TEXAS UTILITIES COMPANY
1987 ANNUAL REPORT

A COMMITMENT TO SERVICE

"As long as I can remember, my dad would get these calls, and 'cause he works for the electric company, he has to go . . .

"It always seems to be stormy and thundering and stuff . . .

"he tells me he just rides around in the truck . . .

I think he says that so I don't worry.

"Hey, Dad, you OK?"

TUELECTRIC

A COMMITMENT TO SERVICE

A COMMITMENT TO SERVICE . . .

. . . is the commitment of more than 16,000 employees doing nearly 2,100 different jobs in the Texas Utilities Company System. It is exemplified in the cover photograph taken from a television spot (shown at left) which emphasizes this commitment.

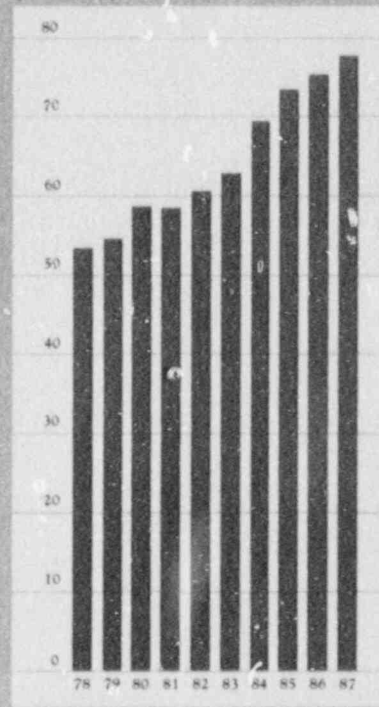
While emergency restoration of electric service is one of the more visible jobs, there are literally hundreds "behind the switch" that customers never see. Some of the jobs, people, and activities necessary to providing round-the-clock reliable electric service are pictured in this report.

Highlights

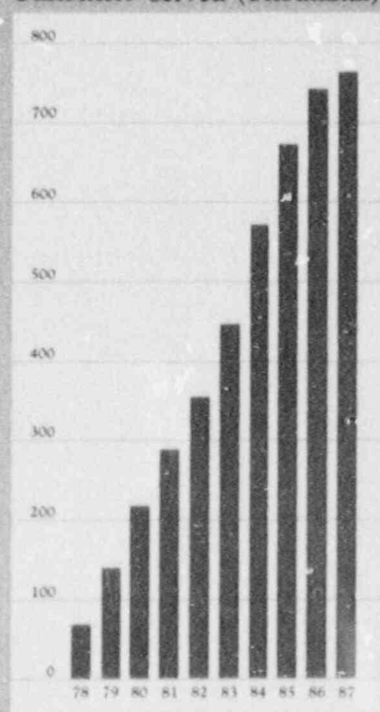
	1987	1986	% Change
Utility Plant*	**$15,172,994,000**	$13,566,133,000	11.8%
Construction Expenditures	**$ 1,688,831,000**	$ 1,519,619,000	11.1
Electric Energy Sales in Kilowatt-hours (000's)	**77,772,652**	75,254,775	3.3
Peak Demand (Kilowatts)†	**16,680,000**	16,537,000	0.9
Operating Revenues	**$ 4,082,923,000**	$ 3,932,045,000	3.8
Fuel and Purchased Power	**$ 1,585,610,000**	$ 1,479,213,000	7.2
Operating Expenses‡	**$ 1,648,430,000**	$ 1,643,272,000	0.3
Consolidated Net Income	**$ 679,976,000**	$ 626,851,000	8.5
Earnings per Share	**$ 4.55**	$ 4.45	2.2
Dividends Declared per Share	**$ 2.80**	$ 2.68	4.5
Book Value per Share*	**$33.02**	$31.24	5.7
Customers*	**2,094,866**	2,074,766	1.0
Employees*	**16,086**	16,927	(5.0)

** End of year*
† 1987 and 1986 include 113,000 and 130,000 kilowatts of interruptible demand, respectively
‡ Excludes fuel and purchased power

Kilowatt-Hour Sales (Billions)



Cumulative Growth in Customers Served (Thousands)



Contents

Management's Letter

To the Shareholders:

During 1987, efforts to complete and license the Comanche Peak nuclear plant continued. It was a year in which the Company made gains in resolving those nuclear issues, as well as in improving competitiveness, holding down costs through better efficiency and productivity, and further diversifying its resources used to generate electricity.

Continued emphasis was placed during the year on the Company's traditional commitment to providing low-cost, reliable electric service to its customers and a fair return to its investors.

Early in 1987, the new "TU Electric" identity was adopted for use throughout the Electric Company. By year end, the new identity was becoming widely accepted by customers and employees, helping focus attention on the company as an efficient provider of quality service.

Implementation of the TU System reorganization that began in 1984 continued last year with the consolidation of the System's communications, personnel, and purchasing departments. Efficiencies achieved through the reorganization and the need to further control costs resulted in an early retirement program, with more than 800 employees taking advantage of the option. Most were long-service employees, and their accomplishments over many years of dedicated service are deeply appreciated.

Through increased productivity, the System continues to serve a growing number of customers without an increase in number of employees. More than 20,000 customers were added last year, even though growth in the service area has slowed from the record levels experienced earlier this decade.

The Company continues to adapt to today's changing and increasingly competitive business environment, and a more competitive spirit was demonstrated in a number of respects in 1987. The Fuel Company paid the lowest average price for natural gas fuel since 1980 because of its pursuit of low-priced spot market gas and renegotiated contracts. Late in the year, a corporate marketing department was created to further consolidate certain related functions and thereby effectively meet the needs of customers in an increasingly competitive marketplace. In addition, three new combustion turbine generating units — the company's first new generating units since 1981 — were brought on line in early 1988 ahead of schedule and under budget.

The new combustion turbine units, the first of nine scheduled to be in service in 1988, are designed to serve peak periods of demand and provide important flexibility in the System's resource plan for providing reliable electric service. Reduced forecasted growth rates in demand for electricity were reflected in the deferral of the two Twin Oak lignite generating units and the Forest Grove lignite unit for two to three years each. The resource plan includes a carefully planned mix of lignite and nuclear generation, along with combustion turbines, cogeneration, load management, and a life-extension program for existing natural gas- and oil-fueled units.

Significant progress was made during the year in the effort to assure the safety of Comanche Peak's design and construction. TU Electric's detailed reinspection of construction and review of design, underway since 1984, have been completed and all reports submitted. A Corrective Action Program for Unit 1 is underway. The programs, which include validation of safety-related construction work, as well as 100% of the safety-related design of the plant, have received the approval of the Nuclear Regulatory Commission staff.

In January 1988, the Comanche Peak Response Team reported that about 98% of the reinspection and documentation reviews were in compliance with applicable design requirements. The CPRT also reported that the corrective action program provides reasonable assurance that the plant's structures, systems, and components will be capable of performing their intended functions.

TU Electric agreed in February 1988 to purchase, subject to regulatory approval, the Texas Municipal Power Agency's 6.2% share of Comanche Peak and settle pending litigation between the parties. The company will purchase TMPA's share for a current dollar cost of approximately $456 million, which is based on TU Electric's cost per kilowatt for its existing share of the plant.

In November 1987, the Atomic Safety and Licensing Board issued a schedule for resuming the Comanche Peak operating licensing hearing process. Public hearings are expected to begin later in 1988. Because the reinspection, reanalysis and corrective action program is demonstrating that Comanche Peak is being built with a high level of quality, management is confident that an operating license will be granted.

In March 1988, the company estimated that Unit 1 would be in commercial operation at the end of 1989, with that estimate based on the granting of an operating license and fuel load in mid-1989. Construction and capitalization of allowance for funds used during construction on Unit 2 will be suspended for about one year, beginning in April 1988. The suspension of construction will allow concentration of resources on Unit 1. Suspending capitalization of AFUDC will reduce earnings. Unit 2 is not expected to be in commercial operation until after the peak season of 1991.

If the schedule for Unit 1 is achieved, it is estimated that TU Electric's 94 percent share will cost $8.54 billion, or $3,950 per kilowatt. Because of uncertainty about the commercial operation date of Unit 2, no estimates for AFUDC after construction resumes have been included.

Operating results for 1987 reflect the effect of cost control and productivity efforts. Earnings per share of common stock were $4.55, compared to $4.45 in 1986. Electric energy sales were up 3.3%.

Construction expenditures during the year totalled $1.69 billion. Funds from operations provided 18.2% of 1987 construction expenditures.

During 1987, the System raised about $1.49 billion through long-term financing, including about $142.5 million from participation in the dividend reinvestment and employee savings plans. A portion of these funds was used to retire $132.5 million of high-interest debt.

The elections of Jerry Farrington as chairman of the board and chief executive and Erle Nye as president became effective in February 1987. Farrington succeeded Perry G. Brittain, who retired in the spring of 1987 after 37 years of valued service to the Company.

In February 1988, the Board raised the regular quarterly dividend from 70 cents per share to 72 cents. The new quarterly rate is payable April 1. Dividends declared on the common stock have been increased for 41 consecutive years.

Continuing commitment to providing low-cost, reliable service to customers is essential if the Company is to succeed in today's competitive business climate. The employees of the System continue to perform with distinction, and their continued dedication and commitment to safety, improved productivity and excellence in all aspects of customer service will ensure that success. Their efforts and the continued interest and support of our shareholders are appreciated.

March 18, 1988

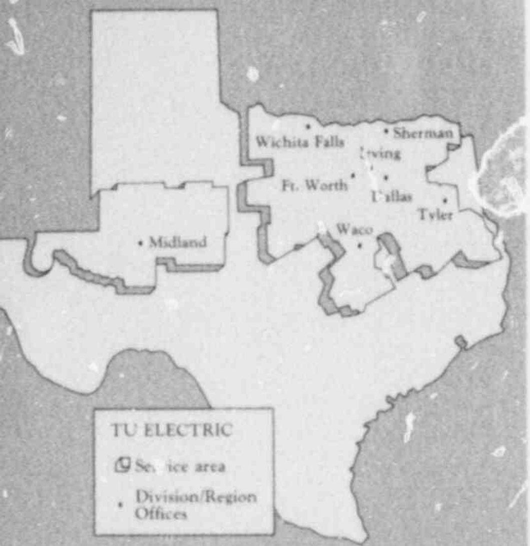
JERRY FARRINGTON
Chairman of the Board

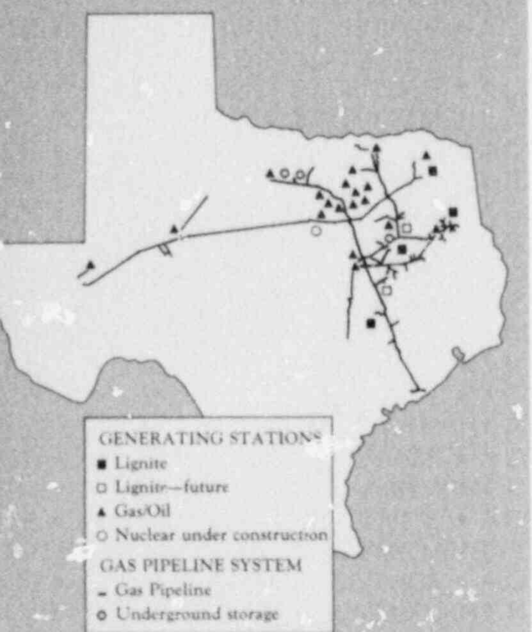
Jerry Farrington

ERLE NYE
President

Erle Nye

System Companies





Texas Utilities Company is an investor-owned holding company for an electric utility system. The Company provides its six wholly owned subsidiaries with common stock capital and short-term funds required for their construction programs. At year-end, the common stock of the Company was owned by some [illegible]3,300 registered shareholders. The Company's principal subsidiary is Texas Utilities Electric Company, now known as TU Electric.

Texas Utilities Electric Company (TU Electric) is engaged in the generation, purchase, transmission, distribution, and sale of electricity. The company operates 19 gas-/oil-fueled and four lignite-fueled generating stations.

TU Electric provides electric energy to approximately 5,160,000 people—about one-third of the state's population. The service territory extends 600 miles from far West Texas eastward to near Louisiana, and is about 250 miles deep, from the Oklahoma border southward into Central Texas.

Service is provided in 87 counties to 361 incorporated cities, including Dallas—the nation's eighth-largest city—and Fort Worth, Midland-Odessa, Wichita Falls, Arlington, Irving, Plano, Waco, Tyler, and Killeen. The economy of the service area is highly diversified. Major industries include defense, electronics, aerospace manufacturing, and oil and gas development. In addition, the area is a center for banking, insurance, commerce, distribution, farming and ranching, and recreational and cultural activities. Dallas-Fort Worth International Airport—the world's fourth-busiest airport—has helped make the Dallas-Fort Worth area third in the nation in concentration of corporate headquarters.

Texas Utilities Fuel Company owns a natural gas pipeline system; acquires, stores, and delivers fuel gas; and provides other services for the generation of electric energy by TU Electric.

Texas Utilities Mining Company owns and operates fuel production facilities for the surface mining and recovery of lignite for use as fuel for TU Electric's generating stations.

Texas Utilities Services Inc. (TU Services) furnishes financial, accounting, computer, and other administrative services at cost to the System companies.

Basic Resources Inc. is engaged primarily in the development of energy resources and related technology and services.

Chaco Energy Company was organized to own and operate facilities for the acquisition, production, sale, and delivery of coal and other fuels.

System Report

OPERATIONS

The System continued its growth at a slower pace during 1987, adding some 20,000 new customers, despite an overall slowdown in the state's economy.

The diversity of the service area contributed to better economic conditions than most of the state experienced. Service area unemployment was 5.5% at year-end 1987, compared to 6.5% at the end of 1986 and to the December 1987 state-wide figure of 6.8%.

TU Electric's energy sales were again the highest of any investor-owned electric utility in the nation, totalling nearly 78 billion kilowatt-hours, a 3.3% increase over 1986.

Peak demand record set

On August 6, customers set a record peak demand of 16,680,000 kilowatts, including 113,000 kilowatts of interruptible demand, exceeding the previous record set in July 1986 by about 1%. System net capability at the time of the peak was 19,465,000 kilowatts, including 850,000 kilowatts of short-term cogeneration and 130,000 kilowatts of other purchased power capacity.

A new daily record for energy consumption was set on August 17, as customers used 317,657,000 kilowatt-hours.

Weather conditions for the summer of 1987 were milder than normal and comparable to those of 1986. The peak load occurred during a 102-degree temperature day, after four consecutive days of 100-degree or higher temperatures.

Employees meet challenges

Employees' dedication, skills and efforts helped meet the record demand and other challenges in carrying out the System's commitment to service during 1987.

Employees from around the System were called on to restore two units damaged by fire in February at the Lake Hubbard generating station near Dallas and were able to restore both units in time for service in the summer peak season.

Employees also responded to weather problems during the year. On November 16, a tornado swept through Palestine in East Texas, knocking out electric service and damaging transmission towers, lines, and other equipment. Round-the-clock efforts by employees restored service in three days.

An ice storm in early January 1988 again tested employees' preparedness and ability to respond to an emergency situation, and their efforts helped minimize power outages.

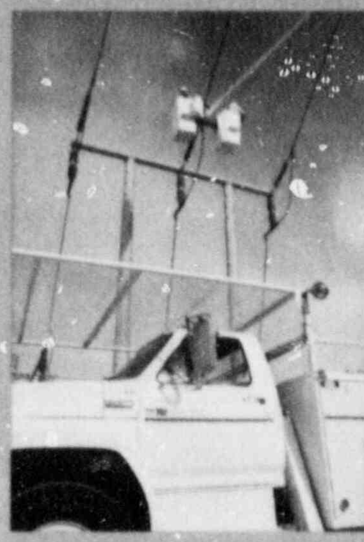
The System emphasizes safety in every phase of its operations. These efforts were again effective in 1987, as numerous employee groups reached safety milestones, set records, and earned distinguished safety awards. The continuing attention to safety contributes significantly to employees' health and welfare, as well as to the System's productivity.

Consolidations continue

As part of continuing efforts to serve customers more efficiently at lower cost, a new corporate identity, "TU Electric," was introduced for Texas Utilities Electric Company in early 1987. Also in 1987, Texas Utilities Services Inc. became known as "TU Services."

Control room at gas-fired plant

Employees' safety performance



Service truck

System operations center

Mountain Creek Data Center

Competitive marketing

The realignment of accounting and treasury operations in TU Electric that was effective January 1, 1987, is providing savings and improved management and accounting information. The Personnel, Purchasing, and Communications functions were consolidated in 1987 to achieve additional economies.

Because of the consolidations and the continuing emphasis on cost control, a special early retirement program was offered in June. More than 800 employees accepted the plan.

Computerization continues to make more efficiencies possible. The new Mountain Creek Data Center went into operation in late 1987. The new facility is the TU System's second computer center. It will absorb part of the growing load and eventually will serve as a backup facility to the Mesquite Data Center.

Marketing role to increase

In 1987, the company took steps to return to more aggressive marketing in an increasingly competitive business environment.

A marketing function was created at the TU Electric corporate level to plan and develop the company's marketing policies and programs to more effectively serve the needs of customers and to support economic development. A campaign began in 1987 to inform customers, builders, and developers of the company's comparatively attractive rates, high-quality service, and the benefits of homes built to TU Electric's Energy Action standards.

TU Electric continues to emphasize load management as a key element in reducing the expense of new generating capacity needed for customer growth. Since 1981, load management has reduced growth in peak load by more than 785 megawatts, an amount more than the output of one large lignite unit. The program has been successful because it provides participating customers the convenience and reduced operating costs of high-efficiency equipment and building structures. All customers benefit through reductions in the company's construction expenditures.

