UNITED STATES SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549
FORM 10-Q

(Mark One)

[X] QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

FOR THE QUARTERLY PERIOD ENDED JUNE 30, 1995

OR

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

For the transition period from _____ to _____

Commission file number 1-7629

HOUSTON INDUSTRIES INCORPORATED
(Exact name of registrant as specified in its charter)

Texas	74-1885573
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)
5 Post Oak Park 4400 Post Oak Parkway Houston, Texas	77027
(Address of principal executive offices)	(Zip Code)

(713) 629-3000
(Registrant's telephone number, including area code)

Commission file number 1-3187

HOUSTON LIGHTING & POWER COMPANY
(Exact name of registrant as specified in its charter)

Texas	74-0694415
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)
611 Walker Avenue Houston, Texas	77002
(Address of principal executive offices)	(Zip Code)

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

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

As of July 31, 1995, Houston Industries Incorporated had 131,336,234 shares of common stock outstanding, including 7,438,726 ESOP shares not deemed outstanding for financial statement purposes. As of July 31, 1995, all 1,100 shares of Houston Lighting & Power Company's common stock were held, directly or indirectly, by Houston Industries Incorporated.

HOUSTON INDUSTRIES INCORPORATED AND HOUSTON LIGHTING & POWER COMPANY
QUARTERLY REPORT ON FORM 10-Q
FOR THE QUARTER ENDED JUNE 30, 1995

This combined Form 10-Q is separately filed by Houston Industries Incorporated and Houston Lighting & Power Company. Information contained herein relating to Houston Lighting & Power Company is filed by Houston Industries Incorporated and separately by Houston Lighting & Power Company on its own behalf. Houston Lighting & Power Company makes no representation as to information relating to Houston Industries Incorporated (except as it may relate to Houston Lighting & Power Company) or to any other affiliate or subsidiary of Houston Industries Incorporated.

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PART I. FINANCIAL INFORMATION

ITEM 1. FINANCIAL STATEMENTS.

HOUSTON INDUSTRIES INCORPORATED AND SUBSIDIARIES
STATEMENTS OF CONSOLIDATED INCOME
(THOUSANDS OF DOLLARS)

	THREE MONTHS ENDED JUNE 30,		SIX MONTHS ENDED JUNE 30,	
	1995	1994 (Restated)	1995	1994 (Restated)
REVENUES	$ 978,225	$1,004,906	$1,724,391	$1,826,487
EXPENSES:				
Fuel	238,465	235,514	422,067	452,702
Purchased power	50,822	103,906	116,410	202,455
Operation and maintenance	217,650	204,089	416,179	397,940
Taxes other than income taxes	64,616	62,959	135,566	126,071
Depreciation and amortization	112,286	99,967	216,482	199,191
Total	683,839	706,435	1,306,704	1,378,359
OPERATING INCOME	294,386	298,471	417,687	448,128
OTHER INCOME (EXPENSE):				
Allowance for other funds used during construction	2,014	93	4,643	1,409
Other - net	(17,394)	(6,349)	(27,653)	(13,429)
Total	(15,380)	(6,256)	(23,010)	(12,020)
INTEREST AND OTHER CHARGES:				
Interest on long-term debt	64,042	66,356	129,258	133,001
Other interest	9,678	6,623	18,677	13,035
Allowance for borrowed funds used during construction	(1,133)	(129)	(2,938)	(1,817)
Preferred dividends of subsidiary	7,450	8,403	16,435	16,676
Total	80,037	81,253	161,432	160,895
INCOME FROM CONTINUING OPERATIONS BEFORE INCOME TAXES AND CUMULATIVE EFFECT OF CHANGE IN ACCOUNTING	198,969	210,962	233,245	275,213
INCOME TAXES	65,709	76,654	76,136	99,306
INCOME FROM CONTINUING OPERATIONS BEFORE CUMULATIVE EFFECT OF CHANGE IN ACCOUNTING	133,260	134,308	157,109	175,907
DISCONTINUED OPERATIONS:				
Loss from discontinued cable television operations (net of applicable income taxes)		(7,583)		(15,084)
Tax benefit from discontinued cable television operations			90,607	
CUMULATIVE EFFECT OF CHANGE IN ACCOUNTING FOR POSTEMPLOYMENT BENEFITS (NET OF INCOME TAXES OF $4,415)				(8,200)
NET INCOME	$ 133,260	$ 126,725	$ 247,716	$ 152,623

(continued)

EARNINGS PER COMMON SHARE:

CONTINUING OPERATIONS BEFORE

CUMULATIVE EFFECT OF CHANGE IN ACCOUNTING	$ 1.08	$ 1.09	$ 1.27	$ 1.44
DISCONTINUED OPERATIONS:				
Loss from discontinued cable television operations		(.06)		(.12)
Tax benefit from discontinued cable television operations			.73	
CUMULATIVE EFFECT OF CHANGE IN ACCOUNTING FOR POSTEMPLOYMENT BENEFITS				(.07)
EARNINGS PER COMMON SHARE	$ 1.08	$ 1.03	$ 2.00	$ 1.25
DIVIDENDS DECLARED PER COMMON SHARE	$ .75	$ .75	$ 1.50	$ 1.50
WEIGHTED AVERAGE COMMON SHARES OUTSTANDING (000)	123,769	122,508	123,684	122,465

See Notes to Consolidated Financial Statements.

HOUSTON INDUSTRIES INCORPORATED AND SUBSIDIARIES
CONSOLIDATED BALANCE SHEETS
(THOUSANDS OF DOLLARS)

ASSETS

	JUNE 30, 1995	DECEMBER 31, 1994
PROPERTY, PLANT AND EQUIPMENT - AT COST:		
Electric plant:		
Plant in service	$ 11,936,270	$ 11,743,070
Construction work in progress	320,253	333,180
Nuclear fuel	215,399	212,795
Plant held for future use	201,764	201,741
Electric plant acquisition adjustments	3,166	3,166
Other property	69,739	85,529
Total	12,746,591	12,579,481
Less accumulated depreciation and amortization	3,697,205	3,527,598
Property, plant and equipment - net	9,049,386	9,051,883
CURRENT ASSETS:		
Cash and cash equivalents	37,578	10,443
Special deposits	10	10
Accounts receivable - net	55,745	22,149
Accrued unbilled revenues	20,568	38,372
Fuel stock, at lifo cost	65,612	56,711
Materials and supplies, at average cost	148,866	148,007
Prepayments	11,790	14,398
Total current assets	340,169	290,090
OTHER ASSETS:		
Net assets of discontinued cable television operations	701,330	618,982
Deferred plant costs - net	626,026	638,917
Deferred debits	303,216	281,204
Regulatory asset - net	232,472	235,463
Unamortized debt expense and premium on reacquired debt	157,915	161,885
Recoverable project costs - net	89,216	98,954
Equity investment in foreign electric utility	26,286	25,699
Total other assets	2,136,461	2,061,104
Total	$ 11,526,016	$ 11,403,077

See Notes to Consolidated Financial Statements.

HOUSTON INDUSTRIES INCORPORATED AND SUBSIDIARIES
CONSOLIDATED BALANCE SHEETS
(THOUSANDS OF DOLLARS)

CAPITALIZATION AND LIABILITIES

	JUNE 30, 1995	DECEMBER 31, 1994
CAPITALIZATION:		
Common Stock Equity:		
Common stock, no par value	$ 2,438,573	$ 2,437,638
Unearned ESOP shares	(278,217)	(289,611)
Retained earnings	1,283,326	1,221,221
Total common stock equity	3,443,682	3,369,248
Preference Stock, no par value, authorized 10,000,000 shares; none outstanding		
Cumulative Preferred Stock of Subsidiary, no par value:		
Not subject to mandatory redemption	351,345	351,345
Subject to mandatory redemption	51,055	121,910
Total cumulative preferred stock	402,400	473,255
Long-Term Debt:		
Debentures	548,821	548,729
Long-term debt of subsidiaries:		
First mortgage bonds	2,851,822	3,020,400
Pollution control revenue bonds	155,262	155,247
Other	7,774	9,757
Total long-term debt	3,563,679	3,734,133
Total capitalization	7,409,761	7,576,636
CURRENT LIABILITIES:		
Notes payable	698,165	423,291
Accounts payable	159,235	159,225
Taxes accrued	108,261	169,690
Interest accrued	83,130	73,527
Dividends accrued	98,502	98,469
Accrued liabilities to municipalities	19,507	21,307
Customer deposits	63,305	64,905
Current portion of long-term debt and preferred stock	179,460	49,475
Other	62,258	64,026
Total current liabilities	1,471,823	1,123,915
DEFERRED CREDITS:		
Accumulated deferred federal income taxes	1,711,196	1,763,230
Unamortized investment tax credit	401,865	411,580
Fuel-related credits	154,168	242,912
Other	377,203	284,804
Total deferred credits	2,644,432	2,702,526
COMMITMENTS AND CONTINGENCIES		
Total	$ 11,526,016	$ 11,403,077

See Notes to Consolidated Financial Statements.

HOUSTON INDUSTRIES INCORPORATED AND SUBSIDIARIES
STATEMENTS OF CONSOLIDATED CASH FLOWS

INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS
(THOUSANDS OF DOLLARS)

	SIX MONTHS ENDED JUNE 30,	
	1995	1994
		(Restated)
CASH FLOWS FROM OPERATING ACTIVITIES:		
Income from continuing operations	$ 157,109	$ 175,907
Adjustments to reconcile income from continuing operations to net cash provided by operating activities:		
Depreciation and amortization	216,482	199,191
Amortization of nuclear fuel	13,912	5,421
Deferred income taxes	38,573	28,265
Investment tax credit	(9,715)	(9,695)
Allowance for other funds used during construction	(4,643)	(1,409)
Fuel cost (refund) and over/(under) recovery - net	(83,337)	27,408
Net cash provided by discontinued cable television operations	5,495	20,122
Changes in other assets and liabilities:		
Accounts receivable and accrued unbilled revenues	(15,792)	(6,070)
Inventory	(9,760)	548
Other current assets	2,608	12,304
Accounts payable	10	(41,769)
Interest and taxes accrued	(51,826)	(62,300)
Other current liabilities	(5,165)	2,094
Other - net	90,115	72,304
Net cash provided by operating activities	344,066	422,321
CASH FLOWS FROM INVESTING ACTIVITIES:		
Electric capital and nuclear fuel expenditures (including allowance for borrowed funds used during construction)	(133,151)	(191,637)
Non-regulated electric power project expenditures	(12,378)	(406)
Corporate headquarters expenditures (including capitalized interest)	(56,899)	(12,253)
Net cash used in discontinued cable television operations	(47,045)	(36,949)
Other - net	(7,552)	(16,269)
Net cash used in investing activities	(257,025)	(257,514)
CASH FLOWS FROM FINANCING ACTIVITIES:		
Payment of matured bonds		(19,500)
Redemption of preferred stock	(91,400)	(20,000)
Payment of common stock dividends	(185,581)	(183,735)
Increase in notes payable - net	274,874	58,415
Extinguishment of long-term debt	(20,273)	
Net cash used in discontinued cable television operations	(40,798)	(10,384)
Other - net	3,272	3,611
Net cash used in financing activities	(59,906)	(171,593)
NET INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS	27,135	(6,786)
CASH AND CASH EQUIVALENTS AT BEGINNING OF PERIOD	10,443	14,884
CASH AND CASH EQUIVALENTS AT END OF PERIOD	$ 37,578	$ 8,098
SUPPLEMENTAL DISCLOSURE OF CASH FLOW INFORMATION:		
Cash Payments:		
Interest (net of amounts capitalized)	$ 188,852	$ 186,935
Income taxes	30,525	65,090

See Notes to Consolidated Financial Statements.

HOUSTON INDUSTRIES INCORPORATED AND SUBSIDIARIES
STATEMENTS OF CONSOLIDATED RETAINED EARNINGS
(THOUSANDS OF DOLLARS)

	THREE MONTHS ENDED JUNE 30,		SIX MONTHS ENDED JUNE 30,	
	1995	1994	1995	1994
Balance at Beginning of Period.....	$1,242,925	$1,125,253	$1,221,221	$1,191,230
Net Income for the Period.....	133,260	126,725	247,716	152,623
Total.....	1,376,185	1,251,978	1,468,937	1,343,853
Common Stock Dividends.....	(92,859)	(91,898)	(185,611)	(183,773)
Balance at End of Period.....	$1,283,326	$1,160,080	$1,283,326	$1,160,080

See Notes to Consolidated Financial Statements.

HOUSTON LIGHTING & POWER COMPANY
STATEMENTS OF INCOME
(THOUSANDS OF DOLLARS)

	THREE MONTHS ENDED JUNE 30,		SIX MONTHS ENDED JUNE 30,	
	1995	1994	1995	1994
OPERATING REVENUES	$ 978,225	$ 1,004,906	$ 1,724,391	$ 1,826,487
OPERATING EXPENSES:				
Fuel	238,465	235,514	422,067	452,702
Purchased power	50,822	103,906	116,410	202,455
Operation	153,606	141,835	294,926	274,802
Maintenance	64,044	62,254	121,253	123,138
Depreciation and amortization	111,961	99,675	215,874	198,604
Income taxes	77,292	81,921	96,310	108,994
Other taxes	64,616	62,959	135,566	126,071
Total	760,806	788,064	1,402,406	1,486,766
OPERATING INCOME	217,419	216,842	321,985	339,721
OTHER INCOME (EXPENSE):				
Allowance for other funds used during construction	2,014	93	4,643	1,409
Other - net	(9,055)	(2,773)	(10,508)	(5,759)
Total	(7,041)	(2,680)	(5,865)	(4,350)
INCOME BEFORE INTEREST CHARGES	210,378	214,162	316,120	335,371
INTEREST CHARGES:				
Interest on long-term debt	61,399	61,557	122,917	123,399
Other interest	789	1,853	3,924	4,749
Allowance for borrowed funds used during construction	(1,133)	(129)	(2,938)	(1,817)
Total	61,055	63,281	123,903	126,331
INCOME BEFORE CUMULATIVE EFFECT OF CHANGE IN ACCOUNTING	149,323	150,881	192,217	209,040
CUMULATIVE EFFECT OF CHANGE IN ACCOUNTING FOR POSTEMPLOYMENT BENEFITS (NET OF INCOME TAXES OF $4,415)				(8,200)
NET INCOME	149,323	150,881	192,217	200,840
DIVIDENDS ON PREFERRED STOCK	7,450	8,403	16,435	16,676
INCOME AFTER PREFERRED DIVIDENDS	$ 141,873	$ 142,478	$ 175,782	$ 184,164

See Notes to Financial Statements.

HOUSTON LIGHTING & POWER COMPANY
BALANCE SHEETS
(THOUSANDS OF DOLLARS)

ASSETS

	JUNE 30, 1995	DECEMBER 31, 1994
PROPERTY, PLANT AND EQUIPMENT - AT COST:		
Electric plant in service	$ 11,936,270	$ 11,743,070
Construction work in progress	320,253	333,180
Nuclear fuel	215,399	212,795
Plant held for future use	201,764	201,741
Electric plant acquisition adjustments	3,166	3,166

Total	12,676,852	12,493,952
Less accumulated depreciation and amortization	3,687,185	3,517,923
Property, plant and equipment - net	8,989,667	8,976,029
CURRENT ASSETS:		
Cash and cash equivalents	94,403	235,867
Special deposits	10	10
Accounts receivable:		
Affiliated companies	2,339	4,213
Others	30,992	8,896
Accrued unbilled revenues	20,568	38,372
Inventory:		
Fuel stock, at lifo cost	65,612	56,711
Materials and supplies, at average cost	148,449	147,922
Prepayments	8,833	9,665
Total current assets	371,206	501,656
OTHER ASSETS:		
Deferred plant costs - net	626,026	638,917
Deferred debits	254,333	241,611
Unamortized debt expense and premium on reacquired debt	155,814	158,351
Regulatory asset - net	232,472	235,463
Recoverable project costs - net	89,216	98,954
Total other assets	1,357,861	1,373,296
Total	$ 10,718,734	$ 10,850,981

See Notes to Financial Statements.

HOUSTON LIGHTING & POWER COMPANY
BALANCE SHEETS
(THOUSANDS OF DOLLARS)

CAPITALIZATION AND LIABILITIES

	JUNE 30, 1995	DECEMBER 31, 1994
CAPITALIZATION:		
Common Stock Equity:		
Common stock, class A; no par value	$ 1,524,949	$ 1,524,949
Common stock, class B; no par value	150,978	150,978
Retained earnings	2,164,391	2,153,109
Total common stock equity	3,840,318	3,829,036
Cumulative Preferred Stock:		
Not subject to mandatory redemption	351,345	351,345
Subject to mandatory redemption	51,055	121,910
Total cumulative preferred stock	402,400	473,255
Long-Term Debt:		
First mortgage bonds	2,851,822	3,020,400
Pollution control revenue bonds	155,262	155,247
Other	7,774	9,757
Total long-term debt	3,014,858	3,185,404
Total capitalization	7,257,576	7,487,695
CURRENT LIABILITIES:		
Accounts payable	146,272	148,042
Accounts payable to affiliated companies	6,731	10,936
Taxes accrued	132,616	181,043
Interest accrued	71,283	64,732
Accrued liabilities to municipalities	19,507	21,307
Customer deposits	63,305	64,905
Current portion of long-term debt and preferred stock	179,460	49,475
Other	57,899	59,912
Total current liabilities	677,073	600,352
DEFERRED CREDITS:		
Accumulated deferred federal income taxes	1,917,233	1,876,300
Unamortized investment tax credit	401,865	411,580
Fuel-related credits	154,168	242,912
Other	310,819	232,142
Total deferred credits	2,784,085	2,762,934
COMMITMENTS AND CONTINGENCIES		
Total	$ 10,718,734	$ 10,850,981

See Notes to Financial Statements.

HOUSTON LIGHTING & POWER COMPANY
STATEMENTS OF CASH FLOWS

INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS
(THOUSANDS OF DOLLARS)

	SIX MONTHS ENDED JUNE 30,	
	1995	1994
CASH FLOWS FROM OPERATING ACTIVITIES:		
Net income	$ 192,217	$ 200,840
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	215,874	198,604
Amortization of nuclear fuel	13,912	5,421
Deferred income taxes	40,933	36,588
Investment tax credits	(9,715)	(9,695)
Allowance for other funds used during construction	(4,643)	(1,409)
Fuel cost (refund) and over/(under) recovery - net	(83,337)	27,408
Cumulative effect of change in accounting for postemployment benefits		8,200
Changes in other assets and liabilities:		
Accounts receivable - net	(2,418)	1,731
Material and supplies	(527)	2,915
Fuel stock	(8,901)	(2,337)
Accounts payable	(5,975)	(21,769)
Interest and taxes accrued	(41,876)	(45,250)
Other current liabilities	(3,311)	3,547
Other - net	72,415	58,217
Net cash provided by operating activities	374,648	463,011
CASH FLOWS FROM INVESTING ACTIVITIES:		
Capital and nuclear fuel expenditures (including allowance for borrowed funds used during construction)	(218,151)	(191,637)
Other - net	(6,940)	(6,355)
Net cash used in investing activities	(225,091)	(197,992)
CASH FLOWS FROM FINANCING ACTIVITIES:		
Payment of matured bonds		(19,500)
Payment of dividends	(183,057)	(181,885)
Decrease in notes payable		(57,600)
Redemption of preferred stock	(91,400)	(20,000)
Extinguishment of long-term debt	(20,273)	
Other - net	3,709	1,981
Net cash used in financing activities	(291,021)	(277,004)
NET DECREASE IN CASH AND CASH EQUIVALENTS	(141,464)	(11,985)
CASH AND CASH EQUIVALENTS AT BEGINNING OF PERIOD	235,867	12,413
CASH AND CASH EQUIVALENTS AT END OF PERIOD	$ 94,403	$ 428
SUPPLEMENTAL DISCLOSURE OF CASH FLOW INFORMATION:		
Cash Payments:		
Interest (net of amounts capitalized)	$ 123,563	$ 131,236
Income taxes	34,974	57,913

See Notes to Financial Statements.

HOUSTON LIGHTING & POWER COMPANY
STATEMENTS OF RETAINED EARNINGS
(THOUSANDS OF DOLLARS)

	THREE MONTHS ENDED JUNE 30,		SIX MONTHS ENDED JUNE 30,	
	1995	1994	1995	1994
Balance at Beginning of Period	$ 2,104,768	$ 1,990,614	$ 2,153,109	$ 2,028,924
Net Income for the Period	149,323	150,881	192,217	200,840
Total	2,254,091	2,141,495	2,345,326	2,229,764
Deductions - Cash Dividends:				
Preferred	7,450	8,403	16,435	16,676
Common	82,250	84,499	164,500	164,495
Total	89,700	92,902	180,935	181,171
Balance at End of Period	$ 2,164,391	$ 2,048,593	$ 2,164,391	$ 2,048,593

See Notes to Financial Statements.

HOUSTON INDUSTRIES INCORPORATED AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

AND

HOUSTON LIGHTING & POWER COMPANY

NOTES TO FINANCIAL STATEMENTS

(1) GENERAL

(a) DISCONTINUED OPERATIONS. On July 6, 1995, Houston Industries Incorporated (Company) sold KBLCOM Incorporated, its cable television subsidiary (KBLCOM), to Time Warner Inc. (Time Warner). For a description of the sale, see Note 10 to these financial statements. The Company's consolidated financial statements for the first and second quarters of 1995 reflect KBLCOM as a discontinued operation. The Company's consolidated financial statements and certain other financial information contained in the Company's and Houston Lighting & Power Company's (HL&P) Annual Report on Form 10-K for the year ended December 31, 1994 (1994 Combined Form 10-K), were restated for consistency to reflect KBLCOM as a discontinued operation. See the Company's and HL&P's Combined Form 8-K (File Nos. 1-7629 and 1-3187) dated May 12, 1995 (Combined Form 8-K). The sale of KBLCOM did not affect the financial statements of HL&P.

(b) REGULATORY PROCEEDINGS AND LITIGATION. The information presented in the following Notes in this Form 10-Q should be read in conjunction with the Combined Form 8-K, including the Notes to the Company's Consolidated and HL&P's Financial Statements. Notes 1(a), 1(f), 2, 3, 4 and 5 to the Company's Consolidated and HL&P's Financial Statements in the Combined Form 8-K, as updated by the description of developments in the regulatory and litigation matters contained in the notes to these financial statements, are incorporated herein by reference as they relate to the Company and HL&P, respectively.

(2) JOINTLY-OWNED NUCLEAR PLANT

(a) HL&P INVESTMENT. HL&P is the project manager (and one of four co-owners) of the South Texas Project Electric Generating Station (South Texas Project), which consists of two 1,250 megawatt (MW) nuclear generating units. HL&P has a 30.8 percent interest in the project and bears a corresponding share of capital and operating costs associated with the project. As of June 30, 1995, HL&P's investments (net of $414.2 million accumulated plant depreciation and $127.8 million nuclear fuel amortization) in the South Texas Project and in nuclear fuel, including allowance for funds used during construction, were $2.1 billion and

$87.6 million, respectively.

(b) UNITED STATES NUCLEAR REGULATORY COMMISSION (NRC) INSPECTIONS AND OPERATIONS. HL&P removed both generating units at the South Texas Project from service in February 1993 when a problem was encountered with certain of the units' auxiliary feedwater pumps. The units were

out of service from February 1993 to February 1994, when Unit No. 1 was returned to service. Unit No. 2 was returned to service in May 1994. In June 1993, the NRC placed the South Texas Project on its "watch list" of plants with weaknesses that warrant increased attention after a review of the South Texas Project operations. In February 1995, the NRC removed the South Texas Project from its "watch list".

For a discussion concerning litigation by certain current and former employees or contractors of HL&P asserting that their employment was terminated or disrupted in retaliation for their having made safety-related complaints to the NRC, see Note 2(b) of the notes to the financial statements included in the Combined Form 8-K and Note 2(b) to the financial statements included in the Company's and HL&P's Combined Quarterly Report on Form 10-Q for the quarter ended March 31, 1995 (Combined Form 10-Q).

While no prediction can be made at this time as to the ultimate outcome of these matters, the Company and HL&P do not believe that they will have a material adverse effect on the Company's or HL&P's financial condition or results of operations.

(c) LITIGATION WITH CO-OWNERS OF THE SOUTH TEXAS PROJECT. In February 1994, the City of Austin (Austin), one of the four co-owners of the South Texas Project, filed suit (Austin II Litigation) against HL&P. That suit is now pending in the 11th District Court of Harris County, Texas, having recently been transferred from the 152nd District. It is not currently anticipated that the trial will commence before March 1996. Austin alleges that the outages at the South Texas Project from early 1993 to early 1994 were due to HL&P's failure to perform obligations it owed to Austin under the Participation Agreement among the four co-owners of the South Texas Project (Participation Agreement). Austin also asserts that HL&P breached certain undertakings voluntarily assumed by HL&P on behalf of the co-owners under the terms and conditions of the NRC Operating Licenses and Technical Specifications relating to the South Texas Project. Under its amended pleadings, Austin claims that such failures have caused Austin damages of at least $150 million due to the incurrence of increased operating and maintenance costs, the cost of replacement power and lost profits on wholesale transactions that did not occur.

In May 1994, the City of San Antonio (San Antonio), another co-owner of the South Texas Project, intervened in the litigation filed by Austin against HL&P and asserted claims similar to those asserted by Austin. Although San Antonio has not specified the damages sought in its complaint, expert reports filed in the litigation have indicated that San Antonio's claims may be in excess of $275 million. HL&P is contesting San Antonio's intervention and has called for arbitration of San Antonio's claim under the arbitration provisions of the Participation Agreement. The trial court denied HL&P's motions to strike San Antonio's intervention and to compel San Antonio to arbitrate its claims against HL&P and in April 1995, the Court of Appeals of the First District of Texas affirmed the trial court's decision. HL&P is seeking further review of these decisions by the Texas Supreme Court.

For a discussion of a previous lawsuit relating to the South Texas Project filed in 1983 by Austin against the Company and HL&P (in which the Company and HL&P prevailed), of certain claims by San Antonio against the Company and HL&P and the related arbitration thereof, and of the

settlement entered into by the Company, HL&P and Central and South West Corporation, see Note 2(c) of the notes to the financial statements included in the Combined Form 8-K.

Although HL&P and the Company do not believe there is merit to either Austin's or San Antonio's claims and have opposed San Antonio's intervention in the Austin II Litigation, there can be no assurance as to the ultimate outcome of these matters.

(d) NUCLEAR INSURANCE. For a discussion of the nuclear property and nuclear liability insurance maintained in connection with the South Texas

Project and potential assessments associated therewith, see Note 2(d) of the notes to the financial statements included in the Combined Form 8-K.

(e) NUCLEAR DECOMMISSIONING. For a discussion of nuclear decommissioning costs, the Company's decommissioning funding level and the accounting for debt and equity securities held by the decommissioning trust, see Note 2(e) of the notes to financial statements included in the Combined Form 8-K.

(f) DEFERRED PLANT COSTS. For a discussion of deferred plant costs, see Note 1(f) of the notes to the financial statements included in the Combined Form 8-K. The amortization of these deferrals totaled $6.4 million and $12.9 million for the three and six months ended June 30, 1995, respectively, and is included on the Company's Statements of Consolidated Income and HL&P's Statements of Income in depreciation and amortization expense.

(3) RATE REVIEW, FUEL RECONCILIATION AND OTHER PROCEEDINGS

In February 1994, the Public Utility Commission of Texas (Utility Commission) initiated a proceeding (Docket No. 12065) to determine whether HL&P's existing rates are just and reasonable and to reconcile HL&P's fuel costs from April 1, 1990 to July 31, 1994. The Utility Commission also initiated a separate proceeding (Docket No. 13126) to review issues regarding the prudence of operation of the South Texas Project from the date of commercial operation through the present (a period including the outage at the South Texas Project during 1993 and 1994).

In February 1995, all major parties to these proceedings signed an agreement resolving the issues with respect to HL&P, including the prudence issues related to operation of the South Texas Project (Proposed Settlement). In July 1995, an Administrative Law Judge (ALJ) recommended that the Utility Commission issue a final order consistent with the Proposed Settlement. A decision is expected by the Utility Commission at a Final Order Meeting scheduled for August 30, 1995.

Under the Proposed Settlement, HL&P's base rates would be reduced by approximately $62 million per year, effective retroactively to January 1, 1995, and HL&P would be precluded from seeking rate increases for three years, subject to certain conditions. Under the Proposed Settlement, HL&P would amortize its remaining investment ($211 million as of June 30, 1995) in the cancelled Malakoff Electric Generating Station (Malakoff) plant over a period not to exceed

seven years. HL&P also would increase its decommissioning expense for the South Texas Project by $9 million per year.

The Proposed Settlement also provides HL&P the option to write down a portion of its investment in the South Texas Project during the five-year period commencing January 1, 1995. The parties to the Proposed Settlement agreed that up to $50 million per year of any write down would be treated as a reasonable and necessary expense during routine reviews of HL&P's earnings and any rate review proceeding initiated against HL&P. In the second quarter of 1995, HL&P recorded a $7 million write down of its investment in the South Texas Project pursuant to this provision of the Proposed Settlement, which amount is included on the Company's Consolidated and HL&P's Statements of Income in depreciation and amortization expense.

Until the approval of the Proposed Settlement by the Utility Commission, HL&P's existing rates will continue in effect; however, HL&P's financial statements for 1995 reflect the estimated effects of the Proposed Settlement. In the second quarter and first six months of 1995, HL&P's pre-tax earnings were reduced by approximately $39 million and $56 million, respectively, which represent the estimated effects of the Proposed Settlement on revenues and expenses. Included in these reductions are charges of $7 million related to the South Texas Project investment as discussed above and a one-time, pre-tax charge of $9 million incurred in connection with certain mine-related costs which were not previously recorded and are not recoverable under the terms of the Proposed Settlement. (See Note 5 to these financial statements.) Deferred revenues are included on the Company's Consolidated and HL&P's Balance Sheets in other deferred credits subject to refund in the event the Proposed Settlement is approved.

