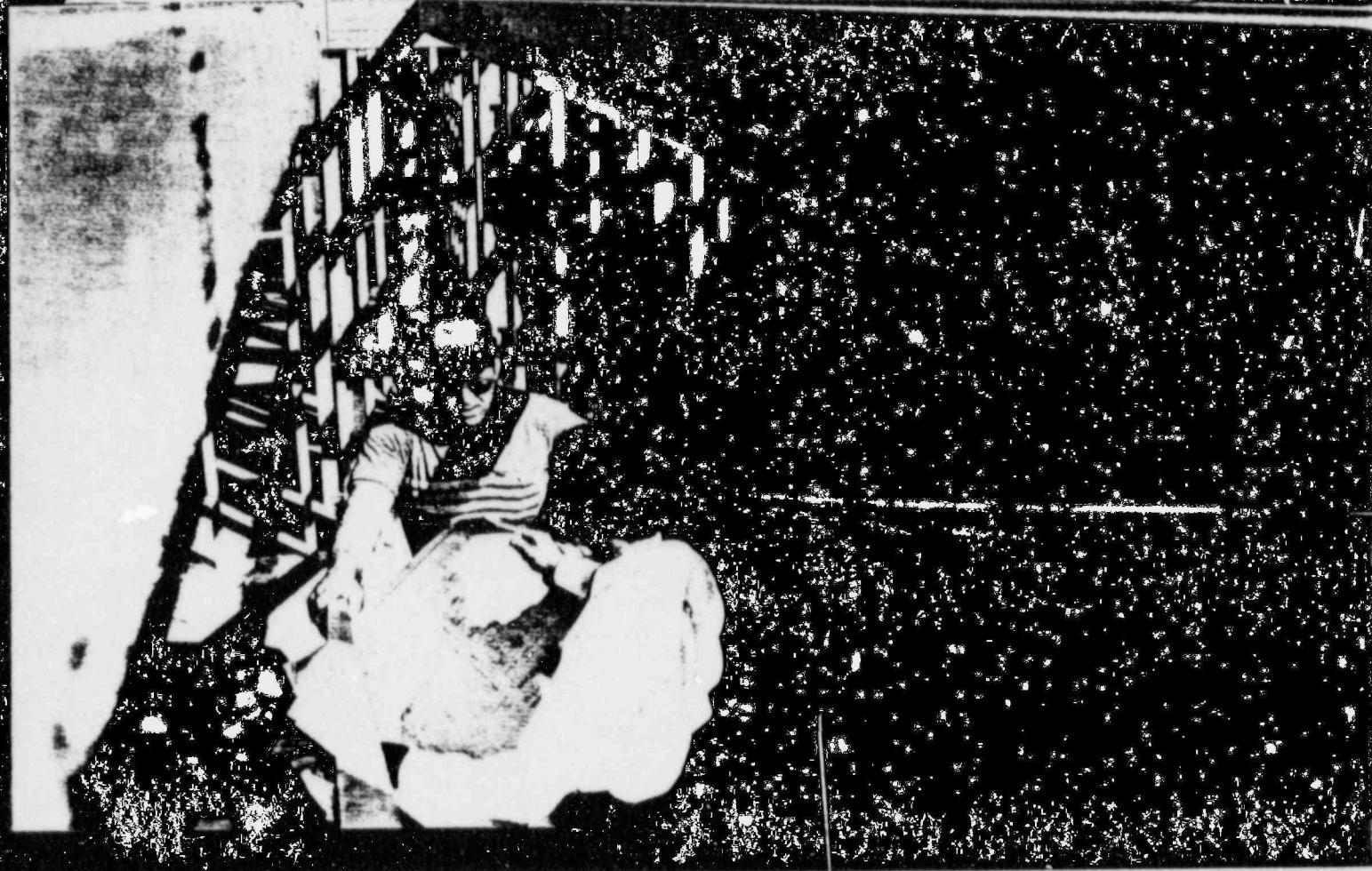
- Continue competitive load sales.
- Minimize load and revenue erosion.
- Promote energy efficiency in all aspects of the marketing effort.
- Encourage off-peak kwh sales to improve system load factor.
- Increase direct customer contact and build business relationships.
- Increase customer knowledge of energy alternatives.
- Encourage and support employee involvement in the marketing program.

In the residential category, the Good Cents program in new homes will continue as the centerpiece of the marketing

With the cooperation of employees in all areas and work groups, sales of security lights were nearly quadruple the marketing goal.

Because of increasing competition, marketing employees are facing greater challenges than ever before.





plan. The Centsable program, a companion to Good Cents that applies to existing residences, will be promoted heavily as a means of compensating for the downturn in the new home market. Heat pumps, another essential element in the residential plan and conservation of energy, will be promoted with the continuation of cash incentives. The Good Cents, Centsable, and heat pump programs all offer significant efficiencies to customers.

During 1987, with the participation of many employees in all areas of the Company, the sales goal of 5,000 installations for security lighting was exceeded by almost four times. These installations will contribute more than 18 million kilowatt-hours to off-peak sales on an annualized basis. That program, along with a new floodlighting program, will be continued in 1988. The Company's

lighting programs are based on the use of high intensity discharge type lighting applications, the most efficient lighting technology available.

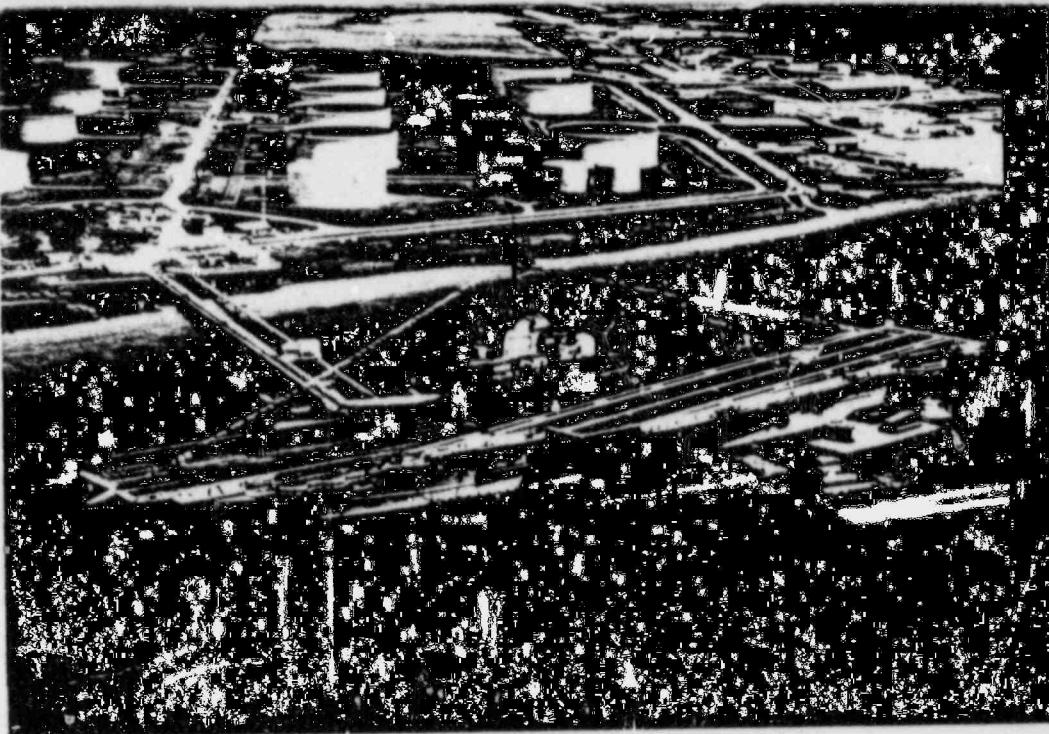
Sales to commercial customers will be encouraged in such applications as food service equipment, heat pumps, and indoor/outdoor lighting. We will continue offering commercial lighting and heating, ventilation and air conditioning design assistance as a means of promoting efficiency.

A new industrial load retention program, identified as Better Thermal Utilization, will provide customers energy cost reduction options through waste heat recovery applications.

Irrigation pumping tests will continue in 1988, and continued agribusiness support will be provided to the communities we serve.

Remodeled homes which earn the CPL Centsable Home Award are highly efficient in terms of energy use.

Ground has been broken for construction of Naval Station Ingleside, the future home of the battleship USS Wisconsin, the aircraft carrier USS Lexington, and several support ships.



Area Concentrates Energies On New Kinds Of Industry

South Texas isn't waiting for oil to come back.

That is not said to discount some credible evidence that the petroleum industry can expect some modest gains in 1988. At the very least there seems to be a consensus that the industry's decline has bottomed out. But there is also a consensus that a recovery will be slow, taking at least the better part of a decade. Encouraging signs include a rise in prices on the natural gas spot market, an increase some forecasters say could be substantial by year's end. Also, refineries and petrochemical companies are operating profitably.

Nevertheless, South Texas communities and economic development agencies are looking elsewhere for future growth. Throughout the area there is a determination to make better use of other existing resources, to promote the multitude of advantages that are available to industry and business, and to compete effectively for industries that have the freedom to choose among a variety of locations.

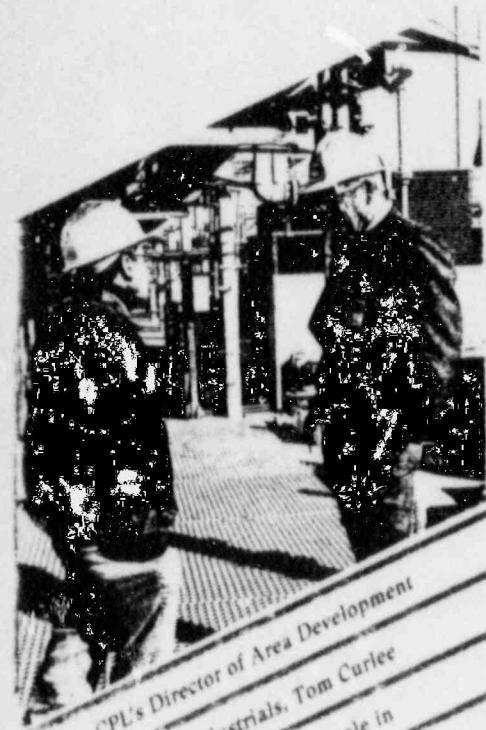
The most prominent example of this competitive spirit is the successful 1985 campaign to win the U.S. Navy's selection of a homeport for the refurbished battleship USS Wisconsin, an aircraft carrier, and several support ships. With the combined support of citizens, local governments, state and national elected officials, business and industry, and many public and private organizations,

the Corpus Christi area's bid prevailed over those of 14 other sites along the Gulf Coast.

Groundbreaking ceremonies for Homeport, now officially named Naval Station Ingleside, were held on February 20, 1988. Completion is expected in 1990. Overall, Naval Station Ingleside is expected to improve the area's economy by \$300 million annually.

In 1987 Occidental Chemical Corporation (Oxychem) purchased the chlor-alkali facilities near Ingleside, which had been previously owned and operated by E. I. du Pont de Nemours & Co. The plant had been shut down in 1986 and was scheduled to be dismantled by year's end. With estimated usage of approximately 100 million kilowatt-hours per month, Oxychem will be CPL's largest customer. The plant was operating again in March 1988. Oxychem has already announced expansion of its newly acquired facilities indicating that a \$40 million ethylene dichloride plant will be constructed and operating by late 1989. Representatives of CPL played a key role in getting this load back on line.

An entirely new kind of industry for South Texas may emerge in the Rio Grande Valley — paper manufacturing. A \$300-million newsprint mill near McAllen is being planned. Raw material for the plant would be kenaf, a hemp-like plant that grows well in the area and can be



CPL's Director of Area Development and Large Industrials, Tom Curlee (right), played a prominent role in arranging Occidental Chemical Corporation's purchase of facilities that had been closed by DuPont.

used as an inexpensive substitute for wood in the paper making process. At Harlingen, General Dynamics will open a manufacturing plant for refurbishing aircraft and electronic systems.

Hilex-Poly Company of Los Angeles has started operations in a factory at Victoria to manufacture grocery and other plastic bags. The firm has already announced expansion plans. Also in Victoria, the New Business Incubator Project has begun operating. It is a public/private coalition aimed at encouraging the development of small firms.

Along the border, growth of maquiladoras, or twin plants, is running at more

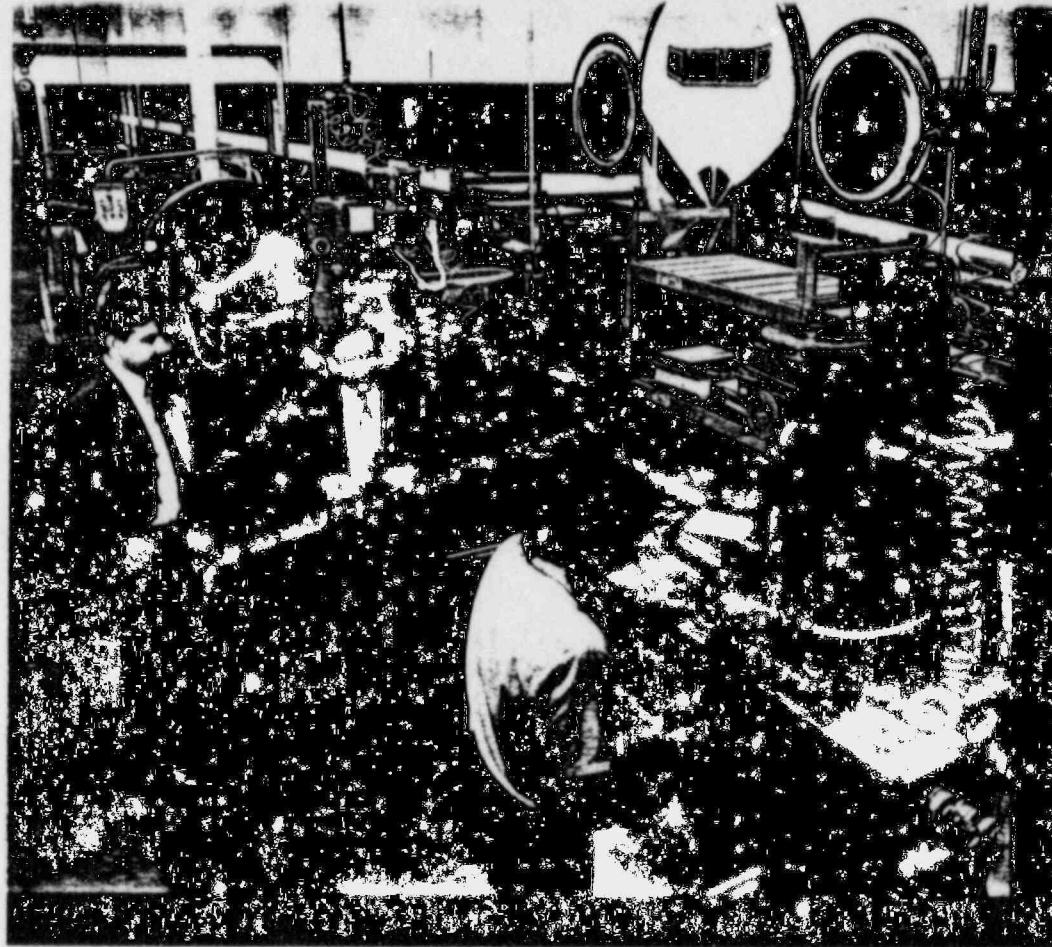
than 10% per year in Mexico. The U. S. Government Accounting Office estimates that 60% of imports from Mexico come through Texas. Laredo is the largest port of entry. The GAO expects continued growth for the maquiladoras, predicting 1,500 plants and a million workers by 1995. That compares with 789 twin plants and 217,000 workers in 1985.

Tourism in all parts of South Texas is expected to continue growing. The Winter Texan business, especially in the Rio Grande Valley, will show gradual increases according to state tourist officials. The Texas State Aquarium, due for groundbreaking in Corpus Christi this year, will be a top tourist attraction.

CPL's area development representatives work with South Texas' communities in their efforts to attract new business and industry.



At Aviall's plant in McAllen, jet engine parts are re-tooled.



The area's agricultural picture is mixed. The cattle business is good, with fair prices expected to continue in 1988. Changes in government programs are turning the cotton market around. Demand is improving and farmers are realizing better returns on their crops. The outlook for grains, however, is not bright. There is a surplus of wheat, corn, and grain

sorghum. The vegetable market is encouraging and the citrus industry is continuing its recovery from the disastrous freeze of 1983.

Other than the oil and gas industry, the poorest performing segments of the South Texas economy are retail trade, banking, and construction.

Reorganization Plan, Early Retirement Lead Productivity Measures

Already among the industry's leaders in terms of its small ratio of employees to customers, CPL took major steps in 1987 to further increase productivity. These steps were taken in recognition of the changing nature of utility operations. We believe our ability to succeed in the emerging era of increased competition and changing regulatory patterns depends on the extent to which we can achieve maximum efficiencies.

In pursuit of that objective, the Company initiated a comprehensive study of the entire organization to determine where changes would produce worthwhile results. The study revealed that certain organization changes could be made that would increase productivity on a per-employee basis and would

create a reduction of 11% in the total number of employees. The study showed this could be done without reducing the quality of service to customers.

A reorganization plan was developed and was announced near the end of the year. Major elements of the reorganization included 1) the consolidation of work units, 2) the resultant elimination of managerial positions, and 3) the reassignment of employees from discontinued positions to those left vacant by early retirements.

As a means of putting the reorganization plan into effect with the least possible hardship on employees, a voluntary early retirement plan was offered to all employees aged 56 or older with at least 15 years of service as of January 1, 1988.

Operating efficiently is largely a matter of Company employees doing a good job every day.

Financing

Retirement Plus, as the plan is called, offered several enhanced benefits. The plan eliminated the pension reductions that normally apply to those who retire before age 62; it used the employee's salary as of December 31, 1987 to calculate pension benefits instead of the usual highest 36-month average pay; and it will pay a supplemental benefit, in addition to the pension, equal to the amount of Social Security offset in the pension formula.

Of the 268 employees eligible for the plan, 236, or 88% elected to accept it. Those who chose to retire under the plan were given the option to choose their own retirement date between January 1 and June 1, 1988.

Commenting on the restructuring, President and Chief Executive T. V. Shockley III, said: "This new organization reflects a streamlined way of doing business that should serve the Company well in the future. A leaner organization will emerge, and we will be better equipped to fulfill our future obligations."

In October the Company issued \$100 million of first mortgage bonds, substantially all of which has been used to pay off short-term loans and finance capital expenditures. The issue was purchased by Kidder, Peabody and Company, Inc., at a coupon rate of 9.75% and a cost to the Company of 10.04%. Due date of the bonds is November 1, 1994.

During the year the Company redeemed the remaining \$15,742,000 of the Series 1982, 15-7/8% debentures due April 1, 2012 and \$230,000 of the Guadalupe Blanco River Authority 1977-A Series, 6% pollution control revenue bonds.

Factoring of unbilled revenue through CSW Credit, Inc., brought in \$43 million on a timely basis at a discount rate lower than rates for short-term borrowing.

On February 17, 1988, the Company accepted pricing terms on \$85 million of Auction Preferred Stock, Series A and Series B, at an initial rate of 5.50%. Proceeds from the stock sales will be used to repay a portion of the Company's short-term debt, which was incurred primarily to pay STP construction costs.

CPL local office employees continue a strong tradition of staying in close touch with community needs and goals.





Outstanding performances by individual employees and work groups help the Company achieve, and sometimes exceed, its goals.

Taking Care of Business

Football is won on the line of scrimmage; business succeeds on the basis of daily performance. Clichés, yes, but still the truth. In an era of increasing competition, it becomes more and more important not only that we shape our organization to meet the coming challenges, but that we also recognize the incalculable contributions of those who, by excelling at their jobs, help the Company achieve higher standards of excellence. We take this space, then, to mention only a few of the many individual employees and work groups who

do their jobs well, who make this a better organization simply by taking care of business.

Larry Banduch, a Serviceman in Kenedy, accounted for 166 security light sales in the Mid Coast District. In addition, he contributed more productive leads for Good Cents Homes and for commercial and food service equipment than any other employee in the district. Larry earned the district's Marketing Pacesetter of the Month Award for five consecutive months.

In Pleasonton, Shirley Lester, a Senior Customer Accounts Clerk, turned in more than 35 heat pump leads to the Winter Garden Marketing Department.

Twenty-one led to sales.

In Corpus Christi, the district's entire residential marketing staff outworked the competition and succeeded at turning the 1987 Parade of Homes into a showcase of electric living. Of the 23 homes entered in the parade, 21 were all-electric and 13 earned the Good Cents award.

When Du Pont shut down a large part of the Ingleside operations in 1986, CPL lost its largest customer. Du Pont was considering selling the plant as scrap metal. But Tom Curlee, Director of Area Development and Large Industrials, started making phone calls. After others had given up on trying to sell the plant intact, Tom found five bidders for it. The winning bidder, Oxychem, will be CPL's largest customer.

The persistence and diligence of two

CPL auditors, Sam Barrett and Jacinta Davenport, saved the Company at least \$1.8 million. They discovered that CPL and the other partners in STP had been unintentionally overbilled for certain plant expenses since 1982. The continuing error had never been discovered by STP's managing partner, by their outside auditor, or by the other partners who were also being overbilled.

Bertha Vargas, Equipment Operator with the Harlingen Underground Crew, sold more than 700 security lights during 1987, mostly on her own time. That was 14% of the goal for the entire Company. Bertha may have been an inspiration to other employees because the goal of 5,000 was eclipsed by actual sales of nearly 20,000.

New Officers And Directors Elected

On June 1, 1987, T. V. Shockley, III, was elected to succeed E. R. Brooks as President and Chief Executive Officer. Mr. Brooks was named to the new position of Executive Vice President of Electric Operations for Central and South West Corporation, CPL's parent company. Mr. Brooks had been the Company's President and Chief Executive Officer since January, 1986. He joined CPL in 1982 after serving more than 20 years in various engineering and management positions and as Vice President and a Director at West Texas Utilities Company, a CSW subsidiary.

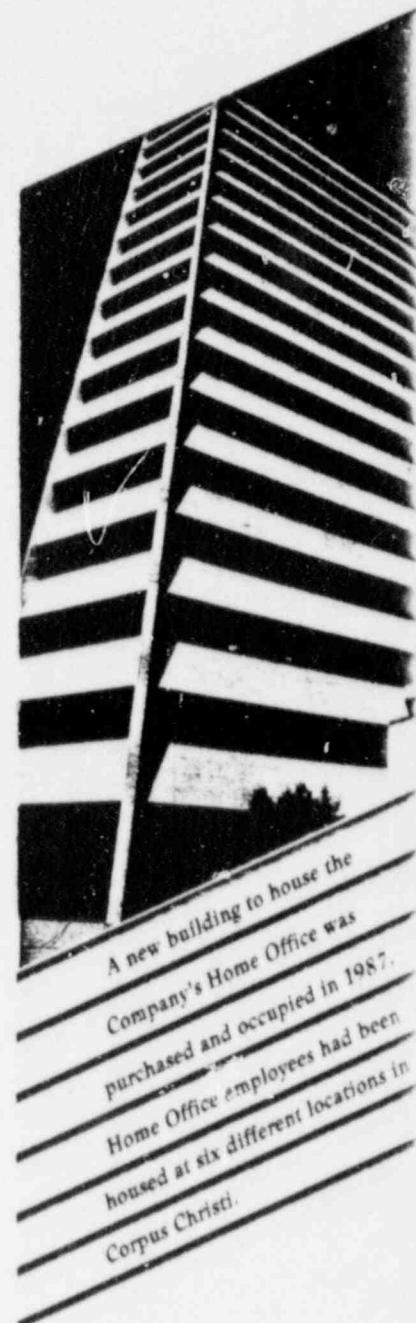
Mr. Shockley has been with CPL for more than 10 years. He worked in several engineering capacities for the Company, and was elected a Director and Chief Engineering Officer on January 14, 1986.

Other changes among Company officers

included the election of Richard P. Verret, Vice President, Power to Vice President and Chief Engineering Officer; the retirement of William C. Price as Vice President, Strategic Planning; the retirement of Florine Gupton as Assistant Secretary; and the election of Mary E. Sullivan as Treasurer to replace Jerry J. Matula, who transferred to a position in operations.

Three new members were elected to the Board of Directors. They are Ronald L. Kellett of Kingsville, a Certified Public Accountant, and Vice President and Controller of the King Ranch; H. Lee Richards of Harlingen, President of Hygeia Dairy Company; President of COHYCO, Inc., and a Director of Harlingen National Bank; and Richard H. Bremer, CPL's Vice President, Finance.

Outgoing Directors were Herbert L. Miller and W. C. Price.



Directors and Officers



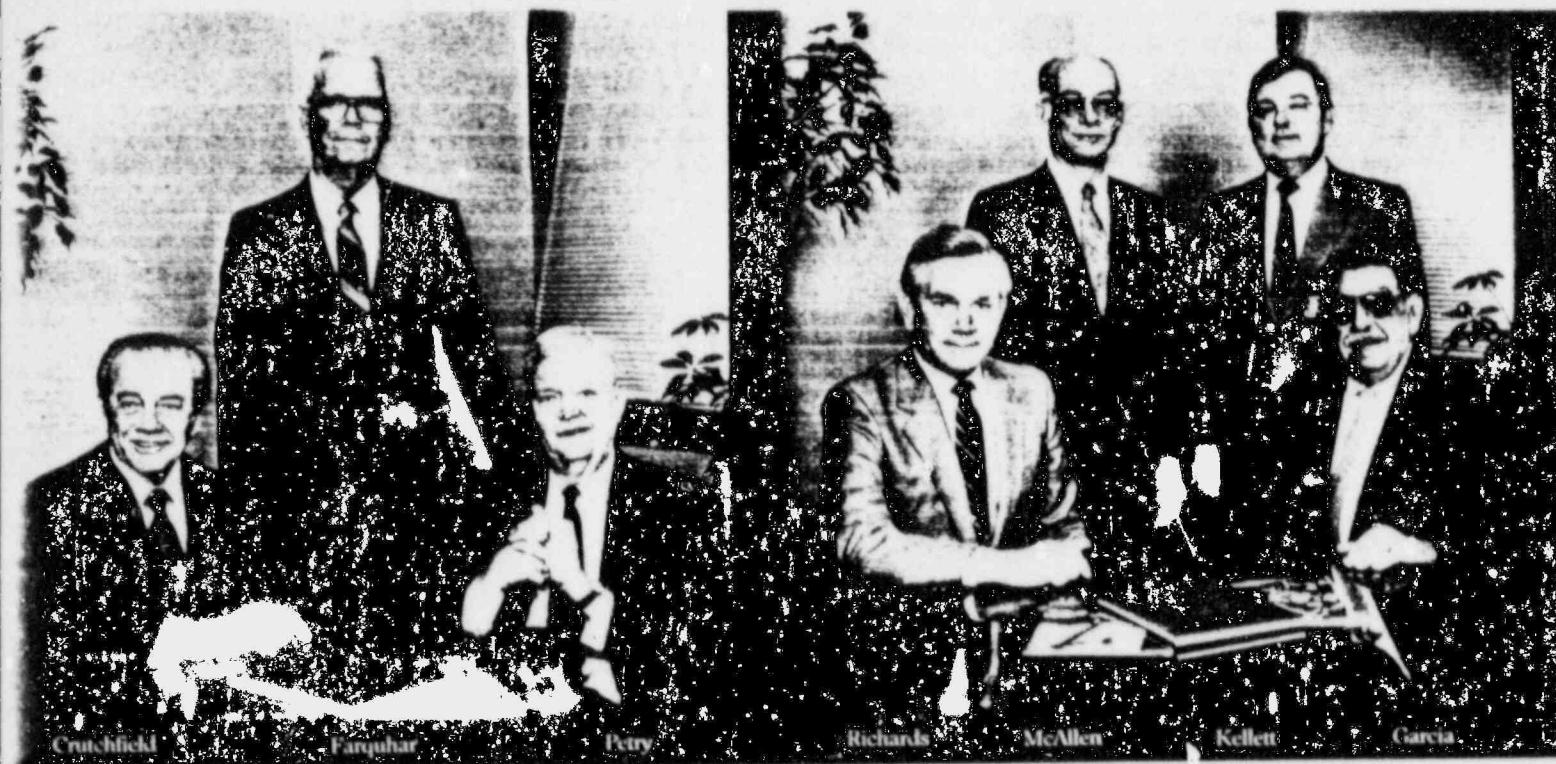
Shockley

Chalker

Bremer

Teague

Range



Crutchfield

Farquhar

Petry

Richards

McAllen

Kellett

Garcia



BOARD OF DIRECTORS

V. Shockley, III
President and Chief Executive Officer,
Central Power and Light Company,
Corpus Christi

Burwood Chalker
Chairman and Chief Executive Officer,
Central and South West Corporation and
Central and South West Services, Inc., Dallas

John W. Crutchfield
President and owner, John W. Crutchfield &
Company, a diversified company,
Corpus Christi

R. Farquhar, Jr.
Retired General Manager, Lavaca-Navidad
River Authority, Edna

Ben M. Garcia
President of manager of several firms
engaged in construction and land
development, Laredo

Robert A. McAllen
Chairman, Texas Valley Bancshares, Inc.,
Dallas

Donald L. Kellert
Vice President and Corporate Controller,
King Ranch, Inc., Kingsville

Lee Richards
President, Hyatt Corp., Hesitation

Albert C. Petry, Jr.
Chairman, Camion Springs

Robert L. Range
Executive Vice President, Central Power and
Light Company, Corpus Christi

B. W. Teague
Chief Vice President, Central Power and
Light Company, Corpus Christi

Richard H. Bremer
President-Finance, Central Power and
Light Company, Corpus Christi

OFFICERS

T. V. Shockley, III
President and Chief Executive Officer

Robert L. Range
Executive Vice President

Richard P. Verret
Vice President and Chief Engineering Officer

B. W. Teague
Senior Vice President, District Operations

Walter A. Ratcliff
Vice President, Corporate Services and
Secretary

Richard H. Bremer
Vice President, Finance

Clayton R. Kirk
Vice President, Customer Services

Gerald W. Tucker
Controller

Mary E. Sullivan
Treasurer

Mary E. Hunt
Assistant Secretary

Jerry J. Matula resigned as Treasurer
February 1, 1987

Florine Gupton retired as Assistant Secretary
June 1, 1987

E. R. Brooks, former President and CEO and
Director assumed duties as Executive Vice
President, Central and South West Corporation
June 1, 1987.

Herbert L. Miller retired as a Director
April 6, 1987

W. C. Price retired as a Director April 6, 1987
and retired as Vice President Strategic Planning
March 1, 1987.

TRANSFER AGENT/ REGISTRAR OF STOCK

**Central and South West
Services, Inc.**
P. O. Box 660164
Dallas, Texas 75266

This report is prepared primarily for the
information of security holders, employees
and customers of the Company and is not
transmitted in connection with the sale of
any security or offer to sell or offer to buy
any security.

Copies of this report and the financial
statements included therein and the
Securities and Exchange Commission
Annual Report on Form 10-K are available
generally to all security holders of the
Company. A copy will be mailed to any
security holder or other interested party
upon written request to Walter A. Ratcliff,
Secretary, P. O. Box 2121, Corpus Christi,
Texas 78403-2121.

Financial Summary

CENTRAL POWER AND LIGHT COMPANY

SUMMARY OF FINANCIAL AND OPERATING STATISTICS

	1987	1986	% CHANGE
FINANCIAL STATISTICS (Thousands)			
Operating Revenues	\$ 768,264	\$ 859,975	(11)%
Fuel and Purchased Power	317,307	397,404	(20)
Other Operating Expenses	220,282	211,630	4
State, Local and Other Taxes	38,177	36,388	5
Federal Income Taxes	50,063	69,087	(28)
Operating Income	142,435	145,466	(2)
Net Income	191,927	174,165	10
OPERATING STATISTICS			
Kilowatt-hour Sales (Thousands)	14,028,160	15,640,017	(10)
System Maximum Demand (Kilowatts)	2,881,000	2,974,000	(3)
Electric Customers (Year-end)	532,546	527,392	1
Average Kilowatt-hour Sales Per Residential Customer	10,369	10,338	—
Average Residential Rate Per Kilowatt-hour	5.90¢	6.22¢	(5)

REPORT OF INDEPENDENT PUBLIC ACCOUNTANTS

To the Stockholders and
Board of Directors of
Central Power and Light Company:

We have examined the balance sheets and statements of capitalization of Central Power and Light Company (a Texas corporation and wholly owned subsidiary of Central and South West Corporation) as of December 31, 1987 and 1986, and the related statements of income, retained earnings and funds provided for gross additions to electric utility plant for each of the three years in the period ended December 31, 1987. Our examinations were made in accordance with generally accepted auditing standards and, accordingly, included such tests of the accounting records and such other

auditing procedures as we considered necessary in the circumstances.

In our opinion, the financial statements referred to above present fairly the financial position of Central Power and Light Company as of December 31, 1987 and 1986, and the results of its operations and funds provided for gross additions to electric utility plant for each of the three years in the period ended December 31, 1987, in conformity with generally accepted accounting principles applied on a consistent basis.

Arthur Andersen & Co.

Dallas, Texas
February 8, 1988

Arthur Andersen & Co.

Financial Review

REPORT OF MANAGEMENT

Management is responsible for the preparation, integrity and objectivity of the financial statements of Central Power and Light Company as well as all other information contained in this Annual Report. The financial statements have been prepared in conformity with generally accepted accounting principles applied on a consistent basis and, in some cases, reflect amounts based on the best estimates and judgments of management, giving due consideration to materiality. Financial information contained elsewhere in this Annual Report is consistent with that in the financial statements.

The Company maintains an adequate system of internal controls to provide reasonable assurance that transactions are executed in accordance with management's authorization, financial statements are prepared in accordance with generally accepted accounting principles and that the assets of the Company are properly safeguarded. The system of internal controls is documented, evaluated and tested by the Company's internal auditors on a continuing basis. No internal control system can provide absolute assurance that errors and irregularities will not occur due to the inherent limitations of the effectiveness of internal controls; however, management strives to maintain a balance recognizing that the cost of such a system should not exceed the benefits derived.

Arthur Andersen & Co. was engaged to examine the financial statements of the Company and issue a

report thereon. Their examination was conducted in accordance with generally accepted auditing standards. Such standards require a review of internal controls, examination of selected transactions and other procedures sufficient to provide reasonable assurance that the financial statements are neither misleading nor contain material errors. No material internal control weaknesses were reported to management by the independent auditors during 1987. The Report of Independent Public Accountants does not limit the responsibility of management for information contained in the financial statements and elsewhere in the Annual Report.

T. V. Shockley, III
President and Chief Executive Officer

Robert L. Range
Executive Vice President

March 10, 1988

REPORT OF AUDIT COMMITTEE

The Audit Committee of the Board of Directors is composed of seven outside directors. The members of the Audit Committee are: H. C. Petry, Jr., Chairman, John W. Crutchfield, Ruben M. Garcia, W. R. Farquhar, Jr., Robert A. McAllen, Ronald L. Kellett and H. Lee Richards. The Committee held two meetings during 1987.

The Audit Committee oversees the Company's financial reporting process on behalf of the Board of Directors. In fulfilling its responsibility, the Committee recommends to the Board of Directors, subject to shareholder approval, the selection of the Company's independent public accountants. The Audit Committee discusses with the internal auditors and

the independent public accountants the overall scope and specific plans for their respective audits. The Committee also discusses the Company's financial statements and the adequacy of internal controls. The Committee meets regularly with the Company's internal auditors and independent public accountants, without management present, to discuss the results of their examinations, their evaluations of internal controls, and the overall quality of the Company's financial reporting. The meetings are designed to facilitate any private communication with the Committee desired by the internal auditors or independent public accountants.

H. C. Petry, Jr.
Chairman, Audit Committee

March 10, 1988

Statements Of Funds Provided For Gross Additions To Electric Utility Plant

CENTRAL POWER AND LIGHT COMPANY

For the Years Ended December 31

	1987	1986	1985
	(thousands)		
Funds Provided from Operations			
Net income	\$191,927	\$174,165	\$152,164
Depreciation	61,752	61,078	58,207
Deferred income taxes	35,477	42,834	40,210
Deferred investment tax credits	14,301	19,748	11,606
Allowance for funds used during construction	(168,877)	(139,937)	(129,158)
Funds Provided from Operations	134,580	157,888	133,029
Less - Dividends	65,820	42,165	102,526
Reinvested Funds Provided from Operations	68,760	45,723	30,503
Funds Provided (Used) By Investors			
Capital contributions from parent company	—	—	70,000
Sale of long-term debt	100,000	260,000	251,700
Sale of preferred stock	—	75,000	—
Retirement of long-term debt	(131)	(10,123)	(116)
Reacquisition of long-term debt	(17,915)	(212,501)	(141,240)
Redemption of preferred stock	—	(42,853)	—
Funds held for pollution control facilities	58,462	19,977	23,950
	140,416	89,500	204,294
Other Funds Provided (Used)			
Advances to from affiliates	44,559	35,323	(38,257)
Unbilled customer accounts sold	35,917	—	—
Fuel refund due customers	(17,161)	13,555	(36,769)
Materials, supplies and fuel inventory	(7,030)	23,569	(2,755)
A accrued interest	6,803	1,648	13,802
Accounts payable	5,289	(25,217)	2,841
Prepayments and other	(5,157)	(3,761)	26,817
Accounts receivable	1,800	(6,908)	45,567
Accrued taxes	(1,359)	23,217	(4,846)
Cash and temporary cash investments	265	48,521	(49,041)
Sale of electric utility plant	—	50,537	—
Settlement on South Texas Project	—	—	146,826
Other	2,744	(2,583)	(12,089)
	66,670	157,901	92,196
Net Additions to Electric Utility Plant	275,846	293,124	326,993
Allowance for funds used during construction	168,877	139,937	129,158
Gross Additions to Electric Utility Plant	\$444,723	\$433,061	\$456,151

The accompanying notes to financial statements are an integral part of these statements.

Statements of Capitalization

CENTRAL POWER AND LIGHT COMPANY

As of December 31		1987	1986
		(thousands)	
COMMON STOCK EQUITY		\$1,159,550	
PREFERRED STOCK		\$1,033,443	
Cumulative \$100 par value, authorized 3,035,000 shares			
Series	Number of Shares Outstanding	Current Redemption Price	
Not subject to mandatory redemption			
4.00%	100,000	\$105.75	10,000
4.20%	75,000	103.75	7,500
7.12%	260,000	108.13	26,000
8.72%	500,000	105.82	50,000
7.98%	750,000	102.00	75,000
Issuance expense		(1,718)	(1,795)
		166,782	166,705
Subject to mandatory redemption			
10.05%	500,000	104.76	50,000
Issuance expense		(792)	(792)
Unamortized redemption costs		(2,548)	(2,853)
		46,660	46,355
LONG-TERM DEBT			
First mortgage bonds			
Series H, 4%, due February 1, 1988		—	12,000
Series I, 4 1/4%, due April 1, 1989		11,000	11,000
Series J, 6 5/8%, due January 1, 1998		28,000	28,000
Series K, 8 1/4%, due January 1, 2000		25,000	25,000
Series L, 7%, due February 1, 2001		36,000	36,000
Series M, 8%, due November 1, 2003		46,000	46,000
Series N, 9 1/8%, due June 1, 2004		40,000	40,000
Series O, 8 1/4%, due October 1, 2007		75,000	75,000
Series P, 8 1/4%, due September 1, 2008		75,000	75,000
Series T, adjustable rate, 9% to December 14, 1989, due December 15, 2014 (net of \$4,768,000 held by trustee in 1986)		111,700	106,932
Series U, 9 1/4%, due July 1, 2015 (net of \$4,606,000 held by trustee in 1986)		81,700	77,094
Series V, 11 1/8%, due August 1, 2015		85,000	85,000
Series W, 8 1/4%, due May 1, 1996		200,000	200,000
Series X, 9 1/4%, due November 1, 1994		100,000	—
Debentures			
Series 1982, 15 1/8%, due April 1, 2012		—	15,742
Series 1985, 12%, due September 1, 2015		85,000	85,000
Installment sales agreements - Pollution control bonds			
7 1/8%, due June 1, 2004		9,825	9,825
6%, due November 1, 2007		34,235	34,465
7 7/8%, due September 15, 2014 (net of \$148,000 held by trustee in 1986)		6,330	6,182
10 1/8%, due October 15, 2014		139,200	139,200
7 7/8%, due December 1, 2016 (net of \$9,920,000 and \$58,860,000 held by trustee)		50,080	1,140
Notes payable, 6 1/2%, due December 8, 1995		1,498	1,637
Unamortized discount		(18,696)	(18,213)
Unamortized costs of reacquired debt		(42,416)	(43,010)
		1,179,456	1,048,987
TOTAL CAPITALIZATION		\$2,552,448	\$2,295,490

The accompanying notes to financial statements are an integral part of these statements.

Notes To Financial Statements

4. PREFERRED STOCK

The dividend on the Company's Money Market Preferred Stock is adjusted every 49 days based on current market rates. The dividend rate averaged 5.16% and 4.62% during 1987 and 1986.

In May 1986, the 10.10% Series Preferred Stock, par value \$100 per share, was called for redemption. The premium and related redemption costs are classified as a reduction to preferred stock on the balance sheet and are being amortized over 10-years.