FUEL AND PURCHASED POWER

Assured supplies of fuel at competitive prices and flexibility in their acquisition and use are vital to the System's commitment to be a low-cost supplier of electricity.

During 1987, the Fuel Company continued its aggressive efforts to make favorable natural gas purchases on the spot market and to renegotiate fuel contracts. These helped lower the price of gas by 8% to \$2.56 per million Btu, down from the 1986 average of \$2.77.

The cost of lignite still averaged considerably less than half that of gas at \$1.07 per million Btu. The composite fuel cost for 1987 of \$1.82 per million Btu, compared to \$1.84 in 1986, is the lowest since 1981. The downward trend of fuel costs over the past three years appears to have leveled off.

The Fuel Company delivered 376 billion cubic feet of natural gas to TU Electric in 1987, and its pipeline system's operating flexibility was enhanced with the completion of a 58-mile natural gas pipeline in East Texas. The new addition, jointly owned with two other gas companies, gives the Fuel Company better access to East Texas gas supplies, particularly during peak demand periods.

The company owns more than 2,200 miles of pipeline along with underground gas storage reservoirs with a total usable capacity of some 28 billion cubic feet.

Lignite supply increased

Lignite coal leases on 8,700 acres in Titus County were obtained in 1987 to help assure a future source of low-cost lignite fuel for the nearby Monticello power plant.

The availability of more than 80 million tons of additional recoverable lignite will provide additional savings to TU Electric customers. The new supply increased the company's proven recoverable lignite reserves to about 800 million tons at year end. TU Electric's lignite plants burned approximately 29 million tons in 1987. The Mining Company continues to be the nation's fourth largest coal miner in annual tonnage mined.

Nuclear fuel ready

Nuclear fuel assemblies needed for initial operation of Comanche Peak's Unit 1 are stored at the plant site. Additional assemblies needed for the start-up of Unit 2 are in storage at the vendor's fabrication facility. Additional fuel is under contract.

Spent fuel for more than 20 years of plant operation can be safely stored on site. This storage capacity can be increased, if needed, until the federal government opens a permanent disposal facility.

Chaco litigation continues

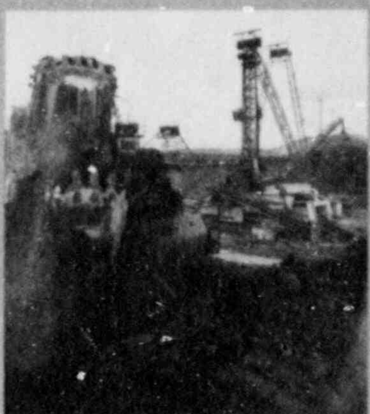
Discovery continues in litigation involving Chaco Energy Company, a nonutility subsidiary of the Company, and Santa Fe Industries, Inc., and its subsidiaries. A trial date is expected to be set sometime in 1989.

In 1977, Chaco signed agreements for more than 320 million tons of coal in northwestern New Mexico. In December 1981, the Company and Chaco filed suit against Santa Fe Industries, Inc., and two of its subsidiaries and against Thercol Energy Company and Peabody Coal Company, alleging, among other things, violation of federal and state antitrust laws and other unlawful conduct involving these agreements, which have made the commercial mining of this coal uneconomical. The suit seeks to have the agreements declared void and unenforceable and also seeks damages and other relief.

In January 1983, the Company and Chaco settled all claims against Thercol and Peabody. The settlement did not affect the claims asserted against Santa Fe Industries and its subsidiaries.

Fuel operations dispatching office

Gas pipeline addition



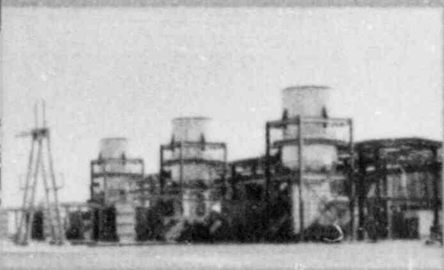
Mining lignite with the cross pit spreader

Sources of Kwh and Fuel Cost

	Percent Kwh by Fuel and Purchases			Cost Per Million Btu		
	1987	1986	1985	**1987**	1986	1985
Fuel Use:						
Gas/Oil*	**43%**	44%	50%	**$2.56**	$2.77	$3.41
Lignite	**44**	50	47	**1.07**	.98	.96
Total/Average Cost	**87**	94	97	**$1.82**	$1.84	$2.25
Purchased Power	**13**	6	3			
TOTAL	**100%**	100%	100%			

*Oil less than 1%

Resource planning



Combustion turbines

New control system at an existing plant

RESOURCE PLANNING

Innovation and flexibility in long-range planning enable the System to provide service to a growing number of customers when and where it is needed.

A revised resource plan for meeting expected requirements for electricity for the next 10 years was announced in March 1988. Customer needs are expected to increase by more than 8,700,000 kilowatts over the next 10 years, based on a projected average annual load increase of 2.5% and maintaining necessary reserve capacity.

The Comanche Peak nuclear plant remains a cornerstone of the plan and is needed, along with lignite and existing gas-fired power plants, for added fuel diversity and stability and to assure reliable power for the future.

The 10-year plan includes load management programs to reduce the need for new generation by some 1,400,000 kilowatts. Other resources utilized are combustion turbines, cogeneration, and a life extension program for existing gas-fired plants.

Resource Plan 1988-1997

Resource	Capability (Kilowatts)	Percent
Lignite	2,250,000	26%
Nuclear	2,162,000	25%
Combustion turbines	1,495,000	17%
Load management	1,422,000	16%
Cogeneration, other purchases* and unspecified additions	1,444,000	16%
Total	8,773,000	100%

*Includes wind, solar, and other resources

Combustion turbines ready

Combustion turbines will supply a significant portion of the projected increased need for capacity during periods of peak usage. Almost 1,500,000 kilowatts will come from these fast-starting units over the next 10 years.

Construction and testing at full load of three new 65,000-kilowatt turbine units were completed in late 1987 at the Permian Basin Plant in far West Texas. Six similar units are being constructed at the Morgan Creek Plant for a total of 585,000 kilowatts to be in service for the 1988 summer peak season. An additional six units (390,000 kilowatts) are scheduled for 1990.

Cogeneration added

Three long-term cogeneration projects, with a total of 611,000 kilowatts of capacity, were placed in service during 1987, making a total of 681,000 kilowatts of such capacity.

Under the new resource plan, cogeneration and small power sources will provide at least an additional 624,000 kilowatts of new capacity from 1988-1997. If needed, more cogeneration is an option, provided qualifying facilities are found and the economics prove to be beneficial.

In June 1987, TU Electric signed its fifth long-term cogeneration contract. Under the 13-year contract, Encogen One Partners, Ltd., will provide as much as 255,000 kilowatts by December 1989 from a facility located near Sweetwater, Texas. The company plans to continue to contract for short-term cogeneration to help meet winter and summer peak needs in 1988 and 1989.

Life of gas units to be extended

A significant change in the revised Resource Plan involves greater reliance on existing gas-fired units through a life extension program. Planned replacement of certain equipment, coupled with existing maintenance programs, can extend the life of a unit beyond its normal life expectancy.

Compared to other options, the relatively low cost of extending the life of existing generating units and the availability of gas supplies make this program especially attractive in today's economy. The life extensions of some power plants will ensure their continued availability and dependability for several more years.

Lignite units deferred

In September 1987, the company announced it would defer construction of three lignite units. Twin Oak Units 1 and 2 in Robertson County were postponed until 1994 and 1995, respectively. Forest Grove Unit 1 near Athens was rescheduled for 1997.

The deferral was in response to the decrease in the growth of long-range forecasted customer demand for electricity and a decision to defer some previously planned retirements of certain gas-fueled generating units.

Construction schedule

Unit	Capability (Kilowatts)	Peak Season Service
Combustion turbines	585,000	1988
Comanche Peak 1	1,081,000*	1990
Combustion turbines	390,000	1990
Comanche Peak 2	1,081,000*	1992
Twin Oak 1	750,000	1994
Twin Oak 2	750,000	1995
Forest Grove 1	750,000	1997

*Net capability to TU Electric, including purchase of TMPA's share

COMANCHE PEAK

Major emphasis during 1987 continued to be on TU Electric's reinspection program, which was nearing completion by early 1988, and the Corrective Action Program. Through this effort, which began in late 1984, the Comanche Peak Response Team has been addressing all concerns about the plant's construction and design adequacy.

A milestone was attained early in 1988 when the Nuclear Regulatory Commission staff's Office of Special Projects, which is assigned to manage all aspects of the NRC staff's licensing and inspection efforts at Comanche Peak, announced its approval of the CPRT and CAP efforts. The office said the plans adequately describe the means by which TU Electric intends to establish the safety of the plant's design and construction.

The programs have included validation of safety-related construction as well as 100% of the safety-related design of the plant (except for components provided by proven nuclear vendors).

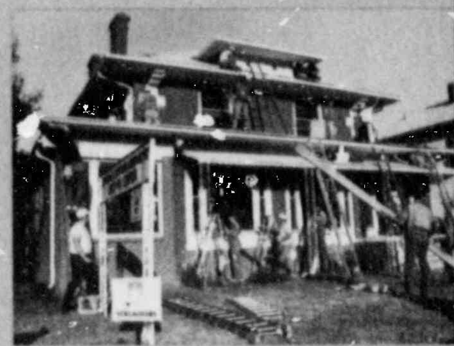
Another milestone was reached when the NRC staff, in March 1988, issued a Supplemental Safety Evaluation Report on TU Electric's programs to address all piping and pipe support issues. The report concluded that the programs are sufficient to ensure that licensing commitments are satisfied and that the issues raised are being properly resolved.

In December 1987 and February 1988, the CPRT submitted to the Nuclear Regulatory Commission two reports — the Collective Evaluation Report and Collective Significance Report — stating its overall summary and conclusions about the plant's design, quality of construction, and its quality assurance and testing programs.

In the Collective Evaluation Report, the CPRT stated that about 98% of the reinspection and documentation reviews were in compliance with applicable design requirements and identified no programmatic problem not already being addressed.

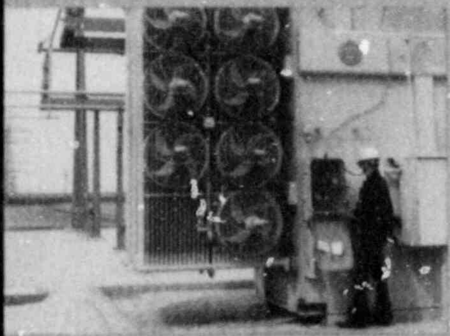
The Response Team also found that the present quality assurance program is effective and the historic quality

Customer communications



Employee community volunteers

Transmission crew



Substation

Distribution line work

assurance program was generally adequate. Those problems that were identified have been corrected and actions have been taken to prevent recurrence. In addition, the testing program and other start-up activities were found to have been generally adequate and properly implemented.

According to the Collective Significance Report, the Corrective Action Program provides reasonable assurance that the structures, systems, and components at Comanche Peak will be capable of performing their intended safety functions.

In December 1987, TU Electric and Gibbs & Hill, Inc., reached agreement settling TU Electric's potential claims against Gibbs & Hill related to engineering and design services performed for Comanche Peak. TU Electric and the joint owners are to receive a total of $25 million in cash, deferred payments, and future engineering services to be provided to TU Electric on non-nuclear projects.

The settlement is considered favorable to TU Electric and its customers. Protracted litigation would have depleted Gibbs & Hill's limited resources and created large legal expenses for the Comanche Peak owners.

Preparations made for operation

Progress was made during the year toward fully staffing TU Electric's permanent on-site engineering staff.

In addition, advances were made in preparing for commercial operation. A training annex building, which will allow plant maintenance employees to receive hands-on training in laboratories and realistic environments, opened during the year.

TU Electric is committed to providing all Comanche Peak shift operations supervisors experience through participation in control room operations in an on-line nuclear plant. As of December 1987, the program to carry out that commitment was 88% complete. Further operational experience also was gained in 1987 when a number of Comanche Peak reactor operators and auxiliary operators assisted in preparing a unit at the Braidwood nuclear plant in Illinois for initial start-up.

Licensing effort continues

In November 1987, the Atomic Safety and Licensing Board issued a schedule for resuming the Comanche Peak operating licensing hearing process. Hearings had been suspended since January 1985 so the CPRT could address concerns about the plant's design and construction.

Under the schedule, which is similar to ones proposed by TU Electric and the NRC staff, public hearings are expected to begin later in 1988 after the NRC staff issues its Supplemental Safety Evaluation Reports on the Collective Significance Report and status reports on the Corrective Action Program.

In July 1987, the Atomic Safety and Licensing Appeal Board ruled that an amended contention contesting the NRC's extension of the construction permit for Unit 1 is appropriate as the basis for ASLB hearings on the extension. The contention was filed by two intervenors, Citizens Association for Sound Energy and a former plant employee.

In March 1988, the company filed a motion to consolidate the construction permit extension and operating license proceedings because of their many common issues.

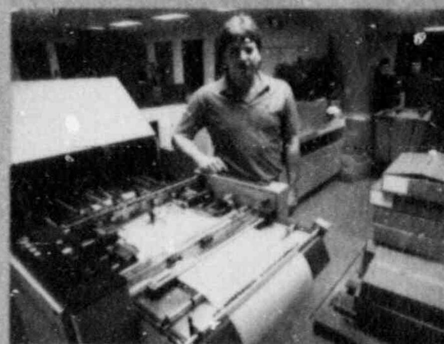
Cost and schedule revised

Because of the schedule established by the Atomic Safety and Licensing Board for resumed licensing hearings and TU Electric's schedule for completing reports on which the hearings would be based, the company announced in November 1987 that the schedule estimate for Unit 1, made in November 1986, was no longer achievable.

Revised cost and schedule estimates were announced in March 1988. The company estimates that Unit 1 will be in commercial operation at the end of 1989, with that estimate based on the granting of an operating license and fuel load in mid-1989.

Construction and capitalization of allowance for funds used during construction on Unit 2 will be temporarily suspended for about one year, starting in April

Reference library



Bill preparation

Computer training

Construction expenditures

	1987	Estimated 1988	Estimated 1989	Estimated 1990
	Millions of Dollars			
Electric property:				
Production*	$ 972	$ 842	$ 592	$ 438
Transmission	61	50	69	76
Distribution	209	195	225	233
General	34	20	28	30
Other utility property	26	43	23	73
Total	1,302	1,150	937	850
AFUDC*‡	387	350	463	50
Total construction expenditures*†	$1,689	$1,500	$1,400	$ 900
Such expenditures do not include AFUDC on Unit 2 of Comanche Peak for any period after March 1988 or the following:				
Nuclear fuel*	$ 1	$33	$15	$15
Non-utility property	28	37	48	59

*Includes ongoing amounts for an additional 6.2% interest in Comanche Peak, which is subject to purchase from TMPA as follows (see Note 11 to Financial Statements):

	1988	1989	1990
Production	$ 50	$ 32	$ 16
AFUDC	23	30	1
Total construction expenditures	$ 73	$ 62	$ 17
Nuclear fuel	$ —	$ 1	$ 1

‡Allowance for funds used during construction.

†Estimated construction expenditures do not include amounts for the 1988 and 1990 combustion turbine units. Plans call for the 1988 combustion turbines to be owned and constructed by a third party and sold to a lessor after the tax in-service date; TU Electric will then lease the units. Turnkey construction of the 1990 combustion turbines is planned, and TU Electric will then enter into an operating lease agreement.

Customer information center

Telephone customer service

Display at State Fair of Texas

1988. The suspension of construction will allow concentration of resources on Unit 1. Suspending capitalization of AFUDC will reduce earnings. Unit 2 is not expected to be in commercial operation until after the peak season of 1991.

The new estimates represent a delay of about a year for Unit 1 and about two years for Unit 2 from the estimates announced in November 1986.

Based on this schedule, it is estimated that TU Electric's 87⅘ percent share of Comanche Peak will cost $7.98 billion, including AFUDC, compared to the $6.7 billion estimated in November 1986.

In early 1988, the company agreed to purchase the Texas Municipal Power Agency's 6.2 percent share of Comanche Peak. With regulatory approval, the company's share of the plant will be increased to approximately 94 percent and will bring TU Electric's estimated completed cost to $8.54 billion, including AFUDC, or about $3,950 per kilowatt. The previous estimated cost was about $3,300 per kilowatt.

Because of uncertainty about the commercial operation date of Unit 2, the cost projections do not include estimates for AFUDC after construction of the unit resumes.

Since the company has only limited control over the licensing process, no assurance can be given that estimates of commercial operation dates of the Comanche Peak units can be met or that their estimated completion costs will not be exceeded.

Litigation

In May 1986, TU Electric filed suit in State District Court in Dallas County against the minority owners—the Texas Municipal Power Agency, Brazos Electric Power Cooperative, Inc., and Tex-La Electric Cooperative of Texas, Inc.—asking the court to resolve disagreements over the Comanche Peak Joint Ownership Agreement. In response, cross-actions and lawsuits against TU Electric and the company were filed by the minority owners.

In February 1988, TU Electric agreed to purchase TMPA's 6.2% share of Comanche Peak and settle pending litigation between the parties. Under terms of the agreement, which is subject to regulatory approval, the present value of the amount TU Electric will pay TMPA over the next five years for its share of Comanche Peak, nuclear fuel, transmission facilities, and costs related to the pending litigation is approximately $456 million.

The company believes the agreement is in its best interests since it provides TU Electric with additional needed generating capacity without increasing the company's cost per kilowatt in the Comanche Peak project and reduces its expenses associated with the litigation.

Additional discovery is scheduled with the other two parties, Brazos and Tex-La, with trial set for October 1988.

RATES AND REGULATIONS

TU Electric's current rate levels, excluding fuel charges, were set by the PUC in November of 1984. Based on factors that are presently known, TU Electric does not plan to receive a rate increase until Comanche Peak Unit 1 is in commercial operation.