Under the terms of the Proposed Settlement, HL&P previously agreed that approximately $70 million of fuel expenditures and related interest incurred during the fuel reconciliation period would not be recoverable from ratepayers. This $70 million was recorded in December 1994 as a one-time, pre-tax charge to reconcilable fuel revenues and will be refunded to ratepayers in the event that the Proposed Settlement is approved by the Utility Commission.

For additional information regarding Docket Nos. 12065 and 13126, see Note 3 to the financial statements included in the Combined Form 10-Q, which note is incorporated herein by reference.

(4) APPEALS OF PRIOR UTILITY COMMISSION RATE ORDERS

Pursuant to a series of applications filed by HL&P in recent years, the Utility Commission has granted HL&P rate increases to reflect in electric rates HL&P's substantial investment in new plant construction, including the South Texas Project. Although Utility Commission action on those applications has been completed, judicial review of a number of the Utility Commission orders is pending. In the event the courts ultimately reverse actions of the Utility Commission in any of these proceedings, such matters would be remanded to the Utility Commission for action in light of the courts' orders. Because of the number of variables which can affect the ultimate resolution of such matters on remand, the Company and HL&P generally are not in a position at this time to predict the outcome of the matters on appeal or the ultimate effect that adverse action by the courts could have on the Company and HL&P.

(a) 1991 RATE CASE. In HL&P's 1991 rate case (Docket No. 9850), the Utility Commission approved a non-unanimous settlement agreement providing for a $313 million increase in HL&P's base rates, termination of deferrals granted with respect to Unit No. 2 of the South Texas Project and of the qualified phase-in plan deferrals granted with respect to Unit No. 1 of the South Texas Project, and recovery of deferred plant costs. The settlement authorized a 12.55 percent return on common equity for HL&P. Rates contemplated by the settlement agreement were implemented in May 1991 and remain in effect (subject to the outcome of the current rate proceeding described in Note 3 to these financial statements).

The Utility Commission's order in Docket No. 9850 was affirmed on review by a District Court, and the Court of Appeals for the 3rd District at Austin (Austin Court of Appeals) affirmed that decision on procedural grounds due to the failure of the Appellant to file the statement of facts with the court in a timely manner. On review, the Texas Supreme Court has remanded the case to the Austin Court of Appeals for consideration of any asserted errors of law that may be evident from the face of the Utility Commission's order. The Appellant has raised issues regarding deferred accounting, the treatment of federal income tax expense and certain other matters. As to federal tax issues, in an appeal involving GTE-SW (to which HL&P was not a party), the Texas Supreme Court held in April 1995 that the Utility Commission is not required by the Public Utility Regulatory Act of 1975, as amended (PURA) to take into account the tax effects of expenses disallowed for rate making purposes in determining a utility's federal income tax expense for rate making purposes, that the Utility Commission has discretion in determining the utility's "fair share" of tax savings when a utility pays federal income taxes as part of a consolidated group, and is not required to reduce utility tax expense by savings resulting from unregulated activities. The GTE-SW opinion clarified a 1987 Texas Supreme Court decision in an HL&P case and rejected arguments that the HL&P decision required utility tax expense to be calculated on the basis of "actual taxes paid". Although no assurance can be given in this matter, the Company believes that if the principles and rationale of the GTE-SW decision discussed above were applied, the Utility Commission's treatment of the tax issue in Docket No. 9850 should be upheld.

For a discussion of another recent Texas Supreme Court decision upholding deferred accounting treatment, see Note 4(c) of the notes to the financial statements included in the Combined Form 8-K.

Because the Utility Commission's order in Docket No. 9850 found that HL&P would have been entitled to rate relief greater than the $313 million agreed to in the settlement, HL&P believes that any disallowance that might be required if the Austin Court of Appeals concludes that the Utility Commission's inclusion of deferred accounting costs in the settlement was improper would be offset by that greater amount.

The parties to the Proposed Settlement have agreed to withdraw their appeals of the Utility Commission's orders in such docket, subject to HL&P's dismissing its appeal in Docket No. 6668. (See Note 4(d) to these financial statements.)

(b) 1988 RATE CASE. In HL&P's 1988 rate case (Docket No. 8425), the Utility Commission granted HL&P a $227 million increase in base revenues, allowed a 12.92 percent return on common equity, authorized a qualified

phase-in for Unit No. 1 of the South Texas Project (including

approximately 72 percent of HL&P's investment in Unit No. 1 of the South Texas Project in rate base) and authorized HL&P to use deferred accounting for Unit No. 2 of the South Texas Project. Rates substantially corresponding to the increase granted were implemented by HL&P in June 1989 and remained in effect until May 1991.

In August 1994, the Austin Court of Appeals affirmed the Utility Commission's order in Docket No. 8425 on all matters other than the Utility Commission's treatment of tax savings associated with deductions taken for expenses disallowed from cost of service. The court held that the Utility Commission had failed to require that such tax savings be passed on to ratepayers. Both HL&P and other parties sought review by the Texas Supreme Court, which granted discretionary review as to the issue of certain Malakoff plant expenditures treated as "Plant Held for Future Use", and brought the entire case before it for consideration, including the tax issue raised by HL&P. The case has been scheduled for oral argument in September 1995 by the Texas Supreme Court.

Although no assurance can be given in this matter, the Company believes that if the principles and rationale of the GTE-SW decision discussed in Note 4(a) above were applied, the Utility Commission's treatment of the tax issue in Docket No. 8425 should be upheld.

(c) DEFERRED ACCOUNTING. For information regarding deferred accounting treatment granted for certain costs associated with the South Texas Project, see Note 4(c) of the notes to the financial statements included in the Combined Form 8-K and Note 2(f) to these financial statements.

The Office of the Public Utility Counsel (OPUC) has agreed, pursuant to the Proposed Settlement, to withdraw and dismiss its appeal of the Utility Commission's order granting deferred accounting if the Proposed Settlement becomes effective and on the condition that HL&P dismisses its appeal in Docket No. 6668. However, the appeal of the State of Texas remains pending.

(d) PRUDENCE REVIEW OF THE CONSTRUCTION OF THE SOUTH TEXAS PROJECT. For a discussion of the Utility Commission's inquiry into the prudence of the planning, management and construction of the South Texas Project (Docket No. 6668), see Note 4(d) of the notes to the financial statements included in the Combined Form 8-K.

Under the Proposed Settlement, OPUC, HL&P and the City of Houston each has agreed to dismiss its respective appeals of Docket No. 6668. A separate party to this appeal, however, has not agreed to dismiss its appeal. If this party does not elect to dismiss its appeal, HL&P may elect to maintain its appeal, whereupon OPUC and the City of Houston shall also be entitled to maintain their appeals.

(5) MALAKOFF

For a discussion of the current and Proposed Settlement rate treatment of HL&P's investment in Malakoff and related matters, see Note 3 of the notes to these financial statements and Note 5 of the notes to the financial statements included in the Combined Form 8-K.

(6) COMMON STOCK

(a) COMPANY. At June 30, 1995 and December 31, 1994, the Company had authorized 400,000,000 shares of common stock, of which 123,876,880 and 123,526,350 shares, respectively, were outstanding. Outstanding shares exclude the unallocated Employee Stock Ownership Plan shares which as of June 30, 1995 and December 31, 1994 were 7,459,354 and 7,770,313, respectively.

(b) HL&P. All issued and outstanding Class A voting common stock of HL&P is held by the Company and all issued and outstanding Class B non-voting common stock of HL&P is held by Houston Industries (Delaware) Incorporated (HI Delaware), a wholly-owned subsidiary of the Company.

(7) HL&P PREFERRED STOCK

At June 30, 1995, and December 31, 1994, HL&P had 10,000,000 shares of preferred stock authorized, of which 4,318,397 and 5,232,397 shares, respectively, were outstanding.

In April 1995, HL&P redeemed, at $100 per share, 514,000 shares of its $9.375 cumulative preferred stock. The redemption included 257,000 shares in satisfaction of mandatory sinking fund requirements, and an additional 257,000 shares as an optional retirement.

In June 1995, HL&P redeemed, at $100 per share, all 400,000 shares of its $8.50 cumulative preferred stock. The redemption included 200,000 shares in satisfaction of mandatory sinking fund requirements, and the remaining 200,000 shares as an optional retirement.

(8) HL&P LONG-TERM DEBT

In June 1995, HL&P purchased from a third party $19.0 million aggregate principal amount of its 8 3/4% first mortgage bonds due 2022 for a total purchase price of $20.7 million.

Reference is made to Note 12(b) to these financial statements with respect to HL&P's redemption and refunding of $150,850,000 aggregate principal amount of pollution control revenue bonds subsequent to June 30, 1995.

(9) EARNINGS PER COMMON SHARE

(a) COMPANY. Earnings per common share for the Company is computed by dividing net income by the weighted average number of shares outstanding during the respective period.

(b) HL&P. Earnings per share data for HL&P is not computed since all of its common stock is held by the Company and HI Delaware.

(10) DISCONTINUED CABLE TELEVISION OPERATIONS

On July 6, 1995, the Company closed its sale of KBLCOM to Time Warner in a tax-deferred, stock-for-stock merger valued at approximately $2.4 billion. In anticipation of the sale, effective January 1, 1995, the operations of KBLCOM have been accounted for as discontinued and prior periods were restated for consistency in reflecting KBLCOM as a discontinued operation. The Company recorded a $90.6 million tax benefit in the first quarter of 1995 in recognition of the deferred tax asset arising from the Company's excess tax basis in KBLCOM stock. Based on a Time Warner common stock price of $43.25 on July 6, 1995, the Company will recognize in the third quarter of 1995 an additional after-tax gain estimated to be $690 million, which is subject to post closing adjustments. For additional information regarding the sale of KBLCOM, see the Company's Current Report on Form 8-K (File No. 1-7629) dated July 6, 1995, which is incorporated herein by reference. For a presentation of the Company's financial statements for the years 1992 through 1994 which reflects KBLCOM on a discontinued operations basis, reference is made to the Company's Consolidated Financial Statements contained in the Combined Form 8-K.

Operating results from discontinued operations for the six months ended June 30, 1995 and 1994 were as follows:

	SIX MONTHS ENDED JUNE 30,	
	1995	1994
	(Thousands of Dollars)	
Revenues	$139,440	$ 122,274
Operating expenses (1)	84,487	78,150
Gross operating margin (1)	54,953	44,124
Depreciation, amortization, interest and other	75,063	63,652
Income tax benefit	(4,174)	(4,444)
Deferred loss (2)	(15,936)	
Loss from discontinued operations (3)	$ 0	($ 15,084)

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(1) Exclusive of depreciation and amortization.

(2) The net loss from discontinued operations of KBLCOM for the six months ended June 30, 1995 was deferred by the Company until the sale is recognized in the third quarter of 1995. The deferred loss is included on the Company's Consolidated Balance Sheets in net

assets of discontinued cable television operations.

(3) Loss from discontinued operations of KBLCOM excludes the effects of corporate overhead charges and includes interest expense relating to the amount of intercompany debt that Time Warner purchased from the Company.

Net assets of discontinued operations were as follows:

	JUNE 30, 1995	DECEMBER 31, 1994
	(Thousands of Dollars)	
Assets:		
Cable television property, net of accumulated depreciation of $179,200 and $161,402 for 1995 and 1994, respectively	$ 297,829	$ 276,624
Equity in cable television partnerships	185,368	160,363
Intangible assets	1,007,243	1,029,440
Other assets	49,894	43,625
Total assets	1,540,334	1,510,052
Less:		
Cable television debt	(463,782)	(504,580)
Accumulated deferred income taxes	(313,585)	(316,241)
Other liabilities	(61,637)	(70,249)
Net assets	$ 701,330	$ 618,982

In March 1995, KBL Cable, Inc. (KBL Cable), a subsidiary of KBLCOM, made a scheduled repayment of $15.8 million principal amount of its senior notes and senior subordinated notes. In the first quarter of 1995, KBL Cable repaid borrowings under its senior bank credit facility in the amount of $25.0 million.

(11) CHANGE IN ACCOUNTING FOR THE COMPANY AND HL&P

The Company and HL&P recorded in the first quarter of 1994 a one-time, after-tax charge to income of $8.2 million resulting from the Company's and HL&P's adoption of Statement of Financial Accounting Standards (SFAS) No. 112, "Employer's Accounting for Postemployment Benefits", effective January 1, 1994. For additional information regarding SFAS No. 112, see Note 9 to the financial statements included in the Combined Form 10-Q.

(12) SUBSEQUENT EVENTS

(a) COMPANY. The Company offered eligible employees (excluding officers) of the Company, HL&P and Houston Industries Energy, Inc. (HI Energy) who were 55 years of age or older and had at least 10 years of service as of July 31, 1995 an incentive program to retire early. For employees electing early retirement, the program would add five years of service credit and five years in age up to 35 years of service and age 65, respectively, in determining an employee's pension. Each participating employee (under age 62) would also receive a supplemental benefit to age 62. During July 1995, the early retirement incentive was accepted by approximately 290 employees.

Pension benefits and supplemental benefits (if applicable) are being paid out from the Houston Industries Incorporated Retirement Trust. Upon adoption of the early retirement plan, the projected benefit obligations pertaining to HL&P's retirement plan and supplemental benefits

will be increased by approximately $27 million and $5 million, respectively. Pursuant to SFAS No. 71, "Accounting for the Effects of Certain Types of Regulation", HL&P will defer the costs associated with the increases in these benefit obligations and will amortize the costs over a period which corresponds to the estimated period over which savings will offset these additional costs.

(b) HL&P. During July 1995, the Brazos River Authority and the Matagorda County Navigation District Number One issued on behalf of HL&P $150,850,000 aggregate principal amount of revenue refunding bonds collateralized by HL&P's first mortgage bonds. The new bonds bear an initial interest rate of 5.8%, variable at HL&P's option after a

five-year no-call period, and mature in 2015. Proceeds from these issuances will be used in 1995 to redeem, at 102% of their aggregate principal amount, pollution control revenue bonds aggregating $150,850,000 and bearing a weighted average interest rate of 9.9%.

(13) INTERIM PERIOD RESULTS: RECLASSIFICATIONS

The results of interim periods are not necessarily indicative of results expected for the year due to the seasonal nature of HL&P's business. In the opinion of management, the interim information reflects all adjustments (consisting only of normal recurring adjustments) necessary for a full presentation of the results for the interim periods. Certain amounts from the previous year have been reclassified to conform to the 1995 presentation of financial statements. Such reclassifications do not affect earnings.

ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS.

CURRENT ISSUES

HL&P

RATE REVIEW, FUEL RECONCILIATION AND OTHER PROCEEDINGS. In February 1994, the Utility Commission initiated a proceeding (Docket No. 12065) to determine whether HL&P's existing rates are just and reasonable and to reconcile HL&P's fuel costs from April 1, 1990 to July 31, 1994. The Utility Commission initiated a separate proceeding (Docket No. 13126) to review issues regarding the prudence of operation of the South Texas Project from the date of commercial operation through the present. In February 1995, all major parties to these proceedings signed a settlement agreement resolving the issues with respect to HL&P, including the prudence issues related to the operation of the South Texas Project. In July 1995, an ALJ recommended that the Utility Commission issue a final order consistent with the Proposed Settlement. A decision is expected by the Utility Commission at a Final Order Meeting scheduled for August 30, 1995.

Under the Proposed Settlement, HL&P's base rates would be reduced by approximately $62 million per year, effective retroactively to January 1, 1995, and HL&P would be precluded from seeking rate increases for three years, subject to certain conditions. Under the Proposed Settlement, HL&P would amortize its remaining investment ($211 million as of June 30, 1995) in the cancelled Malakoff plant, over a period not to exceed seven years. The Proposed Settlement also provides HL&P the option to write down a portion of its investment in the South Texas Project during the five-year period commencing January 1, 1995. The parties to the Proposed Settlement agreed that up to $50 million per year of any write down would be treated as a reasonable and necessary expense during routine reviews of HL&P's earnings and any rate review proceeding initiated against HL&P. Decommissioning expenses for the South Texas Project would increase by $9 million per year under the Proposed Settlement.

The estimated effects of the Proposed Settlement have been recorded on HL&P's financial statements effective as of January 1, 1995. In the second quarter and first six months of 1995, the Proposed Settlement reduced HL&P's pre-tax earnings by approximately $39 million and $56 million, respectively. These reductions reflect HL&P's decision in the second quarter to write off (i) $7 million of its investment in the South Texas Project discussed above and (ii) the one-time, pre-tax charge of $9 million incurred in connection with certain mine-related costs which were not previously recorded and are not recoverable under the terms of the Proposed Settlement.

Under the terms of the Proposed Settlement, HL&P previously agreed that approximately $70 million of fuel expenditures and related interest incurred during the fuel reconciliation period would not be recoverable from ratepayers. This $70 million was recorded in December 1994 as a one-time, pre-tax charge to reconcilable fuel revenues and will be refunded to ratepayers in the event that the Proposed Settlement is approved by the Utility Commission. For additional information regarding the Proposed Settlement, see Note 3 to the Company's Consolidated and HL&P's Financial Statements (Financial Statements) in Item 1 of this Report.

COMPETITION. HL&P and other members of the electric utility industry, like other regulated industries, continue to be subject to technological, regulatory and economic pressures that are increasing competition and offer the possibility for fundamental changes in the industry and its regulation.

In its 1995 session, pursuant to Sunset legislation, the Texas Legislature considered the reenactment of PURA, the basic statute governing the regulation of electric utilities in Texas. During that legislative debate, a number of

proposals were made by utilities and others to change various provisions of the regulatory structure, particularly in response to developing competition in the industry. Although a number of administrative and procedural changes were made to PURA, the law as reenacted generally preserves the basic regulatory framework that has existed with respect to electric utilities such as HL&P. However, new provisions were added allowing for increased competition in connection with wholesale sales, including the recognition of wholesale generators and power marketers, who may engage in sales activities without regulation as electric utilities. Provisions regarding access by non-utility generators to transmission facilities were added, as were new provisions regarding rates charged by utilities for transmission of power for themselves and for third parties. The effect of these revisions likely will be an increase in competition for wholesale sales in Texas, but HL&P's wholesale sales traditionally have accounted for less than 1% of its total revenues.

For additional information regarding the impact of competition on HL&P's business, see "Business of HL&P - Competition" and "Regulation of the Company - Federal" in Part I of the 1994 Combined Form 10-K and Note 1(a) of the notes to the financial statements included in the Combined Form 8-K, which information is incorporated herein by reference.

DISCONTINUED CABLE TELEVISION OPERATIONS

On July 6, 1995, the Company closed its sale of KBLCOM to Time Warner in a tax-deferred, stock-for-stock merger valued at approximately $2.4 billion. In anticipation of the sale, effective January 1, 1995, the operations of KBLCOM have been accounted for as discontinued and prior periods were restated for consistency in reflecting KBLCOM as a discontinued operation. The Company recorded a $90.6 million tax benefit in the first quarter of 1995 in recognition of the deferred tax asset arising from the Company's excess tax basis in KBLCOM stock. Based on a Time Warner common stock price of $43.25 on July 6, 1995, the Company will recognize in the third quarter of 1995 an additional after-tax gain estimated to be $690 million, which is subject to post closing adjustments. For additional information regarding the sale of KBLCOM, see the Company's Current Report on Form 8-K (File No. 1-7629) dated July 6, 1995, which is incorporated herein by reference. For a presentation of the Company's financial statements for the years 1992 through 1994 which reflects KBLCOM on a discontinued operations basis, reference is made to the Company's Consolidated Financial Statements contained in the Combined Form 8-K.

RESULTS OF OPERATIONS

COMPANY

Summary of selected financial data for the Company and its subsidiaries is set forth below:

	THREE MONTHS ENDED JUNE 30,		
	1995	1994	PERCENT CHANGE
		(Restated)	
	(Thousands of Dollars)		
Revenues	$ 978,225	$1,004,906	(3)
Operating Expenses	683,839	706,435	(3)
Operating Income	294,386	298,471	(1)
Interest and Other Charges	80,037	81,253	(1)
Income Taxes	65,709	76,654	(14)
Discontinued Operations		(7,583)	-
Net Income	133,260	126,725	5

	SIX MONTHS ENDED JUNE 30,		
	1995	1994	PERCENT CHANGE
		(Restated)	
	(Thousands of Dollars)		
Revenues	$1,724,391	$1,826,487	(6)
Operating Expenses	1,306,704	1,378,359	(5)
Operating Income	417,687	448,128	(7)
Interest and Other Charges	161,432	160,895	-
Income Taxes	76,136	99,306	(23)
Discontinued Operations	90,607	(15,084)	-
Net Income	247,716	152,623	62

The Company had consolidated earnings per share of $1.08 for the second quarter of 1995, compared to consolidated earnings per share of $1.03 for the second quarter of 1994. Consolidated earnings per share for the six months ended June 30, 1995 was $2.00 per share, compared to $1.25 per share for the same period in 1994. The increase in earnings for the six months ended June 30, 1995 is due to the recognition in the first quarter of 1995 of a $90.6 million tax benefit in recognition of the deferred tax asset arising from the Company's excess tax basis in KBLCOM stock, partially offset by the estimated effects of HL&P's Proposed Settlement which reduced operating income as discussed below. The Company's earnings per share for the six months ended June 30, 1995 would have been $1.27 per share without the tax benefit.

HL&P

Summary of selected financial data for HL&P is set forth below:

	THREE MONTHS ENDED JUNE 30,		
	1995	1994	PERCENT CHANGE
	(Thousands of Dollars)		
Revenues	$ 978,225	$1,004,906	(3)
Operating Expenses (1)	760,806	788,064	(3)
Operating Income (1)	217,419	216,842	-
Interest Charges	61,055	63,281	(4)
Income After Preferred Dividends	141,873	142,478	-

	SIX MONTHS ENDED JUNE 30,		
	1995	1994	PERCENT CHANGE
	(Thousands of Dollars)		
Revenues	$1,724,391	$1,826,487	(6)
Operating Expenses (1)	1,402,406	1,486,766	(6)
Operating Income (1)	321,985	339,721	(5)
Interest Charges	123,903	126,331	(2)
Income After Preferred Dividends	175,782	184,164	(5)

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(1) Inclusive of income taxes

In the second quarter and first six months of 1995, HL&P's pre-tax earnings were reduced by approximately $39 million and $56 million, respectively, which represents the estimated effects of the Proposed Settlement on revenues and expenses. For information regarding HL&P's current regulatory proceedings and the Proposed Settlement, see "CURRENT ISSUES - HL&P - Rate Review, Fuel Reconciliation and Other Proceedings" above and Note 3 to the Financial Statements in Item 1 of this Report.

OPERATING REVENUES AND SALES

Operating revenues decreased $26.7 million for the second quarter of 1995 and $102.1 million for the first six months of 1995, compared to the same periods in 1994. The decreases were primarily due to decreases in reconcilable fuel revenues of $49.9 million and $114.9 million, respectively, and the effects of the settlement-related rate reduction of $19.7 million and $33.6 million, respectively, for these same comparative periods. These decreases were partially offset by increases in kilowatt-hour (KWH) sales during the periods. For the second quarter and first six months of 1995, residential KWH sales increased 8% and 4%, respectively, compared to the same periods in 1994, while commercial KWH sales increased 4% and 5%, respectively, for the same periods. The increases in residential and commercial sales were due to growth in the number of customers and usage within these classes. Additionally, warmer weather experienced in the second quarter of 1995 compared to 1994 contributed to increased residential sales. Firm

industrial KWH sales decreased 4% and 3% for the second quarter and first six months of 1995, respectively, compared to the same periods in 1994. However, industrial base revenues for these periods were essentially flat due to the expiration in December 1994 of HL&P's discounted economic development tariff. Firm industrial sales exclude electricity sold at a reduced rate under agreements which allow HL&P to interrupt service under some circumstances.

FUEL AND PURCHASED POWER EXPENSES

Fuel expenses, while relatively unchanged for the second quarter, decreased $30.6 million for the first six months of 1995 compared to the same period of 1994. The decrease was primarily due to a decrease in the unit cost of gas and an increase in nuclear generation which has a per unit fuel cost that is substantially lower than HL&P's other fuel sources. The average cost of fuel for the second quarter and first six months of 1995 was $1.66 per million British Thermal Units (MMBtu) and $1.65 per MMBtu, respectively, compared to $1.63 per MMBtu and $1.71 per MMBtu for the same periods in 1994. Purchased power expense decreased $53.1 million and $86.0 million for the second quarter and first six months of 1995 when compared to the same period in 1994 primarily due to the expiration of firm purchased power contracts.

OPERATION AND MAINTENANCE, DEPRECIATION AND AMORTIZATION, AND OTHER

Operation and maintenance expense for the second quarter and first six months of 1995 increased $13.6 million and $18.2 million, respectively, compared to the same periods in 1994. Substantially all of the increase in operation and maintenance expense resulted from a lump sum wage increase under a union contract and increased litigation expenses. Depreciation and amortization expense for the second quarter and first six months of 1995 increased $12.3 million and $17.3 million, respectively, compared to 1994, primarily due to an increase in depreciable property and increases recorded as a result of the Proposed Settlement (see "CURRENT ISSUES - HL&P - Rate Review, Fuel Reconciliation and Other Proceedings" above and Note 3 to the Financial Statements in Item 1 of this Report). Other taxes increased $9.5 million in the first six months of 1995 compared to the same period in 1994, primarily due to increased state franchise tax obligations. Substantially all of the increase in the loss attributable to other-net was the one-time, pre-tax charge of $9 million incurred in connection with certain mine-related costs which were not previously recorded and are not recoverable under the terms of the Proposed Settlement.

LIQUIDITY AND CAPITAL RESOURCES

COMPANY

GENERAL

The Company's cash requirements stem primarily from operating expenses, capital expenditures, payment of common stock dividends, payment of preferred stock dividends and interest and principal payments on debt. Net cash provided by operating activities totaled $344.1 million for the six months ended June 30, 1995.

Net cash used in investing activities for the six months ended June 30, 1995, totaled $257.0 million, primarily due to electric capital expenditures of $133.2 million (including allowance for borrowed

funds used during construction), corporate headquarters expenditures (including capitalized interest) of $56.9 million and discontinued cable television operations expenditures of $47.0 million.

Financing activities for the first six months of 1995 resulted in a net cash outflow of $59.9 million. The Company's primary financing activities were the increase in short-term borrowings offset by the payment of dividends, the redemption of preferred stock and the extinguishment and repayment of long-term debt. For information with respect to these matters, reference is made to Notes 7, 8, and 10 to the Financial Statements in Item 1 of this Report.

SOURCES OF CAPITAL RESOURCES AND LIQUIDITY

The Company has registered with the Securities and Exchange Commission (SEC) $250 million of debt securities which remain unissued. Proceeds from any sales of these securities are expected to be used for general corporate purposes including investments in and loans to subsidiaries.

The Company also has registered with the SEC five million shares of its common stock. Proceeds from the sale of these securities will be used for general corporate purposes, including, but not limited to, the redemption, repayment or retirement of outstanding indebtedness of the Company or the advance or contribution of funds to one or more of the Company's subsidiaries to be used for their general corporate purposes, including, without limitation, the redemption, repayment or retirement of indebtedness or preferred stock.

The Company's outstanding commercial paper at June 30, 1995 was approximately $698.2 million, which is supported by an $800 million bank credit facility.

On July 6, 1995, the Company closed its sale of KBLCOM to Time Warner in a tax-deferred, stock-for-stock merger. In exchange for KBLCOM's common stock, Time Warner issued to the Company one million shares of its common stock and 11 million shares of a newly-issued series of its convertible preferred stock. Such securities were valued at approximately $1.1 billion based, in part, on the closing price of Time Warner common stock on July 6 ($43.25 per share). In addition, Time Warner purchased from the Company for cash approximately $621 million of KBLCOM's outstanding intercompany indebtedness and assumed approximately $650 million of KBLCOM's external debt and other liabilities. The preferred stock is convertible into approximately 22.9 million shares of Time Warner common stock. Until the earlier of conversion or July 6, 1999, the terms of the preferred stock provide for the payment of an annual dividend of at least $3.75 per share. After four years, Time Warner will have the right to exchange the preferred stock for common stock at the stated conversion rate. After five

years, Time Warner will have the right to redeem all or part of the preferred stock at its liquidation preference of $100 per share, plus accrued and unpaid dividends thereon to the date fixed for redemption. The Company believes that the transaction will improve its liquidity by exchanging the Company's investment in KBLCOM for cash and marketable securities. For more information concerning the sale, see the Company's Current Report on Form 8-K dated July 6, 1995, which is incorporated herein by reference.

The Company recorded a $90.6 million tax benefit in the first quarter of 1995 in recognition of the deferred tax asset arising from the Company's excess tax basis in KBLCOM stock. Based, in part, on a Time Warner common stock price of $43.25 on July 6, 1995, the Company will recognize in

the third quarter of 1995 an additional after-tax gain estimated to be $690 million, which is subject to post closing adjustments.

In accordance with SFAS No. 115, "Accounting for Certain Investments in Debt and Equity Securities," the Time Warner stock will be classified as "available-for-sale securities" and recorded by the Company at fair value. Unrealized holding gains and losses will be excluded from earnings and reported as a component of shareholders' equity until the securities are sold.

The $621 million of proceeds received in connection with the sale of KBLCOM has initially been used to retire short-term indebtedness of the Company under its commercial paper program. It is anticipated that the proceeds ultimately will be used for general corporate purposes, including but not limited to the redemption of or retirement of indebtedness of the Company, the advance or contribution of funds to one or more subsidiaries to be used for their general corporate purposes or (depending on market and other conditions) the possible repurchase of outstanding shares of the Company's common stock.

In June 1995, a subsidiary of HI Energy, the Company's non-regulated electric power subsidiary, entered into an agreement to construct, own and operate a 160 MW cogeneration facility to be built adjacent to a steel plant in San Nicolas, Argentina. The projected completion date for the project is October 15, 1997. The plant is to be constructed by a consortium composed of GE Power Systems, Inc. and an Argentine construction company. The construction contract provides, subject to certain adjustments, for a contract price of approximately $65 million to be paid in installments during the construction of the project. Upon completion, the project will sell steam to the steel plant and sell electricity on the wholesale Argentina electricity market. The project is subject to the satisfaction of certain conditions precedent, prior to September 15, 1995, including the obtaining of required regulatory permits and an exemption from certain Argentine customs duties.