The Company's 10.05% Series, \$100 par value preferred stock requires a mandatory sinking fund sufficient to retire 35,250 shares in each twelve-month period beginning February 1, 1990 and ending January 1,

2001, and a specified number of shares in each twelve-month period thereafter. The sinking fund, redemption price is \$100 per share.

Each series of the preferred stock is redeemable at the option of the Company upon 30 days notice at the current redemption price per share. Redemption prices of the 7.12%, 8.72% and 10.05% Series decline at specified intervals in future years. The 10.05% Series is not refundable until 1994. The Money Market Preferred may also be redeemed on any dividend payment date at a redemption price of \$100 per share plus accrued dividends.

5. SHORT-TERM AND OTHER FINANCING

The Company, together with other members of the CSW System, has established a System money pool to coordinate short-term borrowings and to make borrowings outside the money pool through the issuance of commercial paper and from banks. In connection therewith, System 24-month bank lines of credit

aggregating \$200,000,000, including the Company's lines-of credit, have been obtained. These lines of credit generally require compensating balances or an annual fee. Short-term cash surpluses transferred to the money pool receive interest income in accordance with the money pool arrangement.

6. BENEFIT PLANS

The Company, together with other members of the CSW System, participates in a non-contributory defined benefit pension plan covering substantially all its employees. Benefits are based on employees' years of service, age at retirement and compensation. The CSW System's funding policy is based on actuarially determined contributions taking into account amounts deductible for income tax purposes and minimum contributions required by the Employee Retirement Income Security Act of 1974, as amended.

The CSW System adopted Statement of Financial Accounting Standards No. 87, Employers' Accounting for Pensions (SFAS 87), during 1987. This change in accounting did not have a material effect on the Company's results of operations or financial condition. Pension costs and related disclosures for the plan in 1986 and 1985 were determined and are presented under the provisions of previous accounting principles.

The components of net pension cost for 1987 are as follows:

	(thousands)
Service cost	\$4,802
Interest cost on projected benefit obligation	9,794
Actual return on assets	(7,235)
Net amortization and deferral	(2,590)
	\$4,771

Assumptions used in the accounting under SFAS 87 were a discount rate of 7.5%, a long-term rate of compensation increase of 6.2% and a return on plan assets of 8.5%.

As of December 31, 1987 and January 1, 1986, the plan's net assets exceeded the total actuarial present value of accumulated benefit obligations. The Company's pension cost accruals were \$5,642,000 and \$5,665,000 for the years 1986 and 1985.

In addition to the pension plan, the Company also participates, with other members of the CSW System, in medical and death benefit plans for substantially all active employees and employees who retire with the CSW System. The Company's cost of providing those benefits was \$6,646,000 in 1987, covering 2,602 active employees and 669 retirees; in 1986, the cost was \$5,958,000, covering 2,671 active employees and 646 retirees; and in 1985, the cost was \$5,929,000, covering 2,630 active employees and 610 retirees.

7. JOINTLY OWNED ELECTRIC UTILITY PLANT

The Company has entered into a participation agreement with three non-affiliated entities covering the construction of the South Texas Project consisting of two nuclear generating units. (Reference is made to Note 8.) The Company also has a joint ownership agreement with other members of the CSW System and non-affiliated entities to provide for the construction and operation of the 665 megawatt, coal-fired Oklaunion Power Station Unit No. 1 (Oklaunion) and its related facilities. Each participant

provides financing for its share of the project which was placed in service in December 1986. The statements of income reflect the Company's portion of the operating costs of the plant. In August 1986, the Company sold 67.6 megawatts, a 10.2% interest in Oklaunion to the Public Utilities Board of the City of Brownsville for approximately \$50.5 million. At December 31, 1987, the Company's participation in the jointly owned plants is shown below:

	South Texas Project	Oklaunion
	(dollars in thousands)	
Plant in service	\$ —	\$35,606
Accumulated depreciation	—	1,171
Plant under construction	1,948,452	—
Plant capacity - Megawatts	2,500	665
Participation	25.2%	7.8%
Share of capacity - Megawatts	630	52

8. LITIGATION AND REGULATORY PROCEEDINGS

SOUTH TEXAS PROJECT

Introduction. The Company owns 25.2% of the South Texas Project (STP) nuclear power plant under construction at a site near Bay City, Texas. In addition to the Company's share, Houston Lighting and Power Company (HLP), the project manager, owns 30.8%; the City of San Antonio (San Antonio) owns 28.0%; and the City of Austin (Austin) owns 16.0%.

Project Cost and Schedule. In September 1987, HLP and Bechtel Energy Corporation, the plant's architect-engineer, presented a completion assessment report for STP to the STP Management Committee. In that report HLP projected that the in-service date of STP Unit 1 would be delayed until February 1988 due to a delay in the receipt of the low-power operating license until August 1987. HLP also estimated the completed cash cost of STP to be approximately \$5.3 billion.

In November 1987, the projected in-service date for Unit 1 was delayed to March 1988, reflecting difficulties encountered with certain equipment during pre-critical testing. Equipment problems identified have been corrected.

The Nuclear Regulatory Commission (NRC), after completing an operational readiness review in January 1988, identified a need for additional operator training, which has been undertaken. Certain delays have postponed HLP's application to the NRC for a full-power license, and while the Company is certain that the plant will not begin commercial operation in March as previously scheduled, the Company does believe that Unit 1 will be in operation prior to its peak load of 1988, assuming that no additional delays are required as a result of any findings from the NRC's current investigation (described below) or as a result of other now unidentified difficulties. The

Company's peak load typically occurs during August of each year. Unit 2 is scheduled for commercial operation in June 1989. The construction permit for Unit 2 expires in December 1989.

The delayed in-service date of STP Unit 1 is not expected to have a significant effect on the estimated cash cost. Assuming an in-service date for Unit 1 of June 1988, the Company's cost of STP, based upon information furnished by HLP, is \$2,246 million, including AFUDC of \$836 million. The estimated total cost, net of related deferred taxes of \$156 million, is \$2,090 million. If the actual in-service date varies from June, the estimated amount of AFUDC would increase or decrease by approximately \$12 million a month, accordingly.

NRC Investigation. The NRC conducted in January 1988 an on-site investigation of allegations made by the Government Accountability Project (GAP), a consumer group, that STP has safety-related defects that have not been reported. Based on the result of this investigation, the NRC will determine whether further investigation is warranted. Although management cannot predict the results of this investigation, the Company believes that any concerns that might have been raised by GAP have been previously investigated and addressed.

Brown & Root Settlement. As the result of litigation filed in December 1981, each of the owners received a pro rata share of \$750 million from Brown & Root, Inc. (Brown & Root), the former architect-engineer and constructor of the project, payable in quarterly payments over seven years, without interest. The Company elected to receive \$146.8 million, the present value of its \$189 million share of the settlement, in December 1985. The amount has been recorded as a reduction in the cost of STP.

Selected Financial Data

The following selected financial data for each of the five years in the period ended December 31, 1987, are

provided to highlight significant trends in the financial condition and results of operations for the Company.

	1987	1986	1985	1984	1983
(In thousands, except ratios)					
Electric Operating Revenues	\$ 768,264	\$ 859,975	\$ 924,908	\$ 972,184	\$ 946,281
Net Income	191,927	174,165	152,164	137,734	121,568
Preferred Stock Dividends	15,820	16,010	15,991	16,005	11,120
Net Income for Common Stock	176,107	158,155	136,173	121,729	110,448
Total Assets	3,341,949	2,950,129	2,723,361	2,455,612	2,129,755
Preferred Stock					
Not Subject to Mandatory Redemption	166,782	166,705	93,115	93,115	93,115
Subject to Mandatory Redemption	46,660	46,355	88,864	88,874	88,909
Long-Term Debt	1,179,456	1,048,987	981,481	866,551	728,149
Ratio of Earnings to Fixed Charges (SEC Method)	3.00	3.16	2.86	3.37	3.52
Capitalization Ratios					
Common Stock Equity	45.4%	45.0%	45.5%	44.8%	44.3%
Preferred Stock	8.4	9.3	8.5	9.6	11.1
Long-Term Debt	46.2	45.7	46.0	45.6	44.6

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

Reference is made to the Financial Statements and related Notes to Financial Statements included on pages 27 to 32 and the Selected Financial Data included on page 33. The information contained therein should be read in conjunction with and is essential in understanding the following discussion and analysis.

REGULATORY MATTERS

Under rules established by the Texas Commission, the Company recovers fuel costs as a fixed component of base rates as discussed in Note 1 of the Notes to Financial Statements. In accordance with this rule, the Company lowered its fuel factor in April 1986 and again in January

1987. In addition, the Company refunded over-recovered fuel costs of \$34 million in January 1987, \$19 million in August 1987 and \$21 million in February 1988, including interest.

In September 1986, the Company filed an application with the FERC for an increase in base rates charged to its wholesale customers. The final order increased rates by \$2.2 million per year through June 1987 and \$1.3 million thereafter. During 1987, the Company received approximately \$1.9 million in rate relief from wholesale customers.

In anticipation of the completion of STP Unit 1, the Company filed with the Texas Commission in June 1987, a petition for approval of deferred accounting treatment of certain costs related to

STP Unit 1. In October 1987, the Company supplemented its filing to include new information on STP available at that time and the effects of Statement of Financial Accounting Standards No. 92 (SFAS 92), Regulated Enterprises - Accounting for Phase-in Plans, an amendment of the Financial Accounting Standards Board (FASB) Statement No. 71. SFAS 92 changed the accounting rules for capitalization of carrying charges associated with deferred accounting orders for financial reporting purposes.

Hearings on the Company's petition have been stayed by order of the Supreme Court of Texas. This order is in response to an appeal of a Texas Commission ruling that denied intervenor status to the Texas State Agencies because they were represented by the Attorney General of Texas. The Supreme Court heard the appeal in December 1987, and a decision is expected during the first half of 1988. All hearings and actions in the deferred accounting filing are suspended until a decision is reached by the Court. In February 1988, the Company filed a motion with the Supreme Court to lift the stay in this proceeding.

The Company's supplemental petition anticipates a total deferral of \$232 million of expenses and carrying charges over an assumed 11-month period between commercial operation and the time rates are placed in effect reflecting Unit 1 in service. Included in this deferral is an \$87 million portion of carrying charges, which the Company has requested be treated as interest to the extent interest has been incurred. The Company estimates that \$26 million of the total carrying charges could not be deferred under SFAS 92 for financial reporting purposes. However, SFAS 92 does not restrict the Texas Commission from allowing the Company to recover all deferred costs related to STP Unit 1, including all carrying charges. This petition would provide for an after-tax effect of \$144 million.

The Company is currently reviewing its options, including alternatives to the deferred accounting petition and phase-in plans, before filing with the Texas Commission for a general rate increase to reflect the effects of STP on its financial position and results of operations. It is expected that new rates reflecting STP Unit 1 in base rates will be in effect during the second quarter of 1989.

In September 1987, the Texas Commission approved the Company's request to reduce rates for its large industrial customers, effective retroactively to August 1987. This reduction is in response to competitive conditions in the energy market in south Texas. Reduced rates will remain in effect only until new rates are determined in the Company's general rate increase filing discussed above. As a condition of receiving the discounted rate, the industrial customers must agree to purchase firm power from the Company until 1991. Through the end of 1987, 10 of the 16 eligible customers have become a part of this program. The annual revenue reduction to the Company is estimated to be \$13 million.

Reference is made to Note 8 of the Notes to Financial Statements for a discussion of current actions by the Texas Commission regarding STP.

CONSTRUCTION PROGRAM

The Company's need for capital results primarily from its construction program which is designed to provide reliable electric service to its customers. During 1987, the Company continued its construction program which is expected to decline during the next three years due to the scheduled completion of STP. It is estimated that construction expenditures during the 1988 through 1990 period will aggregate \$611 million (including AFUDC of \$163 million). This is a decrease of 54% as compared to the three years ended December 31, 1987.

The South Texas Project nuclear plant is expected to account for approximately 49% of the Company's construction expenditures over the next three years. Unit 1 of STP is scheduled to begin commercial operation prior to the summer peak of 1988 and Unit 2 in June 1989. As of January 31, 1988, construction of Unit 1 was complete and Unit 2 was 90% complete. Reference is made to Notes 7 and 8 of the accompanying Notes to Financial Statements. After the completion of STP, no base-load power plants are currently planned until after the year 2000.

Comparative Statistical Record

CENTRAL POWER AND LIGHT COMPANY

	1987	1986	1985
AVERAGE NUMBER OF CUSTOMERS			
Residential	446,548	441,849	432,90
Commercial	70,008	69,719	68,72
Industrial	6,548	6,713	6,82
All other	3,277	3,254	3,26
Total	526,381	521,535	511,72
NUMBER OF CUSTOMERS — END OF PERIOD			
	532,546	527,392	521,28
SALES — KILOWATT-HOURS (Thousands)			
Residential	4,630,356	4,567,961	4,469,88
Commercial	3,736,151	3,734,321	3,664,44
Industrial	4,325,326	5,521,265	5,985,32
All other	1,336,327	1,816,470	1,501,63
Total	14,028,160	15,640,017	15,621,28
REVENUES (Thousands)			
Residential	\$273,223	\$284,345	\$295,038
Commercial	231,004	241,773	252,33
Industrial	198,481	254,626	300,91
All other	65,556	79,231	76,62
Total	\$768,264	\$859,975	\$924,90
RESIDENTIAL AVERAGES			
Kilowatt-hours per customer	10,369	10,338	10,32
Revenues per customer	\$611.86	\$643.53	\$681.53
Revenues per kilowatt-hour	5.90¢	6.22¢	6.60
SYSTEM CAPABILITY AT PEAK (Kilowatts)			
CPL stations	3,698,000	3,703,000	3,688,00
Purchase contracts	—	—	—
Total system	3,698,000	3,703,000	3,688,00
SYSTEM MAXIMUM DEMAND (Kilowatts)			
	2,881,000	2,974,000	3,022,00
FUEL EFFICIENCY DATA			
Average BTU per net KWH	10,164	10,174	10,04
Cost per million BTU	\$2.08	\$2.33	\$2.8
Cost per KWH generated (mills)	21.17	23.70	29.0
BALANCE SHEET DATA (Thousands)			
Electric utility plant	\$3,853,568	\$3,426,969	\$3,056,61
Annual constructed additions	444,723	433,061	456,15
Accumulated depreciation	589,909	546,285	503,40
Percentage of accumulated depreciation to original cost	15.31%	15.94%	16.47
CAPITALIZATION (Thousands)			
Common stock equity	\$1,159,550	\$1,033,443	\$971,44
Preferred stock	213,442	213,060	181,97
Long-term debt	1,179,456	1,048,987	981,481

1984	1983	1982	1981	1980	1979	1978	1977
20,487	407,006	394,437	376,444	361,181	347,746	334,046	322,607
67,217	65,359	63,581	60,386	57,901	56,023	53,768	50,071
6,717	6,652	6,560	6,322	6,014	5,771	5,619	5,434
3,206	3,185	3,174	3,108	3,051	2,981	2,948	2,885
97,627	482,202	467,752	446,260	428,147	412,521	396,381	380,997
07,402	492,712	477,892	459,003	437,438	422,298	406,447	389,875
09,063	3,863,798	3,988,111	3,736,235	3,574,451	3,202,513	3,108,160	2,908,231
52,989	3,268,206	3,278,005	3,085,744	2,884,986	2,723,446	2,640,039	2,517,413
80,810	5,910,999	5,532,386	5,867,785	5,675,723	5,663,115	5,488,879	5,354,236
66,087	1,116,201	1,111,941	1,531,250	1,251,973	1,131,052	1,210,460	847,157
08,949	14,159,204	13,910,443	14,221,014	13,387,133	12,720,126	12,447,538	11,627,037
98,186	\$286,182	\$282,616	\$233,593	\$203,214	\$159,701	\$150,511	\$138,446
55,879	249,255	242,215	202,819	171,047	127,743	119,240	109,870
42,900	336,604	303,933	277,829	234,906	129,017	175,764	164,649
75	74,240	70,422	79,701	60,429	42,125	41,980	28,401
54	\$946,281	\$899,186	\$793,942	\$669,596	\$518,586	\$487,495	\$441,366
10,010	9,493	10,111	9,925	9,897	9,209	9,305	9,015
709.14	\$703.14	\$716.50	\$620.53	\$562.64	\$459.24	\$450.57	\$429.15
7.08c	7.41c	7.09c	5.25c	5.69c	4.99c	4.84c	4.76c
7,000	3,625,000	3,523,000	3,523,000	2,954,000	2,976,000	2,976,000	3,044,000
—	—	—	—	—	10,000	10,000	10,000
7,000	3,625,000	3,523,000	3,523,000	2,954,000	2,986,000	2,986,000	3,054,000
32,000	2,869,000	2,825,000	2,734,000	2,505,000	2,390,000	2,262,000	2,247,000
0.298	10.231	10.236	10.171	10.374	10.262	10.325	10.372
\$3.27	\$3.47	\$3.51	\$3.04	\$2.55	\$2.20	\$2.07	\$1.96
33.65	35.47	35.97	30.93	26.43	22.58	21.39	20.33
8,977	\$2,385,489	\$2,110,440	\$1,880,395	\$1,687,124	\$1,461,916	\$1,241,935	\$1,054,778
6,952	286,524	237,251	199,519	231,858	228,631	195,362	190,209
8,834	418,037	377,738	339,497	301,299	269,212	243,464	221,601
16.63%	17.52%	17.90%	18.05%	17.86%	18.42%	19.60%	21.01%
1,805	\$723,254	\$635,049	\$555,245	\$478,191	\$426,184	\$377,534	\$323,553
1,989	182,024	132,770	132,770	132,796	93,136	43,569	43,569
6,551	728,149	647,404	573,427	509,024	434,590	444,628	369,909



P. O. Box 2121, Corpus Christi, Texas 78403-2121
Address Correction Requested
A Member of the Central and South West System

BULK RATE
U.S. POSTAGE PAID
PERMIT NO. 182
CORPUS CHRISTI, TEXAS 78403

**425 Units
Auction Preferred Stock, Series A**
**425 Units
Auction Preferred Stock, Series B**

Central Power and Light Company

Each Unit Consists of 1,000 Shares of APS
 (\$100 Par Value Per Share)

Central Power and Light Company (the "Company") is offering 425,000 shares of its Auction Preferred Stock, Series A ("Series A") and 425,000 shares of its Auction Preferred Stock, Series B ("Series B") (collectively, the "APS"), each series being issued in Units ("Units"), with each Unit consisting of 1,000 shares of APS. Shares of APS may only be purchased or transferred in whole Units and the shares included in the Units may not be separately purchased or transferred.

Dividends on the APS offered hereby are cumulative from the Date of Original Issue and are payable commencing on April 13, 1988, in the case of Series A, and on April 27, 1988, in the case of Series B, and in each case on each Wednesday that is the last day of successive 49-day periods thereafter, subject to certain exceptions. The dividend rate on shares of APS for the Initial Dividend Period will be 5.50% per annum for Series A and 5.50% per annum for Series B. For each Dividend Period thereafter with respect to each series, the dividend rate will be the Applicable Rate per annum in effect from time to time for such series. The Applicable Rate for each series for each such Dividend Period will be determined on the basis of Orders placed in an Auction conducted on the Business Day preceding the commencement of such Dividend Period, except as set forth below. In each Auction, each Existing Holder will indicate its desire to (i) continue to hold Units of a series without regard to the Applicable Rate that results from such Auction, (ii) continue to hold Units of a series if the Applicable Rate that results from such Auction is equal to or greater than the rate bid by such Existing Holder, and/or (iii) sell Units of a series without regard to the Applicable Rate that results from such Auction. Each Potential Holder will offer to purchase Units of a series if the Applicable Rate that results from such Auction is equal to or greater than the rate bid by such Potential Holder. The Applicable Rate that results from an Auction for any Dividend Period will not be greater than a rate, determined by reference to the credit rating of the shares of APS, that is a percentage of the 60-day "AA" Composite Commercial Paper Rate. Such Maximum Rate may range from 110% to 150% of the 60-day "AA" Composite Commercial Paper Rate. If the Company fails to pay to the Paying Agent the full amount of any dividend or the redemption price of any shares of a series called for redemption on or within three Business Days after the date when due, the Applicable Rate for each Dividend Period thereafter will not be based on the results of an Auction but will instead be equal to 150% of the 60-day "AA" Composite Commercial Paper Rate.

Prospective purchasers should carefully review the Auction Procedures described in this Prospectus, including its Appendices, and should note that (i) a Bid or Sell Order constitutes a commitment to purchase or sell Units of APS based upon the results of an Auction, (ii) Auctions will be conducted through telephone communications and (iii) settlement for purchases and sales will be on the next Business Day following an Auction.

The APS of each series are redeemable, at the option of the Company on any Dividend Payment Date, as a whole or in part, at a redemption price of \$100.000 per Unit (\$100 per share), plus accrued dividends. The shares of APS are redeemable only in whole Units.

Shares of APS may be transferred only in whole Units and only pursuant to a Bid or a Sell Order placed in an Auction, or to or through a Broker-Dealer or to a person that has delivered a signed Master Purchaser's Letter to the Trust Company.

**THESE SECURITIES HAVE NOT BEEN APPROVED OR DISAPPROVED BY THE
SECURITIES AND EXCHANGE COMMISSION NOR HAS THE COMMISSION
PASSED UPON THE ACCURACY OR ADEQUACY OF THIS PROSPECTUS.
ANY REPRESENTATION TO THE CONTRARY IS A CRIMINAL OFFENSE.**

	Initial Public Offering Price	Underwriting Discount(1)	Proceeds to the Company(2)
Per Unit	\$100,000	\$1,500	\$98,500
Total	\$85,000,000	\$1,275,000	\$83,725,000

(1) The Company has agreed to indemnify the Underwriters with respect to certain liabilities, including certain liabilities under the Securities Act of 1933.

(2) Before deducting expenses payable by the Company estimated at \$162,000.

The shares of APS are offered severally by the Underwriters as specified herein, subject to receipt and acceptance by them and subject to the right to reject any order in whole or in part. It is anticipated that delivery of shares of APS to the Underwriters will be made on or about February 24, 1988.

Goldman, Sachs & Co.

Shearson Lehman Hutton Inc.

The date of this prospectus is February 17, 1988.

AVAILABLE INFORMATION

The Company is subject to the informational requirements of the Securities Exchange Act of 1934 (the "Exchange Act") and in accordance therewith files reports and other information with the Securities and Exchange Commission (the "Commission"). Such reports and other information filed by the Company can be inspected and copied at the public reference facilities maintained by the Commission at 450 Fifth Street, N.W., Washington, D.C. 20549; and at the Commission's Regional Offices at Room 1204, Everett McKinley Dirksen Building, 219 South Dearborn Street, Chicago, Illinois and Room 1100, Jacob K. Javits Building, 26 Federal Plaza, New York, New York. Copies of such material can also be obtained at prescribed rates from the Public Reference Section of the Commission at its principal office at 450 Fifth Street, N.W., Washington, D.C. 20549.

This Prospectus constitutes a part of a Registration Statement which the Company has filed with the Commission under the Securities Act of 1933, as amended, with respect to the APS and the Units. The Prospectus omits certain of the information contained in the Registration Statement, and reference is hereby made to the Registration Statement and related exhibits thereto for further information with respect to the Company and the APS and the Units offered hereby. Such additional information can be obtained from the Commission's office in Washington, D.C. Any statements contained herein concerning the provisions of any documents are not necessarily complete, and, in each instance, reference is made to the copy of such document filed as an exhibit to the Registration Statement or otherwise filed with the Commission. Each such statement is qualified in its entirety by such reference.

It is the Company's current practice to prepare and mail to the holders of its Preferred Stock copies of the Company's annual financial reports. Such reports contain certain financial information that is examined and reported upon, with an opinion expressed, by the Company's independent public accountants.

INCORPORATION OF CERTAIN DOCUMENTS BY REFERENCE

The following documents heretofore filed by the Company with the Commission pursuant to the Exchange Act are incorporated by reference in this Prospectus:

1. The Company's Annual Report on Form 10-K for the year ended December 31, 1986.
2. The Company's Quarterly Reports on Form 10-Q for the quarters ended March 31, 1987, June 30, 1987 and September 30, 1987.
3. The Company's Current Reports on Form 8-K filed October 16, 1987 and February 4, 1988.

All documents filed by the Company pursuant to Sections 13(a), 13(c), 14 or 15(d) of the Exchange Act subsequent to the date of this Prospectus and prior to the termination of the offering of the APS and the Units shall be deemed to be incorporated by reference into this Prospectus from their respective dates of filing.

The Company hereby undertakes to provide without charge to each person to whom this Prospectus has been delivered, upon the written or oral request of any such person, a copy of any or all of the foregoing documents incorporated herein by reference (other than exhibits to such documents which are not specifically incorporated by reference into the information that the Registration Statement incorporates). Written or telephone requests should be directed to Mary E. Sullivan, Treasurer, at the Company's principal executive office, 565 North Carancahua Street, Corpus Christi, Texas 78401, telephone (512) 881-5300.

IN CONNECTION WITH THIS OFFERING, THE UNDERWRITERS MAY OVER-ALLOT OR EFFECT TRANSACTIONS WHICH STABILIZE OR MAINTAIN THE MARKET PRICE OF THE SHARES OFFERED HEREBY AT A LEVEL ABOVE THAT WHICH MIGHT OTHERWISE PREVAIL IN THE OPEN MARKET. SUCH STABILIZING, IF COMMENCED, MAY BE DISCONTINUED AT ANY TIME.

SUMMARY

This Summary is qualified in its entirety by the detailed information appearing elsewhere in this Prospectus, including the Appendices hereto. Terms not defined in this Summary are defined elsewhere herein.

The Company

The Company is a public utility engaged in the production, purchase, transmission, distribution and sale of electricity in portions of south Texas. Central and South West Corporation, a registered public utility holding company, owns all of the issued and outstanding Common Stock of the Company.

The Offering

The Company is offering 425,000 shares of Series A and 425,000 shares of Series B in Units, with each Unit consisting of 1,000 shares of APS, at a purchase price of \$100,000 per Unit (\$100 per share). The shares of APS may only be purchased or transferred in whole Units, and the shares included in the Units may not be separately purchased or transferred. All references in the Prospectus to the ownership, purchase, redemption or transfer of, and orders relating to, shares of APS, shall be deemed to refer to shares of APS in whole Units.

Dividends

Dividends on shares of APS offered hereby are cumulative from the Date of Original Issue and are payable, when, as and if declared by the Board of Directors of the Company out of funds legally available therefor, commencing on April 13, 1988, in the case of Series A, and on April 27, 1988, in the case of Series B, and in each case on each Wednesday that is the last day of successive 49-day periods thereafter, subject to certain exceptions. Dividends will be paid through the Securities Depository (The Depository Trust Company or any successor) on each Dividend Payment Date in accordance with its normal procedures, which now provide for it to distribute dividends in next-day funds settled through the New York Clearing House to Agent Members, who in turn are expected to distribute such dividend payments to the persons for whom they are acting as agents.

The dividend rate for the Initial Dividend Period for the APS shall be 5.50% per annum for Series A and 5.50% per annum for Series B. For each Dividend Period thereafter, the dividend rate for the APS will be the Applicable Rate per annum that the Trust Company (Bankers Trust Company or any successor) advises the Company results from an Auction relating to that particular series, unless the Company fails to pay to the Paying Agent on or within three Business Days after the date when due the full amount of any dividend or the redemption price of any shares of such series called for redemption. In such event, Auctions for such series will be discontinued and the Applicable Rate for the series for each Dividend Period thereafter will be equal to 150% of the 60-day "AA" Composite Commercial Paper Rate. The Maximum Rate that results from an Auction will not be greater than the percentage of the 60-day "AA" Composite Commercial Paper Rate (at the close of business on the Business Day immediately preceding the Auction Date) determined as set forth below based on the prevailing rating (as defined under "The Auction—Orders by Existing Holders and Potential Holders") in effect at the close of business on such Business Day:

<u>Prevailing Rating</u>	<u>Percentage</u>
AA/aa or Above	110%
A/a	120%
BBB/Baa	130%
Below BBB/baa	150%

Auction Procedures

On each Auction Date with respect to a Dividend Period (the Business Day, usually a Tuesday prior to the beginning of each Dividend Period after the Initial Dividend Period), each Existing Holder may submit Orders through a Broker-Dealer to the Trust Company as follows:

- Hold Order—indicating its desire to hold without regard to the Applicable Rate for the next Dividend Period.
- Bid—indicating its desire to hold if the Applicable Rate for the next Dividend Period is not less than the rate specified in such Bid.
- Sell Order—indicating its desire to sell without regard to the Applicable Rate for the next Dividend Period.

All Orders by Existing Holders and Potential Holders must specify numbers of shares of APS in whole Units. Any Order that specifies a number of shares of APS other than in whole Units will not be accepted and will not be considered a Submitted Order for purposes of an Auction.

An Existing Holder may submit different types of Orders in an Auction with respect to shares of each series of APS then held by such Existing Holder. An Existing Holder that offers to purchase additional shares of APS is, for purposes of such offer, treated as a Potential Holder as described below. Bids by Existing Holders with rates higher than the Maximum Rate on the Auction Date will be treated as Sell Orders. A Hold Order will be deemed to have been submitted on behalf of an Existing Holder if an Order is not submitted on behalf of such Existing Holder for any reason, including the failure of a Broker-Dealer to submit such Existing Holder's Order to the Trust Company.

Potential Holders of shares of APS of any series may submit Bids in which they will offer to purchase shares of such series of APS if the Applicable Rate for the next Dividend Period is not less than the rate specified in such Bid. A Bid by a Potential Holder specifying a rate higher than the Maximum Rate will not be accepted.

If Sufficient Clearing Bids exist (that is, the number of shares of APS of a particular series subject to Bids by Potential Holders with rates equal to or lower than the Maximum Rate is at least equal to the number of shares of APS of such series subject to Sell Orders by Existing Holders), the Applicable Rate for such series will be the lowest rate specified in the Submitted Bids which, taking into account such rate and all lower rates bid by Existing Holders and Potential Holders, would result in Existing Holders and Potential Holders owning all of the shares of APS available for purchase in the Auction. If Sufficient Clearing Bids do not exist, the Applicable Rate for such series will be the Maximum Rate on the Auction Date, and, in such event, Existing Holders that have submitted Sell Orders will be able to sell in the Auction none or only a portion of the Units of APS subject to such Sell Orders. If all Existing Holders submit Hold Orders or are deemed to have submitted Hold Orders, the Applicable Rate will be 58% of the 60-day "AA" Composite Commercial Paper Rate.

The Auction Procedures include a pro rata allocation of Units for purchase and sale, which may result in an Existing Holder continuing to hold or selling, or a Potential Holder purchasing, a number of Units of APS that is fewer than the number of Units of APS specified in its Order.

A Bid placed by an Existing Holder specifying a rate greater than the Applicable Rate determined in the Auction or a Sell Order shall constitute an irrevocable offer to sell the shares of APS subject thereto, in each case at a price per Unit of \$100,000 (\$100 per share). A Bid placed by a Potential Holder shall constitute an irrevocable offer to purchase the shares of APS subject thereto at a price per Unit of \$100,000 (\$100 per share) if the rate specified in such Bid is less than or equal to the rate determined in the Auction. Settlement of purchases and sales will be made on the next Business Day (also a Dividend Payment Date) after the

Auction Date through the Securities Depository. Purchasers will make payment on such date through their Agent Members in next-day funds settled through the New York Clearing House to the Securities Depository against delivery to their respective Agent Members. The Securities Depository will make payment to the sellers' Agent Members in accordance with the Securities Depository's normal procedures, which now provide for payment against delivery by their Agent Members in next-day funds settled through the New York Clearing House.

Redemption

The shares of APS of each series are redeemable at the option of the Company, as a whole or in part, on any Dividend Payment Date at \$100.000 per Unit (\$100 per share), plus accrued dividends. The shares of APS are redeemable only in whole Units.

Liquidation Preference

The liquidation preference of the APS of each series shall be \$100.000 per Unit (\$100 per share), plus accrued dividends.

Voting Rights

The holders of outstanding shares of APS of each series do not have any voting rights, except as expressly provided in the Articles and summarized under "Description of APS—Voting Rights" and except as required by law.

Master Purchaser's Letter

Each prospective purchaser of shares of APS will be required to sign and deliver a Master Purchaser's Letter, in the form of Appendix C hereto, to a Broker-Dealer (who will deliver copies thereof to the Trust Company) pursuant to which each prospective purchaser will agree, among other things, that so long as the Company has not failed to pay to the Paying Agent the full amount of any dividend or the redemption price, plus accrued and unpaid dividends, of any shares of APS called for redemption on or within three Business Days after the date when due (i) shares of APS may be transferred only pursuant to a Bid or Sell Order placed in an Auction, or to or through a Broker-Dealer or to a person that has delivered, or caused to be delivered on its behalf, a signed copy of a Master Purchaser's Letter to the Trust Company, provided that in the case of all transfers other than those pursuant to Auctions, the Existing Holder of the shares so transferred, its Agent Member or its Broker-Dealer advises the Trust Company of such transfer and (ii) ownership of shares of APS will be maintained in book entry form by the Securities Depository for the account of such prospective purchaser's Agent Member, which in turn will maintain records of such prospective purchaser's beneficial ownership. An execution copy of the Master Purchaser's Letter is included inside the back cover of this Prospectus.

Execution of a Master Purchaser's Letter is not a commitment to purchase shares of APS in the offering made by this Prospectus or in any Auction, but is a condition precedent to purchasing shares of APS.

THE COMPANY

Central Power and Light Company (the "Company"), a Texas corporation, is a public utility engaged in the production, purchase, transmission, distribution and sale of electricity in portions of south Texas. Central and South West Corporation, a registered public utility holding company, owns all of the issued and outstanding Common Stock of the Company.

Ratio of Earnings to Combined Fixed Charges and Preferred Stock Dividends

Twelve Months Ended September 30, 1987 (Unaudited)	Year Ended December 31				
	1986	1985	1984	1983	1982
2.64	2.61	2.39	2.64	2.05	2.81

For computation of the ratio: (i) earnings consist of net income plus fixed charges, federal income taxes, deferred income taxes and investment tax credits; (ii) fixed charges consist of interest on long term debt, other interest charges, the interest component of leases and amortization of debt discount, premium and expense; and (iii) preferred dividends consist of an amount equal to the pre-income tax earnings necessary to cover the preferred dividend requirements.

USE OF PROCEEDS

The net proceeds from the sale of the shares of APS offered hereby will be used by the Company to repay a portion of its outstanding short-term borrowings incurred and expected to be incurred primarily to finance construction expenditures of the Company and for other corporate purposes. Such borrowings incurred by the Company primarily to finance construction expenditures amounted to approximately \$42,400,000 at December 31, 1987.

The Company's capital expenditures for 1988-1989, including allowance for funds used during construction ("AFUDC"), are estimated \$236,000,000 and \$178,000,000, respectively. The Company anticipates that approximately 70% (including AFUDC) and 55% (excluding AFUDC) of the funds required for its 1988-1989 construction program will be provided from internal sources and pollution control revenue bond proceeds held by a trustee. These estimates are subject to change due to numerous factors including escalation of construction costs, licensing delays, adequacy and timeliness of rate relief and the ability to raise necessary capital.

THE AUCTION

General

Dividends on each series of APS will be payable, when, as and if declared by the Board of Directors of the Company out of funds legally available therefor, on each Dividend Payment Date with respect to a Dividend Period then ending (in the case of the Initial Dividend Period, the period ending on April 13, 1988, in the case of Series A, and the period ending on April 27, 1988, in the case of Series B, and in the case of each Subsequent Dividend Period thereafter, a period of 49 days, subject to certain exceptions as set forth under "Description of APS—Dividends—General") at the rate per share equal to the Applicable Rate per annum for each such Dividend Period. For definitions of the terms "Dividend Payment Date," "Dividend Period," "Initial Dividend Period," "Subsequent Dividend Period" and "Applicable Rate," see "Description of APS—Dividends—General" and "Description of APS—Dividends—Determination of Dividend Rate."

The proposed forms of Statements of Resolution Establishing Series of Shares (the "Statements of Resolution") authorizing the issuance of Series A and Series B offered hereby provide that the Applicable Rate per annum for each Dividend Period after the Initial Dividend Period shall be equal to the rate per

annum that the Trust Company (as defined under "Trust Company Agreement" below) advises has resulted on the Business Day preceding the first day of such Dividend Period from implementation of the auction procedures (the "Auction Procedures") set forth in the Statements of Resolution, in which persons determine to hold or offer to sell or, based on dividend rates bid by them, offer to purchase or sell shares of APS of each series. Each periodic implementation of the Auction Procedures, which are attached as Appendix A to this Prospectus, is referred to as an "Auction." However, if with respect to any series of APS the Company shall have failed to pay to the Paying Agent the full amount of any dividend for such series, or the redemption price of any shares of such series after it has given notice of redemption, on or within three Business Days after the date when due. Auctions will be discontinued with respect to such series and the Applicable Rate for such series for each Dividend Period thereafter will instead be 150% of the 60-Day "AA" Composite Commercial Paper Rate.

Trust Company Agreement. The Company will enter into an agreement (the "Trust Company Agreement") with Bankers Trust Company (together with any successor bank or trust company or other entity entering into a similar agreement with the Company, the "Trust Company") which provides, among other things, that the Trust Company will follow the Auction Procedures for the purposes of determining the Applicable Rate for each series of APS so long as the Applicable Rate for such series is to be based on the results of an Auction.

Broker-Dealer Agreements. Each Auction requires the participation of one or more broker-dealers. The Trust Company will enter into an agreement with each of Goldman, Sachs & Co. and Shearson Lehman Commercial Paper Inc. and may enter into similar agreements (collectively, the "Broker-Dealer Agreements") with one or more additional broker-dealers (collectively, the "Broker-Dealers") selected by the Company which provide for the participation of Broker-Dealers in Auctions.

Master Purchaser's Letter. Each prospective purchaser of shares of APS will be required to sign and deliver to the Trust Company, as a condition to purchasing Units of APS in any Auction or otherwise, a Master Purchaser's Letter, an execution copy of which is attached to this Prospectus as Appendix C (the "Master Purchaser's Letter"), in which such prospective purchaser will agree that shares of APS may only be purchased or transferred as whole Units and the shares included in the Units may not be separately purchased or transferred, and will further agree, among other things, that so long as the Company has not failed to pay to the Paying Agent the full amount of any dividend for a series of APS or the redemption price of any shares of a series of APS called for redemption on or within three Business Days after the date when due,

(a) to participate in Auctions with respect to such series on the terms set forth in Appendix A

(b) to sell, transfer or otherwise dispose of shares of such series of APS only pursuant to a Bid or a Sell Order (as defined under "Orders by Existing Holders and Potential Holders" below) in an Auction, or to or through a Broker-Dealer or to a person that has delivered a signed Master Purchaser's Letter to the Trust Company, provided that in the case of all transfers other than those pursuant to Auctions, the Existing Holder (as defined below) of the shares so transferred, its Agent Member (as defined below) or its Broker-Dealer advises the Trust Company of such transfer; and

(c) to have the ownership of the shares of such series of APS as to which such purchaser is the Existing Holder maintained in book entry form by The Depository Trust Company ("DTC," together with any successor securities depository selected by the Company, the "Securities Depository") for the account of its Agent Member (the "Agent Member") of such Securities Depository, which in turn will maintain records of such purchaser's beneficial ownership and to authorize such Agent Member to disclose to the Trust Company such information with respect to such purchaser's beneficial ownership as the Trust Company may request.

An Execution copy of the Master Purchaser's Letter must be delivered to a Broker-Dealer, who will deliver copies thereof to the Trust Company. Execution of a Master Purchaser's Letter is not a commitment to purchase shares of APS in the offering being made by this Prospectus or in any Auction, but is a condition precedent to purchasing shares of APS.

As used herein, "Existing Holder" of Units of APS means a person who has signed a Master Purchaser's Letter and is listed as the beneficial owner of such Units of APS in the records of the Trust Company. The Trust Company may rely upon, as evidence of the identities of the Existing Holders, a list of the initial owners of the Units of APS provided by the Company, the results of Auctions and notices from any Existing Holder, the Agent Member of any Existing Holder or the Broker-Dealer of any Existing Holder with respect to such Existing Holder's transfer of Units of APS to another person. The Trust Company shall be required to register a transfer of Units of APS from an Existing Holder to another person only if such transfer is made to a person that has delivered a signed Master Purchaser's Letter to the Trust Company and if (i) such transfer is pursuant to an Auction or (ii) the Trust Company has been notified in writing (A) by such Existing Holder, the Agent Member of such Existing Holder or the Broker-Dealer of such Existing Holder of such transfer or (B) by the Broker-Dealer of any person that purchased or sold such Units of APS in an Auction of the failure of such Units of APS to be transferred as a result of such Auction. The Trust Company is not required to accept any such notice for an Auction unless it is received by the Trust Company by 3:00 P.M., New York City time, on the Business Day preceding such Auction.

The Trust Company is not required to accept the Master Purchaser's Letter of any Potential Holder who wishes to submit a Bid for the first time in an Auction or of any Potential Holder or Existing Holder who wishes to amend its Master Purchaser's Letter unless it is received by the Trust Company by 3:00 P.M., New York City time, on the Business Day preceding such Auction.