Since the rate changes made in 1984, TU Electric's rates have decreased by more than

10% because of declining fuel costs and the Fuel Company's aggressive gas contract renegotiations. The company continues to believe that the rate increase when Comanche Peak Unit 1 goes into service can be held to about 10%. Therefore, the increase for Unit 1 would bring the company's current rates only to the level they were after the 1984 rate proceedings.

Rates decrease

The company's rates compare favorably to others in the state and nation. For the 12 months ended February 1988, TU Electric had the second lowest residential rates of investor-owned utilities in Texas. It also had the sixth-lowest residential rates of the 25 largest cities in the nation.

In 1987, two fuel-related refunds were made. A request to refund over $55 million was authorized for February and a second approved for nearly $70 million for May. Also, the composite fuel charge was lowered in February 1987. Since February 1986, $391 million in fuel costs have been refunded to customers and rates have been lowered overall by 10.3%.

RESEARCH AND DEVELOPMENT

The System continues to be involved in research and development of new products, procedures, and technologies that improve service and save the customer money.

At the Environmental Research Center at Big Brown, graduate level studies continued for the 17th consecutive year. The research, coordinated through an independent committee of university professors, addresses environmental concerns and provides information to improve the land, air, and water quality programs at the System's lignite facilities.

The System also actively supports research conducted through the Electric Power Research Institute. EPRI administers a coordinated, nationwide research and development program to ensure future availability, efficient production, delivery, and use of electric energy while minimizing effects on the environment.

As an example, EPRI is involved in a number of major research programs related to electric and magnetic fields produced by power lines, which were the subject of considerable publicity in 1987. Research has not proven that electric or magnetic fields cause any adverse health effects.

System projects save money

TU Electric continues to be a leader in innovative uses of technology. In 1987, employees received three First Use Awards from the Electric Power Research Institute for their involvement in:

- Developing on-line monitors for use on large economical base-load generating units. The monitors ensure early detection of potential problems before they cause lengthy outages that would make it necessary to operate less-efficient units.
- Solving chemical process problems in flue gas desulfurization systems, an achievement that has reduced scrubber system operating costs by 20% and saved customers millions of dollars annually.
- Eliminating boiler feed pump vibration and hydraulic instability, thereby improving the reliability of major generating units.

Low-cost lignite fuel

Power plant chemical technician

Load management customer contact

Financial Report

Contents

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

Liquidity and Capital Resources

The primary capital requirements for 1987 and as estimated for 1988 through 1990 are as follows:

	1987	1988	1989	1990
		Thousands of Dollars		
Construction expenditures (excluding AFUDC)	**$1,302,000**	$1,150,000	$ 937,000	$ 850,000
Nuclear fuel and non-utility property	**29,000**	70,000	63,000	74,000
Maturities of long-term debt and sinking fund requirements (includes early redemptions in 1987 of $133,000,000)	**188,000**	55,000	52,000	135,000
Installment/principal payments to TMPA (see Notes 10 and 11 to Financial Statements)	—	125,000	58,000	64,000
Total	**$1,519,000**	$1,400,000	$1,110,000	$1,123,000

For detail concerning major construction work now in progress or contemplated by the System Companies and commitments with respect thereto, see Resource Planning and Comanche Peak.

The System Companies generate funds from operations sufficient to meet operating needs, pay dividends on capital stock and finance a portion of capital requirements. These funds are derived from consolidated net income, depreciation, deferred taxes and investment tax credits. Factors affecting the ability of TU Electric to continue to fund a portion of its capital requirements from operations include adequate rate relief and regulatory practices allowing a substantial portion of construction work in progress (CWIP) in rate base, adequate depreciation rates, normalization of federal income taxes, recovery of the cost of fuel and purchased power and the opportunity to earn competitive rates of return required in the capital markets. For 1987, approximately 18% of the funds needed for construction was generated from operations.

External funds of a permanent or long-term nature are obtained through the sale of common stock by the Company, and the sales of preferred stock and long-term debt by the System Companies. The capitalization ratios of the Company and its subsidiaries at December 31, 1987 consisted of approximately 45% long-term debt, 10% preferred stock and 45% common stock equity. Similar ratios are expected to be maintained in the future. For information regarding bank lines of credit and short-term borrowings of the Company, see Note 2 to Financial Statements.

Financings in 1987 by TU Electric and the Company included the following:

Long-Term Debt (TU Electric):

Month	Principal Amount	Description
February	$ 250,000,000	9¼% First Mortgage and Collateral Trust Bonds due 2017
March	100,000,000	7⅞% Collateralized Pollution Control Revenue Bonds due 2017
April	250,000,000	10½% First Mortgage and Collateral Trust Bonds due 2017
July	150,000,000	9½% First Mortgage and Collateral Trust Bonds due 1997
July	150,000,000	10½% First Mortgage and Collateral Trust Bonds due 2017
September	67,000,000	9% Collateralized Pollution Control Revenue Bonds due 2007
October	112,000,000	9⅞% Collateralized Pollution Control Revenue Bonds due 2017
Total	$1,079,000,000	

Preferred Stock (TU Electric):

Month	Shares	Net Proceeds	Description
July	1,000,000	$98,215,000	Stated Rate Auction Preferred Stock, Series A

Common Stock (the Company):

Month	Shares	Net Proceeds	Description
March	5,000,000	$170,452,000	Common Stock sale to the public

Early redemptions of long-term debt by TU Electric in 1987 included the following:

Month	Principal Amount	Redemption Cost	Description
April	$ 32,531,000	$ 36,523,000	16% First Mortgage Bonds due 2012
June	50,000,000	56,085,000	15⅞% First Mortgage Bonds due 2012
July	50,000,000	56,335,000	16% First Mortgage Bonds due 2012
Total	$132,531,000	$148,943,000	

Management's Discussion and Analysis of Financial Condition and Results of Operations (concluded)

Additional early redemptions may occur from time to time in amounts presently undetermined. The Company anticipates the sale to the public of 5,000,000 shares of its authorized but unissued common stock in April 1988 and the issuance in April 1988 by the Brazos River Authority of $100,000,000 principal amount of pollution control revenue bonds to be collateralized by the issuance of an equal principal amount of TU Electric's first mortgage and collateral trust bonds. The System Companies expect to sell securities as needed, including the possible future sale by TU Electric of up to $300,000,000 principal amount of first mortgage and collateral trust bonds and up to 1,000,000 shares of cumulative preferred stock, both currently registered with the Securities and Exchange Commission for offering pursuant to Rule 415 under the Securities Act of 1933, sales of additional shares of common stock of the Company pursuant to various plans described in Note 3 to Financial Statements and sales of additional securities from time to time, in amounts and of types presently undetermined.

The Tax Reform Act of 1986 (TRA), among other things, repealed the investment tax credit, lengthened depreciation lives, created an alternative minimum tax and lowered the corporate tax rate subject to certain transition rules. Other tax accounting changes were required including the capitalization of items previously expensed and a change in the timing of income recognition for certain items. Substantially all of the tax changes, with the exception of the rate reduction, will result in the Company paying more taxes currently, will eliminate sources of internally generated funds for the Company and thereby increase financing requirements in the future. The TRA did not have a material effect on the Company for the years ended December 31, 1987 and 1986.

Although TU Electric cannot predict future regulatory practices, the extent of any further delays in the licensing of the Comanche Peak Nuclear Generating Station (Comanche Peak) or any changes in economic and securities market conditions, no changes are expected in trends or commitments which might significantly alter its basic financial position or ability to finance capital requirements. However, TU Electric has indicated that it does not currently plan to implement increased electric service rates which reflect any additional Comanche Peak costs until Unit 1 is ready for commercial operation and TU Electric continues to believe, based upon revised cost estimates and using acceptable rate making approaches and assumptions, that the rate increase, when Unit 1 goes into service, can be held to about 10%. Therefore, prior to the completion of Comanche Peak and its inclusion in rate base, a relatively small percentage of capital requirements may be generated internally. (See Notes 10 and 11 to Financial Statements.)

See Financial Statistics for additional information.

Results of Operations

Operating revenues increased $150,878,000 in 1987 and decreased $238,112,000 in 1986. The following table details the factors contributing to the increase and decrease:

Factors	Increase (Decrease) 1987	1986
	Thousands of Dollars	
Fuel revenue	**$ 73,589**	$(316,545)
Power cost recovery factor revenue	**32,485**	25,668
Increased energy sales	**51,954**	61,492
Other	**(7,150)**	(8,727)
Total	**$150,878**	$(238,112)

The increase in operating revenues for 1987 was the result of increased fuel and purchased power revenue and increased energy sales. Energy sales for 1987 increased 3.3% and were attributable to increased customers and customer usage. Operating revenues decreased in 1986 as the result of decreased fuel revenue partially offset by increases in purchased power revenue and energy sales. See Operating Statistics.

Fuel and purchased power expense increased $106,397,000 in 1987 and decreased $309,671,000 in 1986. The increase for 1987 was due primarily to increased off-system purchases partially offset by lower fuel costs. Lower fuel expense for 1987 reflects the decrease in the unit cost of gas from $2.77 per million Btu in 1986 to $2.56 in 1987. The decrease in 1986 was due primarily to the decrease in the unit cost of gas offset in part by increased purchased power. See Operating Statistics.

Operation expense increased $66,115,000 and $38,901,000 for 1987 and 1986, respectively. Operation expense for 1987 was affected by increases in the cost of labor, liability and property insurance and the one-time cost of the special early retirement program. Increases in wheeling costs and liability and property insurance had a significant impact on operation expense for 1986.

Maintenance expense decreased $18,619,000 for 1987 and increased $19,540,000 for 1986. The decrease for 1987 was due primarily to revisions in the scope of certain scheduled overhauls. The increase in maintenance for 1986 was the result of increases in power production expenses associated with lignite and gas plants and programs to improve and ensure the availability of all generating units. Increased distribution maintenance also added to the increase for 1986.

Taxes other than income increased $13,755,000 and $4,117,000 for 1987 and 1986, respectively. The increases for 1987 and 1986 resulted primarily from increases in franchise and property based taxes.

Allowance for funds used during construction (AFUDC) increased as a result of the ongoing construction program and the resultant increase in the level of CWIP of TU Electric not included in rate base partially offset, in 1987, by the reduction in the AFUDC rates and the suspension of AFUDC on the Twin Oak and Forest Grove generating stations.

Other income and deductions - net increased $9,359,000 and $11,585,000 for 1987 and 1986, respectively. The increase for 1987 was due primarily to increased interest on temporary cash investments. The increase for 1986 was the result of a gain on the sale of certain properties.

Interest on first mortgage bonds increased in 1987 and 1986 due to the sale of new issues during the years and annualized interest of issues sold in the prior years, partially offset by retirements and redemptions of certain higher interest rate issues.

Other interest charges decreased $16,347,000 for 1987 and increased $9,570,000 for 1986. The decrease for 1987 reflects decreased interest cost on over-recovered fuel revenue and short-term borrowings. The increase for 1986 reflects increased interest cost on over-recovered fuel revenue offset in part by decreased interest on short-term borrowings.

Preferred stock dividends increased for 1987 and 1986, $10,663,000 and $12,099,000, respectively, due to new issues sold during these periods and the full year's effect of prior period issuances, offset in part in 1986 by lower dividend rates on the adjustable rate series.

Consolidated net income increased $53,125,000 in 1987 and $39,093,000 in 1986 which represents a culmination of the factors described above. Included in consolidated net income were increases in AFUDC of $83,297,000 in 1987 and $74,114,000 in 1986 which represent non-cash earnings to the Company.

Estimated Effect of Pending Accounting Change

In December 1987, the Financial Accounting Standards Board issued Statement of Financial Accounting Standards No. 96 entitled "Accounting for Income Taxes" which becomes effective for fiscal years beginning after December 15, 1988. The Statement, among other things, requires 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 the Statement 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. Although the application of the Statement will increase both total assets and liabilities, these requirements are not expected to have a material effect on the Company's financial position or results of operations.

Suspension of Capitalization of AFUDC

In September 1987, TU Electric announced the suspension of construction on the Twin Oak and Forest Grove generating stations. Therefore, capitalization of AFUDC was suspended in October 1987 until active construction resumes. Expenditures not included in rate base as of December 31, 1987, applicable to these stations, totaled approximately $468,000,000.

In March 1988, TU Electric announced the temporary suspension of construction on Unit 2 of Comanche Peak for an anticipated period of one year. Therefore, beginning in April 1988, capitalization of AFUDC will be suspended until active construction resumes. Expenditures not included in rate base as of December 31, 1987, applicable to this unit, totaled approximately $1,513,000,000.

The above suspensions of AFUDC reduced consolidated net income by approximately $10,000,000 in 1987 and are expected to reduce consolidated net income in 1988 by approximately $160,000,000 from the level it would otherwise have been.

Statement of Consolidated Income
Year Ended December 31,

	1987	1986	1985
	Thousands of Dollars		
OPERATING REVENUES	$4,082,923	$3,932,045	$4,170,157
OPERATING EXPENSES			
Fuel and purchased power	1,585,610	1,479,213	1,788,884
Operation	624,053	557,938	519,037
Maintenance	300,451	319,070	299,530
Depreciation	234,139	220,381	207,592
Federal income taxes (Note 7)	194,460	264,311	276,711
Taxes other than income	295,327	281,572	277,455
Total operating expenses	3,234,040	3,122,485	3,369,209
OPERATING INCOME	848,883	809,560	800,948
OTHER INCOME			
Allowance for equity funds used during construction	283,061	231,880	173,846
Other income and deductions—net	14,371	5,012	(6,573)
Federal income taxes (Note 7)	(232)	3,034	2,165
Total other income	297,200	239,926	169,438
TOTAL INCOME	1,146,083	1,049,486	970,386
INTEREST CHARGES			
Interest on mortgage bonds	402,389	317,978	285,693
Interest on other long-term debt	67,934	71,073	68,940
Other interest	10,808	27,155	17,585
Allowance for borrowed funds used during construction	(104,062)	(71,946)	(55,866)
Total interest charges	377,069	344,260	316,352
PREFERRED STOCK DIVIDENDS OF SUBSIDIARY	89,038	78,375	66,276
CONSOLIDATED NET INCOME	$ 679,976	$ 626,851	$ 587,758
Average shares of common stock outstanding (thousands)	149,449	140,982	135,267
Earnings and dividends per share of common stock:			
Earnings (on average shares outstanding)	$4.55	$4.45	$4.35
Dividends declared	2.80	2.68	2.52

Statement of Consolidated Retained Earnings
Year Ended December 31,

	1987	1986	1985
	Thousands of Dollars		
BALANCE AT BEGINNING OF YEAR	$2,180,293	$1,931,307	$1,686,913
ADD—Consolidated net income	679,976	626,851	587,758
Total	2,860,269	2,558,158	2,274,671
DEDUCT—Dividends declared on common stock (for amounts per share, see Statement of Consolidated Income)	421,418	377,865	343,364
BALANCE AT END OF YEAR (Note 4)	$2,438,851	$2,180,293	$1,931,307

See accompanying Notes to Financial Statements.

Statement of Consolidated Source of Funds for Construction

Year Ended December 31,

	1987	1986	1985
		Thousands of Dollars	
FUNDS FROM OPERATIONS			
Consolidated net income	$ 679,976	$ 626,851	$ 587,758
Depreciation (including amounts charged to fuel)	260,808	248,329	231,711
Deferred federal income taxes—net	48,912	140,479	124,325
Federal investment tax credits—net	56,012	66,302	77,285
Allowance for funds used during construction	(387,123)	(303,826)	(229,712)
Total funds from operations	658,585	778,135	791,367
Less—Dividends declared on common stock	421,418	377,865	343,364
Net funds from operations	237,167	400,270	448,003
FUNDS FROM FINANCING			
Sales of securities:			
First mortgage bonds	1,058,852	970,000	475,000
Other long-term debt	—	—	75,000
Preferred stock	98,697	197,728	83,513
Common stock	312,952	145,171	249,167
Retirement of long-term securities (Note 6)	(188,324)	(305,792)	(258,156)
Increase (decrease) in notes payable—commercial paper	(11,300)	11,300	(59,700)
Net funds from financing	1,270,877	1,018,407	564,824
OTHER SOURCES (USES) OF FUNDS			
Changes in working capital, excluding notes payable, long-term debt due currently and over-recovered fuel revenue:			
Cash in banks and temporary cash investments	(88,936)	(129,345)	(39,613)
Accounts receivable—net	(122,238)	10,944	(37,484)
Inventories	12,976	9,397	9,795
Accounts payable	41,703	43,034	18,777
Taxes accrued	(35,710)	(41,209)	(18,420)
Other—net	86,510	(25,049)	5,408
Net change	(105,695)	(132,228)	(61,537)
Non-utility property—net	(28,232)	(20,880)	(19,925)
Nuclear fuel	(797)	2,760	(54,803)
Over/under-recovered fuel revenue—net of deferred income taxes	(60,834)	(12,309)	52,301
Unamortized loss on reacquired debt—net (Note 6)	(15,548)	(23,398)	(32,021)
Other—net	4,770	(16,829)	(17,693)
Net other sources (uses) of funds	(206,336)	(202,884)	(133,678)
Total	$1,301,708	$1,215,793	$ 879,149
CONSTRUCTION EXPENDITURES			
Utility plant	$1,688,831	$1,519,619	$1,108,861
Allowance for funds used during construction	(387,123)	(303,826)	(229,712)
CONSTRUCTION EXPENDITURES (excluding allowance for funds used during construction)	$1,301,708	$1,215,793	$ 879,149

See accompanying Notes to Financial Statements.