RATIOS OF EARNINGS TO FIXED CHARGES

The Company's ratios of earnings to fixed charges for the six and twelve months ended June 30, 1995 were 2.34 and 2.77, respectively. The Company believes that the ratio for the six-month period is not necessarily indicative of the ratio for a twelve-month period due to the seasonal nature of HL&P's business.

HL&P

GENERAL

HL&P's cash requirements stem primarily from operating expenses, capital expenditures, payment of dividends and interest and principal payments on debt. HL&P's net cash provided by operating activities for the first six months of 1995 totaled $374.6 million.

Net cash used in HL&P's investing activities for the first six months of 1995 totaled $225.1 million. HL&P's capital and nuclear fuel expenditures (excluding allowance for funds used during construction) for the first six months of 1995 totaled $215.2 million out of the $449 million revised

annual budget. HL&P expects to finance substantially all of its 1995 capital expenditures through funds generated internally from operations.

HL&P's financing activities for the first six months of 1995 resulted in a net cash outflow of approximately $291.0 million. Included in these activities were the payment of dividends, the redemption of preferred stock, and the extinguishment of long-term debt. For information with respect to these matters, reference is made to Notes 7 and 8 to the Financial Statements in Item 1 of this Report.

SOURCES OF CAPITAL RESOURCES AND LIQUIDITY

HL&P has registered with the SEC $230 million aggregate liquidation value of preferred stock and $580 million aggregate principal amount of debt securities that may be issued as first mortgage bonds and/or as debt securities collateralized by first mortgage bonds. Proceeds from any sale of these securities are expected to be used for general corporate purposes including the purchase, redemption (to the extent permitted by the terms of the outstanding securities), repayment or retirement of outstanding indebtedness or preferred stock of HL&P.

At June 30, 1995, HL&P had approximately $94 million in cash and cash equivalents invested in short-term investments. In addition, HL&P has a commercial paper program supported by a bank credit facility of $400 million. HL&P had no commercial paper outstanding at June 30, 1995.

RATIOS OF EARNINGS TO FIXED CHARGES

HL&P's ratios of earnings to fixed charges for the six and twelve months ended June 30, 1995 were 3.17 and 3.70, respectively. HL&P's ratios of earnings to fixed charges and preferred dividends for the six and twelve months ended June 30, 1995, were 2.67 and 3.12, respectively. HL&P believes that the ratios for the six-month period are not necessarily indicative of the ratios for a twelve-month period due to the seasonal nature of its business.

NEW ACCOUNTING PRONOUNCEMENTS

In October 1994, the Financial Accounting Standards Board (FASB) issued SFAS No. 119, "Disclosure about Derivative Financial Instruments and Fair Value of Financial Instruments," effective for fiscal years ending after December 15, 1994. SFAS No. 119 extends current disclosure practices set forth in SFAS No. 105 "Disclosure of Information about Financial Instruments with Off-Balance-Sheet Risk and Financial Instruments with Concentrations of Credit Risk" and SFAS No. 107 "Disclosures about Fair Value of Financial Instruments." SFAS No. 119 requires companies to disclose information about the amounts, nature and terms for all derivative financial instruments not within the scope of SFAS No. 105. The Company and HL&P adopted SFAS No. 119 with no effect on the Company or HL&P's financial condition or results of operations.

In March 1995, FASB issued SFAS No. 121, "Accounting for the Impairment of Long-Lived Assets and for Long-Lived Assets to Be Disposed Of." This accounting standard, effective for fiscal years beginning after December 15, 1995, requires companies to review certain assets for impairment whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable (such determination generally being made on the basis of whether net cash

flows expected to result from such assets will recover the carrying amount of the assets). If an impairment is found to exist, the impairment loss to be recognized is the amount by which the carrying amount exceeds the fair value. The Company and HL&P are currently reviewing the provisions of SFAS No. 121, but, based on current estimates, the Company and HL&P do not expect the adoption of SFAS No. 121 to have a material impact on the Company's or HL&P's financial condition or results of operations.

PART II. OTHER INFORMATION

ITEM 1. LEGAL PROCEEDINGS.

For a description of legal proceedings affecting the Company and its subsidiaries, including HL&P, reference is made to the information set forth in Item 3 of the 1994 Combined Form 10-K, Item 1 of Part II of the Combined Form 10-Q, Notes 2, 3 and 4 to the Company's Consolidated and HL&P's Financial Statements in the Combined Form 8-K and Notes 2(b) and 3 to the Company's Consolidated and HL&P's Financial Statements in the Combined Form 10-Q, which information, as qualified and updated by the description of developments in regulatory and litigation matters contained in Notes 2, 3 and 4 of the Notes to the Financial Statements included in Part I of this Report, is incorporated herein by reference.

GULF STATES UTILITIES CO. V. HOUSTON LIGHTING & POWER CO., ET AL., formerly pending in the United States District Court for the Southern District of Texas, Houston Division, was dismissed upon joint stipulation of all the parties in June 1995. Under the terms of the Agreement of Compromise and Settlement, HL&P bears its own fees, costs and expenses, but is not required to pay any other amounts.

ITEM 6. EXHIBITS AND REPORTS ON FORM 8-K.

(a) Exhibits.

HOUSTON INDUSTRIES INCORPORATED:

Exhibit 10(a) - Sixth Amendment to the Houston Industries Incorporated Executive Incentive Compensation Plan (As Amended and Restated Effective January 1, 1991), Effective August 1, 1995.

Exhibit 10(b) - Sixth Amendment to the Houston Industries Incorporated Deferred Compensation Plan (As Amended and Restated Effective January 1, 1991), Effective August 1, 1995.

Exhibit 10(c) - Fifth Amendment to the Houston Industries Incorporated Deferred Compensation Plan (As Amended and Restated Effective January 1, 1989), Effective August 1, 1995.

Exhibit 10(d) - Fifth Amendment to the Houston Industries Incorporated Deferred Compensation Plan (As Established Effective September 1, 1985), Effective August 1, 1995.

Exhibit 10(e) - First Amendment to Houston Industries Incorporated Executive Life Insurance Plan (Effective January 1, 1994), Executed June 16, 1995.

Exhibit 11 - Computation of Earnings per Common Share and Common Equivalent Share.

Exhibit 12 - Computation of Ratios of Earnings to Fixed Charges.

Exhibit 27 - Financial Data Schedule.

Exhibit 99(a) - Notes 1(a), 1(f), 2, 3, 4 and 5 to the Company's Consolidated Financial Statements included on pages 39 through 67 of the Combined Form 8-K.

Exhibit 99(b) - Notes 2, 3, and 4 to the Company's Consolidated and HL&P's Financial Statements included on pages 71 through 81 of the 1994 Combined Form 10-K.

Exhibit 99(c) - Notes 2(b), 3 and 9 to the Company's Consolidated and HL&P's Financial Statements included on pages 14 through 18 and 22 of the Combined Form 10-Q.

Exhibit 99(d) - Part I, Item 3 - Legal Proceedings included on pages 31 through 32 of the 1994 Combined Form 10-K.

Exhibit 99(e) - Part II, Item 1 - Legal Proceedings included on page 32 of the Combined Form 10-Q.

Exhibit 99(f) - Part I, Item 1 - Business of HL&P - Competition and Regulation of the Company - Federal included on pages 5 through 7 and 26 of the 1994 Combined Form 10-K.

Exhibit 99(g) - First Amendment to the Houston Industries Incorporated Savings Plan (As Amended and Restated Effective July 1, 1995), Effective June 30, 1995.

HOUSTON LIGHTING & POWER COMPANY:

Exhibit 12 - Computation of Ratios of Earnings to Fixed Charges and Ratios of Earnings to Fixed Charges and Preferred Dividends.

Exhibit 27 - Financial Data Schedule.

Exhibit 99(a) - Notes 1(f), 2, 3, 4 and 5 to the Company's Consolidated Financial Statements included on pages 39 through 50 of the Combined Form 8-K.

Exhibit 99(b) - Notes 2, 3 and 4 to the Company's Consolidated and HL&P's Financial Statements included on pages 71 through 81 of the 1994 Combined Form 10-K.

Exhibit 99(c) - Notes 2(b), 3 and 9 to the Company's Consolidated and HL&P's Financial Statements included on pages 14 through 18 and 22 of the Combined Form 10-Q.

Exhibit 99(d) - Part I, Item 3 - Legal Proceedings included on pages 31 through 32 of the 1994 Combined Form 10-K.

Exhibit 99(e) - Part II, Item 1 - Legal Proceedings included on page 32 of the Combined Form 10-Q.

Exhibit 99(f) - Part I, Item 1 - Business of HL&P - Competition and Regulation of the Company - Federal included on pages 5 through 7 and 26 of the 1994 Combined Form 10-K.

(b) Reports on Form 8-K.

HOUSTON INDUSTRIES INCORPORATED:

Current Report on Form 8-K dated July 6, 1995 (Item 2. Acquisition or Disposition of Assets).

HOUSTON INDUSTRIES INCORPORATED AND HOUSTON LIGHTING & POWER COMPANY:

Current Report on Form 8-K dated May 12, 1995 (Item 5. Other Events).

SIGNATURE

Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

HOUSTON INDUSTRIES INCORPORATED
(Registrant)

/s/ MARY P. RICCIARDELLO
Mary P. Ricciardello
Comptroller and
Principal Accounting Officer

Date: August ___, 1995

SIGNATURE

Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

HOUSTON LIGHTING & POWER COMPANY
(Registrant)

/s/ KEN W. NABORS
Ken W. Nabors
Vice President and Comptroller
and Principal Accounting Officer

Date: August ____, 1995

EXHIBIT 10(a)

HOUSTON INDUSTRIES INCORPORATED
EXECUTIVE INCENTIVE COMPENSATION PLAN

(As Amended and Restated Effective January 1, 1991)

SIXTH AMENDMENT

Houston Industries Incorporated, a Texas corporation (the "Company"), having amended and restated the Houston Industries Incorporated Executive Incentive Compensation Plan, effective January 1, 1991 (the "Plan"), and having reserved the right under Section 18 thereof to amend the Plan, does hereby amend Section 10 of the Plan by adding a new paragraph (H) thereto, effective August 1, 1995, to read as follows:

"(H) TERMINATIONS UNDER 1995 PROGRAM. Notwithstanding anything herein to the contrary, if a Participant fulfills the requirements for the Voluntary Early Pension for 1995 Program participants under Section 9.7(a) of the Houston Industries Incorporated Retirement Plan, the Participant shall be deemed to have completed the applicable Forfeiture Period with respect to the contingent portion of his Annual Award granted with respect to the 1991 Plan Year, if any. The Award vested pursuant to this Paragraph shall be paid in a lump sum as soon as practicable following January 1, 1996 (or the January 1 following actual termination, if later) unless otherwise elected by the Participant pursuant to Section 10.D. Such terminated Participants are not entitled to any Long-Term Awards payable after June 30, 1995 under the Plan."

IN WITNESS WHEREOF, Houston Industries Incorporated has caused these presents to be executed by its duly authorized officer in a number of copies, all of which shall

constitute one and the same instrument, which may be sufficiently evidenced by any executed copy hereof, this 18th day of May, 1995, but effective as of the date stated herein.

HOUSTON INDUSTRIES INCORPORATED

By /s/ D. D. SYKORA
D. D. Sykora
President and Chief
Operating Officer

ATTEST:

/s/ RICHARD B. DAUPHIN
Richard B. Dauphin
Assistant Corporate Secretary

EXHIBIT 10(b)

HOUSTON INDUSTRIES INCORPORATED
DEFERRED COMPENSATION PLAN

(As Amended and Restated Effective January 1, 1991)

SIXTH AMENDMENT

Houston Industries Incorporated, a Texas corporation (the "Company"), having amended and restated the Houston Industries Incorporated Deferred Compensation Plan, effective January 1, 1991 (the "Plan"), and having reserved the right under Section 7.1 thereof to amend the Plan, does hereby amend Article V of the Plan by adding the following Section 5.8 thereto, effective August 1, 1995:

"5.8 TERMINATIONS UNDER THE 1995 VOLUNTARY EARLY RETIREMENT PROGRAM.

(a) PRIOR TO EARLY RETIREMENT DATE. Notwithstanding any other provision of the Plan to the contrary, if the employment of a Participant who fulfills the requirements for the Voluntary Early Pension for 1995 Program participants under Section 9.7(a) of the Houston Industries Incorporated Retirement Plan is terminated prior to the first day of the month coincident with or next following the date of the Participant's 60th birthday, a Normal Retirement Distribution as described in Section 5.1 or a distribution as described in Section 5.4 shall not be made, but the Employer (x) shall pay the Participant the sum or sums of Compensation actually deferred, with interest thereon, compounded annually, at the applicable Interest Crediting Rate for each Participation Year, from the Commencement Date through the date of payment, minus any Early Distributions, (y) shall make a lump sum distribution or 15 annual installment payments in accordance with the Participant's election under Section 5.1(b) and, if payable in a lump sum, in the January following the Participant's termination of employment or, if payable in installments, commencing the month following the month in which the Participant terminates employment and payable thereafter in that same month in each remaining year, and (z) shall not make any Early Distributions to such Participant.

(b) AFTER EARLY RETIREMENT DATE. If the employment of a Participant is terminated voluntarily as described in subsection (a) above but after the first day of the month

coincident with or next following the date of the Participant's 60th birthday, distributions (including Early Distributions) shall be made as otherwise provided in this Article V.

(c) COMMUTATION. Any installment payments hereunder may be commuted as provided in Section 5.1(e)."

IN WITNESS WHEREOF, Houston Industries Incorporated has caused these presents to be executed by its duly authorized officer in a number of copies, all of which shall constitute one and the same instrument, which may be sufficiently evidenced by any executed copy hereof, this 18th day of May, 1995, but effective as of the date stated herein.

HOUSTON INDUSTRIES INCORPORATED

By /s/ D. D. SYKORA
D. D. Sykora
President and Chief
Operating Officer

ATTEST:

/s/ RICHARD B. DAUPHIN
Richard B. Dauphin
Assistant Corporate Secretary

EXHIBIT 10(c)

HOUSTON INDUSTRIES INCORPORATED
DEFERRED COMPENSATION PLAN

(As Amended and Restated Effective January 1, 1989)

FIFTH AMENDMENT

Houston Industries Incorporated, a Texas corporation (the "Company"), having amended and restated the Houston Industries Incorporated Deferred Compensation Plan, effective January 1, 1989 (the "Plan"), and having reserved the right under Section 7.1 thereof to amend the Plan, does hereby amend the Plan, effective August 1, 1995, as follows:

1. Section 5.1(f) of the Plan is hereby amended to read as follows:

"(f) Any installment benefits, at the request of the Participant and in the sole discretion of the Committee, may be commuted to a lump-sum payment or may be paid over a shorter period of time, with interest accrued to such date at the applicable Interest Crediting Rate."

2. Section 5.2(c) of the Plan is hereby amended to read as follows:

"(c) Any installment death benefits, at the request of the Beneficiary and in the sole discretion of the Committee, may be commuted to a lump-sum payment or may be paid over a shorter period of time, with interest accrued to such date at the applicable Interest Crediting Rate."

3. The second sentence of Section 5.3 of the Plan is hereby amended to read as follows:

"The benefits payable to such Participant under the Plan shall be paid in the amounts and at the times otherwise provided in Section 5.1, all in accordance with the Participant's initial election under Section 3.3, except that at the request of the Participant and in the sole discretion of the Committee any such payments may be commuted to a lump-sum payment or may be paid over a shorter period of time, with interest accrued to such date at the applicable Interest Crediting Rate."

4. Article V of the Plan is hereby amended by adding the following Section 5.8 thereto:

"5.8 TERMINATIONS UNDER THE 1995 VOLUNTARY EARLY RETIREMENT PROGRAM.

(a) PRIOR TO EARLY RETIREMENT DATE. Notwithstanding any other provision of the Plan to the contrary, if the employment of a Participant who fulfills the requirements for the Voluntary Early Pension for 1995 Program participants under Section 9.7(a) of the Houston Industries Incorporated Retirement Plan is terminated prior to the first day of the month coincident with or next following the date of the Participant's 60th birthday, a Normal Retirement Distribution as described in Section 5.1 or a distribution as described in Section 5.4 shall not be made, but the Employer (x) shall pay the Participant the sum or sums of Compensation actually deferred, with interest thereon, compounded annually, at the applicable Interest Crediting Rate for each Participation Year, from the Commencement Date through the date of payment, minus any Early Distributions, (y) shall make a lump-sum distribution or 15 annual installment payments in accordance with the Participant's election under Section 5.1(b) and, if payable in a lump sum, in the January following the Participant's termination of employment or, if payable in installments, commencing the month following the month in which the Participant terminates employment and payable thereafter in that same month in each remaining year, and (z) shall not make any Early Distributions to such Participant.

(b) AFTER EARLY RETIREMENT DATE. If the employment of a Participant is terminated voluntarily as described in subsection (a) above but after the first day of the month coincident with or next following the date of the Participant's 60th birthday, distributions (including Early Distributions) shall be made as otherwise provided in this Article V.

(c) COMMUTATION. Any installment payments hereunder may be commuted as provided in Section 5.1(e)."

IN WITNESS WHEREOF, Houston Industries Incorporated has caused these presents to be executed by its duly authorized officer in a number of copies, all of which shall

constitute one and the same instrument, which may be sufficiently evidenced by any executed copy hereof, this 18th day of May, 1995, but effective as of the date stated herein.

HOUSTON INDUSTRIES INCORPORATED

By /s/ D. D. SYKORA
D. D. Sykora
President and Chief
Operating Officer

ATTEST:

/s/ RICHARD B. DAUPHIN
Richard B. Dauphin
Assistant Corporate Secretary

EXHIBIT 10(d)

HOUSTON INDUSTRIES INCORPORATED
DEFERRED COMPENSATION PLAN

(As Established September 1, 1985)

FIFTH AMENDMENT

Houston Industries Incorporated, a Texas corporation (the "Company"), having established the Houston Industries Incorporated Deferred Compensation Plan, effective September 1, 1985 (the "Plan"), and having reserved the right under Section 7.1 thereof to amend the Plan, does hereby amend Article Five of the Plan by adding the following Section 5.8 thereto, effective August 1, 1995:

"5.8 TERMINATIONS UNDER THE 1995 VOLUNTARY EARLY RETIREMENT PROGRAM.

(a) PRIOR TO EARLY RETIREMENT DATE. Notwithstanding any other provision of the Plan to the contrary, if the employment of a Participant who fulfills the requirements for the Voluntary Early Pension for 1995 Program participants under Section 9.7(a) of the Houston Industries Incorporated Retirement Plan is terminated prior to the first day of the month coincident with or next following the date of the Participant's 60th birthday, distribution shall not be made as described in Section 5.1(a)-(c), but the Employer (x) shall pay the Participant the sum or sums of Compensation actually deferred, with interest thereon, compounded annually, at the applicable interest rate specified in the Participant's Agreement for each Participation Year, from the Commencement Date through the date of payment, (y) shall pay such amount in 15 annual installment payments, commencing the first day of the month following the month in which the Participant terminates employment and payable thereafter in that same month in each remaining year, and (z) shall not pay any equal annual installments (as described in Section 5.1(a)-(b)) to such Participant.

(b) AFTER EARLY RETIREMENT DATE. If the employment of a Participant is terminated voluntarily as described in subsection (a) above but after the Participant's Early Retirement Date, distributions (including the equal annual installments) shall be made as otherwise provided in this Article Five.

(c) COMMUTATION. Any installment payments hereunder may be commuted as provided in Section 5.1(e)."

IN WITNESS WHEREOF, Houston Industries Incorporated has caused these presents to be executed by its duly authorized officer in a number of copies, all of which shall constitute one and the same instrument, which may be sufficiently evidenced by any executed copy hereof, this 18th day of May, 1995, but effective as of the date stated herein.

HOUSTON INDUSTRIES INCORPORATED

By /s/ D. D. SYKORA
D. D. Sykora
President and Chief
Operating Officer

ATTEST:

/s/ RICHARD B. DAUPHIN
Richard B. Dauphin
Assistant Corporate Secretary

Exhibit 10(e)

HOUSTON INDUSTRIES INCORPORATED
EXECUTIVE LIFE INSURANCE PLAN

(Effective January 1, 1994)

FIRST AMENDMENT

The Benefits Committee of Houston Industries Incorporated, a Texas corporation, having been delegated the right under Section 6.2 of the Houston Industries Incorporated Executive Life Insurance Plan, effective January 1, 1994 (the "Plan"), to amend the Plan in certain respects, does hereby amend the Plan, effective as of January 1, 1994, as follows:

1. Section 4.5 is hereby amended by adding the following sentence at the end of that Section:

> "Notwithstanding the foregoing, a Benefit Owner may irrevocably assign its right to purchase all ownership rights in the Insurance Contract pursuant to this Section 4.5 by a signed writing delivered to the Committee prior to the termination of the Participant's employment with the Company. The `signed writing' as contemplated in this paragraph shall be in such form as may be prescribed by the Committee from time to time."

2. Section 8.1 is hereby amended to read in its entirety as follows:

> "8.1 Except as provided in Sections 4.4 and 4.5 of this Plan, no benefit under the Plan shall be subject in any manner to anticipation, alienation, sale, transfer, assignment, pledge, encumbrance or charge, except by will, or the laws of descent and distribution, and any attempt thereat shall be void. No such benefit shall, prior to receipt thereof, be in any manner liable for or subject to the debts, contracts, liabilities, engagements or torts of any Participant, Benefit Owner, or Beneficiary."

IN WITNESS WHEREOF, the Benefits Committee of Houston Industries Incorporated has caused these presents to be executed by its duly authorized officer in a number of copies, all of which shall constitute one and the same instrument, which may be

sufficiently evidenced by any executed copy hereof, this 16th day of June, 1995, but effective as of January 1, 1994.

BENEFITS COMMITTEE OF HOUSTON
INDUSTRIES INCORPORATED

By /s/ D. D. SYKORA
D. D. Sykora
Chairman

ATTEST:

/s/ RICHARD B. DAUPHIN
Richard B. Dauphin
Assistant Corporate Secretary

Exhibit 11

HOUSTON INDUSTRIES INCORPORATED AND SUBSIDIARIES

COMPUTATION OF EARNINGS PER COMMON SHARE
AND COMMON EQUIVALENT SHARE
(THOUSANDS OF DOLLARS, EXCEPT PER SHARE AMOUNTS)

		THREE MONTHS ENDED JUNE 30,		SIX MONTHS ENDED JUNE 30,	
		1995	1994	1995	1994
Primary Earnings Per Share:					
(1)	Weighted average shares of common stock outstanding.....	123,769,249	122,507,671	123,684,286	122,464,654
(2)	Effect of issuance of shares from assumed exercise of stock options (treasury stock method).....	(4,633)	(66,344)	(12,095)	(42,705)
(3)	Weighted average shares.....	123,764,616	122,441,327	123,672,191	122,421,949
(4)	Net income.....	$ 133,260	$ 126,725	$ 247,716	$ 152,623
(5)	Primary earnings per share (line 4/line 3).....	$ 1.08	$ 1.03	$ 2.00	$ 1.25
Fully Diluted Earnings Per Share:					
(6)	Weighted average shares per computation on line 3 above.....	123,764,616	122,441,327	123,672,191	122,421,949
(7)	Shares applicable to options included on line 2 above.....	4,633	66,344	12,095	42,705
(8)	Dilutive effect of stock options based on the average price for the period or period-end price, whichever is higher, of $42.13 and $33.63 for the second quarter of 1995 and 1994, respectively, and $42.13 and $37.06 for the first six months of 1995 and 1994, respectively. (treasury stock method).....	(1,364)	(66,344)	(1,364)	(42,705)
(9)	Weighted average shares.....	123,767,885	122,441,327	123,682,922	122,421,949
(10)	Net income.....	$ 133,260	$ 126,725	$ 247,716	$ 152,623
(11)	Fully diluted earnings per share (line 10/line 9).....	$ 1.08	$ 1.03	$ 2.00	$ 1.25

Notes:

These calculations are submitted in accordance with Regulation S-K item 601(b) (11) although it is not required for financial presentation disclosure per footnote 2 to paragraph 14 of Accounting Principles Board (APB) Opinion No. 15 because it does not meet the 3% dilutive test.

The calculations for the quarters and six months ended June 30, 1995 and 1994 are submitted in accordance with Regulation S-K item 601(b) (11) although they are contrary to paragraphs 30 and 40 of APB No. 15 because they produce anti-dilutive results.

EXHIBIT 12

HOUSTON INDUSTRIES INCORPORATED AND SUBSIDIARIES
COMPUTATION OF RATIOS OF EARNINGS TO FIXED CHARGES
(THOUSANDS OF DOLLARS)

		SIX MONTHS ENDED JUNE 30, 1995	TWELVE MONTHS ENDED JUNE 30, 1995
Fixed Charges as Defined:			
(1)	Interest on Long-Term Debt	$ 129,258	$ 261,751
(2)	Other Interest	18,677	30,718
(3)	Preferred Dividends Factor of Subsidiary	24,324	50,346
(4)	Interest Component of Rentals Charged to Operating Expense	1,926	3,967
(5)	Total Fixed Charges	$ 174,185	$ 346,782
Earnings as Defined:			
(6)	Income from Continuing Operations Before Cumulative Effect of Change in Accounting	$ 157,109	$ 405,187
(7)	Income Taxes for Continuing Operations Before Cumulative Effect of Change in Accounting	76,136	207,254
(8)	Total Fixed Charges (line 5)	174,185	346,782
(9)	Income from Continuing Operations Before Cumulative Effect of Change in Accounting, Income Taxes and Fixed Charges	$ 407,430	$ 959,223
Preferred Dividends Factor of Subsidiary:			
(10)	Preferred Stock Dividends of Subsidiary	$ 16,435	$ 33,342
(11)	Ratio of Pre-Tax Income from Continuing Operations to Income from Continuing Operations (line 6 plus line 7 divided by line 6)	1.48	1.51
(12)	Preferred Dividends Factor of Subsidiary (line 10 times line 11)	$ 24,324	$ 50,346
Ratio of Earnings to Fixed Charges (line 9 divided by line 5)		2.34	2.77

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THIS SCHEDULE CONTAINS SUMMARY FINANCIAL INFORMATION EXTRACTED FROM THE COMPANY'S AND HL&P'S FINANCIAL STATEMENTS AND IS QUALIFIED IN ITS ENTIRETY BY REFERENCE TO SUCH FINANCIAL STATEMENTS.

0000202131
HOUSTON INDUSTRIES
1000
6-MOS
DEC-31-1995
JUN-30-1995
PER-BOOK
8,989,667
86,005
340,169
1,408,845
701,330
11,526,016
2,160,356
0
1,283,326
3,443,682
51,055
351,345
3,556,770
0
0
698,165
150,144
25,700
6,909
3,616
3,238,630
11,526,016
1,724,391
76,136
1,306,704
1,306,704
417,687
(23,010)
394,677
144,997
264,151
16,435
247,716
185,611
122,878
344,066
$2.00
$2.00

Total annual interest charges on all bonds for year-to-date 6/30/95.

(1) SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

(a) SYSTEM OF ACCOUNTS AND EFFECTS OF REGULATION. The accounting records of Houston Lighting & Power Company (HL&P), the principal subsidiary of Houston Industries Incorporated (Company), are maintained in accordance with the Federal Energy Regulatory Commission's (FERC) Uniform System of Accounts. HL&P's accounting practices are subject to regulation by the Public Utility Commission of Texas (Utility Commission), which has adopted the FERC system of accounts.

As a result of Utility Commission regulation, HL&P follows the accounting set forth in Statement of Financial Accounting Standards (SFAS) No. 71 "Accounting for the Effects of Certain Types of Regulation". This statement requires a rate-regulated entity to reflect the effects of regulatory decisions in its financial statements. In accordance with the statement, the Company has deferred certain costs pursuant to rate actions of the Utility Commission and is recovering or expects to recover such costs in electric rates charged to customers. The regulatory assets are included in plant held for future use and other assets on the Company's Consolidated and HL&P's Balance Sheets. The regulatory liabilities are included in deferred credits on the Company's Consolidated and HL&P's Balance Sheets. In the event the Company is no longer able to apply SFAS No. 71 due to future changes in regulation or competition, the Company's ability to recover these assets and/or liabilities may not be assured. Following are significant regulatory assets and liabilities:

	December 31, 1994
	(Millions of Dollars)
Deferred plant costs - net	$ 639
Malakoff Electric Generating Station (Malakoff) investment	252
Regulatory tax asset - net	235
Unamortized loss on reacquired debt	117
Deferred debits	105
Unamortized investment tax credit	(412)
Accumulated deferred income taxes - regulatory tax asset	(82)

(f) DEFERRED PLANT COSTS. The Utility Commission authorized deferred accounting treatment for certain costs related to the South Texas Project Electric Generating Station (South Texas Project) in two contexts. The first was "deferred accounting" where HL&P was permitted to continue to accrue carrying costs in the form of AFUDC and defer and capitalize depreciation and other operating costs on its investment in the South Texas Project until such costs were reflected in rates. The second was the "qualified phase-in plan" where HL&P was permitted to capitalize as deferred charges allowable costs, including return, deferred for future recovery under the approved plan. The accumulated deferrals for "deferred accounting" and "qualified phase-in plan" are being recovered over the estimated depreciable life of the South Texas Project and within the ten year phase-in period, respectively. The amortization of these deferrals totaled $25.8 million for each of the years 1994, 1993, and 1992 and is included on the Company's Statements of Consolidated Income and HL&P's Statements of Income in depreciation and amortization expense. Under the terms of the settlement agreement regarding the issues raised in Docket Nos. 12065 and 13126 (Proposed Settlement), see Note 3, the South Texas Project deferrals will continue to be amortized using the schedules discussed above.