Securities Depository. DTC will act as Securities Depository for the Agent Members with respect to shares of APS. One certificate for all of the shares of APS of each series offered hereby will be registered in the name of Cede & Co. ("Cede"), as nominee of the Securities Depository. Such certificate will bear a legend to the effect that such certificate is issued subject to the provisions restricting transfers of shares of APS contained in the Statement of Resolution for such series and the Master Purchaser's Letters. The Company will also issue stop-transfer instructions to the transfer agent for each series of APS. For the Initial Dividend Period and so long as the Applicable Rate for a series is based upon the results of an Auction, Cede will be the holder of record of all shares of APS of such series, and Existing Holders of shares of APS of such series will not receive certificates representing their ownership interest in such shares. If the Applicable Rate for a series becomes 150% of the 60-day "AA" Composite Commercial Paper Rate, as defined and set forth under "Description of APS—Dividends—Determination of Dividend Rate," as a result of a failure to pay a dividend amount or redemption price on or within three Business Days after the date when due, an Existing Holder may obtain a certificate for the shares of APS of such series owned by it.

DTC, which is a New York-chartered limited purpose trust company, performs services for its participants (including the Agent Members), some of whom (and/or their representatives) own DTC. DTC maintains lists of its participants and will maintain the positions (ownership interests) held by each Agent Member in shares of APS, whether as an Existing Holder for its own account or as a nominee for another Existing Holder.

The following is a brief summary of the procedures to be used in conducting Auctions. Separate Auctions will be conducted with respect to each series of APS. This summary is qualified by reference to the Auction Procedures. The settlement procedures to be used with respect to Auctions are set forth in Appendix B hereto.

Auction Dates

An Auction to determine the Applicable Rate with respect to each series of the APS for each Dividend Period after the Initial Dividend Period therefor will be held on the first Business Day (as hereinafter

defined) preceding the first day of such Dividend Period (the date of each Auction being referred to herein as an "Auction Date"). The first Auction for the APS will be held on April 12, 1988, in the case of Series A, and on April 26, 1988, in the case of Series B, each of which is the Business Day preceding the Dividend Payment Date for the Initial Dividend Period for that series (see "Description of APS—Dividends"). Thereafter, Auctions for each series will normally be held every seventh Tuesday after the preceding Auction Date, and each Subsequent Dividend Period will normally begin on the following Wednesday. The Auction Date and the Dividend Payment Date (both of which must be Business Days) need not be consecutive days. "Business Day" means a day on which the New York Stock Exchange is open for trading and banks in New York City are not authorized by law to close. See "Description of APS—Dividends—General" for information concerning the circumstances under which the Dividend Payment Date or the Auction Date, or both, may be moved to a date other than such Wednesday and Tuesday, respectively. For example, in most cases if the Tuesday that would normally be an Auction Date is not a Business Day, then the Auction Date will be the preceding Monday if such Monday is a Business Day or, if such Monday is not a Business Day, then the Auction Date will be on a Business Day following such Tuesday.

It is anticipated that Auctions to determine the Applicable Rate for the shares of APS of each series for Dividend Periods after the Initial Dividend Period will be held during the next two years on the dates set forth below. Except for November 20, 1989, all of such days are Tuesdays.

<u>Auction Date for Series A</u>	<u>Auction Date for Series B</u>
April 12, 1988	April 26, 1988
May 31, 1988	June 14, 1988
July 19, 1988	August 2, 1988
September 6, 1988	September 20, 1988
October 25, 1988	November 8, 1988
December 13, 1988	December 27, 1988
January 31, 1989	February 14, 1989
March 21, 1989	April 4, 1989
May 9, 1989	May 23, 1989
June 27, 1989	July 11, 1989
August 15, 1989	August 29, 1989
October 3, 1989	October 17, 1989
November 20, 1989	December 5, 1989
January 9, 1990	January 23, 1990

Orders by Existing Holders and Potential Holders

On or prior to the Submission Deadline (as defined under "Submission of Orders by Broker-Dealers to Trust Company" below) on each Auction Date with respect to a series of APS:

(a) each Existing Holder may submit to a Broker by telephone or otherwise a:

(i) Hold Order—specifying the number of outstanding Units of such series, if any, that such Existing Holder desires to continue to hold without regard to the Applicable Rate for the next Dividend Period;

(ii) Bid—specifying the number of outstanding Units of such series, if any, of APS that such Existing Holder desires to continue to hold if the Applicable Rate for the next Dividend Period shall not be less than the rate per annum then specified by such Existing Holder; and/or

(iii) Sell Order—specifying the number of outstanding Units of such series, if any, of APS that such Existing Holder offers to sell without regard to the Applicable Rate for the next Dividend Period; and

(b) Broker-Dealers shall contact prospective purchasers of Units of APS of such series (each such prospective purchaser is herein referred to as a "Potential Holder," and the term Potential Holder includes an Existing Holder with respect to an offer by such Existing Holder to purchase additional Units of such series) by telephone or otherwise to determine whether such Potential Holders desire to

submit Bids, in which such Potential Holders will indicate the number of Units of APS of such series that they offer to purchase if the Applicable Rate for the next Dividend Period is not less than the rate per annum specified in such Bids.

The communication to a Broker-Dealer of the foregoing information is herein referred to as an "Order" and collectively as "Orders." An Existing Holder or a Potential Holder placing an Order is herein referred to as a "Bidder" and collectively as "Bidders."

All Orders by Existing Holders and Potential Holders must specify numbers of shares of APS in whole Units.

An Existing Holder may submit different types of Orders in an Auction with respect to the different Units of a series of APS then held by such Existing Holder. An Existing Holder that offers to purchase additional Units of APS of such series is, for purposes of such offer, treated as a Potential Holder. For information concerning the priority given to different types of Orders placed by Existing Holders, see "Submission of Orders by Broker-Dealers to Trust Company" below.

Any Bid specifying a rate higher than the Maximum Rate (as defined below) will (i) be treated as a Sell Order if submitted by an Existing Holder and (ii) not be accepted if submitted by a Potential Holder. Accordingly, the Auction Procedures establish the Maximum Rate as the maximum rate per annum that can result from an Auction. See "Determination of Sufficient Clearing Bids, Winning Bid Rate and Applicable Rate" and "Acceptance and Rejection of Submitted Bids and Submitted Sell Orders and Allocation of Shares" below.

As used herein, "Maximum Rate," when used with respect to shares of a series of APS on an Auction Date, means the percentage of the "AA" Composite Commercial Paper Rate (as defined under "Description of APS—Dividends"), as announced on such Auction Date for the preceding Business Day, determined as set forth below, based on the prevailing rating of shares of such series of APS in effect at the close of business on such Business Day:

<u>Prevailing Rating*</u>	<u>Percentage</u>
AA/aa or Above	110%
A/a	120%
BBB/baa	130%
Below BBB/baa	150%

* In the case of a split rating, the Maximum Rate will be determined on the basis of the lower rating. For example, a rating of A+/aa3 would result in a Maximum Rate of 120% of the 60-Day "AA" Composite Commercial Paper Rate.

For purposes of this definition, the "prevailing rating" of Units of a series of APS shall be (i) AA/aa or Above if the shares of such series of APS have ratings of both AA- or better by Standard & Poor's Corporation or its successor ("S&P") and aa3 or better by Moody's Investors Service, Inc. or its successor ("Moody's"), or the equivalent of both of such ratings by such agencies or a substitute rating agency or substitute rating agencies selected as provided below, (ii) if not AA/aa or Above, then A/a if the shares of such series of APS have ratings of both A- or better by S&P and a3 or better by Moody's or the equivalent of both of such ratings by such agencies or a substitute rating agency or substitute rating agencies selected as provided below, (iii) if not AA/aa or Above or A/a, then BBB/baa if the shares of such series of APS have ratings of both BBB- or better by S&P and baa3 or better by Moody's or the equivalent of both of such ratings by such agencies or a substitute rating agency or substitute rating agencies selected as provided below, and (iv) if not AA/aa or Above, A/a or BBB/baa, then Below BBB/baa. The Company shall take all reasonable action necessary to enable S&P and Moody's to provide a rating for each series of APS. If either S&P or Moody's shall not make such a rating available, or neither S&P nor Moody's shall make such a rating available, Goldman, Sachs & Co. or its successor shall select a nationally recognized statistical rating organization (as that term is used in the rules and regulations of the Commission under the Exchange Act) or two nationally recognized statistical rating organizations to act as substitute rating agency or substitute

rating agencies, as the case may be, and the Company shall take all reasonable action to enable such rating agency or rating agencies to provide a rating or ratings for each series of APS.

The Master Purchaser's Letter to be signed by each Existing Holder and each Potential Holder provides that (i) a Sell Order placed by an Existing Holder shall constitute an irrevocable offer to sell the Units subject thereto, (ii) a Bid placed by an Existing Holder shall constitute an irrevocable offer to sell the Units subject thereto if the rate specified in such Bid is greater than the rate determined in the Auction, and (iii) a Bid placed by a Potential Holder shall constitute an irrevocable offer to purchase the number of Units specified in such Bid if the rate specified in the Bid is less than or equal to the rate determined in the Auction. The number of Units purchased or sold may be subject to proration procedures. See "Acceptance and Rejection of Submitted Bids and Submitted Sell Orders and Allocation of Shares" below. Each purchase or sale shall be made for settlement on the Business Day next succeeding the Auction Date at a price per Unit equal to \$100,000 (\$100 per share). See "Notification of Results; Settlement" below. The Trust Company is entitled to rely upon the terms of any Order submitted to it by a Broker-Dealer.

If an Order or Orders covering all of the outstanding Units of the series of APS to which the Auction relates held by an Existing Holder is or are not submitted to the Trust Company prior to the Submission Deadline, either because a Broker-Dealer failed to contact such Existing Holder or otherwise, the Trust Company shall deem a Hold Order to have been submitted on behalf of such Existing Holder covering the number of outstanding Units of APS of such series held by such Existing Holder and not subject to Orders submitted to the Trust Company.

Neither the Company nor any affiliate thereof may submit an Order in any Auction except as set forth in the next sentence. Any Broker-Dealer that is an affiliate of the Company may submit Orders in Auctions but only if such Orders are not for its own account, except that if such affiliated Broker-Dealer holds shares for its own account, it must submit a Sell Order in the next Auction with respect to such shares.

Submission of Orders by Broker-Dealers to Trust Company

Prior to 1:00 P.M., New York City time, on each Auction Date, or such time on the Auction Date specified by the Trust Company (the "Submission Deadline"), each Broker-Dealer will submit to the Trust Company in writing all Orders obtained by it for the Auction to be conducted on such Auction Date.

If any rate specified in any Bid contains more than three figures to the right of the decimal point, the Trust Company shall round such rate up to the next highest one-thousandth (.001) of 1%.

All Orders by Existing Holders and Potential Holders must specify numbers of shares of APS in whole Units. Any Order that specifies a number of shares of APS other than in whole Units will not be accepted and will not be considered a Submitted Order for purposes of an Auction.

If one or more Orders covering in the aggregate more than the number of outstanding Units of the series of APS subject to such Auction held by any Existing Holder are submitted to the Trust Company on behalf of such Existing Holder, such Orders shall be considered valid in the following order of priority:

(i) All Hold Orders shall be considered valid, but only up to and including in the aggregate the number of Units of APS of such series held by such Existing Holder, and, solely for purposes of allocating compensation among the Broker-Dealers submitting Hold Orders, if the number of Units of APS of such series subject to such Hold Orders exceeds the number of outstanding Units of APS of such series held by such Existing Holder, the number of Units subject to each such Hold Order shall be reduced pro rata to cover the number of outstanding Units of APS of such series held by such Existing Holder.

(ii) (A) any Bid shall be considered valid up to and including the excess of the number of outstanding Units of APS of such series held by such Existing Holder over the number of Units of APS of such series subject to any Hold Orders referred to in clause (i) above.

(B) subject to subclause (A), if more than one Bid with the same rate is submitted on behalf of such Existing Holder and the number of Units of APS of such series subject to such Bids is

greater than such excess, such Bids shall be considered valid up to and including the amount of such excess, and, solely for purposes of allocating compensation among the Broker-Dealers submitting Bids with the same rate, the number of Units of APS of such series subject to each Bid with the same rate shall be reduced pro rata to cover the number of Units of APS of such series equal to such excess;

(C) subject to subclause (A), if more than one Bid with different rates is submitted on behalf of such Existing Holder, such Bids shall be considered valid in the ascending order of their respective rates up to the amount of such excess; and

(D) in any such event, the number, if any, of such Units subject to Bids not valid under this clause (ii) shall be treated as the subject of a Bid by a Potential Holder; and

(iii) all Sell Orders shall be considered valid up to and including the excess of the number of outstanding Units of APS of such series held by such Existing Holder over the sum of the Units of APS of such series subject to valid Hold Orders referred to in clause (i) above and valid Bids by such Existing Holder referred to in clause (ii) above.

If more than one Bid is submitted on behalf of any Potential Holder, each Bid submitted shall be a separate Bid with the rate and number of Units of APS of such series specified.

Determination of Sufficient Clearing Bids, Winning Bid Rate and Applicable Rate

Not earlier than the Submission Deadline on each Auction Date with respect to each series of APS, the Trust Company will assemble all Orders relating to such series submitted or deemed submitted to it by the Broker-Dealers (each such Hold Order, Bid or Sell Order as submitted or deemed submitted by a Broker-Dealer being herein referred to as a "Submitted Hold Order," a "Submitted Bid" or a "Submitted Sell Order," as the case may be, or as a "Submitted Order") and will determine the excess of the number of outstanding Units of APS of the series to which the Auction relates over the number of outstanding Units of APS of such series subject to Submitted Hold Orders (such excess, the "Available APS") and whether Sufficient Clearing Bids have been made in the Auction. Sufficient Clearing Bids will have been made if the number of outstanding Units of APS of such series that are the subject of Submitted Bids by Potential Holders specifying rates not higher than the Maximum Rate equals or exceeds the number of outstanding Units of such series that are the subject of Submitted Sell Orders (including the number of Units of such series subject to Bids by Existing Holders specifying rates higher than the Maximum Rate).

If Sufficient Clearing Bids have been made, the Trust Company will determine the lowest rate specified in the Submitted Bids (the "Winning Bid Rate") which, taking into account the rates in the Submitted Bids of Existing Holders, would result in Existing Holders continuing to hold an aggregate number of outstanding Units of APS of such series which, when added to the number of outstanding Units of APS of such series to be purchased by Potential Holders, based on the rates in their Submitted Bids, would equal not less than the Available APS. In such event, the Winning Bid Rate will be the Applicable Rate for the next Dividend Period for all Units of APS of such series.

If Sufficient Clearing Bids have not been made (other than because all of the outstanding Units of APS of such series are subject to Submitted Hold Orders), the Applicable Rate for the next Dividend Period for all Units of APS of such series will be equal to the Maximum Rate. If Sufficient Clearing Bids have not been made, Existing Holders that have submitted Sell Orders will be able to sell in the Auction none or only a portion of the Units of APS subject to such Sell Orders. See "Acceptance and Rejection of Submitted Bids and Submitted Sell Orders and Allocation of Shares" below.

If all of the outstanding Units of APS of such series are subject to Submitted Hold Orders, the Applicable Rate for the next Dividend Period for the shares of APS of such series will be 58% of the "AA" Composite Commercial Paper Rate.

Acceptance and Rejection of Submitted Bids and Submitted Sell Orders and Allocation of Shares

Based on the determination made under "Determination of Sufficient Clearing Bids, Winning Bid Rate and Applicable Rate" above and, subject to the discretion of the Trust Company to round as described below, Submitted Bids and Submitted Sell Orders shall be accepted or rejected in the order of priority set forth in the Auction Procedures, with the result that Existing Holders and Potential Holders of APS of the series to which the Auction relates shall sell, continue to hold and/or purchase Units of APS of such series as set forth below. Existing Holders that submitted or were deemed to have submitted Hold Orders shall continue to hold the Units of APS of such series subject to such Hold Orders.

If Sufficient Clearing Bids have been made:

- (a) Each Existing Holder that placed a Submitted Sell Order or a Submitted Bid specifying any rate higher than the Winning Bid Rate shall sell the outstanding Units of APS of such series subject to such Submitted Sell Order or Submitted Bid;
- (b) Each Existing Holder that placed a Submitted Bid specifying a rate lower than the Winning Bid Rate shall continue to hold the outstanding Units of APS of such series subject to such Submitted Bid;
- (c) Each Potential Holder that placed a Submitted Bid specifying a rate lower than the Winning Bid Rate shall purchase the number of outstanding Units of APS of such series subject to such Submitted Bid;
- (d) Each Existing Holder that placed a Submitted Bid specifying a rate equal to the Winning Bid Rate shall continue to hold the Units of APS of such series subject to such Submitted Bid, unless the number of outstanding Units of APS of such series subject to all such Submitted Bids is greater than the excess of the Available APS over the number of Units of APS of such series accounted for in clauses (b) and (c) above, in which event each Existing Holder with such a Submitted Bid shall sell a number of outstanding Units of APS of such series subject to such Submitted Bid determined on a pro rata basis based on the number of outstanding Units of APS of such series subject to all such Submitted Bids by such Existing Holders; and
- (e) Each Potential Holder that placed a Submitted Bid specifying a rate equal to the Winning Bid Rate shall purchase any Available APS not accounted for in clauses (b), (c), or (d) above on a pro rata basis based on the outstanding shares of APS of such series subject to all such Submitted Bids.

If Sufficient Clearing Bids have not been made (unless this results because all of the outstanding Units of APS of such series are subject to Submitted Hold Orders):

- (a) Each Existing Holder that placed a Submitted Bid specifying a rate equal to or lower than the Maximum Rate shall continue to hold the outstanding Units of APS of such series subject to such Submitted Bid;
- (b) Each Potential Holder that placed a Submitted Bid specifying a rate equal to or lower than the Maximum Rate shall purchase the number of outstanding Units of APS of such series subject to such Submitted Bid; and
- (c) Each Existing Holder that placed a Submitted Bid specifying a rate higher than the Maximum Rate or a Submitted Sell Order shall sell a number of Units of APS of such series determined on a pro rata basis based on the number of outstanding Units of APS of such series subject to all such Submitted Bids and Submitted Sell Orders.

If, as a result of the Auction Procedures, (i) any Existing Holder would be entitled or required to sell, or any Potential Holder would be entitled or required to purchase, shares of a series of APS other than in whole Units, the Trust Company shall, in such manner as, in its sole discretion, it shall determine, round up or down the number of Units of such series being sold or purchased on such Auction Date so that the number of Units of such series sold or purchased by each Existing Holder or Potential Holder shall be whole Units of APS or (ii) any Potential Holder would be entitled or required to purchase less than a whole Unit of a series, the Trust Company shall, in such manner as, in its sole discretion, it shall determine, allocate Units of such

series for purchase among Potential Holders so that only whole Units of APS are purchased by any such Potential Holder, even if such allocation results in one or more of such Potential Holders not purchasing Units of APS of such series.

Notification of Results; Settlement

The Trust Company will advise each Broker-Dealer that submitted an Order of the Applicable Rate for the next Dividend Period and, if the Order was a Bid or Sell Order, whether such Bid or Sell Order was accepted or rejected, in whole or in part, by telephone by approximately 3:00 P.M., New York City time, on each Auction Date. Each Broker-Dealer that submitted an Order on behalf of a Bidder will then advise such Bidder of the Applicable Rate for the next Dividend Period and, if such Order was a Bid or Sell Order, whether such Bid or Sell Order was accepted or rejected, in whole or in part, will confirm purchases and sales with each Bidder purchasing or selling Units of APS of the series to which the Auction relates as a result of the Auction and will advise each Bidder purchasing or selling Units of APS of such series as a result of the Auction to give instructions to its Agent Member of the Securities Depository to pay the purchase price against delivery of such Units or to deliver such Units against payment therefor, as appropriate. The Trust Company will record each transfer of Units of APS on the registry of Existing Holders to be maintained by the Trust Company. See "General" above.

In accordance with the Securities Depository's normal procedures, on the Business Day after the Auction Date, the transactions described above will be executed through the Securities Depository and the accounts of the respective Agent Members at the Securities Depository will be debited and credited and Units delivered as necessary to effect the purchases and sales of Units of the series of APS as determined in the Auction. Purchasers will make payment through their Agent Members in next-day funds settled through the New York Clearing House to the Securities Depository against delivery through their Agent Members; the Securities Depository will make payment in accordance with its normal procedures, which now provide for payment against delivery by their Agent Members in next-day funds settled through the New York Clearing House.

If any Existing Holder selling Units of APS of any series pursuant to an Auction fails to deliver such Units, the Broker-Dealer of any person that was to have purchased Units of APS in such Auction may deliver to such person a number of Units of APS that is less than the number of Units that otherwise was to be purchased by such person. In such event, the number of Units of APS to be so delivered shall be determined by such Broker-Dealer. Delivery of such lesser number of Units shall constitute good delivery.

Concerning the Trust Company

The Trust Company is acting as agent for the Company in connection with Auctions. In the absence of bad faith or negligence on its part, the Trust Company shall not be liable for any action taken, suffered, or omitted or for any error of judgment made by it in the performance of its duties under the Trust Company Agreement and shall not be liable for any error of judgment made in good faith unless the Trust Company shall have been negligent in ascertaining the pertinent facts.

The Trust Company may terminate the Trust Company Agreement upon notice to the Company on a date no earlier than the Business Day after the second Dividend Payment Date of a series of the APS after such notice. If the Trust Company should resign, the Company will use its best efforts to enter into an agreement with a successor Trust Company containing substantially the same terms and conditions as the Trust Company Agreement. The Company may remove the Trust Company, provided that prior to such removal the Company shall have entered into such an agreement with a successor Trust Company.

Broker-Dealers

The Trust Company after each Auction will pay a service charge, from funds provided by the Company, to each Broker-Dealer at the annual rate of $\frac{1}{4}$ of 1% of the purchase price of Units of APS placed by such Broker-Dealer at such Auction. For the purposes of the preceding sentence, Units of APS will be placed by a

Broker-Dealer if such Units were (i) the subject of Hold Orders deemed to have been made by Existing Holders and were acquired by such Existing Holders through such Broker-Dealer or (ii) the subject of an Order submitted by such Broker-Dealer that is: (A) a Submitted Bid of an Existing Holder that resulted in such Existing Holder continuing to hold such Units as a result of the Auction or (b), a Submitted Bid of a Potential Holder that resulted in such Potential Holder purchasing such Units as a result of the Auction or (C) a valid Hold Order.

The Broker-Dealer Agreements provide that a Broker-Dealer (other than an affiliate of the Company) may submit Orders in Auctions for its own account, unless the Company notifies all Broker-Dealers that they may no longer do so, in which case Broker-Dealers may continue to submit Hold Orders and Sell Orders for their own accounts. Any Broker-Dealer that is an affiliate of the Company may submit Orders in Auctions but only if such Orders are not for its own account, except that if such affiliated Broker-Dealer holds Units for its own account, it must submit a Sell Order in the next Auction with respect to such Units.

If a Broker-Dealer submits an Order for its own account in any Auction, it might have an advantage over other Bidders because it would have knowledge of Orders placed through it in that Auction; such Broker-Dealer, however, would not necessarily have knowledge of Orders submitted by other Broker-Dealers in that Auction.

DESCRIPTION OF APS

The following is a brief description of the terms of the APS of Series A and Series B. This description does not purport to be complete and is qualified in its entirety by the Company's Restated Articles of Incorporation, as amended (the "Articles"), and the Statements of Resolution authorizing the issuance of Series A and Series B, the forms of which are filed as exhibits to the Registration Statement of which this Prospectus is a part.

General

Under the Company's Articles, the Company is authorized to issue up to 3,035,000 shares of Preferred Stock, par value of \$100 per share (the "Preferred Stock"), in one or more series. The Board of Directors has the authority to establish by resolution series of the Preferred Stock and to fix and determine the designations, rates, dates, terms and other conditions upon which dividends shall be payable, redemption prices and terms and conditions of redemption, amounts payable in the event of the voluntary liquidation of the Company, sinking fund provisions, any conversion rights and terms and conditions of conversion and other special rights or preferences which the Board of Directors may have authority to fix under the laws of the State of Texas. As of December 31, 1987, 2,185,000 shares of the Company's Preferred Stock were outstanding. The Company's Articles provide that all of the Company's Preferred Stock shall be of equal rank with each other regardless of series. Series A and Series B of the APS are two series of the Preferred Stock.

Bankers Trust Company will be the transfer agent and registrar for shares of each series of APS and will act as dividend disbursing agent and redemption agent for shares of each series of APS. In such capacity, Bankers Trust Company is referred to herein as the "Paying Agent."

The shares of APS of each series, when issued, will be fully paid and nonassessable, will not be convertible into Common Stock or other capital stock of the Company and will have no preemptive rights. The shares of APS of each series will be subject to redemption under the circumstances described under "Redemption" below.

Dividends

General. The holders of APS of each series shall be entitled to receive, when, as and if declared by the Board of Directors of the Company out of funds legally available therefor, cumulative cash dividends, at the Applicable Rate per annum thereof, determined as set forth below under "Determination of Dividend Rate," and no more, payable on the respective dates set forth below.

Dividends on the shares of APS of each series will accrue from the date on which the Company originally issues the shares of APS (the "Date of Original Issue") and will be payable, when, as and if declared by the Board of Directors commencing on April 13, 1988, in the case of Series A, and on April 27, 1988, in the case of Series B, and on each succeeding seventh Wednesday after such respective date except that (i) (A) if such Wednesday is not a Business Day, then the Dividend Payment Date will be the first Business Day after such Wednesday that is immediately followed by a Business Day and is preceded by a Business Day that is the preceding Monday or a day after such Monday, or (B) if such Wednesday is a Business Day but the Thursday following such Wednesday is not a Business Day, then the Dividend Payment Date will be (x) the preceding Tuesday if such Tuesday and the preceding Monday are Business Days or (y) otherwise the first Business Day after such Wednesday that is immediately followed by a Business Day and preceded by a Business Day that is such Monday or a day after such Monday, or (C) if such Wednesday and the Thursday following such Wednesday are both Business Days but both the preceding Monday and Tuesday are not Business Days, then the Dividend Payment Date will be the first Business Day after such Wednesday that is immediately followed by a Business Day and is preceded by a Business Day that is such Wednesday or a day after such Wednesday, or (ii) if such Wednesday is not a Business Day or both the Monday and Tuesday preceding such Wednesday are not Business Days and if the Securities Depository shall make available to its participants and members, in funds immediately available in New York City on Dividend Payment Dates, the amount due as dividends on such Dividend Payment Dates (and the Securities Depository shall have so advised the Trust Company and the Paying Agent), then the Dividend Payment Date will be the first Business Day after such Wednesday that is preceded by a Business Day that is the preceding Monday or a day after such Monday. Although any particular Dividend Payment Date may not occur on the originally scheduled Wednesday because of the exceptions discussed above, the next succeeding Dividend Payment Date shall be, subject to such exceptions, the seventh Wednesday following the originally designated Wednesday Dividend Payment Date for the prior Dividend Period. Notwithstanding the foregoing, in the event of a change in law lengthening the minimum holding period (currently found in Section 246(c) of the Internal Revenue Code of 1986, as amended (the "Code")) required for taxpayers to be entitled to the dividends received deduction on preferred stock held by non-affiliated corporations (currently found in Section 243(a) of the Code), the Board of Directors of the Company may adjust the period of time between Dividend Payment Dates so as to adjust uniformly the number of days (such number of days, without giving effect to the exceptions referred to above, being hereinafter referred to as "Dividend Period Days"), in Dividend Periods commencing after the date of such change in law to equal or exceed the then current minimum holding period; provided that the number of Dividend Period Days shall not exceed by more than nine days the length of such then current minimum holding period and in no event shall exceed 98 days and that dividends shall continue to be payable on Wednesdays, subject to the exceptions discussed above. Each dividend payment date for each series determined as provided above is herein referred to as a "Dividend Payment Date" and the first Dividend Payment Date for each series is herein referred to as the "Initial Dividend Payment Date." Upon any such change in the number of Dividend Period Days as a result of a change in law, the Company will mail notice of such change to all holders of shares of APS of each series so affected. In addition, under the Broker-Dealer Agreements, each Broker-Dealer is required to mail notice to each Existing Holder who acquired shares of APS of either series through such Broker-Dealer and, to the knowledge of such Broker-Dealer, has not disposed of such shares of APS, at the address specified in such Existing Holder's Master Purchaser's Letter, at least 10 days prior to both (i) the first day of the Dividend Period preceding the Dividend Period for which such change is to be effective, and (ii) the first day of the Dividend Period for which such change is to be effective.

Each dividend will be payable to holders of record as they appear on the stock books of the Company on the Business Day next preceding the Dividend Payment Date thereof, provided that if the Applicable Rate is 150% of the 60-day "AA" Composite Commercial Paper Rate as a result of a failure to pay a dividend amount or redemption price on or within three Business Days after the date when due, such dividend shall be paid to such holders as their names appear on the stock books of the Company on such date, not exceeding 15 days preceding the payment date thereof, as may be fixed by the Board of Directors of the Company. Dividends in arrears for any past Dividend Period may be declared and paid at any time, without reference to

any regular Dividend Payment Date, to the holders as their names appear on the stock books of the Company on such date, not exceeding 15 days preceding the payment date thereof, as may be fixed by the Board of Directors of the Company.

The holders of shares of APS of either series shall not be entitled to receive any dividends thereon other than full cumulative cash dividends as provided in the Statements of Resolution & J described herein. Accumulations of dividends shall not bear interest. When full cumulative dividends have been paid on, and declared or set aside for payment in respect of, all shares of the Preferred Stock and mandatory sinking fund obligations have been satisfied, the Board of Directors of the Company (subject to applicable restrictions described below) may declare dividends on the Common Stock of the Company (the "Common Stock").

Provisions of the Articles which are applicable so long as any shares of Preferred Stock are outstanding limit dividends on Common Stock in any 12-month period ending with and including the date on which the particular dividend is proposed to be paid (a) to 75% of the net income available for Common Stock dividends for the 12 months ending within 60 days next preceding the month in which such dividend is proposed to be declared if the ratio of Common Stock equity to total capitalization of the Company is or as a result of the payment of such dividend would become 20% or more but less than 25% and (b) to 50% of such net income if such ratio is or as a result of the payment of such dividend would become less than 20%; plus any amounts that could have been declared as dividends pursuant to such limitations, but which were not actually declared, during any previous year or years. If such ratio is 25% or more, the total amount of all Common Stock dividends may not exceed a sum which would reduce such ratio below 25%, except to the extent permitted by clauses (a) or (b). At December 31, 1987, such ratio was approximately 45%.

The Indenture pursuant to which the Company has issued first mortgage bonds also contains certain provisions restricting payments of dividends on the Common Stock.

The amount of dividends per share payable on the APS of either series for each Dividend Period shall be computed by multiplying the Applicable Rate for each Dividend Period for such series by a fraction the numerator of which shall be the number of days in such Dividend Period and the denominator of which shall be 360 and applying the rate obtained against \$100 per share of APS. The amount of dividends payable per Unit for each Dividend Period shall be the amount of dividends per share determined as aforesaid multiplied by 1,000.

Determination of Dividend Rate. The dividend rate for the APS during the period from and after the Date of Original Issue to and including the day preceding the Initial Dividend Payment Date (the "Initial Dividend Period") shall be 5.50% for Series A and 5.50% for Series B. Commencing on the Initial Dividend Payment Date, dividend rates on the shares of APS for each subsequent dividend period (herein referred to as a "Subsequent Dividend Period" and collectively as "Subsequent Dividend Periods," and the Initial Dividend Period or any Subsequent Dividend Period being herein referred to as "Dividend Period" and collectively as "Dividend Periods") thereafter, which Subsequent Dividend Periods shall commence on the day on which dividends, if declared, shall be payable (normally a Dividend Payment Date) and shall end on and include the day preceding the next such date, shall be at a rate per annum (the "Applicable Rate"), except as provided in the next paragraph, that results from an Auction relating to that series of APS. Dividends shall be calculated as set forth in the preceding paragraph.

In the event of the failure by the Company to pay to the Paying Agent by 12:00 noon, New York City time, (i) on or within three Business Days after the Business Day next preceding any Dividend Payment Date, the full amount of any dividend (whether or not declared) to be paid on such Dividend Payment Date on any share of any series of APS or (ii) on or within three Business Days after any redemption date, the redemption price in immediately available funds to be paid on such redemption date in respect of shares of any series of APS redeemed as described below under "Redemption," then Auctions will be discontinued with respect to such series of APS and the Applicable Rate for such series for each Dividend Period commencing after the date of any such failure shall be equal to 150% of the 60-day "AA" Composite Commercial Paper Rate.

"'AA' Composite Commercial Paper Rate," on any date, means (i) the interest equivalent of the 60-day rate on commercial paper placed on behalf of issuers whose corporate bonds are rated "AA" by S&P or the equivalent of such rating by S&P or another rating agency, as made available on a discount basis or otherwise by the Federal Reserve Bank of New York for the immediately preceding Business Day prior to such date, or (ii) in the event that the Federal Reserve Bank of New York does not make available such a rate, then the arithmetic average of the interest equivalent of the 60-day rate on commercial paper placed on behalf of such issuers, as quoted on a discount basis or otherwise by Goldman, Sachs & Co., Shearson Lehman Commercial Paper Inc. and Merrill Lynch, Pierce, Fenner & Smith Incorporated, or their respective affiliates or successors (the "Commercial Paper Dealers"), to the Trust Company for the close of business on the immediately preceding Business Day prior to such date. If any Commercial Paper Dealer does not quote a rate required to determine the "AA" Composite Commercial Paper Rate, the "AA" Composite Commercial Paper Rate shall be determined on the basis of the quotation or quotations furnished by the remaining Commercial Paper Dealer or Commercial Paper Dealers and any Substitute Commercial Paper Dealer or Substitute Commercial Paper Dealers selected by the Company to provide such rate or rates not being supplied by any Commercial Paper Dealer or Commercial Paper Dealers, as the case may be, or, if the Company does not select any such Substitute Commercial Paper Dealer or Substitute Commercial Paper Dealers, by the remaining Commercial Paper Dealer or Commercial Paper Dealers. However, if the Board of Directors of the Company shall increase the number of Dividend Period Days in the event of a change in the dividends received deduction holding period contained in the Code (see "Dividends—General" above), with the result that (i) the number of Dividend Period Days shall be 70 or more days but fewer than 85 days, such rate shall be based on the arithmetic average of the interest equivalent of the 60-day and 90-day rates on such commercial paper, or (ii) the number of Dividend Period Days shall be 85 or more days but 98 or fewer days, such rate shall be based on the interest equivalent of the 90-day rate on such commercial paper. For purposes of such definition, the "interest equivalent" means the equivalent yield on a 360-day basis of a discount basis security to an interest bearing security and "Substitute Commercial Paper Dealer" means The First Boston Corporation or Morgan Stanley & Co. Incorporated, or their respective affiliates or successors, if such dealer or affiliate or successor is a commercial paper dealer, provided that neither such dealer nor any of its affiliates or successors is a Commercial Paper Dealer.

Redemption

At the option of the Company, the shares of each series of APS may be redeemed, as a whole or in part, on any Dividend Payment Date at a redemption price of \$100,000 per Unit (\$100 per share), plus accrued and unpaid dividends thereon (whether or not declared) to the date fixed for redemption. The shares of APS are redeemable only in whole Units.

If fewer than all the outstanding shares of APS of a particular series are to be redeemed as set forth above, the number of shares to be redeemed shall be determined by the Board of Directors of the Company, and such shares shall be redeemed in whole Units pro rata from the holders of record of such shares in proportion to the number of shares held by such holders.

Notice of redemption shall be given by mailing the same to each holder of the shares to be redeemed, not less than 30 nor more than 90 days prior to the date fixed for redemption thereof, to the respective addresses of such holders as the same shall appear on the records of the Company. Each such notice shall state: (i) the redemption date; (ii) the number of shares and the series of APS to be redeemed; (iii) the redemption price; and (iv) the place or places where certificates for such shares of APS are to be surrendered for payment of the redemption price.

Notwithstanding the foregoing, the Company may not redeem, purchase or otherwise acquire less than all the outstanding shares of the Preferred Stock if dividends payable on the Preferred Stock are in default in whole or in part, unless prior to or concurrently with such redemption, purchase or other acquisition, all such defaults in dividends shall have been cured, or unless such redemption, purchase or other acquisition

shall have been ordered, approved or permitted by the Commission under the Public Utility Holding Company Act of 1935.

Upon the giving of notice of redemption and upon the deposit of the redemption price with a bank or trust company as provided in the Articles, or if no such deposit is made, upon the redemption date for the shares of APS called for redemption (unless the Company defaults in making payment of the redemption price as set forth in such notice), said shares shall no longer be deemed to be outstanding, and all rights of the holders thereof as stockholders of the Company (except the right to receive the redemption price without interest) shall cease. Upon surrender in accordance with said notice of the certificates for any shares so redeemed, the redemption price shall be paid by the Company or the bank or trust company.

Liquidation Preference

The Preferred Stock is preferred over the Common Stock as to assets in the event of the dissolution of the Company to the extent of the par value thereof plus accrued dividends if such dissolution is involuntary and to the extent of the then effective redemption price thereof (as set forth in the first paragraph under "Description of APS—Redemption") plus accrued dividends if such dissolution is voluntary, except that with respect to the 4% Preferred Stock, the liquidation preference is the par value thereof plus accrued dividends in the case of both voluntary and involuntary dissolution. Neither a consolidation or merger of the Company with or into any other corporation, a merger of any other corporation into the Company, nor the purchase or other acquisition, redemption or other retirement by the Company of all or any part of the outstanding shares of Preferred Stock of any series shall be deemed to be a distribution of assets or a liquidation, dissolution or winding up, of the Company.

Voting Rights

The Preferred Stock has no voting rights for the election of directors or otherwise, except as expressly provided in the Articles and summarized hereunder and except as may be required by law. In such excepted cases, each share of Preferred Stock is entitled to one vote. During any period when dividends on the Preferred Stock are in default in an amount equal to the annual dividends or more per share, and thereafter until all dividends in default on such stock have been paid, the Preferred Stock as a class is entitled to elect the smallest number of directors necessary to constitute a majority of the full Board.

The vote or consent of at least two-thirds of the outstanding shares of the Preferred Stock is required for (i) the authorization of any class of stock ranking prior to the Preferred Stock as to dividends or assets, or any security convertible into such prior stock, or for the issue of any of such prior stock or convertible security more than one year after such vote or consent; or (ii) any adverse change in the rights, preferences or powers of the holders of the Preferred Stock. The vote or consent of a majority of the Preferred Stock is required for (i) any merger or consolidation, or any sale or disposition of substantially all the assets of the Company, unless ordered, approved or permitted by the Commission under the Public Utility Holding Company Act of 1935; (ii) the issue of any shares of Preferred Stock or of any stock on a parity therewith as to dividends or assets, except in exchange for or to effect the retirement of at least an equal amount of the Preferred Stock or of such parity stock, unless (1) the gross income of the Company (computed as provided in the Articles) for a 12-month period ending within three months preceding the issue of such additional shares is at least one and one-half times the sum of (a) the annual interest charges on all indebtedness represented by bonds, notes or other securities and (b) the annual dividend requirements on the Preferred Stock and on all prior or parity stock to be outstanding after the issue of the additional shares to be issued, and (2) common stock equity (computed as provided in the Articles) is not less than the total payable upon involuntary dissolution in respect of the Preferred Stock and all such prior or parity stock; (iii) the issue or assumption of any unsecured notes, debentures or other securities representing unsecured indebtedness ("unsecured obligations") except to refund outstanding unsecured obligations resulting under maturities or to fund existing unsecured indebtedness not represented by unsecured obligations, if immediately after such issue or assumption (1) the principal amount of unsecured obligations would exceed

20% of the aggregate of the principal amount of secured indebtedness and the total capital stock and surplus of the Company, or (2) the principal amount of all unsecured obligations maturing in less than ten years (computed as provided in the Articles) would exceed 10% of such aggregate.

Miscellaneous

The Company reserves the right in its Articles to increase or decrease its authorized capital stock or any class or series thereof, or to reclassify the same, and to change any provision contained in its Articles or any future amendment thereto as then in effect, in the manner now or hereafter prescribed by law, but subject to the conditions and limitations prescribed in the Articles as then in effect; and all rights granted to stockholders in the Articles or any future amendment thereto, are granted subject to such reservation.

UNDERWRITING

Underwriters and Commissions

Goldman, Sachs & Co. and Shearson Lehman Hutton Inc. (the "Underwriters") have agreed, subject to the terms and conditions set forth in the Underwriting Agreement, to purchase from the Company all of the shares of APS of Series A and Series B offered hereby. The Underwriting Agreement provides that the obligations of the Underwriters are subject to certain conditions precedent, and that the Underwriters are obligated to purchase all of the shares of APS of both series if any are purchased. In the Underwriting Agreement, the Company agrees to indemnify the Underwriters with respect to certain liabilities, including liabilities arising under the Securities Act of 1933, and to contribute in respect thereof.