Consolidated Balance Sheet

December 31,

	1987	1986
	Thousands of Dollars	
ASSETS		
UTILITY PLANT		
In service:		
Production	$ 3,968,345	$ 3,902,898
Transmission	1,214,642	1,166,066
Distribution	2,696,523	2,543,163
General	377,590	343,347
Total	8,257,100	7,955,474
Construction work in progress (Notes 10 and 11)	6,642,707	5,351,565
Nuclear fuel	252,761	251,964
Held for future use	20,426	7,130
Total utility plant	15,172,994	13,566,133
Less accumulated depreciation	2,718,328	2,522,016
Utility plant, less accumulated depreciation	12,454,666	11,044,117
INVESTMENTS		
Non-utility property (Note 11)	234,847	206,615
Other investments (Note 1)	22,107	15,113
Total investments	256,954	221,728
CURRENT ASSETS		
Cash in banks (Note 2)	7,230	6,494
Temporary cash investments—at cost	272,400	184,200
Special deposits	38,114	35,299
Accounts receivable:		
Customers	250,684	212,153
Minority owners of Comanche Peak (Note 10)	109,284	58,826
Other	66,522	33,847
Allowance for uncollectible accounts	(13,243)	(13,817)
Inventories—at average cost:		
Materials and supplies	130,941	126,865
Fuel stock	160,613	177,665
Deferred federal income taxes (over-recovered fuel revenue)	—	29,253
Other current assets	47,867	76,586
Total current assets	1,070,412	927,371
DEFERRED DEBITS		
Under-recovered fuel revenue	44,119	—
Unamortized loss on reacquired debt (Note 6)	70,967	55,419
Cancelled lignite unit costs (Note 11)	37,246	36,810
Other deferred debits	51,896	32,747
Total deferred debits	204,228	124,976
Total	$13,986,260	$12,318,192

See accompanying Notes to Financial Statements.

	1987	1986
	Thousands of Dollars	
CAPITALIZATION AND LIABILITIES		
CAPITALIZATION		
Common stock, without par value (Note 3):		
Authorized shares—200,000,000		
Outstanding shares—1987, 152,408,942; 1986, 142,805,206	**$ 2,593,480**	$ 2,280,528
Retained earnings (Note 4)	**2,438,851**	2,180,293
Total common stock equity	**5,032,331**	4,460,821
Preferred stock (Note 5):		
Not subject to mandatory redemption	**909,633**	811,418
Subject to mandatory redemption	**232,906**	232,424
Long-term debt, less amounts due currently (Note 6)	**5,141,491**	4,283,791
Total capitalization	**11,316,361**	9,788,454
CURRENT LIABILITIES		
Notes payable—commercial paper (Note 2)	**—**	11,300
Long-term debt due currently	**54,980**	54,480
Total (to be refinanced)	**54,980**	65,780
Accounts payable	**347,478**	305,775
Dividends declared	**130,365**	116,821
Customers' deposits	**51,259**	44,877
Taxes accrued	**106,587**	142,297
Interest accrued	**139,222**	107,707
Over-recovered fuel revenue	**—**	63,594
Other current liabilities	**33,021**	23,856
Total current liabilities	**862,912**	870,707
DEFERRED CREDITS AND OTHER NONCURRENT LIABILITIES		
Accumulated deferred federal income taxes	**998,476**	931,938
Unamortized federal investment tax credits	**768,203**	712,193
Other deferred credits and noncurrent liabilities	**40,308**	14,900
Total deferred credits and other noncurrent liabilities	**1,806,987**	1,659,031
COMMITMENTS AND CONTINGENCIES (Notes 10 and 11)		
Total	**$13,986,260**	$12,318,192

See accompanying Notes to Financial Statements.

Notes to Financial Statements

1. Significant Accounting Policies

Consolidation—The consolidated financial statements include Texas Utilities Company (Company) and all of its subsidiaries; all significant intercompany items and transactions have been eliminated in consolidation.

Utility Plant—Utility plant is stated at original cost. The cost of property additions charged to utility plant includes labor and materials, applicable overhead and payroll-related costs and an allowance for funds used during construction.

Allowance For Funds Used During Construction—Allowance for funds used during construction (AFUDC) is a cost accounting procedure whereby amounts based upon interest charges on borrowed funds and a return on equity capital used to finance construction are charged to utility plant. The accrual of AFUDC is in accord with generally accepted accounting principles for the industry, but does not represent current cash income.

Texas Utilities Electric Company (TU Electric) is capitalizing AFUDC, compounded semi-annually, on expenditures for ongoing construction work in progress (CWIP) not otherwise allowed in rate base by regulatory authorities. In 1985 and 1986, AFUDC was capitalized using a net-of-tax rate of 9½%. In 1987, pursuant to the passage of the Tax Reform Act of 1986 (TRA), TU Electric began using a comparable gross capitalization rate on projects commenced after March 1, 1986. Beginning July 1, 1987, a net-of-tax rate of 9% and a gross rate of 10½% have been used. All such rates were determined on the basis of, but are less than, the cost of capital used to finance the construction program.

Depreciation—Depreciation is based upon an amortization of the original cost of depreciable properties on a straight-line basis over the estimated service lives of the properties. Depreciation as a percent of average depreciable property approximated 3.4% for 1987, 1986 and 1985.

Other Investments—The difference between the amount at which the investment in a subsidiary is carried by the Company and the underlying book equity of such subsidiary at the respective dates of acquisition of $14,439,000 is included in other investments.

Revenues—Revenues include billings under approved rates (including a fixed fuel factor) applied to meter readings each month on a cycle basis and an amount for under or over recovery of fuel revenue representing the difference between actual fuel cost and billings on the approved fixed fuel factor. Pursuant to a rule adopted in July 1986 by the Public Utility Commission of Texas (PUC), TU Electric is required to refund over-recovered fuel revenue if the amount of over-recovery, including interest, exceeds the lesser of $40 million or 4% of its annual known or reasonably predictable fuel costs most recently approved by the PUC. Reconciliation of fuel costs is to be made in a general rate case or a reconciliation proceeding. Reconciliation may be requested only if it has either been over one year since the utility's last final reconciliation or the utility has materially under-recovered its known or reasonably predictable fuel costs.

Federal Income Taxes—The Company and its subsidiary companies file a consolidated federal income tax return, and federal income taxes are allocated to all subsidiary companies based upon taxable income or loss. Deferred federal income taxes are currently provided for timing differences between book and taxable income; such differences result primarily from the use of liberalized depreciation and cost recovery deductions allowable under the Internal Revenue Code, the under or over recovery of fuel revenue and unbilled revenues on a cycle basis. Cumulative timing differences in earlier years for which deferred federal income taxes were not provided approximated $237,000,000 at December 31, 1987. Investment tax credits are being amortized to income over the estimated service lives of the properties.

In December 1987, the Financial Accounting Standards Board issued Statement of Financial Accounting Standards No. 96 entitled "Accounting for Income Taxes" which becomes effective for fiscal years beginning after December 15, 1988. The Statement, among other things, requires 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 the Statement 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. Although the application of the Statement will increase both total assets and liabilities, these requirements are not expected to have a material effect on the Company's financial position or results of operations.

2. Bank Balances and Short-Term Borrowings

At December 31, 1987, the Company had lines of credit aggregating $1,025,000,000 under an eight-year credit facility agreement with a group of commercial banks. The facility, for which the Company pays a fee, will be reduced in 1993, 1994 and 1995 by $325,000,000, $350,000,000 and $350,000,000, respectively. This credit facility may be used to finance new construction, as backup for commercial paper and for general corporate purposes. The total amount of borrowings authorized by the Board of Directors of the Company from banks or other lenders at December 31, 1987 was $1,075,000,000.

3. Common Stock

The Company issued and sold shares of its authorized but unissued common stock during the years 1987, 1986 and 1985 as follows:

	Public Offering		Automatic Dividend Reinvestment and Common Stock Purchase Plan		Employees' Thrift Plan and Employee Stock Ownership Plan		Total	
Year	Shares	Amount	Shares	Amount	Shares	Amount	Shares	Amount
1987	5,000,000	$170,452,000	3,633,187	$111,184,000	970,549	$31,316,000	9,603,736	$312,952,000
1986	—	—	3,826,687	115,148,000	935,357	30,023,000	4,762,044	145,171,000
1985	5,000,000	130,650,000	3,431,846	90,199,000	1,025,647	28,318,000	9,457,493	249,167,000

At December 31, 1987, 6,315,927 shares of the authorized but unissued common stock of the Company were reserved for issuance and sale pursuant to the above plans.

The Company has 50,000,000 authorized shares of serial preference stock having a par value of $25 a share, none of which has been issued.

4. Retained Earnings

The articles of incorporation, the mortgages, as supplemented, and the debenture agreements of TU Electric contain provisions which, under certain conditions, restrict distributions on or acquisitions of its common stock. At December 31, 1987, $138,736,000 of retained earnings of TU Electric were thus restricted as a result of the provisions of such articles of incorporation. Retained earnings at such date also included $431,243,000, representing the Company's equity in undistributed earnings since acquisition included in transfers by TU Electric from its retained earnings to stated value of common stock, making a total of retained earnings which was restricted of $569,979,000 at December 31, 1987.

5. Preferred Stock of TU Electric (cumulative, without par value, entitled upon liquidation to $100 a share)

Series Groups From	Series Groups To	Shares Outstanding December 31, 1987	Shares Outstanding December 31, 1986	Amount December 31, 1987	Amount December 31, 1986	Redemption Price Per Share (before adding accumulated dividends) Current From	Current To	Eventual Minimum From	Eventual Minimum To
				Thousands of Dollars					
Not Subject to Mandatory Redemption									
$ 4.00	$ 4.84	**1,142,942**	1,142,942	**$114,588**	$114,588	**$101.79**	**$112.00**	$101.79	$112.00
5.08	7.80	**1,629,675**	1,629,675	**163,270**	163,270	**102.40**	**104.82**	102.40	103.60
8.16	8.92	**1,999,475**	1,999,475	**198,642**	198,642	**103.60**	**106.13**	101.00	103.60
9.32	11.32	**1,550,000**	1,550,000	**153,205**	153,205	**104.66**	**111.32***	100.00	102.73
Adjustable rate (a)		**1,850,000**	1,850,000	**181,713**	181,713	—	—	100.00	100.00
Stated rate auction (b)		**1,000,000**	—	**98,215**	—	—	—	100.00	100.00
Total		**9,172,092**	8,172,092	**$909,633**	$811,418				
Subject to Mandatory Redemption (c)									
$ 8.92	$ 9.48	**1,500,000**	1,500,000	**$148,610**	$148,315	**$108.92***	**$109.48***	$100.00	$100.00
10.00	10.08	**850,000**	850,000	**84,296**	84,109	**110.00***	**110.08***	100.00	100.00
Total		**2,350,000**	2,350,000	**$232,906**	$232,424				

*Redemption may not be effected currently through certain refunding operations.

(a) Adjustable rate series A bears a dividend rate for the period ended January 31, 1988 of 7.55% per annum and adjustable rate series B bears a dividend rate for the period ended December 31, 1987 of 9.00% per annum, both of which are based on a fixed liquidation price of $100.00 per share. The series are not redeemable prior to June 1, 1989 and June 1, 1990, respectively.

(b) Stated rate auction series A bears a dividend rate of 8.24% per annum for the fixed dividend period through September 30, 1992 and shares are not redeemable prior to September 29, 1992. The dividend rate for each 49 day dividend period thereafter will be determined on the basis of certain auction procedures. The maximum rate determined by the auction may range from 110% to 200% of the 60-day "AA" composite commercial paper rate index. All redemptions are at a price of $100.00 per share plus accumulated dividends.

(c) TU Electric is required to redeem a specified minimum number of shares annually commencing on the initial dates shown below, except for the $8.92 series which does not have a sinking fund provision. TU Electric may annually redeem, at its option, an aggregate of up to twice the number of shares shown for each series. All such redemptions are at a price of $100.00 per share plus accumulated dividends.

Series	Minimum Redeemable Shares	Initial Date of Mandatory Redemption
$10.08	14,000 annually	4/1/89
9.48	66,700 annually	4/1/92
10.00	20,000 annually	7/1/92
8.92	All outstanding shares	7/1/96

The carrying value of preferred stock subject to mandatory redemption is being increased periodically to equal the redemption amounts at the mandatory redemption dates with a corresponding increase in preferred stock dividends.

TU Electric issued and sold shares of its authorized preferred stock as follows: July 1987, 1,000,000 shares of stated rate auction series A for $98,215,000; July 1986, 500,000 shares of $10.00 series cumulative preferred stock, subject to mandatory redemption, for $49,413,000; July 1986, 500,000 shares of $8.92 series cumulative preferred stock, subject to mandatory redemption, for $49,437,000; February 1986, 1,000,000 shares of $9.48 series cumulative preferred stock, subject to mandatory redemption, for $98,878,000; and June 1985, 850,000 shares of adjustable rate series B preferred stock for $83,513,000.

6. Long-Term Debt of Subsidiaries, less amounts due currently

Maturity Groups From	Maturity Groups To	Interest Rate Groups From	Interest Rate Groups To	December 31, 1987	December 31, 1986
				Thousands of Dollars	
First mortgage bonds:					
1988	1992	4½%	4½%	$ 12,000	$ 34,500
1993	1997	4¼	9½	356,000	206,000
1998	2002	6⅝	9⅜	340,000	340,000
2003	2007	7½	10⅛	750,000	750,000
2008	2012	9⅜	16	250,000	382,531
2013	2017	9¼	13⅝	2,200,000	1,550,000
Pollution control series:					
2007	2017	7¾	10	589,000	310,000
Funds on deposit with trustee				(20,148)	—
Sinking fund debentures:					
1989	1989	4½	4½	17,854	18,454
1993	1994	6⅝	7¾	31,735	32,448
Total				4,526,441	3,623,933
Pollution control revenue bonds:					
2004	2009	5.70	7⅝	160,000	160,000
Senior notes:					
1990	1999	8.50	12.20	502,380	534,860
Unamortized premium and discount				(47,330)	(35,002)
Total long-term debt, less amounts due currently				$5,141,491	$4,283,791

Sinking fund and maturity requirements for the years 1988 through 1992 under long-term debt instruments in effect at December 31, 1987, were as follows:

Year	Sinking Fund (a)	Maturity	Minimum Cash Requirement (b)
		Thousands of Dollars	
1988	$49,850	$ 22,500	$ 54,980
1989	50,932	17,854	50,916
1990	50,956	100,000	133,180
1991	50,776	12,000	45,180
1992	51,846	—	34,250

(a) Excluding requirements satisfied prior to December 31, 1987: $2,433,000 for 1988, $438,000 for 1989, $320,000 for 1990, $320,000 for 1991 and $320,000 for 1992.

(b) Other requirements may be satisfied by certification of property additions at the rate of 167% of such requirements, except for eighteen issues at 100%.

In 1987 and prior years, various principal amounts of first mortgage bonds were redeemed by TU Electric prior to maturity. Pursuant to expected regulatory treatment, the net losses on reacquired debt have been deferred and are being amortized over the remaining lives of the bonds retired.

Utility plant of TU Electric is generally subject to the liens of its mortgages.

7. Federal Income Taxes

The details of federal income taxes are as follows:

	Year Ended December 31,		
	1987	1986	1985
	Thousands of Dollars		
Charged to operating expenses:			
Current	$ 54,909	$ 55,545	$127,114
Deferred—net:			
Differences between depreciation methods and lives	64,115	79,148	85,950
Certain capitalized construction costs	(2,010)	19,320	19,390
Over/under-recovered fuel revenue	46,856	11,935	(44,553)
Cancelled lignite unit	(971)	12,293	—
Early redemptions of long-term debt	6,091	10,763	14,730
Prepaid (accrued) pension cost	(12,443)	6,181	—
Unbilled revenues	(17,367)	(322)	932
Other	(732)	3,146	(4,137)
Total	83,539	142,464	72,312
Investment tax credits—net	56,012	66,302	77,285
Total to operating expenses	194,460	264,311	276,711
Charged (credited) to other income:			
Current	(12,020)	(11,535)	(9,625)
Deferred—net	12,252	8,501	7,460
Total to other income	232	(3,034)	(2,165)
Total federal income taxes	$194,692	$261,277	$274,546

Federal income taxes were less than the amount computed by applying the federal statutory rate to pre-tax book income as follows:

	Year Ended December 31,		
	1987	1986	1985
	Thousands of Dollars		
Federal income taxes at statutory rate (39.95% for 1987 and 46% for 1986 and 1985)	$385,001	$444,591	$427,147
Reductions in federal income taxes resulting from:			
Allowance for funds used during construction	152,816	139,760	105,668
Depletion allowance	26,437	24,006	25,442
Amortization of investment tax credits	16,126	14,982	13,781
Other	(5,070)	4,566	7,710
Total reductions	190,309	183,314	152,601
Total federal income taxes	$194,692	$261,277	$274,546
Effective tax rate	20.2%	27.0%	29.6%

8. Retirement Plans and Other Postretirement Benefits

The System Companies have uniform retirement plans covering substantially all employees. The benefits are based on years of accredited service and the employee's average annual earnings received during the three years of highest earnings. The costs of the plans are determined by independent actuaries. Contributions to the plans were determined using the frozen attained age method which is one of the several actuarial methods allowed by the Employee Retirement Income Security Act of 1974. During 1986, the System Companies adopted the Financial Accounting Standards Board's Statement of Financial Accounting Standards No. 87, "Employers' Accounting for Pensions." The new standard requires, among other things, the use of the projected unit credit actuarial method for determining pension cost for financial reporting purposes. The cumulative difference between pension cost as determined under the new standard and contributions to the plans is recorded either as prepaid pension cost or as accrued pension liability. The adoption of the new accounting standard did not have a material effect upon the Company's financial position or results of operations.