(2) JOINTLY-OWNED NUCLEAR PLANT

(a) HL&P INVESTMENT. HL&P is the project manager (and one of four co-owners) of the South Texas Project, which consists of two 1,250 megawatt nuclear generating units. HL&P has a 30.8 percent interest in the project and bears a corresponding share of capital and operating costs associated with the project. As of December 31, 1994, HL&P's investments (net of accumulated depreciation and amortization) in the South Texas Project and in nuclear fuel, including AFUDC, were $2.1 billion and $99 million, respectively.

(b) UNITED STATES NUCLEAR REGULATORY COMMISSION (NRC) INSPECTIONS AND OPERATIONS. Both generating units at the South Texas Project were out of service from February 1993 to February 1994, when Unit No. 1 was returned to service. Unit No. 2 was returned to service in May 1994. HL&P removed the units from service in February 1993 when a problem

was encountered with certain of the units' auxiliary feedwater pumps.

In February 1995, the NRC removed the South Texas Project from its "watch list" of plants with weaknesses that warranted increased NRC attention. The NRC placed the South Texas Project on the "watch list" in June 1993, following the issuance of a report by an NRC Diagnostic Evaluation Team (DET) which conducted a review of the South Texas Project operations.

Certain current and former employees of HL&P or contractors of HL&P have asserted claims that their employment was terminated or disrupted in retaliation for their having made safetyrelated complaints to the NRC. Civil proceedings by the complaining personnel and administrative proceedings by the Department of Labor remain pending against HL&P, and the NRC has jurisdiction to take enforcement action against HL&P and/or individual employees with respect to these matters. Based on its own internal investigation, in October 1994 the NRC issued a notice of violation and proposed a $100,000 civil penalty against HL&P in one such case in which HL&P had terminated the site access of a former contractor employee. In that action, the NRC also requested information relating to possible further enforcement action in this matter against two HL&P managers involved in such termination. HL&P strongly disagrees with the NRC's conclusions, and has requested the NRC to give further consideration of its notice. In February 1995, the NRC conducted an enforcement conference with respect to that matter, but no result has been received.

HL&P has provided documents and other assistance to a subcommittee of the U. S. House of Representatives (Subcommittee) that is conducting an inquiry related to the South Texas Project. Although the precise focus and timing of the inquiry has not been identified by the Subcommittee, it is anticipated that the Subcommittee will inquire into matters related to HL&P's handling of employee concerns and to issues related to the NRC's 1993 DET review of the South Texas Project. In connection with that inquiry, HL&P has been advised that the U. S. General Accounting Office (GAO) is conducting a review of the NRC's inspection process as it relates to the South Texas Project and other plants, and HL&P is cooperating with the GAO in its investigation and with the NRC in a similar review it has initiated. While no prediction can

be made at this time as to the ultimate outcome of these matters, the Company and HL&P do not believe that they will have a material adverse effect on the Company's or HL&P's financial condition or results of operations.

(c) LITIGATION WITH CO-OWNERS OF THE SOUTH TEXAS PROJECT. In February 1994, the City of Austin (Austin), one of the four co-owners of the South Texas Project, filed suit (Austin II Litigation) against HL&P. That suit is pending in the 152nd District Court for Harris County, Texas, which has set a trial date for October 1995. Austin alleges that the outages at the South Texas Project from early 1993 to early 1994 were due to HL&P's failure to perform obligations it owed to Austin under the Participation Agreement among the four co-owners of the South Texas Project (Participation Agreement). Austin also asserts that HL&P breached certain undertakings voluntarily assumed by HL&P under the terms and conditions of the Operating Licenses and Technical Specifications relating to the South Texas Project. Austin claims that such failures have caused Austin damages of at least $125 million due to the incurrence of increased operating and maintenance costs, the cost of replacement power and lost profits on wholesale transactions that did not occur. In May 1994, the City of San Antonio (San Antonio), another co-owner of the South Texas Project, intervened in the litigation filed by Austin against HL&P and asserted claims similar to those asserted by Austin. San Antonio has not identified the amount of damages it intends to seek from HL&P. HL&P is contesting San Antonio's intervention and has called for arbitration of San Antonio's claim under the arbitration provisions of the Participation Agreement. The trial court has denied HL&P's requests, but review of these decisions is currently pending before the 1st Court of Appeals in Houston.

In a previous lawsuit (Austin I Litigation) filed in 1983 against the Company and HL&P, Austin alleged that it had been fraudulently induced to participate in the South Texas Project and that HL&P had failed to perform properly its duties as project manager. In May 1993, the courts entered a judgement in favor of the Company and HL&P, concluding, among other things, that the Participation Agreement did not impose on HL&P a duty to exercise reasonable skill and care as project manager. During the course of the Austin I Litigation, San

Antonio and Central Power and Light Company (CPL), a subsidiary of Central and South West Corporation, two of the co-owners in the South Texas Project, also asserted claims for unspecified damages against HL&P as project manager of the South Texas Project, alleging HL&P breached its duties and obligations. San Antonio and CPL requested arbitration of their claims under the Participation Agreement. In 1992, the Company and HL&P entered into a settlement agreement with CPL (CPL Settlement) providing for CPL's withdrawal of its demand for arbitration. San Antonio's claims for arbitration remain pending. Under the Participation Agreement, San Antonio's arbitration claims will be heard by a panel of five arbitrators consisting of four arbitrators named by each co-owner and a fifth arbitrator selected by the four appointed arbitrators.

Although the CPL Settlement did not directly affect San Antonio's pending demand for arbitration, HL&P and CPL reached certain understandings in such agreement which contemplated that: (i) CPL's previously appointed arbitrator would be replaced by CPL; (ii) arbitrators approved by CPL or HL&P in any future arbitrations would be mutually acceptable to HL&P and CPL; and (iii) HL&P and CPL would resolve any future disputes between them concerning the South Texas Project without resorting to the arbitration provision of the

Participation Agreement. Austin and San Antonio have asserted in the pending Austin II Litigation that such understandings have rendered the arbitration provisions of the Participation Agreement void and that neither Austin nor San Antonio should be required to participate in or be bound by such proceedings.

Although HL&P and the Company do not believe there is merit to either Austin's or San Antonio's claims and have opposed San Antonio's intervention in the Austin II Litigation, there can be no assurance as to the ultimate outcome of these matters.

(d) NUCLEAR INSURANCE. HL&P and the other owners of the South Texas Project maintain nuclear property and nuclear liability insurance coverage as required by law and periodically review available limits and coverage for additional protection. The owners of the South Texas Project currently maintain the maximum amount of property damage insurance currently available through the insurance industry, consisting of $500 million in primary property damage insurance and excess property insurance in the amount of $2.25 billion. Under the excess property insurance which became effective on March 1, 1995 and under portions of the excess property insurance coverage in effect prior to March 1, 1995, HL&P and the other owners of the South Texas Project are subject to assessments, the maximum aggregate assessment under current policies being $26.9 million during any one policy year. The application of the proceeds of such property insurance is subject to the priorities established by the NRC regulations relating to the safety of licensed reactors and decontamination operations.

Pursuant to the Price Anderson Act (Act), the maximum liability to the public for owners of nuclear power plants, such as the South Texas Project, was decreased from $9.0 billion to $8.92 billion effective in November 1994. Owners are required under the Act to insure their liability for nuclear incidents and protective evacuations by maintaining the maximum amount of financial protection available from private sources and by maintaining secondary financial protection through an industry retrospective rating plan. The assessment of deferred premiums provided by the plan for each nuclear incident is up to $75.5 million per reactor subject to indexing for inflation, a possible 5 percent surcharge (but no more than $10 million per reactor per incident in any one year) and a 3 percent state premium tax. HL&P and the other owners of the South Texas Project currently maintain the required nuclear liability insurance and participate in the industry retrospective rating plan.

There can be no assurance that all potential losses or liabilities will be insurable, or that the amount of insurance will be sufficient to cover them. Any substantial losses not covered by insurance would have a material effect on HL&P's and the Company's financial condition.

(e) NUCLEAR DECOMMISSIONING. HL&P and the other co-owners of the South Texas Project are required by the NRC to meet minimum decommissioning funding requirements to pay the costs of decommissioning the South Texas Project. Pursuant to the terms of the order of the Utility Commission in Docket No. 9850, HL&P is currently funding decommissioning costs for the South Texas Project with an independent

trustee at an annual amount of $6 million, which is recorded in depreciation and amortization expense. HL&P's funding level is estimated to provide approximately $146 million, in 1989 dollars, an amount which exceeds the current NRC minimum.

The Company adopted SFAS No. 115, "Accounting for Certain Investments in Debt and Equity Securities," effective January 1, 1994. At December 31, 1994, the securities held in the Company's nuclear decommissioning trust totaling $25.1 million (reflected on the Company's Consolidated and HL&P's Balance Sheets in deferred debits and deferred credits) are classified as available for sale. Such securities are reported on the balance sheets at fair value, which at December 31, 1994 approximates cost, and any unrealized gains or losses will be reported as a separate component of common stock equity. Earnings, net of taxes and administrative costs, are reinvested in the funds.

In May 1994, an outside consultant estimated HL&P's portion of decommissioning costs to be approximately $318 million, in 1994 dollars. The consultant's calculation of decommissioning costs for financial planning purposes used the DECON methodology (prompt removal/dismantling), one of the three alternatives acceptable to the NRC, and assumed deactivation of Unit Nos. 1 and 2 upon the expiration of their 40 year operating licenses. Under the terms of the Proposed Settlement, HL&P would increase funding of decommissioning costs to an annual amount of approximately $14.8 million consistent with such study. While the current and projected funding levels presently exceed minimum NRC requirements, no assurance can be given that the amounts held in trust will be adequate to cover the actual decommissioning costs of the South Texas Project or the assumptions used in estimating decommissioning costs will ultimately prove to be correct.

(3) RATE REVIEW, FUEL RECONCILIATION AND OTHER PROCEEDINGS

In February 1994, the Utility Commission initiated a proceeding (Docket No. 12065) to determine whether HL&P's existing rates are just and reasonable. Subsequently, the scope of the docket was expanded to include reconciliation of HL&P's fuel costs from April 1, 1990 to July 31, 1994. The Utility Commission also initiated a separate proceeding (Docket No. 13126) to review issues regarding the prudence of operation of the South Texas Project from the date of commercial operation through the present. That review would encompass the outage at the South Texas Project during 1993 through 1994.

Hearings began in Docket No. 12065 in January 1995, and the Utility Commission has retained a consultant to review the South Texas Project for the purpose of providing testimony in Docket No. 13126 regarding the prudence of HL&P's management of operation of the South Texas Project. In February 1995, all major parties to these proceedings signed the Proposed Settlement resolving the issues with respect to HL&P, including the prudence issues related to operation of the South Texas Project. Approval of the Proposed Settlement by the Utility Commission will be required. To that end, the parties have established procedural dates for a hearing on issues raised by the parties who are opposed to the Proposed Settlement. A decision by the Utility Commission on the Proposed Settlement is not anticipated before early summer.

Under the Proposed Settlement, HL&P's base rates would be reduced by approximately $62 million per year, effective retroactively to January 1, 1995, and rates would be frozen for three years, subject to certain conditions. Under the Proposed Settlement, HL&P would amortize its remaining investment of $218 million in the cancelled Malakoff plant over a period not to exceed

seven years. HL&P also would increase its decommissioning expense for the South Texas Project by $9 million per year.

Under the Proposed Settlement, approximately $70 million of fuel expenditures and related interest incurred by HL&P during the fuel reconciliation period would not be recoverable from ratepayers. This $70 million was recorded as a one-time, pre-tax charge to reconcilable fuel revenues to reflect the anticipation of approval of the Proposed Settlement. HL&P also would establish a new fuel factor approximately 17 percent below that currently in effect and would refund to customers the balance in its fuel over-recovery account, estimated to be approximately $180 million after giving effect to the amounts not recoverable from ratepayers.

HL&P recovers fuel costs incurred in electric generation through a fixed fuel factor that is set by the Utility Commission. The difference between fuel revenues billed pursuant to such factor and fuel expense incurred is recorded as an addition to or a reduction of revenue, with a corresponding entry to under- or over-recovered fuel, as appropriate. Amounts collected pursuant to the fixed fuel factor must be reconciled periodically against actual, reasonable costs as determined by the Utility Commission. Currently, HL&P has an over-recovery fuel account balance that will be refunded pursuant to the Proposed Settlement.

In the event that the Proposed Settlement is not approved by the Utility Commission, including issues related to the South Texas Project, Docket No. 12065 will be remanded to an Administrative Law Judge (ALJ) to resume detailed hearings in this docket. Prior to reaching agreement on the terms of the Proposed Settlement, HL&P argued that its existing rates were just and reasonable and should not be reduced. Other parties argued that rate decreases in annual amounts ranging from $26 million to $173 million were required and that additional decreases might be justified following an examination of the prudence of the management of the South Texas Project and the costs incurred in connection with the outages at the South Texas Project. Testimony filed by the Utility Commission staff included a recommendation to remove from rate base $515 million of HL&P's investment in the South Texas Project to reflect the staff's view that such investment was not fully "used and useful" in providing service, a position HL&P vigorously disputes.

In the event the Proposed Settlement is not approved by the Utility Commission, the fuel reconciliation issues in Docket Nos. 12065 and 13126 would be remanded to an ALJ for additional proceedings. A major issue in Docket No. 13126 will be whether the incremental fuel costs incurred as a result of outages at the South Texas Project represent reasonable costs. HL&P filed testimony in Docket No. 13126, which testimony concluded that the outages at the South Texas Project did not result from imprudent management. HL&P also filed testimony analyzing the extent to which regulatory issues extended the outages. In that testimony an outside consultant retained by HL&P concluded that the duration of the outages was controlled by both the resolution of NRC regulatory issues as well as necessary equipment repairs unrelated to NRC regulatory issues and that the incremental effect of NRC regulatory issues on the duration of the outages was only 39 days per unit. Estimates as to the cost of replacement power may vary significantly based on a number of factors, including the capacity factor at which the South Texas Project might be assumed to have operated had it not been out of service due to the outages. However, HL&P believes that applying a reasonable range

of assumptions would result in replacement fuel costs of less than $10 million for the 39 day periods identified by HL&P's consultant and less than $100 million for the entire length of the outages. Any fuel costs determined to have been unreasonably incurred would not be recoverable from customers and would be charged against the Company's earnings.

Although the Company and HL&P believe that the Proposed Settlement is in the best interest of HL&P, its ratepayers, and the Company and its shareholders, no assurance can be given that (i) the Utility Commission ultimately will approve the terms of the Proposed Settlement or (ii) in the event the Proposed Settlement is not approved and proceedings against HL&P resumed, that the outcome of such proceedings would be favorable to HL&P.

(4) APPEALS OF PRIOR UTILITY COMMISSION RATE ORDERS

Pursuant to a series of applications filed by HL&P in recent years, the Utility Commission has granted HL&P rate increases to reflect in electric rates HL&P's substantial investment in new plant construction, including the South Texas Project. Although Utility Commission action on those applications has been completed, judicial review of a number of the Utility Commission orders is pending. In Texas, Utility Commission orders may be appealed to a District Court in Travis County, and from that Court's decision an appeal may be taken to the Court of Appeals for the 3rd District at Austin (Austin Court of Appeals). Discretionary review by the Supreme Court of Texas may be sought from decisions of the Austin Court of Appeals. The pending appeals from the Utility Commission orders are in various stages. In the event the courts ultimately reverse actions of the Utility Commission in any of these proceedings, such matters would be

remanded to the Utility Commission for action in light of the courts' orders. Because of the number of variables which can affect the ultimate resolution of such matters on remand, the Company and HL&P generally are not in a position at this time to predict the outcome of the matters on appeal or the ultimate effect that adverse action by the courts could have on the Company and HL&P. On remand, the Utility Commission's action could range from granting rate relief substantially equal to the rates previously approved to a reduction in the revenues to which HL&P was entitled during the time the applicable rates were in effect, which could require a refund to customers of amounts collected pursuant to such rates. Judicial review has been concluded or currently is pending on the final orders of the Utility Commission described below.

(a) 1991 RATE CASE. In HL&P's 1991 rate case (Docket No. 9850), the Utility Commission approved a non-unanimous settlement agreement providing for a $313 million increase in HL&P's base rates, termination of deferrals granted with respect to Unit No. 2 of the South Texas Project and of the qualified phase-in plan deferrals granted with respect to Unit No. 1 of the South Texas Project, and recovery of deferred plant costs. The settlement authorized a 12.55 percent return on common equity for HL&P. Rates contemplated by the settlement agreement were implemented in May 1991 and remain in effect (subject to the outcome of the current rate proceeding described in Note 3).

The Utility Commission's order in Docket No. 9850 was affirmed on review by a District Court, and the Austin Court of Appeals affirmed that decision on procedural grounds due to the failure of the appellant to file the record with the court in a timely manner. On review, the Texas

Supreme Court has remanded the case to the Austin Court of Appeals for consideration of the appellant's challenges to the Utility Commission's order, which include issues regarding deferred accounting, the treatment of federal income tax expense and certain other matters. As to federal tax issues, a recent decision of the Austin Court of Appeals, in an appeal involving GTE-SW (and to which HL&P was not a party), held that when a utility pays federal income taxes as part of a consolidated group, the utility's ratepayers are entitled to a fair share of the tax savings actually realized, which can include savings resulting from unregulated activities. The Texas Supreme Court has agreed to hear an appeal of that decision, but on points not involving the federal income tax issues, though tax issues could be decided in such opinion.

Because the Utility Commission's order in Docket No. 9850 found that HL&P would have been entitled to rate relief greater than the $313 million agreed to in the settlement, HL&P believes that any disallowance that might be required if the court's ruling in the GTE decision were applied in Docket No. 9850 would be offset by that greater amount. However, that amount may not be sufficient if the Austin Court of Appeals also concludes that the Utility Commission's inclusion of deferred accounting costs in the settlement was improper. For a discussion of the Texas Supreme Court's decision on deferred accounting treatment, see Note 4(c). Although HL&P believes that it could demonstrate entitlement to rate relief equal to that agreed to in the stipulation in Docket No. 9850, HL&P cannot rule out the possibility that a remand and reopening of that settlement would be required if decisions unfavorable to HL&P are rendered on both the deferred accounting treatment and the calculation of tax expense for rate making purposes.

The parties to the Proposed Settlement have agreed to withdraw their appeals of the Utility Commission's orders in such docket, subject to HL&P's dismissing its appeal in Docket No. 6668.

(b) 1988 RATE CASE. In HL&P's 1988 rate case (Docket No. 8425), the Utility Commission granted HL&P a $227 million increase in base revenues, allowed a 12.92 percent return on common equity, authorized a qualified phase-in plan for Unit No. 1 of the South Texas Project (including approximately 72 percent of HL&P's investment in Unit No. 1 of the South Texas Project in rate base) and authorized HL&P to use deferred accounting for Unit No. 2 of the South Texas Project. Rates substantially corresponding to the increase granted were implemented by HL&P in June 1989 and remained in effect until May 1991.

In August 1994, the Austin Court of Appeals affirmed the Utility Commission's order in Docket No. 8425 on all matters other than the Utility Commission's treatment of tax savings associated with

deductions taken for expenses disallowed in cost of service. The court held that the Utility Commission had failed to require that such tax savings be passed on to ratepayers, and ordered that the case be remanded to the Utility Commission with instructions to adjust HL&P's cost of service accordingly. Discretionary review is being sought from the Texas Supreme Court by all parties to the proceeding.

The parties to the Proposed Settlement have agreed to dismiss their respective appeals of Docket No. 8425, subject to HL&P's dismissing its appeal in Docket No. 6668. A separate party to this appeal, however, has not agreed to dismiss its appeal.

(c) DEFERRED ACCOUNTING. Deferred accounting treatment for certain costs associated with Unit No. 1 of the South Texas Project was authorized by the Utility Commission in Docket No. 8230 and was extended in Docket No. 9010. Similar deferred accounting treatment with respect to Unit No. 2 of the South Texas Project was authorized in Docket No. 8425. For a discussion of the deferred accounting treatment granted, see Note 1(f).

In June 1994, the Texas Supreme Court decided the appeal of Docket Nos. 8230 and 9010, as well as all other pending deferred accounting cases involving other utilities, upholding deferred accounting treatment for both carrying costs and operation and maintenance expenses as within the Utility Commission's statutory authority and reversed the Austin Court of Appeals decision to the extent that the Austin Court of Appeals had rejected deferred accounting treatment for carrying charges. Because the lower appellate court had upheld deferred accounting only as to operation and maintenance expenses, the Texas Supreme Court remanded Docket Nos. 8230 and 9010 to the Austin Court of Appeals to consider the points of error challenging the granting of deferred accounting for carrying costs which it had not reached in its earlier consideration of the case. The Texas Supreme Court opinion did state, however, that when deferred costs are considered for addition to the utility's rate base in an ensuing rate case, the Utility Commission must then determine to what extent inclusion of the deferred costs is necessary to preserve the utility's financial integrity. Under the terms of the Proposed Settlement, South Texas Project deferrals will continue to be amortized under the schedule previously established.

The Office of the Public Utility Counsel (OPUC) has agreed, pursuant to the Proposed Settlement, to withdraw and dismiss its appeal if the Proposed Settlement becomes effective and on the condition that HL&P dismisses its appeal in Docket No. 6668. However, the appeal of the State of Texas remains pending.

(d) PRUDENCE REVIEW OF THE CONSTRUCTION OF THE SOUTH TEXAS PROJECT. In June 1990, the Utility Commission ruled in a separate docket (Docket No. 6668) that had been created to review the prudence of HL&P's planning and construction of the South Texas Project that $375.5 million out of HL&P's $2.8 billion investment in the two units of the South Texas Project had been imprudently incurred. That ruling was incorporated into HL&P's 1988 and 1991 rate cases and resulted in HL&P's recording an after-tax charge of $15 million in 1990. Several parties appealed the Utility Commission's decision, but a District Court dismissed these appeals on procedural grounds. The Austin Court of Appeals reversed and directed consideration of the appeals, and the Texas Supreme Court denied discretionary review in 1994. At this time, no action has been taken by the appellants to proceed with the appeals. Unless the order in Docket No. 6668 is modified or reversed on appeal, the amount found imprudent by the Utility Commission will be sustained.

Under the Proposed Settlement, OPUC, HL&P and the City of Houston each has agreed to dismiss its respective appeals of Docket No. 6668. A separate party to this appeal, however, has not agreed to dismiss its appeal. If this party does not elect to dismiss its appeal, HL&P may elect to maintain its appeal, whereupon OPUC and City of Houston shall also be entitled to maintain their appeals.

(5)MALAKOFF

The scheduled in-service dates for the Malakoff units were postponed during the 1980's as expectations of continued strong load growth were tempered. In 1987, all developmental work was stopped and AFUDC accruals ceased. These units have been cancelled due to the availability of other cost effective resource options.

In Docket No. 8425, the Utility Commission allowed recovery of certain costs associated with the cancelled Malakoff units by amortizing those costs over ten years for rate making purposes. Such recoverable costs were not included in rate base and, as a result, no return on investment is being earned during the recovery period. The remaining balance at December 31, 1994 is $34 million with a recovery period of 66 months.

Also as a result of the final order in Docket No. 8425, the costs associated with the engineering design work for the Malakoff units were included in rate base and are earning a return. Subsequently, in December 1992, HL&P determined that such costs would have no future value and reclassified $84.1 million from plant held for future use to recoverable project costs. In 1993, an additional $7 million was reclassified to recoverable project costs. Amortization of these amounts began in 1993. The balance at December 31, 1994 was $65 million with a remaining recovery period of 60 months. The amortization amount is approximately equal to the amount currently earning a cash return in rates. The Utility Commission's decision to allow treatment of these costs as plant held for future use has been challenged in the pending appeal of the Docket No. 8425 final order. See Note 4(b) for a discussion of this proceeding.

In June 1990, HL&P purchased from its then fuel supply affiliate, Utility Fuels, Inc. (Utility Fuels), all of Utility Fuels' interest in the lignite reserves and lignite handling facilities for Malakoff. The purchase price was $138.2 million, which represented the net book value of Utility Fuels' investment in such reserves and facilities. As part of the June 1990 rate order (Docket No. 8425), the Utility Commission ordered that issues related to the prudence of the amounts invested in the lignite reserves be considered in HL&P's next general rate case which was filed in November 1990 (Docket No. 9850). However, under the October 1991 Utility Commission order in Docket No. 9850, this determination was postponed to a subsequent docket.

HL&P's remaining investment in Malakoff lignite reserves as of December 31, 1994 of $153 million is included on the Company's Consolidated and HL&P's Balance Sheets in plant held for future use. HL&P anticipates that an additional $8 million of expenditures relating to lignite reserves will be incurred in 1995 and 1996.

In Docket No. 12065, HL&P filed testimony in support of the amortization of substantially all of its remaining investment in Malakoff, including the portion of the engineering design costs for which amortization had not previously been authorized and the amount attributable to related lignite reserves which had not previously been addressed by the Utility Commission. Under the Proposed Settlement of Docket No. 12065, HL&P would amortize its investment in Malakoff over a period not to exceed seven years such that the entire investment will be written off no later than December 31, 2002. See Note 3. In the event that the Utility Commission does not

approve the Proposed Settlement, and if appropriate rate treatment of these amounts is not ultimately received, HL&P could be required to write off any unrecoverable portions of its Malakoff investment.

(2) JOINTLY-OWNED NUCLEAR PLANT

(a) HL&P INVESTMENT. HL&P is the project manager (and one of four co-owners) of the South Texas Project, which consists of two 1,250 megawatt nuclear generating units. HL&P has a 30.8 percent interest in the project and bears a corresponding share of capital and operating

costs associated with the project. As of December 31, 1994, HL&P's investments (net of accumulated depreciation and amortization) in the South Texas Project and in nuclear fuel, including AFUDC, were $2.1 billion and $99 million, respectively.

(b) UNITED STATES NUCLEAR REGULATORY COMMISSION (NRC) INSPECTIONS AND OPERATIONS. Both generating units at the South Texas Project were out of service from February 1993 to February 1994, when Unit No. 1 was returned to service. Unit No. 2 was returned to service in May 1994. HL&P removed the units from service in February 1993 when a problem was encountered with certain of the units' auxiliary feedwater pumps.

In February 1995, the NRC removed the South Texas Project from its "watch list" of plants with weaknesses that warranted increased NRC attention. The NRC placed the South Texas Project on the "watch list" in June 1993, following the issuance of a report by an NRC Diagnostic Evaluation Team (DET) which conducted a review of the South Texas Project operations.

Certain current and former employees of HL&P or contractors of HL&P have asserted claims that their employment was terminated or disrupted in retaliation for their having made safety-related complaints to the NRC. Civil proceedings by the complaining personnel and administrative proceedings by the Department of Labor remain pending against HL&P, and the NRC has jurisdiction to take enforcement action against HL&P and/or individual employees with respect to these matters. Based on its own internal investigation, in October 1994 the NRC issued a notice of violation and proposed a $100,000 civil penalty against HL&P in one such case in which HL&P had terminated the site access of a former contractor employee. In that action, the NRC also requested information relating to possible further enforcement action in this matter against two HL&P managers involved in such termination. HL&P strongly disagrees with the NRC's conclusions, and has requested the NRC to give further consideration of its notice. In February 1995, the NRC conducted an enforcement conference with respect to that matter, but no result has been received.

HL&P has provided documents and other assistance to a subcommittee of the U. S. House of Representatives (Subcommittee) that is conducting an inquiry related to the South Texas Project. Although the precise focus and timing of the inquiry has not been identified by the Subcommittee, it is anticipated that the Subcommittee will inquire into matters related to HL&P's handling of employee concerns and to issues related to the NRC's 1993 DET review of the South Texas Project. In connection with that inquiry, HL&P has been advised that the U. S. General Accounting Office (GAO) is conducting a review of the NRC's inspection process as it relates to the South Texas Project and other plants, and HL&P is cooperating with the GAO in its investigation and with the NRC in a similar review it has initiated. While no prediction can be made at this time as to the ultimate outcome of these matters, the Company and HL&P do not believe that they will have a material adverse effect on the Company's or HL&P's financial condition or results of operations.

(c) LITIGATION WITH CO-OWNERS OF THE SOUTH TEXAS PROJECT. In February 1994, the City of Austin (Austin), one of the four co-owners of the South Texas Project, filed suit (Austin II Litigation) against HL&P. That suit is pending in the 152nd District Court for Harris County, Texas, which has set a trial date for October 1995. Austin alleges that the outages at the South Texas

Project from early 1993 to early 1994 were due to HL&P's failure to perform obligations it owed to Austin under the Participation Agreement among the four co-owners of the South Texas Project (Participation Agreement). Austin also asserts that HL&P breached certain undertakings voluntarily assumed by HL&P under the terms and conditions of the Operating Licenses and Technical Specifications relating to the South Texas Project. Austin claims that such failures have caused Austin damages of at least $125 million due to the incurrence of increased operating and maintenance costs, the cost of replacement power and lost

profits on wholesale transactions that did not occur. In May 1994, the City of San Antonio (San Antonio), another co-owner of the South Texas Project, intervened in the litigation filed by Austin against HL&P and asserted claims similar to those asserted by Austin. San Antonio has not identified the amount of damages it intends to seek from HL&P. HL&P is contesting San Antonio's intervention and has called for arbitration of San Antonio's claim under the arbitration provisions of the Participation Agreement. The trial court has denied HL&P's requests, but review of these decisions is currently pending before the 1st Court of Appeals in Houston.

