

UNITED STATES  
SECURITIES AND EXCHANGE COMMISSION  
WASHINGTON, D.C. 20549

FORM 10-Q

(Mark One)

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

FOR THE QUARTERLY PERIOD ENDED MARCH 31, 2003

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 1-3187

CENTERPOINT ENERGY HOUSTON ELECTRIC, LLC

(Exact name of registrant as specified in its charter)

TEXAS

(State or other jurisdiction of  
incorporation or organization)

22-3865106  
(I.R.S. Employer  
Identification No.)

1111 LOUISIANA  
HOUSTON, TEXAS 77002  
(Address and zip code of  
principal executive offices)

(713) 207-1111  
(Registrant's telephone number,  
including area code)

-----  
CENTERPOINT ENERGY HOUSTON ELECTRIC, LLC MEETS THE CONDITIONS SET FORTH IN  
GENERAL INSTRUCTION H(1)(A) AND (B) OF FORM 10-Q AND IS THEREFORE FILING THIS  
FORM 10-Q WITH THE REDUCED DISCLOSURE FORMAT.

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

Indicate by check mark whether the registrant is an accelerated filer (as  
defined by Rule 12b-2 of the Exchange Act) Yes  No

As of May 2, 2003, all 1,000 common shares of CenterPoint Energy Houston  
Electric, LLC were held by Utility Holding, LLC, a wholly owned subsidiary of  
CenterPoint Energy, Inc.

CENTERPOINT ENERGY HOUSTON ELECTRIC, LLC  
QUARTERLY REPORT ON FORM 10-Q  
FOR THE QUARTER ENDED MARCH 31, 2003

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## PART I. FINANCIAL INFORMATION

## ITEM 1. FINANCIAL STATEMENTS.

CENTERPOINT ENERGY HOUSTON ELECTRIC, LLC AND SUBSIDIARIES  
(A WHOLLY OWNED SUBSIDIARY OF CENTERPOINT ENERGY, INC.)  
STATEMENTS OF CONSOLIDATED INCOME  
(THOUSANDS OF DOLLARS)  
(UNAUDITED)

	THREE MONTHS ENDED MARCH 31,	
	2002	2003
REVENUES .....	\$ 568,053	\$ 447,403
EXPENSES:		
Purchased power .....	59,580	--
Operation and maintenance .....	141,105	133,008
Depreciation and amortization .....	63,339	64,742
Taxes other than income taxes .....	50,456	44,052
Total .....	314,480	241,802
OPERATING INCOME .....	253,573	205,601
OTHER INCOME (EXPENSE):		
Interest expense and distribution on trust preferred securities .....	(60,097)	(92,230)
Other, net .....	5,392	8,508
Total .....	(54,705)	(83,722)
INCOME FROM CONTINUING OPERATIONS BEFORE INCOME TAXES .	198,868	121,879
Income Tax Expense .....	67,143	41,704
INCOME FROM CONTINUING OPERATIONS .....	131,725	80,175
Loss from Discontinued Operations, net of tax .....	(100,120)	--
NET INCOME .....	\$ 31,605	\$ 80,175

See Notes to the Company's Interim Financial Statements

CENTERPOINT ENERGY HOUSTON ELECTRIC, LLC AND SUBSIDIARIES  
(A WHOLLY OWNED SUBSIDIARY OF CENTERPOINT ENERGY, INC.)  
CONSOLIDATED BALANCE SHEETS  
(THOUSANDS OF DOLLARS)  
(UNAUDITED)

ASSETS	DECEMBER 31, 2002	MARCH 31, 2003
	-----	-----
CURRENT ASSETS:		
Cash and cash equivalents .....	\$ 70,866	\$ 13,267
Accounts and notes receivable, net .....	99,304	110,090
Accrued unbilled revenues .....	70,385	61,376
Materials and supplies .....	59,941	58,033
Taxes receivable .....	--	63,953
Other .....	11,839	11,120
	-----	-----
Total current assets .....	312,335	317,839
	-----	-----
PROPERTY, PLANT AND EQUIPMENT:		
Property, plant and equipment .....	5,959,843	5,980,213
Less accumulated depreciation and amortization .....	(2,122,611)	(2,155,584)
	-----	-----
Property, plant and equipment, net .....	3,837,232	3,824,629
	-----	-----
OTHER ASSETS:		
Other intangibles, net .....	39,912	39,751
Regulatory assets .....	3,970,007	4,527,749
Notes receivable-- affiliated companies .....	814,513	814,513
Other .....	66,049	71,085
	-----	-----
Total other assets .....	4,890,481	5,453,098
	-----	-----
TOTAL ASSETS .....	\$ 9,040,048	\$ 9,595,566
	=====	=====

See Notes to the Company's Interim Financial Statements

CENTERPOINT ENERGY HOUSTON ELECTRIC, LLC AND SUBSIDIARIES  
(A WHOLLY OWNED SUBSIDIARY OF CENTERPOINT ENERGY, INC.)  
CONSOLIDATED BALANCE SHEETS  
(THOUSANDS OF DOLLARS) -- (CONTINUED)  
(UNAUDITED)

LIABILITIES AND MEMBER'S EQUITY

	DECEMBER 31, 2002	MARCH 31, 2003
	-----	-----
<b>CURRENT LIABILITIES:</b>		
Current portion of long-term debt .....	\$ 18,758	\$ 26,398
Accounts payable .....	32,362	22,470
Accounts payable-- affiliated companies, net	43,662	21,243
Notes payable-- affiliated companies, net ..	214,976	171,906
Taxes accrued .....	44,208	33,606
Interest accrued .....	78,355	60,769
Regulatory liabilities .....	168,173	171,742
Other .....	57,513	46,071
	-----	-----
Total current liabilities .....	658,007	554,205
	-----	-----
<b>OTHER LIABILITIES:</b>		
Accumulated deferred income taxes, net .....	1,419,301	1,494,101
Unamortized investment tax credits .....	53,581	52,408
Benefit obligations .....	61,671	60,752
Regulatory liabilities .....	940,615	901,451
Notes payable-- affiliated companies .....	916,400	637,400
Accounts payable-- affiliated companies .....	--	395,516
Other .....	25,206	21,033
	-----	-----
Total other liabilities .....	3,416,774	3,562,661
	-----	-----
LONG-TERM DEBT .....	2,641,281	3,074,539
	-----	-----
<b>COMMITMENTS AND CONTINGENCIES (NOTES 1 AND 9)</b>		
<b>MEMBER'S EQUITY:</b>		
Common stock .....	1	1
Paid-in capital .....	2,205,039	2,205,039
Retained earnings .....	118,946	199,121
	-----	-----
Total member's equity .....	2,323,986	2,404,161
	-----	-----
<b>TOTAL LIABILITIES AND MEMBER'S EQUITY .</b>	<b>\$9,040,048</b>	<b>\$9,595,566</b>
	=====	=====

See Notes to the Company's Interim Financial Statements

CENTERPOINT ENERGY HOUSTON ELECTRIC, LLC AND SUBSIDIARIES  
(A WHOLLY OWNED SUBSIDIARY OF CENTERPOINT ENERGY, INC.)  
STATEMENTS OF CONSOLIDATED CASH FLOWS  
(THOUSANDS OF DOLLARS)  
(UNAUDITED)