In 1987, the Company offered a special early retirement program to those employees who had attained the age of 55 and had 15 or more years of accredited service. The offer provided for a waiver of reduced benefits for early retirement plus 5 additional years of accredited service up to a maximum of 40 years. The cost of the program was recorded in accordance with Financial Accounting Standards Board's Statement of Financial Accounting Standards No. 88, "Employers' Accounting for Settlements and Curtailments of Defined Benefits Pension Plans and for Termination Benefits."

The following table sets forth the plans' funded status and amount recognized in the Company's consolidated balance sheet:

	December 31,	
	1987	1986
	Thousands of Dollars	
Actuarial present value of accumulated benefits:		
Accumulated benefit obligation, including vested benefits ($500,019,000 for 1987 and $387,775,000 for 1986)	$(566,238)	$(446,129)
Projected benefit obligation for service rendered to date	$(738,359)	$(654,102)
Plan assets at fair value, primarily equity investments, government bonds and corporate bonds	732,713	729,003
Plan assets in excess of (less than) projected benefit obligation	(5,646)	74,901
Unrecognized net gain from past experience different from that assumed and effects of changes in assumptions	(2,801)	(51,631)
P r service cost not yet recognized in net eriodic pension expense	16,149	17,042
Unrecognized plan assets in excess of projected benefit obligation at January 1, 1986	(19,738)	(22,584)
Prepaid pension cost (accrued pension liability)	$ (12,036)	$ 17,728

Assumptions used for 1987 and 1986 include a discount rate of 8.0%, an expected long-term rate of return on assets of 8.0% and increases in compensation levels of 5.3% and 6.3%, respectively. Total pension costs for 1987 and 1986, including amounts charged to fuel cost and capitalized, were comprised of the following components:

	December 31,	
	1987	1986
	Thousands of Dollars	
Service cost - benefits earned during the period	$ 30,120	$ 32,752
Interest cost on projected benefit obligation	54,515	46,295
Actual return on plan assets	(347)	(100,288)
Net amortization and deferral	(58,664)	51,303
Net periodic pension cost	25,624	30,062
Termination cost	38,650	—
Total pension cost	$ 64,274	$ 30,062

The cost of the plan for 1985, including amounts charged to fuel cost and capitalized, approximated $48,283,000.

In addition to retirement plans, the System Companies offer certain health care and life insurance benefits to active and retired employees. The costs of such benefits are generally recognized as claims are paid. The costs of providing such benefits to retired employees, net of employee contributions, approximated $8,367,000 for 1987, $6,759,000 for 1986 and $4,831,000 for 1985.

9. Leases

The System Companies have entered into operating leases covering various facilities and properties including such items as data processing, transportation and mining equipment and office space. Lease costs charged to operation expense for the years ended December 31, 1987, 1986 and 1985 were $46,732,000, $40,466,000 and $35,012,000, respectively.

In December 1987, TU Electric entered into an operating lease arrangement covering certain combustion turbine generating facilities with an initial lease term of approximately 27 years. TU Electric expects to lease additional similar facilities in 1988.

The Company's future minimum lease commitments under such operating leases that have initial or remaining noncancelable lease terms in excess of one year as of December 31, 1987 were as follows:

Year	Combustion Turbines	Other	Total
		Thousands of Dollars	
1988	$ —	$ 40,863	$ 40,863
1989	6,082	30,381	36,463
1990	6,082	16,856	22,938
1991	6,082	10,846	16,928
1992	6,082	8,362	14,444
Thereafter	158,130	17,385	175,515
Total minimum lease commitments	$182,458	$124,693	$307,151

10. Comanche Peak Nuclear Generating Station

TU Electric is constructing two nuclear-fueled generating units at the Comanche Peak Nuclear Generating Station (Comanche Peak), each of which is designed for a capability of 1,150 megawatts. This project is subject to the jurisdiction of the Nuclear Regulatory Commission (NRC). NRC regulations govern the granting of licenses for the construction and operation of nuclear power plants. After giving effect to the anticipated completion of the 1988 agreement to purchase the 6.2% ownership interest of Texas Municipal Power Agency (TMPA) in the facility, TU Electric's share of the net capability in each unit is 1,081 megawatts, or approximately 94%. The other participants in the facility are Brazos Electric Power Cooperative, Inc. (BEPC) and Tex-La Electric Cooperative of Texas, Inc. (Tex-La) which own 3.8% and 2⅙%, respectively.

Operating License Application

The NRC has been reviewing TU Electric's application for operating licenses for the Comanche Peak units. As a part of that review, a proceeding was initiated before an Atomic Safety and Licensing Board (ASLB) and proceedings on various issues have been ongoing since December 1981. After completion of such proceeding, the ASLB will make recommendations to the NRC regarding the issuance of operating licenses for the Comanche Peak units. An intervenor is actively involved in this ASLB proceeding.

The one remaining Contention before the ASLB in the operating license proceeding relates to TU Electric's quality assurance/quality control (QA/QC) program for the plant. In December 1983, the ASLB issued a memorandum questioning the QA program for design of certain portions of the plant and requested that TU Electric offer additional proof of adequate design and design review procedures. The ASLB is also reviewing several other related issues and has indicated its intent to review the results of the NRC's Technical Review Team (TRT) investigation discussed below. In July 1984, a separate ASLB, including two of the three members of the original ASLB, was convened to receive testimony on allegations that QC inspectors at the plant had been subjected to an atmosphere of harassment and intimidation which is alleged to have affected the implementation of TU Electric's QA program. In January 1986, this separate ASLB was disestablished with all issues thereafter to be resolved by the original ASLB.

As a separate part of the NRC's review of TU Electric's operating license application, in March 1984, the NRC established a task force to consolidate and carry out the various reviews necessary for the NRC Staff to reach its decision regarding the operating licenses. This effort involved the establishment of the TRT, which began an intensive onsite investigation in July 1984 and subsequently has issued reports requesting additional information from TU Electric with respect to several functional areas of the plant's construction program. TU Electric then formed a special team, the Comanche Peak Response Team (CPRT), which includes a number of independent experts in each area addressed by the TRT, and submitted a

Program Plan (Plan) to respond to the questions raised. Such Plan, which is described further below, is presently being implemented and has been expanded to address the design and other ASLB issues described herein.

In January 1985, the TRT issued a report on its review of the QA/QC programs at Comanche Peak. The report stated that although the QA program documentation met NRC requirements, the implementation of the QA program demonstrated that TU Electric had lacked the commitment to aggressively implement an effective QA/QC program in several areas. The TRT indicated that it had found evidence of faulty construction and ineffective QA and QC inspections. Questions were also raised concerning the training and qualification of QC personnel and in the reporting of deficiencies. The TRT further found that prior to July 1984 problems had existed in the control of documentation. In addition, deficiencies in several other areas were described. TU Electric was requested to submit to the NRC a program and schedule for completing a detailed and thorough assessment of these QA/QC issues presented by the TRT. TU Electric also was asked to consider the use of management personnel with a fresh perspective to evaluate the TRT findings and implement corrective action, and to consider the use of an independent consultant to oversee the corrective action program.

In June 1985, TU Electric filed with the NRC and the ASLB a revision to the Plan which is being utilized by the CPRT to address all outstanding design and construction concerns. This Plan, which was substantially revised and reissued in January 1986, and further revised in July 1987, provides for a complete design review of virtually all safety related systems in the plant, and for the development of a corrective action program as required. In August 1985, the ASLB issued a Memorandum which described areas of the Plan that concerned the ASLB. The Memorandum indicated, however, that if the Plan were revised to address the ASLB's concerns and if it were appropriately implemented, the Plan may demonstrate the quality of the plant. In May 1986, the Staff of the NRC issued a Supplemental Safety Evaluation Report (SSER) containing an evaluation of the Plan as it existed at that time. The SSER concluded that the Plan provided an overall structure and process for addressing and resolving all existing construction and design issues and any future issues that may be identified from further evaluations. In June 1986, the ASLB issued a Memorandum which addressed "Board Concerns" about the adequacy of the CPRT program. The Memorandum stated that, based upon the ASLB's current knowledge of the program, after having reviewed the first results reports and the SSER on the Plan, the ASLB continued to have the concerns expressed in the earlier memorandum described above. The ASLB also raised additional concerns about how findings in one area of the reinspection effort may affect TU Electric's program in other areas, whether sufficient attention is being paid to problems of quality assurance and quality control regarding design, the adequacy of the CPRT sampling program, and perceived oversights in one of the results reports that had been issued. TU Electric is addressing these concerns. In November 1987, the ASLB established a schedule for resolution of all issues remaining in the operating license proceeding. In January 1988, the Staff of the NRC, after further review and analysis, approved the Plan and corrective action program as the basis to resolve outstanding issues. At the end of February 1988, the CPRT completed the publication of its final reports. In March 1988, the Staff issued an SSER approving the design of piping and pipe supports at Comanche Peak, which had been a major issue in the operating license proceeding, and concluded that the Plan provides an effective means to ensure proper implementation of corrective action in this regard. Delivery of this report sets into motion a prehearing schedule adopted by the ASLB which should result in the resumption of hearings on issuance of the operating licenses in the late summer of 1988. Meanwhile, implementation of the corrective action program continues.

In December 1987, TU Electric entered into an agreement to settle potential claims against Gibbs & Hill, Inc. (Gibbs & Hill), the original architect-engineer for Comanche Peak, relating to engineering and design services performed by Gibbs & Hill for Comanche Peak. Under the terms of this settlement, the owners of Comanche Peak will receive a total of $25 million in cash, deferred payments and future engineering services which will be provided to TU Electric on non-nuclear projects.

TU Electric has made a number of key management changes in the nuclear program for Comanche Peak, including the addition of several new officers who bring substantial nuclear experience to TU Electric. This new management team is responsible for oversight and implementation of the reinspection and corrective action program.

The NRC has created an Office of Special Projects to manage all aspects of the NRC's licensing and inspection efforts for Comanche Peak and certain other nuclear power plants.

10. Comanche Peak Nuclear Generating Station (continued)

Construction Permit Extensions

In January 1986, TU Electric filed an application with the NRC for an extension of the construction permit for Unit 1 to reflect a new "latest date for completion" of August 1, 1988; previously such date had been August 1, 1985. In the application, TU Electric stated that the reason the request for extension of the construction permit was not filed at an earlier time was administrative oversight. In February 1986, the NRC issued an order extending the "latest date for completion" of Unit 1 to August 1, 1988. Subsequently, the intervenor involved in the ASLB operating license proceeding filed with the NRC a request to stay the effectiveness of the construction permit extension and to require TU Electric to file a new application for a construction permit for Unit 1 or to order that hearings be held prior to any decision on whether to grant the construction permit extension. The request for a stay was denied by the NRC and the question of whether to hold such hearings was remanded to an ASLB, the members of which are the same as the ASLB for the operating license. In November 1986, the ASLB issued a Memorandum and Order in which it accepted for litigation a new Contention, raised by two intervenors, which alleges that the delay in completing Comanche Peak, which has occurred and has necessitated the extension of the construction permit by the NRC, was the result of dilatory action on the part of TU Electric and that, therefore, good cause did not exist for the extension of such permit. No schedule for hearings on this Contention has been adopted by the ASLB at this time. TU Electric has also applied to the NRC for an extension of the construction permit for Unit 2. Such application is presently under review by the Staff of the NRC. In early March 1988, TU Electric filed with the ASLB a motion to consolidate proceedings in the operating license and construction permit proceedings.

Civil Penalties

In April and June 1986, TU Electric paid civil penalties to the NRC, each in the amount of $40,000, relating to allegations of harassment and intimidation at Comanche Peak. The June 1986 penalty was part of an aggregate of $120,000 in civil penalties previously proposed by the Staff of the NRC. TU Electric requested the Staff to revisit the other alleged violations to determine whether they did in fact occur and to consider mitigating the amount of the penalties, and in August 1987 the Staff decided not to assess the remaining $80,000 in proposed civil penalties. In August 1986, TU Electric paid a civil penalty of $200,000 previously proposed by the Staff of the NRC relating to the findings of the TRT, described above. In addition, TU Electric has paid another civil penalty of $50,000 relating to two alleged violations in TU Electric's reinspection and corrective action effort.

Investigation Regarding NRC Region IV

In December 1986, a portion of a report was released by the Office of Inspector and Auditor of the NRC (OIA Report) containing the results of its investigation of allegations of misconduct by the management of Region IV of the NRC with respect to Comanche Peak. The OIA Report expressed concern about allegations of harassment and intimidation by Region IV management to pressure Region IV inspectors to downgrade or delete proposed inspection findings at Comanche Peak. In addition, the OIA Report concluded that it would not be possible to rely on the Region IV QA inspection as evidence of the safe construction of Comanche Peak. Consequently, it stated that it will be necessary for the NRC to rely largely on recent detailed technical inspections conducted by the NRC, including the TRT, at Comanche Peak. The OIA Report also indicated that the data contained in an internal NRC report on inspection procedures was inaccurate and unreliable due to a lack of understanding by NRC inspectors of the proper method of completing a certain NRC form. NRC officials have indicated that a thorough assessment of the results of this investigation will be made; and in addition, certain personnel changes in the Region IV office have occurred. The OIA Report's findings are restricted to activities in Region IV and do not question other NRC regulatory activities with respect to Comanche Peak, including the detailed technical inspections conducted by the TRT as discussed above. The intervenor in the operating license proceedings, discussed above, has indicated its intent to file a motion raising the OIA Report's findings as issues to be the subject of hearings in such proceedings.

Litigation Relating to Comanche Peak

TU Electric, TMPA, BEPC and Tex-La have been the owners of $87\frac{5}{6}\%$, 6.2%, 3.8% and $2\frac{1}{6}\%$ interests, respectively, in Comanche Peak under the terms of a Joint Ownership Agreement (Agreement) which provides that TU Electric is the Project Manager for Comanche Peak. BEPC has failed to make numerous payments of its portion of the costs of Comanche Peak. BEPC has been experiencing difficulty in obtaining additional financing for Comanche Peak from the Rural Electrification Administration. In addition, since May 1986, Tex-La has failed to make payments to TU Electric for its portion of Comanche Peak and TMPA has made payments under protest. Accounts receivable at December 31, 1987 included \$109,284,000 of amounts due from BEPC and Tex-La. The portion of future construction expenditures due from BEPC and Tex-La is estimated to be \$48,200,000 in 1988, \$30,900,000 in 1989 and \$15,300,000 in 1990. In May 1986, TU Electric filed suit in the 14th Judicial District Court of Dallas County, Texas against TMPA, BEPC and Tex-La because of controversies which exist under the Agreement with respect to the obligations of the parties. TU Electric asserted that each of the defendants has either claimed that it has no further obligation to pay its share of the remaining costs of construction of Comanche Peak, or has claimed that TU Electric has failed to properly construct Comanche Peak or otherwise has breached its obligations under the Agreement. TU Electric sought recovery of damages against Tex-La for its anticipatory breach of the Agreement and asked for a declaratory judgment against Tex-La, BEPC and TMPA declaring among other things that they were obligated to pay their share of the remaining costs of construction of Comanche Peak and that TU Electric has not failed to use prudent utility practices in constructing Comanche Peak in accordance with the Agreement. TMPA, BEPC and Tex-La filed cross-actions in such suit against TU Electric and the Company asserting various causes of action, including a number of alleged breaches of the Agreement by TU Electric and violations of the Texas Deceptive Trade Practices Act (DTPA). In September 1986, the Court in the Dallas County suit ruled in favor of TU Electric with regard to a plea of the defendants attempting to change the venue of such suit. The case is in the discovery phase and trial is currently scheduled for October 1988.

In June 1986, TMPA and Tex-La filed suit in the 98th Judicial District Court of Travis County, Texas against TU Electric and the Company. The petition asserted various causes of action, including a number of alleged breaches of the Agreement by TU Electric and violations of the DTPA. TMPA and Tex-La asked for rescission and modification of the Agreement and payment for damages, including treble damages based upon violations of the DTPA. TU Electric and the Company intend to vigorously contest this suit, which has been stayed as a result of the ruling in the Dallas County suit.

In February 1988, TU Electric entered into an agreement with TMPA pursuant to which TU Electric will purchase TMPA's ownership interest in Comanche Peak and all outstanding claims and pending lawsuits between TMPA and TU Electric will be settled and terminated. Finalization of the agreement is subject to the approval of the NRC and the PUC with respect to the transfer of TMPA's ownership interest. TU Electric has filed applications to obtain such approvals and cannot predict when action with respect thereto will be taken. (See Note 11 to Financial Statements.)

In June 1986, BEPC filed suit in the 345th Judicial District Court of Travis County, Texas against TU Electric, the Company, Texas Utilities Mining Company and Texas Utilities Services Inc. BEPC alleges that the defendants have breached the Agreement, certain implied warranties and fiduciary duties, and have been grossly negligent, acted with willful misconduct and have violated the DTPA and Texas and federal securities laws. BEPC asks for an injunction against efforts by the defendants to recover additional payments, rescission and reformation of the Agreement and payment for damages, trebled pursuant to the DTPA. BEPC alleges actual damages to that date of at least \$216 million. The defendants intend to vigorously contest this suit, which has been stayed as a result of the ruling in the Dallas County suit. In March 1987, BEPC filed a request with the NRC to modify the construction permits and licenses already issued and to impose a prospective condition to any permits and licenses subsequently issued or renewed to require TU Electric to assume BEPC's ownership interest in Comanche Peak by purchase thereof at its net book cost, and for other unspecified relief. In June 1987, the NRC Office of Special Projects denied this request and TU Electric is unable to predict what further action may be taken.