In a previous lawsuit (Austin I Litigation) filed in 1983 against the Company and HL&P, Austin alleged that it had been fraudulently induced to participate in the South Texas Project and that HL&P had failed to perform properly its duties as project manager. In May 1993, the courts entered a judgement in favor of the Company and HL&P, concluding, among other things, that the Participation Agreement did not impose on HL&P a duty to exercise reasonable skill and care as project manager. During the course of the Austin I Litigation, San Antonio and Central Power and Light Company (CPL), a subsidiary of Central and South West Corporation, two of the co-owners in the South Texas Project, also asserted claims for unspecified damages against HL&P as project manager of the South Texas Project, alleging HL&P breached its duties and obligations. San Antonio and CPL requested arbitration of their claims under the Participation Agreement. In 1992, the Company and HL&P entered into a settlement agreement with CPL (CPL Settlement) providing for CPL's withdrawal of its demand for arbitration. San Antonio's claims for arbitration remain pending. Under the Participation Agreement, San Antonio's arbitration claims will be heard by a panel of five arbitrators consisting of four arbitrators named by each co-owner and a fifth arbitrator selected by the four appointed arbitrators.

Although the CPL Settlement did not directly affect San Antonio's pending demand for arbitration, HL&P and CPL reached certain understandings in such agreement which contemplated that: (i) CPL's previously appointed arbitrator would be replaced by CPL; (ii) arbitrators approved by CPL or HL&P in any future arbitrations would be mutually acceptable to HL&P and CPL; and (iii) HL&P and CPL would resolve any future disputes between them concerning the South Texas Project without resorting to the arbitration provision of the Participation Agreement. Austin and San Antonio have asserted in the pending Austin II Litigation that such understandings have rendered the arbitration provisions of the Participation Agreement void and that neither Austin nor San Antonio should be required to participate in or be bound by such proceedings.

Although HL&P and the Company do not believe there is merit to either Austin's or San Antonio's claims and have opposed San Antonio's intervention in the Austin II Litigation, there can be no assurance as to the ultimate outcome of these matters.

(d) NUCLEAR INSURANCE. HL&P and the other owners of the South Texas Project maintain nuclear property and nuclear liability insurance coverage as required by law and periodically review available limits and coverage for additional protection. The owners of the South Texas Project currently maintain the maximum amount of property damage insurance currently available through the insurance industry, consisting of $500 million in primary property damage insurance and excess property insurance in the amount of $2.25 billion. Under the excess property insurance which became effective on March 1, 1995 and under portions of the excess property insurance coverage in effect prior to March 1, 1995, HL&P and the other owners of the South Texas Project are subject to assessments, the maximum aggregate assessment under current policies being $26.9 million during any one policy year. The application of the proceeds of such property insurance is subject to the priorities established by the NRC regulations relating to the safety of licensed reactors and decontamination operations.

Pursuant to the Price Anderson Act (Act), the maximum liability to the public for owners of nuclear power plants, such as the South Texas Project, was decreased from $9.0 billion to $8.92 billion effective in November 1994. Owners are required under the Act to insure their liability for nuclear incidents and protective evacuations by maintaining the maximum amount of financial protection available from private sources and by maintaining secondary financial protection through an industry retrospective rating plan. The assessment of deferred premiums provided by the plan for each nuclear incident is up to $75.5 million per reactor subject to indexing for inflation, a possible 5 percent surcharge (but no more than $10 million per reactor

per incident in any one year) and a 3 percent state premium tax. HL&P and the other owners of the South Texas Project currently maintain the required nuclear liability insurance and participate in the industry retrospective rating plan.

There can be no assurance that all potential losses or liabilities will be insurable, or that the amount of insurance will be sufficient to cover them. Any substantial losses not covered by insurance would have a material effect on HL&P's and the Company's financial condition.

(e) NUCLEAR DECOMMISSIONING. HL&P and the other co-owners of the South Texas Project are required by the NRC to meet minimum decommissioning funding requirements to pay the costs of decommissioning the South Texas Project. Pursuant to the terms of the order of the Utility Commission in Docket No. 9850, HL&P is currently funding decommissioning costs for the South Texas Project with an independent trustee at an annual amount of $6 million, which is recorded in depreciation and amortization expense. HL&P's funding level is estimated to provide approximately $146 million, in 1989 dollars, an amount which exceeds the current NRC minimum.

The Company adopted SFAS No. 115, "Accounting for Certain Investments in Debt and Equity Securities," effective January 1, 1994. At December 31, 1994, the securities held in the Company's nuclear decommissioning trust totaling $25.1 million (reflected on the Company's Consolidated and HL&P's Balance Sheets in deferred debits and deferred credits) are classified as available for sale. Such securities are reported on the balance sheets at fair value, which at December 31, 1994 approximates cost, and any unrealized gains or losses will be reported as a separate component of common stock equity. Earnings, net of taxes and administrative costs, are reinvested in the funds.

In May 1994, an outside consultant estimated HL&P's portion of decommissioning costs to be approximately $318 million, in 1994 dollars. The consultant's calculation of decommissioning costs for financial planning purposes used the DECON methodology (prompt removal/dismantling), one of the three alternatives acceptable to the NRC, and assumed deactivation of Unit Nos. 1 and 2 upon the expiration of their 40 year operating licenses. Under the terms of the Proposed Settlement, HL&P would increase funding of decommissioning costs to an annual amount of approximately $14.8 million consistent with such study. While the current and projected funding levels presently exceed minimum NRC requirements, no assurance can be given that the amounts held in trust will be adequate to cover the actual decommissioning costs of the South Texas Project or the assumptions used in estimating decommissioning costs will ultimately prove to be correct.

(3) RATE REVIEW, FUEL RECONCILIATION AND OTHER PROCEEDINGS

In February 1994, the Utility Commission initiated a proceeding (Docket No. 12065) to determine whether HL&P's existing rates are just and reasonable. Subsequently, the scope of the docket was expanded to include reconciliation of HL&P's fuel costs from April 1, 1990 to July 31, 1994. The Utility Commission also initiated a separate proceeding (Docket No. 13126) to review issues regarding the prudence of operation of the South Texas Project from the date of commercial operation through the present. That review would encompass the outage at the South Texas Project during 1993 through 1994.

Hearings began in Docket No. 12065 in January 1995, and the Utility Commission has retained a consultant to review the South Texas Project for the purpose of providing testimony in Docket No. 13126 regarding the prudence of HL&P's management of operation of the South Texas Project. In February 1995, all major parties to these proceedings signed the Proposed Settlement resolving the issues with respect to HL&P, including the prudence issues related to operation of the South Texas Project. Approval of the Proposed Settlement by the Utility Commission will be required. To that end, the parties have established procedural dates for a hearing on issues raised by the parties who are opposed to the Proposed Settlement. A decision by the Utility Commission on the Proposed Settlement is not anticipated before early summer.

Under the Proposed Settlement, HL&P's base rates would be reduced by approximately $62 million per year, effective retroactively to January 1, 1995, and rates would be frozen for three years, subject to certain conditions. Under the Proposed Settlement, HL&P would amortize its remaining investment of $218 million in the cancelled Malakoff plant over a period not to exceed seven years. HL&P also would increase its decommissioning expense for the South Texas Project by $9 million per year.

Under the Proposed Settlement, approximately $70 million of fuel expenditures and related interest incurred by HL&P during the fuel reconciliation period would not be recoverable from ratepayers. This $70 million was recorded as a one-time, pre-tax charge to reconcilable fuel revenues to reflect the anticipation of approval of the Proposed Settlement. HL&P also would establish a new fuel factor approximately 17 percent below that currently in effect and would

refund to customers the balance in its fuel over-recovery account, estimated to be approximately $180 million after giving effect to the amounts not recoverable from ratepayers.

HL&P recovers fuel costs incurred in electric generation through a fixed fuel factor that is set by the Utility Commission. The difference between fuel revenues billed pursuant to such factor and fuel expense incurred is recorded as an addition to or a reduction of revenue, with a corresponding entry to under- or over-recovered fuel, as appropriate. Amounts collected pursuant to the fixed fuel factor must be reconciled periodically against actual, reasonable costs as determined by the Utility Commission. Currently, HL&P has an over-recovery fuel account balance that will be refunded pursuant to the Proposed Settlement.

In the event that the Proposed Settlement is not approved by the Utility Commission, including issues related to the South Texas Project, Docket No. 12065 will be remanded to an Administrative Law Judge (ALJ) to resume detailed hearings in this docket. Prior to reaching agreement on the terms of the Proposed Settlement, HL&P argued that its existing rates were just and reasonable and should not be reduced. Other parties argued that rate decreases in annual amounts ranging from $26 million to $173 million were required and that additional decreases might be justified following an examination of the prudence of the management of the South Texas Project and the costs incurred in connection with the outages at the South Texas Project. Testimony filed by the Utility Commission staff included a recommendation to remove from rate base $515 million of HL&P's investment in the South Texas Project to reflect the staff's view that such investment was not fully "used and useful" in providing service, a position HL&P vigorously disputes.

In the event the Proposed Settlement is not approved by the Utility Commission, the fuel reconciliation issues in Docket Nos. 12065 and 13126 would be remanded to an ALJ for additional proceedings. A major issue in Docket No. 13126 will be whether the incremental fuel costs incurred as a result of outages at the South Texas Project represent reasonable costs. HL&P filed testimony in Docket No. 13126, which testimony concluded that the outages at the South Texas Project did not result from imprudent management. HL&P also filed testimony analyzing the extent to which regulatory issues extended the outages. In that testimony an outside consultant retained by HL&P concluded that the duration of the outages was controlled by both the resolution of NRC regulatory issues as well as necessary equipment repairs unrelated to NRC regulatory issues and that the incremental effect of NRC regulatory issues on the duration of the outages was only 39 days per unit. Estimates as to the cost of replacement power may vary significantly based on a number of factors, including the capacity factor at which the South Texas Project might be assumed to have operated had it not been out of service due to the outages. However, HL&P believes that applying a reasonable range of assumptions would result in replacement fuel costs of less than $10 million for the 39 day periods identified by HL&P's consultant and less than $100 million for the entire length of the outages. Any fuel costs determined to have been unreasonably incurred would not be recoverable from customers and would be charged against the Company's earnings.

Although the Company and HL&P believe that the Proposed Settlement is in the best interest of HL&P, its ratepayers, and the Company and its shareholders, no assurance can be given that (i) the Utility Commission ultimately will approve the terms of the Proposed Settlement or

(ii) in the event the Proposed Settlement is not approved and proceedings against HL&P resumed, that the outcome of such proceedings would be favorable to HL&P.

(4) APPEALS OF PRIOR UTILITY COMMISSION RATE ORDERS

Pursuant to a series of applications filed by HL&P in recent years, the Utility Commission has granted HL&P rate increases to reflect in

electric rates HL&P's substantial investment in new plant construction, including the South Texas Project. Although Utility Commission action on those applications has been completed, judicial review of a number of the Utility Commission orders is pending. In Texas, Utility Commission orders may be appealed to a District Court in Travis County, and from that Court's decision an appeal may be taken to the Court of Appeals for the 3rd District at Austin (Austin Court of Appeals). Discretionary review by the Supreme Court of Texas may be sought from decisions of the Austin Court of Appeals. The pending appeals from the Utility Commission orders are in various stages. In the event the courts ultimately reverse actions of the Utility Commission in any of these proceedings, such matters would be remanded to the Utility Commission for action in light of the courts' orders. Because of the number of variables which can affect the ultimate resolution of such matters on remand, the Company and HL&P generally are not in a position at this time to predict the outcome of the matters on appeal or the ultimate effect that adverse action by the courts could have on the Company and HL&P. On remand, the Utility Commission's action could range from granting rate relief substantially equal to the rates previously approved to a reduction in the revenues to which HL&P was entitled during the time the applicable rates were in effect, which could require a refund to customers of amounts collected pursuant to such rates. Judicial review has been concluded or currently is pending on the final orders of the Utility Commission described below.

(a) 1991 RATE CASE. In HL&P's 1991 rate case (Docket No. 9850), the Utility Commission approved a non-unanimous settlement agreement providing for a $313 million increase in HL&P's base rates, termination of deferrals granted with respect to Unit No. 2 of the South Texas Project and of the qualified phase-in plan deferrals granted with respect to Unit No. 1 of the South Texas Project, and recovery of deferred plant costs. The settlement authorized a 12.55 percent return on common equity for HL&P. Rates contemplated by the settlement agreement were implemented in May 1991 and remain in effect (subject to the outcome of the current rate proceeding described in Note 3).

The Utility Commission's order in Docket No. 9850 was affirmed on review by a District Court, and the Austin Court of Appeals affirmed that decision on procedural grounds due to the failure of the appellant to file the record with the court in a timely manner. On review, the Texas Supreme Court has remanded the case to the Austin Court of Appeals for consideration of the appellant's challenges to the Utility Commission's order, which include issues regarding deferred accounting, the treatment of federal income tax expense and certain other matters. As to federal tax issues, a recent decision of the Austin Court of Appeals, in an appeal involving GTE-SW (and to which HL&P was not a party), held that when a utility pays federal income taxes as part of a consolidated group, the utility's ratepayers are entitled to a fair share of the tax savings actually realized, which can include savings resulting from unregulated activities. The

Texas Supreme Court has agreed to hear an appeal of that decision, but on points not involving the federal income tax issues, though tax issues could be decided in such opinion.

Because the Utility Commission's order in Docket No. 9850 found that HL&P would have been entitled to rate relief greater than the $313 million agreed to in the settlement, HL&P believes that any disallowance that might be required if the court's ruling in the GTE decision were applied in Docket No. 9850 would be offset by that greater amount. However, that amount may not be sufficient if the Austin Court of Appeals also concludes that the Utility Commission's inclusion of deferred accounting costs in the settlement was improper. For a discussion of the Texas Supreme Court's decision on deferred accounting treatment, see Note 4(c). Although HL&P believes that it could demonstrate entitlement to rate relief equal to that agreed to in the stipulation in Docket No. 9850, HL&P cannot rule out the possibility that a remand and reopening of that settlement would be required if decisions unfavorable to HL&P are rendered on both the deferred accounting treatment and the calculation of tax expense for rate making purposes.

The parties to the Proposed Settlement have agreed to withdraw their appeals of the Utility Commission's orders in such docket, subject to HL&P's dismissing its appeal in Docket No. 6668.

(b) 1988 RATE CASE. In HL&P's 1988 rate case (Docket No. 8425), the Utility Commission granted HL&P a $227 million increase in base revenues, allowed a 12.92 percent return on common equity, authorized a qualified phase-in plan for Unit No. 1 of the South Texas Project (including

approximately 72 percent of HL&P's investment in Unit No. 1 of the South Texas Project in rate base) and authorized HL&P to use deferred accounting for Unit No. 2 of the South Texas Project. Rates substantially corresponding to the increase granted were implemented by HL&P in June 1989 and remained in effect until May 1991.

In August 1994, the Austin Court of Appeals affirmed the Utility Commission's order in Docket No. 8425 on all matters other than the Utility Commission's treatment of tax savings associated with deductions taken for expenses disallowed in cost of service. The court held that the Utility Commission had failed to require that such tax savings be passed on to ratepayers, and ordered that the case be remanded to the Utility Commission with instructions to adjust HL&P's cost of service accordingly. Discretionary review is being sought from the Texas Supreme Court by all parties to the proceeding.

The parties to the Proposed Settlement have agreed to dismiss their respective appeals of Docket No. 8425, subject to HL&P's dismissing its appeal in Docket No. 6668. A separate party to this appeal, however, has not agreed to dismiss its appeal.

(c) DEFERRED ACCOUNTING. Deferred accounting treatment for certain costs associated with Unit No. 1 of the South Texas Project was authorized by the Utility Commission in Docket No. 8230 and was extended in Docket No. 9010. Similar deferred accounting treatment with respect to Unit No. 2 of the South Texas Project was authorized in Docket No. 8425. For a discussion of the deferred accounting treatment granted, see Note 1(f).

In June 1994, the Texas Supreme Court decided the appeal of Docket Nos. 8230 and 9010, as well as all other pending deferred accounting cases involving other utilities, upholding deferred accounting treatment for both carrying costs and operation and maintenance expenses as within the Utility Commission's statutory authority and reversed the Austin Court of Appeals decision to the extent that the Austin Court of Appeals had rejected deferred accounting treatment for carrying charges. Because the lower appellate court had upheld deferred accounting only as to operation and maintenance expenses, the Texas Supreme Court remanded Docket Nos. 8230 and 9010 to the Austin Court of Appeals to consider the points of error challenging the granting of deferred accounting for carrying costs which it had not reached in its earlier consideration of the case. The Texas Supreme Court opinion did state, however, that when deferred costs are considered for addition to the utility's rate base in an ensuing rate case, the Utility Commission must then determine to what extent inclusion of the deferred costs is necessary to preserve the utility's financial integrity. Under the terms of the Proposed Settlement, South Texas Project deferrals will continue to be amortized under the schedule previously established.

The Office of the Public Utility Counsel (OPUC) has agreed, pursuant to the Proposed Settlement, to withdraw and dismiss its appeal if the Proposed Settlement becomes effective and on the condition that HL&P dismisses its appeal in Docket No. 6668. However, the appeal of the State of Texas remains pending.

(d) PRUDENCE REVIEW OF THE CONSTRUCTION OF THE SOUTH TEXAS PROJECT. In June 1990, the Utility Commission ruled in a separate docket (Docket No. 6668) that had been created to review the prudence of HL&P's planning and construction of the South Texas Project that $375.5 million out of HL&P's $2.8 billion investment in the two units of the South Texas Project had been imprudently incurred. That ruling was incorporated into HL&P's 1988 and 1991 rate cases and resulted in HL&P's recording an after-tax charge of $15 million in 1990. Several parties appealed the Utility Commission's decision, but a District Court dismissed these appeals on procedural grounds. The Austin Court of Appeals reversed and directed consideration of the appeals, and the Texas Supreme Court denied discretionary review in 1994. At this time, no action has been taken by the appellants to proceed with the appeals. Unless the order in Docket No. 6668 is modified or reversed on appeal, the amount found imprudent by the Utility Commission will be sustained.

Under the Proposed Settlement, OPUC, HL&P and the City of Houston each has agreed to dismiss its respective appeals of Docket No. 6668. A separate party to this appeal, however, has not agreed to dismiss its appeal. If this party does not elect to dismiss its appeal, HL&P may elect to maintain its appeal, whereupon OPUC and City of Houston shall also be entitled to maintain their appeals.

(b) UNITED STATES NUCLEAR REGULATORY COMMISSION (NRC) INSPECTIONS AND OPERATIONS. HL&P removed both generating units at the South Texas Project from service in February 1993 when a problem was encountered with certain of the units' auxiliary feedwater pumps. The units were out of service from February 1993 to February 1994, when Unit No. 1 was returned to service.

Unit No. 2 was returned to service in May 1994. In June 1993, the NRC placed the South Texas Project on its "watch list" of plants with weaknesses that warrant increased attention after a review of the South Texas Project operations. In February 1995, the NRC removed the South Texas Project from its "watch list".

Certain current and former employees or contractors of HL&P have asserted claims that their employment was terminated or disrupted in retaliation for their having made safety-related complaints to the NRC. Civil proceedings by the complaining personnel and administrative proceedings by the Department of Labor remain pending against HL&P, and the NRC has jurisdiction to take enforcement action against HL&P and/or individual employees with respect to these matters. On May 8, 1995, the NRC announced that it was withdrawing a previously proposed Notice of Violation and $100,000 civil penalty, as well as possible individual enforcement action against two HL&P managers in connection with one such case, involving a contractor employee whose site access was terminated. Allegations of retaliation by that individual remain pending before an Administrative Law Judge (ALJ) of the Department of Labor. In another such case, involving two former HL&P employees who were terminated during a reduction in force, another Department of Labor ALJ in April 1995 issued his recommended decision in favor of the former employees, ordering reinstatement of one with back-pay and back-pay without reinstatement to another. The ALJ ruled out ordering HL&P to pay exemplary damages to the individuals, but indicated his intention to hold a further hearing to consider whether additional compensatory damages should be awarded. HL&P considers the ALJ's conclusions to be erroneous and is asking the Secretary of Labor not to adopt the ALJ's recommendation. If the recommendation is adopted by the Secretary of Labor, HL&P could appeal that decision to the United States Court of Appeals. Civil actions by these employees remain pending. For additional information, see Note 2(b) of the notes to the financial statements included in the Combined Form 8-K.

While no prediction can be made at this time as to the ultimate outcome of these matters, the Company and HL&P do not believe that they will have a material adverse effect on the Company's or HL&P's financial condition or results of operations.

(3) RATE REVIEW, FUEL RECONCILIATION AND OTHER PROCEEDINGS

In February 1994, the Public Utility Commission of Texas (Utility Commission) initiated a proceeding (Docket No. 12065) to determine whether HL&P's existing rates are just and reasonable. Subsequently, the scope of the docket was expanded to include reconciliation of HL&P's fuel costs from April 1, 1990 to July 31, 1994. The Utility Commission also initiated a

separate proceeding (Docket No. 13126) to review issues regarding the prudence of operation of the South Texas Project from the date of commercial operation through the present. That review would encompass the outage at the South Texas Project during 1993 and 1994.

Hearings began in Docket No. 12065 in January 1995. In February 1995, all major parties to these proceedings signed an agreement resolving the issues with respect to HL&P, including the prudence issues related to operation of the South Texas Project (Proposed Settlement). Approval of the Proposed Settlement by the Utility Commission will be required. Hearings on the Proposed Settlement are currently scheduled to begin in early June 1995. A decision by the Utility Commission on the Proposed Settlement is not anticipated before late summer.

Under the Proposed Settlement, HL&P's base rates would be reduced by approximately $62 million per year, effective retroactively to January 1, 1995, and HL&P would be precluded from seeking rate increases for three years, subject to certain conditions. Under the Proposed Settlement, HL&P would amortize its remaining investment of $218 million in the cancelled Malakoff Electric Generating Station (Malakoff) plant over a period not to exceed seven years. HL&P also would increase its decommissioning expense for the South Texas Project by $9 million per

year.

The Proposed Settlement also provides HL&P the option to write down up to $50 million per year of its investment in the South Texas Project during the five-year period commencing January 1, 1995. The parties to the Proposed Settlement agreed that any write down would be treated as a reasonable and necessary expense during routine reviews of HL&P's earnings and any rate review proceeding initiated against HL&P.

Until the approval of the Proposed Settlement by the Utility Commission, HL&P's existing rates will continue in effect; however, HL&P's financial statements for the first quarter of 1995 reflect the estimated effects of the Proposed Settlement. In the first quarter of 1995, HL&P's pre-tax earnings were reduced by approximately $17 million in the aggregate as a result of reflecting the estimated effects of the Proposed Settlement on revenues and expenses for the quarter. Deferred revenues are included on the Company's Consolidated and HL&P's Balance Sheets in other deferred credits subject to refund when the Proposed Settlement is approved.

Under the Proposed Settlement, approximately $70 million of fuel expenditures and related interest incurred by HL&P during the fuel reconciliation period would not be recoverable from ratepayers. This $70 million was recorded in the fourth quarter of 1994 as a one-time, pre-tax charge to reconcilable fuel revenues to reflect the anticipation of approval of the Proposed Settlement. Under the Proposed Settlement, HL&P would also establish a new fuel factor approximately 17 percent below that currently in effect and would refund to customers the balance in its fuel over-recovery account, estimated to be approximately $180 million after giving effect to the amounts not recoverable from ratepayers. As contemplated by the Proposed Settlement and approved by an ALJ, HL&P implemented a new fuel factor 17 percent lower than its previous factor and refunded to customers approximately $110 million of the approximately $180 million in fuel cost overrecoveries in April 1995. The remaining $70 million will be refunded if the Proposed Settlement is approved by the Utility Commission.

In the event the Proposed Settlement is not approved by the Utility Commission, Docket No. 12065 would be remanded to an ALJ to resume detailed hearings in this docket and with respect to issues related to the South Texas Project. Prior to reaching agreement on the terms of the Proposed Settlement, HL&P argued that its existing rates were just and reasonable and should not be reduced. Other parties argued that rate decreases in annual amounts ranging from $26 million to $173 million were required and that additional decreases might be justified following an examination of the prudence of the management of the South Texas Project and the costs incurred in connection with the outages at the South Texas Project. Testimony filed by the Utility Commission staff included a recommendation to remove from rate base $515 million of HL&P's investment in the South Texas Project to reflect the staff's view that such investment was not fully "used and useful" in providing service, a position HL&P vigorously disputes.

In the event the Proposed Settlement is not approved by the Utility Commission, the fuel reconciliation issues in Docket Nos. 12065 and 13126 would be remanded to an ALJ for additional proceedings. A major issue in Docket No. 13126 would be whether the incremental fuel costs incurred as a result of outages at the South Texas Project represent reasonable costs. The Utility Commission has retained a consultant to review the South Texas Project for the purpose of providing testimony in Docket No. 13126 regarding the prudence of HL&P's management of operation of the South Texas Project. HL&P filed testimony in Docket No. 13126, which testimony concluded that the outages at the South Texas Project did not result from imprudent management. HL&P also filed testimony analyzing the extent to which regulatory issues extended the outages. In that testimony an outside consultant retained by HL&P concluded that the duration of the outages was controlled by both the resolution of NRC regulatory issues as well as necessary equipment repairs unrelated to NRC regulatory issues and that the incremental effect of NRC regulatory issues on the duration of the outages was only 39 days per unit. Estimates as to the cost of replacement power may vary significantly based on a number of factors, including the capacity factor at which the South Texas Project might be assumed to have operated had it not been out of service due to the outages. However, HL&P believes that applying a reasonable range of assumptions would result in replacement fuel costs of less than $10 million for the 39 day periods identified by HL&P's consultant and less than $100 million for the entire length of the outages. Any fuel costs determined to have been unreasonably incurred would not be recoverable from customers and would be charged against the Company's earnings.

Although the Company and HL&P believe that the Proposed Settlement is in the best interest of HL&P, its ratepayers, the Company and its shareholders, no assurance can be given that (i) the Utility Commission ultimately will approve the terms of the Proposed Settlement or (ii) in the event the Proposed Settlement is not approved and proceedings against HL&P are resumed, that the outcome of such proceedings would be favorable to HL&P.

(9) CHANGE IN ACCOUNTING FOR THE COMPANY AND HL&P

The Company and HL&P adopted Statement of Financial Accounting Standards (SFAS) No. 112, "Employer's Accounting for Postemployment Benefits", effective January 1, 1994. SFAS No. 112 requires companies to recognize the liability for benefits provided to former or inactive employees, their beneficiaries and covered dependents after employment but before retirement. Those benefits include, but are not limited to, salary continuation, supplemental unemployment benefits, severance benefits, disability-related benefits (including worker's compensation), job training and counseling, and continuation of benefits such as health care and life insurance. SFAS No. 112 requires the transition obligation (liability from prior years) to be expensed upon adoption. As a result, the Company and HL&P recorded in the first quarter of 1994 a one-time, after-tax charge to income of $8.2 million.

ITEM 3. LEGAL PROCEEDINGS.

For a description of certain legal and regulatory proceedings affecting the Company and its subsidiaries (including (i) HL&P's rate cases, (ii) certain environmental matters and (iii) litigation related to the South Texas Project), see "Business - Regulatory Matters - Environmental Quality" in Item 1 of this Report, "LIQUIDITY AND CAPITAL RESOURCES - HL&P - Environmental Expenditures" in Item 7 of this Report and Notes 1(f) and 2 through 5 to the Financial Statements in Item 8 of this Report, which sections and notes are incorporated herein by reference.

HL&P is a defendant in litigation arising out of the environmental remediation of a site in Corpus Christi, Texas. The site in question was operated as a metals reclaiming operation for a number of years, and, though HL&P neither operated nor had any ownership interest in the site, some transformers and other equipment that HL&P sold as surplus allegedly were delivered to that site, where the site operators subsequently disposed of the materials in ways that caused environmental damage. In one case, DUMES, ET AL. V. HL&P, ET AL., pending in the U.S. District Court for the Southern District of Texas, Corpus Christi Division, a group of approximately 70 landowners near the site are seeking damages primarily for lead contamination to their property. They have pled damages of approximately $1 million each and also seek punitive damages totaling $51 million. The Plaintiffs seek to impose responsibility on HL&P and the other utility that undertook to clean up the property, neither of which contributed more than an insignificant amount of lead to the site, on the theory that lead was deposited on their properties during the site remediation itself. In addition, Gulf States Utilities Company (Gulf States) filed suit (GULF STATES UTILITIES CO. V. HOUSTON LIGHTING & POWER CO., ET AL.) in the United States District Court for the Southern District of Texas, Houston Division, against HL&P and two other utilities concerning a site in Houston, Texas, which allegedly has been contaminated by polychlorinated biphenyls and which Gulf States has undertaken to remediate pursuant to an EPA order. HL&P does not believe, based on its records, that it contributed material to that site and in October 1994, Gulf States dismissed its claims against HL&P. HL&P remains in the case on cross-claims asserted by two co-defendants. The ultimate outcome of these pending cases cannot be predicted at this time. Based on information currently available, the Company and HL&P believe that none of these cases will result in a material adverse effect on the Company's or HL&P's financial condition or results of operations.

HL&P and the other owners of the South Texas Project filed suit in 1990 against Westinghouse Electric Corporation (Westinghouse) in the 23rd District Court for Matagorda County, Texas (Cause No. 90-S-0684-C), alleging breach of warranty and misrepresentation in connection with the steam generators supplied by Westinghouse for the South Texas Project. In recent years, other utilities have encountered stress corrosion cracking in steam generator tubes in Westinghouse units similar to those supplied for the South Texas Project. Failure of such tubes can result in a reduction of plant efficiency, and, in some cases, utilities have replaced their steam generators. During an inspection concluded in the fall of 1993, evidence was found of stress corrosion cracking consistent with that encountered with Westinghouse steam generators at other facilities, and a small number of tubes were found to require plugging. To date, stress corrosion cracking has not had a significant impact on operation of either unit; however, the owners of the South Texas Project have approved remedial operating

plans and have undertaken expenditures to minimize and delay further corrosion. The litigation, which is in discovery, seeks appropriate damages and other relief from Westinghouse and is currently scheduled for trial in July 1995. No prediction can be made as to the ultimate outcome of this litigation.

In April 1994, two former employees of HL&P filed a class action and shareholder derivative suit on behalf of all shareholders of the Company. This lawsuit (PACE AND FUENTEZ V. HOUSTON INDUSTRIES INCORPORATED) alleges various acts of mismanagement against certain officers and directors of the Company and HL&P and, seeks unspecified actual and punitive damages for the benefit of shareholders of the Company. The Company and HL&P believe that the suit is without merit. The lawsuit is pending in the 122nd Judicial District of Galveston County, Texas.