	THREE MONTHS ENDED MARCH 31,	
	2002	2003
<b>CASH FLOWS FROM OPERATING ACTIVITIES:</b>		
Net Income .....	\$ 31,605	\$ 80,175
Less: Loss from discontinued operations .....	(100,120)	--
	131,725	80,175
Income from continuing operations .....		
Adjustments to reconcile income from continuing operations to net cash used in operating activities:		
Depreciation and amortization .....	63,339	64,742
Deferred income taxes .....	83,127	74,267
Investment tax credits .....	(1,172)	(1,173)
Changes in other assets and liabilities:		
Accounts and notes receivable, net .....	(269,676)	(1,777)
Accounts receivable/payable, affiliates .....	(80,168)	(22,418)
Inventory .....	4,549	1,908
Accounts payable .....	11,676	(9,892)
Fuel cost over recovery .....	138,819	--
Interest and taxes accrued .....	(58,599)	(92,141)
Net regulatory assets and liabilities .....	(188,091)	(201,816)
Other current assets .....	(2,174)	718
Other current liabilities .....	(71,853)	(11,442)
Other assets .....	87,845	12,200
Other liabilities .....	(152,667)	(4,559)
	(303,320)	(111,208)
Net cash used in operating activities .....	(303,320)	(111,208)
<b>CASH FLOWS FROM INVESTING ACTIVITIES:</b>		
Capital expenditures, net .....	(67,796)	(47,983)
	(67,796)	(47,983)
Net cash used in investing activities .....	(67,796)	(47,983)
<b>CASH FLOWS FROM FINANCING ACTIVITIES:</b>		
Increase in cash related to securitization financing .....	2,958	--
Proceeds from issuance of long-term debt .....	--	758,830
Increase in short-term borrowing, net .....	236,178	--
Increase (decrease) in notes with affiliates, net .....	(6,402)	106,930
Payments of long-term debt .....	(283)	(318,649)
Decrease in long-term notes payable with affiliates .....	--	(429,000)
Debt issuance costs .....	--	(17,296)
Payment of common stock dividend .....	(110,936)	--
Other, net .....	--	777
	121,515	101,592
Net cash provided by financing activities .....	121,515	101,592
<b>NET CASH PROVIDED BY DISCONTINUED OPERATIONS</b> .....	256,067	--
<b>NET INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS</b> .....	6,466	(57,599)
<b>CASH AND CASH EQUIVALENTS AT BEGINNING OF PERIOD</b> .....	3,428	70,866
<b>CASH AND CASH EQUIVALENTS AT END OF PERIOD</b> .....	\$ 9,894	\$ 13,267
<b>SUPPLEMENTAL DISCLOSURE OF CASH FLOW INFORMATION:</b>		
Cash Payments:		
Interest .....	\$ 24,853	\$ 43,188
Income taxes .....	--	--

See Notes to the Company's Interim Financial Statements

CENTERPOINT ENERGY HOUSTON ELECTRIC, LLC AND SUBSIDIARIES

NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS

(1) BACKGROUND AND BASIS OF PRESENTATION

Included in this Quarterly Report on Form 10-Q (Form 10-Q) of CenterPoint Energy Houston Electric, LLC (CenterPoint Houston, together with its subsidiaries, the Company), are the Company's consolidated interim financial statements and notes (Interim Financial Statements) including its wholly owned subsidiaries. The Interim Financial Statements are unaudited, omit certain financial statement disclosures and should be read with the Annual Report on Form 10-K of CenterPoint Houston (CenterPoint Houston Form 10-K) for the year ended December 31, 2002.

ORGANIZATIONAL STRUCTURE AND RESTRUCTURING

CenterPoint Houston is a regulated utility engaged in the transmission and distribution of electric energy in a 5,000 square mile area located along the Texas Gulf Coast, including the City of Houston. CenterPoint Houston is an indirect wholly owned subsidiary of CenterPoint Energy, Inc. (CenterPoint Energy), a public utility holding company.

The Company's business includes:

- Transmission. The Company's transmission business transports electricity from power plants to substations and from one substation to another in locations in the control area managed by the Electric Reliability Council of Texas, Inc. (ERCOT).
- Distribution. The Company's electric distribution business distributes electricity for retail electric providers in its certificated service area by carrying power from the substation to the retail electric customer.

The Company's business also includes the stranded costs and regulatory asset recovery associated with the Company's historical generating operations. The Company operates its business as a single segment. In addition to the electric transmission and distribution business, the consolidated financial statements include the operations of one financing subsidiary.

The Company's business does not include:

- the generation or sale of electricity;
- the procurement, supply or delivery of fuel for the generation of electricity; or
- the marketing to or billing of retail electric customers.

Effective August 31, 2002, Reliant Energy, Incorporated (Reliant Energy) consummated a restructuring transaction (Restructuring) in which it, among other things, (1) conveyed its Texas electric generation assets to Texas Genco Holdings, Inc. (Texas Genco), (2) became an indirect, wholly owned subsidiary of a new utility holding company, CenterPoint Energy, (3) was converted into a Texas limited liability company named CenterPoint Energy Houston Electric, LLC and (4) distributed the capital stock of its operating subsidiaries, including Texas Genco, to CenterPoint Energy. As part of the Restructuring, each share of Reliant Energy common stock was converted into one share of CenterPoint Energy common stock. The Company's operating subsidiaries which were distributed in connection with the Restructuring and presented as discontinued operations included \$2.1 billion of indebtedness. An additional \$1.9 billion of indebtedness was assumed by CenterPoint Energy at the time of the Restructuring, consisting of \$1.6 billion of debt and \$0.3 billion of trust preferred securities that were reflected in continuing operations in the Company's Consolidated Balance Sheet as of December 31, 2001. Additionally, at Restructuring the Company issued a \$1.6 billion note payable to CenterPoint Energy. CenterPoint Energy assumed a \$2.5 billion Senior A Credit Agreement, dated as of July 13, 2001 among Houston Industries FinanceCo LP (a subsidiary of Reliant Energy), Reliant Energy and the lender parties thereto, and a \$1.8 billion Senior B Credit Agreement, dated as of July 13, 2001 among Houston Industries FinanceCo LP, Reliant Energy and the lender

parties thereto.

In a July 2002 order, the Securities and Exchange Commission (SEC) limited the aggregate amount of our external borrowings to \$3.55 billion. Our ability to pay dividends is restricted by the SEC's requirement that common equity as a percentage of total capitalization must be at least 30% after the payment of any dividend. In addition, the order restricts our ability to pay dividends out of capital accounts to the extent current or retained earnings are insufficient for those dividends. Under these restrictions, we are permitted to pay dividends in excess of our current or retained earnings in an amount up to \$200 million.

#### BASIS OF PRESENTATION

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America (GAAP) requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

The Interim Financial Statements reflect all normal recurring adjustments that are, in the opinion of management, necessary to present fairly the financial position and results of operations for the respective periods. Amounts reported in the Company's Statements of Consolidated Income are not necessarily indicative of amounts expected for a full year period due to the effects of, among other things, (a) fluctuations in demand for energy, (b) timing of maintenance and other expenditures and (c) acquisitions and dispositions of assets and other interests. In addition, certain amounts from the prior year have been reclassified to conform to the Company's presentation of financial statements in the current year. These reclassifications do not affect net income.

Notes 4 (Regulatory Matters), 3(e) (Regulatory Assets and Liabilities), 8(a) (Pension Plans) and 10 (Commitments and Contingencies) to the consolidated financial statements in the CenterPoint Houston Form 10-K (CenterPoint Houston 10-K Notes) relate to certain contingencies. These notes, as updated herein, are incorporated herein by reference.

For information regarding certain legal and regulatory proceedings, see Note 9.

#### (2) DISCONTINUED OPERATIONS

The Interim Financial Statements have been prepared to reflect the effect of the Restructuring as described above as it relates to CenterPoint Houston and have been prepared based upon Reliant Energy's historical consolidated financial statements.

The Interim Financial Statements present the regulated and unregulated operations of Reliant Energy that were distributed to CenterPoint Energy in the restructuring as discontinued operations, in accordance with Statement of Financial Accounting Standards (SFAS) No. 144, "Accounting for the Impairment or Disposal of Long-Lived Assets" (SFAS No. 144). Included in discontinued operations of CenterPoint Energy Houston are Reliant Energy's unregulated operations previously reported in the Wholesale Energy, European Energy and Retail Energy business segments. Also included in discontinued operations are the regulated businesses conveyed to CenterPoint Energy which have previously been reported in the Natural Gas Distribution and Pipelines and Gathering business segments as well as the Electric Generation business segment. Accordingly, the Interim Financial Statements of CenterPoint Houston reflect these operations as discontinued operations for the three months ended March 31, 2002.