10. Comanche Peak Nuclear Generating Station (concluded)

Cost and Schedule Estimates

In March 1988, TU Electric announced that following its review of the cost and schedule for Comanche Peak, commercial operation of Unit 1 is presently anticipated at the end of 1989. All Unit 1 corrective action activities are scheduled for completion to permit fuel loading in mid-1989. TU Electric also announced the temporary suspension of construction activities and accrual of AFUDC on Unit 2 beginning in April 1988 for a period of approximately one year. Unit 2 is not expected to be ready for commercial operation until after the 1991 peak season. The delay of Unit 2 was implemented to allow TU Electric to concentrate its resources on the completion of Unit 1, thereby reducing the duplication of effort that would be required to maintain the previous timing between the two units and strengthen TU Electric's ability to manage construction and start-up activities for both units more efficiently with fewer personnel. Additionally, such delay will allow time to make a more complete determination of any modifications that may be required for Unit 2 based upon the knowledge gained from the reinspection and corrective action program applied to Unit 1. The delay of Unit 2 will also permit TU Electric time to implement rates for Unit 1 prior to the final completion and operation of Unit 2. Although construction on Unit 2 has been temporarily suspended, there will be some ongoing expenditures required to maintain the unit until construction is resumed. Additionally, to the extent the work necessary to place Unit 1 into service affects various common systems, some capital expenditures will be associated with Unit 2.

Based upon this revised schedule, the total cost of TU Electric's 94% share of the plant, excluding AFUDC, is estimated to be $6.37 billion. TU Electric's estimated cost of its share, including AFUDC, is $8.54 billion or about $3,950 per kilowatt. Because of the uncertainty regarding the date of commercial operation of Unit 2, no provision has been included in such amount for reestablishing the accrual of AFUDC on Unit 2 after construction resumes. The total cost of the plant, excluding AFUDC, is estimated to be $6.62 billion. Because of the uncertainties regarding payments by the other owners of Comanche Peak of their share of the remaining construction costs, no estimate of the amount of AFUDC that may be attributable to their interests in the plant has been made.

TU Electric had previously estimated, in November 1986, that commercial operation of Unit 1 would be achievable in early 1989 and that Unit 2 would not be ready for commercial operation until after the 1989 summer peak season. Based upon such schedule, the total cost, excluding AFUDC, of TU Electric's $87\frac{5}{6}\%$ share of the plant (which excludes the presently anticipated purchase of TMPA's share) was estimated to be $4.63 billion. TU Electric's estimated cost for its $87\frac{5}{6}\%$ share, including AFUDC, was $6.70 billion or about $3,300 per kilowatt. The total cost of the plant, excluding AFUDC, was estimated to be $5.27 billion.

Because of numerous uncertainties in the licensing process, no assurance can be given that the revised estimated schedule can be met or that the estimated completion cost will not be exceeded. Failure to secure timely and favorable regulatory approvals or further delays occasioned by additional reanalysis, reinspection or rework will increase the cost of the plant and will likely increase financing requirements. At December 31, 1987 and 1986, TU Electric's investment in Comanche Peak, including AFUDC, was $5,808,000,000 and $4,600,000,000, respectively, of which $1,284,000,000 has been allowed in rate base by regulatory authorities. TU Electric has indicated that it does not currently plan to implement increased electric service rates which reflect any additional Comanche Peak costs until Unit 1 is ready for commercial operation. TU Electric continues to believe, based upon revised cost estimates and using acceptable ratemaking approaches and assumptions, that the rate increase, when Unit 1 goes into service, can be held to about 10%. Such rate application will be subject to challenge with respect to the prudence of certain costs, for which an estimate is not presently determinable.

11. Commitments and Contingencies

Construction Program

For major construction work now in progress or contemplated by the System Companies, and commitments with respect thereto, see Resource Planning and Comanche Peak.

Cooling Water Contracts

TU Electric has entered into contracts with public agencies to purchase cooling water for use in the generation of electric energy and has agreed, in effect, to guarantee the principal, $47,920,000 at December 31, 1987, and interest on bonds issued to finance the reservoirs from which the water is supplied. The bonds mature at various dates through 2011 and have interest rates ranging from 5½% to 9%. TU Electric is required to make periodic payments equal to such principal and interest for the years 1988 through 1992 as follows: $4,387,000 for 1988, $4,396,000 for 1989, $4,423,000 for 1990, $4,435,000 for 1991 and $4,430,000 for 1992. In addition, TU Electric is obligated to pay certain variable costs of operating and maintaining the reservoirs. Total payments, including amounts capitalized, under such contracts for 1987, 1986 and 1985 were $4,400,000, $4,833,000 and $4,779,000, respectively. TU Electric has assigned to a municipality all contract rights and obligations of TU Electric in connection with $100,695,000 remaining principal amount of bonds at December 31, 1987 issued for similar purposes which had previously been guaranteed by TU Electric; TU Electric is, however, contingently liable in the event of default by the municipality.

Chaco Coal Properties

Chaco Energy Company (Chaco) entered into an agreement in 1977 for the rights to over 200 million tons of surface mineable coal located in New Mexico. The agreement provides, subject to certain limitations, for advance royalty payments, payable over a period of approximately 35 years, which are based upon annual quantities ranging from approximately 5.1 million tons in 1988 to a maximum of approximately 8.3 million tons in 1991. Such payments approximated $6.60 per ton in 1987 and are subject to escalation in the future due to inflation. In connection with the foregoing, the Company entered into a surety agreement pursuant to which it has undertaken to assure the performance by Chaco with respect to this agreement. Non-utility property at December 31, 1987 and 1986 includes $145,900,000 and $114,400,000, respectively, of minimum advance royalties paid by Chaco under the terms of this agreement.

Capacity and Energy Purchase

TU Electric entered into an agreement in 1982 with Tex-La, a 2⅙% owner of Comanche Peak, whereby TU Electric agreed to purchase an assignment of portions of Tex-La's entitlement to capacity and energy from Comanche Peak in declining amounts over the first eight years of commercial operation of each generating unit. Under the agreement, TU Electric is required to make annual payments to Tex-La comprising a pro rata share of operating costs plus a capital charge on Tex-La's net investment applicable to the portion of Tex-La's entitlement assigned. (See Note 10 concerning litigation proceedings regarding Tex-La's participation in Comanche Peak.)

Martin Lake Unit 4 Construction Cancellation

In November 1986, TU Electric announced that it was not economically feasible to construct a fourth unit at the Martin Lake Steam Electric Station (Martin Lake Unit 4) and cancelled the project which was scheduled for service in 1994. Pursuant to expected regulatory treatment, expenditures of approximately $37,246,000, including contractor termination costs, have been recorded as a deferred asset to be amortized as approved by regulatory authorities. The application in 1988 of Financial Accounting Standards Board's Statement of Financial Accounting Standards No. 90 entitled "Regulated Enterprises - Accounting for Abandonments and Disallowances of Plant Costs" to the accounting for the abandonment of Martin Lake Unit 4 will not have a material effect on the Company's financial statements.

Notes to Financial Statements (concluded)

11. Commitments and Contingencies — (concluded)

Purchase of Utility Plant and Nuclear Fuel

In February 1988, TU Electric entered into an agreement with TMPA pursuant to which TU Electric will purchase TMPA's ownership interest in Comanche Peak. Under the terms of the agreement, TU Electric will make a series of payments to TMPA over approximately a five year period totaling about $456 million on a present value basis. The purchase price is based on TU Electric's incurred cost per kilowatt, including AFUDC, for its existing share plus payment for TMPA's interest in the nuclear fuel for Comanche Peak, certain transmission facilities associated with Comanche Peak and certain expenses. In connection with the purchase of TMPA's ownership interest by TU Electric, all outstanding claims and pending lawsuits between TMPA and TU Electric will be settled and terminated. Finalization of the agreement is subject to the approval of the NRC and the PUC with respect to the transfer of TMPA's ownership interest. An initial payment of approximately $58.7 million was made by TU Electric in February 1988; following such regulatory approvals, which must be received no later than September 22, 1988, TU Electric will make an additional payment of approximately $51.8 million plus interest to the date of initial closing. Thereafter, TU Electric will make ten equal semi-annual payments, including interest, each in the amount of approximately $45 million, for the balance of the purchase.

General

In addition to the above, the Company and its subsidiaries are involved in various legal and administrative proceedings which, in the opinion of the Company, should not have a material effect upon its financial position or results of operations.

12. Supplementary Financial Information (Unaudited)

In the opinion of the Company, the following information includes all adjustments (constituting only normal recurring accruals) necessary to a fair statement of such amounts; quarterly results are not necessarily indicative of expectations for a full year's operations because of seasonal and other factors, including rate changes and variations in maintenance and other operating expense patterns.

	Operating Revenues		Operating Income		Consolidated Net Income		Earnings Per Share of Common Stock	
Quarter Ended	1987	1986	1987	1986	1987	1986	1987	1986
			Thousands of Dollars (except per share amounts)					
March 31	$ 870,525	$ 830,298	$172,941	$169,081	$130,298	$119,167	$0.90	$0.86
June 30	1,010,889	942,481	199,646	173,711	159,083	122,682	1.07	0.88
September 30	1,269,525	1,248,119	299,980	297,056	258,596	249,299	1.71	1.76
December 31	931,984	911,147	176,316	169,712	131,999	135,703	0.87	0.95
Total	$4,082,923	$3,932,045	$848,883	$809,560	$679,976	$626,851	$4.55	$4.45

Statement of Responsibility

The management of Texas Utilities Company is responsible for the preparation, integrity and objectivity of the consolidated financial statements of the Company and its subsidiaries and other information included in this report. The consolidated financial statements have been prepared in conformity with generally accepted accounting principles applied on a consistent basis. As appropriate, the statements include amounts based on informed estimates and judgments of management.

The Company's system of internal accounting control is designed to provide reasonable assurance, on a cost-effective basis, that assets are safeguarded, transactions are executed in accordance with management's authorization and financial records are reliable for preparing consolidated financial statements. Management believes that the system of control provides reasonable assurance that errors or irregularities that could be material to the consolidated financial statements are prevented or would be detected within a timely period. Key elements in this system include the effective communication of established written policies and procedures, selection and training of qualified personnel and organizational arrangements that provide an appropriate division of responsibility. This system of control is augmented by an ongoing internal audit program designed to evaluate its adequacy and effectiveness.

The Board of Directors of the Company addresses its oversight responsibility for the consolidated financial statements through its Audit Committee, which is composed of directors who are not employees of the Company. The Audit Committee meets regularly with the Company's management, internal auditors and independent certified public accountants to review matters relating to financial reporting, auditing and internal controls. To ensure auditor independence, both the internal auditors and independent certified public accountants have full and free access to the Audit Committee.

The independent certified public accounting firm of Deloitte Haskins & Sells is engaged to examine, in accordance with generally accepted auditing standards, the consolidated financial statements of the Company and its subsidiaries and to express an opinion thereon.

Accountants' Opinion

DELOITTE HASKINS & SELLS
CERTIFIED PUBLIC ACCOUNTANTS

To the Shareholders of Texas Utilities Company:

We have examined the consolidated balance sheet of Texas Utilities Company and subsidiaries as of December 31, 1987 and 1986 and the related consolidated statements of income, retained earnings and source of funds for construction 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 consolidated financial statements referred to above present fairly the financial position of the companies at December 31, 1987 and 1986 and the results of their operations and the source of their funds for construction 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.

DELOITTE HASKINS & SELLS

Dallas, Texas
March 18, 1988

Financial Statistics

	1987	1986	1985
TOTAL ASSETS end of year *(thousands)*	**$13,986,260**	$12,318,192	$10,867,022
UTILITY PLANT end of year *(thousands)*	**$15,172,994**	$13,566,133	$12,144,563
Accumulated depreciation end of year	**2,718,328**	2,522,016	2,331,783
Construction expenditures (including allowance for funds used during construction)	**1,688,831**	1,519,619	1,108,861
CAPITALIZATION end of year *(thousands)*			
Long-term debt	**$5,141,491**	$4,283,791	$3,615,669
Preferred stock:			
Not subject to mandatory redemption	**909,633**	811,418	811,418
Subject to mandatory redemption	**232,906**	232,424	34,696
Common stock equity	**5,032,331**	4,460,821	4,066,664
Total	**$11,316,361**	$9,788,454	$8,528,447
CAPITALIZATION RATIOS end of year			
Long-term debt	**45.4%**	43.7%	42.4%
Preferred stock	**10.1**	10.7	9.9
Common stock equity	**44.5**	45.6	47.7
Total	**100.0%**	100.0%	100.0%
EMBEDDED INTEREST COST ON LONG-TERM DEBT end of year	**9.9%**	10.0%	10.3%
EMBEDDED DIVIDEND COST ON PREFERRED STOCK end of year	**8.3%**	8.1%	8.2%
CONSOLIDATED NET INCOME *(thousands)*	**$679,976**	$626,851	$587,758
DIVIDENDS DECLARED ON COMMON STOCK *(thousands)*	**$421,418**	$377,865	$343,364
COMMON STOCK DATA			
Shares outstanding—average	**149,449,134**	140,981,671	135,266,534
Shares outstanding—end of year	**152,408,942**	142,805,206	138,043,162
Earnings per average share	**$4.55**	$4.45	$4.35
Dividends declared per share	**$2.80**	$2.68	$2.52
Book value per share—end of year	**$33.02**	$31.24	$29.46
Return on average common stock equity	**14.3%**	14.7%	15.4%
ALLOWANCE FOR FUNDS USED DURING CONSTRUCTION AS PERCENT OF CONSOLIDATED NET INCOME	**56.9%**	48.5%	39.1%
NET FUNDS FROM OPERATIONS AS PERCENT OF CONSTRUCTION EXPENDITURES (excluding allowance for funds used during construction)	**18.2%**	32.9%	51.0%

1984	1983	1982	1981	1980	1979	1978	1977
$9,759,148	$8,780,954	$8,021,407	$7,306,658	$6,552,972	$5,821,933	$5,161,808	$4,563,806
$11,031,699	$9,967,653	$9,051,442	$8,194,803	$7,438,877	$6,631,618	$5,862,096	$5,111,037
2,143,863	1,958,103	1,758,156	1,560,754	1,378,654	1,213,927	1,057,068	917,637
951,323	906,930	891,560	792,268	807,008	872,916	737,353	734,282
$3,322,925	$3,103,452	$2,973,253	$2,713,863	$2,527,716	$2,368,612	$2,038,654	$1,859,057
727,911	629,779	600,109	600,109	600,109	535,824	506,233	476,578
34,696	34,696	—	—	—	—	—	—
3,573,103	3,235,375	2,810,195	2,421,864	2,090,520	1,830,472	1,624,298	1,432,830
$7,658,635	$7,003,302	$6,383,557	$5,735,836	$5,218,345	$4,734,908	$4,169,185	$3,768,465
43.4%	44.3%	46.6%	47.3%	48.4%	50.0%	48.9%	49.3%
10.0	9.5	9.4	10.5	11.5	11.3	12.1	12.7
46.6	46.2	44.0	42.2	40.1	38.7	39.0	38.0
100.0%	100.0%	100.0%	100.0%	100.0%	100.0%	100.0%	100.0%
10.1%	[illegible]7%	9.5%	9.0%	8.3%	7.9%	7.5%	7.3%
8.3%	8.0%	7.7%	7.7%	7.7%	7.4%	7.3%	7.2%
$526,041	$461,468	$428,646	$359,398	$297,844	$211,151	$200,738	$175,919
$298,878	$262,659	$227,076	$192,306	$164,527	$142,262	$119,945	$103,250
126,626,241	118,454,666	111,556,815	102,292,239	93,719,257	86,319,396	79,026,787	73,194,444
128,585,669	123,685,058	114,182,319	105,236,301	96,088,645	87,985,098	80,665,889	75,000,000
$4.15	$3.90	$3.85	$3.51	$3.18	$2.45	$2.54	$2.40
$2.36	$2.20	$2.04	$1.88	$1.76	$1.64	$1.52	$1.40
$27.79	$26.16	$24.61	$23.01	$21.76	$20.80	$20.14	$19.10
15.5%	15.3%	16.4%	15.9%	15.2%	12.2%	13.1%	13.0%
32.7%	34.4%	31.7%	26.1%	26.2%	28.2%	26.9%	33.3%
58.4%	53.9%	60.0%	58.8%	52.7%	40.3%	44.1%	36.4%

Operating Statistics

	1987	1986	1985
ELECTRIC ENERGY GENERATED AND PURCHASED *(mwh)*			
Generated—net station output	**71,878,925**	75,467,871	76,355,396
Purchased and net interchange	**11,019,037**	4,712,082	2,057,490
Total generated and purchased	**82,897,962**	80,179,953	78,412,886
Company use, losses and unaccounted for	**5,125,310**	4,925,178	5,042,990
Total electric energy sales	**77,772,652**	75,254,775	73,369,896
ELECTRIC ENERGY SALES *(mwh)*			
Residential	**25,716,080**	24,604,109	24,300,788
Commercial	**22,324,328**	21,453,435	20,349,334
Industrial	**21,420,705**	21,013,278	20,921,530
Government and municipal	**2,499,981**	2,385,168	2,324,785
Total general business	**71,961,094**	69,455,990	67,896,437
Other electric utilities	**5,811,558**	5,798,785	5,473,459
Total electric energy sales	**77,772,652**	75,254,775	73,369,896
OPERATING REVENUES *(thousands)*			
Residential	**$1,603,446**	$1,530,258	$1,673,378
Commercial	**1,166,832**	1,137,944	1,207,784
Industrial	**800,635**	822,831	935,849
Government and municipal	**140,291**	134,927	145,256
Total general business	**3,711,204**	3,625,960	3,962,267
Other electric utilities	**221,413**	222,644	250,857
Total from electric energy sales	**3,932,617**	3,848,604	4,213,124
Other operating revenues (including over/under-recovered fuel revenue)	**150,306**	83,441	(42,967)
Total operating revenues	**$4,082,923**	$3,932,045	$4,170,157
ELECTRIC CUSTOMERS end of year			
Residential	**1,838,467**	1,820,381	1,764,346
Commercial	**218,641**	217,232	214,386
Industrial	**24,006**	23,912	24,148
Government and municipal	**13,690**	13,180	12,080
Total general business	**2,094,804**	2,074,705	2,014,960
Other electric utilities	**62**	61	63
Total electric customers	**2,094,866**	2,074,766	2,015,023
RESIDENTIAL STATISTICS (excludes master-metered customers, mwh sales and revenues)			
Average kwh per customer	**13,147**	12,749	13,062
Average revenue per kwh	**6.33¢**	6.31¢	6.99¢