The Company has been advised that the Underwriters propose initially to offer Units of APS of both series to the public at the price set forth on the cover page of this Prospectus and to certain dealers ("Selected Dealers") at such price less a concession not to exceed \$1,050 per Unit. After the initial public offering, the public offering price and the concession may be changed by the Underwriters.

The Underwriters and their affiliates have acted in the past as underwriters and in various other capacities on behalf of the Company, and have received fees in connection therewith. The Underwriters and their affiliates may continue such activities in the future.

Settlement

Payment by each initial purchaser of shares of APS will be made through such purchaser's Agent Member on the date of delivery of such shares of APS to the Underwriter or Selected Dealer from which such purchaser purchased such shares of APS in next-day funds settled through the New York Clearing House. At the closing for each series of the APS the Underwriters will accept delivery of the shares of such series of APS and each Underwriter will thereafter deposit the shares purchased by it in its account at DTC. Immediately thereafter on the closing date, DTC will deliver the shares of APS of such series purchased by each Selected Dealer and each purchaser from the respective Underwriter's account to the account of such Selected Dealer's or purchaser's Agent Member of DTC, as the case may be, against payment to the account of such Underwriter of an amount equal to the purchase price from the account of such Selected Dealer's or purchaser's Agent Member of DTC. In the case of initial purchasers that purchase shares of APS from a Selected Dealer, DTC will deliver the shares of APS purchased by such purchaser from such Selected Dealer's account to the account of such purchaser's Agent Member of DTC against payment to the account of such Selected Dealer of an amount equal to the purchase price from the account of such purchaser's Agent Member of DTC. Under the Master Purchaser's Letter, each purchaser will be required, so long as the Company has not failed to pay to the Paying Agent the full amount of any dividend or the redemption price of any shares of APS called for redemption on or within three Business Days after the date when due, to have the ownership of the shares of APS owned by it maintained in book entry form by the Securities Depository

through such purchaser's Agent Member, which in turn will maintain records of such purchaser's beneficial ownership.

LEGAL OPINIONS

Legal opinions relating to the validity of the APS will be given by Jones, Day, Reavis & Pogue, 2300 Trammell Crow Center, 2001 Ross Avenue, Dallas, Texas 75201, counsel for the Company, and Sidley & Austin, One First National Plaza, Chicago, Illinois 60603, counsel for the Underwriters.

EXPERTS

The audited financial statements and schedules of the Company, incorporated by reference in this Prospectus and elsewhere in the Registration Statement of which this Prospectus is a part, have been examined by Arthur Andersen & Co., independent public accountants, as indicated in their reports dated February 9, 1987 with respect thereto which have also been incorporated by reference herein in reliance upon the authority of said firm as experts in accounting and auditing in giving said reports.

ADDITIONAL INFORMATION

The Company owns a 25.2% share in the two-unit South Texas Nuclear Project ("STP"). For further information concerning the construction and licensing of and certain proceedings relating to STP, see the documents listed under "Incorporation of Certain Documents by Reference".

On February 11, 1988, Houston Lighting & Power Company ("HLP"), as project manager of STP, received a notice of violation and proposed imposition of civil penalty (the "NRC Notice") from the Nuclear Regulatory Commission ("NRC") resulting from inspections conducted during November 1987 and January 1988. The violations cited by the NRC involved the failure to satisfy certain technical specification requirements during the testing of STP Unit 1. The NRC Notice specified a proposed civil penalty in the amount of \$75,000 for the violations, but allows HLP to contest the NRC's findings and to petition for mitigation of the proposed penalty.

The Company has been assured that the operational violations have been corrected. Management of the Company cannot predict the outcome of the proceedings resulting from the NRC Notice, but believes that these proceedings will not result in additional delays in the in-service date for STP Unit 1.

APPENDIX A

AUCTION PROCEDURES

The following procedures will be set forth as Part II of the Statement of Resolution establishing each series of the APS. The terms not defined below (and referred to as defined in Part I of the Statement of Resolution) are defined in the forepart of this Prospectus. The Statement of Resolution for each series of the APS will refer to the particular designation of such series; however, such series of APS may be defined as "APS" therein.

1. Certain Definitions. Capitalized terms not defined in this Section 1 shall have the respective meanings specified in Part I hereof. As used in this Part II, the following terms shall have the following meanings, unless the context otherwise requires:

(a) "'AA' Rate Multiple," on any Auction Date, shall mean the percentage determined as set forth below based on the prevailing rating of APS in effect at the close of business on the Business Day immediately preceding such Auction Date:

<u>Prevailing Rating*</u>	<u>Percentage</u>
AA/aa or Above.....	110%
A/a	120%
BBB/baa	130%
Below BBB/baa	150%

* In the case of a split rating, the Maximum Rate will be determined on the basis of the lower rating. For example, a rating of A+/aa3 would result in a Maximum Rate of 120% of the "AA" Composite Commercial Paper Rate.

For purposes of this definition, the "prevailing rating" of Units of a series of APS shall be (i) AA/aa or Above if the shares of such series of APS have ratings of both AA- or better by S&P and aa3 or better by Moody's or the equivalent of both of such ratings by such agencies or a substitute rating agency or substitute rating agencies selected as provided below, (ii) if not AA/aa or Above, then A/a if the shares of such series of APS have ratings of both A- or better by S&P and a3 or better by Moody's or the equivalent of both of such ratings by such agencies or a substitute rating agency or substitute rating agencies selected as provided below, (iii) if not AA/aa or Above or A/a, then BBB/baa if the shares of such series of APS have ratings of both BBB- or better by S&P and baa3 or better by Moody's or the equivalent of both of such ratings by such agencies or a substitute rating agency or substitute rating agencies selected as provided below, and (iv) if not AA/aa or Above, A/a or BBB/baa, then Below BBB/baa. The Corporation shall take all reasonable action necessary to enable S&P and Moody's to provide a rating for APS. If either S&P or Moody's shall not make such a rating available, or neither S&P nor Moody's shall make such a rating available, Goldman, Sachs & Co. or its successor shall select a nationally recognized statistical rating organization (as that term is used in the rules and regulations of the Securities and Exchange Commission under the Securities Exchange Act of 1934, as amended) or two nationally recognized statistical rating organizations to act as substitute rating agency or substitute rating agencies, as the case may be, and the Corporation shall take all reasonable action to enable such rating agency or rating agencies to provide a rating or ratings for each series of the APS.

(b) "Affiliate" shall mean any Person known to the Trust Company to be controlled by, in control of or under common control with the Corporation.

(c) "Agent Member" shall mean the member of, or participant in, the Securities Depository that will act on behalf of a Bidder and is identified as such in such Bidder's Master Purchaser's Letter.

(d) "Auction" shall mean the periodic implementation of the procedures set forth in this Part II.

- (e) "Auction Date" shall mean the Business Day next preceding the first day of a Dividend Period.
- (f) "Available APS" shall have the meaning specified in paragraph (a) of Section 4 of this Part II.
- (g) "Bid" and "Bids" shall have the respective meanings specified in paragraph (a) of Section 2 of this Part II.
- (h) "Bidder" and "Bidders" shall have the respective meanings specified in paragraph (a) of Section 2 of this Part II.
- (i) "Broker-Dealer" shall mean any broker-dealer, or other entity permitted by law to perform the functions required of a Broker-Dealer in this Part II, that is a member of, or a participant in, the Securities Depository, has been selected by the Corporation and has entered into a Broker-Dealer Agreement with the Trust Company that remains effective.
- (j) "Broker-Dealer Agreement" shall mean an agreement between the Trust Company and a Broker-Dealer pursuant to which such Broker-Dealer agrees to follow the procedures specified in this Part II.
- (k) "Existing Holder," when used with respect to shares of APS, shall mean a Person who has signed a Master Purchaser's Letter and is listed as the beneficial owner of shares of APS in the records of the Trust Company.
- (l) "Hold Order" and "Hold Orders" shall have the respective meanings specified in paragraph (a) of Section 2 of this Part II.
- (m) "Master Purchaser's Letter" shall mean a letter, the form of which is attached hereto, addressed to the Corporation, the Trust Company, a Broker-Dealer and an Agent Member in which a Person agrees, among other things, to offer to purchase, to purchase, to offer to sell and/or to sell shares of APS as set forth in this Part II.
- (n) "Maximum Rate," on any Auction Date, shall mean the product of the "AA" Composite Commercial Paper Rate times the "AA" Rate Multiple.
- (o) "Order" and "Orders" shall have the respective meanings specified in paragraph (a) of Section 2 of this Part II.
- (p) "Outstanding" shall mean, as of any date, shares of APS theretofore issued by the Corporation except, without duplication, (i) any shares of APS theretofore cancelled or delivered to the Corporation for cancellation or redeemed by the Corporation or as to which a notice of redemption shall have been given by the Corporation, (ii) any shares of APS as to which the Corporation or any Affiliate thereof (other than a Broker-Dealer Affiliate) shall be an Existing Holder and (iii) any shares of APS represented by any certificate in lieu of which a new certificate has been executed and delivered by the Corporation.
- (q) "Paying Agent" shall mean Bankers Trust Company or any other bank or trust company appointed as such pursuant to a resolution of the Board of Directors.
- (r) "Person" shall mean and include an individual, a partnership, a corporation, a trust, an unincorporated association, a joint venture or other entity or a government or any agency or political subdivision thereof.
- (s) "Potential Holder" shall mean any Person, including any Existing Holder, (i) who shall have executed a Master Purchaser's Letter and (ii) who may be interested in acquiring shares of APS (or, in the case of an Existing Holder, additional shares of APS).

(t) "Securities Depository" shall mean The Depository Trust Company and its successors and assigns or any other securities depository selected by the Corporation which agrees to follow the procedures required to be followed by such securities depository in connection with shares of APS.

(u) "Sell Order" and "Sell Orders" shall have the respective meanings specified in paragraph (a) of Section 2 of this Part II.

(v) "Submission Deadline" shall mean 1:00 P.M., New York City time, on any Auction Date or such other time on any Auction Date by which Broker-Dealers are required to submit Orders to the Trust Company as specified by the Trust Company from time to time.

(w) "Submitted Bid" and "Submitted Bids" shall have the respective meanings specified in paragraph (a) of Section 4 of this Part II.

(x) "Submitted Hold Order" and "Submitted Hold Orders" shall have the respective meanings specified in paragraph (a) of Section 4 of this Part II.

(y) "Submitted Order" and "Submitted Orders" shall have the respective meanings specified in paragraph (a) of Section 4 of this Part II.

(z) "Submitted Sell Order" and "Submitted Sell Orders" shall have the respective meanings specified in paragraph (a) of Section 4 of this Part II.

(aa) "Sufficient Clearing Bids" shall have the meaning specified in paragraph (a) of Section 4 of this Part II.

(bb) "Units" shall mean Units of 1,000 shares of APS.

(cc) "Winning Bid Rate" shall have the meaning specified in paragraph (a) of Section 4 of this Part II.

2. Orders by Existing Holders and Potential Holders.

(a) On or prior to the Submission Deadline on each Auction Date with respect to each series:

(i) each Existing Holder may submit to a Broker-Dealer information as to:

(A) the number of Outstanding Units, if any, of APS held by such Existing Holder which such Existing Holder desires to continue to hold without regard to the Applicable Rate for the next succeeding Dividend Period;

(B) the number of Outstanding Units, if any, of APS which such Existing Holder desires to continue to hold if the Applicable Rate for the next succeeding Dividend Period shall not be less than the rate per annum specified by such Existing Holder; and/or

(C) the number of Outstanding Units, if any, of APS held by such Existing Holder which such Existing Holder offers to sell without regard to the Applicable Rate for the next succeeding Dividend Period; and

(ii) one or more Broker-Dealers, using lists of Potential Holders, shall, in good faith for the purpose of conducting a competitive Auction in a commercially reasonable manner, contact Potential Holders, including Persons that are not Existing Holders, on such lists to determine the number of Units, if any, of APS which each such Potential Holder offers to purchase if the Applicable Rate for the next succeeding Dividend Period shall not be less than the rate per annum specified by such Potential Holder.

For the purposes hereof, the communication to a Broker-Dealer of information referred to in clause (i)(A), (i)(B), (i)(C) or (ii) of this paragraph (a) is hereinafter referred to as an "Order" and collectively as "Orders" and each Existing Holder and each Potential Holder placing an Order is hereinafter referred to as a "Bidder" and collectively as "Bidders;" an Order containing the information referred to in clause (i)(A) of

this paragraph (a) is hereinafter referred to as a "Hold Order" and collectively as "Hold Orders;" an Order containing the information referred to in clause (i)(B) or (ii) of this paragraph (a) is hereinafter referred to as a "Bid" and collectively as "Bids;" and an Order containing the information referred to in clause (i)(C) of this paragraph (a) is hereinafter referred to as a "Sell Order" and collectively as "Sell Orders."

(b)(i) A Bid by an Existing Holder shall constitute an irrevocable offer to sell:

(A) the number of Outstanding Units of APS specified in such Bid if the Applicable Rate determined on such Auction Date shall be less than the rate specified therein;

(B) such number or a lesser number of Outstanding Units of APS to be determined as set forth in clause (iv) of paragraph (a) of Section 5 of this Part II if the Applicable Rate determined on such Auction Date shall be equal to the rate specified therein; or

(C) a lesser number of Outstanding Units of APS to be determined as set forth in clause (iii) of paragraph (b) of Section 5 of this Part II if the rate specified therein shall be higher than the Maximum Rate and Sufficient Clearing Bids do not exist.

(ii) A Sell Order by an Existing Holder shall constitute an irrevocable offer to sell:

(A) the number of Outstanding Units of APS specified in such Sell Order; or

(B) such number or a lesser number of Outstanding Units of APS as set forth in clause (iii) of paragraph (b) of Section 5 of this Part II if Sufficient Clearing Bids do not exist.

(iii) A Bid by a Potential Holder shall constitute an irrevocable offer to purchase:

(A) the number of Outstanding Units of APS specified in such Bid if the Applicable Rate determined on such Auction Date shall be higher than the rate specified therein; or

(B) such number or a lesser number of Outstanding Units of APS as set forth in clause (v) of paragraph (a) of Section 5 of this Part II if the Applicable Rate determined on such Auction Date shall be equal to the rate specified therein.

3. Submission of Orders by Broker-Dealers to Trust Company.

(a) Each Broker-Dealer shall submit in writing to the Trust Company prior to the Submission Deadline on each Auction Date all Orders obtained by such Broker-Dealer and shall specify with respect to each Order:

(i) the name of the Bidder placing such Order;

(ii) the aggregate number of Units of a series of APS that are the subject of such Order;

(iii) to the extent that such Bidder is an Existing Holder:

(A) the number of Units, if any, of such series of APS subject to any Hold Order placed by such Existing Holder;

(B) the number of Units, if any, of such series of APS subject to any Bid placed by such Existing Holder and the rate specified in such Bid; and

(C) the number of Units, if any, of such series of APS subject to any Sell Order placed by such Existing Holder; and

(iv) to the extent that such Bidder is a Potential Holder, the rate and number of Units specified in such Potential Holder's Bid.

(b) If any rate specified in any Bid contains more than three figures to the right of the decimal point, the Trust Company shall round such rate up to the next highest one thousandth (.001) of 1%.

(c) If an Order or Orders covering all of the Outstanding Units of a series of APS held by an Existing Holder is not submitted to the Trust Company prior to the Submission Deadline, the Trust Company shall deem a Hold Order to have been submitted on behalf of such Existing Holder covering the number of Outstanding Units of such series of APS held by such Existing Holder and not subject to Orders submitted to the Trust Company.

(d) If one or more Orders covering in the aggregate more than the number of Outstanding Units of a series of APS held by any Existing Holder are submitted to the Trust Company, such Orders shall be considered valid as follows and in the following order of priority:

(i) all Hold Orders shall be considered valid, but only up to and including in the aggregate the number of Outstanding Units of such series of APS held by such Existing Holder, and, solely for purposes of allocating compensation among the Broker-Dealers submitting Hold Orders, if the number of Units of such series of APS subject to such Hold Orders exceeds the number of Outstanding Units of such series of APS held by such Existing Holder, the number of Units subject to each such Hold Order shall be reduced pro rata to cover the number of Outstanding Units of such series of APS held by such Existing Holder;

(ii) (A) any Bid shall be considered valid up to and including the excess of the number of Outstanding Units of such series of APS held by such Existing Holder over the number of Units of such series of APS subject to any Hold Orders referred to in clause (i) above;

(B) subject to subclause (A), if more than one Bid with the same rate is submitted on behalf of such Existing Holder and the number of Outstanding Units of such series of APS subject to such Bids is greater than such excess, such Bids shall be considered valid up to and including the amount of such excess, and, solely for purposes of allocating compensation among the Broker-Dealers submitting Bids with the same rate, the number of Units of such series of APS subject to each Bid with the same rate shall be reduced pro rata to cover the number of Units of such series of APS equal to such excess;

(C) subject to subclause (A), if more than one Bid with different rates is submitted on behalf of such Existing Holder, such Bids shall be considered valid in the ascending order of their respective rates up to and including the amount of such excess; and

(D) in any such event, the number, if any, of such Outstanding Units of such series of APS subject to Bids not valid under this clause (ii) shall be treated as the subject of a Bid by a Potential Holder at the rate therein specified; and

(iii) all Sell Orders shall be considered valid up to and including the excess of the number of Outstanding Units of such series of APS held by such Existing Holder over the sum of the Units of such series of APS subject to valid Hold Orders referred to in clause (i) above and valid Bids by such Existing Holder referred to in clause (ii) above.

(e) If more than one Bid is submitted on behalf of any Potential Holder, each Bid submitted shall be a separate Bid with the rate and number of Units therein specified.

(f) Orders by Existing Holders and Potential Holders must specify numbers of Units of a series of APS in whole Units. Any Order that specifies a number of Units of a series of APS other than in whole Units will not be accepted and will not be considered a Submitted Order for purposes of an Auction.

4. Determination of Sufficient Clearing Bids, Winning Bid Rate and Applicable Rate.

(a) Not earlier than the Submission Deadline on each Auction Date with respect to each series of APS, the Trust Company shall assemble all Orders relating to such series submitted or deemed submitted to it by the Broker-Dealers (each such Order as submitted or deemed submitted by a Broker-Dealer being hereinafter referred to individually as a "Submitted Hold Order," a "Submitted Bid" or a "Submitted Sell Order," as the

case may be, or as a "Submitted Order" and collectively as "Submitted Hold Orders," "Submitted Bids" or "Submitted Sell Orders," as the case may be, or as "Submitted Orders") and shall determine:

(i) the excess of the total number of Outstanding Units of such series of APS over the number of Outstanding Units of such series of APS that are the subject of Submitted Hold Orders (such excess being hereinafter referred to as the "Available APS");

(ii) from the Submitted Orders whether:

(A) the number of Outstanding Units of such series of APS that are the subject of Submitted Bids by Potential Holders specifying one or more rates equal to or lower than the Maximum Rate; exceeds or is equal to the sum of:

(B) the number of Outstanding Units of such series of APS that are the subject of Submitted Bids by Existing Holders specifying one or more rates higher than the Maximum Rate; and

(C) the number of Outstanding Units of such series of APS that are subject to Submitted Sell Orders;

(in the event of such excess or such equality (other than because the number of Units of such series of APS in subclauses (B) and (C) above is zero because all of the Outstanding Units of such series of APS are the subject of Submitted Hold Orders), such Submitted Bids in subclause (A) above being hereinafter referred to collectively as "Sufficient Clearing Bids"); and

(iii) if Sufficient Clearing Bids exist, the lowest rate specified in the Submitted Bids (the "Winning Bid Rate") which if:

(A) (I) each Submitted Bid from Existing Holders specifying such lowest rate and (II) all other Submitted Bids from Existing Holders specifying lower rates were accepted, thus entitling such Existing Holders to continue to hold the Units of such series of APS that are the subject of such Submitted Bids; and

(B) (I) each Submitted Bid from Potential Holders specifying such lowest rate and (II) all other Submitted Bids from Potential Holders specifying lower rates were accepted, thus entitling the Potential Holders to purchase the Units of APS that are the subject of those Submitted Bids,

would result in such Existing Holders continuing to hold an aggregate number of Outstanding Units of such series of APS which, when added to the number of Outstanding Units of such series of APS to be purchased by such Potential Holders, would equal not less than the Available APS with respect to such series.

(b) Promptly after the Trust Company has made the determinations pursuant to paragraph (a) of this Section 4, the Trust Company shall advise the Corporation of the "AA" Composite Commercial Paper Rate and the Maximum Rate on the Auction Date with respect to each series of APS and, based on such determinations, the Applicable Rate for such series for the next succeeding Dividend Period as follows:

(i) if Sufficient Clearing Bids exist, that the Applicable Rate for the next succeeding Dividend Period shall be equal to the Winning Bid Rate so determined;

(ii) if Sufficient Clearing Bids do not exist (other than because all the Outstanding Units of APS are the subject of Submitted Hold Orders), that the Applicable Rate for the next succeeding Dividend Period shall be equal to the Maximum Rate; or

(iii) if all of the Outstanding Units of such series of APS are the subject of Submitted Hold Orders, that the Applicable Rate for the next succeeding Dividend Period shall be equal to 58% of the "AA" Composite Commercial Paper Rate.

5. Acceptance and Rejection of Submitted Bids and Submitted Sell Orders and Allocation of Units. Existing Holders shall continue to hold the Units of a series of APS that are the subject of Submitted Hold Orders, and based on the determinations made pursuant to paragraph (a) of Section 4 of this Part II,

the Submitted Bids and Submitted Sell Orders shall be accepted or rejected and the Trust Company shall take such other action as set forth below with respect to such series:

(a) If Sufficient Clearing Bids have been made, all Submitted Sell Orders shall be accepted, and subject to the provisions of paragraphs (d) and (e) of this Section 5, Submitted Bids shall be accepted or rejected as follows in the following order of priority and all other Submitted Bids shall be rejected:

(i) the Submitted Sell Orders of Existing Holders shall be accepted and Existing Holders' Submitted Bids specifying any rate that is higher than the Winning Bid Rate shall be rejected, thus requiring each such Existing Holder to sell the Units of APS that are the subject of such Submitted Sell Orders or Submitted Bids;

(ii) Existing Holders' Submitted Bids specifying any rate that is lower than the Winning Bid Rate shall be accepted, thus entitling each such Existing Holder to continue to hold the Units of APS that are the subject of such Submitted Bids;

(iii) Potential Holders' Submitted Bids specifying any rate that is lower than the Winning Bid Rate shall be accepted;

(iv) each Existing Holder's Submitted Bid specifying a rate that is equal to the Winning Bid Rate shall be accepted, thus entitling each such Existing Holder to continue to hold the Units of APS that are the subject of such Submitted Bid, unless the number of Outstanding Units of APS subject to all such Submitted Bids shall be greater than the number of Units of such series of APS ("remaining Units") equal to the excess of the Available APS of such series over the number of Units of APS subject to Submitted Bids described in clauses (ii) and (iii) of this paragraph (a), in which event such Submitted Bid of such Existing Holder shall be accepted in part, and such Existing Holder shall be required to sell Units of APS subject to such Submitted Bid, but only in an amount equal to the difference between (A) the number of Outstanding Units of APS then held by such Existing Holder subject to such Submitted Bid and (B) the number of Units of such series of APS obtained by multiplying the number of remaining Units of such series by a fraction the numerator of which shall be the number of Outstanding Units of such series of APS held by such Existing Holder subject to such Submitted Bid and the denominator of which shall be the aggregate number of Outstanding Units of APS subject to such Submitted Bids made by all such Existing Holders that specified a rate equal to the Winning Bid Rate; and

(v) each Potential Holder's Submitted Bid specifying a rate that is equal to the Winning Bid Rate shall be accepted but only in an amount equal to the number of Units of APS obtained by multiplying the difference between the Available APS of such series and the number of Units of APS subject to Submitted Bids described in clauses (ii), (iii) and (iv) of this paragraph (a) by a fraction the numerator of which shall be the number of Outstanding Units of APS subject to such Submitted Bid and the denominator of which shall be the aggregate number of Outstanding Units of APS subject to such Submitted Bids made by all such Potential Holders that specified a rate equal to the Winning Bid Rate.

(b) If Sufficient Clearing Bids have not been made (other than because all of the Outstanding Units of such series of APS are the subject of Submitted Hold Orders), subject to the provisions of paragraph (d) of this Section 5, Submitted Orders shall be accepted or rejected as follows in the following order of priority, and all other Submitted Bids shall be rejected:

(i) Existing Holders' Submitted Bids specifying any rate that is equal to or lower than the Maximum Rate shall be accepted, thus entitling such Existing Holders to continue to hold the Units of APS that are the subject of such Submitted Bids;

(ii) Potential Holders' Submitted Bids specifying any rate that is equal to or lower than the Maximum Rate shall be accepted; and

(iii) each Existing Holder's Submitted Bid specifying any rate that is higher than the Maximum Rate shall be rejected and the Submitted Sell Order of each Existing Holder shall be accepted, but in both cases only in an amount equal to the difference between (A) the number of Outstanding Units of

APS then held by such Existing Holder subject to such Submitted Bid or Submitted Sell Order and (B) the number of Units of APS obtained by multiplying the difference between the Available APS of such series and the aggregate number of Units of APS subject to Submitted Bids described in clauses (i) and (ii) of this paragraph (b) by a fraction the numerator of which shall be the number of Outstanding Units of APS held by such Existing Holder subject to such Submitted Bid or Submitted Sell Order and the denominator of which shall be the aggregate number of Outstanding Units of APS subject to all such Submitted Bids and Submitted Sell Orders.

(c) If all of the Outstanding Units of APS are the subject of Submitted Hold Orders, all Submitted Bids shall be rejected.

(d) If, as a result of the procedures described in paragraph (a) or (b) of this Section 5, any Existing Holder would be entitled or required to sell, or any Potential Holder would be entitled or required to purchase, Units of APS other than in whole Units on any Auction Date, the Trust Company shall, in such manner as, in its sole discretion, it shall determine, round up or down the number of Units of APS to be purchased or sold by any Existing Holder or Potential Holder on such Auction Date so that the number of Units purchased or sold by each Existing Holder or Potential Holder on such Auction Date shall be whole Units of APS.

(e) If, as a result of the procedures described in paragraph (a) of this Section 5, any Potential Holder would be entitled or required to purchase less than a whole Unit on any Auction Date, the Trust Company shall, in such manner as, in its sole discretion, it shall determine, allocate Units for purchase among Potential Holders so that only whole Units of APS are purchased on such Auction Date by any Potential Holder, even if such allocation results in one or more of such Potential Holders not purchasing Units of APS on such Auction Date.

(f) Based on the results of each Auction, the Trust Company shall determine the aggregate number of Units of APS to be purchased and the aggregate number of Units of APS to be sold by Potential Holders and Existing Holders on whose behalf each Broker-Dealer submitted Bids or Sell Orders and, with respect to each Broker-Dealer, to the extent that such aggregate number of Units to be purchased and such aggregate number of Units to be sold differ, determine to which other Broker-Dealer or Broker-Dealers acting for one or more purchasers such Broker-Dealer shall deliver, or from which other Broker-Dealer or Broker-Dealers acting for one or more sellers such Broker-Dealer shall receive, as the case may be, Units of APS.

6. Miscellaneous.

(a) The Board of Directors of the Corporation may interpret the provisions of this Part II to resolve any inconsistency or ambiguity which may arise or be revealed in connection with the Auction Procedures provided for herein, and if such inconsistency or ambiguity reflects an inaccurate provision hereof, the Board of Directors of the Corporation may, in appropriate circumstances, authorize the filing of Articles of Correction.

(b) For so long as the Corporation has not failed to pay to the Paying Agent the full amount of any dividend or the redemption price of any shares of APS called for redemption on or within three Business Days after the date when due, an Existing Holder (i) may sell, transfer or otherwise dispose of shares of APS only pursuant to a Bid or Sell Order in accordance with the procedures described in this Part II or to or through a Broker-Dealer or to a Person that has delivered a signed copy of a Master Purchaser's Letter to the Trust Company, provided that in the case of all transfers other than pursuant to Auctions, such Existing Holder, its Broker-Dealer or its Agent Member advises the Trust Company of such transfer, and (ii) shall have the ownership of the shares of APS held by it maintained in book entry form by the Securities Depository for the account of its Agent Member, which in turn will maintain records of such Existing Holder's beneficial ownership. Shares of APS may be sold or transferred only in whole Units.

(c) Neither the Corporation nor any affiliate thereof may submit an Order in any Auction except as set forth in the next sentence. Any Broker-Dealer that is an affiliate of the Corporation may submit Orders in Auctions but only if such Orders are not for its own account, except that if such affiliated Broker-Dealer holds shares of APS for its own account, it must submit a Sell Order in the next Auction with respect to such shares.

(d) Commencing with the first day of the first Dividend Period for which the Applicable Rate for a particular series of APS is 150% of the 60-day "AA" Composite Commercial Paper Rate as a result of a failure to pay a dividend amount or redemption price on or within three Business Days after the date when due, as set forth in subparagraph (c)(i) of Section 2 of Part I hereof, the Corporation or an Affiliate thereof at the option of the Corporation, may perform any of the functions to be performed by the Trust Company set forth herein with respect to such series.

APPENDIX B

SETTLEMENT PROCEDURES

Capitalized terms used herein shall have the respective meanings specified in the forepart of this Prospectus or Appendix A hereto, as the case may be.

- (a) On each Auction Date, the Trust Company shall notify by telephone the Broker-Dealers that participated in the Auction held on such Auction Date and submitted an Order on behalf of any Existing Holder or Potential Holder:
 - (i) of the Applicable Rate fixed for the next succeeding Dividend Period;
 - (ii) whether Sufficient Clearing Bids existed for the determination of the Applicable Rate;
 - (iii) if such Broker-Dealer submitted a Bid or a Sell Order on behalf of an Existing Holder, whether such Bid or Sell Order was accepted or rejected, in whole or in part, and the number of Units, if any, of APS then Outstanding to be sold by such Existing Holder;
 - (iv) if such Broker-Dealer submitted a Bid on behalf of a Potential Holder, whether such Bid was accepted or rejected, in whole or in part, and the number of Units, if any, of APS to be purchased by such Potential Holder;
 - (v) if the aggregate number of Units of APS to be sold by all Existing Holders on whose behalf such Broker-Dealer submitted Bids or Sell Orders is different from the aggregate number of Units of APS to be purchased by all Potential Holders on whose behalf such Broker-Dealer submitted Bids, the name or names of one or more other Broker-Dealers (and the Agent Member, if any, of each such other Broker-Dealer) and the number of Units of APS to be (x) purchased from one or more Existing Holders on whose behalf such other Broker-Dealers submitted Bids or Sell Orders, or (y) sold to one or more Potential Holders on whose behalf such other Broker-Dealers submitted Bids; and
 - (vi) the Auction Date of the next succeeding Auction.
- (b) On each Auction Date, each Broker-Dealer that submitted an Order on behalf of any Existing Holder or Potential Holder shall:
 - (i) advise each Existing Holder and Potential Holder on whose behalf such Broker-Dealer submitted a Bid or Sell Order whether such Bid or Sell Order was accepted or rejected, in whole or in part;
 - (ii) instruct each Potential Holder on whose behalf such Broker-Dealer submitted a Bid that was accepted, in whole or in part, to instruct such Bidder's Agent Member to pay to such Broker-Dealer (or its Agent Member) through the Securities Depository the amount necessary to purchase the number of Units of APS to be purchased pursuant to such Bid against receipt of such Units;
 - (iii) instruct each Existing Holder on whose behalf such Broker-Dealer submitted a Bid that was accepted, in whole or in part, or a Sell Order that was accepted, in whole or in part, to instruct such Bidder's Agent Member to deliver to such Broker-Dealer (or its Agent Member) through the Securities Depository the number of Units of APS to be sold pursuant to such Bid or Sell Order against payment thereof;
 - (iv) advise each Existing Holder on whose behalf such Broker-Dealer submitted an Order and each Potential Holder on whose behalf such Broker-Dealer submitted a Bid of the Applicable Rate for the next succeeding Dividend Period;
 - (v) advise each Existing Holder on whose behalf such Broker-Dealer submitted an Order of the Auction Date of the next succeeding Auction; and
 - (vi) advise each Potential Holder on whose behalf such Broker-Dealer submitted a Bid that was accepted, in whole or in part, of the Auction Date for the next succeeding Auction.

(c) On the basis of the information provided to it pursuant to paragraph (a) above, each Broker-Dealer that submitted a Bid or Sell Order shall allocate any funds received by it pursuant to paragraph (b)(ii) above, and any Units of APS received by it pursuant to paragraph (b)(iii) above, among the Potential Holders, if any, on whose behalf such Broker-Dealer submitted Bids, the Existing Holders, if any, on whose behalf such Broker-Dealer submitted Bids or Sell Orders, and any Broker-Dealers identified to it by the Trust Company pursuant to paragraph (a)(v) above.

(d) On the Business Day after the Auction Date, the Securities Depository shall execute the transactions described above, debiting and crediting the accounts of the respective Agent Members as necessary to effect the purchases and sales of Units of APS as determined in the Auction.

APPENDIX C

TO BE SUBMITTED TO YOUR BROKER-DEALER WHO WILL THEN DELIVER COPIES
ON YOUR BEHALF TO THE TRUST COMPANY

MASTER PURCHASER'S LETTER

Relating to Securities Involving Rate Settings
Through Auctions

The Company
The Trust Company
A Broker-Dealer
An Agent Member
Other Persons

Dear Sirs:

1. This letter is designed to apply to publicly or privately offered debt or equity securities ("Securities") of any issuer ("Company") which are described in any final prospectus or other offering materials relating to such Securities as the same may be amended or supplemented (collectively, with respect to the particular Securities concerned, the "Prospectus") and which involve periodic rate settings through auctions ("Auctions"). This letter shall be for the benefit of any Company and of any Trust Company, auction agent, paying agent (collectively, "Trust Company"), broker-dealer, agent member, securities depository or other interested person in connection with any Securities and related Auctions (it being understood that such persons may be required to execute specified agreements and nothing herein shall alter such requirements). The terminology used herein is intended to be general in its application and not to exclude any Securities in respect of which (in the Prospectus or otherwise) alternative terminology is used.

2. We may from time to time offer to purchase, purchase, offer to sell and/or sell Securities of any Company as described in the Prospectus relating thereto. We agree that this letter shall apply to all such purchases, sales and offers and to Securities owned by us. We understand that the dividend/interest rate on Securities may be based from time to time on the results of Auctions as set forth in the Prospectus.

3. We agree that any bid or sell order placed by us in an Auction shall constitute an irrevocable offer (except as otherwise described in the Prospectus) by us to purchase or sell the Securities subject to such bid or sell order, or such lesser amount of Securities as we shall be required to sell or purchase as a result of such Auction, at the applicable price, all as set forth in the Prospectus, and that if we fail to place a bid or sell order with respect to Securities owned by us with a broker-dealer on any Auction date, or a broker-dealer to which we communicate a bid or sell order fails to submit such bid or sell order to the Trust Company concerned, we shall be deemed to have placed a hold order with respect to such Securities as described in the Prospectus. We authorize any broker-dealer that submits a bid or sell order, as our agent in Auctions to execute contracts for the sale of Securities covered by such bid or sell order. We recognize that the payment by such broker-dealer for Securities purchased on our behalf shall not relieve us of any liability to such broker-dealer for payment for such Securities.

4. We agree that, during the applicable period as described in the Prospectus, dispositions of Securities can be made only in the denominations set forth in the Prospectus and we will sell, transfer or otherwise dispose of any Securities held by us from time to time only pursuant to a bid or sell order placed in an Auction, to or through a broker-dealer or, when permitted in the Prospectus, to a person that has signed and delivered to the applicable Trust Company a letter substantially in the form of this letter (or other applicable purchaser's letter), provided that in the case of all transfers other than pursuant to Auctions we or our broker-dealer or our agent member shall advise such Trust Company of such transfer. We understand that a restrictive legend will be placed on certificates representing the Securities and stop-transfer instructions will be issued to the transfer agent and/or registrar, all as set forth in the Prospectus.

5. We agree that, during the applicable period as described in the Prospectus, ownership of Securities shall be represented by one or more global certificates registered in the name of the applicable securities depository or its nominee, that we will not be entitled to receive any certificate representing the Securities and

that our ownership of any Securities will be maintained in book entry form by the securities depository for the account of our agent member, which in turn will maintain records of our beneficial ownership. We authorize and instruct our agent member to disclose to the applicable Trust Company such information concerning our beneficial ownership of Securities as such Trust Company shall request.

6. We acknowledge that partial deliveries of Securities purchased in Auctions may be made to us and such deliveries shall constitute good delivery as set forth in the Prospectus.

7. This letter is not a commitment by us to purchase any Securities.

8. This letter supersedes any prior-dated version of this master purchaser's letter, and supplements any prior- or post-dated purchaser's letter specific to particular Securities, and this letter may only be revoked by a signed writing delivered to the original recipients hereof.

9. The descriptions of Auction procedures set forth in each applicable Prospectus are incorporated by reference herein and in case of any conflict between this letter, any purchaser's letter specific to particular Securities and any such description, such description shall control.

10. Any xerographic or other copy of this letter shall be deemed of equal effect as a signed original.

11. Our agent member of The Depository Trust Company currently is _____

12. Our personnel authorized to place orders with broker-dealers for the purpose set forth in the Prospectus in Auctions currently is/are _____, telephone number (____) _____

13. Our taxpayer identification number is _____

14. In the case of each offer to purchase, purchase, offer to sell or sale by us of Securities not registered under the Securities Act of 1933, as amended (the "Act"), we represent and agree as follows:

A. We understand and expressly acknowledge that the Securities have not been and will not be registered under the Act and, accordingly, that the Securities may not be reoffered, resold or otherwise pledged, hypothecated or transferred unless an applicable exemption from the registration requirements of the Act is available.

B. We hereby confirm that any purchase of Securities made by us will be for our own account, or for the account of one or more parties for which we are acting as trustee or agent with complete investment discretion and with authority to bind such parties, and not with a view to any public resale or distribution thereof. We and each other party for which we are acting which will acquire Securities will be "accredited investors" within the meaning of Regulation D under the Act with respect to the Securities to be purchased by us or such party, as the case may be, will have previously invested in similar types of instruments and will be able and prepared to bear the economic risk of investing in and holding such Securities.

C. We acknowledge that prior to purchasing any Securities we shall have received a Prospectus (or private placement memorandum) with respect thereto and acknowledge that we will have had access to such financial and other information, and have been afforded the opportunity to ask such questions of representatives of the Company and receive answers thereto, as we deem necessary in connection with our decision to purchase Securities.

D. We recognize that the Company and broker-dealers will rely upon the truth and accuracy of the foregoing investment representations and agreements, and we agree that each of our purchases of Securities now or in the future shall be deemed to constitute our concurrence in all of the foregoing which shall be binding on us and each party for which we are acting as set forth in Subparagraph B above.

Dated: _____

Mailing Address of Purchaser: _____ (Name of Purchaser)

By: _____

Printed Name: _____

Title: _____

EXECUTION COPY

TO BE SUBMITTED TO YOUR BROKER-DEALER WHO WILL THEN DELIVER COPIES
ON YOUR BEHALF TO THE TRUST COMPANY

MASTER PURCHASER'S LETTER

Relating to Securities Involving Rate Settings
Through Auctions

The Company
The Trust Company
A Broker-Dealer
An Agent Member
Other Persons

Dear Sirs:

1. This letter is designed to apply to publicly or privately offered debt or equity securities ("Securities") of any issuer ("Company") which are described in any final prospectus or other offering materials relating to such Securities as the same may be amended or supplemented (collectively, with respect to the particular Securities concerned, the "Prospectus") and which involve periodic rate settings through auctions ("Auctions"). This letter shall be for the benefit of any Company and of any Trust Company, auction agent, paying agent (collectively, "Trust Company"), broker-dealer, agent member, securities depository or other interested person in connection with any Securities and related Auctions (it being understood that such persons may be required to execute specified agreements and nothing herein shall alter such requirements). The terminology used herein is intended to be general in its application and not to exclude any Securities in respect of which (in the Prospectus or otherwise) alternative terminology is used.

2. We may from time to time offer to purchase, purchase, offer to sell and/or sell Securities of any Company as described in the Prospectus relating thereto. We agree that this letter shall apply to all such purchases, sales and offers and to Securities owned by us. We understand that the dividend/interest rate on Securities may be based from time to time on the results of Auctions as set forth in the Prospectus.

3. We agree that any bid or sell order placed by us in an Auction shall constitute an irrevocable offer (except as otherwise described in the Prospectus) by us to purchase or sell the Securities subject to such bid or sell order, or such lesser amount of Securities as we shall be required to sell or purchase as a result of such Auction, at the applicable price, all as set forth in the Prospectus, and that if we fail to place a bid or sell order with respect to Securities owned by us with a broker-dealer on any Auction date, or a broker-dealer to which we communicate a bid or sell order fails to submit such bid or sell order to the Trust Company concerned, we shall be deemed to have placed a hold order with respect to such Securities as described in the Prospectus. We authorize any broker-dealer that submits a bid or sell order as our agent in Auctions to execute contracts for the sale of Securities covered by such bid or sell order. We recognize that the payment by such broker-dealer for Securities purchased on our behalf shall not relieve us of any liability to such broker-dealer for payment for such Securities.