Total revenues included in discontinued operations were \$2.9 billion for the three months ended March 31, 2002. Income from discontinued operations for the three months ended March 31, 2002 is reported net of income tax expense of \$47 million. These amounts have been restated to reflect Reliant Resources' adoption of Emerging Issues Task Force (EITF) Issue No. 02-3, "Issues Related to Accounting for Contracts Involved in Energy Trading and Risk Management Activities" during the third quarter of 2002, as reported in Reliant Resources' Annual Report on Form 10-K/A, Amendment No. 1, filed with the SEC on April 30, 2003.

#### (3) NEW ACCOUNTING PRONOUNCEMENTS

Effective January 1, 2003, the Company adopted SFAS No. 143, "Accounting for Asset Retirement Obligations"



(SFAS No. 143). SFAS No. 143 requires the fair value of an asset retirement obligation to be recognized as a liability is incurred and capitalized as part of the cost of the related tangible long-lived asset. Over time, the liability is accreted to its present value each period, and the capitalized cost is depreciated over the useful life of the related asset. Retirement obligations associated with long-lived assets included within the scope of SFAS No. 143 are those for which a legal obligation exists under enacted laws, statutes and written or oral contracts, including obligations arising under the doctrine of promissory estoppel.

The Company has not identified any asset retirement obligations; however, the Company has previously recognized removal costs as a component of depreciation expense in accordance with regulatory treatment. As of March 31, 2003, these previously recognized removal costs of \$254 million do not represent SFAS No. 143 asset retirement obligations, but rather embedded regulatory liabilities.

In April 2002, the Financial Accounting Standards Board (FASB) issued SFAS No. 145, "Rescission of FASB Statements No. 4, 44, and 64, Amendment of FASB Statement No. 13, and Technical Corrections" (SFAS No. 145). SFAS No. 145 eliminates the current requirement that gains and losses on debt extinguishment must be classified as extraordinary items in the income statement. Instead, such gains and losses will be classified as extraordinary items only if they are deemed to be unusual and infrequent. SFAS No. 145 also requires that capital leases that are modified so that the resulting lease agreement is classified as an operating lease be accounted for as a sale-leaseback transaction. The changes related to debt extinguishment are effective for fiscal years beginning after May 15, 2002, and the changes related to lease accounting are effective for transactions occurring after May 15, 2002. The Company has applied this guidance as it relates to lease accounting and is applying the accounting provision related to debt extinguishment. Upon adoption of SFAS No. 145, any gain or loss on extinguishment of debt that was classified as an extraordinary item in prior periods presented that does not meet the criteria in APB Opinion No. 30 for classification as an extraordinary item in prior periods will be reclassified. No such reclassification was required for the three-month period ended March 31, 2002. The Company has reclassified the \$25 million loss on debt extinguishment related to the fourth quarter of 2002 from extraordinary item to interest expense.

In June 2002, the FASB issued SFAS No. 146, "Accounting for Costs Associated with Exit or Disposal Activities" (SFAS No. 146). SFAS No. 146 nullifies EITF Issue No. 94-3, "Liability Recognition for Certain Employee Termination Benefits and Other Costs to Exit an Activity (including Certain Costs Incurred in a Restructuring)" (EITF No. 94-3). The principal difference between SFAS No. 146 and EITF No. 94-3 relates to the requirements for recognition of a liability for costs associated with an exit or disposal activity. SFAS No. 146 requires that a liability be recognized for a cost associated with an exit or disposal activity when it is incurred. A liability is incurred when a transaction or event occurs that leaves an entity little or no discretion to avoid the future transfer or use of assets to settle the liability. Under EITF No. 94-3, a liability for an exit cost was recognized at the date of an entity's commitment to an exit plan. In addition, SFAS No. 146 also requires that a liability for a cost associated with an exit or disposal activity be recognized at its fair value when it is incurred. SFAS No. 146 is effective for exit or disposal activities that are initiated after December 31, 2002 with early application encouraged. The Company will apply the provisions of SFAS No. 146 to all exit or disposal activities initiated after December 31, 2002.

In November 2002, the FASB issued FASB Interpretation No. (FIN) 45, "Guarantor's Accounting and Disclosure Requirements for Guarantees, Including Indirect Guarantees of Indebtedness of Others" (FIN 45). FIN 45 requires that a liability be recorded in the guarantor's balance sheet upon issuance of certain guarantees. In addition, FIN 45 requires disclosures about the guarantees that an entity has issued. The provision for initial recognition and measurement of the liability will be applied on a prospective basis to guarantees issued or modified after December 31, 2002. The disclosure provisions of FIN 45 are effective for financial statements of interim or annual periods ending after December 15, 2002. The adoption of FIN 45 did not materially affect the Company's consolidated financial statements.

#### (4) REGULATORY MATTERS

##### (a) Excess Cost Over Market (ECOM) True-Up.

Our affiliate, Texas Genco, sells, through auctions, entitlements to substantially all of its installed electric generation capacity, excluding reserves for planned and forced outages. From September 2001 to March 2003, it conducted auctions, as required by the Public Utility Commission of Texas (Texas Utility Commission) and by

CenterPoint Energy's Master Separation Agreement with Reliant Resources. Texas Genco will conduct the final auction mandated by the Texas Utility Commission for the purposes of the ECOM True-Up in July 2003.

The capacity auctions continue to be consummated at market-based prices that are substantially below the estimate of those prices made by the Texas Utility Commission in the spring of 2001. The Texas electric restructuring law provides for the recovery in a "true-up" proceeding in 2004 (2004 True-Up Proceeding) of any difference between market power prices and the earlier estimates of those market prices by the Texas Utility Commission, using the prices received in the auctions required by the Texas Utility Commission as the measure of market prices (ECOM True-Up). For the three months ended March 31, 2002 and 2003, CenterPoint Energy recorded approximately \$141 million and \$132 million, respectively, in non-cash revenue related to the cost recovery of the difference between the market power prices and the Texas Utility Commission's earlier estimates. For additional information regarding the capacity auctions and the related true-up proceeding, please read Notes 3(e) and 4(a) to the CenterPoint Houston 10-K Notes, which are incorporated herein by reference.

(b) Regulatory Assets Contingency.

As of March 31, 2003, in contemplation of the 2004 True-Up Proceeding, the Company has recorded a regulatory asset of \$2.5 billion representing the estimated future recovery of previously incurred stranded costs. This amount includes \$1.1 billion of previously recorded accelerated depreciation (an amount equal to earnings above a stated overall annual rate of return on invested capital that was used to recover CenterPoint Energy's investment in generation assets) and redirected depreciation of \$841 million, both reversed in 2001. In addition, the Company has recorded a regulatory asset associated with CenterPoint Energy's distribution of approximately 19% of the 80 million outstanding shares of common stock of Texas Genco to their shareholders on January 6, 2003 (Texas Genco distribution). As a result of the distribution of Texas Genco common stock, CenterPoint Energy recorded an impairment change of \$396 million. That impairment was transferred to the Company as it represents stranded costs recoverable through the 2004 True-Up Proceeding. Offsetting this regulatory asset is a \$932 million regulatory liability to refund the excess mitigation to ratepayers. This estimated recovery is based upon current projections of the market value of CenterPoint Energy's Texas generation assets to be covered by the 2004 True-up Proceeding calculations. The regulatory liability reflects a current refund obligation arising from prior mitigation of stranded costs deemed excessive by the Texas Utility Commission. The Company began refunding excess mitigation credits with the January 2002 bills. These credits are to be refunded over a seven-year period. Because GAAP requires the Company to estimate fair market values in advance of the final reconciliation, the financial impacts of the Texas electric restructuring law with respect to the final determination of stranded costs in the 2004 True-Up Proceeding are subject to material changes. Factors affecting such changes may include estimation risk, uncertainty of future energy and commodity prices and the economic lives of the plants. If events were to occur that made the recovery of some of the remaining generation related regulatory assets no longer probable, the Company would write off the unrecoverable balance of such assets as a charge against earnings.