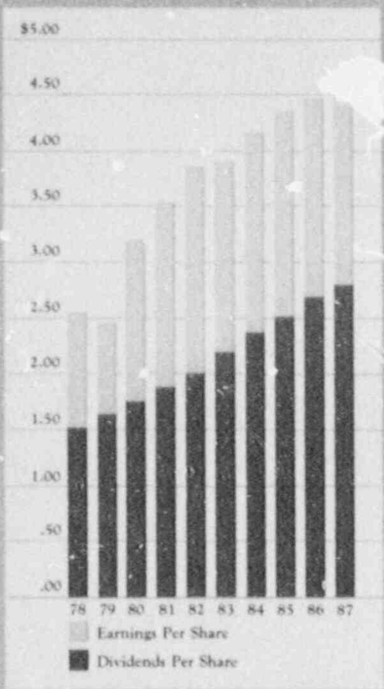
Industrial classification includes service to Alcoa—Sandow:

	1987	1986	1985
Electric energy sales *(mwh)*	**3,409,332**	3,092,696	2,861,454
Operating revenues *(thousands)*	**$62,630**	$65,664	$68,946

1984	1983	1982	1981	1980	1979	1978	1977
72,582,637	67,706,594	64,224,726	62,447,413	62,865,641	58,051,429	57,196,077	53,156,235
382,651	343,581	371,190	91,091	56,388	75,695	79,688	72,845
72,965,288	68,050,175	64,595,916	62,538,504	62,922,029	58,127,124	57,275,765	53,229,080
3,839,517	5,340,248	4,215,774	4,166,327	4,422,762	4,001,684	4,041,486	3,549,768
69,125,771	62,709,927	60,380,142	58,372,177	58,499,267	54,125,440	53,234,279	49,679,312
22,693,290	20,162,506	19,945,087	18,676,240	19,844,409	17,394,402	17,943,224	16,642,382
19,026,267	17,366,563	16,475,253	15,383,162	14,683,104	13,264,436	13,117,202	12,347,755
20,343,558	18,690,077	17,526,412	17,992,261	17,581,265	17,275,859	16,469,636	15,678,254
1,920,420	1,790,476	1,730,273	1,692,106	1,796,988	1,669,726	1,728,056	1,565,518
63,983,535	58,009,622	55,677,025	53,743,769	53,905,766	49,604,423	49,258,118	46,233,909
5,142,236	4,700,305	4,703,117	4,628,408	4,593,501	4,521,017	3,976,161	3,445,403
69,125,771	62,709,927	60,380,142	58,372,177	58,499,267	54,125,440	53,234,279	49,679,312
$1,546,081	$1,306,912	$1,237,632	$1,044,761	$ 877,555	$ 672,340	$ 640,611	$ 552,331
1,127,766	998,362	911,487	778,008	590,921	488,170	439,146	375,822
893,531	808,016	745,243	659,678	482,919	419,224	373,456	310,811
117,793	104,730	95,673	83,077	68,396	54,565	49,623	40,331
3,685,171	3,218,020	2,990,035	2,565,524	2,019,791	1,634,299	1,502,836	1,279,295
233,296	202,387	190,727	161,998	123,188	105,306	87,592	69,975
3,918,467	3,420,407	3,180,762	2,727,522	2,142,979	1,739,605	1,590,428	1,349,270
13,768	67,509	57,263	10,855	31,574	16,684	13,928	18,508
$3,932,235	$3,487,916	$3,238,025	$2,738,377	$2,174,553	$1,756,289	$1,604,356	$1,367,778
1,669,735	1,556,760	1,477,097	1,421,273	1,356,651	1,287,701	1,221,468	1,159,885
208,477	198,548	187,065	177,269	171,495	164,291	160,170	153,658
24,058	22,761	21,478	20,692	19,590	18,654	17,953	17,216
11,455	10,210	10,148	10,263	10,488	11,257	11,260	11,274
1,913,725	1,788,279	1,695,788	1,629,497	1,558,224	1,481,903	1,410,851	1,342,033
66	68	75	78	80	80	62	60
1,913,791	1,788,347	1,695,863	1,629,575	1,558,304	1,481,983	1,410,913	1,342,093
12,887	12,073	12,320	11,862	13,125	11,897	12,747	12,213
6.93¢	6.60¢	6.34¢	5.72¢	4.54¢	3.98¢	3.70¢	3.45¢
2,989,272	2,660,564	2,316,308	2,648,997	2,918,794	3,076,399	2,891,259	2,786,027
$70,825	$68,121	$68,035	$64,016	$48,813	$48,400	$41,572	$36,878

Shareholder Information

Consolidated Earnings Dividends Declared



Quarterly Market Price Ranges

Quarter Ended	Price Range 1987 High	1987 Low	1986 High	1986 Low
March 31	$36⅝	$31½	$34¾	$29½
June 30	33½	30	35¼	29¾
September 30	34⅜	30⅛	37½	30¼
December 31	31¾	25½	34¾	31¼

Dividends Paid per Share of Common Stock

Quarter Ended	Dividends Paid 1987	1986
March 31	$0.67	$0.63
June 30	0.70	0.67
September 30	0.70	0.67
December 31	0.70	0.67
	$2.77	$2.64

The Company has declared common stock dividends payable in cash in each year since its incorporation in 1945 and has continued its record of annual dividend increases, which commenced in 1948. At its February 1988 meeting, the Board of Directors again raised the quarterly dividend by two cents per share, from 70 cents to 72 cents. This regular quarterly dividend is payable April 1, 1988, to shareholders of record on March 7. Dividends are paid in cash to shareholders who are not participating in the Automatic Dividend Reinvestment and Common Stock Purchase Plan; all dividends are reportable for federal income tax purposes as ordinary dividend income. Reference is made to Note 4 to Financial Statements regarding limitations upon payment of dividends on common stock.

1988 Annual Meeting

The Annual Meeting of Shareholders of the Company will be held at 9:30 a.m. on Friday, May 20, 1988, in the Plaza Ballroom at the Plaza of the Americas Hotel, 650 North Pearl Street, Dallas, Texas. Shareholders are cordially invited to be present at the annual meeting. Those unable to attend are urged to exercise their right to vote by proxy. Notice of meeting and proxy statement and form of proxy will be mailed shortly after March 21, the record date for the meeting. Following the meeting, a report of the proceedings will be prepared and distributed to all shareholders.

Directory

TRANSFER AGENTS AND REGISTRARS
MTrust Corp, N.A.
Dallas, Texas

Morgan Shareholder Services Trust Company
New York, New York

DIVIDEND DISBURSING AGENT
Morgan Shareholder Services Trust Company
30 West Broadway
New York, New York 10007-2192

AGENT FOR PARTICIPANTS AUTOMATIC DIVIDEND REINVESTMENT AND COMMON STOCK PURCHASE PLAN
Morgan Shareholder Services Trust Company
Dividend Reinvestment Plans
P.O. Box 3506, Church Street Station
New York, New York 10008-3506

STOCK EXCHANGE LISTINGS
New York Stock Exchange, Inc.
New York, New York

Midwest Stock Exchange, Incorporated
Chicago, Illinois

The Pacific Stock Exchange Incorporated
Los Angeles and San Francisco, California

Ticker Symbol - TXU

The Annual Report has been prepared for the purpose of providing shareholders with information concerning the Company and not in connection with any sale or purchase of, or any offer or solicitation of an offer to buy or sell, any securities.

Texas Utilities Company distributes a booklet containing detailed System financial and operating data, which have been compiled for the convenience of financial analysts; a copy will be furnished upon request.

A copy of the Annual Report to the Securities and Exchange Commission, Form 10-K, will be furnished by the Company upon request.

Requests for copies or other shareholder information should be directed to:
Shareholder Relations
Texas Utilities Company
2001 Bryan Tower
Dallas, Texas 75201
(214) 812-4646

Directors and Officers

Directors

JAMES K. DOBEY
Aptos, California
Retired Chairman of the Board, Wells Fargo & Company

JACK W. EVANS
Dallas, Texas
Chairman of the Board and Chief Executive Officer of Cullum Companies, Inc.

JERRY FARRINGTON
Dallas, Texas
Chairman of the Board and Chief Executive of the Company

WILLIAM M. GRIFFIN
Hartford, Connecticut
Corporate Director

BURL B. HULSEY, JR.
Fort Worth, Texas
Retired Vice Chairman of the Board of the Company

MARGARET N. MAXEY
Austin, Texas
Director of the Chair of Free Enterprise and Professor, Biomedical Engineering Program, College of Engineering at The University of Texas at Austin.

ERLE NYE
Dallas, Texas
President of the Company

CHARLES R. PERRY
Odessa, Texas
Investments, Oil and Gas Interests

CHARLES N. PROTHRO
Wichita Falls, Texas
Owner, Perkins-Prothro Company

WILLIAM H. SEAY
Dallas, Texas
Investments, Retired Chairman and Chief Executive Officer of Southwestern Life Insurance Company

Officers

JERRY FARRINGTON
Chairman of the Board and Chief Executive

ERLE NYE
President

T. L. BAKER
Vice President

W. H. GOODENOUGH
Treasurer

H. A. HORN
Assistant Treasurer and Assistant Secretary

S. S. SWIGER
Controller

PETER B. TINKHAM
Secretary and Assistant Treasurer

TEXAS UTILITIES COMPANY
2001 BRYAN TOWER
DALLAS, TEXAS 75201
(214) 812-4600

TEX-LA ELECTRIC COOPERATIVE OF TEXAS, INC.

FINANCIAL STATEMENTS

December 31, 1987 and 1986

and

ACCOUNTANTS' REPORT

AXLEY & RODE
CERTIFIED PUBLIC ACCOUNTANTS
LUFKIN · NACOGDOCHES · CROCKETT · LIVINGSTON
TEXAS

A. WAYNE CORLEY, CPA
C. BYRON SMITH, CPA
LYNN MONTES, CPA
BRUCE SIEFFERT, CPA
DON DENNIS, CPA
J. LEON MANNING, CPA
ERNEST J. KING, CPA
GARVEY JACKSON, CPA
IRIE MONTES, CPA
DAVE R. STEWART, CPA
GAYLON R. CLARK, CPA
TRACY W. GOLDEN, CPA
J. LEE BRITTAIN, CPA

AXLEY & RODE
CERTIFIED PUBLIC ACCOUNTANTS

BRANCH L. AXLEY, CPA (RETIRED)
CARL F. RODE, CPA (RETIRED)
SAM TARRY, CPA (RETIRED)
HORACE CLIFTON, JR., CPA (1942-1981)
TUCKER WEEMS, CPA (RETIRED)

LUFKIN

LUFKIN, TEXAS 75902-1388
(409) 634-6621
1217 S. TIMBERLAND
P.O. BOX 1388
NACOGDOCHES, TEXAS 75961
(409) 569-0518
420 NORTH STREET
CROCKETT, TEXAS 75835
(409) 544-2256
P.O. BOX 695
LIVINGSTON, TEXAS 77351
(409) 327-3166
619 N. WASHINGTON

March 30, 1988

Board of Directors
Tex-La Electric Cooperative of Texas, Inc.
Nacogdoches, Texas

Members of the Board:

We have examined the financial statements of Tex-La Electric Cooperative of Texas, Inc. (the Cooperative) for the years ended December 31, 1987 and 1986, and have issued our report thereon dated March 30, 1988. As part of our examination, we made a study and evaluation of the Cooperative's system of internal accounting control to the extent we considered necessary to evaluate the system as required by generally accepted auditing standards and specific REA audit requirements as set out in 7 CFR Part 1789 - REA Policy on Audits of Electric and Telephone Borrowers. The purposes of our study and evaluation were to determine the nature, timing, and extent of the auditing procedures necessary for expressing an opinion on the Cooperative's financial statements. Our study was more limited than would be necessary to express an opinion on the system of internal accounting control taken as a whole.

The management of the Cooperative is responsible for establishing and maintaining a system of internal accounting control. In fulfilling this responsibility, estimates and judgments by management are required to assess the expected benefits and related costs of control procedures. The objectives of a system are to provide reasonable, but not absolute, assurance that assets are safeguarded against loss from unauthorized use or disposition, and that transactions are executed in accordance with management's authorization and recorded properly to permit the preparation of financial statements in accordance with generally accepted accounting principles.

Because of inherent limitations in any system of internal accounting control, errors or irregularities may nevertheless occur and not be detected. Also, projection of any evaluation of the system to future periods is subject to the risk that procedures may become inadequate because of changes in conditions or that the degree of compliance with the procedures may deteriorate.

Our study and evaluation made for the limited purposes described in the first paragraph would not necessarily disclose all material weaknesses in the system. Accordingly, we do not express an opinion on the system of internal accounting control of the Cooperative taken as a whole. However, our study and evaluation disclosed no condition that we believed to be a material weakness.

Our comments on specific financial and accounting matters as required by REA and other comments and recommendations developed during our examination, which do not represent internal control weaknesses, are detailed below.

COMMENTS

Examination Procedures:

The procedures specified in Part 1789 have been performed.

Special Reports:

No special reports, summary of recommendations or similar communications other than this management letter were furnished to the Cooperative's management during the course of the audit or during interim audit work.

Material Weaknesses in Internal Accounting Control:

Not applicable.

Weaknesses in Internal Accounting Control Not Considered Material:

Due to the limited number of personnel employed by the Cooperative, a total segregation of certain accounting functions is not possible, nor would it be economically feasible to employ a large accounting staff. Sufficient compensating controls are being utilized to provide assurance that assets are safeguarded and transactions are proper and recorded in a timely manner.

Required Comments:

Internal Accounting Control:

As stated above, a total segregation of certain accounting functions is not possible nor is it economically feasible; however, a system of authorization and recording procedures adequate to provide reasonable accounting control over assets, liabilities, revenues, and expenses is in place. Personnel assigned to specific duties are of a quality commensurate with their expected responsibilities.

Due to the limited segregation of duties, more substantive work was performed than compliance work.

An electronic data processing system is used to produce the Cooperative's accounting records. This system was externally tested to prove mathematical accuracy and proper posting of entries. No errors were noted.

Accounting and Records -

The accounting and reporting procedures used by the Cooperative were adequate and effective and the general condition of the records was good. The methods used in accumulating costs for material, transportation, labor and overhead, and the distribution of these costs to construction and/or expense accounts were proper. During our examination, nothing came to our attention to indicate that the Cooperative has not maintained its records in accordance with the prescribed uniform system of accounts, and no recommendations for improvement are warranted.

Materials Control -

Control over materials and supplies is adequate.

Compliance With Loan Documents -

There has been full compliance with the provisions of the loan contract and mortgage to REA relating to the redemption of capital and payment of dividends during the audit period.

Reports to REA -

The information in the December 31, 1987 financial statements (Form 12) submitted to REA is in agreement in all material respects with the borrower's records.

Service Contracts -

The Cooperative and Sam Rayburn G & T, Inc. (a Texas electric utility cooperative) share office space and employees. The Cooperative pays common expenses and Sam Rayburn reimburses the Cooperative for 50% of the common expenses.

Deposits -

Funds were only deposited with financial institutions insured by an agency of the Federal government.

Income Tax Status -

For the year ended December 31, 1987, more than 85 percent of the income of the Cooperative was received from members. Exemption from Federal income tax has been obtained. Internal Revenue Service Form 990 is being filed annually.

Related Party Transactions -

There are no material related party transactions that came to our attention during our examination that have not been disclosed in the financial statements of the Cooperative.

Acquisitions or Sales of Property -

There were no significant acquisitions of land during the year.

Depreciation Rates -

Depreciation was computed in accordance with REA guidelines, and no unusual charges or credits occurred in the depreciable asset accounts.

Insurance Certifications -

All insurance policies which were in force during the prior one-year period have been renewed or replaced.

This letter supplements the information included in the financial statements and notes. It is intended solely for the use of management, the REA and supplemental lenders and should not be used for any other purpose.

In accordance with the terms of our engagement, we are enclosing copies of the report and management letter for each member of the Board, the General Manager, and other required distribution. Two copies of the report and management letter should be transmitted to the REA and one copy transmitted to supplemental lenders, where applicable.

We express our gratitude to the officers and employees of the Cooperative for the courtesies extended us during the course of our examination. We shall be pleased to discuss the contents of this letter with you in greater detail at your convenience.

Very truly yours,

AXLEY & RODE

Ernest J King

ERNEST J. KING, CPA
PARTNER

EJK:rs

TEX-LA ELECTRIC COOPERATIVE OF TEXAS, INC.

FINANCIAL STATEMENTS

December 31, 1987 and 1986

and

ACCOUNTANTS' REPORT

AXLEY & RODE

CERTIFIED PUBLIC ACCOUNTANTS

CONTENTS

AXLEY & RODE
CERTIFIED PUBLIC ACCOUNTANTS
LUFKIN · NACOGDOCHES · CROCKETT · LIVINGSTON
TEXAS

March 30, 1988

The Board of Directors
Tex-La Electric Cooperative of Texas, Inc.

We have examined the balance sheets of Tex-La Electric Cooperative of Texas, Inc. (the Cooperative) as of December 31, 1987 and 1986, and the related statements of revenue and expenses, patronage capital and other equities, 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.

The balance sheets at December 31, 1987 and 1986 include the Cooperative's share of certain construction costs in connection with the 2 1/6% joint ownership of the Comanche Peak Nuclear Generating Station. As discussed in Notes 2 and 11, recovery of these costs is uncertain and dependent upon future events, the outcome of which cannot presently be determined.