4. We agree that, during the applicable period as described in the Prospectus, dispositions of Securities can be made only in the denominations set forth in the Prospectus and we will sell, transfer or otherwise dispose of any Securities held by us from time to time only pursuant to a bid or sell order placed in an Auction, to or through a broker-dealer or, when permitted in the Prospectus, to a person that has signed and delivered to the applicable Trust Company a letter substantially in the form of this letter (or other applicable purchaser's letter), provided that in the case of all transfers other than pursuant to Auctions we or our broker-dealer or our agent member shall advise such Trust Company of such transfer. We understand that a restrictive legend will be placed on certificates representing the Securities and stop-transfer instructions will be issued to the transfer agent and/or registrar, all as set forth in the Prospectus.

5. We agree that, during the applicable period as described in the Prospectus, ownership of Securities shall be represented by one or more global certificates registered in the name of the applicable securities depository or its nominee, that we will not be entitled to receive any certificate representing the Securities and

that our ownership of any Securities will be maintained in book entry form by the securities depository for the account of our agent member, which in turn will maintain records of our beneficial ownership. We authorize and instruct our agent member to disclose to the applicable Trust Company such information concerning our beneficial ownership of Securities as such Trust Company shall request.

6. We acknowledge that partial deliveries of Securities purchased in Auctions may be made to us and such deliveries shall constitute good delivery as set forth in the Prospectus.

7. This letter is not a commitment by us to purchase any Securities.

8. This letter supersedes any prior-dated version of this master purchaser's letter, and supplements any prior- or post-dated purchaser's letter specific to particular Securities, and this letter may only be revoked by a signed writing delivered to the original recipients hereof.

9. The descriptions of Auction procedures set forth in each applicable Prospectus are incorporated by reference herein and in case of any conflict between this letter, any purchaser's letter specific to particular Securities and any such description, such description shall control.

10. Any xerographic or other copy of this letter shall be deemed of equal effect as a signed original.

11. Our agent member of The Depository Trust Company currently is _____

12. Our personnel authorized to place orders with broker-dealers for the purpose set forth in the Prospectus in Auctions currently is/are _____, telephone number () _____

13. Our taxpayer identification number is _____

14. In the case of each offer to purchase, purchase, offer to sell or sale by us of Securities not registered under the Securities Act of 1933, as amended (the "Act"), we represent and agree as follows:

A. We understand and expressly acknowledge that the Securities have not been and will not be registered under the Act and, accordingly, that the Securities may not be reoffered, resold or otherwise pledged, hypothecated or transferred unless an applicable exemption from the registration requirements of the Act is available.

B. We hereby confirm that any purchase of Securities made by us will be for our own account, or for the account of one or more parties for which we are acting as trustee or agent with complete investment discretion and with authority to bind such parties, and not with a view to any public resale or distribution thereof. We and each other party for which we are acting which will acquire Securities will be "accredited investors" within the meaning of Regulation D under the Act with respect to the Securities to be purchased by us or such party, as the case may be, will have previously invested in similar types of instruments and will be able and prepared to bear the economic risk of investing in and holding such Securities.

C. We acknowledge that prior to purchasing any Securities we shall have received a Prospectus (or private placement memorandum) with respect thereto and acknowledge that we will have had access to such financial and other information, and have been afforded the opportunity to ask such questions of representatives of the Company and receive answers thereto, as we deem necessary in connection with our decision to purchase Securities.

D. We recognize that the Company and broker-dealers will rely upon the truth and accuracy of the foregoing investment representations and agreements, and we agree that each of our purchases of Securities now or in the future shall be deemed to constitute our concurrence in all of the foregoing which shall be binding on us and each party for which we are acting as set forth in Subparagraph B above.

Dated: _____

Mailing Address of Purchaser: _____

(Name of Purchaser) _____

By: _____

Printed Name: _____

Title: _____

No person has been authorized to give any information or to make any representation other than those contained or incorporated by reference in this Prospectus and, if given or made, such information or representations must not be relied upon as having been authorized. This Prospectus does not constitute an offer to sell or the solicitation of an offer to buy any Securities other than the Securities described in this Prospectus, or an offer to sell or the solicitation of any offer to buy such Securities in any circumstances in which such offer or solicitation is unlawful. Neither the delivery of this Prospectus nor any sale made hereunder shall, under any circumstances, create any implication that the information contained or incorporated by reference herein is correct as of any time subsequent to the date of such information.

TABLE OF CONTENTS

	<u>Page</u>
Available Information	2
Incorporation of Certain Documents by Reference	2
Summary	3
The Company	6
Use of Proceeds	6
The Auction	6
Description of APS	15
Underwriting	20
Legal Opinions	21
Experts	21
Additional Information	21
Appendix A: Auction Procedures	
Appendix B: Settlement Procedures	
Appendix C: Master Purchaser's Letter	

425 Units
Auction Preferred Stock, Series A

425 Units
Auction Preferred Stock, Series B

Central Power and Light Company

PROSPECTUS

**Goldman, Sachs & Co.
Shearson Lehman Hutton Inc.**

SECURITIES AND EXCHANGE COMMISSION
Washington, D. C. 20549

FORM 10-K

**ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d)
OF THE SECURITIES EXCHANGE ACT OF 1934**

FOR THE FISCAL YEAR ENDED DECEMBER 31, 1987

COMMISSION FILE NUMBER 0-346

CENTRAL POWER AND LIGHT COMPANY

(Exact name of registrant as specified in its charter)

TEXAS

(State or other jurisdiction of
incorporation or organization)

74-0550600

(IRS Employer
Identification No.)

565 North Carancahua Street, Corpus Christi, Texas 78401-2802

(Address of principal executive offices, including zip code)

Registrant's telephone number, including area code: 512/881-5300

Securities registered pursuant to Section 12(b) of the Act:

Title of each class

Name of each exchange
on which registered

None

None

Securities registered pursuant to Section 12(g) of the Act:

Cumulative Preferred Stock, \$100 Par Value

(Title of Class)

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months and (2) has been subject to such filing requirements for the past 90 days. Yes No

Number of shares of Common Stock outstanding at December 31, 1987: 6,755,535

(None of such shares are held by non-affiliates.)

DOCUMENTS INCORPORATED BY REFERENCE

Pages 21-36 of Central Power and Light Company's Annual Report to Stockholders for the year ended December 31, 1987 are incorporated into Part II hereof.

DEFINITIONS

The following abbreviations or acronyms used in this text are defined below:

Abbreviation or Acronym	Term
AFUDC.....	Allowance for funds used during construction
ASLB.....	Atomic Safety and Licensing Board
Austin.....	Municipal electric system of Austin, Texas
Bechtel.....	Bechtel Energy Corporation
Brown & Root.....	Brown & Root, Inc.
Btu.....	British thermal unit
CEO.....	Chief Executive Officer
CERCLA.....	Comprehensive Environmental Response, Compensation and Liability Act of 1980
Company.....	Central Power and Light Company, Corpus Christi, Texas
CSW.....	Central and South West Corporation, Dallas, Texas
CSW System.....	CSW and the electric operating companies
DTPA.....	Texas Deceptive Trade Practices - Consumer Protection Act
Ebasco.....	Ebasco Services, Inc.
Electric operating companies.....	The Company, PSO, SWEPCO and WTU
EPA.....	United States Environmental Protection Agency
ERCOT.....	Electric Reliability Council of Texas
FERC.....	Federal Energy Regulatory Commission
HLP.....	Houston Lighting & Power Company
Holding Company Act.	Public Utility Holding Company Act of 1935
Houston Industries..	Houston Industries Incorporated
HVdc.....	High-voltage direct-current
Kw.....	Kilowatt
Kwh.....	Kilowatt-hour
LCRA.....	Lower Colorado River Authority
Mcf.....	1,000 cubic feet
Mw.....	Megawatt
NPDES.....	National Pollution Discharge Elimination System
NRC.....	Nuclear Regulatory Commission
Oklauunion.....	Oklauunion Power Station Unit No. 1
PCB.....	Polychlorinated biphenyl
PSD.....	Prevention of Significant Deterioration
PSO.....	Public Service Company of Oklahoma, Tulsa, Oklahoma
RCRA.....	Federal Resource Conservation and Recovery Act of 1976
Rose.....	Martha C. Rose Chemicals, Inc.
San Antonio.....	Municipal electric system of San Antonio, Texas
SEC.....	Securities and Exchange Commission
STP.....	South Texas Nuclear Project
SWEPCO.....	Southwestern Electric Power Company, Shreveport, Louisiana
TACB.....	Texas Air Control Board
Texas Commission....	Public Utility Commission of Texas
TWC.....	Texas Water Commission
WTU.....	West Texas Utilities Company, Abilene, Texas

PART I

ITEM 1. BUSINESS.

The Company. The Company, a Texas corporation, is a public utility engaged in generating, purchasing, transmitting, distributing and selling electricity in south Texas. It is a wholly-owned subsidiary of CSW, a registered public utility holding company.

At December 31, 1987, the Company supplied electric service to approximately 533,000 retail customers in a 44,000 square mile area in south Texas, with an estimated population of 1,835,000. It supplied at wholesale all or a portion of the electric energy requirements of five rural electric cooperatives and two municipal electric systems. The three largest cities served by the Company, and their estimated populations, are Corpus Christi, 260,000; Laredo, 109,000; and McAllen, 68,000.

Manufacturing, metal refining, petroleum, agriculture and tourism comprise the economic base for the Company's service territory. In 1987, industrial customers accounted for 26% of the Company's total operating revenues. Contracts with substantially all industrial customers provide for both demand and energy charges. Demand charges continue under such contracts even during periods of reduced industrial activity, thus mitigating the effect of reduced activity on operating income.

The Company carries on a continuing construction program, the nature and extent of which is based upon current and estimated future loads of its system. (See "ITEM 2. PROPERTIES -- Construction").

REGULATION AND RATES

Regulation. The Company, as a subsidiary of CSW, is subject to the jurisdiction of the SEC under the Holding Company Act with respect to the issuance, acquisition and sale of securities; acquisition and sale of certain assets or any interest in any business, including certain aspects of fuel exploration and development programs; accounting practices and other matters.

The FERC has jurisdiction under the Federal Power Act over certain of the Company's electric utility facilities and operations, including wholesale rates, and certain other matters.

The Texas Commission has exclusive jurisdiction over accounts, certification of utility service territories, sale or acquisition of certain utility property, mergers and certain other matters. Neither the governing bodies of incorporated municipalities nor the Texas Commission have jurisdiction over the issuance of securities.

Rates. The Texas Commission has original jurisdiction over retail rates in all unincorporated areas. The governing bodies of incorporated municipalities have such jurisdiction over rates within their incorporated limits. Municipalities may elect, and some have elected, to surrender this jurisdiction to the Texas Commission. The Texas Commission has appellate jurisdiction on a "de novo" basis over rates set by incorporated municipalities.

Electric utilities in Texas are not allowed to make automatic adjustments to recover changes in fuel costs from retail customers. A utility is allowed to recover its known and reasonably predictable fuel costs through a fixed fuel factor established during a general rate case, fuel reconciliation proceeding or interim fuel proceeding. An interim fuel proceeding is conducted at the request of a utility when a utility has materially over-recovered and projects to materially over-recover its known or reasonably predictable fuel costs or under such other circumstances upon the initiative of the Texas Commission. In the event that reasonably unforeseeable circumstances have resulted in a material under-recovery of known or reasonably predictable fuel costs, a utility may petition the Texas Commission for an emergency interim fuel factor; the Texas Commission must act on such petition within 30 d. In the case of an over-recovery in excess of 4% of annual fuel costs, a utility must file a petition to make interim refunds and such petition may be granted by the Texas Commission without a hearing. Final reconciliation of fuel costs are made at the time of the utility's general rate case or a reconciliation proceeding. In the event that the utility does not recover all of its fuel costs under these procedures, such event could have an adverse impact on net income. Under the Texas Commission's rules the Company made refunds of over-recovered fuel costs in 1987.

In September 1986, the Company filed an application with the FERC for an increase in base rates charged to its wholesale customers. The application requested a two-step increase of \$2.6 million and \$4.9 million, respectively. The FERC granted the Company's request to place the \$2.6 million increase in effect in December 1986, subject to refund. A settlement among parties was agreed on in the final order which increased rates by \$2.2 million per year through June 1987 and \$1.3 million thereafter. The settlement provides for customers to be individually assigned annual costs of STP Unit 1 and defers charges of \$9.2 million per year to be repaid by affected customers over a five-year period after rates reflecting STP Unit 1 in rate base are placed into effect.

In August 1987, the Texas Commission approved a rider which reduced the cost of power to the Company's large industrial customers and results in a \$13.2 million per year revenue loss that will be absorbed by the Company's stockholders until rates reflecting the Company's investment in STP in rate base are put into effect.

In November 1987, the Texas Commission approved a new contract for Occidental Chemical Corporation's caustic chlorine facility on the north shore of Corpus Christi Bay, near Ingleside. The contract provides for a combination of firm and interruptible service to the facility and results in more than \$5 million per year for the Company from the plant's operation. Similar pricing arrangements are available to other new customers of the same class.

All of the Company's contracts with its wholesale customers contain fuel-adjustment provisions that permit it to automatically pass actual fuel costs (including those associated with purchased power) through to its customers.

See "ITEM 2. PROPERTIES -- STP Construction" for information as to rates relating to STP.

OPERATIONS

Peak Loads and Capability. The following table sets forth for the years 1985 through 1987 the net capability of the Company (including the net of contracted purchases and contracted sales) at the time of peak demand, the maximum coincident system demand on a one-hour integrated basis (exclusive of sales to other electric utilities), and the respective amounts and percentages of peak demand generated by the Company and purchased from and sold to others:

Year	Net System Capability	Mw	Coincident System Demand	Mw	Percent Increase (Decrease)		Generation at Time of Peak	Mw	Net Purchases (Sales) at Time of Peak
					In Peak Demand	Over Prior Period			
					Mw	%			
1985	3,587	3,022		6.7	3,205	106.1	(183)	(6.1)	
1986	3,661	2,974		(1.6)	3,156	106.1	(182)	(6.1)	
1987	3,644*	2,881		(3.1)	2,674	92.8	207	7.2	

*This total does not include the 107 Mw of system capability represented by the generating plants in storage as described under "ITEM 2. PROPERTIES -- Facilities."

The Company is a member of ERCOT, which also includes Texas Utilities Electric Company, HLP, WTU, Texas Municipal Power Agency, Texas Municipal Power Pool, LCRA, the municipal systems of San Antonio, Austin and Brownsville, the South Texas and Medina Electric Cooperatives, and several other interconnected systems and cooperatives. The ERCOT members interchange power and energy on firm, economy and emergency bases. The Company also engages in economy interchanges with the other electric operating companies in the CSW System.

The Company, along with the remainder of the CSW System, operates on an interstate basis. The electric operating companies are installing HVdc transmission interconnections to facilitate exchanges of power. The first link, the North HVdc Tie, a 200,000 Kw tie at Oklaunion between and owned by WTU (25,000 Kw) and PSO (175,000 Kw), was completed in December 1984. The second link, known as the South HVdc Tie, was planned as a 500,000 Kw interconnection between SWEPCO and STP. In November 1987, the Texas Commission dismissed the application by the Company, SWEPCO and HLP to build the South HVdc Tie. As a result of delays in the application for the South HVdc Tie, the co-owners of this second link filed an application in May 1986 with FERC requesting approval to move this second link to a new location in Titus County in east Texas. This new project, referred to as the East HVdc Tie, is presently proposed to be a 600,000 Kw back-to-back direct-current terminal built at SWEPCO's Welsh Power Plant near Cason, Texas and a 16 mile, 345 kilovolt alternating-current transmission line from the Welsh terminal to Texas Utilities Electric Company's Monticello power plant near Mount Pleasant, Texas. The East HVdc Tie is presently proposed to be owned 50% by the Company and SWEPCO with the balance to be owned by non-affiliated

third parties. The FERC has approved the request to build the East HVdc Tie but a Certificate of Convenience and Necessity still must be obtained from the Texas Commission.

Employees. At December 31, 1987, the Company had 2,650 employees.

CENTRAL POWER AND LIGHT COMPANY

OPERATING STATISTICS

	Year Ended December 31,		
	1987	1986	1985
KILOWATT-HOUR SALES (Millions):			
Residential	4,630	4,568	4,470
Commercial	3,736	3,734	3,664
Industrial	4,325	5,522	5,985
Electric utilities and other..	325	351	347
Sales to retail customers ..	13,046	14,175	14,466
Sales for resale	982	1,465	1,155
Total	<u>14,028</u>	<u>15,640</u>	<u>15,621</u>
NUMBER OF ELECTRIC CUSTOMERS AT END OF PERIOD:			
Residential	452,449	447,554	441,411
Commercial	70,310	70,017	69,799
Industrial	6,503	6,599	6,824
Electric utilities and other..	3,284	3,222	3,247
Total	<u>532,546</u>	<u>527,392</u>	<u>521,281</u>
RESIDENTIAL SALES AVERAGES:			
Kwh per customer	10,369	10,338	10,325
Revenue per customer	\$612	\$644	\$682
Revenue per Kwh	5.90¢	6.22¢	6.60¢
REVENUES PER KWH ON TOTAL SALES ..	5.48¢	5.50¢	5.92¢
FUEL COST DATA:			
Average Btu per net Kwh	10,164	10,174	10,040
Cost per million Btu	\$2.08	\$2.33	\$2.89
Cost per Kwh generated	2.12¢	2.37¢	2.90¢
Cost as a percentage of revenue	39.6	45.6	52.2

The Company has experienced some loss of industrial load due to plants either closing or installing cogeneration facilities. It is expected that further losses may occur. The Company plans to file economic development tariffs with the Texas Commission in early 1988. These tariffs are designed to provide rate incentives for present and new industrial customers to promote Kwh sales to this class. The Company cannot predict the outcome of these actions.

FUEL SUPPLY

General. The Company's present electric generating plants and those under construction, showing the type of fuel used and to be used, are set forth under "ITEM 2. PROPERTIES." All planned base load units are expected to use coal or nuclear fuel.

During 1987, approximately 70% of Kwh generation was from gas and 30% from coal. Natural gas requirements totaled 98,199,000 Mcf and coal requirements were 2,075,000 tons.

Natural Gas. The Company's eight gas-fired electric generating plants are supplied by 23 separate long-term natural gas purchase agreements accounting for approximately 52% of the total gas requirements in 1987. The balance of the Company's natural gas requirements could have been supplied under existing long-term arrangements. However, with the soft spot market existing during the period, the Company elected to purchase most of these requirements under spot market arrangements. The Company's principal long-term gas supplies are those provided under the long-term firm agreements with Valero Transmission Company, Enron Industrial Natural Gas Co. and Corpus Christi Gas Marketing, Inc. They supplied approximately 14%, 14% and 5%, respectively, of the Company's total natural gas purchases. These agreements expire in 1992, 1990 and 1991, respectively. Including spot market suppliers, the Company had 36 individual suppliers of natural gas during 1987.

Coal. The Company's two coal-fired electric generating plants, Coleto Creek and Oklaunion, are both primarily supplied by single long-term coal purchase agreements. At Coleto Creek, the long-term agreement, which expires in 1994, is with Colowyo Coal Company and provides approximately 75% of the coal requirements of the plant. The coal is mined in northwestern Colorado and is transported approximately 1,400 miles under a long-term rail agreement with the Denver & Rio Grande Western Railroad Company, the Burlington Northern Railroad Company, and the Southern Pacific Transportation Company. The balance of the Coleto Creek requirements are currently being procured on the spot market. At year-end 1987 the Company had approximately 325,000 tons of coal in inventory at Coleto Creek. At Oklaunion, the long-term coal supply is provided under a twenty year agreement with Exxon Coal USA, Inc. This agreement is for Wyoming coal which is railed approximately 1,100 miles to the plant by the Burlington Northern Railroad Company. All of the 1987 Oklaunion coal requirements were supplied under the Exxon Agreement. The December 31, 1987 coal inventory at Oklaunion was approximately 298,000 tons.

Nuclear Fuel. The nuclear fuel cycle entails several steps, including purchase of uranium concentrate, conversion of uranium concentrate to uranium hexafluoride, enrichment of uranium hexafluoride in the isotope

U235, fabrication of the enriched uranium into fuel rods and fuel assemblies, and reprocessing of spent fuel rods. Fuel requirements for STP (see "ITEM 2. PROPERTIES -- STP Construction") are being handled by a committee comprised of representatives of all participants in STP.

The Company and the other STP participants have entered into contracts with suppliers for an equivalent of approximately 12 million pounds of uranium concentrate, which quantity would be sufficient for the initial cores and 10 years of fuel reloads for both STP units. Enrichment contracts have been secured for a 30-year period for each unit. Contracts have been secured for conversion of the initial cores and approximately six annual reloads for both units. Also, fuel fabrication services have been contracted for the initial cores and 16 years of operation of each unit. The Company believes it will be able to obtain adequate supplies of nuclear fuel components and services that will be required for STP.

No commercial nuclear fuel reprocessing is presently permitted in the United States. If spent fuel cannot be reprocessed, it must either be stored permanently or treated as waste for disposal. No permanent waste disposal facilities are currently available. The Nuclear Waste Policy Act of 1982 provides that the Federal government, beginning not later than January 31, 1998, will dispose of spent nuclear fuel in return for the payment of certain fees. These fees will be established by the Federal government to allow full cost recovery. It also requires the Federal government to take title to the spent fuel at the reactor site and assigns the responsibility for transportation of the spent fuel to the Federal government. STP is currently planned to have on site storage facilities with the capability to store up to 30 years of spent fuel discharged from each unit.

Governmental Regulation. The price and availability of each of the foregoing fuel types are significantly affected by governmental regulation. Any inability in the future to obtain adequate fuel supplies or adoption of additional regulatory measures restricting the use of such fuels for the generation of electricity might affect the Company's ability to meet economically the needs of its customers and could require it to supplement or replace, prior to normal retirement, existing generating capability with units using other fuels. This would be impossible to accomplish quickly, would require additional expenditures for construction and could have a significant adverse effect on the Company's financial position, revenues and income.

Fuel Costs. In recent years, the Company has been able to reduce unit fuel costs by taking advantage of favorable pricing in the natural gas market, renegotiating some of its long-term contracts to allow more volume/price flexibility and making spot purchases of coal at reduced prices. Information as to historic costs of fuel appears under "OPERATING STATISTICS." The Company is unable to predict accurately the cost of fuel in the future.

ENVIRONMENTAL MATTERS

The Company is subject to regulation with respect to air and water quality and solid waste standards, along with other environmental matters.

by various Federal, state and local authorities. These authorities have continuing jurisdiction in most cases to require modifications in the Company's facilities and operations. The Company is not a party to any litigation or administrative proceedings with respect to environmental matters, except as described below.

Air Quality. The TACB has jurisdiction over air quality standards and emission limitations, except for standards imposed by the PSD program which the EPA administers. The Company complies with regulations of the TACB, which require permits for all generating units on which construction is commenced or units that are substantially modified after the effective date of the applicable regulations. The Company believes that all of its present units comply in all material respects with existing Federal, state and local air quality and emission regulations. Permits have been received for the STP plant, subject to final operating approval on the basis of start-up tests to be conducted during initial operations.

The EPA has approved and may enforce air standards and limitations, which have been adopted by the TACB, and has adopted ambient air quality standards for all new or substantially modified generating units. Currently, no modifications of existing plants are expected which may require permits or permit amendments under current EPA or TACB regulations. The Clean Air Act Amendments of 1977 provide for limitations on certain new or expanded emission sources and require use of emission control devices or precombustion fuel cleaning for such sources, except under limited circumstances. Such requirements could affect the siting, construction and cost of future generating units.

Water Quality. The TWC and EPA have jurisdiction over all waste water discharges into waters of the state. The TWC has jurisdiction for establishing water quality standards and issuing permits covering discharges which might affect the quality of state waters. The EPA has jurisdiction over "point source" discharges through the NPDES provisions of the Clean Water Act. The Company has obtained or is renewing all required Federal and state waste water permits for facilities currently in operation. The project manager has obtained Federal and state permits for STP.

Solid Waste Disposal. The EPA and the TWC solid waste rules provide for comprehensive control of all solid wastes from generation to final disposal. The TWC has received authorization from EPA to administer the RCRA program in the State of Texas. The Company believes it is in compliance with all such applicable regulations.

CERCLA and Other. Under CERCLA, owners, operators, transporters and/or generators of hazardous substances for disposal can be held liable for the cleanup of hazardous substance disposal sites which pose or may pose an imminent risk to the public or environment. Similar liabilities for hazardous substance disposal can arise under applicable state law.

In November 1985, the Texas Attorney General's office brought suit against the Company under the Solid Waste Disposal Act, alleging that the Company was one of the parties responsible for PCB contamination at the Industrial Road Site in Corpus Christi, Texas and therefore should be responsible for the cleanup of the site. The site was used by several metal salvage companies, electric utilities, including the Company, and other

companies for the salvage of various materials. Depositions continue to be taken in this case.

In December 1986, the EPA named 650 entities including the Company as potentially responsible parties for cleaning up PCB contamination at a processing facility in Holden, Missouri, formerly operated by Rose. In September 1984, the Company shipped 11 transformers containing PCBs to the site for treatment and disposal. In April 1985, the Company received certificates of processing from Rose which indicated that all of the Company's transformers had been properly treated and disposed. In March 1986, Rose ceased operations and abandoned its Holden facility, leaving large quantities of PCB materials untreated and/or improperly disposed. Subsequently, major shippers of materials to the site formed a generator's group to work with the EPA on a site assessment and appropriate response actions. The Company is a member of the generator's group and has agreed to cooperate in the site investigation and, to the extent of its liability, to participate in the site cleanup process. The Company is presently unable to ascertain what portion of the ultimate cleanup costs will be assessed to it.

ITEM 2. PROPERTIES.

Facilities. At December 31, 1987, the Company owned and operated the following electric generating plants (or portion thereof in the case of the jointly owned Oklaunion plant). (See "ITEM 1. BUSINESS -- FUEL SUPPLY").

Plant Name and Location	Type of Fuel	Net Dependable Capability Mw
	Primary/Secondary	-----
Barney M. Davis Corpus Christi, Texas	gas/oil(a) gas/oil	334 338
Coleto Creek Goliad, Texas	coal	605
Lon C. Hill Corpus Christi, Texas	gas/oil(a)	557
Nueces Bay Corpus Christi, Texas	gas/oil(a)	536
Victoria Victoria, Texas	gas/oil(a)	246(b)
La Palma San Benito, Texas	gas/oil gas/oil(a)	43 156(b)
E. S. Joslin Point Comfort, Texas	gas/oil(a)	257
J. L. Bates Mission, Texas	gas/oil(a)	183
Laredo Laredo, Texas	gas/oil(a) gas/oil	65 104
Eagle Pass Eagle Pass, Texas	hydro	6
Oklauunion(c) Vernon, Texas	coal	52 ----- 3,482

-
- (a) For extended periods of operation, oil can be used only in combination with gas. Use of oil in facilities primarily designed to burn gas results in increased maintenance expense and a reduction of 5% to 10% in capability.
- (b) Excludes units in long-term storage - 229 Mw at Victoria and 47 Mw at La Palma.
- (c) The Company owns 7.81% of the 665 Mw unit operated by WTU.

All of the generating plants described above are located on land owned by the Company. The Company's electric transmission and distribution facilities are for the most part located over or under highways, streets and other public places or property owned by others, for which permits, grants, easements or licenses (deemed satisfactory, but without examination of underlying land titles) have been obtained. The principal plants and properties of the Company are subject to the lien of the first mortgage indenture under which the Company's first mortgage bonds are issued.

Construction. The estimated total capital expenditures (including AFUDC) for the years 1988-1990 are as follows:

	1988	1989	1990	Total
	----	----	----	-----
(Millions)				
Generation	\$252	\$ 64	\$ 15	\$331
Transmission	11	49	30	90
Distribution.....	32	39	41	112
Fuel	19	20	14	53
Other	8	8	9	25
	----	----	----	-----
Total (a)	\$322	\$180	\$109	\$611
	----	----	----	-----

(a) Includes AFUDC in the following amounts: 1988 - \$124,000,000; 1989 - \$34,000,000; 1990 - \$5,000,000.

The following table shows the Company's estimated costs and expenditures (including AFUDC) for its 25.2% interest in each of the 1,250 Mw units at STP that are jointly owned with non-affiliated participants.

Plant & Unit No.	Fuel	Mw	Scheduled Planned Capability	Estimated Cost For Service	Expenditures	
			(peak season)	Total (Millions)	Through Dec. 31, 1987 Per Kw (Millions)	
STP Unit No. 1	Nuclear	315	1988))	\$2,246(*)	\$3,565(*) \$1,948
STP Unit No. 2	Nuclear	315	1989))		

(*) The project's estimated cost net of related deferred taxes of \$156 million is approximately \$2,090 million or \$3,317 per Kw.

Information in the foregoing tables is subject to change due to numerous factors, including the rate of load growth, escalation of construction costs, changes in nuclear and environmental regulation, delays

in obtaining permits and from regulatory hearings, the adequacy of rate relief and the availability of necessary external capital (see "Financing" below). Changes in these and other factors could result in the adjustment of the ownership percentage of CSW joint units, or cause the Company to defer or accelerate construction or to sell or buy more power, which would affect its cash position, revenues and income to an extent that cannot now be reliably predicted.

STP - General. STP is a two-unit, 2,500 Mw nuclear power plant under construction near Bay City, Texas. In addition to the Company's 25.2% share in STP, HLP owns a 30.8% interest, San Antonio owns 28.0%, and Austin owns 16.0%. HLP is the project manager, Bechtel is responsible for the engineering, design and construction management services and Ebasco is the project constructor. Unit 1 has been completed and in August 1987 HLP received a license from the NRC authorizing fuel loading and low-power testing of the unit. As of the end of 1987, construction was estimated by Bechtel to be 88% complete on Unit 2 and 95% complete on the overall project. The nuclear fuel for Unit 1 was loaded in August, and low-power testing began. Unit 1 began using nuclear fuel to generate thermal output in early March 1988. The NRC is expected to vote on granting a full-power operating license for Unit 1 prior to April 1988. The steps remaining before Unit 1 can be placed into commercial operation are satisfactory completion of the low-power operation and the receipt from the NRC of a full-power operating license.

In September 1987, HLP and Bechtel released the 1987 Completion Assessment (the "Assessment"), which increased the forecasted completion cost of the plant by \$300 million. Including the proceeds received from the Brown & Root litigation settlement (described below), the total forecasted cost of the plant was reduced from approximately \$5.5 billion to \$5.3 billion, assuming an in-service date in February 1988.

In November 1987, the projected in-service date for Unit 1 was delayed to March 1988, reflecting difficulties encountered with certain equipment during pre-critical testing. Equipment problems identified have been corrected.

The NRC, after completing an operational readiness review of Unit 1 in January 1988, identified a need for additional operator training which has been undertaken. Certain delays have postponed HLP's application to the NRC for a full-power license, and while the Company and CSW are certain that the plant will not begin commercial operation in March as previously scheduled, they do believe that Unit 1 will be in operation prior to the peak load of 1988, assuming that no additional delays are required as a result of any findings from the NRC's current investigation (described below) or as a result of other now unidentified difficulties. The peak load typically occurs during August of each year. The delayed in-service date of STP Unit 1 is not expected to have a significant effect on the estimated cash cost. Assuming an in-service date for Unit 1 of June 1988 for the purpose of determining costs only, the Company's estimated cost of STP, including AFUDC of \$836 million, is \$2,246 million. The estimated total cost, net of related deferred taxes of \$156 million, is \$2,090 million. If the actual in-service date varies from June, the estimated amount of AFUDC would increase or decrease by approximately \$12 million a month, accordingly.

Nuclear Licensing. The construction and operation of STP are subject to the jurisdiction of the NRC. A construction permit was issued for STP in December 1975. In 1981, operating license hearings were instituted by the NRC's ASLB. In March 1984, the ASLB issued a Partial Initial Decision in Phase I of the hearings, concluding that the quality of construction at STP was acceptable and that HLP was managing the project in a manner that provided reasonable assurance that STP will be completed in accordance with NRC requirements. The ASLB completed Phase II hearings in June 1986, ruling that HLP had the character and competence to build and operate STP safely. In August 1986, the ASLB issued its final Partial Initial Decision. This decision authorized the Director of Nuclear Reactor Regulation to issue, following completion of the NRC staff review, licenses for fuel loading and operation of STP Unit 1 up to 5% power and, upon completion of requisite testing, licenses for full-power operation. The ASLB affirmed this decision in October 1986 ("ALAB-849"). In December 1986 the Secretary of the NRC notified all parties that the NRC has declined any review of ALAB-849 and that the ASLB's decision became final agency action as of December 1, 1986. This marked the favorable completion of the operating license hearings for STP.

A license for the fuel loading and low-power testing of STP Unit 2 is scheduled to be obtained from the NRC by December 1988. Unit 2 is scheduled for commercial operation in June 1989. The construction permit for Unit 2 expires in December 1989.

NRC Investigation. The NRC conducted in January 1988 an on-site investigation of allegations made by the Government Accountability Project ("GAP"), a consumer group, that STP has safety-related defects that have not been reported. Based on the result of this investigation, the NRC will determine whether further investigation is warranted. Although management cannot predict the results of this investigation, the Company and CSW believe that any concerns that might have been raised by GAP have been previously investigated and addressed.

In February 1988, HLP received a notice of violation and proposed imposition of civil penalty from the NRC, resulting from reports made by HLP and the operational readiness review concluded in January 1988. The violations cited by the NRC involved the failure to satisfy certain technical specification requirements during the testing of STP Unit 1. The notice specified a civil penalty of \$75,000 for the violations which HLP has paid. Additionally, in March 1988, HLP received another notice of violation and proposed imposition of civil penalty from the NRC specifying a \$50,000 civil penalty for violations documented in 1987 by NRC inspectors reviewing the security plan and its implementation at STP. The Company cannot predict whether HLP will receive additional penalties from the NRC.

The Company has been assured by HLP that the operational and security violations have been corrected. Management of the Company and CSW believe that these penalties will not result in additional delays in the in-service date for STP Unit 1.

Prudence Review. In 1985, the Texas Commission hired a consultant to review the prudence and efficiency of the construction of STP. In June 1986, the consultant submitted a report to the Texas Commission, covering the period from 1973 through January 1983. The consultant claimed in its

report that \$1.1 to \$1.3 billion of direct costs were spent imprudently on STP by all parties. According to the consultant's report, these amounts do not include AFUDC or rate effects that, the consultant concluded, substantially offset each other. The amounts also do not take into account the proceeds from the Brown & Root settlement (described below). The report recommended that the Texas Commission decline to review the merits of the Brown & Root settlement and concluded "that it was not unreasonable for the STP owners to settle the litigation on the terms they did." The consultant recommended that the Texas Commission inquiry into the economic viability of Unit 2 be expanded to consider both STP units and that a further investigation of whether STP should have been cancelled in 1982 may be warranted. The Company disagrees strongly with the amount specified in the consultant's report because management believes the settlement was fair, reasonable and sufficiently compensatory for the problems attributable to Brown & Root.

In January 1986, the Texas Commission staff opened a docket for the purpose of determining the prudence and efficiency of planning, management and construction of STP. The accounting treatment of the Brown & Root settlement proceeds (described below) has been consolidated with this docket. The Company and HLP filed initial direct testimony in December 1986 and supplemental direct testimony in February 1988. A new schedule for hearings is currently under review, which is expected to delay hearings until the fall of 1988. Additionally, new consultants are expected to be appointed by the Texas Commission in early 1988 to review separately HLP's and the Company's prudence related to STP. It is expected that the consultants would review and evaluate already prepared materials, which include the prior consultant's report, materials previously filed and to be filed by HLP and the Company covering the complete planning and construction period for STP, and third party reports prepared separately for HLP and the Company. It is not expected that the newly appointed consultants will undertake a comprehensive audit of STP. Company officials will present evidence at that hearing to meet the burden of proof regarding their participation in STP.

If the Texas Commission finds a portion of the STP costs in excess of the Brown & Root settlement to be imprudent, current accounting rules would require immediate write-off against earnings for any such costs that are not recoverable through rates or otherwise.

Viability Review. In March 1985, a docket was initiated for the purpose of gathering evidence concerning the economic viability of STP Unit 2. Initial hearings were held in January 1987 for the purpose of determining the appropriate computer model to be used for the economic study. Hearings in the final phase were held in October 1987 to consider the appropriate inputs for the study. An Examiner's report is expected to be issued in 1988.

Deferred Accounting and Rates. In anticipation of the completion of STP Unit 1, the Company filed with the Texas Commission in June 1987, a petition for approval of deferred accounting treatment of certain costs related to STP Unit 1. In October 1987, the Company supplemented its filing to include new information on STP available at the time and the effects of Statement of Financial Accounting Standards No. 92 ("SFAS 92"), Regulated Enterprises - Accounting for Phase-in Plans, an amendment of FASB statement

No. 71. SFAS 92 changed the accounting rules for capitalization of carrying charges associated with deferred accounting orders for financial reporting purposes.

The Company's supplemental petition anticipates a total deferral of \$232 million of expenses and carrying charges over an assumed 11-month period between commercial operation and the time rates are placed in effect reflecting Unit 1 in service. Included in this deferral is an \$87 million portion of carrying costs which the Company has requested be treated as interest to the extent interest has been incurred. The Company estimates that \$26 million of the total carrying charges could not be deferred, under SFAS 92, for financial reporting purposes. However, the Texas Commission is not restricted from allowing the Company to recover all deferred costs related to Unit 1, including all carrying costs. The petition would provide for an after-tax effect of \$144 million.

Hearings on the deferred accounting petition which were scheduled to begin December 1, 1987, have been stayed by the Supreme Court of Texas by a Writ of Mandamus. The order is in response to an appeal of a Texas Commission ruling that denied intervenor status to the Texas State Agencies because they were represented by the Attorney General of Texas. The Supreme Court heard the appeal in December 1987, and a decision is expected during the first half of 1988. All hearings and actions in the deferred accounting filing are suspended until a decision is reached by the Court. In February 1988, the Company filed a motion with the Supreme Court to lift the stay in this proceeding.

Management has no reason to believe that the Texas Commission will deny the Company's petition for deferred accounting treatment. However, if the Texas Commission were to deny the petition, or to disallow recording the carrying cost as interest to the extent interest expense is incurred, there could be a material adverse effect on the results of operations during the deferral period. If the Texas Commission does allow the Company to record the carrying cost as interest to the extent interest expense is incurred, there would still be an adverse effect on the results of operations but the amount would be considerably reduced.

The Company will need significant rate relief when STP Unit 1 is placed in commercial operation. The Company is currently reviewing its options, including alternatives to the deferred accounting petition and phase-in plans, before filing with the Texas Commission for a general rate increase to reflect the effects of STP on its financial position and results of operations. Under the current rules of the Texas Commission, post-test year adjustments are not permitted. Under a proposed rule pending before the Texas Commission, post-test year adjustments would be permitted in certain circumstances. Management cannot predict whether the proposed rule will be adopted or what form of rule may be adopted. If the Texas Commission does not adopt a rule allowing post-test year adjustments, the Company's request for rate relief could be significantly delayed. If timely rate relief is not granted by the Texas Commission allowing recovery of STP costs, it could have a material adverse effect on the results of operations.

STP Litigation. Brown & Root Suit. In December 1981, HLP filed suit against Brown & Root, the former architect, engineer and constructor for STP, and its parent company. The Company and the other participants joined

HLP in the suit, which alleged that Brown & Root breached engineering and construction contract agreements on the project. In December 1985, the Company and the other participants settled the lawsuit. The settlement agreement provided that each of the owners would receive a pro rata share of \$750 million from Brown & Root, payable in quarterly payments over seven years, without interest. The Company elected to receive \$146.8 million, the present value of its \$189 million share of the settlement, in December 1985. This amount has been recorded as a reduction in the cost of STP.

HLP Suit. The Company and CSW have received a copy of a First Amended Original Third Party Petition (the "Petition"), which HLP filed in Dallas County in the 101st Judicial District, asking the Court for authority to add the Company, CSW and San Antonio as parties to a suit (the "Austin Suit") between HLP and Austin. The Austin Suit (described below) was filed in January 1983. Austin filed a motion to strike the Petition and not allow the adding of the additional parties. HLP has also filed an original complaint in Matagorda County against the Company, CSW and San Antonio requesting the same relief as requested in the Petition.

At a hearing on January 27, 1988, the Court set the Austin Suit for trial the first week in June 1988. The Court allowed HLP to serve the Petition on the Company, CSW and San Antonio without prejudice to the right of the Company, CSW and San Antonio to assert at a later hearing that the Petition should be dismissed, severed for a separate trial in the Austin Suit or severed into a separate docket independent of the Austin Suit. A date for the subsequent hearing on this matter will be set in the near future. The Court also advised the parties that in no event would the Company, CSW and San Antonio be required to participate in the June 1988 trial between HLP and Austin. Management believes that HLP does not have a sustainable claim for contribution or indemnity against CSW or the Company.

HLP has asserted in the Petition that if it is liable to Austin for any damages in the Austin Suit, HLP is entitled to contribution or indemnity from the Company, CSW and San Antonio because all the activities complained of were decisions or activities of the STP Management Committee, which had members from all STP participants, rather than HLP's decisions as Project Manager, or that HLP was acting as an agent for the other participants and, therefore, all participants are liable for the actions complained of by Austin. HLP has alleged that CSW is a proper party to this suit because it participated through control of and direction of the Company in all major STP decisions.