(c) Fuel Reconciliation Contingency.

Texas Genco and the Company filed their joint application to reconcile fuel revenues and expenses with the Texas Utility Commission on July 1, 2002. This final fuel reconciliation filing covers reconcilable fuel revenue, fuel expense and interest of approximately \$8.5 billion incurred from August 1, 1997 through January 30, 2002. Also included in this amount is an under-recovery of \$94 million, which was the balance at July 31, 1997 as approved in the Company's last fuel reconciliation. On March 3, 2003, a settlement agreement was filed under which certain items totaling \$24 million would be written off during the fourth quarter of 2002 and items totaling \$203 million would be carried forward for resolution by the Texas Utility Commission in late 2003 or early 2004.

(5) INTANGIBLES

Amortization expense for the Company's specifically identifiable intangible assets was immaterial and is expected to be immaterial for the next five years.

(6) LONG-TERM DEBT AND SHORT-TERM BORROWINGS

	DECEMBER 31, 2002		MARCH 31, 2003	
	LONG-TERM	CURRENT(1)	LONG-TERM	CURRENT(1)
Long-term debt:				
First mortgage bonds 5.70% to 9.15% due 2013 to 2033.....	\$ 615	\$ --	\$ 1,065	\$ --
Term loan, LIBOR plus 9.75%, due 2005(2).....	1,310	--	1,310	--
Series 2001-1 Transition Bonds 3.84% to 5.63% Due 2002 to 2013(3).....	717	19	703	26
Other.....	(1)	--	(3)	--
Long-term debt to third parties.....	2,641	19	3,075	26
Notes payable to affiliate 4.90% to 6.70%(4).....	916	167	637	17
Total borrowings.....	\$ 3,557	\$ 186	\$ 3,712	\$ 43

(1) Includes amounts due within one year of the date noted.

(2) LIBOR has a minimum rate of 3%. This collateralized term loan is secured by the Company's general mortgage bonds.

(3) The Series 2001-1 Transition Bonds were issued by one of the Company's subsidiaries, and are non-recourse to the Company. For further discussion of the securitization financing, see Note 4(a) of the CenterPoint Houston Form 10-K, which is incorporated herein by reference.

(4) Of the total \$654 million notes payable to affiliate at March 31, 2003, \$397 million has the same principal amounts and interest rates as the pollution control bond obligations of CenterPoint Energy that are secured by first mortgage bonds of CenterPoint Houston.

Money Pool Borrowings

On March 31, 2003, the Company had borrowed approximately \$155 million from its affiliates, which had a weighted average interest rate of 6.25%. The Company participates in a "money pool" through which it can borrow or invest on a short-term basis. Funding needs are aggregated and external borrowing or investing is based on the net cash position. The money pool's net funding requirements are generally met with borrowings of CenterPoint Energy. The terms of the money pool are in accordance with requirements applicable to registered public utility holding companies under the 1935 Act.

Long-Term Debt

On March 18, 2003, the Company issued \$762.3 million aggregate principal amount of general mortgage bonds composed of \$450 million principal amount of 10-year bonds with an interest rate of 5.7% and \$312.3 million principal amount of 30-year bonds with an interest rate of 6.95%. Proceeds were used to repay a \$150 million note payable to CenterPoint Energy that matured on April 21, 2003, to redeem approximately \$312 million aggregate principal amount of the Company's first mortgage bonds and to repay \$279 million of a \$537 million intercompany note payable to CenterPoint Energy.

The following table shows future maturity dates of long-term debt issued by CenterPoint Houston and expected future maturity dates of the transition bonds issued by CenterPoint Energy Transition Company, LLC, a subsidiary of the Company (Bond Company) as of March 31, 2003. Amounts are expressed in thousands.

YEAR	CENTERPOINT HOUSTON			TRANSITION BONDS	TOTAL
	THIRD-PARTY	AFFILIATE	SUB-TOTAL		
2003.....	\$ --	\$ 16,600	\$ 16,600	\$ 12,357	\$ 28,957
2004.....	--	--	--	41,189	41,189
2005.....	1,310,000	--	1,310,000	46,806	1,356,806
2006.....	--	--	--	54,295	54,295
2007.....	--	--	--	59,912	59,912
2008.....	--	--	--	65,529	65,529
2009.....	--	--	--	73,018	73,018
2010.....	--	--	--	80,506	80,506
2011.....	--	--	--	87,995	87,995
2012.....	--	45,570	45,570	99,229	144,799
2013.....	450,000	--	450,000	108,590	558,590
2015.....	--	150,850	150,850	--	150,850
2017.....	--	127,385	127,385	--	127,385
2021.....	102,442	--	102,442	--	102,442
2023.....	200,000	--	200,000	--	200,000
2027.....	--	56,095	56,095	--	56,095
2028.....	--	257,500	257,500	--	257,500
2033.....	312,275	--	312,275	--	312,275
Total	\$2,374,717	\$ 654,000	\$3,028,717	\$729,426	\$3,758,143

First mortgage bonds and general mortgage bonds in aggregate principal amounts of \$302 million and \$762 million, respectively, have been issued directly to third parties. External debt of \$1.3 billion maturing in 2005 is senior and secured by general mortgage bonds. The affiliate debt is senior and unsecured.

Other than the affiliate note due 2028 set forth in the above table, the amounts, maturities and interest rates of the intercompany debt payable to CenterPoint Energy of \$397 million effectively match the amounts, maturities and interest rates of certain pollution control bond obligations of CenterPoint Energy that are secured by the Company's first mortgage bonds in the same amounts in the table below.

The following table shows the maturity dates of the \$924 million of first mortgage bonds and general mortgage bonds that the Company has issued as collateral for long-term debt of CenterPoint Energy. These bonds are not reflected on the financial statements of CenterPoint Houston because of the contingent nature of the obligations. Amounts are expressed in thousands.

YEAR	FIRST MORTGAGE BONDS	GENERAL MORTGAGE BONDS	TOTAL
2003.....	\$ 16,600	\$ --	\$ 16,600
2011.....	--	19,200	19,200
2012.....	45,570	--	45,570
2015.....	150,850	--	150,850
2017.....	127,385	--	127,385
2018.....	--	50,000	50,000
2019.....	--	200,000	200,000
2020.....	--	90,000	90,000
2026.....	--	100,000	100,000
2027.....	56,095	--	56,095
2028.....	--	68,000	68,000
Total	\$396,500	\$ 527,200	\$ 923,700

The aggregate amount of additional general mortgage bonds and first mortgage bonds that could be issued is approximately \$600 million based on estimates of the value of property encumbered by the general mortgage, the cost of such property and the 70% bonding ratio contained in the general mortgage. As a result of contractual limitations expiring in November 2005, the aggregate amount of first mortgage bonds and general mortgage bonds cannot currently be increased. As of March 31, 2003, outstanding first mortgage bonds and general mortgage bonds aggregated approximately \$3.3 billion as shown in the following table. Amounts are expressed in thousands.

	ISSUED DIRECTLY TO THIRD PARTIES	ISSUED AS COLLATERAL FOR THE COMPANY'S DEBT	ISSUED AS COLLATERAL FOR CENTERPOINT ENERGY'S DEBT	TOTAL
First Mortgage Bonds	\$ 302,442	\$ --	\$ 396,500	\$ 698,942
General Mortgage Bonds	762,275	1,310,000	527,200	2,599,475
Total	\$ 1,064,717	\$1,310,000	\$ 923,700	\$ 3,298,417

The Bond Company has \$729 million aggregate principal amount of outstanding transition bonds. Classes of the transition bonds have final maturity dates of September 15, 2007, September 15, 2009, September 15, 2011 and September 15, 2015 and bear interest at rates of 3.84%, 4.76%, 5.16% and 5.63%, respectively. The transition bonds are secured by "transition property," as defined in the Texas electric restructuring law, which includes the irrevocable right to recover, through non-bypassable transition charges payable by retail electric customers, qualified costs provided in the Texas electric restructuring law and a tariff issued by the Texas Utility Commission. The transition bonds are reported as CenterPoint Houston's long-term debt, although the holders of the transition bonds have no recourse to any of CenterPoint Houston's assets or revenues, and CenterPoint Houston's creditors have no recourse to any assets or revenues (including, without limitation, the transition charges) of the Bond Company. CenterPoint Houston has no payment obligations with respect to the transition bonds except to remit collections of transition charges as set forth in a servicing agreement between CenterPoint Houston and the Bond Company and in an intercreditor agreement among CenterPoint Houston, the Bond Company and other parties.