In our opinion, subject to the effects on the financial statements of such adjustments, if any, as might have been required had the outcome of the uncertainty discussed in the preceding paragraph been known, the financial statements referred to above present fairly the financial position of Tex-La Electric Cooperative of Texas, Inc. as of December 31, 1987 and 1986, and the results of its operations and the changes in its financial position for the years then ended in conformity with generally accepted accounting principles applied on a consistent basis.

Axley & Rode
CERTIFIED PUBLIC ACCOUNTANTS

TEX-LA ELECTRIC COOPERATIVE OF TEXAS, INC.
BALANCE SHEETS
December 31, 1987 and 1986

	1987	1986
ASSETS		
Electric Plant, At Cost (Notes 2, 6 and 11):		
Furniture and fixtures	$ 25 906	$ 24 753
Office building	91 102	91 102
	117 008	115 855
Less accumulated depreciation	14 050	8 651
	102 958	107 204
Construction work in progress	189 764 145	170 128 561
	189 867 103	170 235 765
Other Assets and Investments:		
Investment in associated organizations (Note 3)	2 164 673	2 838 157
Other assets	7 686	3 731
	2 172 359	2 841 888
Current Assets:		
Cash, including temporary cash investments of $1,678,571 and $987,839 in 1987 and 1986 - General funds	1 681 308	1 011 071
Cash, including temporary cash investments of $6,019 and $152,632 in 1987 and 1986 - Construction funds	216 109	259 763
Accounts receivable (includes receivables from member cooperatives of $2,519,269 in 1987 and $1,654,900 in 1986)	2 595 091	1 723 594
Prepaid expenses	6 368	50 625
	4 498 876	3 045 053
	$196 538 338	$176 122 706
EQUITIES AND LIABILITIES		
Patronage Capital and Other Equities (Note 11):		
Memberships	$ 700	$ 700
Patronage capital (Note 4)	422 726	359 819
Other equities (Note 5)	194 375	152 100
	617 801	512 619
Long-term debt (Notes 6 and 12)	191 663 255	173 035 986
Current Liabilities:		
Accounts payable	4 257 282	2 574 101
	$196 538 338	$176 122 706

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

TEX-LA ELECTRIC COOPERATIVE OF TEXAS, INC.
STATEMENTS OF REVENUE AND EXPENSES
For The Years Ended December 31, 1987 and 1986

	1987	1986
Operating Revenue:		
Power sales (Notes 7 and 10)	$27 104 885	$27 412 058
Operating Expenses:		
Cost of purchased power	24 540 147	26 526 304
Administrative and general (Notes 8 and 9)	923 608	766 547
Depreciation	5 399	4 739
	25 469 154	27 297 590
Operating margins before interest expense	1 635 731	114 468
Interest Expense:		
Interest on long-term debt	17 058 705	16 577 621
Allowance for borrowed funds used during construction	(15 415 095)	(16 577 621)
	1 643 610	-
Operating margin (deficit)	(7 879)	114 468
Nonoperating Margin:		
Interest income	113 061	42 275
Net margin	$ 105 182	$ 156 743

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

TEX-LA ELECTRIC COOPERATIVE OF TEXAS, INC.
STATEMENTS OF PATRONAGE CAPITAL AND OTHER EQUITIES
For The Years Ended December 31, 1987 and 1986

	MEMBERSHIPS	PATRONAGE CAPITAL	OTHER EQUITIES	TOTAL
Balance, December 31, 1985	$700	$258 101	$ 97 075	$355 876
Net margin	-	156 743	-	156 743
Transfer to appropriated margins	-	(55 025)	55 025	-
Balance, December 31, 1986	700	359 819	152 100	512 619
Net margin	-	105 182	-	105 182
Transfer to appropriated margins	-	(42 275)	42 275	-
Balance, December 31, 1987	$700	$422 726	$194 375	$617 801

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

TEX-LA ELECTRIC COOPERATIVE OF TEXAS, INC.
STATEMENTS OF CHANGES IN FINANCIAL POSITION
For The Years Ended December 31, 1987 and 1986

	1987	1986
Funds Were Provided By:		
Net margin	$ 105 182	$ 156 743
Add Items Not Requiring Funds:		
Depreciation	5 399	4 739
TOTAL FROM OPERATIONS	110 581	161 482
Advances from REA	6 964 000	21 257 986
Advances from CFC	11 663 269	-
Decrease in investment in associated organizations	673 484	-
Decrease in working capital	229 358	1 381 045
	$19 640 692	$22 800 513
Funds Were Used For:		
Additions to construction work in progress	$19 635 584	$22 697 178
Additions to furniture and fixtures	1 153	8 502
Additions to building	-	91 102
Additions to other assets	3 955	3 731
	$19 640 692	$22 800 513
Increase (Decrease) in Working Capital By Components:		
Cash - General	$ 670 237	$ 375 788
Cash - Construction	(43 654)	(1 313 423)
Accounts receivable	871 497	(735 411)
Prepaid expenses	(44 257)	43 489
Accounts payable	(1 683 181)	243 551
Accrued interest	-	4 961
	$ (229 358)	$(1 381 045)

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

TEX-LA ELECTRIC COOPERATIVE OF TEXAS, INC.
NOTES TO FINANCIAL STATEMENTS

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Organization and Operation:

Tex-La Electric Cooperative of Texas, Inc. (the Cooperative) is an electric generating and transmission cooperative formed pursuant to the Texas Electric Cooperative Corporation Act. The Cooperative provides wholesale electric service to the distribution cooperatives of Cherokee County Electric Cooperative Association, Deep East Texas Electric Cooperative, Inc., Jasper-Newton Electric Cooperative, Inc., Houston County Electric Cooperative, Inc., Rusk County Electric Cooperative, Inc., Sam Houston Electric Cooperative, Inc. and Wood County Electric Cooperative, Inc. (Members).

The Cooperative was formed principally to provide dependable power and energy to its members at the lowest cost possible. In doing so, the Cooperative works closely with its members in determining their power requirements and in contracting with its respective bulk power suppliers to satisfy such requirements.

Chart of Accounts:

The Cooperative maintains its accounting records in accordance with the Federal Energy Regulatory Commission's Uniform System of Accounts as adopted by the Rural Electrification Administration. The more significant accounting policies are described below.

Electric Plant:

Office building and furniture and fixtures are stated at historical cost. Depreciation of these assets is computed at a straight-line composite rate of 4% and 7%, respectively.

Construction work in progress represents the Cooperative's share of the project costs for the construction of the Comanche Peak Steam Electric Station not yet in production.

Allowance for Borrowed Funds Used During Construction:

The Cooperative has capitalized as permitted to electric plant the cost of borrowed funds used for the construction of the Comanche Peak Steam Electric Station net of the related interest income from invested construction funds.

Income Taxes:

The Cooperative is exempt from Federal income tax under the provisions of Section 501(c)(12) of the Internal Revenue Code.

NOTE 2 - JOINTLY-OWNED FACILITIES

On December 9, 1980, the Cooperative executed a Joint Ownership Agreement with Texas Power & Light Company to acquire a 4 1/3% undivided ownership interest in the Comanche Peak Steam Electric Station, a two unit 1150 megawatts each nuclear fueled electric generating station, located near Glen Rose, Texas in Hood and Somervell Counties, Texas, being constructed by Texas Utilities Generating Company.

On February 12, 1982, following the announcement of a substantial increase in the cost of the project and delay in the projected commercial operation date, the Cooperative agreed to reduce its interest in the project to 2 1/6%. In 1982 the Cooperative, based on Texas Utilities Electric Company's (Texas Utilities) estimates, expected that Comanche Peak Units 1 and 2 would be licensed by the Nuclear Regulatory Commission (NRC) and commence commercial operation in 1984 and 1985, respectively, and that the Cooperative's share of the project would cost a total of $120 million. The Cooperative planned to fund its participation in the project by means of a loan from the Federal Financing Bank of up to $180 million, guaranteed by the Rural Electrification Administration (REA).

As a result of difficulties which Texas Utilities has encountered in the NRC licensing process, primarily in convincing the NRC that Comanche Peak has been properly constructed, the NRC to date has not issued an operating license for either Unit 1 or 2. At present, the Cooperative is not able to predict when, if ever, the NRC will issue an operating license for the project. The Cooperative does not expect commercial operation of the project to commence prior to January, 1990 for Unit 1 and December, 1991 for Unit 2. As of December 31, 1987, the Cooperative's total expenditures for its 2 1/6 percent share of the project is approximately $190 million. Based on the Cooperative's current estimates for the completion and licensing of the project, the Cooperative's share of Comanche Peak is expected ultimately to cost approximately $330 million. This figure could increase further in the event of added delays or other difficulties with the project beyond those currently anticipated. Construction of Unit 1 of Comanche Peak is virtually complete, but because of numerous uncertainties in the licensing process no assurance can be given that the estimated commercial operation dates of these units can be met or that the current estimated completion costs thereof will not be exceeded. Failure to secure timely and favorable regulatory approvals or any further delay occasioned by reinspections or possible rework resulting therefrom will increase the cost of the plant.

If the plant becomes licensed and the Cooperative files an application for a rate increase which includes the costs associated with Comanche Peak, the Texas Public Utility Commission may find a portion of the Comanche Peak costs to be imprudent. Should this happen, current accounting rules would require immediate write-off against margins for any such costs that are not recoverable through rates or otherwise.

NOTE 3 - INVESTMENTS IN ASSOCIATED ORGANIZATIONS

Investments in associated organizations at December 31, 1987 and 1986 consisted of the following:

	1987	1986
Patronage capital from the National Rural Utilities Cooperative Finance Corporation (CFC)	$2 163 673	$2 837 157
Memberships	1 000	1 000
	$2 164 673	$2 838 157

The investment in CFC represents patronage capital credits allocated to the Cooperative. Realization of cash from this investment is within the control of CFC.

NOTE 4 - PATRONAGE CAPITAL

The details of Patronage Capital at December 31, 1987 and 1986 are as follows:

	1987	1986
Assignable	$422 726	$359 819
Assigned	-	-
	422 726	359 819
Less: Retired	-	-
	$422 726	$359 819

NOTE 5 - OTHER EQUITIES

The details of other equities at December 31, 1987 and 1986 are as follows:

	1987	1986
Appropriated margins	$194 375	$152 100

The by-laws of the Cooperative provide that non-operating margins be used initially to offset any losses incurred during the current or any prior fiscal year. Upon recovery of any losses, a fund in the amount of $400,000 shall be accumulated from these remaining non-operating margins and funded each year, if necessary, to maintain the $400,000 balance.

NOTE 6 - LONG-TERM DEBT

Long-term debt at December 31, 1987 and 1986 consisted of the following:

	1987	1986
Mortgage notes payable to the Federal Financing Bank at interest rates from 6.679% to 11.911% with the Rural Electrification Administration (REA) as administrator	$179 999 986	$173 035 986
Note payable to CFC at 8.0%	11 663 269	-
	$191 663 255	$173 035 986

NOTE 6 - LONG-TERM DEBT - CONTINUED

In July, 1981, the Cooperative entered into a loan agreement not to exceed $180,000,000 to finance the construction and operation of generating facilities, electric transmission, distribution and service lines by the Cooperative payable to the Federal Financing Bank (FFB) pursuant to an agreement between the FFB and the REA.

The maturity date of each amount advanced under the loan agreement shall not be less than two years nor more than seven years after the date of the advance and shall be designated in writing at the time of request by the borrower subject to REA approval. Under the terms of the agreement, the Cooperative may designate a maturity date of thirty-four years after the end of the calendar year in which such advance was made. The interest rate applicable to each advance is the respective rate established by the FFB at the time of the advance. The Cooperative has designated a long-term maturity of thirty-four years for a portion of the FFB advances. It is anticipated that the amounts due in 1988, together with future additional borrowings from FFB, will be extended.

During 1987, the Cooperative submitted a deficiency loan application to REA to fund additional costs of the Comanche Peak project. In January, 1988 a $35.5 million deficiency loan agreement was finalized with FFB and REA. The terms of the deficiency loan are substantially the same as the original $180 million loan. In January, 1988, approximately $10.9 million was borrowed to reduce the obligation on the CFC line of credit, which had to be used until the deficiency loan was approved.

Substantially all of the Cooperative's assets are pledged as security for the long-term debt owed FFB.

The Cooperative has a $12,000,000 line of credit with CFC which expires in 1988. During 1987, CFC agreed to allow the Cooperative to use the line of credit to fund the costs and expenses of litigation with Texas Utilities Generating Company relating to the Comanche Peak Nuclear Station.

NOTE 7 - POWER CONTRACTS

The Cooperative has wholesale power contracts with each of its members which require the members to buy and receive from the Cooperative all their power and energy requirements and require the Cooperative to sell and deliver power and energy in satisfaction of such requirements. The contracts extend to December 30, 2026 and thereafter, as permitted by law until the expiration of six months after notice of cancellation by either the Cooperative or the Members.

The Cooperative purchased all of its power at wholesale from Texas Utilities Electric Company, the Southwestern Power Administration, an agency of the Department of Energy, Southwestern Electric Power Company, and Houston Lighting and Power Company.

NOTE 8 - PENSION PLAN

All employees of the Cooperative participate in the National Rural Electric Cooperative Association (NRECA) Retirement & Security Program (Program), a defined benefit pension plan qualified under section 401 and tax-exempt under section 501(a) of the Internal Revenue Code. The Cooperative makes annual contributions to the Program equal to the amounts accrued for pension expense except for the period when a moratorium on contributions has been in effect since July 1, 1987 due to reaching full funding limitation. In this multiemployer plan, which is available to all member cooperatives of NRECA, the accumulated benefits and plan assets are not determined or allocated separately by individual employer. The total pension expense for 1987 and 1986 was $11,754 and $14,333, respectively, for this cooperative.

NOTE 9 - RELATED PARTY TRANSACTIONS

The Cooperative and Sam Rayburn G & T, Inc. (SRG&T), an electric generating and transmission cooperative, share facilities and personnel. SRG&T reimburses the Cooperative for its proportionate share of the related expenses and equipment purchases. The total reimbursement for the years ended December 31, 1987 and 1986 was $122,224 and $131,582, respectively. Certain members of the Cooperative are members of SRG&T.

NOTE 10 - RATE MATTERS

In December, 1986 the Cooperative filed a request for rate increase with the Public Utility Commission of Texas (PUCT) to increase revenues by 10 percent, or by approximately $3 million. In 1987, the Cooperative was allowed to increase rates by 10 percent over an adjusted revenue requirement which would result in the Cooperative's increase being approximately $3 million. The new rates were implemented June 16, 1987.

NOTE 11 - COMANCHE PEAK LITIGATION

In May, 1986, the Cooperative and the other minority owners of the Comanche Peak Steam Electric Station (Comanche Peak), a two-unit nuclear fueled power generation plant, were sued by the majority owner, Texas Utilities Electric Company (Texas Utilities). The suit seeks a declaration that Texas Utilities has properly performed all its obligations under the Joint Ownership Agreement relating to Comanche Peak and seeks to force those minority owners who have discontinued making payments to Texas Utilities to resume making payments. Texas Utilities' lawsuit was filed after months of settlement negotiations with the Cooperative had reached an impasse and after the Cooperative, in a letter dated May 20, 1986 to Texas Utilities, formally notified Texas Utilities that future payments would not be made because the Cooperative believes that Texas Utilities has mismanaged the construction of Comanche Peak and has failed to provide a cost estimate and a schedule of completion to the Cooperative as required by a Joint Ownership Agreement. From that time to December 31, 1987, a total of $32,074,900 would have been payable by the Cooperative to Texas Utilities. At this time, the Cooperative is not making any payments.

NOTE 11 - COMANCHE PEAK LITIGATION - CONTINUED

In June, 1986, the Cooperative and two minority owners (Texas Municipal Power Agency and Brazos Electric Power Cooperative, Inc.) of the Comanche Peak project instituted litigation against Texas Utilities claiming various breaches of the Joint Ownership Agreement by Texas Utilities (Note 12). The estimated cost of the Comanche Peak project increased from $764 million in 1974 to $9 billion as currently estimated by Texas Utilities. Completion dates of these two units were estimated in 1972 to be 1980 and 1982 for units one and two. On November 18, 1985, Texas Utilities announced that, assuming no further unforeseen difficulties, commercial operations of unit one could not commence until mid-1987, with unit two commencing commercial operations 6 months later. On April 18, 1986, Texas Utilities announced that, because of new problems that had been uncovered through its reinspection program, the estimate for commercial operation made in November, 1985 was no longer valid. At present, Texas Utilities has indicated that Comanche Peak will not begin operating before 1989.

In the litigation, the minority owners assert their rights under the Texas Deceptive Trade Practices Act (DTPA). They seek to be compensated for their damages, including, but not limited to, damages related to increased costs of completion, delay damages and attorney's fees and expenses. Furthermore, under the DTPA, the minority owners may recover up to three times the amount of actual damages, plus court costs and reasonable attorney's fees.

Although settlement discussions have taken place, they have been unproductive. The litigation currently is set for trial commencing in the fall of 1988. Presently, the Cooperative is not able to predict whether the settlement talks will be successful or, if not, what the outcome of the litigation will be.

NOTE 12 - SUBSEQUENT EVENTS

On February 12, 1988 Texas Utilities and the Texas Municipal Power Agency reached a settlement as to their claims against each other in the foregoing litigation.

On March 16, 1988 the Cooperative completed the refinancing of certain long-term Federal Financing Bank loans in the principal amount of $102,203,000. The refinancing resulted in a decrease in the effective interest rate (including servicing fee) from 10.66% to 9.76%. The issuance costs related to this refinancing have been deferred and will be amortized over the term of the debt.