HLP is also seeking a declaratory judgment construing the STP Participation Agreement to the effect that HLP, as Project Manager, has no liability to Austin, San Antonio, the Company or CSW for its actions relating to any matter complained of in the Austin Suit. HLP has also requested the Court to direct implementation of alternative methods of dispute resolution as authorized by Texas law, such as nonbinding arbitration, in order to settle the disputes related to STP.

In June 1985, HLP, the Company and San Antonio entered into a Reservation of Rights ("Rights Agreement") in which the parties agreed, subject to certain exceptions, that "in order to maintain their cooperative efforts to construct, license and operate the South Texas Project," they would forbear any formal assertion of any claims among themselves relating to STP until the commercial operation of STP Unit 2 (currently scheduled for

June 1989), but in no event beyond December 31, 1990. HLP, while claiming it has the right to file suit pursuant to an exception in the Rights Agreement, is also seeking to enforce a delay or abatement of the STP litigation until the earlier of December 31, 1990 or the commercial operation of Unit 2, allegedly pursuant to the Rights Agreement.

On March 3, 1988, pursuant to the STP Participation Agreement, the Company and San Antonio called for binding arbitration of the disputes with HLP. The arbitration call stated that HLP as Project Manager has breached its duties and obligations to the other STP participants and is liable to the Company and San Antonio for damages and that the Company and San Antonio have no liability to HLP for any portion of the damages alleged against HLP by Austin. Also on that date, the Company filed with the District Court its response to the Petition. In that response the Company requested the Court to abate both of HLP's petitions until the conclusion of arbitration, limit all action to the arbitration procedure and compel arbitration in accordance with the STP Participation Agreement in the event HLP refuses to arbitrate. Subject to its request for abatement, the Company has counterclaimed against HLP for damages in an unspecified amount related to HLP's breach of duties and obligations pursuant to the STP Participation Agreement, requested that all relief sought against the Company and CSW in the petition be denied, requested that the Court enter a declaratory judgment construing the STP Participation Agreement and declare HLP liable to the Company for breaches thereunder and stated that CSW is not a proper party to the action.

Austin Suit. In January 1983, Austin filed suit against HLP and its parent company, Houston Industries, alleging that HLP had misrepresented the capabilities of Brown & Root as the original architect-engineer and construction manager of the project and had failed to properly perform its duties as project manager. Austin requested, among other things, (a) a reformation of the STP Participation Agreement with Austin conveying to HLP its 16% interest in STP, (b) a refund from HLP of the approximately \$437 million expended by Austin to that date, and of all sums expended by Austin on STP thereafter, and (c) damages in an additional unspecified amount. In December 1985, Austin filed an amended petition that asserted additional claims against HLP under the DTPA and sought, from HLP and Houston Industries, either (i) an unspecified amount of damages, including treble damages to the extent proper under the DTPA, as well as pre-judgment interest costs and attorneys' fees, or (ii) a reformation or rescission of the STP Participation Agreement requiring HLP to return to Austin all of the monies expended by Austin with respect to its 16% interest in STP to the date of the judgment, with interest, relieving Austin of all future obligations with respect to its interest in STP and providing for a concurrent transfer by Austin of such interest to HLP.

On May 27, 1987, Austin filed another amended petition in which it specified \$938 million as the maximum amount of damages claimed (all or some portion of which was alleged to be subject to trebling under the DTPA), exclusive of attorneys fees and court costs.

Austin and HLP have filed motions for partial summary judgment. On October 10, 1986, the trial judge ruled that Austin is not entitled to reformation or rescission of the STP Participation Agreement. The trial judge denied HLP's motion for partial summary judgment directed at Austin's allegations asserting a cause of action under the DTPA and HLP's motion for

partial summary judgment directed at Austin's allegations that there was fraud in the inducement relating to Austin's entry into the STP Participation Agreement. On June 29, 1987, a newly appointed trial judge denied Austin's motion seeking to hold HLP responsible for the actions of the former architect-engineer. The judge denied, however, HLP's request for summary judgment on all claims relating to the Participation Agreement. The judge ruled that Austin must prove that HLP breached the Participation Agreement by failing to report material information and must prove damages specifically related to such failure to provide information. The judge permitted Austin to maintain its claim for \$830 million under this theory of recovery if it could show that the owners would have cancelled STP in 1976 and that Austin would have built a coal plant in lieu of STP. On August 10, 1987, Austin provided an updated calculation of its alleged damages under that claim, dropping its claim under this theory of recovery to \$740 million. On August 11, 1987, the judge reversed the earlier order, denying HLP's motion for summary judgment as to Austin's DTPA claims.

In September 1987, HLP announced that HLP and Austin had reached an agreement in principle under which HLP would acquire all of Austin's interest in STP, Austin would acquire an interest in an HLP coal plant and all litigation between HLP and Austin would be dismissed. The agreement in principle is subject to conditions including execution of definitive contractual documents, approval by the Texas Commission and the NRC, and waiver of the right of first refusal by the Company and San Antonio relating to acquiring Austin's STP interest. HLP has publicly reported that substantial differences with respect to several issues remain unresolved, and HLP can make no prediction as to whether a settlement with Austin can be achieved.

Nuclear Insurance. In connection with the licensing and operation of STP, the participants have purchased the maximum limits of nuclear liability insurance available from private sources, and have executed an indemnification agreement with the NRC, in accordance with the financial protection requirements of the Price-Anderson Act.

The owners of STP are insured against \$720 million of liability claims, the full amount to which claims are limited under the Price-Anderson Act, which may result from a nuclear incident. Nuclear liability insurance limits available from private sources are presently \$160 million and the Secondary Financial Protection (indemnification) provisions of the Price-Anderson Act presently provide a limit of liability of \$560 million based upon an assessment of \$5 million per reactor per each incident, \$10 million per reactor annual aggregate. There are currently 112 reactors included in the Secondary Financial Protection Program.

The most recent 10-year extension of the Price-Anderson Act expired on August 1, 1987, and at this date the Congress has not approved an extension of the provisions of the Act. Various bills have been introduced to amend the Act, which will increase the limit of liability under the Act and will increase the level of assessments to reactor operators who participate in the Secondary Financial Protection Program.

The participants have obtained from American Nuclear Insurers ("ANI") and Nuclear Electric Insurance Limited ("NEIL") nuclear property insurance and decontamination liability and excess property insurance with limits

totaling \$1.23 billion. The STP Management Committee has given approval to obtain an additional \$165 million of decontamination liability and excess property insurance, available from NEIL, at the time the full power license for STP Unit 1 is obtained. Further consideration is being given to obtaining an additional \$130 million of property insurance, now available from ANI. Present NRC regulations require reactor operators to obtain \$1.06 billion of nuclear property insurance and decontamination liability and excess property insurance. The participants are continuously reviewing the STP nuclear property insurance program and plan to maintain such nuclear property insurance coverages and limits as are customary in the industry for similar nuclear generating stations.

As a member insured of NEIL, CPL will become subject to its share of annual assessments, which could amount to approximately \$9 million for the total project, in the event of a nuclear incident at a NEIL member facility. Under the South Texas Project Nuclear Property Insurance Project Agreement, each of the participants share pro rata, based upon ownership interest, in the premiums and assessments incurred under the NEIL program, and premiums incurred under the ANI nuclear property insurance program.

Financing. Long-term financing will be required during the 1988-1990 period, but, except for the Auction Preferred Stock of the Company ("APS") described below, the nature, amount and timing of the financing have not been determined. In February 1988, the Company issued and sold 425,000 shares of APS, Series A and 425,000 shares of APS, Series B in a negotiated underwriting. In addition to funds required for its construction program, the Company will require \$23,000,000 to retire first mortgage bonds maturing in the period. The Company anticipates that approximately 79% (including AFUDC) and 58% (excluding AFUDC) of the funds required for its 1988-1990 construction program will be provided from internal sources and pollution control funds held by a trustee and anticipates that the balance of the funds required for that period will come from long-term financing.

The issuance and sale of first mortgage bonds and preferred stock by the Company are subject to compliance with earnings coverage and other requirements of its first mortgage indenture and its articles of incorporation. The respective earnings coverage provisions require, in general, (i) for the issuance of additional first mortgage bonds, a minimum before-income-tax earnings coverage of two times the pro forma annual interest charges on first mortgage bonds and indebtedness secured by a prior or equal ranking lien, and (ii) for the issuance of additional preferred stock, a minimum after-income-tax earnings coverage of one and one-half times pro forma annual interest charges and preferred stock dividend requirements, in each case for a 12-month period ending within a specified period no more than 90 days preceding issuance. Earnings used in calculating such coverages include, in the case of the preferred stock coverage, all non-operating items including AFUDC and, in the case of the first mortgage bond coverage, such items to the extent they do not exceed 10% of earnings.

The Company's first mortgage indenture requires in effect that the Company certify property additions to the extent that expenditures for maintenance and repairs are less than 15% of utility operating revenues after deducting the cost of electricity purchased for resale. The Company has been required to certify property additions to satisfy deficiencies

under this requirement. However, the Company's present projections do not indicate any shortage of property additions usable as a basis for issuance of first mortgage bonds expected to be issued at least through 1990.

The earnings coverage provisions under the first mortgage indenture with respect to the issuance of additional first mortgage bonds similarly require minimum deductions from earnings for maintenance, repairs and depreciation equal to at least 15% of such revenues after deducting the cost of electricity purchased for resale. This requirement has reduced earnings coverage. Although not presently anticipated, the earnings coverage provisions may require the use of alternative debt financing by the Company at intervals during the next three years which could result in higher financing costs to the Company.

The first mortgage bond indenture cannot be amended to alter the above described provisions until the bonds of all series maturing during or before 2004 are retired or unless there is approval by 100% of such bondholders.

The Company's articles of incorporation generally prohibit the issuance or assumption, without the affirmative vote by the holders of a majority of the preferred stock, of any unsecured debt obligations if, after such issuance or assumption, (i) the principal amount of unsecured debt would exceed 20% of the aggregate of the principal amount of secured indebtedness and total capital stock and surplus or (ii) the principal amount of unsecured debt maturing in less than 10 years would exceed 10% of such aggregate. An unsecured borrowing which has a maturity of more than 10 years at the date of issuance is not considered an unsecured obligation maturing in less than 10 years until the principal thereof shall be due within three years. These limitations are not expected to interfere with any presently projected requirements for unsecured debt for the 1988-1990 period.

The projections upon which the foregoing statements and estimates are made are based on a number of general assumptions as to revenues, earnings, construction and other costs, the adequacy and timeliness of rate increases, interest rates and other factors. Actual experience may vary significantly from these assumptions.

ITEM 3. LEGAL PROCEEDINGS.

See "ITEM 1. BUSINESS -- REGULATION AND RATES" for information relating to regulatory proceedings.

See "ITEM 1. BUSINESS -- OPERATIONS" for information relating to system interconnection.

See "ITEM 1. BUSINESS -- ENVIRONMENTAL MATTERS" for information relating to environmental proceedings.

See "ITEM 2. PROPERTIES -- STP Construction" for information as to pending legal proceedings relating to STP.

ITEM 4. SUBMISSION OF MATTERS TO A VOTE OF SECURITY HOLDERS.

None.

PART II

ITEM 5. MARKET FOR REGISTRANT'S COMMON EQUITY AND RELATED STOCKHOLDER MATTERS.

All of the outstanding shares of Common Stock of the Company are owned by its parent, CSW.

ITEM 6. SELECTED FINANCIAL DATA.

The information required by Item 6 is incorporated by reference to page 33 of the Company's 1987 Annual Report to Stockholders.

ITEM 7. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS.

The information required by Item 7 is incorporated by reference to pages 33-36 of the Company's 1987 Annual Report to Stockholders.

ITEM 8. FINANCIAL STATEMENTS AND SUPPLEMENTARY DATA.

The information required by Item 8 is incorporated by reference to pages 21-32 of the Company's 1987 Annual Report to Stockholders.

ITEM 9. CHANGES IN AND DISAGREEMENTS WITH ACCOUNTANTS ON ACCOUNTING AND FINANCIAL DISCLOSURE.

None.

PART III

ITEM 10. DIRECTORS AND EXECUTIVE OFFICERS OF THE REGISTRANT.

(a) The following is a list of directors of the Company, together with certain information with respect to each of them:

Name, age, principal occupation, business experience and other directorships	Year First Became Director	Shares Beneficially Owned by Directors(1)		
		CSW	Company Common	Preferred
RICHARD H. BREMER AGE - 39	1987	5,681	-	-
Vice President - Finance of the Company from 1986 to 1988. Vice President and Controller from 1980 to 1986.(2)				
DURWOOD CHALKER AGE - 64	1979	79,654	-	-
Chairman, President and CEO of CSW. Director of CSW, each of its subsidiaries and MCorp, Dallas, Texas.				
JOHN W. CRUTCHFIELD AGE - 68	1972	-	-	-
President and owner of John W. Crutchfield & Company (capital investments) Corpus Christi, Texas. Director of First City Bank of Corpus Christi, Corpus Christi, Texas.				
W. R. FARQUHAR, JR. AGE - 67	1984	1,000	-	-
Retired. Prior to his retirement Mr. Farquhar was General Manager and Chief Executive Officer of Lavaca-Navidad River Authority, Edna, Texas.				
RUBEN M. GARCIA AGE - 56	1981	-	-	-
President or principal of several firms engaged primarily in construction and land development in the Laredo, Texas area. Director of Federal Reserve Bank of Dallas San Antonio Branch, San Antonio, Texas.				

Name, age, principal occupation, business experience and other directorships	Year First Became Director	Shares Beneficially Owned by Directors(1)

	-----	CSW Common Preferred
RONALD LEE KELLETT AGE - 47 Vice President and Controller of King Ranch, Inc., Kingsville, Texas.	1987	- - - - -
ROBERT A. McALLEN AGE - 53 President, CEO and director of Texas Valley Bancshares and subsidiaries. Vice Chairman and director of Hidalgo County Bank and Trust Company, Mercedes, Texas. Chairman and director of National Bank of Commerce, Edinburg, Texas.	1983	- - - - -
HERBERT C. PETRY, JR. AGE - 70 Partner in the law firm of Petry & Petry, Carrizo Springs, Texas. Director of Union State Bank, Carrizo Springs, Texas.	1964	300
ROBERT L. RANGE AGE - 54 Executive Vice President of the Company.	1979	6,818
H. LEE RICHARDS AGE - 53 President of Hygeia Dairy Company, Harlingen, Texas. Director of Harlingen National Bank, Harlingen, Texas.	1987	- - - - -
T. V. SHOCKLEY, III AGE - 42 President and CEO of the Company since June 1987. Senior Vice President and Chief Engineering Officer of the Company from 1986 to 1987. Other executive and managerial positions with the Company from 1983 to 1985.	1986	726

Name, age, principal occupation, business experience and other directorships	Year First Became Director	Shares Beneficially Owned by Directors ⁽¹⁾
		CSW Company Common Preferred
B. W. TEAGUE AGE - 49	1984	3,046 -
Senior Vice President, Regional Operations of the Company.		
All 17 directors and executive officers of the Company as a group.		103,262 -

- (1) All directors' and executive officers' shares owned as of January 1, 1988 as indicated are owned directly, and aggregate less than 1.0% of the outstanding shares of such class.
- (2) Mr. Bremer will resign as Vice President - Finance and from the Board of Directors in April 1988 to assume the duties of General Manager - Central Region of the Company.

All directors presently serving as executive officers of the Company have been employed in a managerial or executive capacity with a member or members of the CSW System for at least the past five years, and all outside directors have engaged in their respective principal occupations listed above for a period of more than five years unless otherwise indicated.

(b) The following is a list of the executive officers who are not directors of the Company, together with certain information with respect to each of them:

Name	Age	Present Position	Year First Elected to Present Position
Walter A. Ratcliff	57	Vice President - Corporate Services and Secretary	1983
Clayton R. Kirk	58	Vice President - Business Development	1986
Richard P. Verret	41	Vice President and Chief Engineering Officer	1986
Gerald W. Tucker	41	Controller	1986
Mary E. Sullivan	31	Treasurer	1988

Each of the directors and executive officers of the Company is elected to hold office until the first meeting of the Company's Board of Directors after the 1988 annual meeting of stockholders, presently scheduled to be held on April 14, 1988. Each of the executive officers listed in the table above has been employed by the Company or an affiliate in the CSW System in an executive or managerial capacity for more than the last five years.

except for Mr. Tucker. Mr. Tucker was with the Certified Public Accounting firm of Knuckles, Duvall and Hallum in 1986 and held various managerial positions with SWEPCO prior to 1986.

ITEM 11. EXECUTIVE COMPENSATION.

The following table contains information with respect to cash compensation paid by the Company to each of the five most highly compensated executive officers of the Company for all services rendered during 1987 and the aggregate cash compensation so paid by the Company during 1987 to all of the Company's executive officers as a group:

Name of Individual or Number in Group	Capacities In Which Served	Cash Compensation
T. V. Shockley, III	President and CEO	\$123,326
Robert L. Range	Executive Vice President	118,419
B. W. Teague	Senior Vice President, District Operations	88,893
Clayton R. Kirk	Vice President - Business Development	86,078
Richard H. Bremer	Vice President - Finance	81,812
All 11 executive officers of the Company as a group (a)		\$857,057

(a) Pursuant to the rules of the SEC, this total excludes the aggregate incremental cost to the Company of certain non-cash benefits made available to executive officers.

CSW provides an Employees' Stock Ownership Plan for the benefit of CSW System employees. Employees are eligible to participate in the Plan as of January 1 of the year in which they complete one year of service. Consistent with previous Federal tax law, the Plan allowed CSW to contribute CSW Common Stock for the benefit of CSW System employees in an amount equal to 1/2 of 1% of the aggregate compensation paid to employees covered by the Plan for the tax years 1983 through 1986. CSW's contribution to this Plan is offset by Federal income tax credits. Contributions, if made, are allocated among Plan participants pro rata on the basis of each participant's eligible compensation for the year in respect of which the contribution is made. CSW Common Stock allocated to employees' accounts may not be withdrawn for a period of 85 months or until retirement, resignation or death. Allocations in 1987 to Messrs. Shockley, Range, Teague, Kirk and Bremer were \$451, \$503, \$440, \$387 and \$411, respectively. Allocations to all 11 executive officers as a group in 1987 totaled \$3,799.

CSW provides an Employees' Thrift Plan to all CSW System employees over the age of 20 who have completed one year of service. The Plan is a savings plan which allows employees to contribute up to 10% of annual compensation.

The first 6% of contributed employee compensation is matched 50% by the Company; 75% if the employee has over 20 years of service. Deposits and Company contributions for certain participants, including executive officers, may be limited as required by the Tax Reform Act of 1986. Employee contributions up to the 6% level and matching Company contributions may be invested at the employee's option in CSW Common Stock, in a guaranteed fixed income program or split equally between the two. Contributions over 6% are not matched by the Company and must be invested in the guaranteed fixed income program. Employees are vested as to the Company's contributions after three years of participation or five years service. Employees may withdraw all their contributions from the Plan at any time. The Company's contributions and investment gains on employee and Company contributions may not be withdrawn until retirement, resignation or death. All employees listed in the table participated in the Plan in 1987. Company matching contributions during 1987 for Messrs. Shockley, Range, Teague, Kirk and Bremer were \$2,646, \$5,211, \$3,698, \$3,510 and \$2,340, respectively. Total Company contributions to all 11 executive officers as a group in 1987 were \$26,789.

CSW shareholders approved the establishment of the CSW Restricted Stock Plan at the 1984 annual meeting. The purpose of the Plan is to assist CSW and its subsidiaries in securing and retaining key executive employees of outstanding ability, and to recognize their best efforts on behalf of CSW and its subsidiaries, through awards of CSW Common Stock. Any employee who is responsible for the management, growth or protection of the business of CSW or its subsidiaries is eligible for awards under the Plan. The Plan permits CSW's Board of Directors (or a committee thereof), at its discretion, to award up to a maximum of 500,000 shares of CSW Common Stock, in the aggregate, to eligible employees subject to certain adjustments for a change in classification, subdivision or combination of shares. In addition, in connection with any such award, CSW's Board of Directors determines the group of eligible employees and the restricted period over which such award will vest. No shares may be awarded beyond April 19, 1994, the tenth anniversary of the Plan's effective date.

Awards under the Plan were made to Vice Presidents and above of CSW and its subsidiaries on January 2, 1987. All the executives included in the compensation table included herein received an award in 1987. Messrs. Shockley, Range, Teague, Kirk and Bremer were awarded 393, 413, 345, 232 and 164 shares, respectively. Eight of the 11 executive officers as a group were awarded 2,895 shares in 1987. The restricted period for the 1987 awards has lapsed or will lapse as to 20% of the awards on January 2, 1988, 1989 and 1990 and as to the remaining 40% on January 2, 1991. Each participant must render substantial services to the Company on a regular basis during the restricted period. If such service is not rendered for such period, except by reason of the participant's death, total disability or normal retirement, the participant will forfeit those shares which were previously awarded and are still subject to the restricted period. During the restricted period, the participant will have all the rights of a shareholder, including the right to receive dividends paid on such shares, except that the participant may not sell, assign, transfer, pledge or otherwise encumber the shares. The fair market value of shares to which restrictions lapsed in 1987 awarded to Messrs. Shockley, Range, Teague and Bremer was \$2,024, \$14,733, \$6,071 and \$6,603, respectively. Messrs. Shockley, Range, Teague and Bremer were the only executive officers listed

in the compensation table for which restrictions lapsed in 1987 on shares previously awarded. The fair market value of shares to which restrictions lapsed in 1987 awarded to all 11 executive officers as a group was \$59,676.

Executive officers, like other employees, are also eligible to participate in the CSW System Pension Plan, and all eligible persons whose compensation is reported in the table participated in this Plan. Contributions to the Plan are determined actuarially and cannot be readily calculated with respect to any individual participant or small group of participants. The amount of such contribution is thus omitted from the table. For purposes of determining Plan benefits, compensation for each of the individuals listed in the table is substantially the same as the amounts set forth in the table.

Plan benefits depend upon years of credited service, age at retirement and amount of compensation. Compensation under the Plan includes base salaries, exclusive of bonuses, overtime, expense allowances and other compensation. Assuming retirement at age 65, a Plan participant would be eligible at retirement for a maximum annual pension benefit as follows (reduced by half of primary Social Security benefits payable at age 65):

Average Earnings	Annual Benefits After Specified Years of Service		
	20	25	30 or more
\$100,000	\$ 33,333	\$ 41,667	\$ 50,000
150,000	50,000	62,500	75,000
200,000	66,667	83,333	100,000
250,000	83,333	104,167	125,000
300,000	100,000	125,000	150,000

Messrs. Shockley, Range, Teague, Kirk and Bremer had 11, 30, 26, 30 and 10 years, respectively, of credited service under the Pension Plan at December 31, 1987. "Average earnings" means the average annual earnings during the 36 consecutive months of highest pay during the 120 months prior to retirement.

CSW shareholders approved the establishment of the CSW Stock Option Plan at the 1986 annual meeting. The purpose of the Plan is to assist CSW and its subsidiaries in securing and retaining key executive employees of outstanding ability and to recognize their best efforts on behalf of CSW and its subsidiaries. The Plan authorizes the grant of options to purchase shares of CSW Common Stock and stock appreciation rights to officers and key employees of CSW and its subsidiaries. Any employee who is responsible for the management, growth or protection of the business of CSW or its subsidiaries is eligible for such selection. The Plan is administered by a committee of not less than three directors appointed by the Board of Directors of CSW (the "Committee"). Under the Plan, the Committee is authorized to grant stock options at an option price not less than the fair market value of the shares covered by the option at the time the option is granted. The Plan also permits the Committee to grant stock appreciation rights which permit an optionee to receive from CSW, upon exercise, cash or shares of CSW Common Stock with an aggregate fair market value equal to the aggregate appreciation in value of the shares in respect of which the right was exercised. Stock appreciation rights may be granted with respect to

stock options granted under the Plan. Options granted under the Plan may be options that are intended to qualify under particular provisions of the Internal Revenue Code of 1986 (the "Code"), as in effect from time to time ("incentive stock options"), options that are not intended so to qualify under the Code ("nonqualified stock options") or combinations of the foregoing.

No option can run for more than ten years, and no option is exercisable until the optionee has been continuously employed by CSW or any subsidiary for one year from the date the option was granted. The Plan does not limit either the number of persons who are eligible to receive options or stock appreciation rights or the number of shares subject to nonqualified options or stock appreciation rights that may be granted to any one person. The Plan does not limit the aggregate number of stock options and stock appreciation rights that may be granted; only the number of shares authorized for issuance and sale and the number of shares with respect to which stock appreciation rights may be exercised are limited.

The maximum number of shares of CSW Common Stock to be issued and sold under the Plan is 1,500,000, subject to adjustments to reflect stock splits and certain other changes in the number and kind of outstanding shares. The maximum number of shares with respect to which stock appreciation rights may be granted pursuant to any particular award shall not exceed 50% of the shares subject to the options granted under such award.

On April 16, 1987, 36 key employees of CSW and its subsidiaries received incentive stock options and stock appreciation rights pursuant to the Plan. As of January 1, 1988, 1,310,200 shares of CSW Common Stock were not subject to outstanding options and remained available for issuance under the Plan, while an aggregate of 189,300 shares of CSW Common Stock were subject to outstanding options under the Plan. Incentive stock options and stock appreciation rights granted on April 16, 1987 each had a per share exercise price of \$32.50 and an expiration date of April 1997. The closing sale price of CSW Common Stock on April 16, 1987, as reported in the composite quotations of the Wall Street Journal, was \$32.50 per share. Mr. Shockley received 2,500 incentive stock options and 1,250 related stock appreciation rights. Mr. Range received 3,000 incentive stock options and 1,500 related stock appreciation rights and Mr. Teague received 2,500 incentive stock options and 1,250 related stock appreciation rights. Messrs. Shockley, Range and Teague were the only executive officers listed in the compensation table to receive incentive stock options or stock appreciation rights in 1987. Total options and related stock appreciation rights granted to 4 of the 11 executive officers as a group in 1987 were 9,500 incentive stock options and 4,750 related stock appreciation rights.

Other Information Respecting Director Compensation:

The Board of Directors held 5 meetings during 1987. Directors who are not also executive officers or employees of the Company or its affiliates receive \$4,800 annually for service on the Board and \$200 plus expenses for each meeting and each audit committee meeting attended.

Directors who are not also officers and employees of the Company were eligible in 1987 to participate in a deferred compensation plan. Under this plan, directors could elect to defer payment of annual directors' and meeting fees until they retire from the Board or as they otherwise direct.

ITEM 12. SECURITY OWNERSHIP OF CERTAIN BENEFICIAL OWNERS AND MANAGEMENT.

All 6,755,535 shares of the Company's outstanding common stock, \$25 par value, are owned beneficially and of record by CSW, 2121 San Jacinto Street, Dallas, Texas 75201.

For information regarding the amount of each class of equity securities of the Company and of CSW beneficially owned directly or indirectly by all directors and executive officers of the Company, see "ITEM 10. DIRECTORS AND EXECUTIVE OFFICERS OF THE REGISTRANT."

ITEM 13. CERTAIN RELATIONSHIPS AND RELATED TRANSACTIONS.

The Company retains as legal counsel the law firm of Petry & Petry, Carrizo Springs, Texas, of which Mr. Herbert C. Petry, Jr., a director, is a partner.

PART IV

ITEM 14. EXHIBITS, FINANCIAL STATEMENT SCHEDULES AND REPORTS ON FORM 8-K.

The financial statements included in the Company's 1987 Annual Report to Stockholders are hereby incorporated by reference and made a part of this report.

	Page Reference

	1987 Annual
1987	Report to
10-K	Stockholders

(a) Financial Statements (Included under "ITEM 8. FINANCIAL STATEMENTS AND SUPPLEMENTARY DATA"):	
Report of Independent Public Accountants.	21
Statements of Income for the years ended December 31, 1987, 1986 and 1985.	23
Statements of Retained Earnings for the years ended December 31, 1987, 1986 and 1985.	23
Balance Sheets as of December 31, 1987 and 1986.	24
Statements of Funds Provided for Gross Additions to Electric Utility Plant for the years ended December 31, 1987, 1986 and 1985.	25
Statements of Capitalization as of December 31, 1987 and 1986.	26

Page Reference

1987 Annual
1987 Report to
10-K Stockholders
...

Notes to Financial Statements.

27-32

(b) Reports on Form 8-K:

On October 16, 1987, a Form 8-K was filed by the Company, reporting Item 5, "Other Events."

(c) Exhibits:

3. (a) Restated Articles of Incorporation, as amended, of the Company (incorporated herein by reference to Exhibit 4(a) to the Company's Registration Statement No. 33-4897, Exhibits 5 and 7 to Form U-1 File No. 70-7171, Exhibits 5, 8.1, 8.2 and 19 to Form U-1 File No. 70-7472).

(b) Bylaws, as amended, of the Company (incorporated herein by reference to Exhibit 6 to Form U-1 File No. 70-7472.)

4. (a) Indenture of Mortgage or Deed of Trust dated November 1, 1943, executed by the Company to The First National Bank of Chicago and Robert L. Grinnell, as Trustees, as amended through October 1, 1977 (incorporated herein by reference to Exhibit 5.01 in File No. 2-60712), and the Supplemental Indentures of the Company dated September 1, 1978, January 1, 1980, January 1, 1981, March 1, 1983 (incorporated herein by reference to Exhibit 2.02 in File No. 2-62271, Exhibit 2.02 in File No. 2-66202, Exhibit 2.02 in File No. 2-69943, Exhibit 4.02 in File No. 2-76811 and Exhibit 4(b) in File No. 2-82095 and Exhibit 12 to Form U-1 File No. 70-6121) and December 15, 1984, July 1, 1985, August 1, 1985, May 1, 1986 and November 1, 1987 (incorporated herein by reference to Exhibit 17 to Form U-1 File No. 70-7003, Exhibit 4(b) in File No. 2-98942, Exhibit 4 to Form U-1 File No. 70-7128, Exhibit 4 to Form U-1 File No. 70-7236 and Exhibit 4 to Form U-1 File No. 70-7249).

	Page Reference

	1987 Annual
1987	Report to
10-K	Stockholders

(b) Debenture Indenture dated April 1, 1982 executed by the Company to The Bank of New York, as Trustee (incorporated here- in by reference to Exhibit 4.01 in File No. 2-76811) and the Supplemental Inden- ture of the Company dated September 1, 1985 (incorporated herein by reference to Exhibit 18 to Form U-1 File No. 70-7128).	
12. Statement re computation of Ratio of Earnings to Fixed Charges for the five years ended December 31, 1987.	40
13. 1987 Annual Report to Stockholders.	Filed Herewith
24. Consent of Independent Public Accountants.	41
25. Powers of Attorney.	Filed Herewith
(d) Schedules:	
Report of Independent Public Accountants on Supplemental Schedules and Exhibit.	35
V. Property, Plant and Equipment f the years ended December 31, 1987, and 1985.	36
VI. Accumulated Depreciation, Depletion and Amortization of Property, Plant and Equipment for the years ended December 31, 1987, 1986 and 1955.	37
IX. Short-Term Borrowings for the years ended December 31, 1987, 1986 and 1985.	38
X. Supplementary Income Statement In- formation for the years ended December 31, 1987, 1986 and 1985.	39

All other exhibits and schedules are omitted because of the absence of the conditions under which they are required or because the required information is included in the financial statements and related notes to financial statements.

SIGNATURES

Pursuant to the requirements of Section 13 or 15(d) of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized, on March 18, 1988.

CENTRAL POWER AND LIGHT COMPANY

By /s/ Robert L. Range
Robert L. Range
Executive Vice President

Pursuant to the requirements of the Securities Exchange Act of 1934, this report is signed below by the following persons on behalf of the registrant in the capacities indicated on March 18, 1988.

Signature	Title
-----	-----
*T. V. Shockley, III	President and CEO and Director (Principal executive officer)
*Robert L. Range	Executive Vice President (Principal financial officer)
*Gerald W. Tucker	Controller (Principal accounting officer)
*Richard H. Bremer	Director
*Durwood Chalker	Director
*John W. Crutchfield	Director
*W. R. Farquhar, Jr.	Director
*Ruben M. Garcia	Director
*Ronald Lee Kellett	Director
*Robert A. McAllen	Director
*Herbert C. Petry, Jr.	Director
*H. Lee Richards	Director
*B. W. Teague	Director

*By: /s/ Robert L. Range
Robert L. Range
Attorney-in-Fact

REPORT OF INDEPENDENT PUBLIC ACCOUNTANTS ON SUPPLEMENTAL SCHEDULES AND EXHIBIT

.....

To Central Power and Light Company:

In connection with our examinations of the financial statements included in Central Power and Light Company's Annual Report to Stockholders and incorporated by reference in this Form 10-K, we have also examined the supplemental schedules V, VI, IX and X and Exhibit 12. Our examinations of the financial statements were made for the purpose of forming an opinion on the basic financial statements taken as a whole. The supplemental schedules and exhibit are presented for purposes of complying with the Securities and Exchange Commission's rules and are not part of the basic financial statements. The schedules and exhibit have been subjected to the auditing procedures applied in the examinations of the basic financial statements and, in our opinion, fairly state in all material respects the financial data required to be set forth therein in relation to the basic financial statements taken as a whole.

ARTHUR ANDERSEN & CO.

Dallas, Texas
February 8, 1988

SCHEDULE V

CENTRAL POWER AND LIGHT COMPANY
PROPERTY, PLANT AND EQUIPMENT
FOR THE YEARS ENDED DECEMBER 31, 1987, 1986 and 1985

Column A Classification	Column B Balance Beginning of Year	Column C Additions at Cost	Column D Retirements at Cost	Column E Other Changes Add/(Deduct)	Column F Balance End of Year
				(Thousands)	
Year 1987					
Electric Utility Plant:					
Production	\$ 715,779	\$ 12,323	\$ 393	\$ (23)	\$ 727,686
Transmission	268,648	14,764	1,716	7,922	289,618
Distribution	534,081	38,976	9,339	(7,804)	555,914
General	162,081	34,704	2,557	(4,180)	190,048
Construction work in progress	1,646,332	341,454	-	-	1,987,786
Nuclear fuel	100,048	2,502	-	(34)	102,516
	\$3,426,969	\$ 444,723	\$ 14,005	\$ (4,119)	\$3,853,568
Year 1986					
Electric Utility Plant:					
Production	\$ 670,242	\$ 49,874	\$ 4,337	\$ -	\$ 715,779
Transmission	261,984	16,399	1,129	(8,606)	268,648
Distribution	497,466	35,489	7,915	9,041	534,081
General	157,786	7,060	2,303	(462)	162,081
Construction work in progress	1,375,267	318,065	-	(47,000)	1,646,332
Nuclear fuel	93,874	6,174	-	-	100,048
	\$3,056,619	\$ 433,061	\$ 15,684	\$ (47,027)	\$3,426,969
Year 1985					
Electric Utility Plant:					
Production	\$ 662,240	\$ 8,805	\$ 748	\$ (55)	\$ 670,242
Transmission	241,038	21,924	947	(31)	261,984
Distribution	456,909	48,436	7,851	(28)	497,466
General	139,252	20,557	1,693	(330)	157,786
Construction work in progress	1,171,503	350,590	-	(146,826)	1,375,267
Nuclear fuel	88,035	5,839	-	-	93,874
	\$2,758,977	\$ 456,151	\$ 11,239	\$ (147,270)	\$ 3,056,619

SCHEDULE VI

CENTRAL POWER AND LIGHT COMPANY
 ACCUMULATED DEPRECIATION, DEPLETION AND
 AMORTIZATION OF PROPERTY, PLANT AND EQUIPMENT
 FOR THE YEARS ENDED DECEMBER 31, 1987, 1986 AND 1985

Column A Classification	Column B Beginning of Year	Column C Additions Charged to Costs and Expenses Depreciation	Column D Other Changes Retirements(*)	Column E Add/ (Deduct)	Column F Balance End of Year
		(Thousands)			
Year 1987					
Electric Utility					
Plant:					
Production	\$ 264,750	\$ 23,817	\$ 1,090	\$ 394	\$ (68) \$289,195
Transmission	84,314	8,235	-	1,716	(456) 90,377
Distribution	142,028	20,800	-	9,339	(1,841) 151,648
General	55,193	2,263	5,547	2,406	(1,908) 58,689
	<u>\$ 546,285</u>	<u>\$ 55,115</u>	<u>\$ 6,637</u>	<u>\$ 13,855</u>	<u>\$ (4,273) \$589,909</u>
Year 1986					
Electric Utility					
Plant:					
Production	\$ 245,245	\$ 22,905	\$ 1,090	\$ 4,336	\$ (154) \$264,750
Transmission	77,630	7,954	-	1,129	(141) 84,314
Distribution	132,783	19,386	-	7,914	(2,227) 142,028
General	47,747	1,978	7,765	2,296	(1) 55,193
	<u>\$ 503,405</u>	<u>\$ 52,223</u>	<u>\$ 8,855</u>	<u>\$ 15,675</u>	<u>\$ (2,523) \$546,285</u>
Year 1985					
Electric Utility					
Plant:					
Production	\$ 223,158	\$ 22,005	\$ 1,090	\$ 748	\$ (260) \$245,245
Transmission	71,218	7,335	-	935	12 77,630
Distribution	124,923	17,926	-	7,850	(2,216) 132,783
General	39,535	1,311	8,540	1,693	54 47,747
	<u>\$ 458,834</u>	<u>\$ 48,577</u>	<u>\$ 9,630</u>	<u>\$ 11,226</u>	<u>\$ (2,410) \$503,405</u>

(*) Retirements are at original cost, net of removal costs and salvage.

SCHEDULE IX

CENTRAL POWER AND LIGHT COMPANY
SHORT-TERM BORROWINGS
 FOR THE YEARS ENDED DECEMBER 31, 1987, 1986 AND 1985

Column A	Column B	Column C	Column D	Column E	Column F
Category of Aggregate Short-term Borrowings	Balance at end of Period	Weighted Average Interest Rate	Maximum Outstanding Month-end	Average Outstanding During the Period	Weighted Average Interest Rate During the Period
			(Thousands)		

Year Ended

December 31, 1987 Advances
 from
 Affiliates \$42,430 8.3% \$73,383 \$37,335 7.0%

December 31, 1986 Advances
 from
 Affiliates \$.0- -8 \$ 5,178 \$ 432 7.3%

December 31, 1985 Advances
 from
 Affiliates \$ -0- -* \$72,726 \$30,501 8.1%

SCHEDULE X

CENTRAL POWER AND LIGHT COMPANY
SUPPLEMENTARY INCOME STATEMENT INFORMATION
FOR THE YEARS ENDED DECEMBER 31, 1987, 1986 and 1985

	Year Ended December 31		
	1987	1986	1985
(Thousands)			
Real estate and personal property taxes	\$15,174	\$13,429	\$12,479
State gross receipts taxes	8,679	9,346	9,079
Payroll taxes	4,860	4,727	4,179
Franchise taxes	8,031	7,278	5,608
State utility commission assessments	1,220	1,407	1,418
Other taxes	213	201	177
	<hr/>	<hr/>	<hr/>
	<hr/> <u>\$38,177</u>	<hr/> <u>\$36,388</u>	<hr/> <u>\$32,940</u>

The amounts of taxes, depreciation and maintenance charged to accounts other than income and expense accounts were not significant. Rents, royalties, advertising and research and development costs during these years were not significant.

EXHIBIT 12

CENTRAL POWER AND LIGHT COMPANY
RATIO OF EARNINGS TO FIXED CHARGES
FOR THE FIVE YEARS ENDED DECEMBER 31, 1987

	1987	1986	1985	1984	1983
	-----	-----	-----	-----	-----
(Thousands except Ratios)					
Operating income	\$142,435	\$145,466	\$138,912	\$143,923	\$145,248
Adjustments:					
Federal income taxes	6,873	6,589	(16,709)	31,642	33,057
Provision for deferred Federal income taxes	28,889	42,750	68,069	11,006	15,080
Deferred investment tax credits	14,301	19,748	11,606	24,258	19,122
Other income and deductions	(963)	6,840	119	1,145	1,578
Allowance for borrowed and equity funds used during construction	168,877	139,937	129,158	79,765	50,800
Earnings	<u>\$360,412</u>	<u>\$361,330</u>	<u>\$331,155</u>	<u>\$291,739</u>	<u>\$264,885</u>
Fixed charges:					
Interest on long-term debt	\$108,038	\$107,521	\$101,325	\$ 77,667	\$ 73,376
Interest on short-term debt and other	12,172	6,770	14,645	8,905	1,956
Fixed Charges	<u>\$120,210</u>	<u>\$114,291</u>	<u>\$115,970</u>	<u>\$ 86,572</u>	<u>\$ 75,332</u>
Ratio of Earnings to Fixed Charges	<u>3.00</u>	<u>3.16</u>	<u>2.86</u>	<u>3.37</u>	<u>3.52</u>

CONSENT OF INDEPENDENT PUBLIC ACCOUNTANTS

As independent public accountants, we hereby consent to the incorporation by reference in the registration statements of Central Power and Light Company on Form S-3 (File No. 2-82387 and 33-4897) of our reports dated February 8, 1988, included herein and incorporated by reference in this Form 10-K. It should be noted that we have not examined any financial statements of the Company subsequent to December 31, 1987 or performed any audit procedures subsequent to the date of our report.