In June 1994, a former employee of HL&P filed a lawsuit (PACE, INDIVIDUALLY AND AS A REPRESENTATIVE OF ALL OTHERS SIMILARLY SITUATED V. HOUSTON LIGHTING & POWER COMPANY) in the 56th Judicial District Court of Galveston County, Texas alleging that HL&P has been overcharging ratepayers and owes a refund of more than $500 million. The claim was based on the argument that the Utility Commission failed to allocate to ratepayers alleged tax benefits accruing to the Company and HL&P because HL&P's federal income taxes are paid as part of a consolidated group. The court has granted HL&P's motion for summary

judgment, which has now become final.

In July 1990, the Company paid approximately $104.5 million to the Internal Revenue Service (IRS) in connection with an IRS audit of the Company's 1983 and 1984 federal income tax returns. In November 1991, the Company filed a refund suit in the U.S. Court of Federal Claims seeking the return of $52.1 million of tax, $36.3 million of accrued interest, plus interest on both of those amounts accruing after July 1990. The major contested issue in the refund case involved the IRS's allegation that certain amounts related to the over-recovery of fuel costs should have been included as taxable income in 1983 and 1984 even though HL&P had an obligation to refund the over-recoveries to its ratepayers. In October 1994, the Court granted the Company's Motion for Partial Summary Judgment on the fuel cost over-recovery issue. On February 21, 1995, the Court entered partial judgment in favor of the Company for this issue. The U.S. Government (Government) must file its notice of appeal on or before April 24, 1995. If the Government does not appeal or if the Government appeals but does not prevail, the Company would be entitled to a refund of overpaid tax, interest paid on the overpaid tax in July 1990 and interest on both of those amounts from July 1990. Although, the Company would not be entitled to a refund until all appeals are decided in its favor, the amount owed to the Company will continue to accrue interest. If the Government appeals and prevails, the Company's ultimate financial exposure should be immaterial because of offsetting tax deductions to which the Company is entitled in the year the over-recovery was refunded to ratepayers (and which the IRS has conceded).

EXHIBIT 99(e)

ITEM 1. LEGAL PROCEEDINGS.

For a description of legal proceedings affecting the Company and its subsidiaries, including HL&P, reference is made to the information set forth in Item 3 of the Company's and HL&P's Annual Report on Form 10-K for the year ended December 31, 1994 (1994 Combined Form 10-K) and Notes 2, 3 and 4 to the Company's Consolidated and HL&P's Financial Statements in the Combined Form 8-K, which information, as qualified and updated by the description of developments in regulatory and litigation matters contained in Notes 2, 3 and 4 of the Notes to the Company's Consolidated and HL&P's Financial Statements included in Part I of this Report, is incorporated herein by reference.

In April 1995, the government filed a notice of appeal with respect to the judgment entered in favor of the Company in its refund suit pending in the U.S. Court of Federal Claims. For additional information regarding the Company's tax case, see Item 3 to the 1994 Combined Form 10-K.

COMPETITION

HL&P and other members of the electric utility industry, like other regulated industries, are being subjected to technological, regulatory and economic pressures that are increasing competition and offer the possibility for fundamental changes in the industry and its regulation. The electric utility industry historically has been composed of vertically integrated companies which largely have been the exclusive providers of electric service within a governmentally- defined geographic area. Prices for that service have been set by governmental authority under

principles that were designed to provide the utility with an opportunity to recover its costs of providing electric service plus a reasonable return on its invested capital.

By legislation adopted in 1978, Congress contributed to the development of new sources of electric generation by freeing cogenerators (i.e., facilities which produce electrical energy along with thermal energy used for industrial processes, usually the generation of steam) from most regulatory constraints applicable to traditional utilities, such as state and federal pricing regulation and organizational restrictions arising under the 1935 Act. This legislation contributed to the development of approximately 40 cogeneration facilities in the highly industrialized Houston area, with a power generation capability of over 5,000 MW. As a consequence, HL&P has lost some industrial customers to self-generation (representing approximately 2,500 MW), and additional projects continue to be considered by customers.

In 1992 Congress authorized, in the Energy Policy Act, another category of wholesale generators, Exempt Wholesale Generators (EWGs). Like cogenerators, these entities exist to sell electric energy at wholesale, but unlike cogenerators, EWGs may be formed for the generation of electricity without regard to the simultaneous production of thermal energy. Congress chose to free EWGs from the structural constraints applicable to traditional utilities under the 1935 Act, but Congress also authorized traditional utilities to form such entities themselves without being burdened by those restrictions. At the same time, Congress placed significant limitations on the ability of traditional utilities to purchase power in their own service territories from an affiliated EWG.

There are increasing pressures today by both cogenerators and exempt wholesale generators for access to the electric transmission and distribution systems of the regulated utilities in order to have greater flexibility in moving power to other purchasers, including access for the purpose of making retail sales to either affiliates of the unregulated generator or to other customers of the regulated utility. In February 1995, a new entity sought permission from the Public Utility Commission of Texas (Utility Commission) to construct a transmission line within HL&P's service territory for the purpose of transmitting power from a cogeneration facility owned by an industrial concern to an affiliate of that concern. This proceeding has been docketed by the Utility Commission, but currently is in its early stages.

Neither federal nor Texas law currently permits retail sales by unregulated entities. However, changes to the Federal Power Act made in the Energy Policy Act of 1992 increase the power of the Federal Energy Regulatory Commission (FERC) to order utilities to transmit power generated by both regulated and unregulated entities to other wholesale customers, and efforts are underway in some states that may lead to broader authorization of transmission access for such entities and even to retail sales by such entities. HL&P anticipates that some of those arguments will be advanced in the current session of the Texas legislature during the consideration of the re-enactment to the Public Utility Regulatory Act (PURA), which governs electric regulation in Texas.

Traditional utilities such as HL&P also face increased competition from alternate energy sources, primarily natural gas. Gas suppliers increasingly are seeking to supplant traditional electric loads with gas-powered equipment, such as gas-powered chillers in air conditioning installations.

HL&P continues to maintain an aggressive approach in attempting to preserve its existing customer base. HL&P has instituted various programs to reduce its costs and has adopted aggressive marketing programs to identify and respond to customer needs. One example is HL&P's development of the San Jacinto Steam Electric Station, a rate-based cogeneration facility that will begin service in 1995. In addition, in February 1995, the Utility Commission approved a new tariff proposed by HL&P that will allow special pricing for industrial customers who can demonstrate the ability to obtain electric service on terms more favorable than HL&P's traditional tariff offerings. While such pricing may retain such customers and minimize the prospect that HL&P would be left with

stranded investment whose costs might have to be borne by customers who have no other alternatives, HL&P's revenues and earnings will be reduced from such pricing tariffs.

In addition, HL&P and nine other Texas investor-owned utilities are supporting a legislative proposal for amendment to the PURA. That proposal calls for (i) a streamlined resource planning process, (ii) competitive bidding for new generation capacity requirements, (iii) regulatory incentives that reward efficiency and innovation and (iv) granting utilities pricing flexibility to meet the changing needs of their customers. These changes, if adopted in the form proposed by the utilities, would enhance the flexibility of regulated entities to address competition, while also providing utility customers with the benefits of more diverse energy supplies.

Under rules adopted by the Utility Commission and under interconnection guidelines adopted by the Electric Reliability Council of Texas, Inc., through which a number of utilities and unregulated suppliers are connected, HL&P and other Texas utilities have provided for movement of power for both regulated and unregulated power suppliers at compensatory rates. Unregulated power suppliers continue to seek additional access and more favorable pricing provisions.

At this time it is impossible to predict what changes to the electric utility industry will emerge as a result of any legislative changes that may be adopted by the Texas legislature. Nor is it possible to predict what other changes to the industry will emerge from federal regulatory and legislative initiatives or from regulatory decisions of the Utility Commission, though, it seems likely that such changes ultimately will increase the competition HL&P faces in supplying electric energy to its customers.

REGULATION OF THE COMPANY

FEDERAL

The Company is a holding company as defined in the 1935 Act; however, based upon the intrastate operations of HL&P and the exemptions applicable to the affiliates of HI Energy, the Company is exempt from regulation as a "registered" holding company under the 1935 Act except with respect to the acquisition of voting securities of other domestic public utility companies and holding companies. The Company has no present intention of entering into any transaction which would cause it to become a registered holding company subject to regulation by the Securities and Exchange Commission (SEC) under the 1935 Act. In November 1994, the SEC issued a Concept Release that called for comments on a broad range of topics relevant to regulation of both registered and exempt companies under the 1935 Act. In calling for comments, the SEC acknowledged that significant changes are affecting the electric utility industry, and in responding, some utilities have argued for repeal or substantial modification of the 1935 Act and the regulation it provides. At this time, no prediction can be made as to what changes, if any, will result from this review by the SEC, but repeal or significant modification to the 1935 Act may have an effect on the electric utility industry. In addition, it is possible that changes to the 1935 Act and its interpretation would eliminate some distinctions between exempt and registered companies in their regulation under the 1935 Act, possibly in ways that would increase the regulatory burdens on exempt companies such as the Company.

EXHIBIT 99(g)

HOUSTON INDUSTRIES INCORPORATED
SAVINGS PLAN

(As Amended and Restated Effective July 1, 1995)

FIRST AMENDMENT

Houston Industries Incorporated, a Texas corporation (the "Company"), established the Houston Industries Incorporated Savings Plan, as amended and restated effective July 1, 1995 and thereafter amended (the "Plan"), and reserved the right to amend the Plan to itself, and to the Benefits Committee of the Company (the "Committee") with regard to modification of the administrative provisions of the Plan, under Section 10.3 of the Plan.

By Agreement and Plan of Merger, dated as of January 26, 1995, by and among the Company, KBLCOM INCORPORATED, a Delaware corporation ("KBLCOM"), TIME WARNER INC., a Delaware corporation ("TW"), and TW KBLCOM ACQUISITION CORP., a Delaware corporation and wholly owned subsidiary of TW, TW will acquire by merger all of the issued and outstanding common stock of KBLCOM on or about July 6, 1995 (the "Merger" herein). In connection with said Merger, and as authorized by the related resolutions of the Special Meeting of the Board of Directors of the Company dated January 25, 1995, the Company hereby amends the Plan as set forth in Items 1-18 below, to reflect KBLCOM's termination of the Plan with respect to its employees effective as of the close of business on June 30, 1995, such amendments to be contingent upon the consummation of the Merger prior to August 1, 1995. Pursuant to its authority to make administrative amendments to the Plan, the Committee hereby amends the Plan effective as of June 30, 1995, as set forth in Item 19 below.

1. Section 1.2 of the Plan is amended by deleting the last sentence thereof.

2. The second sentence of Section 1.11 of the Plan is amended to read as follows:

> "Compensation specifically includes salaries, wages, commissions, overtime pay, benefits paid under the Houston Industries Incorporated Executive Incentive Compensation Plan (including annual and long-term awards) and the Houston Industries Energy, Inc. Annual Incentive Compensation Plan, and any other payments of compensation which would be subject to tax under Code Section 3101(a), without the dollar limitations of Code Section 3121(a)(1)."

3. Section 1.13 of the Plan is hereby amended in its entirety to read as follows:

> "1.13 DEFINED BENEFIT PLAN: The Houston Industries Incorporated Retirement Plan and/or any other defined benefit plan (as defined in Section 415(k) of the Code) maintained by the Company or by any Affiliate."

4. Section 1.16 of the Plan is hereby amended in its entirety to read as follows:

> "1.16 EMPLOYER: The Company (including its successors), Houston Lighting & Power Company, Houston Industries Energy, Inc., Houston Industries Products, Inc., and any other eligible organization that shall adopt this Plan pursuant to the provisions of Article X, and the successors, if any, to such organization."

5. Section 1.27 of the Plan is hereby amended in its entirety to read as follows:

> "1.27 HII PARTICIPANT: A Participant who is participating as an employee of Houston Industries Incorporated or as an employee of any of its subsidiaries or affiliates."

6. Section 1.30 is hereby amended in its entirety to read as follows:

> "1.30 KBLCOM PARTICIPANT: A Participant who was actively participating in this Plan as an employee of KBLCOM Incorporated or as an employee of any of KBLCOM Incorporated's subsidiaries prior to July 1, 1995."

7. Section 1.39 of the Plan is hereby amended in its entirety to read as follows:

"1.39 RETIREMENT DATE: With respect to HII Participants employed prior to January 1, 1988, the term `Retirement Date' shall mean the first day of the calendar month coincident with or next following the 65th birthday of a Participant; and, with respect to HII Participants hired on or after January 1, 1988, such term shall mean the later of (i) the Participant's attainment of age 65 or (ii) the fifth anniversary of the Participant's commencement of participation in the Plan."

8. Section 3.1 of the Plan is amended by adding the following sentence at the end thereof:

"The foregoing provisions of this Section 3.1 notwithstanding, no Employee of KBLCOM shall be eligible to participate in the Plan after June 30, 1995; provided, however, that a KBLCOM Participant with an Account balance under the Plan as of June 30, 1995 which has not been forfeited shall have those rights of participation granted to a former Employee in Section 1.31."

9. The second paragraph of Section 4.1 of the Plan is hereby amended in its entirety to read as follows:

"The Employer shall also make an Employer Matching Contribution (subject to adjustments for forfeitures and limitations on annual additions as elsewhere specified in the Plan) in the amount, if any, necessary to result in a total allocation under Article V to each Participant's Prior Plan and ESOP Accounts of not less than 70% of the total of his Pre-Tax Basic Contribution and After-Tax Basic Contribution for the Plan Year in the case of HII Participants. Further, the Employer shall make an additional ESOP Contribution and/or Employer Matching Contribution, if necessary, to make the allocation required under Section 5.3(d)(ii) with respect to dividends used to repay an Exempt Loan. The above provisions of this Section 4.1 notwithstanding, KBLCOM shall make no Employer Contributions to the Plan after June 30, 1995, except such Employer Contributions due with respect to services performed by Employees of KBLCOM on or before June 30, 1995."

10. The second sentence of Section 4.2 of the Plan is amended to read as follows:

"In addition, each HII Participant may also elect to defer any whole percent, up to a maximum of 10%, of his Compensation, as a Pre-Tax Excess Contribution."

11. Section 4.2 of the Plan is amended by adding the following sentence at the end thereof:

"The foregoing provisions of this Section 4.2 notwithstanding, no KBLCOM Participant shall be allowed to make Pre-Tax Contributions to the Plan with respect to employment with KBLCOM after June 30, 1995."

12. The last paragraph of Section 4.3 of the Plan is hereby deleted.

13. The third sentence of Section 5.3(b) is amended to read as follows:

"Allocations made pursuant to this Section 5.3(b) shall be made as soon as practicable after the close of each payroll period in an amount not to exceed 70% of the total of each HII Participant's Pre-Tax Basic Contributions and After-Tax Basic Contributions."

14. The first paragraph of Section 6.1 of the Plan is amended by adding the following sentence at the end thereof:

"The foregoing provisions of this Section 6.1 notwithstanding, each KBLCOM Participant who was an active Employee at any time between January 1, 1995 and June 30, 1995, inclusive, and each KBLCOM Participant with an Account balance under the Plan as of January 1, 1995 which was subject to forfeiture as of such date, shall be fully vested in his Accounts as of that date."

15. The last sentence of Section 6.5 is amended to read as follows:

"Otherwise, except to the extent that distribution of a Participant's Account is required prior to termination of employment under Section 6.10 hereof (in the case of a Participant whose required beginning date occurs prior to his termination of employment) or under Section 10.5 hereof relating to termination of the Plan, or at the election of the Participant under Article VII hereof relating to certain withdrawals and

loans, no distribution or withdrawal of any benefits under the Plan shall be permitted prior to the Participant's "separation from service, death or disability" within the meaning of Code Section 401(k) and the regulations thereunder other than a distribution authorized under the Plan upon the occurrence of an event described in, and made in accordance with, Code Section 401(k)(10) or any successor provision of the Code."

16. Section 6.8 of the Plan is amended by adding the following sentence at the end thereof:

"The foregoing provisions of this Section 6.8 notwithstanding, (a) eligible KBLCOM Participants shall be entitled to receive a final distribution of their

Accounts in accordance with the provisions of Code Section 401(k)(10) upon the closing of that certain Agreement and Plan of Merger among the Company, KBLCOM, Time Warner Inc. and TW KBLCOM Acquisition Corp. dated as of January 26, 1995 and (b) such KBLCOM Participants who made an election on or before June 30, 1995 to receive a final distribution of their Accounts shall receive a final distribution of their Accounts as soon as practicable following such closing, valued in accordance with Section 6.8 of the Prior Plan as though such KBLCOM Participants had terminated employment on June 30, 1995."

17. Section 7.4 of the Plan is amended by adding the following sentence at the end thereof:

"The foregoing provisions of this Section 7.4 notwithstanding, no KBLCOM Participant shall be allowed to receive a new loan or maintain an outstanding loan under the Plan after June 30, 1995 and prior to the closing of that certain Agreement and Plan of Merger among the Company, KBLCOM, Time Warner Inc. and TW KBLCOM Acquisition Corp. dated as of January 26, 1995."

18. Article XII of the Plan is amended by adding the following Section 12.9 at the end thereof:

"12.9 TRANSITION PERIOD: Notwithstanding any provision of the Plan to the contrary, during the period of transition from the provisions of the Prior Plan to this Plan, commencing July 1, 1995 and ending on or about September 15, 1995 as determined by the Committee in its sole discretion, the following restrictions shall apply: (i) Participants may not change their investment directions with respect to future contributions or existing Account balances; (ii) Participants may be limited in their ability to make changes in the amount of their Pre-Tax and After-Tax Contributions; and (iii) loans, withdrawals and distributions otherwise available under the Plan may be temporarily delayed, all in accordance with such administrative procedures as may be decided by the Committee and communicated to Participants during said transition."

IN WITNESS WHEREOF, Houston Industries Incorporated has caused these presents to be executed by its duly authorized officers in a number of copies, all of which shall constitute one and the same instrument, which may be sufficiently evidenced by any executed copy hereof, on this 29th day of June, 1995, but effective as of the close of business on June 30, 1995, subject to the consummation of the Merger on or before July 31, 1995.

HOUSTON INDUSTRIES INCORPORATED

By /s/ D. D. SYKORA
D. D. Sykora
President and Chief
Operating Officer

ATTEST:

/s/ RUFUS S. SCOTT
Rufus S. Scott
Assistant Corporate Secretary

IN WITNESS WHEREOF, the Benefits Committee of Houston Industries Incorporated has caused these presents to be executed by its duly authorized Chairman in a number of copies, all of which shall constitute one and the same instrument, which may be sufficiently evidenced by any executed copy hereof, on this 29th day of June, 1995, but effective as of June 30, 1995.

BENEFITS COMMITTEE OF HOUSTON
INDUSTRIES INCORPORATED

By /s/ D. D. SYKORA
D. D. Sykora, Chairman

ATTEST:

/s/ E. P. WEYLANDT
E. P. Weylandt
Secretary

EXHIBIT 12

HOUSTON LIGHTING & POWER COMPANY
COMPUTATION OF RATIOS OF EARNINGS TO FIXED CHARGES AND
RATIOS OF EARNINGS TO FIXED CHARGES AND PREFERRED DIVIDENDS
(THOUSANDS OF DOLLARS)

	SIX MONTHS ENDED JUNE 30,1995	TWELVE MONTHS ENDED JUNE 30, 1995
Fixed Charges as Defined:		
(1) Interest on Long-Term Debt	$ 122,917	$ 246,051
(2) Other Interest	3,924	7,668
(3) Amortization of (Premium) Discount	4,247	8,489
(4) Interest Component of Rentals Charged to Operating Expense	1,926	3,967
(5) Total Fixed Charges	$ 133,014	$ 266,175
Earnings as Defined:		
(6) Net Income	$ 192,217	$ 478,140
Federal Income Taxes:		
(7) Current	61,609	165,957
(8) Deferred (Net)	34,276	75,502
(9) Total Federal Income Taxes	95,885	241,459
(10) Total Fixed Charges (line 5)	133,014	266,175
(11) Earnings Before Income Taxes and Fixed Charges (line 6 plus line 9 plus line 10)	$ 421,116	$ 985,774
Ratio of Earnings to Fixed Charges (line 11 divided by line 5)	3.17	3.70
Preferred Dividends Requirements:		
(12) Preferred Dividends	$ 16,435	$ 33,342
(13) Less Tax Deduction for Preferred Dividends	27	54
(14) Total	16,408	33,288
(15) Ratio of Pre-Tax Income to Net Income (line 6 plus line 9 divided by line 6)	1.50	1.50
(16) Line 14 times line 15	24,612	49,932
(17) Add Back Tax Deduction (line 13)	27	54
(18) Preferred Dividends Factor	$ 24,639	$ 49,986
(19) Total Fixed Charges (line 5)	$ 133,014	$ 266,175
(20) Preferred Dividends Factor (line 18)	24,639	49,986
(21) Total	$ 157,653	$ 316,161
Ratio of Earnings to Fixed Charges and Preferred Dividends Requirements (line 11 divided by line 21)	2.67	3.12

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THIS SCHEDULE CONTAINS SUMMARY FINANCIAL INFORMATION EXTRACTED FROM HL&P'S FINANCIAL STATEMENTS AND IS QUALIFIED IN ITS ENTIRETY BY REFERENCE TO SUCH FINANCIAL STATEMENTS.

0000048732
HOUSTON LIGHTING & POWER
1000
6-MOS
DEC-31-1995
JUN-30-1995
PER-BOOK
8,989,667
0
371,206
1,357,861
0
10,718,734
1,675,927
0
2,164,391
3,840,318
51,055
351,345
3,007,949
0
0
0
150,144
25,700
6,909
3,616
3,281,698
10,718,734
1,724,391
96,310
1,306,096
1,402,406
321,985
(5,865)
316,120
123,903
192,217
16,435
175,782
164,500
122,878
374,648
0
0

Total annual interest charges on all bonds for year-to-date 6/30/95.

(f) DEFERRED PLANT COSTS. The Utility Commission authorized deferred accounting treatment for certain costs related to the South Texas Project Electric Generating Station (South Texas Project) in two contexts. The first was "deferred accounting" where HL&P was permitted to continue to accrue carrying costs in the form of AFUDC and defer and capitalize depreciation and other operating costs on its investment in the South Texas Project until such costs were reflected in rates. The second was the "qualified phase-in plan" where HL&P was permitted to capitalize as deferred charges allowable costs, including return, deferred for future recovery

under the approved plan. The accumulated deferrals for "deferred accounting" and "qualified phase-in plan" are being recovered over the estimated depreciable life of the South Texas Project and within the ten year phase-in period, respectively. The amortization of these deferrals totaled $25.8 million for each of the years 1994, 1993, and 1992 and is included on the Company's Statements of Consolidated Income and HL&P's Statements of Income in depreciation and amortization expense. Under the terms of the settlement agreement regarding the issues raised in Docket Nos. 12065 and 13126 (Proposed Settlement), see Note 3, the South Texas Project deferrals will continue to be amortized using the schedules discussed above.

(2) JOINTLY-OWNED NUCLEAR PLANT

(a) HL&P INVESTMENT. HL&P is the project manager (and one of four co-owners) of the South Texas Project, which consists of two 1,250 megawatt nuclear generating units. HL&P has a 30.8 percent interest in the project and bears a corresponding share of capital and operating costs associated with the project. As of December 31, 1994, HL&P's investments (net of accumulated depreciation and amortization) in the South Texas Project and in nuclear fuel, including AFUDC, were $2.1 billion and $99 million, respectively.

(b) UNITED STATES NUCLEAR REGULATORY COMMISSION (NRC) INSPECTIONS AND OPERATIONS. Both generating units at the South Texas Project were out of service from February 1993 to February 1994, when Unit No. 1 was returned to service. Unit No. 2 was returned to service in May 1994. HL&P removed the units from service in February 1993 when a problem was encountered with certain of the units' auxiliary feedwater pumps.

In February 1995, the NRC removed the South Texas Project from its "watch list" of plants with weaknesses that warranted increased NRC attention. The NRC placed the South Texas Project on the "watch list" in June 1993, following the issuance of a report by an NRC Diagnostic Evaluation Team (DET) which conducted a review of the South Texas Project operations.

Certain current and former employees of HL&P or contractors of HL&P have asserted claims that their employment was terminated or disrupted in retaliation for their having made safetyrelated complaints to the NRC. Civil proceedings by the complaining personnel and administrative proceedings by the Department of Labor remain pending against HL&P, and the NRC has jurisdiction to take enforcement action against HL&P and/or individual employees with respect to these matters. Based on its own internal investigation, in October 1994 the NRC issued a notice of violation and proposed a $100,000 civil penalty against HL&P in one such case in which HL&P had terminated the site access of a former contractor employee. In that action, the NRC also requested information relating to possible further enforcement action in this matter against two HL&P managers involved in such termination. HL&P strongly disagrees with the NRC's conclusions, and has requested the NRC to give further consideration of its notice. In February 1995, the NRC conducted an enforcement conference with respect to that matter, but no result has been received.

HL&P has provided documents and other assistance to a subcommittee of the U. S. House of Representatives (Subcommittee) that is conducting an inquiry related to the South Texas Project. Although the precise focus and timing of the inquiry has not been identified by the Subcommittee, it is anticipated that the Subcommittee will inquire into matters related to HL&P's handling of employee concerns and to issues related to the NRC's 1993 DET review of the South Texas Project. In connection with that inquiry, HL&P has been advised that the U. S. General Accounting Office (GAO) is conducting a review of the NRC's inspection process as it relates to the South Texas Project and other plants, and HL&P is cooperating with the GAO in its

investigation and with the NRC in a similar review it has initiated. While no prediction can

be made at this time as to the ultimate outcome of these matters, the Company and HL&P do not believe that they will have a material adverse effect on the Company's or HL&P's financial condition or results of operations.

(c) LITIGATION WITH CO-OWNERS OF THE SOUTH TEXAS PROJECT. In February 1994, the City of Austin (Austin), one of the four co-owners of the South Texas Project, filed suit (Austin II Litigation) against HL&P. That suit is pending in the 152nd District Court for Harris County, Texas, which has set a trial date for October 1995. Austin alleges that the outages at the South Texas Project from early 1993 to early 1994 were due to HL&P's failure to perform obligations it owed to Austin under the Participation Agreement among the four co-owners of the South Texas Project (Participation Agreement). Austin also asserts that HL&P breached certain undertakings voluntarily assumed by HL&P under the terms and conditions of the Operating Licenses and Technical Specifications relating to the South Texas Project. Austin claims that such failures have caused Austin damages of at least $125 million due to the incurrence of increased operating and maintenance costs, the cost of replacement power and lost profits on wholesale transactions that did not occur. In May 1994, the City of San Antonio (San Antonio), another co-owner of the South Texas Project, intervened in the litigation filed by Austin against HL&P and asserted claims similar to those asserted by Austin. San Antonio has not identified the amount of damages it intends to seek from HL&P. HL&P is contesting San Antonio's intervention and has called for arbitration of San Antonio's claim under the arbitration provisions of the Participation Agreement. The trial court has denied HL&P's requests, but review of these decisions is currently pending before the 1st Court of Appeals in Houston.

In a previous lawsuit (Austin I Litigation) filed in 1983 against the Company and HL&P, Austin alleged that it had been fraudulently induced to participate in the South Texas Project and that HL&P had failed to perform properly its duties as project manager. In May 1993, the courts entered a judgement in favor of the Company and HL&P, concluding, among other things, that the Participation Agreement did not impose on HL&P a duty to exercise reasonable skill and care as project manager. During the course of the Austin I Litigation, San Antonio and Central Power and Light Company (CPL), a subsidiary of Central and South West Corporation, two of the co-owners in the South Texas Project, also asserted claims for unspecified damages against HL&P as project manager of the South Texas Project, alleging HL&P breached its duties and obligations. San Antonio and CPL requested arbitration of their claims under the Participation Agreement. In 1992, the Company and HL&P entered into a settlement agreement with CPL (CPL Settlement) providing for CPL's withdrawal of its demand for arbitration. San Antonio's claims for arbitration remain pending. Under the Participation Agreement, San Antonio's arbitration claims will be heard by a panel of five arbitrators consisting of four arbitrators named by each co-owner and a fifth arbitrator selected by the four appointed arbitrators.

Although the CPL Settlement did not directly affect San Antonio's pending demand for arbitration, HL&P and CPL reached certain understandings in such agreement which contemplated that: (i) CPL's previously appointed arbitrator would be replaced by CPL; (ii) arbitrators approved by CPL or HL&P in any future arbitrations would be mutually acceptable to HL&P and CPL; and (iii) HL&P and CPL would resolve any future disputes between them concerning the South Texas Project without resorting to the arbitration provision of the

Participation Agreement. Austin and San Antonio have asserted in the pending Austin II Litigation that such understandings have rendered the arbitration provisions of the Participation Agreement void and that neither Austin nor San Antonio should be required to participate in or be bound by such proceedings.

Although HL&P and the Company do not believe there is merit to either Austin's or San Antonio's claims and have opposed San Antonio's intervention in the Austin II Litigation, there can be no assurance as to the ultimate outcome of these matters.

(d) NUCLEAR INSURANCE. HL&P and the other owners of the South Texas Project maintain nuclear property and nuclear liability insurance

coverage as required by law and periodically review available limits and coverage for additional protection. The owners of the South Texas Project currently maintain the maximum amount of property damage insurance currently available through the insurance industry, consisting of $500 million in primary property damage insurance and excess property insurance in the amount of $2.25 billion. Under the excess property insurance which became effective on March 1, 1995 and under portions of the excess property insurance coverage in effect prior to March 1, 1995, HL&P and the other owners of the South Texas Project are subject to assessments, the maximum aggregate assessment under current policies being $26.9 million during any one policy year. The application of the proceeds of such property insurance is subject to the priorities established by the NRC regulations relating to the safety of licensed reactors and decontamination operations.