Liens. The Company's assets are subject to liens securing approximately \$699 million of first mortgage bonds. Sinking or improvement fund and replacement fund requirements on the first mortgage bonds may be satisfied by certification of property additions. Sinking fund and replacement fund requirements for 2001, 2002 and 2003 have been satisfied by certification of property additions. The replacement fund requirement satisfied in 2003 was approximately \$354 million, and the sinking fund requirement satisfied in 2003 was approximately \$8 million. The Company's assets are subject to liens securing approximately \$2.6 billion of general mortgage bonds, which are junior to the liens of the first mortgage bonds.

(7) COMPREHENSIVE INCOME

The following table summarizes the components of total comprehensive income:

	FOR THE THREE MONTHS ENDED MARCH 31,	
	2002	2003
	(IN MILLIONS)	
Net income .....	\$ 32	\$80
Other comprehensive income:		
Other comprehensive income from discontinued operations .....	174	--
Additional minimum non-qualified pension liability adjustment .....	1	--
Other comprehensive income .....	175	--
Comprehensive income .....	\$207	\$80

(8) RELATED PARTY TRANSACTIONS

From time to time, the Company has advanced money to, or borrowed money from, CenterPoint Energy or its subsidiaries. As of December 31, 2002, the Company had net short-term borrowings included in accounts payable-affiliated companies of \$44 million and \$215 million included in notes payable-affiliated companies. As of March 31, 2003, the Company had net short-term-borrowings of \$21 million in accounts payable-affiliated companies, which included accounts payable of \$45 million, partially offset by accounts receivable of \$24 million. The Company had net short-term borrowings of \$172 million in notes payable-affiliated companies as of March 31,

2003, which included net short-term notes payables of \$155 million and \$17 million current portion of long-term notes payable. The Company had a long-term note receivable from affiliate of \$815 million, as of December 31, 2002 and March 31, 2003, as further discussed below. Long-term note payable to affiliate was \$1.1 billion as of December 31, 2002 and \$654 million as of March 31, 2003. For more information on the long-term note payable to affiliate see Note 6. The Company had net interest expense related to affiliate borrowings of \$30 million and \$18 million for the three months ended March 31, 2002 and March 31, 2003, respectively. As of March 31, 2003, the Company had \$396 million in long-term accounts payable-affiliated companies, which related to the Texas Genco distribution. For more information on the long-term accounts payable to affiliate see Note 4(b).

Prior to August 31, 2002, the Company had \$737 million invested in a money fund through which the Company and certain of its affiliates could borrow and/or invest on a short-term basis. At the time of the Restructuring, the Company converted a money fund investment into a \$750 million note receivable from CenterPoint Energy payable on demand and bearing interest at the prime rate, leaving \$13 million borrowed from the money fund. Since August 31, 2002, the Company has been a participant in the CenterPoint Energy money pool. The \$750 million note receivable is included in long-term notes receivable from affiliate in the Consolidated Balance Sheets because CenterPoint Energy does not plan to repay the note within the next twelve months.

For the three months ended March 31, 2002, revenues, excluding transition charges, derived from energy delivery charges provided by the Company to subsidiaries of Reliant Resources, Inc. (Reliant Resources), a former affiliate, totaled \$117 million.

Although the former retail sales business is no longer conducted by the Company, retail customers remained regulated customers of the Company through the date of their first meter reading in January 2002. During this transition period, the Company purchased \$60 million of power from Texas Genco as of March 31, 2002.

CenterPoint Energy provides some corporate services to the Company. The costs of services have been charged directly to the Company using methods that management believes are reasonable. These methods include negotiated usage rates, dedicated asset assignment and proportionate corporate formulas based on assets, operating expenses and employees. These charges are not necessarily indicative of what would have been incurred had the Company not been an affiliate. Amounts charged to the Company for these services were \$11 million and \$32 million for the three months ended March 31, 2002 and 2003, respectively, and are included primarily in operation and maintenance expenses.

## (9) LEGAL PROCEEDINGS

### (a) Legal Matters

The Company's predecessor, Reliant Energy, and certain of its former subsidiaries are named as defendants in several lawsuits described below. Under a master separation agreement between Reliant Energy and Reliant Resources, CenterPoint Energy and its subsidiaries, including the Company, are entitled to be indemnified by Reliant Resources for any losses arising out of the lawsuits described under "California Class Actions and Attorney General Cases," "Long-Term Contract Class Action," "Washington and Oregon Class Actions," "Bustamante Price Reporting Class Action," "Gas Trading Class Action" and "Trading and Marketing Activities," including attorneys' fees and other costs. Pursuant to the indemnification obligation, Reliant Resources is defending CenterPoint Energy and its subsidiaries, including the Company, to the extent named in these lawsuits. The ultimate outcome of these matters cannot be predicted at this time.

California Class Actions and Attorney General Cases. Reliant Energy, Reliant Resources, Reliant Energy Power Generation, Inc. (REPG) and several other subsidiaries of Reliant Resources, as well as two former officers and one present officer of some of these companies, have been named as defendants in class action lawsuits and other lawsuits filed against a number of companies that own generation plants in California and other sellers of electricity in California markets. While the plaintiffs allege various violations by the defendants of antitrust laws and state laws against unfair and unlawful business practices, each of the lawsuits is grounded on the central allegation that the defendants conspired to drive up the wholesale price of electricity. In addition to injunctive relief, the plaintiffs in these lawsuits seek treble the amount of damages alleged, restitution of alleged overpayments, disgorgement of alleged unlawful profits for sales of electricity, costs of suit and attorneys' fees. The first six of these suits originally were filed in state courts in San Diego, San Francisco and Los Angeles Counties. The suits in San Diego and Los

Angeles Counties were consolidated and removed to the federal district court in San Diego, but on December 13, 2002, that court remanded the suits to the state courts. Prior to the remand, Reliant Energy was voluntarily dismissed from two of the suits. Several parties, including the Reliant defendants, have appealed the judge's remand decision. The United States court of appeals has entered a briefing schedule that could result in oral arguments by the summer of 2003 and stayed the remand order pending that appeal.

In March and April 2002, the California Attorney General filed three complaints, two in state court in San Francisco and one in the federal district court in San Francisco, against Reliant Energy, Reliant Resources, Reliant Energy Services and other subsidiaries of Reliant Resources alleging, among other matters, violations by the defendants of state laws against unfair and unlawful business practices arising out of transactions in the markets for ancillary services run by the California independent systems operator, charging unjust and unreasonable prices for electricity, in violation of antitrust laws in connection with the acquisition in 1998 of electric generating facilities located in California. The complaints variously seek restitution and disgorgement of alleged unlawful profits for sales of electricity, civil penalties and fines, injunctive relief against unfair competition, divestment of Reliant Resources' generation capacity and undefined equitable relief. Reliant Resources removed the two state court cases to the federal district court in San Francisco. In August 2002, the district court dismissed the two cases originally filed in state court and also dismissed the damages claims asserted in the antitrust case. The Attorney General has appealed the dismissal of these cases to the court of appeals.

Following the filing of the Attorney General cases, seven additional class action cases were filed in state courts in Northern California. Each of these purports to represent the same class of California ratepayers, assert the same claims as asserted in the other California class action cases, and in some instances repeat as well the allegations in the Attorney General cases. All of these cases have been removed to federal district court in San Diego. Reliant Resources has not filed an answer in any of these cases.