ARTHUR ANDERSEN & CO.

Dallas, Texas
March 18, 1988

TENNESSEE VALLEY AUTHORITY

CHATTANOOGA, TENNESSEE 37401

5N 157B Lookout Place

JUN 09 1988

U.S. Nuclear Regulatory Commission
ATTN: Document Control Desk
Washington, D.C. 20555

Gentlemen:

In the Matter of the Application of) Docket Nos. 50-390
Tennessee Valley Authority) 50-391

WATTS BAR NUCLEAR PLANT (WBN) - REGION II INSPECTION REPORT NOS. 50-390/88-01
AND 50-391/88-01 - REPLY TO A NOTICE OF VIOLATION 390, 391/88-01-01, FAILURE
TO FOLLOW PROCEDURES, AND VIOLATION 390, 391/88-01-02, CABLE TRAY INSTALLATION

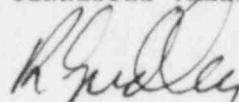
Enclosed is our response to Kenneth P. Barr's letter dated April 29, 1988, to
S. A. White, which transmitted the subject inspection report, citing
activities at WBN that appear to be in violation of NRC regulations.
Enclosure 1 is our response to the Notice of Violation (NRC Inspection Report
Nos. 50-390, 391/88-01-01 and 50-390, 391/88-01-02). Enclosure 2 contains a
list of commitments made by TVA in this response.

A supplemental response to violation 390, 391/88-01-01 will be submitted by
August 16, 1988. The response to violation 390, 391/88-01-02 will be updated
to provide more specific details by November 11, 1988, when sufficient
progress has been made to completely identify the extent of the problem and
its corrective actions.

If there are any questions, please telephone C. J. Riedl at (615) 365-8527.

Very truly yours,

TENNESSEE VALLEY AUTHORITY



R. Gridley, Director
Nuclear Licensing and
Regulatory Affairs

Enclosures
cc: See page 2

IEO1
|||

U.S. Nuclear Regulatory Commission

JUN 09 1988

cc (Enclosures):

Mr. K. P. Barr, Acting Assistant Director
for Inspection Programs
TVA Projects Division
U.S. Nuclear Regulatory Commission
Region II
101 Marietta Street, NW, Suite 2900
Atlanta, Georgia 30323

Mr. G. G. Zech, Assistant Director
for Projects
TVA Projects Division
U.S. Nuclear Regulatory Commission
One White Flint, North
11555 Rockville Pike
Rockville, Maryland 20852

U.S. Nuclear Regulatory Commission
Watts Bar Resident Inspector
P.O. Box 700
Spring City, Tennessee 37381

ENCLOSURE 1

WATTS BAR NUCLEAR PLANT (WBN) UNITS 1 AND 2
TVA RESPONSE TO VIOLATIONS 390, 391/88-01-01 AND 390, 391/88-01-02
REFERENCE: NRC INSPECTION REPORT NOS.
50-390/88-01 AND 50-391/88-01

Violation 390, 391/88-01-01, "Failure to Follow Procedures"

10 CFR Part 50, Appendix B, Criterion V, as implemented by TVA's Quality Assurance (QA) Topical Report, TVA-TR75-1A, Rev. 9, Sections 17.1.5 and 17.2.5, "Instructions, Procedures, and Drawings", requires that activities affecting quality be accomplished in accordance with instructions, procedures, or drawings.

QA Topical Report Table 17E-1 states that the Nuclear Quality Assurance Manual (NQAM) delineates responsibilities, requirements, and commitments for the QA Program during design and construction.

NQAM, Part I, Section 2.16, Rev. 3, "Corrective Action", Paragraph 10.5, requires that these condition adverse to quality reports (CAQRs) classified as "potentially generic" be reviewed by the potentially affected organization within 70 calendar days from the origination date of the CAQR.

Contrary to the above, CAQRs SQP [SQD] 871347, SQP 871003, SQP 871066, SQP 871743, SQP [SQT] 871304, and BFP 871056 were classified as potentially affecting Watts Bar and did not receive generic review within 70 calendar days from the origination date of the CAQR.

This is a Severity Level IV violation (Supplement II) and applies to units 1 and 2.

Admission or Denial of Violation

TVA admits the violation occurred as stated.

Since the CAQR program was implemented, approximately 72 percent of the CAQR reviews for applicability to WBN were not completed within the 70-day timeframe required by NQAM, Part 1, section 2.16.

Reason for the Violation

The following reasons caused this violation:

- * The organizations responsible for providing CAQRs for generic review failed to transmit CAQRs within 30 or 40 days of the origination date as required.
- * There was insufficient management attention to ensure adequate priority and resources were applied to meet CAQR timeframes.
- * Reviewing organizations onsite failed to perform generic reviews within 30 days, or 70 days from the CAQR origination date, because of a lack of management attention to meeting the timeframes.

- No procedural requirement exists to escalate late generic reviews; however, the NQAM, Part I, section 2.16, requires that timeframes be evaluated on a trend basis to determine the need for corrective action.
- Because all timeframes were based on the origination date, a missed schedule early in the process impacted the subsequent timeframes so that they were also late.

For the six CAQRs (SQN 871347 D1, SQP 871003, SQP 871066 R2, SQP 871743 R1, SQT 871304, and BFP 871056) specifically identified in the violation, the lack of management attention to meeting timeframes is the primary reason the generic reviews were not completed within the required timeframe.

Corrective Steps Which Have Been Taken and Results Achieved

In an effort to improve timeliness of processing conditions adverse to quality (CAQs) within the Office of Nuclear Power (ONP), the NQAM, Part I, section 2.16, was rewritten to implement the CAQR process. The revision to the NQAM set timeframes for the completion of various stages of CAQRs. These timeframes were established as targets for optimum performance. Some deviation from these targets will always be present in the system. Therefore, the NQAM requires that missed timeframes be evaluated on a trend basis to determine the need for corrective action.

The CAQR program was implemented at WBN in March 1987. In June 1987, WBN site organizations were late on 31 percent of all specified timeframes. ONP developed a timeliness report in June 1987 for each site to monitor all timeframes that are identified by the NQAM, Part I, section 2.16. As a result of additional management attention, timeliness for WBN site organizations has steadily improved with 10 percent late for the month of March 1988. Therefore, from an overall perspective, this approach has been effective.

To ensure that proper management attention is given to timeliness at WBN, CAQR timeframes (with the exception of generic reviews) are presently being discussed in weekly meetings held by the site director. Presently, weekly meetings within various site organizations are held to place emphasis on meeting timeframes. WBN site organizations have assigned managers to coordinate CAQRs and track timeframes. These designated managers report to upper management on areas of needed improvement and the general status of CAQRs within their respective organizations. To ensure that proper management attention is given to timeliness, WBN has implemented a timeliness summary report. This report receives appropriate management attention which will resolve specific problems and prevent buildups of timeliness problems experienced in the past.

The reviews for all of the CAQR examples cited in this violation have been completed.

Corrective Steps Taken to Avoid Further Violation

- Revision 4 of NQAM, Part I, section 2.16, was approved May 16, 1988. When implemented, timeframes for completing generic reviews will no longer be measured from the CAQR origination date. Division of Nuclear Engineering-

Engineering Assurance (DNE-EA) and Division of Nuclear Licensing and Regulatory Affairs (DNLRA) will have 10 days from receipt of the review request to complete their review, versus the current 40 days from the origination date of the CAQR. Potentially affected organizations will have 30 days from receipt of request to complete their reviews, versus the current 70 days from the origination date of the CAQR.

- To ensure that proper attention is given to late generic review responses, a requirement has been established that late responses to generic reviews which are not progressing satisfactorily be escalated by the CAQ coordinator. This will be added to a Quality Notice issued to revision 3 and is implemented in revision 4 of the NQAM, Part I, section 2.16.
- Reporting late generic reviews will be added to the timeliness summary report. This report receives appropriate management attention, which will not completely eliminate all late actions, but will resolve specific problems and prevent buildups of timeliness problems experienced in the past.
- The NQAM currently specifies that timeframes shall be met for completing various stages of CAQRs. As written, each timeframe that is missed may be considered a failure to comply with the NQAM. TVA will make a change to the NQAM to address missed CAQR timeframes, recognizing that on occasion they will be missed, but providing for appropriate management attention and corrective action. This change will require that missed timeframes be trended, and if adverse trends are identified, CAQRs shall be initiated to document the trend and correct the problems. Further clarification will be made on the CAQR timeframes for plants with a construction permit, such that, with the ONP manager's or DNQA director's approval, these schedules may be adjusted to be compatible with staffing and construction completion priorities.

Date When Full Compliance Will Be Achieved

TVA will provide NRC with details of the changes to the CAQR program by August 16, 1988. TVA has recognized that the problem with meeting the required timeframes exists to varying degrees at all TVA nuclear sites. The CAQR program changes should provide the clarification necessary to resolve the problem for all sites. Implementation of the changes to the CAQR program will be complete by August 16, 1988.

Violation 390, 391/88-01-02 "Cable Tray Installation"

10 CFR Part 50, Appendix B, Criterion III, as implemented by TVA's QA Topical Report, Section 17.1.3, "Design Control," requires measures for verifying or checking the adequacy of design, such as by the performance of design reviews, calculations, or suitable testing.

QA Topical Report Table 17D-1, "Quality Assurance Standards for Design and Construction", commits to conforming fully to ANSI N45.2-1971, "Quality Assurance Program Requirements for Nuclear Power Plants".

ANSI N45.2-1971, Paragraph 4.3, requires the following in those cases where the adequacy of a design is to be verified by test:

- The testing is to be identified.
- The testing must demonstrate adequacy of performance under the most adverse design conditions.
- If testing indicates that modifications are necessary, the item shall be modified and retested.

10 CFR Part 50, Appendix B, Criterion V, as implemented by the QA Topical Report, Sections 17.1.5 and 17.2.5, "Instruction, Procedures and Drawings", requires that activities affecting quality be accomplished in accordance with instructions, procedures, or drawings.

TVA Design Criteria WB-DC-20-21.1 requires cable tray fittings and supports to be qualified by:

- conformance to NEMA Standard VE1-1971, Section 5.05 or
- requirements specified by the cable tray manufacturer or
- analysis or testing.

TVA drawings 48W970-1 thru -5 and 45W869-Series drawings specify the installation details for cable trays attached to the steel containment vessel.

1. Contrary to the above, cable tray fittings and supports were not properly qualified for the as-built plant. Examples include:
 - a. adjustable horizontal connectors (ZNK) have not been qualified.
 - b. adjustable riser connectors (ZNB) have not been qualified for use in the vertical position. ZNB connectors are installed in the plant in the vertical position.
 - c. ZNB connectors have been qualified for use in the horizontal position when used within 12 inches of a support. Many ZNB connectors used in the plant are greater than 12 inches from the nearest support.
 - d. offset fittings have not been qualified.
2. Contrary to the above, the as-installed configuration of cable trays do not match design drawings. An example is that drawing 45W869-2 fails to show the location of all ZNB connectors on Cable raceway 4A1916 in the Reactor Building Annulus.

This is a Severity Level IV violation (Supplement II) and applies to units 1 and 2.

Admission or Denial of the Violation

TVA admits the violation occurred as stated.

Reason for the Violation

PART 1:

While the application of fittings and connectors were not always specified in accordance with design criteria requirements, they typically were specified in applications and configurations similar to qualified configurations. These configurations were specified on design output drawings based on engineering judgement made at the time of the original design. Although this judgement was (and still is) considered to be technically correct, TVA failed to document engineering judgement pertaining to qualification at the time the design for these fittings, connectors, and supports was issued. The undocumented engineering judgement resulted in designs which do not comply with the design criteria with no documented basis for exceptions.

PART 2:

Appropriate administrative emphasis was not placed on controlling documentation of construction-identified field changes necessary for the installation of the cable trays. This resulted in field changes that were either not documented or were not incorporated into the design drawings.

Quality Control Procedure (QCP) 3.04, revision 0, "Installation, Inspection, and Documentation of Cable Tray Systems," was used for field verification of the as-installed configuration. Cable tray fittings and connectors were not considered as essential attributes and, therefore, were not specifically detailed in the procedure.

Corrective Steps Which Have Been Taken and Results Achieved

CAQRs WBP 880040 for unit 1 and WBP 880041 for unit 2 have been issued to address the lack of qualification documentation of the cable tray fittings, connectors, and supports. CAQR WBP 880167 has been issued to address the fact that the as-installed configuration of the cable trays do not match the design drawings.

The corrective action plan for these CAQRs is as follows:

An engineering walk through will be performed to determine cable tray fittings and support configurations to be evaluated. An acceptance criteria will be determined from new analysis and tests performed for these selected configurations. The acceptance criteria will also take into consideration any vendor information, contractor data, and currently available TVA data. From the engineering walk through and the established acceptance criteria, bounding configuration will be determined and evaluated to determine the limits of acceptable configurations. The cable tray and cable tray support drawings will then be revised to reflect the acceptable configurations for cable tray fittings (ZNB, ZNK, etc.) in all category I structures including appropriate bolting details. Where required, field modifications will be made.

Engineering evaluation has begun on the cable tray fittings in the Reactor Building annulus region. Preparation of calculations has been initiated to assess qualification of the existing fittings. Preliminary results indicate that the configurations of the ZNK and ZNB fittings used in the annulus are acceptable. The lack of full thread engagement on the ZNB fittings and the orientation of the hinge pins on the ZNK fittings are still being evaluated.

Corrective Steps Taken to Avoid Further Violation

PART 1:

Procedures are in place now that require the documentation of engineering judgement and the basis for which that judgement was made--Nuclear Engineering Procedure (NEP) 3.1, "Calculations." No further recurrence control actions are required.

PART 2:

TVA has implemented a Design Change Improvement Program at WBN in which greater administrative control has been placed on field-identified changes. A Design Change Notice (DCN) will be used for identification, request, evaluation, resolution, and approval of necessary changes or clarifications to engineering documents. Their primary use will be to resolve installation problems encountered during construction or design change implementation. For completion of major modifications, an Engineering Change Notice (ECN) modification package will become the primary means to maintain design control. It is a standalone document which provides design requirements, design bases, installation guidelines, and verification requirements for a plant modification. Drawing Change Authorizations (DCAs) are prepared as part of the ECN modification package to provide a method of revising issued drawings or detailing design information not on the issued drawing. Drawing and document revisions necessary to reflect design changes will be issued after the modification is completed, verified, and accepted before the ECN package or DCN is closed. The use of ECNs and DCNs will provide the necessary controls for field-identified changes.

When installation or design change implementation problems occur, the responsible site organization is to initiate a DCN. Construction Engineering Procedure (CEP)-1.13 requires that field work shall not be performed related to the change until the change is formally approved. Work may be performed before formal approval if advance engineering authorization is given and documented on an A-DCN. Unauthorized work is considered to be a CAQ and will be documented on a CAQR.

For verification of as-installed cable tray configuration, QCP 3.04 will be revised by August 31, 1988, to include verifying correct installation of fittings and connectors.

Date for full Compliance

TVA will be in full compliance by fuel load of each respective unit. An updated report will be provided by November 7, 1989, to provide you the details of the corrective actions.

ENCLOSURE 2

LIST OF COMMITMENTS

Violation 390, 391/88-01-01

The following is a listing of the commitments made in this response:

- Revision 4 of NQAM, Part I, section 2.16, was approved May 16, 1988. When implemented, timeframes for completing generic reviews will no longer be measured from the CAQR origination date. Division of Nuclear Engineering-Engineering Assurance (DNE-EA) and Division of Nuclear Licensing and Regulatory Affairs (DNLRA) will have 10 days from receipt of the review request to complete their review, versus the current 40 days from the origination date of the CAQR. Potentially affected organizations will have 30 days from receipt of request to complete their reviews, versus the current 70 days from the origination date of the CAQR.
- To ensure that proper attention is given to late generic review responses, the requirement that late responses to generic reviews which are not progressing satisfactorily be escalated by the condition adverse to quality (CAQ) coordinator. This will be added to a Quality Notice issued to revision 3 and as implemented in revision 4 of the NQAM, Part I, section 2.16.
- Reporting late generic reviews will be added to the timeliness summary report. This report receives appropriate management attention, which will not completely eliminate all late actions, but will resolve specific problems and prevent buildups of timeliness problems experienced in the past.
- The NQAM currently specifies that timeframes shall be met for completing various stages of CAQRs. As written, each timeframe that is missed may be considered a failure to comply with the NQAM. TVA will make a change to the NQAM to address missed CAQR timeframes, recognizing that on occasion they will be missed, but providing for appropriate management attention and corrective action. This change will require that missed timeframes be trended, and if adverse trends are identified, CAQRs shall be initiated to document the trend and correct the problems. Further clarification will be made on the CAQR timeframes for plants with a construction permit, such that, with the ONP manager's or DNQA director's approval, these schedules may be adjusted to be compatible with staffing and construction completion priorities.
- TVA will provide NRC with details of the changes to the CAQR program by August 16, 1988. TVA has recognized that the problem with meeting the required timeframes exists to varying degrees at all TVA nuclear sites. The CAQR program changes should provide the clarification necessary to resolve the problem for all sites. Implementation of the changes to the CAQR program will be complete by August 16, 1988.

Violation 390, 391/88-01-02

The following is a listing of the commitments made in this response:

- ° An engineering walk through will be performed to determine cable tray fittings/connectors and support configurations to be evaluated.
- ° Acceptance criteria will be determined by DNE.
- ° DNE will determine the limits of acceptable field configurations.
- ° Bounding configurations will be determined by DNE and evaluated to determine the limits of acceptable configurations.
- ° Cable tray support drawings will be revised by DNE to reflect revised acceptable configurations.
- ° Cable tray drawings will be revised by DNE to reflect revised acceptable configurations including appropriate bolting details.
- ° Construction will perform any necessary field modifications.
- ° Provide updated report to NRC by November 7, 1989, to provide details of corrective actions.
- ° DNQA will revise QCP 3.04 by August 31, 1988, to include cable tray fittings and connections as essential attributes for inspection.



South Carolina Electric & Gas Company
P.O. Box 88
Jenkinsville, SC 29065
(803) 345-4041

Dan A. Nauman
Vice President
Nuclear Operations

June 3, 1988

Dr. J. Nelson Grace
Regional Administrator
U. S. Nuclear Regulatory Commission
Region II, Suite 2900
101 Marietta Street, NW
Atlanta, Georgia 30323

Subject: Virgil C. Summer Nuclear Station
Docket No. 50/395
Operating License No. NPF-12
Response to Inspector Followup
Items
NRC Inspection Report 88-06

Dear Dr. Grace:

Enclosed is the South Carolina Electric & Gas Company (SCE&G) response to the appraisal open items addressed in Appendix A of NRC Inspector Report 50-395/88-06. The enclosed response addresses the open items and the actions being taken to resolve each item.

If you should have any questions, please advise.

Very truly yours,
D. A. Nauman

HID:DAN/1cd
Enclosures

c: J. G. Connelly, Jr./O. W. Dixon, Jr./T. C. Nichols, Jr.
E. C. Roberts
W. A. Williams, Jr. J. C. Snelson
General Managers G. O. Percival
L. A. Blue R. L. Prevatte
C. A. Price J. B. Knotts, Jr.
R. B. Clary B. L. Johnson
W. R. Higgins NSRC
J. R. Proper RTS (IE 880601, 02, 03)
R. M. Campbell, Jr. NPCF
K. E. Nodland File (815.01)

Enclosure I to Dr. J. Nelson Grace Letter
June 3, 1988
Page 1 of 1

ENCLOSURE I

RESPONSE TO INSPECTOR FOLLOWUP ITEMS

ITEM:

Unresolved item 50-395/88-06-01, "Steam Line Monitor Effectiveness."

RESPONSE:

Specifications and documentation on the steam line monitors have been reviewed to determine their sensitivity for projection of off-site doses. This review has determined that these monitors are effective in providing dose assessment well below Protective Action Guide (PAG) limits.

ITEM:

Unresolved item 50-395/88-06-02, "Maintenance Of Documentation For Dose Assessment Models."

RESPONSE:

Information pertaining to validation, verification, and methodology for methods of dose assessment in use will be centralized in the Plant Record System by September 30, 1988.

ITEM:

Unresolved item 50-395/88-06-03, "Calculational Comparison Between Dose Assessment Models."

RESPONSE:

Calculational comparisons will be performed with dose assessment models used by SCE&G, South Carolina Department of Health and Environmental Control (SCDHEC), and the NRC. Comparisons will be fully documented with reasons for significant differences by January 31, 1989. Procedures will be revised by January 31, 1989 to require an annual review of these models to identify and resolve any changes that may lead to significant differences in results.

VIRGINIA ELECTRIC AND POWER COMPANY
RICHMOND, VIRGINIA 23261

June 10, 1988

D. S. CRUDEN
VICE PRESIDENT - NUCLEAR

United States Nuclear Regulatory Commission
Attention: Document Control Desk
Washington, D.C. 20555

Serial No. 86-477E
NO/RMK:v1h
Docket Nos. 50-338
50-339
License Nos. NPF-4
NPF-7

Gentlemen:

VIRGINIA ELECTRIC AND POWER COMPANY
NORTH ANNA POWER STATION UNITS 1 AND 2
PROPOSED LICENSE AMENDMENT GDC4
RESPONSE TO REQUEST FOR ADDITIONAL INFORMATION

Virginia Electric and Power Company requested an amendment to Operating License Nos. NPF-4 and NPF-7 for the North Anna Power Station Units 1 and 2 by letter dated November 6, 1986 (Serial No. 86-477A). The proposed amendment would add a license condition stating that the design of the reactor coolant pump and steam generator supports may be revised in accordance with our November 6, 1986 submittal. Discussions were then held between members of our respective staffs during telephone conferences on January 23, 1987 and February 5, 1987. In response to NRC questions raised during these discussions, we submitted additional information in our letters dated February 25, 1987 (Serial No. 86-477B) and March 12, 1987 (Serial No. 86-477C). The NRC subsequently requested additional information by letter dated July 17, 1987. The requested information was provided by our letter dated March 8, 1988 (Serial No. 86-477D).

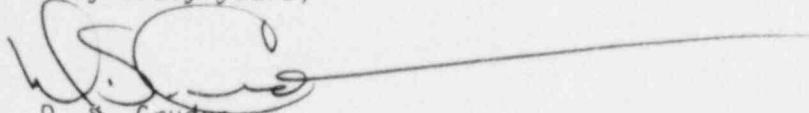
On May 12, 1988, a telephone conference was held between a member of the NRC staff and representatives of Virginia Electric and Power Company. The purpose of this call was to obtain information regarding those snubbers which would remain in place after the reactor coolant pump and steam generator supports were modified as proposed. Specifically, information concerning the general design, vendor supplied maintenance and inspection recommendations, size, and capacity of the remaining snubbers was requested.

As explained during the May 12, 1988 discussion, Virginia Electric and Power Company has procured new snubbers to replace the snubbers remaining after the proposed support modification. Accordingly, the requested information with respect to the replacement snubbers, as well as a comparison to the existing snubbers, was provided. The attachment to this letter documents the information provided during the May 12, 1988 discussion.

A001
11

Should you have any further questions, please contact us.

Very truly yours,



D. S. Cruden

Attachment

cc: U. S. Nuclear Regulatory Commission
Region II
101 Marietta Street, N. W.
Suite 2900
Atlanta, Georgia 30323

Mr. J. L. Caldwell
NRC Senior Resident Inspector
North Anna Power Station

ATTACHMENT

REQUEST FOR ADDITIONAL INFORMATION
ON ELIMINATION OF DYNAMIC EFFECTS OF POSTULATED
PRIMARY LOOP RUPTURES FROM DESIGN BASIS OF
NORTH ANNA POWER STATION UNITS 1 AND 2
DOCKET NOS 50-338 AND 50-339

On May 12, 1988, discussions were held between a member of the NRC staff and Virginia Electric and Power Company. During this discussion, the NRC requested the following additional information on the remaining snubbers for the proposed design configuration: (1) general design, (2) manufacturer's suggested maintenance and inspection requirements, and (3) size and capacity. The requested information is provided in this attachment.

Virginia Electric and Power Company has procured new snubbers from Taylor Devices, Inc. and intends to use those to replace the remaining Milwaukee snubbers in the proposed design configuration. Accordingly, the requested information is provided for the Taylor Devices snubbers and compared to the existing Milwaukee snubbers.

GENERAL DESIGN OF SNUBBERS

- Taylor snubbers have balanced rod design like the Milwaukee snubbers.
- Taylor snubbers have an improved design control valve mounted on the piston of the snubbers. The valve is the self-flushing type, and because of its location, is less susceptible to contamination or clogging. The Milwaukee snubbers have block valves mounted on the outer surface of the cylinders.
- Taylor snubbers have long life TEFZEL and HYTREL seals which are less susceptible to aging. The Milwaukee snubbers have relatively shorter life VITON seals.
- Taylor snubbers use GE-SF-1154 silicone fluid which is less susceptible to degradation, exhibits consistent properties in normal and adverse environments, and is a more prevalent snubber fluid currently used in the industry. The Milwaukee snubber uses DURO S-150 snubber fluid.
- Taylor snubbers do not need any external fluid reservoirs because of the location of the valves, and therefore the possibility of fluid contamination or leakage through the reservoirs and the connected tubing is avoided. The Milwaukee snubbers are connected to remote reservoirs and one reservoir feeds several snubbers.
- Taylor snubbers are maintained pressurized during normal operation and that keeps the seals tight. The Milwaukee snubbers remain at ambient pressure during normal operation.

- Taylor snubbers are fitted with test-in-place ports which permit in-place testing. This reduces the possibility of mishandling of snubbers during removal and reinstallation for testing purposes. This also would reduce future man-rem exposures during periodic testing. The Milwaukee snubbers do not have test-in-place ports.

The above design features were very carefully considered and were built into the Taylor snubbers to improve safety and reliability in every aspect.

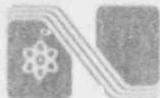
MANUFACTURER'S SUGGESTED MAINTENANCE AND INSPECTION REQUIREMENTS

The Taylor snubbers are designed to be maintenance free. The cylinders and the snubber piston rod assemblies are made out of stainless steel and are not subject to corrosion or aging. The seals are made out of TEFZEL and HYTREL and are certified by the manufacturers for life of the plant use. GE-SF-1154 snubber fluid is used in a closed system inside the snubbers and is not subject to degradation or contamination. The only manufacturer suggested inspection requirement is to periodically verify that the snubber is full of fluid. The current inspection program required by Technical Specifications exceeds the manufacturer suggested inspection requirements.

SIZE AND CAPACITY OF SNUBBERS

The Taylor snubbers were procured to duplicate the capacity and size envelope of the existing snubbers. The following is a comparison of the size and capacities of snubbers.

	MILWAUKEE SNUBBERS		TAYLOR SNUBBERS	
Load Capacity (Kips)	1900	1000	1900	1000
Cylinder Dia. (Inches)	14.0	10.0	16.5	12.0



Nebraska Public Power District

COOPER NUCLEAR STATION
P.O. BOX 98, BROWNVILLE, NEBRASKA 68321
TELEPHONE (402) 825-3811

CNSS887289

June 8, 1988

U.S. Nuclear Regulatory Commission
Document Control Desk
Washington, DC 20555

Subject: NPPD Response to NRC Inspection Report No. 50-298/88-13

Gentlemen:

This letter is written in response to your letter dated May 11, 1988, which transmitted NRC Inspection Report No. 59-298/88-13. Therein you indicated that certain of our activities were in violation of NRC requirements.

The following is the statement of the violation and our response in accordance with 10CFR2.201:

A. STATEMENT OF VIOLATION

Failure to Evaluate Nonessential Items Prior to Declaring Systems or Components Operable

Criterion V of Appendix B to 10CFR Part 50 and the licensee's approved "Quality Assurance Program for Operation" require that activities affecting quality be prescribed by documented instructions and procedures, and that they be accomplished in accordance with those instructions and procedures.

Section II.A.8 in Cooper Nuclear Station Operations Manual Procedure 0.27 states, in part, "...the use of unapproved spare parts in maintenance of repairs, such as the use of...nonessential classified parts when essential parts were required, may make the component inoperable as its ability to perform its safety functions during accidents cannot be certain. The parts must then be replaced or accepted as satisfactory by an Engineering review in order to return the component to service (operable)."

Contrary to the above, components and/or systems have been declared operable even though nonessential items have been installed in applications designated as essential for as much as 5½ months prior to their receiving an engineering evaluation.

This is a Severity Level IV violation. (Supplement I) (298/8813-01)

IEO 1
|||

REASON FOR THE VIOLATION

CNS Procedure 1.8, "Warehouse Issue and Requisition", allows nonessential parts to be issued for use in an essential application provided (1) a Nonconformance Report is written to address the specific situation and (2) the Warehouse Issue Ticket has been signed by an Engineer and the Division Manager of Nuclear Operations (DMNO). The initial review by the Engineer, prior to issuing the part, includes an evaluation of the part, its application, the documentation associated with the part, and whether, in the Engineer's judgement, there are any issues that would preclude final engineering acceptance of the part. CNS Procedure 0.27, "Component Operability", addresses the requirements for performing operability reviews to document the engineering judgement regarding the use of nonessential parts in essential applications. The violation occurred because neither procedure clearly delineated that a documented review per CNS Procedure 0.27 was required prior to returning the affected component to service. As a result, some operability reviews were not performed in a timely manner.

CORRECTIVE STEPS WHICH HAVE BEEN TAKEN AND THE RESULTS ACHIEVED

As a result of this violation, and as an interim measure, a documented operability review in accordance with CNS Procedure 0.27 is now completed prior to DMNO approval to release a non-essential part for an essential application. This prevents the installation of inappropriate parts in safety-related applications.

CORRECTIVE STEPS WHICH WILL BE TAKEN TO AVOID FURTHER VIOLATIONS

CNS Procedures 0.27 and 1.8 will be revised to clearly indicate that the performance of a documented operability review will be required prior to the issuance of a non-essential part for an essential application. In addition, a recently approved parts dedication procedure will streamline and concentrate the engineering evaluation effort of parts by combining elements currently found in several procedures. The implementation of this procedure and the revision to the referenced CNS Procedures should resolve all concerns regarding the installation of unacceptable parts in essential components.

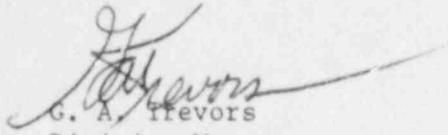
DATE WHEN FULL COMPLIANCE WILL BE ACHIEVED

Full compliance will be achieved by July 31, 1988.

U.S. Nuclear Regulatory Commission
June 8, 1988
Page 3

If you have any questions regarding this response, please contact me or
G. R. Horn at the site.

Sincerely,



G. A. Trevors
Division Manager
Nuclear Support

GAT:MAD:ss

cc: U.S. Nuclear Regulatory Commission
Region Office - Region IV

NRC Resident Inspector
Cooper Nuclear Station



30 JUN 6 A/M: 16

JUNE 1 1988

L-88-248

Dr. J. Nelson Grace
Regional Administrator, Region II
U. S. Nuclear Regulatory Commission
101 Marietta Street, N. W., Suite 2900
Atlanta, Georgia 30323

Re: Turkey Point Units 3 and 4
Docket Nos. 50-250 and 50-251
Management-on-Shift Weekly Report

Dear Dr. Grace:

Pursuant to the Nuclear Regulatory Commission Order dated October 19, 1987, the attached summary of Management-on-Shift (MOS) reports is submitted. The Plant Supervisor-Nuclear MOS Reports are also being submitted.

Should there be any questions on this information, please contact us.

Very truly yours,

W. F. Conway
Senior Vice President-Nuclear

WFC/SDF/dd
attachment

cc: J. Lieberman, Director, Office of Enforcement, USNRC
Dr. G. E. Edison, Project Manager, NRR, USNRC
Senior Resident Inspector, USNRC, Turkey Point Plant
R. E. Tallon, President, FPL

D036

11

MANAGEMENT ON SHIFT (MOS)

WEEKLY SUMMARY REPORT

WEEK STARTING: May 23, 1988

PAGE 1 OF 2

Four MOS Observers were on shift. Peter L. Walker, Westinghouse Electric Corporation (05/23-29/88, days); Jeff A. Spodick, St. Lucie Nuclear Plant Training Department (05/23-30/88, evenings); Howard L. Schneider, Turkey Point Nuclear Plant Planned Maintenance Special Projects Coordinator (05/23-25/88, evenings); and Wallace R. Williams, Jr. Turkey Point Nuclear Plant Assistant Superintendent Planned Maintenance (05/25-30/88, evenings).

Unit 3 operated at 100% power throughout the reporting period. Unit 4 progressed through startup operations returning to 100% power on May 29, 1988.

No immediate safety problems were identified by the MOS Observers during the reporting period.

One questionable work practice concerning leaving a hydrometer lying on safety-related batteries near terminals was identified by the MOS Observers.

During the reporting period, the MOS Observers noted ten recommendations and areas for improvements. These comments and suggestions involved:

Four comments were made concerning equipment such as the condition of turbine building systems piping hangers and supports, Control Room door inoperability and the operation of grass removal equipment at the Intake structure.

Three comments were made concerning documentation and procedural items such as Control Room notification of Non-Conformance Reports involving equipment operability, logging of the status of Transformer Cooling Fans and improvements to the procedure for Generator Gas Temperature Monitoring.

Three miscellaneous comments were made concerning the availability of people to do monthly walkdowns on safety-related systems, a method to eliminate accumulation of water in the Steam Air Ejector drain lines and a need for better stroke time data and bench spring settings for the Pressurizer Spray Valves.

MANAGEMENT ON SHIFT (MOS)

WEEK STARTING: May 23, 88

WEEKLY SUMMARY REPORT

PAGE 2 OF 2

During the reporting period the Plant Supervisor-Nuclear (PSN) MOS reporting program continued.

The PSN's identified four questionable work practices during this reporting period. These items were associated with: the use of the Operations page channel by Security personnel for non work-related conversations, the presence of high pressure industrial gas bottles with hydrostatic tests cut-of-date, availability of personnel to walkdown safety-related systems and the need for improved I & C technician training and turnover practices associated with the Main Steam Isolation Valve nitrogen regulators.

Additionally, the PSN's identified eight areas for improvement. These concerns included the existence of out-of-date procedures in the spare copy files, guidance on when to use Non-Conformance Reports instead of Plant Work Orders, repair of equipment room doors after major maintenance and maintenance of current phone numbers in the PSN Duty Call Book.

0-ADM-019

Management on Shift (MOS)
MOS DAILY REPORT

Page

1

To: Operations Superintendent - Nuclear

Date: 05/23/88

From: P. L. Walker
(MOS Observer)Shift: Day
 Night**A. Plant evolutions observed**

- o Unit 3, 100% Steady State Operations
- o Unit 4, Holding at less than 350° F, waiting for Nuclear Instrumentation and Heat tracing repairs
- o Attended Plan of the Day Meeting

B. Immediate safety problems

None

C. Questionable work practices

None

D. Areas for improvement

None

E. Professionalism, Summary of Shift, Comments

No problems - The operability concerns resulting from the heat tracing problems were properly addressed by the staff.

Completed By: P. L. Walker
MOS Observer Date: 05/23/88Reviewed By: L. L. Walker
Operations Superintendent - Nuclear Date: 5/24/88Management Review By: J. B. 15 May 88 J. H. 15 May 88 VP Date
PM/N Date SVP Date VP Date
05/23/88

0-ADM-019

Management on Shift (MOS)
MOS DAILY REPORT

Page

1

To: Operations Superintendent - Nuclear

Date: 05/23-24/88

From: Jeff Spodick
(MOS Observer)Shift: Day
 Night**A. Plant evolutions observed**

- o Maintenance activities at Unit 4
-N 32 and N 36, Source Range and Intermediate Range Nuclear Instrument Resistance checks
- o Unit 4 heatup to Mode 3 (greater than 350° F)
- o Full power steady state operation at Unit 3

B. Immediate safety problems

None

C. Questionable work practices

None

D. Areas for improvement

None observed

E. Professionalism, Summary of Shift, Comments

The pre-shift briefing was attended by all shift operators and the major maintenance disciplines. This made it easy to communicate shift goals to the work crews.

Completed By:

Jeff Spodick
MOS Observer

Date: 05/23-24/88

Reviewed By:

Dewitt Price
Operations Superintendent - Nuclear

Date: 5/24/88

Management Review By:

OB 15/24/88 VP 15/24/88 /
PM Date SVP Date VP Date
Date 05/23-24/88

0-ADM-019

Management on Shift (MOS)
MOS DAILY REPORT

Page

1

To: Operations Superintendent - Nuclear

Date: 05/23-24/88

From: H. L. Schneider
(MOS Observer)Shift: Day
 Night**A. Plant evolutions observed**

- o Unit 3, 100% power operation
- o Unit 4, Mode 3
- o "A" Emergency Diesel Generator Operability Test
- o Electrical Maintenance performing Heat Trace Periodic on circuit 6
- o Toured various plant areas: e.g., Intake; Turbine area; Radiation Control area; Unit 4, 4160 Volt switchgear rooms; Cable Spreading area
- o Beginning of shift (mids) meeting

B. Immediate safety problems

None

C. Questionable work practices

None

D. Areas for improvement

Operations experiences problems regarding monthly verification of safety related system flow paths. They have to followup to ensure the assigned people come out and do the walkdowns.

E. Professionalism, Summary of Shift, Comments

Mid shift meeting was very informative and provided excellent communication among people involved.

Completed By:

H. L. Schneider
MOS Observer

Date: 05/23-24/88

Reviewed By:

Operations Superintendent - Nuclear

Date: 5/24/88

Management
Review By:

OB 15/24/88 JF 15/24/88 / Date SVP VP Date PMN Date 05/23-24/88

Date Started

05/23/88

PSN MOS

Date Finished

05/23/88

Initiating PSN

Schimkus

PSN

Completed PSN

Schimkus

Initiating APSN

Dallau

APSN

Completed APSN

Dallau

A. Questionable Work Practices/Actions Taken/Recommendations

None

B. Areas for Improvement/Recommendations/Actions Taken

1. Control Room carpets need to be swept once per shift. The electric vacuum is so noisy that it is a total distraction to the RCO's, thus is used only once a day on peaks. The non-electric carpet sweeper is quiet but is so cheaply constructed that it won't pick up anything other than lint balls. Recommendation: Find a good industrial type non-electric or quiet electric sweeper that can be used on each shift by the cleaning personnel and not disrupt the Control Room operations. Need ASAP.

C. Good Practices/Professionalism Observed

Normal Operations - Good teamwork

L. Dallau Date 5/24/88 Actions Completed Date _____

Date Started	5/23/88	PSN MOS	Date Finished	05/24/88
--------------	---------	----------------	---------------	----------

Initiating PSN	Anderson	PSN	Completed PSN	Anderson
Initiating APSN	Reese	APSN	Completed APSN	Reese

A. Questionable Work Practices/Actions Taken/Recommendations

Each time we need safety system walkdowns done, the Control Room has to call the personnel to perform the walkdown. Many times the person scheduled to do the walkdown is not available and we spend many hours getting someone to perform the walkdown. Recommend: the person responsible for the safety system walkdown be accountable for its completion. If he is scheduled to be out of town or can't perform it for any other reason, he should make arrangements so as to have it done by someone else instead of leaving it up to the APSN or PSN to do it.

B. Areas for Improvement/Recommendations/Actions Taken

None

C. Good Practices/Professionalism Observed

None

D. J. Hansen

Date 5/24/88 Actions Completed _____ Date _____

To: Operations Superintendent - Nuclear

Date: 05/24/88

From: P. L. Walker
*(MOS Observer)*Shift: Day
 Night**A. Plant evolutions observed**

- Unit 3, Steady State Operations
- Unit 4, cleared a few hurdles and continued to heat up toward normal operating temperature.
- Attended Plan-of-the-Day meeting (7:20) and morning conference call meeting (7:40)

B. Immediate safety problems

None

C. Questionable work practices

None

D. Areas for improvement

1. Checking with Turbine Operators, I observed that there is still no method of tracking when transformer cooling fans are taken in and out-of-service, or why Transmission and Distribution does so. When I closed out item 88-0652, I was assured that a log entry would be provided to enable tracking of fan status. Nothing has changed.
2. Condenser Steam Jet Air Ejector Drain Line design needs to be looked at to evaluate water accumulation drain-off. Personnel and equipment are still getting doused when "Hogger" is placed in service, even with procedural change to ensure that drain valve is opened. The amount of water released is much less than before, but I'm still concerned about dousing the ejector radiation monitor.
3. I have seen quite a few cases of improperly supported pipes in the secondary system. An evaluation method is being proposed by Frank Muhammed which, if implemented fully, would correct the types of support problems I observed. The following questionable supports were observed:
 - a. Support for Unit 4 Priming Jet Piping between two Velan check valves - completely unloaded, no contact with spring support pad.
 - b. Support under valve 4-30-770 (north end of MSR-4A) almost fully compressed, and off center of spring.