Pursuant to the Price Anderson Act (Act), the maximum liability to the public for owners of nuclear power plants, such as the South Texas Project, was decreased from $9.0 billion to $8.92 billion effective in November 1994. Owners are required under the Act to insure their liability for nuclear incidents and protective evacuations by maintaining the maximum amount of financial protection available from private sources and by maintaining secondary financial protection through an industry retrospective rating plan. The assessment of deferred premiums provided by the plan for each nuclear incident is up to $75.5 million per reactor subject to indexing for inflation, a possible 5 percent surcharge (but no more than $10 million per reactor per incident in any one year) and a 3 percent state premium tax. HL&P and the other owners of the South Texas Project currently maintain the required nuclear liability insurance and participate in the industry retrospective rating plan.

There can be no assurance that all potential losses or liabilities will be insurable, or that the amount of insurance will be sufficient to cover them. Any substantial losses not covered by insurance would have a material effect on HL&P's and the Company's financial condition.

(e) NUCLEAR DECOMMISSIONING. HL&P and the other co-owners of the South Texas Project are required by the NRC to meet minimum decommissioning funding requirements to pay the costs of decommissioning the South Texas Project. Pursuant to the terms of the order of the Utility Commission in Docket No. 9850, HL&P is currently funding decommissioning costs for the South Texas Project with an independent trustee at an annual amount of $6 million, which is recorded in depreciation and amortization expense. HL&P's funding level is estimated to provide approximately $146 million, in 1989 dollars, an amount which exceeds the current NRC minimum.

The Company adopted SFAS No. 115, "Accounting for Certain Investments in Debt and Equity Securities," effective January 1, 1994. At December 31, 1994, the securities held in the Company's nuclear decommissioning trust totaling $25.1 million (reflected on the Company's Consolidated and HL&P's Balance Sheets in deferred debits and deferred credits) are classified as available for sale. Such securities are reported on the balance sheets at fair value, which at December 31, 1994 approximates cost, and any unrealized gains or losses will be reported as a separate component of common stock equity. Earnings, net of taxes and administrative costs, are reinvested in the funds.

In May 1994, an outside consultant estimated HL&P's portion of decommissioning costs to be approximately $318 million, in 1994 dollars. The consultant's calculation of decommissioning costs for financial planning purposes used the DECON methodology (prompt removal/dismantling), one of the three alternatives acceptable to the NRC, and assumed deactivation of Unit Nos. 1 and 2 upon the expiration of their 40 year operating licenses. Under the terms of the Proposed Settlement, HL&P would increase funding of decommissioning costs to an annual amount of approximately $14.8 million consistent with such study. While the current and projected funding levels presently exceed minimum NRC requirements, no assurance can be given that the amounts held in trust will be adequate to cover the actual decommissioning costs of the South Texas Project or the assumptions used in estimating decommissioning costs will ultimately prove to be correct.

(3) RATE REVIEW, FUEL RECONCILIATION AND OTHER PROCEEDINGS

In February 1994, the Utility Commission initiated a proceeding (Docket No. 12065) to determine whether HL&P's existing rates are just and reasonable. Subsequently, the scope of the docket was expanded to

include reconciliation of HL&P's fuel costs from April 1, 1990 to July 31, 1994. The Utility Commission also initiated a separate proceeding (Docket No. 13126) to review issues regarding the prudence of operation of the South Texas Project from the date of commercial operation through the present. That review would encompass the outage at the South Texas Project during 1993 through 1994.

Hearings began in Docket No. 12065 in January 1995, and the Utility Commission has retained a consultant to review the South Texas Project for the purpose of providing testimony in Docket No. 13126 regarding the prudence of HL&P's management of operation of the South Texas Project. In February 1995, all major parties to these proceedings signed the Proposed Settlement resolving the issues with respect to HL&P, including the prudence issues related to operation of the South Texas Project. Approval of the Proposed Settlement by the Utility Commission will be required. To that end, the parties have established procedural dates for a hearing on issues raised by the parties who are opposed to the Proposed Settlement. A decision by the Utility Commission on the Proposed Settlement is not anticipated before early summer.

Under the Proposed Settlement, HL&P's base rates would be reduced by approximately $62 million per year, effective retroactively to January 1, 1995, and rates would be frozen for three years, subject to certain conditions. Under the Proposed Settlement, HL&P would amortize its remaining investment of $218 million in the cancelled Malakoff plant over a period not to exceed

seven years. HL&P also would increase its decommissioning expense for the South Texas Project by $9 million per year.

Under the Proposed Settlement, approximately $70 million of fuel expenditures and related interest incurred by HL&P during the fuel reconciliation period would not be recoverable from ratepayers. This $70 million was recorded as a one-time, pre-tax charge to reconcilable fuel revenues to reflect the anticipation of approval of the Proposed Settlement. HL&P also would establish a new fuel factor approximately 17 percent below that currently in effect and would refund to customers the balance in its fuel over-recovery account, estimated to be approximately $180 million after giving effect to the amounts not recoverable from ratepayers.

HL&P recovers fuel costs incurred in electric generation through a fixed fuel factor that is set by the Utility Commission. The difference between fuel revenues billed pursuant to such factor and fuel expense incurred is recorded as an addition to or a reduction of revenue, with a corresponding entry to under- or over-recovered fuel, as appropriate. Amounts collected pursuant to the fixed fuel factor must be reconciled periodically against actual, reasonable costs as determined by the Utility Commission. Currently, HL&P has an over-recovery fuel account balance that will be refunded pursuant to the Proposed Settlement.

In the event that the Proposed Settlement is not approved by the Utility Commission, including issues related to the South Texas Project, Docket No. 12065 will be remanded to an Administrative Law Judge (ALJ) to resume detailed hearings in this docket. Prior to reaching agreement on the terms of the Proposed Settlement, HL&P argued that its existing rates were just and reasonable and should not be reduced. Other parties argued that rate decreases in annual amounts ranging from $26 million to $173 million were required and that additional decreases might be justified following an examination of the prudence of the management of the South Texas Project and the costs incurred in connection with the outages at the South Texas Project. Testimony filed by the Utility Commission staff included a recommendation to remove from rate base $515 million of HL&P's investment in the South Texas Project to reflect the staff's view that such investment was not fully "used and useful" in providing service, a position HL&P vigorously disputes.

In the event the Proposed Settlement is not approved by the Utility Commission, the fuel reconciliation issues in Docket Nos. 12065 and 13126 would be remanded to an ALJ for additional proceedings. A major issue in Docket No. 13126 will be whether the incremental fuel costs incurred as a result of outages at the South Texas Project represent reasonable costs. HL&P filed testimony in Docket No. 13126, which testimony concluded that the outages at the South Texas Project did not result from imprudent management. HL&P also filed testimony analyzing the extent to which regulatory issues extended the outages. In that testimony an outside consultant retained by HL&P concluded

that the duration of the outages was controlled by both the resolution of NRC regulatory issues as well as necessary equipment repairs unrelated to NRC regulatory issues and that the incremental effect of NRC regulatory issues on the duration of the outages was only 39 days per unit. Estimates as to the cost of replacement power may vary significantly based on a number of factors, including the capacity factor at which the South Texas Project might be assumed to have operated had it not been out of service due to the outages. However, HL&P believes that applying a reasonable range

of assumptions would result in replacement fuel costs of less than $10 million for the 39 day periods identified by HL&P's consultant and less than $100 million for the entire length of the outages. Any fuel costs determined to have been unreasonably incurred would not be recoverable from customers and would be charged against the Company's earnings.

Although the Company and HL&P believe that the Proposed Settlement is in the best interest of HL&P, its ratepayers, and the Company and its shareholders, no assurance can be given that (i) the Utility Commission ultimately will approve the terms of the Proposed Settlement or (ii) in the event the Proposed Settlement is not approved and proceedings against HL&P resumed, that the outcome of such proceedings would be favorable to HL&P.

(4) APPEALS OF PRIOR UTILITY COMMISSION RATE ORDERS

Pursuant to a series of applications filed by HL&P in recent years, the Utility Commission has granted HL&P rate increases to reflect in electric rates HL&P's substantial investment in new plant construction, including the South Texas Project. Although Utility Commission action on those applications has been completed, judicial review of a number of the Utility Commission orders is pending. In Texas, Utility Commission orders may be appealed to a District Court in Travis County, and from that Court's decision an appeal may be taken to the Court of Appeals for the 3rd District at Austin (Austin Court of Appeals). Discretionary review by the Supreme Court of Texas may be sought from decisions of the Austin Court of Appeals. The pending appeals from the Utility Commission orders are in various stages. In the event the courts ultimately reverse actions of the Utility Commission in any of these proceedings, such matters would be remanded to the Utility Commission for action in light of the courts' orders. Because of the number of variables which can affect the ultimate resolution of such matters on remand, the Company and HL&P generally are not in a position at this time to predict the outcome of the matters on appeal or the ultimate effect that adverse action by the courts could have on the Company and HL&P. On remand, the Utility Commission's action could range from granting rate relief substantially equal to the rates previously approved to a reduction in the revenues to which HL&P was entitled during the time the applicable rates were in effect, which could require a refund to customers of amounts collected pursuant to such rates. Judicial review has been concluded or currently is pending on the final orders of the Utility Commission described below.

(a) 1991 RATE CASE. In HL&P's 1991 rate case (Docket No. 9850), the Utility Commission approved a non-unanimous settlement agreement providing for a $313 million increase in HL&P's base rates, termination of deferrals granted with respect to Unit No. 2 of the South Texas Project and of the qualified phase-in plan deferrals granted with respect to Unit No. 1 of the South Texas Project, and recovery of deferred plant costs. The settlement authorized a 12.55 percent return on common equity for HL&P. Rates contemplated by the settlement agreement were implemented in May 1991 and remain in effect (subject to the outcome of the current rate proceeding described in Note 3).

The Utility Commission's order in Docket No. 9850 was affirmed on review by a District Court, and the Austin Court of Appeals affirmed that decision on procedural grounds due to the failure of the appellant to file the record with the court in a timely manner. On review, the Texas

Supreme Court has remanded the case to the Austin Court of Appeals for consideration of the appellant's challenges to the Utility Commission's order, which include issues regarding deferred accounting, the treatment of federal income tax expense and certain other matters. As to federal tax issues, a recent decision of the

Austin Court of Appeals, in an appeal involving GTE-SW (and to which HL&P was not a party), held that when a utility pays federal income taxes as part of a consolidated group, the utility's ratepayers are entitled to a fair share of the tax savings actually realized, which can include savings resulting from unregulated activities. The Texas Supreme Court has agreed to hear an appeal of that decision, but on points not involving the federal income tax issues, though tax issues could be decided in such opinion.

Because the Utility Commission's order in Docket No. 9850 found that HL&P would have been entitled to rate relief greater than the $313 million agreed to in the settlement, HL&P believes that any disallowance that might be required if the court's ruling in the GTE decision were applied in Docket No. 9850 would be offset by that greater amount. However, that amount may not be sufficient if the Austin Court of Appeals also concludes that the Utility Commission's inclusion of deferred accounting costs in the settlement was improper. For a discussion of the Texas Supreme Court's decision on deferred accounting treatment, see Note 4(c). Although HL&P believes that it could demonstrate entitlement to rate relief equal to that agreed to in the stipulation in Docket No. 9850, HL&P cannot rule out the possibility that a remand and reopening of that settlement would be required if decisions unfavorable to HL&P are rendered on both the deferred accounting treatment and the calculation of tax expense for rate making purposes.

The parties to the Proposed Settlement have agreed to withdraw their appeals of the Utility Commission's orders in such docket, subject to HL&P's dismissing its appeal in Docket No. 6668.

(b) 1988 RATE CASE. In HL&P's 1988 rate case (Docket No. 8425), the Utility Commission granted HL&P a $227 million increase in base revenues, allowed a 12.92 percent return on common equity, authorized a qualified phase-in plan for Unit No. 1 of the South Texas Project (including approximately 72 percent of HL&P's investment in Unit No. 1 of the South Texas Project in rate base) and authorized HL&P to use deferred accounting for Unit No. 2 of the South Texas Project. Rates substantially corresponding to the increase granted were implemented by HL&P in June 1989 and remained in effect until May 1991.

In August 1994, the Austin Court of Appeals affirmed the Utility Commission's order in Docket No. 8425 on all matters other than the Utility Commission's treatment of tax savings associated with deductions taken for expenses disallowed in cost of service. The court held that the Utility Commission had failed to require that such tax savings be passed on to ratepayers, and ordered that the case be remanded to the Utility Commission with instructions to adjust HL&P's cost of service accordingly. Discretionary review is being sought from the Texas Supreme Court by all parties to the proceeding.

The parties to the Proposed Settlement have agreed to dismiss their respective appeals of Docket No. 8425, subject to HL&P's dismissing its appeal in Docket No. 6668. A separate party to this appeal, however, has not agreed to dismiss its appeal.

(c) DEFERRED ACCOUNTING. Deferred accounting treatment for certain costs associated with Unit No. 1 of the South Texas Project was authorized by the Utility Commission in Docket No. 8230 and was extended in Docket No. 9010. Similar deferred accounting treatment with respect to Unit No. 2 of the South Texas Project was authorized in Docket No. 8425. For a discussion of the deferred accounting treatment granted, see Note 1(f).

In June 1994, the Texas Supreme Court decided the appeal of Docket Nos. 8230 and 9010, as well as all other pending deferred accounting cases involving other utilities, upholding deferred accounting treatment for both carrying costs and operation and maintenance expenses as within the Utility Commission's statutory authority and reversed the Austin Court of Appeals decision to the extent that the Austin Court of Appeals had rejected deferred accounting treatment for carrying charges. Because the lower appellate court had upheld deferred accounting only as to operation and maintenance expenses, the Texas Supreme Court remanded Docket Nos. 8230 and 9010 to the Austin Court of Appeals to consider the points of error challenging the granting of deferred accounting for carrying costs which it had not reached in its earlier consideration of the case. The Texas Supreme Court opinion did state, however, that when deferred costs are considered for addition to the utility's rate base in an ensuing rate case, the Utility Commission must then determine to what extent

inclusion of the deferred costs is necessary to preserve the utility's financial integrity. Under the terms of the Proposed Settlement, South Texas Project deferrals will continue to be amortized under the schedule previously established.

The Office of the Public Utility Counsel (OPUC) has agreed, pursuant to the Proposed Settlement, to withdraw and dismiss its appeal if the Proposed Settlement becomes effective and on the condition that HL&P dismisses its appeal in Docket No. 6668. However, the appeal of the State of Texas remains pending.

(d) PRUDENCE REVIEW OF THE CONSTRUCTION OF THE SOUTH TEXAS PROJECT. In June 1990, the Utility Commission ruled in a separate docket (Docket No. 6668) that had been created to review the prudence of HL&P's planning and construction of the South Texas Project that $375.5 million out of HL&P's $2.8 billion investment in the two units of the South Texas Project had been imprudently incurred. That ruling was incorporated into HL&P's 1988 and 1991 rate cases and resulted in HL&P's recording an after-tax charge of $15 million in 1990. Several parties appealed the Utility Commission's decision, but a District Court dismissed these appeals on procedural grounds. The Austin Court of Appeals reversed and directed consideration of the appeals, and the Texas Supreme Court denied discretionary review in 1994. At this time, no action has been taken by the appellants to proceed with the appeals. Unless the order in Docket No. 6668 is modified or reversed on appeal, the amount found imprudent by the Utility Commission will be sustained.

Under the Proposed Settlement, OPUC, HL&P and the City of Houston each has agreed to dismiss its respective appeals of Docket No. 6668. A separate party to this appeal, however, has not agreed to dismiss its appeal. If this party does not elect to dismiss its appeal, HL&P may elect to maintain its appeal, whereupon OPUC and City of Houston shall also be entitled to maintain their appeals.

(5)MALAKOFF

The scheduled in-service dates for the Malakoff units were postponed during the 1980's as expectations of continued strong load growth were tempered. In 1987, all developmental work was stopped and AFUDC accruals ceased. These units have been cancelled due to the availability of other cost effective resource options.

In Docket No. 8425, the Utility Commission allowed recovery of certain costs associated with the cancelled Malakoff units by amortizing those costs over ten years for rate making purposes. Such recoverable costs were not included in rate base and, as a result, no return on investment is being earned during the recovery period. The remaining balance at December 31, 1994 is $34 million with a recovery period of 66 months.

Also as a result of the final order in Docket No. 8425, the costs associated with the engineering design work for the Malakoff units were included in rate base and are earning a return. Subsequently, in December 1992, HL&P determined that such costs would have no future value and reclassified $84.1 million from plant held for future use to recoverable project costs. In 1993, an additional $7 million was reclassified to recoverable project costs. Amortization of these amounts began in 1993. The balance at December 31, 1994 was $65 million with a remaining recovery period of 60 months. The amortization amount is approximately equal to the amount currently earning a cash return in rates. The Utility Commission's decision to allow treatment of these costs as plant held for future use has been challenged in the pending appeal of the Docket No. 8425 final order. See Note 4(b) for a discussion of this proceeding.

In June 1990, HL&P purchased from its then fuel supply affiliate, Utility Fuels, Inc. (Utility Fuels), all of Utility Fuels' interest in the lignite reserves and lignite handling facilities for Malakoff. The purchase price was $138.2 million, which represented the net book value of Utility Fuels' investment in such reserves and facilities. As part of the June 1990 rate order (Docket No. 8425), the Utility Commission ordered that issues related to the prudence of the amounts invested in the lignite reserves be considered in HL&P's next general rate case which was filed in November 1990 (Docket No. 9850). However, under the October 1991 Utility Commission order in Docket No. 9850, this determination was postponed to a subsequent docket.

HL&P's remaining investment in Malakoff lignite reserves as of December 31, 1994 of $153 million is included on the Company's

Consolidated and HL&P's Balance Sheets in plant held for future use. HL&P anticipates that an additional $8 million of expenditures relating to lignite reserves will be incurred in 1995 and 1996.

In Docket No. 12065, HL&P filed testimony in support of the amortization of substantially all of its remaining investment in Malakoff, including the portion of the engineering design costs for which amortization had not previously been authorized and the amount attributable to related lignite reserves which had not previously been addressed by the Utility Commission. Under the Proposed Settlement of Docket No. 12065, HL&P would amortize its investment in Malakoff over a period not to exceed seven years such that the entire investment will be written off no later than December 31, 2002. See Note 3. In the event that the Utility Commission does not

approve the Proposed Settlement, and if appropriate rate treatment of these amounts is not ultimately received, HL&P could be required to write off any unrecoverable portions of its Malakoff investment.

(2) JOINTLY-OWNED NUCLEAR PLANT

(a) HL&P INVESTMENT. HL&P is the project manager (and one of four co-owners) of the South Texas Project, which consists of two 1,250 megawatt nuclear generating units. HL&P has a 30.8 percent interest in the project and bears a corresponding share of capital and operating

costs associated with the project. As of December 31, 1994, HL&P's investments (net of accumulated depreciation and amortization) in the South Texas Project and in nuclear fuel, including AFUDC, were $2.1 billion and $99 million, respectively.

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(c) LITIGATION WITH CO-OWNERS OF THE SOUTH TEXAS PROJECT. In February 1994, the City of Austin (Austin), one of the four co-owners of the South Texas Project, filed suit (Austin II Litigation) against HL&P. That suit is pending in the 152nd District Court for Harris County, Texas, which has set a trial date for October 1995. Austin alleges that the outages at the South Texas

Project from early 1993 to early 1994 were due to HL&P's failure to perform obligations it owed to Austin under the Participation Agreement among the four co-owners of the South Texas Project (Participation Agreement). Austin also asserts that HL&P breached certain undertakings voluntarily assumed by HL&P under the terms and conditions of the Operating Licenses and Technical Specifications relating to the South Texas Project. Austin claims that such failures have caused Austin damages of at least $125 million due to the incurrence of increased operating and maintenance costs, the cost of replacement power and lost profits on wholesale transactions that did not occur. In May 1994, the

City of San Antonio (San Antonio), another co-owner of the South Texas Project, intervened in the litigation filed by Austin against HL&P and asserted claims similar to those asserted by Austin. San Antonio has not identified the amount of damages it intends to seek from HL&P. HL&P is contesting San Antonio's intervention and has called for arbitration of San Antonio's claim under the arbitration provisions of the Participation Agreement. The trial court has denied HL&P's requests, but review of these decisions is currently pending before the 1st Court of Appeals in Houston.

In a previous lawsuit (Austin I Litigation) filed in 1983 against the Company and HL&P, Austin alleged that it had been fraudulently induced to participate in the South Texas Project and that HL&P had failed to perform properly its duties as project manager. In May 1993, the courts entered a judgement in favor of the Company and HL&P, concluding, among other things, that the Participation Agreement did not impose on HL&P a duty to exercise reasonable skill and care as project manager. During the course of the Austin I Litigation, San Antonio and Central Power and Light Company (CPL), a subsidiary of Central and South West Corporation, two of the co-owners in the South Texas Project, also asserted claims for unspecified damages against HL&P as project manager of the South Texas Project, alleging HL&P breached its duties and obligations. San Antonio and CPL requested arbitration of their claims under the Participation Agreement. In 1992, the Company and HL&P entered into a settlement agreement with CPL (CPL Settlement) providing for CPL's withdrawal of its demand for arbitration. San Antonio's claims for arbitration remain pending. Under the Participation Agreement, San Antonio's arbitration claims will be heard by a panel of five arbitrators consisting of four arbitrators named by each co-owner and a fifth arbitrator selected by the four appointed arbitrators.

Although the CPL Settlement did not directly affect San Antonio's pending demand for arbitration, HL&P and CPL reached certain understandings in such agreement which contemplated that: (i) CPL's previously appointed arbitrator would be replaced by CPL; (ii) arbitrators approved by CPL or HL&P in any future arbitrations would be mutually acceptable to HL&P and CPL; and (iii) HL&P and CPL would resolve any future disputes between them concerning the South Texas Project without resorting to the arbitration provision of the Participation Agreement. Austin and San Antonio have asserted in the pending Austin II Litigation that such understandings have rendered the arbitration provisions of the Participation Agreement void and that neither Austin nor San Antonio should be required to participate in or be bound by such proceedings.

Although HL&P and the Company do not believe there is merit to either Austin's or San Antonio's claims and have opposed San Antonio's intervention in the Austin II Litigation, there can be no assurance as to the ultimate outcome of these matters.

(d) NUCLEAR INSURANCE. HL&P and the other owners of the South Texas Project maintain nuclear property and nuclear liability insurance coverage as required by law and periodically review available limits and coverage for additional protection. The owners of the South Texas Project currently maintain the maximum amount of property damage insurance currently available through the insurance industry, consisting of $500 million in primary property damage insurance and excess property insurance in the amount of $2.25 billion. Under the excess property insurance which became effective on March 1, 1995 and under portions of the excess property insurance coverage in effect prior to March 1, 1995, HL&P and the other owners of the South Texas Project are subject to assessments, the maximum aggregate assessment under current policies being $26.9 million during any one policy year. The application of the proceeds of such property insurance is subject to the priorities established by the NRC regulations relating to the safety of licensed reactors and decontamination operations.

Pursuant to the Price Anderson Act (Act), the maximum liability to the public for owners of nuclear power plants, such as the South Texas Project, was decreased from $9.0 billion to $8.92 billion effective in November 1994. Owners are required under the Act to insure their liability for nuclear incidents and protective evacuations by maintaining the maximum amount of financial protection available from private sources and by maintaining secondary financial protection through an industry retrospective rating plan. The assessment of deferred premiums provided by the plan for each nuclear incident is up to $75.5 million per reactor subject to indexing for inflation, a possible 5 percent surcharge (but no more than $10 million per reactor per incident in any one year) and a 3 percent state premium tax. HL&P

and the other owners of the South Texas Project currently maintain the required nuclear liability insurance and participate in the industry retrospective rating plan.

There can be no assurance that all potential losses or liabilities will be insurable, or that the amount of insurance will be sufficient to cover them. Any substantial losses not covered by insurance would have a material effect on HL&P's and the Company's financial condition.

(e) NUCLEAR DECOMMISSIONING. HL&P and the other co-owners of the South Texas Project are required by the NRC to meet minimum decommissioning funding requirements to pay the costs of decommissioning the South Texas Project. Pursuant to the terms of the order of the Utility Commission in Docket No. 9850, HL&P is currently funding decommissioning costs for the South Texas Project with an independent trustee at an annual amount of $6 million, which is recorded in depreciation and amortization expense. HL&P's funding level is estimated to provide approximately $146 million, in 1989 dollars, an amount which exceeds the current NRC minimum.

The Company adopted SFAS No. 115, "Accounting for Certain Investments in Debt and Equity Securities," effective January 1, 1994. At December 31, 1994, the securities held in the Company's nuclear decommissioning trust totaling $25.1 million (reflected on the Company's Consolidated and HL&P's Balance Sheets in deferred debits and deferred credits) are classified as available for sale. Such securities are reported on the balance sheets at fair value, which at December 31, 1994 approximates cost, and any unrealized gains or losses will be reported as a separate component of common stock equity. Earnings, net of taxes and administrative costs, are reinvested in the funds.

In May 1994, an outside consultant estimated HL&P's portion of decommissioning costs to be approximately $318 million, in 1994 dollars. The consultant's calculation of decommissioning costs for financial planning purposes used the DECON methodology (prompt removal/dismantling), one of the three alternatives acceptable to the NRC, and assumed deactivation of Unit Nos. 1 and 2 upon the expiration of their 40 year operating licenses. Under the terms of the Proposed Settlement, HL&P would increase funding of decommissioning costs to an annual amount of approximately $14.8 million consistent with such study. While the current and projected funding levels presently exceed minimum NRC requirements, no assurance can be given that the amounts held in trust will be adequate to cover the actual decommissioning costs of the South Texas Project or the assumptions used in estimating decommissioning costs will ultimately prove to be correct.

(3) RATE REVIEW, FUEL RECONCILIATION AND OTHER PROCEEDINGS

In February 1994, the Utility Commission initiated a proceeding (Docket No. 12065) to determine whether HL&P's existing rates are just and reasonable. Subsequently, the scope of the docket was expanded to include reconciliation of HL&P's fuel costs from April 1, 1990 to July 31, 1994. The Utility Commission also initiated a separate proceeding (Docket No. 13126) to review issues regarding the prudence of operation of the South Texas Project from the date of commercial operation through the present. That review would encompass the outage at the South Texas Project during 1993 through 1994.

Hearings began in Docket No. 12065 in January 1995, and the Utility Commission has retained a consultant to review the South Texas Project for the purpose of providing testimony in Docket No. 13126 regarding the prudence of HL&P's management of operation of the South Texas Project. In February 1995, all major parties to these proceedings signed the Proposed Settlement resolving the issues with respect to HL&P, including the prudence issues related to operation of the South Texas Project. Approval of the Proposed Settlement by the Utility Commission will be required. To that end, the parties have established procedural dates for a hearing on issues raised by the parties who are opposed to the Proposed Settlement. A decision by the Utility Commission on the Proposed Settlement is not anticipated before early summer.

Under the Proposed Settlement, HL&P's base rates would be reduced by approximately $62 million per year, effective retroactively to January 1, 1995, and rates would be frozen for three years, subject to certain conditions. Under the Proposed Settlement, HL&P would amortize its remaining investment of $218 million in the cancelled Malakoff plant over a period not to exceed seven years. HL&P also would increase its decommissioning expense for the South Texas Project by $9 million per year.

Under the Proposed Settlement, approximately $70 million of fuel expenditures and related interest incurred by HL&P during the fuel reconciliation period would not be recoverable from ratepayers. This $70 million was recorded as a one-time, pre-tax charge to reconcilable fuel revenues to reflect the anticipation of approval of the Proposed Settlement. HL&P also would establish a new fuel factor approximately 17 percent below that currently in effect and would

refund to customers the balance in its fuel over-recovery account, estimated to be approximately $180 million after giving effect to the amounts not recoverable from ratepayers.

HL&P recovers fuel costs incurred in electric generation through a fixed fuel factor that is set by the Utility Commission. The difference between fuel revenues billed pursuant to such factor and fuel expense incurred is recorded as an addition to or a reduction of revenue, with a corresponding entry to under- or over-recovered fuel, as appropriate. Amounts collected pursuant to the fixed fuel factor must be reconciled periodically against actual, reasonable costs as determined by the Utility Commission. Currently, HL&P has an over-recovery fuel account balance that will be refunded pursuant to the Proposed Settlement.

In the event that the Proposed Settlement is not approved by the Utility Commission, including issues related to the South Texas Project, Docket No. 12065 will be remanded to an Administrative Law Judge (ALJ) to resume detailed hearings in this docket. Prior to reaching agreement on the terms of the Proposed Settlement, HL&P argued that its existing rates were just and reasonable and should not be reduced. Other parties argued that rate decreases in annual amounts ranging from $26 million to $173 million were required and that additional decreases might be justified following an examination of the prudence of the management of the South Texas Project and the costs incurred in connection with the outages at the South Texas Project. Testimony filed by the Utility Commission staff included a recommendation to remove from rate base $515 million of HL&P's investment in the South Texas Project to reflect the staff's view that such investment was not fully "used and useful" in providing service, a position HL&P vigorously disputes.

In the event the Proposed Settlement is not approved by the Utility Commission, the fuel reconciliation issues in Docket Nos. 12065 and 13126 would be remanded to an ALJ for additional proceedings. A major issue in Docket No. 13126 will be whether the incremental fuel costs incurred as a result of outages at the South Texas Project represent reasonable costs. HL&P filed testimony in Docket No. 13126, which testimony concluded that the outages at the South Texas Project did not result from imprudent management. HL&P also filed testimony analyzing the extent to which regulatory issues extended the outages. In that testimony an outside consultant retained by HL&P concluded that the duration of the outages was controlled by both the resolution of NRC regulatory issues as well as necessary equipment repairs unrelated to NRC regulatory issues and that the incremental effect of NRC regulatory issues on the duration of the outages was only 39 days per unit. Estimates as to the cost of replacement power may vary significantly based on a number of factors, including the capacity factor at which the South Texas Project might be assumed to have operated had it not been out of service due to the outages. However, HL&P believes that applying a reasonable range of assumptions would result in replacement fuel costs of less than $10 million for the 39 day periods identified by HL&P's consultant and less than $100 million for the entire length of the outages. Any fuel costs determined to have been unreasonably incurred would not be recoverable from customers and would be charged against the Company's earnings.