In all of these cases pending before the federal and state courts in California, the Reliant defendants have filed or intend to file motions to dismiss on grounds that the claims are barred by federal preemption and the filed rate doctrine.

Long-Term Contract Class Action. In October 2002, a class action was filed in state court in Los Angeles against Reliant Energy and several subsidiaries of Reliant Resources. The complaint in this case repeats the allegations asserted in the California class actions as well as the Attorney General cases and also alleges misconduct related to long-term contracts purportedly entered into by the California Department of Water Resources. None of the Reliant entities, however, has a long-term contract with the Department of Water Resources. This case has been removed to federal district court in San Diego. The Reliant defendants intend to file motions to dismiss on grounds that the claims are barred by federal preemption and the filed rate doctrine.

Washington and Oregon Class Actions. In December 2002, a lawsuit was filed in Circuit Court of the State of Oregon for the County of Multnomah on behalf of a class of all Oregon purchasers of electricity and natural gas. Reliant Energy, Reliant Resources and several Reliant Resources subsidiaries are named as defendants, along with many other electricity generators and marketers. Like the other lawsuits filed in California, the plaintiffs claim the defendants manipulated wholesale power prices in violation of state and federal law. The plaintiffs seek injunctive relief and payment of damages based on alleged overcharges for electricity. Also in December 2002, a nearly identical lawsuit on behalf of consumers in the State of Washington was filed in federal district court in Seattle. Reliant Resources has removed the Oregon suit to federal district court in Portland. It is anticipated that before answering the lawsuits, the defendants will file motions to dismiss on the grounds that the claims are barred by federal preemption and by the filed rate doctrine.

Bustamante Price Reporting Class Action. In November 2002, California Lieutenant Governor Cruz Bustamante filed a lawsuit in state court in Los Angeles on behalf of a class of purchasers of gas and power alleging violations of state antitrust laws and state laws against unfair and unlawful business practices based on an alleged conspiracy to report and publish false and fraudulent natural gas prices with an intent to affect the market prices of natural gas and electricity in California. Reliant Energy, Reliant Resources and several Reliant Resources subsidiaries are named as defendants, along with other market participants and publishers of some of the price indices. The complaint seeks injunctive relief, compensatory and punitive damages, restitution of alleged overpayment, disgorgement of all profits and funds acquired by the alleged unlawful conduct, costs of suit and attorneys' fees. The Reliant defendants intend to deny both their alleged violation of any laws and their alleged participation in any conspiracy.

Gas Trading Class Action. CenterPoint Energy, Reliant Resources and Reliant Energy have been named as defendants in a lawsuit filed in April 2003 in state court in Los Angeles County, California on behalf of a class of purchasers of natural gas alleging violations of state antitrust laws and state laws against unfair and unlawful business practices based on an alleged conspiracy with Enron Corp. to manipulate the California natural gas markets in 2000 and 2001. The complaint is based on certain conclusions in a report by the staff of the Federal Energy Regulatory Commission (FERC) that has not been subject to procedures designed to allow parties to either discover or test the basis for the conclusions. The complaint seeks injunctive and declaratory relief, compensatory and punitive damages, restitution, costs of suit and attorneys' fees. The complaint alleges that there was "well over one billion dollars in excess charges to California consumers during the 2000 through 2001 time period." The plaintiffs are seeking a trebling of any damages award. While Reliant Resources has not yet filed an answer, CenterPoint Energy understands that Reliant Resources intends to deny both the alleged violation of any laws and the participation in a conspiracy with Enron. Further, neither CenterPoint Energy nor any of its current subsidiaries has ever engaged in gas trading in California

Trading and Marketing Activities. Reliant Energy has been named as a party in several lawsuits and regulatory proceedings relating to the trading and marketing activities of its former subsidiary, Reliant Resources.

In June 2002, the SEC advised Reliant Resources and Reliant Energy that it had issued a formal order in connection with its investigation of Reliant Resources' financial reporting, internal controls and related matters. The Company understands that the investigation is focused on Reliant Resources' same-day commodity trading transactions involving purchases and sales with the same counterparty for the same volume at substantially the same price and certain structured transactions. These matters were previously the subject of an informal inquiry by the SEC. Reliant Resources and CenterPoint Energy are cooperating with the SEC staff. On May 12, 2003, the SEC advised Reliant Resources and Reliant Energy that it had issued a formal order in connection with this investigation. Reliant Energy, through the Company as its successor, has entered into a settlement with the SEC that concludes this investigation. Under the settlement, Reliant Resources and Reliant Energy consented to the entry of an administrative cease-and-desist order with respect to future violations of certain provisions of the Securities Act of 1933 and the Securities Exchange Act of 1934, without admitting or denying the SEC's findings that violations of these laws had occurred. The SEC did not assess monetary penalties or fines against Reliant Energy, CenterPoint Energy or any of its subsidiaries including the Company.

In connection with the Texas Utility Commission's industry-wide investigation into potential manipulation of the ERCOT market on and after July 31, 2001, Reliant Energy and Reliant Resources have provided information to the Texas Utility Commission concerning their scheduling and trading activities.

Fifteen class action lawsuits filed in May, June and July 2002 on behalf of purchasers of securities of Reliant Resources and/or Reliant Energy have been consolidated in federal district court in Houston. Reliant Resources and certain of its former and current executive officers are named as defendants. Reliant Energy is also named as a defendant in seven of the lawsuits. Two of the lawsuits also name as defendants the underwriters of the May 2001 initial public offering of approximately 20% of the common stock of Reliant Resources (Reliant Resources Offering). One lawsuit names Reliant Resources' and Reliant Energy's independent auditors as a defendant. The consolidated amended complaint seeks monetary relief purportedly on behalf of three classes: (1) purchasers of Reliant Energy common stock from February 3, 2000 to May 13, 2002; (2) purchasers of Reliant Resources common stock on the open market from May 1, 2001 to May 13, 2002; and (3) purchasers of Reliant Resources common stock in the Reliant Resources Offering or purchasers of shares that are traceable to the Reliant Resources Offering. The plaintiffs allege, among other things, that the defendants misrepresented their revenues and trading volumes by engaging in round-trip trades and improperly accounted for certain structured transactions as cash-flow hedges, which resulted in earnings from these transactions being accounted for as future earnings rather than being accounted for as earnings in fiscal year 2001.

In February 2003, a lawsuit was filed by three individuals in federal district court in Chicago against CenterPoint Energy and certain former and current officers of Reliant Resources for alleged violations of federal securities laws. The plaintiffs in this lawsuit allege that the defendants violated federal securities laws by issuing false and misleading statements to the public, and that the defendants made false and misleading statements as part of an alleged scheme to inflate artificially trading volumes and revenues. In addition, the plaintiffs assert claims of



fraudulent and negligent misrepresentation and violations of Illinois consumer law. The defendants expect to file a motion to transfer this lawsuit to the federal district court in Houston and to consolidate this lawsuit with the consolidated lawsuits described above.

The Company believes that none of these lawsuits has merit because, among other reasons, the alleged misstatements and omissions were not material and did not result in any damages to any of the plaintiffs.

In May 2002, three class action lawsuits were filed in federal district court in Houston on behalf of participants in various employee benefits plans sponsored by Reliant Energy. Reliant Energy and its directors are named as defendants in all of the lawsuits. Two of the lawsuits have been dismissed without prejudice. The remaining lawsuit alleges that the defendants breached their fiduciary duties to various employee benefits plans, directly or indirectly sponsored by Reliant Energy, in violation of the Employee Retirement Income Security Act. The plaintiffs allege that the defendants permitted the plans to purchase or hold securities issued by Reliant Energy when it was imprudent to do so, including after the prices for such securities became artificially inflated because of alleged securities fraud engaged in by the defendants. The complaints seek monetary damages for losses suffered by a putative class of plan participants whose accounts held Reliant Energy or Reliant Resources securities, as well as equitable relief in the form of restitution.