- c. On both units, the purge valves which run in parallel with the main steam supplies to the MSR's are supported in piggy back fashion on the spring supports for the main steam inlet piping. These lines tend to have a lot of vibration, and the valve operators have a large momentarm to put stress on the valves and pipes.
 - d. A whole section of piping adjacent to Feedwater Heater 6B is misaligned and the supports are almost ineffective. This was addressed by REA 84-93, and is to be corrected under NCR 87-0052. Five supports are involved; two are off center of base pads, one is cocked and bent, and two spring supports are almost completely off the spring pads.
 - e. Support for valve 3-CV 2910 is completely pulled free of the concrete deck and the line is vibrating.
 - f. Valve 3-MOC-1431 support is shimmed and misaligned.
 - g. A spring support under a line on the south end of the 3B MSR is not contacting the line-totally non-supportive. (ne 20 TR 419 PTN).
 - h. Concerning two spring pads under line GPJ419 PTN (main steam to 3B MSR), one is fully compressed and the other is almost completely unloaded and is an example of a piggy-backed support for another line.
 - i. With regards to the massive MSR support pads, there seems to be an inconsistent philosophy with respect to the number of through bolts used in each support, ranging from no bolts at all to 3 or 4.
4. Work platforms around the MSR 4D and MSR 3B Reheat Line Valves have supports which are loose (unsecured) at the Turbine Operating Deck.

E.

Professionalism, Summary of Shift, Comments

A lot of work was done today in support of Unit 4's heat up, in conjunction with an emergency drill. The staff did a good job of coordinating all of the various efforts.

Completed By:

P. L. Walker

MOS Observer

Date: 05/24/88

Reviewed By:

J.W. Price
Operations Superintendent-Nuclear

Date: 5/25/88

Management
Review By:

PM-N

Date

SVP

Date

A.J.D.

5/25/88

Date

05/24/88

To: Operations Superintendent - Nuclear

Date: 05/24-25/88

From: Jeff Spodick
(MOS Observer)Shift: Day
 Night**A. Plant evolutions observed**

- Unit 4:
 - RPS Logic Testing
 - Safeguards Relay Testing
 - Safety Injection Check Valve Testing
- Unit 3:
 - Normal operation at 100% power
 - Response to Generator RTD Hi Temperature Alarm
- Common:
 - Shift briefing, PSN,APSN turnover

B. Immediate safety problems

None

C. Questionable work practices

None

D. Areas for improvement

Operating procedure 8702.2 Generator Gas H2 Temperature monitoring, provides instructions for the Generator RTD Hi Temperature Alarm Condition.

The procedure does not suggest reduction of megavars or increase in Turbine Cooling Water (TCW) flow as possible solutions to the high stator differential temperature condition.

The RCO correctly reduced megavars and increased generator gas pressure to correct the high differential temperature condition.

The procedures group should consider the above two items for inclusion in the procedure where appropriate.

E. Professionalism, Summary of Shift, Comments

Both unit 3 and Unit 4 Control Board operators exhibited close attention to detail in responding to abnormal plant conditions. The Unit 4 Control Board operator detected an abnormal pressurizer pressure control system response. He initiated actions to commence steam space venting of the pressurizer when he diagnosed the possibility of a "hard bubble" in the pressurizer.

The shift PSN, although busy most of the shift with numerous activities, managed to conduct a training checkout with the SRO trainee on shift. This shows a positive commitment toward training.

Completed By: Jeff Spodick
MOS Observer

Date: 05/24-25/88

Reviewed By: L.W. Price
Operations Superintendent-Nuclear

Date: 5/25/88

Management
Review By:

PM-N / Date / SVP / Date

JAD / 5/25/88 / VP / Date
05/24-25/88

0-ADM-019

Management on Shift (MOS)
MOS DAILY REPORT

Page

1

To: Operations Superintendent - Nuclear

Date: 05/24-25/88

From: H. L. Schneider
(MOS Observer)Shift: Day
 Night**A. Plant evolutions observed**

- o Unit 3, 100% Reactor Power
- o Unit 4, Mode 3
- o Beginning of shift (mids) meeting
- o Toured plant areas e.g., intake, turbine and radiation control area
- o Unit 4, reactor protection test
- o 4A Intake Cooling Water pump shaft invertigation

B. Immediate safety problems

None

C. Questionable work practices

None observed

D. Areas for improvement

No recommendations

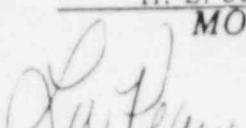
E. Professionalism, Summary of Shift, Comments

Good shift meeting, excellent exchange of information among all personnel involved.

Shift encountered many situations while completing their assigned tasks, each was addressed in a professional manner.

Completed By: H. L. Schneider
MOS Observer

Date: 05/24-25/88

Reviewed By: 
Operations Superintendent - Nuclear

Date: 5/25/88

Management
Review By: PM-N / Date / SVP / DateH.L.S. / 5/25/88
VP / Date
05/24-25/88

Date Started 05/24/88

PSN MOS

Date Finished 05/24/88

Initiating PSN Schimkus PSN _____ Completed PSN Schimkus

Initiating APSN Dallau APSN _____ Completed APSN Dallau

A. Questionable Work Practices/Actions Taken/Recommendations

None

B. Areas for Improvement/Recommendations/Actions Taken

1. Following PCM changes for undervoltage protection on 480 Volt Load Centers (past years), the door screws on the backside of Unit 4 480 Volt Load Center were stripped and won't secure into the doors. This should not have been left in this condition. Recommendation: Have Construction renew door screws to original condition. In the future don't leave a components equipment doors in poor condition because door repair is not part of the original PCM package. Workers should identify and PWO these items.

C. Good Practices/Professionalism Observed

Routine operations - Good operator actions to continue Unit 4 Heat up.

Date Started <u>05/25/88</u>	PSN MOS	Date Finished <u>05/25/88</u>
------------------------------	----------------	-------------------------------

Initiating PSN Salkeld PSN _____ Completed PSN Salkeld

Initiating APSN Guyer APSN _____ Completed APSN Guyer

A. Questionable Work Practices/Actions Taken/Recommendations

None

B. Areas for Improvement/Recommendations/Actions Taken

None

C. Good Practices/Professionalism Observed

All activities performed in a professional manner.

Reviewed By *DwP*

Date 5/24/88 Actions Completed _____ Date _____

Date Started	05/24/88	PSN MOS	Date Finished	05/24/88
--------------	----------	---------	---------------	----------

Initiating PSN	Wogan	PSN	Completed PSN	Wogan
Initiating APSN	Hollinger	APSN	Completed APSN	Hollinger

A. Questionable Work Practices/Actions Taken/Recommendations

B. Areas for Improvement/Recommendations/Actions Taken

C. Good Practices/Professionalism Observed

0-ADM-019

Management on Shift (MOS)
MOS DAILY REPORT

Page

1

To: Operations Superintendent - Nuclear

Date: 05/25/88

From: P. L. Walker
(MOS Observer)Shift: Day
 Night**A. Plant evolutions observed**

- o Unit 3, Steady State 100% Power Operations
- o Unit 4, Mode 3 cooled down and depressurized to less than 1000 psig to attempt a successful retest of check valves 876 A, B, and C

B. Immediate safety problems

None

C. Questionable work practices

None

D. Areas for improvement

None

E. Professionalism, Summary of Shift, Comments

Due to the amount of activity and the concern over the spray valves and the check valves, the shift was not as smoothly run or quiet as others I have observed.

Completed By: P. L. Walker
MOS Observer Date: 05/25/88Reviewed By: P. L. Walker
Operations Superintendent - Nuclear Date: 5/26/88Management Review By: CFB 15/56/88 SVP 10/24/88 VP _____ i Date
PM-N Date SVP Date VP Date

0-ADM-019

Management on Shift (MOS)
MOS DAILY REPORT

Page

1

To: Operations Superintendent - Nuclear

Date: 05/25-26/88

From: Jeff Spodick
(MOS Observer)Shift: Day
 Night**A. Plant evolutions observed**

- o Unit 3: Normal Full Power Operations
- o Unit 4: Reactor Coolant System (RCS) Pressure Boundary Check Valve Test
I&C and Operations repair and calibration of V-455B Pressurizer Spray Valve
- o PSN/APSN turnover
- o Shift Briefings

B. Immediate safety problems

None

C. Questionable work practices

None

D. Areas for improvement

None

E. Professionalism, Summary of Shift, Comments

A tailboard session and briefing was conducted in the control room prior to conducting the RCS Pressure Boundary Check Valve Test. This is an effective method of ensuring proper communications and coordination of effort between the Operations Department and the various Maintenance Departments.

Completed By:

Jeff Spodick
MOS Observer

Date: 05/25-26/88

Reviewed By:

L.W. Pearce
Operations Superintendent - Nuclear

Date: 5/26/88

Management Review By:

CB 15/26/88 ND 15/26/88 / VP Date 05/25-26/88

To: Operations Superintendent - Nuclear

Date: 05/25-26/88

From: W. R. Williams, Jr
*(MOS Observer)*Shift: Day
 Night**A. Plant evolutions observed**

- Mid shift start of shift briefing
- Operations and technical tailboard for Reactor Coolant System (RCS) check valve testing
- Residual Heat Removal (RHR) Heat Exchanger Hanger NCR discussions
- I&C work on spray valve 455B
- Toured:
3B and 4A Battery rooms, Inverter rooms, Cable Spreading Room, #3 Turbine Deck, #4 TPCW area, and #3 TPCW area
- Talked with various Maintenance foreman, chief, and supervisors; Technical department supervisors and Operations personnel

B. Immediate safety problems

None

C. Questionable work practices

None

D. Areas for improvement

Need better valve stroke values and bench spring settings to avoid rework on the spray valves as the units are heated-up.

Technical/Engineering needs to evaluate and provide valve stroke and bench spring settings to allow the spray valves to be set correctly when they are worked.

E. Professionalism, Summary of Shift, Comments

Good tailboard between Operations and Technical prior to the RCS check valve testing.

Good response by Electrical Maintenance to provide planning for work on MOV-4-865C problem. Also Mechanical Maintenance provided support to scope-out scaffolding needs and access any problems with inter-services.

I&C, Operations, and H.P. working closely to resolve 455B problems.

Mechanical Maintenance and Operations working to resolve leaking valves identified during over-pressure test.

Operations - good attention to detail. Example: tracking and correcting for increase in vibration on #9 Exciter bearing.

Operations/Maintenance Coordinator and Q.C. Supervisor made prompt notification to Control Room of RHR Heat Exchanger Hangers - NCR. The receipt of a copy of the NCR in the Control Room helped to further clarify the issue. Backfit was turned-on to make the repairs and were starting the repairs on early mid-shift.

Good positive attitude and teamwork through-out the night.

Completed By: W. R. Williams, Jr.
MOS Observer

Date: 05/25-26/88

Reviewed By: L.W. Penne
Operations Superintendent-Nuclear

Date: 5/26/88

Management
Review By:

CB 152488 ML 1526100 VP 1 Date
PMN Date SVP Date VP Date

Dr Started	05/25/88	PSN MOS	Date Finished	05/25/88
Initiating PSN	Schimkus	PSN	Completed PSN	Schimkus
Initiating APSN	Dallau	APSN	Completed APSN	Dallau

A. Questionable Work Practices/Actions Taken/Recommendations

None

B. Areas for Improvement/Recommendations/Actions Taken

Today I had to make a one hour reportable 10CFR50.72 notice to the NRC Operations Center. This was easily accomplished utilizing the PSN Emergency Plan/Significant Event Procedure Book. Then I had to notify the plant and corporate individuals of the event. The PSN duty call book was in such bad condition that I could not locate the Corporate V.P. of Nuclear Operations phone number. Thus I called the Juno Beach office operator to obtain his number.

Recommendations: Make this duty call book a controlled book in which the Emergency Preparedness Department is solely responsible to update and audit the book weekly to ensure completeness.

Note: They should be responsible for providing all department call supervisor phone numbers each week.

C. Good practices/professionalism Observed

Dayshift received excellent feedback from two Vice Presidents from two independent utilities as they toured our Nuclear Control Room. I was approached by one V.P. who informed me that he was totally impressed by how our Control Room Staff handled various off-normal situations being caused by a violent rain-storm outside. Some of the situations were a multitude of rain induced grounds, and Unit 3 Generator Exciter #9 bearing rapid increase in vibration due to rain induced cool down of secondary oil systems.

Date Started	05/25/88	PSN MOS	Date Finished	05/26/88
Initiating PSN	Salkeld	PSN	Completed PSN	Salkeld
Initiating APSN	Guyer	APSN	Completed APSN	Guyer

A. Questionable Work Practices/Actions Taken/Recommendations

None

B. Areas for Improvement/Recommendations/Actions Taken

The major steps of the PCV-455B maintenance procedure were not reviewed with the RCO prior to commencing work. Thus the RCO was unaware that the Pressurizer Spray valve was to be opened. After the initial transient, the I&C Supervisor was consulted and the maintenance procedure was modified to allow the RCO to cycle the valve when needed, giving him positive control of the activity.

C. Good practices/Professionalism Observed

During maintenance on PCV-455B, I&C in accordance with their procedure, locally opened this Pressurizer spray valve without notifying the RCO. The RCO, Rick Adamson, spotted the reduction in Reactor Coolant System (RCS) pressure, identified the cause (with no valve position indication and the hand auto station de-energized) and took compensatory action to stabilize the unit quickly. This is an example of continuous vigilance to plant conditions which is a cornerstone to watch standing professionalism.

Wkly

0-ADM-019

Management on Shift (MOS)
MOS DAILY REPORT

Page

1

To: Operations Superintendent - Nuclear

Date: 05/26/88

From: P. L. Walker
*(MOS Observer)*Shift: Day
 Night**A. Plant evolutions observed**

- Unit 3, 100% Steady State Operations - Generator temperature very close to load reduction setpoint (must go off-line).
- Unit 4, Heated up to 547° F, 2235 PSIG and stabilized.
- Attended Plan of the Day, morning phone call and afternoon shift turnover meetings

B. Immediate safety problems

None

C. Questionable work practices

None

D. Areas for improvement

None

E. Professionalism, Summary of Shift, Comments

Good shift - Unit 4 heatup was skillfully completed. Near the end of my shift, turbine/generator gas temperatures in Unit 3 reached load-threatening values, and the crew was monitoring them closely. Actions were taken to maximize cooling of generator.

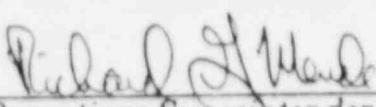
Completed By:

P. L. Walker

MOS Observer

Date: 05/26/88

Reviewed By:


P. L. Walker

Date: 5-27-88

Management
Review By:

10/16 10/27/88 / /
 PM-N Date SVP Date VP Date

To: Operations Superintendent - Nuclear

Date: 05/26-27/88

From: Wallace R. Williams, Jr.
(MOS Observer)Shift: Day
 Night**A. Plant evolutions observed**

- o Electrical Maintenance work on #3 Generator Resistance Temperature Detector (RTD) high delta temperature
- o Midshift turnover and start of shift briefing
- o Toured:
 - 3C and 4C Battery and Load Center Rooms
 - #4-480 Volt Load Center Rooms
 - Ground level of Unit 3 and 4 Turbine Building

B. Immediate safety problems

None

C. Questionable work practices

None

D. Areas for improvement

1. Operators not provided a copy of NCR on Unit #3 Residual Heat Removal Heat Exchanger hangers until Mechanical Maintenance brought one to the shift briefing. Last night (5/26-27) the copy provided to the Control Room helped answer concerns. Information of this type should be provided to the Control Room in a prompt manner.
2. Grass from the canal system is causing a burden for Operations and Mechanical Maintenance in keeping the various strainers clean and the equipment operating temperatures under control. Method to collect and dispose of grass is greatly needed. (This is a repeat of previous recent MOS reports).

E. Professionalism, Summary of Shift, Comments

1. Assisted Electrical Maintenance on high delta temperature on #3 Generator. Problem appears to be point #7 reading 2.4 degrees lower than any other point. Electrical Maintenance to complete review of historical data and provide recommendation.
2. Reviewed Electrical Maintenance work package for troubleshooting Exhaust Hood Temperature Alarm on Unit #3. Package was very good. It included Troubleshooting Guide Procedure, O-GME-102.1 and complete set of hi-highlighted drawings showing the circuits to be checked in yellow and those which are in the Generator lock-out circuit in red (and not to be checked).
3. Continue to have good start of shift briefing meetings.

Completed By:

Wallace R. Williams, Jr.

Date: 05/26-27/88

MOS Observer

Reviewed By:

Operations Superintendent-Nuclear

Date: 5-27-88

Management
Review By:CMB 15/5/88
PM-N Date SVP Date VP Date

0-ADM-019

Management on Shift (MOS)
MOS DAILY REPORT

Page

1

To: Operations Superintendent - Nuclear

Date: 05/26-27/88

From: Jeff Spodick
(MOS Observer)Shift: Day
 Night**A. Plant evolutions observed**

- Unit 3
 - Normal full power operation and scheduled surveillances
- Unit 4
 - Mode 3 operations and plant maintenance activities

B. Immediate safety problems

None

C. Questionable work practices

None

D. Areas for improvement

Non-Conformance Reports: These reports at times address safety-related equipment. When the reports finally make their way to the Control Room, they may be several hours old. Operations then may find that equipment referenced in the NCR places the operability of safety-related equipment in doubt.

Plant management should resolve the communications problems associated with the NCR system. The 5/26-27/88 PSN MOS Report contains a more detailed account of weaknesses associated with this system.

E. Professionalism, Summary or Shift, Comments

During the mid shift, the PSN was presented a Non-Conformance Report referencing the Residual Heat Removal (RHR) Room piping and supports. He conducted a thorough review of the report and concluded that based upon information in the report, the operability of the RHR System was in question. The PSN then took positive action to repair the equipment rather than waiting for disposition of the NCR.

Completed By:

Jeff Spodick
MOS Observer

Date: 05/26-27/88

Reviewed By:

Operations Superintendent - Nuclear

Date: 5-27-88

Management
Review By:OB 15/78 /
PM N Date SVP Date VP Date
Date 05/27/88

Date Started	05/26/88	PSN MOS	Date Finished	05/26/88
--------------	----------	---------	---------------	----------

Initiating PSN	Wogan	PSN	Completed PSN	Wogan
Initiating APSN	Hollinger	APSN	Completed APSN	Hollinger

A. Questionable Work Practices/Actions Taken/Recommendations

None

B. Areas for Improvement/Recommendations/Actions Taken

Place the Control Room i.e., PSN, APSN, on distribution for NCR's generated on plant equipment. Tech. Spec. requirements for action to be taken are as little as one hour. Timely evaluation of this information is absolutely essential.

C. Good Practices/Professionalism Observed

Unit 3, Normal operation

Unit 4, Plant startup with all required testing and support done satisfactorily.

DA 416.0

5-22-88

Completed

Date

Date Started 05/26/88

PSN MOS

Date Finished 05/27/88

Initiating PSN	Salkeld	PSN	Completed PSN	Salkeld
Initiating APSN	Guyer	APSN	Completed APSN	Guyer

A. Questionable Work Practices/Actions Taken/Recommendations

Two or three guards were engaged in informal conversation on the operations channel. The Security Shift Supervisor was notified. He identified two of those involved and will take appropriate action.

B. Areas for Improvement/Recommendations/Actions Taken

NCR 88-067 noted eleven items of concern. There were several problems with this NCR.

- | | |
|---------------|--|
| Item #2: | Referenced the wrong specification to which to inspect the hanger. |
| Item #5: | Said the reach rod to Residual Heat Removal (RHR) valve 757A "was found disconnected at the first gear box." In fact, the roll pin was found to be displaced about 1/4". |
| Item #8: | Identified hanger 3-ARH-118 as being discrepant when in fact it was hanger 3-AHR-84. Furthermore, the corrective action was inappropriate for this type of hanger. |
| Item #11: | Described a heat tracing line that was apparently spliced using red duct tape. In fact it was a scrap 3/4" piece of red duct tape stuck to a Post Accident Monitoring System pipe. |
| Items 7 & 8: | Were described as an "unanalyzed condition". The cognizant engineer assured us that these items were not "unanalyzed conditions," as per IC CFR 50.72. It is recommended that use of this term be avoided in the future to avoid confusion. |
| Items 5 & 11: | Were to have separate NCR's initiated which would address operability concerns. Either of these, if valid, would put the operating unit into a Limiting Condition for Operation (LCO) action statement. Both are routine maintenance items which should have been documented with a PWO, not an NCR. Had PWO's been written, the Control Room would have been notified and the operability and Tech. Spec. concerns addressed immediately. |

The Control Room was not notified of the NCR or discrepant conditions which were potential operability concerns for 13 hours; and then only after the Construction Supervisor brought a copy of the NCR to the Control Room.

The cognizant engineer was contacted. He told us the reason the Control Room was not informed was because Engineering had no procedure to do so.

It is recommended the QC and JPE be given guidance as to which items are best addressed via the PWO system instead of an NCR. Additionally the Control Room should receive a copy of any NCR's which may effect the operability of systems or components.

C. Good practices/Professionalism Observed

No comment

To: Operations Superintendent - Nuclear

Date: 05/27/88

From: P. L. Walker
(MOS Observer)Shift: Day
 Night**A. Plant evolutions observed**

- Unit 3, 100% Steady State Power Operation
- Unit 4, Mode 3, Getting ready for criticality
 - Working on a few valves
 - Performing Reactor Coolant System pressure leakage test
 - Adjusted boron for criticality
 - Performed turbine valves test

B. Immediate safety problems

None

C. Questionable work practices

None

D. Areas for improvement

None

E. Professionalism, Summary of Shift, Comments

Progressed smoothly, quietly and safely toward establishing criticality conditions.

It was nice to see no leakage develop during the leakage test.

Completed By: P. L. Walker
MOS Observer

Date: 05/27/88

Reviewed By: *P. L. Walker*
Operations Superintendent - Nuclear

Date: 5/31/88

Management
Review By:

PM/N	15/3/88	SVP	15/3/88	VP	1
	Date		Date		Date
					05/27/88

To: Operations Superintendent - Nuclear

Date: 05/27-28/88

From: Jeff Spodick
*(MOS Observer)*Shift: Day
 Night**A. Plant evolutions observed**

- o Unit 3:
 - Normal full power operation
 - Troubleshooting of Pressurizer Heater Control Bank low kilowatts problem.
 - Control Room response to a Reactor Coolant Pump flow perturbation
- o Unit 4:
 - Reactor Engineering shift briefing regarding Rod Position Technical Specifications
 - Reactor Startup
 - Auxiliary Feedwater testing

B. Immediate safety problems

None

C. Questionable work practices

None observed

D. Areas for improvement

Maintenance on the Control Room door: The status of this door has gotten considerably worse over the last two days. It is very difficult to open the door when exiting the Control Room. This could present a personnel hazard during a Control Room inaccessibility event.

E. Professionalism, Summary of shift, Comments

1. The approach to criticality was conducted in a very professional manner. A trainee conducted the approach under the supervision of the Reactor Operator. He was continuously monitored and frequently questioned to ensure he fully understood the process, including theoretical concepts.
2. The Control Room team constantly double checks Interim Technical Specifications, versus the original Technical Specifications to ensure compliance with both.

Completed By:

Jeff Spodick
MOS Observer

Date: 05/27-28/88

Reviewed By:

John J. Hause
Operations Superintendent - Nuclear

Date: 5/31/88

Management
Review By:John J. Hause
PM-N Date SVP Date1 VP Date
05/27-28/88

To: Operations Superintendent - Nuclear

Date: 05/27-28/88

From: Wallace R. Williams, Jr.
(MOS Observer)Shift: Day
 Night**A. Plant evolutions observed**

- o Unit 3, Full Power Operation
- o Paralleling of 4B Motor Generator (MG) set to 4A MG set using 4-OP-028.
- o #4 Reactor startup and criticality
- o 3A Reactor Coolant Pump seal leak-off problem
- o Auxiliary Feedwater testing prior to Unit 4 going on-line
- o Mid shift start of shift briefing

B. Immediate safety problems

None

C. Questionable work practices

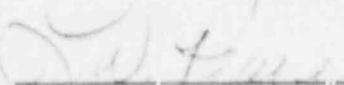
None

D. Areas for improvement

Repair Control Room door. Very difficult to open when exiting from Control Room.

E. Professionalism, Summary of Shift, Comments

1. During Reactor startup, APSN kept control board area clear of those persons not directly involved, thereby allowing the evolution to be done efficiently and without confusion.
2. 3A Reactor Coolant Pump seal leak-off monitored closely by Reactor Operator, APSN and PSN. Condition was discussed at briefing by APSN. Volume Control Tank level was decreased which finally returned leak-off to previous values. Operations personnel didn't stop here, but continued to review procedures, logs, and various parameters to search out why this happened.
3. Auxiliary Feedwater testing was completed successfully.

Completed By: Wallace R. Williams, Jr.
MOS Observer Date: 05/27-28/88Reviewed By: 
Operations Superintendent - Nuclear Date: 05/27-28/88Management Review By:
PM-N Date: 05/27-28/88 SVP Date: 05/27-28/88 VP Date: 05/27-28/88

Date Started 05/27/88

PSN MOS

Date Finished 05/27/88

Initiating PSN Wogan PSN _____ Completed PSN Wogan

Initiating APSN Hollinger APSN _____ Completed APSN Hollinger

A. Questionable Work Practices/Actions Taken/Recommendations

None

B. Areas for Improvement/Recommendations/Actions Taken

None

C. Good Practices/Professionalism Observed

Unit 4 Startup

Reviewed By *M. Hollinger*

Date 5/31/88 Actions Completed _____ Date _____

Date Started 05/28/88

PSN MOS

Date Finished 05/28/88

Initiating PSN Salkeld PSN _____ Completed PSN Salkeld
Initiating APSN Guyer APSN _____ Completed APSN Guyer

A. Questionable Work Practices/Actions Taken/Recommendations

None

B. Areas for Improvement/Recommendations/Actions Taken

The copies of 4-OSP.015.6 taken from the Control Room spare copy file were found to be out-of-date. Had this outdated procedure been used, it would have resulted in a misalignment of the Auxiliary Feedwater System. Additionally, during the last two midshifts, another outdated procedure was pulled from the Control Room spare copy file and an outdated procedure was found in the ANPO's spare copy file. All operators were reminded of the importance of verifying the revision date of a procedure as well as checking to find any active OTSC against the procedures. While the operator bears the final responsibility for assuring the procedure he uses is up to date, a more effective system needs to be established to assure outdated procedures are removed from the field promptly.

C. Good Practices/Professionalism Observed

Good communications and cooperative practices between all departments.

Reviewed By *D.W. Poole*

Date 5/29/88 Actions Completed _____ Date _____

To: Operations Superintendent - Nuclear

Date: 05/28/88

From: P. L. Walker
(MOS Observer)Shift: Day
 Night**A. Plant evolutions observed**

- Unit 3, 100% power, Steady State Operations, evaluating possible RCS leak.
Reportable event: Actuation of Control Room Recirculation and Containment purge isolation when a test switch on Containment Radiation Monitor R-11 was depressed. PWO issued.
- Unit 4, Synchronized to the Grid-power escalation to less than 50% power, held there until Rod Position Indicators were calibrated using flux map. Continued escalation toward 100%.

B. Immediate safety problems

None

C. Questionable work practices

None

D. Areas for improvement

None

E. Professionalism, Summary of Shift, Comments

Loading onto grid and subsequent power increase was performed very well.
Good job.

Completed By:

P. L. Walker

MOS Observer

Date: 05/28/88

Reviewed By:

Operations Superintendent - Nuclear

Date: 05/28/88

Management
Review By:XBS 15/28/88 SVP 15/31/88
PM-N Date SVP DateVP / Date
05/28/88

To: Operations Superintendent - Nuclear

Date: 05/28-29/88

From: Jeff Spodick
*(MOS Observer)*Shift: Day
 Night**A. Plant evolutions observed**

- Unit 3:
 - 100% power operation
 - RCS leak rate determination and crew efforts to determine leakage source
- Unit 4:
 - Power increase from 60%
 - Main Feedwater Pump oil system maintenance, shift turnovers, reliefs and shift briefings

B. Immediate safety problems

None

C. Questionable work practices

None

D. Areas for improvement

None

E. Professionalism, Summary of Shift, Comments

None

Completed By:

Jeff Spodick

MOS Observer

Date: 05/28-29/88

Reviewed By:

Jeff Spodick

Operations Superintendent - Nuclear

Date: *5/29/88*Management
Review By:GP
PM-N15/163
Date

SVP

15/31/88
Date

VP

Date

05/28-29/88

To: Operations Superintendent - Nuclear Date: 05/28-29/88

From: Wallace R. Williams, Jr.
(MOS Observer)Shift: Day
 Night**A. Plant evolutions observed**

- o Unit 3, Full Power Operation
- o Unit 4, about 60% power at start of shift and about 75% power at end of shift.
- o 3B Main Steam Isolation Valve nitrogen leak
- o 3A Reactor Coolant Pump seal leak-off still erratic
- o Toured 3 and 4 Intake area, #4 Feedwater Pump Room, Cable Spreading Room, and 3A and 4B Battery Rooms.

B. Immediate safety problems

None

C. Questionable work practices

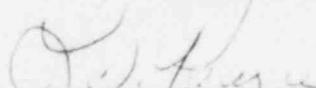
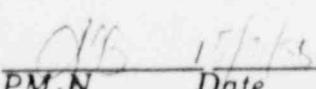
Hydrometer left touching terminal on a cell of 3A Battery and almost touching the terminal of the adjacent cell. Got with PSN and he addressed the concerns with his Turbine Operators. Recommend Training address proper battery care techniques and the reason for such with all personnel who work or take readings on the batteries.

D. Areas for improvement

None

E. Professionalism, Summary of Shift, Comments

1. Operation shift turnover with PSN's and APSN's very thorough and informative for both the on-coming and the off-going shifts.
2. 4B Steam Generator Feedwater Pump water-in-oil problems resolved so that the unit could continue towards 100% power.
3. Repair of the instrumentation nipple that had 3B Component Cooling Water Heat Exchanger out-of-service was completed but now the tubes are being cleaned before returning the heat exchanger to service.
4. 3B Main Steam Isolation Valve Nitrogen Regulator was repaired and leak testing now in progress.
5. Operations continuing to monitor 3A Reactor Coolant Pump seal leak-off. Also Containment Radiation Monitor R-11 and RCS leak rate being tracked as they continue to search for root cause.

Completed By: Wallace R. Williams, Jr.
MOS Observer Date: 05/28-29/88Reviewed By: 
Operations Superintendent - Nuclear Date: 5/31/88Management Review By: 
PM-N Date SVP Date VP Date
05/28-29/88

Date Started	05/28/88	PSN MOS	Date Finished	05/28/88
--------------	----------	---------	---------------	----------

Initiating PSN	Wogan	PSN	Completed PSN	Wogan
Initiating APSN	Hollinger	APSN	Completed APSN	Hollinger

A. Questionable Work Practices/Actions Taken/Recommendations

A nitrogen regulator for Main Steam Isolation Valve 3-2605 was found outside it's acceptable limits. It was subsequently adjusted, apparently without procedural guidance. This resulted in the valve being taken out-of-service due to inoperability. This challenges the design criteria and required a waiver of ADM-021 which is undesirable. No turnover was given on this evolution by I & C Department. This turnover could have helped troubleshoot the problems. The PSN recommended that I & C develop a training brief on proper adjustment of the regulators.

B. Areas for Improvement/Recommendations/Actions Taken

None

C. Good Practices/Professionalism Observed

The back shift I & C crew responded to the second Main Steam Isolation Valve (MSIV) problem very well and troubleshooted the regulator problem without knowledge of the day crew adjustment. Their responsiveness and troubleshooting abilities enabled us to minimize the length of time the MSIV was out-of-service.

Reviewed By

John F. Wogan

Date

5/31/88 Actions Completed _____ Date _____

To: Operations Superintendent - Nuclear

Date: 05/29/88

From: P. L. Walker
*(MOS Observer)*Shift: Day
 Night**A. Plant evolutions observed**

- Unit 3, Steady State Operation, crew successfully dampened out erratic Reactor Coolant Pump Seal behavior
- Unit 4, Power escalation from 60 to 100% power, stabilized unit. A hard ground developed on a bus and was promptly isolated.
- Control Room door is out-of-service again.

B. Immediate safety problems

None

C. Questionable work practices

None

D. Areas for improvement

Control Room door has been sticking (exit only) for the past few days. Maintenance worked on it, got it to function properly for a day, and it is back to being called out-of-service again. It is unfortunate that it is a so highly visible maintenance problem.

E. Professionalism, Summary of Shift, Comments

I liked the way the day shift crew smoothed out the pump seal erratic leak-off flow.

Another good day for all three crews I observed.

Completed By:

P. L. Walker

MOS Observer

Date: 05/29/88

Reviewed By:

John F. Walker

Operations Superintendent - Nuclear

Date: 05/29/88

Management
Review By:

PM-N

Date

SVP

Date

VP

Date
05/29/88

0-ADM-019

Management on Shift (MOS)
MOS DAILY REPORT

Page

1

To: Operations Superintendent - Nuclear

Date: 05/29-30/88

From: Jeff Spodick
(*MOS Observer*)Shift: Day
 Night**A. Plant evolutions observed**

- Normal full power operation at both units
- Unit 3, Turbine Cooling Water and Intake Cooling Water Strainer cleaning

B. Immediate safety problems

None

C. Questionable work practices

None

D. Areas for improvement

None observed

E. Professionalism, Summary of Shift, Comments

During the mid shift, it was necessary to individually valve out and clean the Turbine Cooling Water/Intake Cooling Water strainers. This evolution caused elevated temperatures to individual Turbine Cooling Water cooled components. Control Room personnel continuously monitored the affected components and expeditiously made the necessary adjustments.

Completed By:

Jeff Spodick

Date: 05/29-30/88

Jeff Spodick
MOS Observer

Reviewed By:

John H. Fawcett
Operations Superintendent - Nuclear

Date: 5/31/88

Management Review By:

J. J. S. *15/31/88* *J. J.* *15/31/88*
PM-N Date SVP Date VP Date
05/29-30/88

0-ADM-019

Management on Shift (MOS)
MOS DAILY REPORT

Page

1

To: Operations Superintendent - Nuclear Date: 05/29-30/88

From: Wallace R. Williams, Jr.
(*MOS Observer*)Shift: Day
 Night**A. Plant evolutions observed**

- Units 3 and 4 at full power operation
- 3A Reactor Coolant Pump seal leak-off still erratic at times.
- 4B Steam Generator Feedwater Pump oil is now free of water.

B. Immediate safety problems

None

C. Questionable work practices

None

D. Areas for improvement

None

E. Professionalism, Summary of Shift, Comments

Operations and Mechanical Maintenance displayed great teamwork in keeping the various strainers cleaned and back in service to support the units.

Very quiet and smooth running shift with everyone doing their part to keep the units functioning.

Completed By: Wallace R. Williams, Jr. Date: 05/29-30/88
W.R. Williams
*MOS Observer*Reviewed By: K.L. Tolosa Date: 5/31/88
K.L. Tolosa
*Operations Superintendent - Nuclear*Management Review By: G.B. 15/5/88 D.J. 15/31/88 VP /
PM-N Date SVR Date VP Date
05/29-30/88

Date Started 05/29/88

PSN MOS

Date Finished 05/29/88

Initiating PSN Wogan PSN _____ Completed PSN Wogan

Initiating APSN Hollinger APSN _____ Completed APSN Hollinger

A. Questionable Work Practices/Actions Taken/Recommendations

None

B. Areas for Improvement/Recommendations/Actions Taken

None

C. Good Practices/Professionalism Observed

None

Reviewed By D. D. Price Date 5/31/88 Actions Completed _____ Date _____

Date Started 05/29/88

PSN MOS

Date Finished 05/29/88

Initiating PSN Anderson PSN _____ Completed PSN Anderson

Initiating APSN Reese APSN _____ Completed APSN Reese

A. Questionable Work Practices/Actions Taken/Recommendations

While trying to replace nitrogen bottles to the Unit 3 Main Steam Isolation Valve Back-up System, six different nitrogen bottles were brought to the turbine deck with leaks. Three leaked from the threads where the valve screwed in and three leaked from the weld itself. I went to the gas house and surveyed all the bottles I could get to for a hydrostatic test date. I found about 1/3 of them with a greater than 10 year date. Many looked to be in very bad condition, (rusty, chipped and so on). I brought this matter up about a year ago and was assured that all the bottles would be hydroed that were out-of-date. I think this is a very hazardous condition for the safety of both personnel and equipment. I recommend that all bottles be checked immediately and those found to be out of the legal required hydrostatic test date time be immediately removed from the gas house and be hydroed or disposed of.

B. Areas for Improvement/Recommendations/Actions Taken

No comment

C. Good Practices/Professionalism Observed

No comment

Reviewed By

O.W. Peace

Date

5/31/88

Actions Completed _____

Date _____

Date Started 05/29/88

PSN MOS

Date Finished 05/29/88

Initiating PSN Salkeld PSN _____ Completed PSN Salkeld

Initiating APSN Guyer APSN _____ Completed APSN Guyer

A. Questionable Work Practices/Actions Taken/Recommendations

None

B. Areas for Improvement/Recommendations/Actions Taken

None

C. Good Practices/Professionalism Observed

Yes

Reviewed By D.W. Henn Date 5/31/88 Actions Completed _____ Date _____

THE SOUTH TEXAS PROJECT PARTICIPATION AGREEMENT AMENDED
HEREBY IS SUBJECT TO ARBITRATION
UNDER THE TEXAS GENERAL ARBITRATION ACT,
ARTICLE 224, ET SEQ., OF THE TEXAS CIVIL STATUTES

SOUTH TEXAS PROJECT
AMENDMENT NO. 3 TO
PARTICIPATION AGREEMENT

1. PARTIES: The parties to this Amendment No. 3 are: CITY OF SAN ANTONIO, acting through the City Public Service Board of San Antonio, hereinafter referred to as "San Antonio"; CENTRAL POWER AND LIGHT COMPANY, a Texas corporation, hereinafter referred to as "Central"; HOUSTON LIGHTING & POWER COMPANY, a Texas corporation, hereinafter referred to as "Houston"; and CITY OF AUSTIN, hereinafter referred to as "Austin".

2. RECITALS: San Antonio, Central and Houston executed as of July 1, 1973, the South Texas Project Participation Agreement providing for the licensing, construction, operation and maintenance of jointly owned and operated electric generation facilities to be known as the South Texas Project. San Antonio, Central, Houston and Austin executed: (i) Amendment No. 1 to the Participation Agreement effective as of December 1, 1973, whereby Austin became a Participant in the South Texas Project, and (ii)

Amendment No. 2 to the Participation Agreement effective as of March 1, 1975, whereby additional modifications were made in the terms and provisions of the Participation Agreement. Said Participation Agreement executed as of July 1, 1973, as amended by said Amendment No. 1 and said Amendment No. 2, is hereinafter referred to as the "Participation Agreement." Contemporaneously herewith San Antonio, Central, Houston and Austin are executing the South Texas Project Nuclear Property Insurance Project Agreement effective as of January 1, 1986.

3. AGREEMENT: The parties hereto, in consideration of the mutual covenants contained herein, agree as follows:

4. AMENDMENTS TO PARTICIPATION AGREEMENT:

The Participation Agreement is amended as follows:

4.1 Section 10.2.9 of the Participation Agreement is amended to read as follows:

"Pending action by the Management Committee on insurance recommendations, procure insurance binders providing such coverage as the Project Manager believes necessary and except as otherwise provided in a Project Agreement other than this Participation Agreement, upon action by the Management Committee, procure and maintain in force as permanent insurance all Project Insurance determined necessary by the Management Committee, furnishing, or causing to be furnished, to each Participant

evidence of the existence of such insurance as required by
Section 20 hereof; and"

4.2 Section 1.6 of Exhibit E to the Participation
Agreement is amended to read as follows:

"All expenses of procuring and maintaining
policies of Project Insurance, excluding, however, expenses
of procuring and maintaining policies of insurance pursuant
to the terms and provisions of any Project Agreement other
than this Participation Agreement."

5. INCORPORATION FROM PARTICIPATION AGREEMENT:

5.1 The definitions of terms contained in Section 4 of
the Participation Agreement, entitled "Definitions," are
incorporated herein by reference and such terms, to the
extent used in this Amendment No. 3, shall have the meanings
prescribed in said Section 4 of the Participation Agreement.

6. EFFECTIVE DATE:

6.1 Upon the execution of a counterpart of this
Amendment No. 3 by a duly authorized officer or
representative of each party hereto, this Amendment No. 3
shall become effective as of the 1st day of January, 1986.

IN WITNESS WHEREOF, the parties hereto have caused
this Amendment No. 3 to be executed as of the effective date
hereof.

ATTEST:

Donald Dunn
Secretary

CITY OF SAN ANTONIO,
acting through the City Public
Service Board of San Antonio

By

J. H. Kueker
General Manager

ATTEST:

Walter A. Ratcliff
Secretary
WALTER A. RATCLIFF

CENTRAL POWER AND LIGHT COMPANY

By

E. R. Brooks
ER BROOKS President and Chief Executive Officer P.M.

HOUSTON LIGHTING & POWER COMPANY

By

John L. Jordan
Chairman of the Board and Chief Executive Officer

CITY OF AUSTIN

By

James E. Asbury
City Clerk

Approved as to
Form - JG

010MDSAW/037E01
JCWLW;AP
05/09/86-1