Although the Company and HL&P believe that the Proposed Settlement is in the best interest of HL&P, its ratepayers, and the Company and its shareholders, no assurance can be given that (i) the Utility Commission ultimately will approve the terms of the Proposed Settlement or

(ii) in the event the Proposed Settlement is not approved and proceedings against HL&P resumed, that the outcome of such proceedings would be favorable to HL&P.

(4) APPEALS OF PRIOR UTILITY COMMISSION RATE ORDERS

Pursuant to a series of applications filed by HL&P in recent years, the Utility Commission has granted HL&P rate increases to reflect in electric rates HL&P's substantial investment in new plant construction,

including the South Texas Project. Although Utility Commission action on those applications has been completed, judicial review of a number of the Utility Commission orders is pending. In Texas, Utility Commission orders may be appealed to a District Court in Travis County, and from that Court's decision an appeal may be taken to the Court of Appeals for the 3rd District at Austin (Austin Court of Appeals). Discretionary review by the Supreme Court of Texas may be sought from decisions of the Austin Court of Appeals. The pending appeals from the Utility Commission orders are in various stages. In the event the courts ultimately reverse actions of the Utility Commission in any of these proceedings, such matters would be remanded to the Utility Commission for action in light of the courts' orders. Because of the number of variables which can affect the ultimate resolution of such matters on remand, the Company and HL&P generally are not in a position at this time to predict the outcome of the matters on appeal or the ultimate effect that adverse action by the courts could have on the Company and HL&P. On remand, the Utility Commission's action could range from granting rate relief substantially equal to the rates previously approved to a reduction in the revenues to which HL&P was entitled during the time the applicable rates were in effect, which could require a refund to customers of amounts collected pursuant to such rates. Judicial review has been concluded or currently is pending on the final orders of the Utility Commission described below.

(a) 1991 RATE CASE. In HL&P's 1991 rate case (Docket No. 9850), the Utility Commission approved a non-unanimous settlement agreement providing for a $313 million increase in HL&P's base rates, termination of deferrals granted with respect to Unit No. 2 of the South Texas Project and of the qualified phase-in plan deferrals granted with respect to Unit No. 1 of the South Texas Project, and recovery of deferred plant costs. The settlement authorized a 12.55 percent return on common equity for HL&P. Rates contemplated by the settlement agreement were implemented in May 1991 and remain in effect (subject to the outcome of the current rate proceeding described in Note 3).

The Utility Commission's order in Docket No. 9850 was affirmed on review by a District Court, and the Austin Court of Appeals affirmed that decision on procedural grounds due to the failure of the appellant to file the record with the court in a timely manner. On review, the Texas Supreme Court has remanded the case to the Austin Court of Appeals for consideration of the appellant's challenges to the Utility Commission's order, which include issues regarding deferred accounting, the treatment of federal income tax expense and certain other matters. As to federal tax issues, a recent decision of the Austin Court of Appeals, in an appeal involving GTE-SW (and to which HL&P was not a party), held that when a utility pays federal income taxes as part of a consolidated group, the utility's ratepayers are entitled to a fair share of the tax savings actually realized, which can include savings resulting from unregulated activities. The

Texas Supreme Court has agreed to hear an appeal of that decision, but on points not involving the federal income tax issues, though tax issues could be decided in such opinion.

Because the Utility Commission's order in Docket No. 9850 found that HL&P would have been entitled to rate relief greater than the $313 million agreed to in the settlement, HL&P believes that any disallowance that might be required if the court's ruling in the GTE decision were applied in Docket No. 9850 would be offset by that greater amount. However, that amount may not be sufficient if the Austin Court of Appeals also concludes that the Utility Commission's inclusion of deferred accounting costs in the settlement was improper. For a discussion of the Texas Supreme Court's decision on deferred accounting treatment, see Note 4(c). Although HL&P believes that it could demonstrate entitlement to rate relief equal to that agreed to in the stipulation in Docket No. 9850, HL&P cannot rule out the possibility that a remand and reopening of that settlement would be required if decisions unfavorable to HL&P are rendered on both the deferred accounting treatment and the calculation of tax expense for rate making purposes.

The parties to the Proposed Settlement have agreed to withdraw their appeals of the Utility Commission's orders in such docket, subject to HL&P's dismissing its appeal in Docket No. 6668.

(b) 1988 RATE CASE. In HL&P's 1988 rate case (Docket No. 8425), the Utility Commission granted HL&P a $227 million increase in base revenues, allowed a 12.92 percent return on common equity, authorized a qualified phase-in plan for Unit No. 1 of the South Texas Project (including approximately 72 percent of HL&P's investment in Unit No. 1 of the South

Texas Project in rate base) and authorized HL&P to use deferred accounting for Unit No. 2 of the South Texas Project. Rates substantially corresponding to the increase granted were implemented by HL&P in June 1989 and remained in effect until May 1991.

In August 1994, the Austin Court of Appeals affirmed the Utility Commission's order in Docket No. 8425 on all matters other than the Utility Commission's treatment of tax savings associated with deductions taken for expenses disallowed in cost of service. The court held that the Utility Commission had failed to require that such tax savings be passed on to ratepayers, and ordered that the case be remanded to the Utility Commission with instructions to adjust HL&P's cost of service accordingly. Discretionary review is being sought from the Texas Supreme Court by all parties to the proceeding.

The parties to the Proposed Settlement have agreed to dismiss their respective appeals of Docket No. 8425, subject to HL&P's dismissing its appeal in Docket No. 6668. A separate party to this appeal, however, has not agreed to dismiss its appeal.

(c) DEFERRED ACCOUNTING. Deferred accounting treatment for certain costs associated with Unit No. 1 of the South Texas Project was authorized by the Utility Commission in Docket No. 8230 and was extended in Docket No. 9010. Similar deferred accounting treatment with respect to Unit No. 2 of the South Texas Project was authorized in Docket No. 8425. For a discussion of the deferred accounting treatment granted, see Note 1(f).

In June 1994, the Texas Supreme Court decided the appeal of Docket Nos. 8230 and 9010, as well as all other pending deferred accounting cases involving other utilities, upholding deferred accounting treatment for both carrying costs and operation and maintenance expenses as within the Utility Commission's statutory authority and reversed the Austin Court of Appeals decision to the extent that the Austin Court of Appeals had rejected deferred accounting treatment for carrying charges. Because the lower appellate court had upheld deferred accounting only as to operation and maintenance expenses, the Texas Supreme Court remanded Docket Nos. 8230 and 9010 to the Austin Court of Appeals to consider the points of error challenging the granting of deferred accounting for carrying costs which it had not reached in its earlier consideration of the case. The Texas Supreme Court opinion did state, however, that when deferred costs are considered for addition to the utility's rate base in an ensuing rate case, the Utility Commission must then determine to what extent inclusion of the deferred costs is necessary to preserve the utility's financial integrity. Under the terms of the Proposed Settlement, South Texas Project deferrals will continue to be amortized under the schedule previously established.

The Office of the Public Utility Counsel (OPUC) has agreed, pursuant to the Proposed Settlement, to withdraw and dismiss its appeal if the Proposed Settlement becomes effective and on the condition that HL&P dismisses its appeal in Docket No. 6668. However, the appeal of the State of Texas remains pending.

(d) PRUDENCE REVIEW OF THE CONSTRUCTION OF THE SOUTH TEXAS PROJECT. In June 1990, the Utility Commission ruled in a separate docket (Docket No. 6668) that had been created to review the prudence of HL&P's planning and construction of the South Texas Project that $375.5 million out of HL&P's $2.8 billion investment in the two units of the South Texas Project had been imprudently incurred. That ruling was incorporated into HL&P's 1988 and 1991 rate cases and resulted in HL&P's recording an after-tax charge of $15 million in 1990. Several parties appealed the Utility Commission's decision, but a District Court dismissed these appeals on procedural grounds. The Austin Court of Appeals reversed and directed consideration of the appeals, and the Texas Supreme Court denied discretionary review in 1994. At this time, no action has been taken by the appellants to proceed with the appeals. Unless the order in Docket No. 6668 is modified or reversed on appeal, the amount found imprudent by the Utility Commission will be sustained.

Under the Proposed Settlement, OPUC, HL&P and the City of Houston each has agreed to dismiss its respective appeals of Docket No. 6668. A separate party to this appeal, however, has not agreed to dismiss its appeal. If this party does not elect to dismiss its appeal, HL&P may elect to maintain its appeal, whereupon OPUC and City of Houston shall also be entitled to maintain their appeals.

(b) UNITED STATES NUCLEAR REGULATORY COMMISSION (NRC) INSPECTIONS AND OPERATIONS. HL&P removed both generating units at the South Texas Project from service in February 1993 when a problem was encountered with certain of the units' auxiliary feedwater pumps. The units were out of service from February 1993 to February 1994, when Unit No. 1 was returned to service.

Unit No. 2 was returned to service in May 1994. In June 1993, the NRC placed the South Texas Project on its "watch list" of plants with weaknesses that warrant increased attention after a review of the South Texas Project operations. In February 1995, the NRC removed the South Texas Project from its "watch list".

Certain current and former employees or contractors of HL&P have asserted claims that their employment was terminated or disrupted in retaliation for their having made safety-related complaints to the NRC. Civil proceedings by the complaining personnel and administrative proceedings by the Department of Labor remain pending against HL&P, and the NRC has jurisdiction to take enforcement action against HL&P and/or individual employees with respect to these matters. On May 8, 1995, the NRC announced that it was withdrawing a previously proposed Notice of Violation and $100,000 civil penalty, as well as possible individual enforcement action against two HL&P managers in connection with one such case, involving a contractor employee whose site access was terminated. Allegations of retaliation by that individual remain pending before an Administrative Law Judge (ALJ) of the Department of Labor. In another such case, involving two former HL&P employees who were terminated during a reduction in force, another Department of Labor ALJ in April 1995 issued his recommended decision in favor of the former employees, ordering reinstatement of one with back-pay and back-pay without reinstatement to another. The ALJ ruled out ordering HL&P to pay exemplary damages to the individuals, but indicated his intention to hold a further hearing to consider whether additional compensatory damages should be awarded. HL&P considers the ALJ's conclusions to be erroneous and is asking the Secretary of Labor not to adopt the ALJ's recommendation. If the recommendation is adopted by the Secretary of Labor, HL&P could appeal that decision to the United States Court of Appeals. Civil actions by these employees remain pending. For additional information, see Note 2(b) of the notes to the financial statements included in the Combined Form 8-K.

While no prediction can be made at this time as to the ultimate outcome of these matters, the Company and HL&P do not believe that they will have a material adverse effect on the Company's or HL&P's financial condition or results of operations.

(3) RATE REVIEW, FUEL RECONCILIATION AND OTHER PROCEEDINGS

In February 1994, the Public Utility Commission of Texas (Utility Commission) initiated a proceeding (Docket No. 12065) to determine whether HL&P's existing rates are just and reasonable. Subsequently, the scope of the docket was expanded to include reconciliation of HL&P's fuel costs from April 1, 1990 to July 31, 1994. The Utility Commission also initiated a

separate proceeding (Docket No. 13126) to review issues regarding the prudence of operation of the South Texas Project from the date of commercial operation through the present. That review would encompass the outage at the South Texas Project during 1993 and 1994.

Hearings began in Docket No. 12065 in January 1995. In February 1995, all major parties to these proceedings signed an agreement resolving the issues with respect to HL&P, including the prudence issues related to operation of the South Texas Project (Proposed Settlement). Approval of the Proposed Settlement by the Utility Commission will be required. Hearings on the Proposed Settlement are currently scheduled to begin in early June 1995. A decision by the Utility Commission on the Proposed Settlement is not anticipated before late summer.

Under the Proposed Settlement, HL&P's base rates would be reduced by approximately $62 million per year, effective retroactively to January 1, 1995, and HL&P would be precluded from seeking rate increases for three years, subject to certain conditions. Under the Proposed Settlement, HL&P would amortize its remaining investment of $218 million in the cancelled Malakoff Electric Generating Station (Malakoff) plant over a period not to exceed seven years. HL&P also would increase its decommissioning expense for the South Texas Project by $9 million per

year.

The Proposed Settlement also provides HL&P the option to write down up to $50 million per year of its investment in the South Texas Project during the five-year period commencing January 1, 1995. The parties to the Proposed Settlement agreed that any write down would be treated as a reasonable and necessary expense during routine reviews of HL&P's earnings and any rate review proceeding initiated against HL&P.

Until the approval of the Proposed Settlement by the Utility Commission, HL&P's existing rates will continue in effect; however, HL&P's financial statements for the first quarter of 1995 reflect the estimated effects of the Proposed Settlement. In the first quarter of 1995, HL&P's pre-tax earnings were reduced by approximately $17 million in the aggregate as a result of reflecting the estimated effects of the Proposed Settlement on revenues and expenses for the quarter. Deferred revenues are included on the Company's Consolidated and HL&P's Balance Sheets in other deferred credits subject to refund when the Proposed Settlement is approved.

Under the Proposed Settlement, approximately $70 million of fuel expenditures and related interest incurred by HL&P during the fuel reconciliation period would not be recoverable from ratepayers. This $70 million was recorded in the fourth quarter of 1994 as a one-time, pre-tax charge to reconcilable fuel revenues to reflect the anticipation of approval of the Proposed Settlement. Under the Proposed Settlement, HL&P would also establish a new fuel factor approximately 17 percent below that currently in effect and would refund to customers the balance in its fuel over-recovery account, estimated to be approximately $180 million after giving effect to the amounts not recoverable from ratepayers. As contemplated by the Proposed Settlement and approved by an ALJ, HL&P implemented a new fuel factor 17 percent lower than its previous factor and refunded to customers approximately $110 million of the approximately $180 million in fuel cost overrecoveries in April 1995. The remaining $70 million will be refunded if the Proposed Settlement is approved by the Utility Commission.

In the event the Proposed Settlement is not approved by the Utility Commission, Docket No. 12065 would be remanded to an ALJ to resume detailed hearings in this docket and with respect to issues related to the South Texas Project. Prior to reaching agreement on the terms of the Proposed Settlement, HL&P argued that its existing rates were just and reasonable and should not be reduced. Other parties argued that rate decreases in annual amounts ranging from $26 million to $173 million were required and that additional decreases might be justified following an examination of the prudence of the management of the South Texas Project and the costs incurred in connection with the outages at the South Texas Project. Testimony filed by the Utility Commission staff included a recommendation to remove from rate base $515 million of HL&P's investment in the South Texas Project to reflect the staff's view that such investment was not fully "used and useful" in providing service, a position HL&P vigorously disputes.

In the event the Proposed Settlement is not approved by the Utility Commission, the fuel reconciliation issues in Docket Nos. 12065 and 13126 would be remanded to an ALJ for additional proceedings. A major issue in Docket No. 13126 would be whether the incremental fuel costs incurred as a result of outages at the South Texas Project represent reasonable costs. The Utility Commission has retained a consultant to review the South Texas Project for the purpose of providing testimony in Docket No. 13126 regarding the prudence of HL&P's management of operation of the South Texas Project. HL&P filed testimony in Docket No. 13126, which testimony concluded that the outages at the South Texas Project did not result from imprudent management. HL&P also filed testimony analyzing the extent to which regulatory issues extended the outages. In that testimony an outside consultant retained by HL&P concluded that the duration of the outages was controlled by both the resolution of NRC regulatory issues as well as necessary equipment repairs unrelated to NRC regulatory issues and that the incremental effect of NRC regulatory issues on the duration of the outages was only 39 days per unit. Estimates as to the cost of replacement power may vary significantly based on a number of factors, including the capacity factor at which the South Texas Project might be assumed to have operated had it not been out of service due to the outages. However, HL&P believes that applying a reasonable range of assumptions would result in replacement fuel costs of less than $10 million for the 39 day periods identified by HL&P's consultant and less than $100 million for the entire length of the outages. Any fuel costs determined to have been unreasonably incurred would not be recoverable from customers and would be charged against the Company's earnings.

Although the Company and HL&P believe that the Proposed Settlement is in the best interest of HL&P, its ratepayers, the Company and its shareholders, no assurance can be given that (i) the Utility Commission ultimately will approve the terms of the Proposed Settlement or (ii) in the event the Proposed Settlement is not approved and proceedings against HL&P are resumed, that the outcome of such proceedings would be favorable to HL&P.

(9) CHANGE IN ACCOUNTING FOR THE COMPANY AND HL&P

The Company and HL&P adopted Statement of Financial Accounting Standards (SFAS) No. 112, "Employer's Accounting for Postemployment Benefits", effective January 1, 1994. SFAS No. 112 requires companies to recognize the liability for benefits provided to former or inactive employees, their beneficiaries and covered dependents after employment but before retirement. Those benefits include, but are not limited to, salary continuation, supplemental unemployment benefits, severance benefits, disability-related benefits (including worker's compensation), job training and counseling, and continuation of benefits such as health care and life insurance. SFAS No. 112 requires the transition obligation (liability from prior years) to be expensed upon adoption. As a result, the Company and HL&P recorded in the first quarter of 1994 a one-time, after-tax charge to income of $8.2 million.

ITEM 3. LEGAL PROCEEDINGS.

For a description of certain legal and regulatory proceedings affecting the Company and its subsidiaries (including (i) HL&P's rate cases, (ii) certain environmental matters and (iii) litigation related to the South Texas Project), see "Business - Regulatory Matters - Environmental Quality" in Item 1 of this Report, "LIQUIDITY AND CAPITAL RESOURCES - HL&P - Environmental Expenditures" in Item 7 of this Report and Notes 1(f) and 2 through 5 to the Financial Statements in Item 8 of this Report, which sections and notes are incorporated herein by reference.

HL&P is a defendant in litigation arising out of the environmental remediation of a site in Corpus Christi, Texas. The site in question was operated as a metals reclaiming operation for a number of years, and, though HL&P neither operated nor had any ownership interest in the site, some transformers and other equipment that HL&P sold as surplus allegedly were delivered to that site, where the site operators subsequently disposed of the materials in ways that caused environmental damage. In one case, DUMES, ET AL. V. HL&P, ET AL., pending in the U.S. District Court for the Southern District of Texas, Corpus Christi Division, a group of approximately 70 landowners near the site are seeking damages primarily for lead contamination to their property. They have pled damages of approximately $1 million each and also seek punitive damages totaling $51 million. The Plaintiffs seek to impose responsibility on HL&P and the other utility that undertook to clean up the property, neither of which contributed more than an insignificant amount of lead to the site, on the theory that lead was deposited on their properties during the site remediation itself. In addition, Gulf States Utilities Company (Gulf States) filed suit (GULF STATES UTILITIES CO. V. HOUSTON LIGHTING & POWER CO., ET AL.) in the United States District Court for the Southern District of Texas, Houston Division, against HL&P and two other utilities concerning a site in Houston, Texas, which allegedly has been contaminated by polychlorinated biphenyls and which Gulf States has undertaken to remediate pursuant to an EPA order. HL&P does not believe, based on its records, that it contributed material to that site and in October 1994, Gulf States dismissed its claims against HL&P. HL&P remains in the case on cross-claims asserted by two co-defendants. The ultimate outcome of these pending cases cannot be predicted at this time. Based on information currently available, the Company and HL&P believe that none of these cases will result in a material adverse effect on the Company's or HL&P's financial condition or results of operations.

HL&P and the other owners of the South Texas Project filed suit in 1990 against Westinghouse Electric Corporation (Westinghouse) in the 23rd District Court for Matagorda County, Texas (Cause No. 90-S-0684-C), alleging breach of warranty and misrepresentation in connection with the steam generators supplied by Westinghouse for the South Texas Project. In recent years, other utilities have encountered stress corrosion cracking in steam generator tubes in Westinghouse units similar to those supplied for the South Texas Project. Failure of such tubes can result in a reduction of plant efficiency, and, in some cases, utilities have replaced their steam generators. During an inspection concluded in the fall of 1993, evidence was found of stress corrosion cracking consistent with that encountered with Westinghouse steam generators at other facilities, and a small number of tubes were found to require plugging. To date, stress corrosion cracking has not had a significant impact on operation of either unit; however, the owners of the South Texas Project have approved remedial operating

plans and have undertaken expenditures to minimize and delay further corrosion. The litigation, which is in discovery, seeks appropriate damages and other relief from Westinghouse and is currently scheduled for trial in July 1995. No prediction can be made as to the ultimate outcome of this litigation.

In April 1994, two former employees of HL&P filed a class action and shareholder derivative suit on behalf of all shareholders of the Company. This lawsuit (PACE AND FUENTEZ V. HOUSTON INDUSTRIES INCORPORATED) alleges various acts of mismanagement against certain officers and directors of the Company and HL&P and, seeks unspecified actual and punitive damages for the benefit of shareholders of the Company. The Company and HL&P believe that the suit is without merit. The lawsuit is pending in the 122nd Judicial District of Galveston County, Texas.

In June 1994, a former employee of HL&P filed a lawsuit (PACE, INDIVIDUALLY AND AS A REPRESENTATIVE OF ALL OTHERS SIMILARLY SITUATED V. HOUSTON LIGHTING & POWER COMPANY) in the 56th Judicial District Court of Galveston County, Texas alleging that HL&P has been overcharging ratepayers and owes a refund of more than $500 million. The claim was based on the argument that the Utility Commission failed to allocate to ratepayers alleged tax benefits accruing to the Company and HL&P because HL&P's federal income taxes are paid as part of a consolidated group. The court has granted HL&P's motion for summary

judgment, which has now become final.

In July 1990, the Company paid approximately $104.5 million to the Internal Revenue Service (IRS) in connection with an IRS audit of the Company's 1983 and 1984 federal income tax returns. In November 1991, the Company filed a refund suit in the U.S. Court of Federal Claims seeking the return of $52.1 million of tax, $36.3 million of accrued interest, plus interest on both of those amounts accruing after July 1990. The major contested issue in the refund case involved the IRS's allegation that certain amounts related to the over-recovery of fuel costs should have been included as taxable income in 1983 and 1984 even though HL&P had an obligation to refund the over-recoveries to its ratepayers. In October 1994, the Court granted the Company's Motion for Partial Summary Judgment on the fuel cost over-recovery issue. On February 21, 1995, the Court entered partial judgment in favor of the Company for this issue. The U.S. Government (Government) must file its notice of appeal on or before April 24, 1995. If the Government does not appeal or if the Government appeals but does not prevail, the Company would be entitled to a refund of overpaid tax, interest paid on the overpaid tax in July 1990 and interest on both of those amounts from July 1990. Although, the Company would not be entitled to a refund until all appeals are decided in its favor, the amount owed to the Company will continue to accrue interest. If the Government appeals and prevails, the Company's ultimate financial exposure should be immaterial because of offsetting tax deductions to which the Company is entitled in the year the over-recovery was refunded to ratepayers (and which the IRS has conceded).

EXHIBIT 99(e)

ITEM 1. LEGAL PROCEEDINGS.

For a description of legal proceedings affecting the Company and its subsidiaries, including HL&P, reference is made to the information set forth in Item 3 of the Company's and HL&P's Annual Report on Form 10-K for the year ended December 31, 1994 (1994 Combined Form 10-K) and Notes 2, 3 and 4 to the Company's Consolidated and HL&P's Financial Statements in the Combined Form 8-K, which information, as qualified and updated by the description of developments in regulatory and litigation matters contained in Notes 2, 3 and 4 of the Notes to the Company's Consolidated and HL&P's Financial Statements included in Part I of this Report, is incorporated herein by reference.

In April 1995, the government filed a notice of appeal with respect to the judgment entered in favor of the Company in its refund suit pending in the U.S. Court of Federal Claims. For additional information regarding the Company's tax case, see Item 3 to the 1994 Combined Form 10-K.

COMPETITION

HL&P and other members of the electric utility industry, like other regulated industries, are being subjected to technological, regulatory and economic pressures that are increasing competition and offer the possibility for fundamental changes in the industry and its regulation. The electric utility industry historically has been composed of vertically integrated companies which largely have been the exclusive providers of electric service within a governmentally- defined geographic area. Prices for that service have been set by governmental authority under

principles that were designed to provide the utility with an opportunity to recover its costs of providing electric service plus a reasonable return on its invested capital.

By legislation adopted in 1978, Congress contributed to the development of new sources of electric generation by freeing cogenerators (i.e., facilities which produce electrical energy along with thermal energy used for industrial processes, usually the generation of steam) from most regulatory constraints applicable to traditional utilities, such as state and federal pricing regulation and organizational restrictions arising under the 1935 Act. This legislation contributed to the development of approximately 40 cogeneration facilities in the highly industrialized Houston area, with a power generation capability of over 5,000 MW. As a consequence, HL&P has lost some industrial customers to self-generation (representing approximately 2,500 MW), and additional projects continue to be considered by customers.

In 1992 Congress authorized, in the Energy Policy Act, another category of wholesale generators, Exempt Wholesale Generators (EWGs). Like cogenerators, these entities exist to sell electric energy at wholesale, but unlike cogenerators, EWGs may be formed for the generation of electricity without regard to the simultaneous production of thermal energy. Congress chose to free EWGs from the structural constraints applicable to traditional utilities under the 1935 Act, but Congress also authorized traditional utilities to form such entities themselves without being burdened by those restrictions. At the same time, Congress placed significant limitations on the ability of traditional utilities to purchase power in their own service territories from an affiliated EWG.

There are increasing pressures today by both cogenerators and exempt wholesale generators for access to the electric transmission and distribution systems of the regulated utilities in order to have greater flexibility in moving power to other purchasers, including access for the purpose of making retail sales to either affiliates of the unregulated generator or to other customers of the regulated utility. In February 1995, a new entity sought permission from the Public Utility Commission of Texas (Utility Commission) to construct a transmission line within HL&P's service territory for the purpose of transmitting power from a cogeneration facility owned by an industrial concern to an affiliate of that concern. This proceeding has been docketed by the Utility Commission, but currently is in its early stages.

Neither federal nor Texas law currently permits retail sales by unregulated entities. However, changes to the Federal Power Act made in the Energy Policy Act of 1992 increase the power of the Federal Energy Regulatory Commission (FERC) to order utilities to transmit power generated by both regulated and unregulated entities to other wholesale customers, and efforts are underway in some states that may lead to broader authorization of transmission access for such entities and even to retail sales by such entities. HL&P anticipates that some of those arguments will be advanced in the current session of the Texas legislature during the consideration of the re-enactment to the Public Utility Regulatory Act (PURA), which governs electric regulation in Texas.

Traditional utilities such as HL&P also face increased competition from alternate energy sources, primarily natural gas. Gas suppliers increasingly are seeking to supplant traditional electric loads with gas-powered equipment, such as gas-powered chillers in air conditioning installations.

HL&P continues to maintain an aggressive approach in attempting to preserve its existing customer base. HL&P has instituted various programs to reduce its costs and has adopted aggressive marketing programs to identify and respond to customer needs. One example is HL&P's development of the San Jacinto Steam Electric Station, a rate-based cogeneration facility that will begin service in 1995. In addition, in February 1995, the Utility Commission approved a new tariff proposed by HL&P that will allow special pricing for industrial customers who can demonstrate the ability to obtain electric service on terms more favorable than HL&P's traditional tariff offerings. While such pricing may retain such customers and minimize the prospect that HL&P would be left with

stranded investment whose costs might have to be borne by customers who have no other alternatives, HL&P's revenues and earnings will be reduced from such pricing tariffs.

In addition, HL&P and nine other Texas investor-owned utilities are supporting a legislative proposal for amendment to the PURA. That proposal calls for (i) a streamlined resource planning process, (ii) competitive bidding for new generation capacity requirements, (iii) regulatory incentives that reward efficiency and innovation and (iv) granting utilities pricing flexibility to meet the changing needs of their customers. These changes, if adopted in the form proposed by the utilities, would enhance the flexibility of regulated entities to address competition, while also providing utility customers with the benefits of more diverse energy supplies.

Under rules adopted by the Utility Commission and under interconnection guidelines adopted by the Electric Reliability Council of Texas, Inc., through which a number of utilities and unregulated suppliers are connected, HL&P and other Texas utilities have provided for movement of power for both regulated and unregulated power suppliers at compensatory rates. Unregulated power suppliers continue to seek additional access and more favorable pricing provisions.

At this time it is impossible to predict what changes to the electric utility industry will emerge as a result of any legislative changes that may be adopted by the Texas legislature. Nor is it possible to predict what other changes to the industry will emerge from federal regulatory and legislative initiatives or from regulatory decisions of the Utility Commission, though, it seems likely that such changes ultimately will increase the competition HL&P faces in supplying electric energy to its customers.

REGULATION OF THE COMPANY

FEDERAL

The Company is a holding company as defined in the 1935 Act; however, based upon the intrastate operations of HL&P and the exemptions applicable to the affiliates of HI Energy, the Company is exempt from regulation as a "registered" holding company under the 1935 Act except with respect to the acquisition of voting securities of other domestic public utility companies and holding companies. The Company has no present intention of entering into any transaction which would cause it to become a registered holding company subject to regulation by the Securities and Exchange Commission (SEC) under the 1935 Act. In November 1994, the SEC issued a Concept Release that called for comments on a broad range of topics relevant to regulation of both registered and exempt companies under the 1935 Act. In calling for comments, the SEC acknowledged that significant changes are affecting the electric utility industry, and in responding, some utilities have argued for repeal or substantial modification of the 1935 Act and the regulation it provides. At this time, no prediction can be made as to what changes, if any, will result from this review by the SEC, but repeal or significant modification to the 1935 Act may have an effect on the electric utility industry. In addition, it is possible that changes to the 1935 Act and its interpretation would eliminate some distinctions between exempt and registered companies in their regulation under the 1935 Act, possibly in ways that would increase the regulatory burdens on exempt companies such as the Company.