In October 2002, a derivative action was filed in the federal district court in Houston, against the directors and officers of CenterPoint Energy. The complaint sets forth claims for breach of fiduciary duty, waste of corporate assets, abuse of control and gross mismanagement. Specifically, the shareholder plaintiff alleges that the defendants caused CenterPoint Energy to overstate its revenues through so-called "round trip" transactions. The plaintiff also alleges breach of fiduciary duty in connection with the spin-off of Reliant Resources and the Reliant Resources Offering. The complaint seeks monetary damages on behalf of CenterPoint Energy as well as equitable relief in the form of a constructive trust on the compensation paid to the defendants. On March 13, 2003, the court dismissed this case on the ground that the plaintiff did not make an adequate demand on CenterPoint Energy before filing suit. On March 26, 2003, the plaintiff sent another demand asserting the same claims.

CenterPoint Energy's board of directors is investigating that demand and similar allegations made in a June 28, 2002 demand letter sent on behalf of a CenterPoint Energy shareholder. The latter letter states that the shareholder and other shareholders are considering filing a derivative suit on behalf of CenterPoint Energy and demands that CenterPoint Energy take several actions in response to alleged round-trip trades occurring in 1999, 2000, and 2001. The Board is reviewing the demands made by the shareholders to determine if these proposed actions are in the best interests of CenterPoint Energy.

Reliant Energy Municipal Franchise Fee Lawsuits. In February 1996, the cities of Wharton, Galveston and Pasadena filed suit, for themselves and a proposed class of all similarly situated cities in Reliant Energy's electric service area, against Reliant Energy and Houston Industries Finance, Inc. (formerly a wholly owned subsidiary of Reliant Energy) alleging underpayment of municipal franchise fees. The plaintiffs claim that they are entitled to 4% of all receipts of any kind for business conducted within these cities over the previous four decades. A jury trial of the original claimant cities (but not the class of cities) in the 269th Judicial District Court for Harris County, Texas, ended in April 2000 (the Three Cities case). Although the jury found for Reliant Energy on many issues, it found in favor of the original claimant cities on three issues, and assessed a total of \$4 million in actual and \$30 million in punitive damages. However, the jury also found in favor of Reliant Energy on the affirmative defense of laches, a defense similar to a statute of limitations defense, due to the original claimant cities having unreasonably delayed bringing their claims during the 43 years since the alleged wrongs began. The trial court in the Three Cities case granted most of Reliant Energy's motions to disregard the jury's findings. The trial court's rulings reduced the judgment to \$1.7 million, including interest, plus an award of \$13.7 million in legal fees. In addition, the trial court granted Reliant Energy's motion to decertify the class. Following this ruling, 45 cities filed individual suits against Reliant Energy in the District Court of Harris County.

On February 27, 2003, the state court of appeals in Houston rendered an opinion reversing the judgment against CenterPoint Energy and rendering judgment that the Three Cities take nothing by their claims. The court of appeals found that the jury's finding of laches barred all of the Three Cities' claims and that the Three Cities were not entitled to recovery of any attorneys' fees. The judgment of the court of appeals is subject to an appeal to the Texas Supreme Court.

The extent to which issues in the Three Cities case may affect the claims of the other cities served by Reliant Energy cannot be assessed until judgments are final and no longer subject to appeal. However, the court of appeals' ruling appears to be consistent with Texas Supreme Court opinions. The Company estimates the range of possible outcomes for recovery by the plaintiffs in the Three Cities case to be between \$0 and \$18 million inclusive of interest and attorneys' fees.

#### Other Matters

The Company is involved in other legal, environmental, tax and regulatory proceedings before various courts, regulatory commissions and governmental agencies regarding matters arising in the ordinary course of business. Some of these proceedings involve substantial amounts. The Company's management regularly analyzes current information and, as necessary, provides accruals for probable liabilities on the eventual disposition of these matters. The Company's management believes that the disposition of these matters will not have a material adverse effect on the Company's financial condition, results of operations or cash flows.

#### (b) "Price to Beat" Clawback Component.

In connection with the implementation of the Texas electric restructuring law, the Texas Utility Commission has set a "price to beat" that retail electric providers affiliated or formerly affiliated with a former integrated utility must charge residential and small commercial customers within their affiliated electric utility's service area. The true-up provides for a clawback of "price to beat" in excess of the market price of electricity if 40% of the "price to beat" load is not served by a non-affiliated retail electric provider by January 1, 2004. Pursuant to the Texas electric restructuring law and the master separation agreement between Reliant Energy and Reliant Resources, Reliant Resources is obligated to pay CenterPoint Houston for the clawback component of the true-up. The clawback may not exceed \$150 times the number of customers served by the affiliated retail electric provider in the transmission and distribution utility's service territory, less the number of customers served by the affiliated retail electric provider outside the transmission and distribution utility's service territory, on January 1, 2004.

ITEM 2. MANAGEMENT'S NARRATIVE ANALYSIS OF THE RESULTS OF OPERATIONS OF  
CENTERPOINT ENERGY HOUSTON ELECTRIC, LLC AND SUBSIDIARIES

The following narrative analysis should be read in combination with CenterPoint Energy Houston Electric, LLC's Interim Financial Statements and notes contained in this Form 10-Q.

Effective August 31, 2002, Reliant Energy, Incorporated (Reliant Energy) consummated a restructuring transaction (the Restructuring) in which it, among other things, (1) conveyed its Texas electric generation assets to an affiliated company, Texas Genco Holdings, Inc. (Texas Genco), (2) became an indirect, wholly owned subsidiary of a new utility holding company, CenterPoint Energy, Inc. (CenterPoint Energy), (3) was converted into a Texas limited liability company named CenterPoint Energy Houston Electric, LLC (CenterPoint Houston or the Company), and (4) distributed the capital stock of its operating subsidiaries, including Texas Genco, to CenterPoint Energy. As part of the Restructuring, each share of Reliant Energy common stock was converted into one share of CenterPoint Energy common stock. Pursuant to the provisions of certain of its existing debt agreements applicable when the properties or assets of Reliant Energy were transferred to another entity substantially as an entirety, CenterPoint Energy expressly assumed certain debt and other obligations of Reliant Energy, and Reliant Energy was released as the primary obligor on such debt. For additional information on the Restructuring, see Note 1 to the Interim Financial Statements.

We operate Reliant Energy's electric transmission and distribution business, which continues to be subject to cost-of-service rate regulation and is responsible for the delivery of electricity sold to retail customers through retail electric providers in the 5,000 square mile service area of Houston, Texas and surrounding metropolitan areas as well as the transmission of bulk power into and out of the Houston area.

Contemporaneous with the Restructuring, CenterPoint Energy registered and became subject, with its subsidiaries, to regulation as a registered holding company system under the Public Utility Holding Company Act of 1935 (1935 Act). The 1935 Act directs the SEC to regulate, among other things, transactions among affiliates, sales or acquisitions of assets, issuance of securities, distributions and permitted lines of business.

The Interim Financial Statements have been prepared to reflect the effect of the Restructuring as described above as it relates to CenterPoint Houston, and have been prepared based upon Reliant Energy's historical consolidated financial statements.

The Interim Financial Statements present the former subsidiaries of Reliant Energy that were distributed to CenterPoint Energy in the Restructuring as discontinued operations, in accordance with Statement of Financial Accounting Standards (SFAS) No. 144, "Accounting for the Impairment or Disposal of Long-Lived Assets" (SFAS No. 144). Accordingly, the Interim Financial Statements of CenterPoint Houston reflect these operations as discontinued operations for the three months ended March 31, 2002.

We meet the conditions specified in General Instruction H(1)(a) and (b) to Form 10-Q and are therefore permitted to use the reduced disclosure format for wholly owned subsidiaries of reporting companies. Accordingly, we have omitted from this report the information called for by Item 2 (Management's Discussion and Analysis of Financial Condition and Results of Operations), Item 3 (Quantitative and Qualitative Disclosures About Market Risk) of Part I and the following Part II items of Form 10-Q: Item 2 (Changes in Securities), Item 3 (Defaults Upon Senior Securities) and Item 4 (Submission of Matters to a Vote of Security Holders). The following discussion explains material changes in CenterPoint Houston's our results of operations between the three months ended March 31, 2003 and the three months ended March 31, 2002. Reference is made to "Management's Narrative Analysis of Results of Operations" in Item 7 of our Annual Report on Form 10-K for the year ended December 31, 2002 (CenterPoint Houston Form 10-K).

#### CONSOLIDATED RESULTS OF OPERATIONS

Our results of operations are affected by, among other things, seasonal fluctuations and other changes in the demand for electricity, the actions of various governmental authorities having jurisdiction over the rates we charge, debt service costs, income tax expense, our ability to collect receivables from retail electric providers and our ability

to recover our stranded costs and regulatory assets. For more information regarding factors that may affect the future results of operations of our business, please read "Business -- Risk Factors" in Item 1 of the CenterPoint Houston Form 10-K and "Management's Narrative Analysis of Results of Operations -- Certain Factors Affecting Future Earnings" in Item 7 of the CenterPoint Houston Form 10-K, each of which is incorporated herein by reference.

The following table sets forth our consolidated results of operations for the three months ended March 31, 2002 and 2003, followed by a discussion of our consolidated results of operations based on earnings from continuing operations before interest expense, distribution on trust preferred securities and income taxes (EBIT). EBIT, as defined, is shown because it is a financial measure we use to evaluate the performance of our business segments and we believe it is a measure of financial performance that may be used as a means to analyze and compare companies on the basis of operating performance. We expect that some analysts and investors will want to review EBIT when evaluating our company. EBIT is not defined under accounting principles generally accepted in the United States of America (GAAP), should not be considered in isolation or as a substitute for a measure of performance prepared in accordance with GAAP and is not indicative of operating income from operations as determined under GAAP. Additionally, our computation of EBIT may not be comparable to other similarly titled measures computed by other companies, because all companies do not calculate it in the same fashion. We consider operating income to be a comparable measure under GAAP. We believe the difference between operating income and EBIT on both a consolidated and business segment basis is not material. We have provided a reconciliation of consolidated operating income to EBIT and EBIT to net income below.

	THREE MONTHS ENDED MARCH 31,	
	2002	2003
	-----	-----
	(IN MILLIONS)	
Operating Revenues:		
Electric revenues .....	\$ 427	\$ 316
ECOM true-up .....	141	132
	-----	-----
Total Operating Revenues .....	568	448
	-----	-----
Operating Expenses:		
Purchased power .....	60	--
Operation and maintenance .....	141	133
Depreciation and amortization .....	63	65
Taxes other than income .....	50	44
	-----	-----
Total Operating Expenses .....	314	242
	-----	-----
Operating Income .....	254	206
Other Income, net .....	5	8
	-----	-----
Earnings Before Interest and Taxes .....	259	214
Interest Expense and Distribution on Trust Preferred Securities .....	(60)	(92)
	-----	-----
Income from Continuing Operations Before Income Taxes .....	199	122
Income Tax Expense .....	(67)	(42)
	-----	-----
Income from Continuing Operations .....	132	80
Loss from Discontinued Operations, net of tax .....	(100)	--
	-----	-----
Net Income .....	\$ 32	\$ 80
	=====	=====
Throughput Data (Gwh(1)):		
Residential .....	4,473	4,558
Commercial .....	3,975	4,008
Industrial .....	6,338	6,186
Other .....	42	36
	-----	-----
Total Throughput .....	14,828	14,788
	=====	=====

(1) Gigawatt hours

THREE MONTHS ENDED MARCH 31, 2003 COMPARED TO THREE MONTHS ENDED MARCH 31, 2002

We reported EBIT of \$214 million for the three months ended March 31, 2003, consisting of \$82 million for the regulated electric transmission & distribution utility and non-cash EBIT of \$132 million associated with generation-related regulatory assets, or Excess Cost Over Market (ECOM), as described below. For the three months ended

March 31, 2002, EBIT was \$259 million, consisting of \$104 million for the regulated electric transmission & distribution utility, non-cash EBIT of \$141 million associated with ECOM, and \$14 million related to the transition to the deregulated electric market. Although our former retail sales business is no longer conducted by us, retail customers remained regulated customers of the regulated utility through the date of their first meter reading in 2002. The purchased power costs of \$60 million for the three months ended March 31, 2002 relate to operation of the regulated utility during this transition period.

Our business, excluding ECOM and transition related-EBIT, continues to benefit from solid customer growth. Reduced revenues from industrial customers (\$9 million) and higher employee benefit and insurance costs (\$8 million) more than offset increased revenues from the addition of over 50,000 metered customers since March 2002 (\$8 million).

Under the Texas electric restructuring law, a regulated utility may recover, in its 2004 stranded cost true-up proceeding, any difference between market prices received through the state mandated auctions and the Texas Utility Commission's earlier estimates of those market prices. During 2002 and 2003, this difference, referred to as ECOM, produces non-cash EBIT and is recorded as a regulatory asset. The reduction in ECOM of \$9 million from 2002 to 2003 resulted from an increase in capacity auction prices at Texas Genco.

In the electric transmission & distribution business, throughput remained level during the three months ended March 31, 2003 as compared to the same period in 2002.

Operation and maintenance expense decreased \$8 million for the three months ended March 31, 2003 as compared to the same period in 2002. The decrease was primarily due to a reduction in bad debt expense of \$17 million related to the reduction in transition period (bundled) revenues (\$14 million) and the termination of a factoring program (\$3 million). This decrease in bad debt expense was partially offset by increased employee benefit expenses primarily due to increased pension costs (\$5 million) and increased insurance expenses (\$3 million).

Depreciation and amortization expense increased \$2 million for the three months ended March 31, 2003 as compared to the same period in 2002 primarily due to increases in plant in service (\$4 million) partially offset by decreased amortization on securitized assets (\$2 million).

Taxes other than income taxes decreased \$6 million for the three months ended March 31, 2003 as compared to the same period in 2002 primarily due to gross receipts tax associated with transition period revenue in the first quarter of 2002.

Other income, net increased \$3 million for the three months ended March 31, 2003, compared to the same period in 2002. The increase was primarily due to interest income partially offset by decreased interest on under recovery of fuel.

CenterPoint Houston's effective tax rate for the three months ended March 31, 2002 and 2003 was 33.8% and 34.2%, respectively.

#### LIQUIDITY

##### Long-Term Debt.

On March 18, 2003, we issued \$762.3 million aggregate principal amount of general mortgage bonds composed of \$450 million principal amount of 10-year bonds with an interest rate of 5.7% and \$312.3 million principal amount of 30-year bonds with an interest rate of 6.95%. Proceeds were used to repay a \$150 million note payable to CenterPoint Energy that matured on April 21, 2003, to redeem approximately \$312.3 million aggregate principal amount of the Company's first mortgage bonds and to repay \$279 million of a \$537 million intercompany note payable to CenterPoint Energy. Proceeds from the note repayment were ultimately used to repay borrowings under CenterPoint Energy's \$3.85 billion credit facility, which is discussed below, and to permanently reduce the term loan component of the credit facility by \$50 million.

The following table shows future maturity dates of long-term debt issued by us to third parties and affiliates and expected future maturity dates of transition bonds issued by our subsidiary, CenterPoint Energy Transition Bond Company, LLC (Bond Company), as of March 31, 2003. Amounts are expressed in thousands.

YEAR	CENTERPOINT HOUSTON			TRANSITION BONDS	TOTAL
	THIRD-PARTY	AFFILIATE	SUB-TOTAL		
2003.....	\$ --	\$ 16,600	\$ 16,600	\$12,357	\$ 28,957
2004.....	--	--	--	41,189	41,189
2005.....	\$1,310,000	--	1,310,000	46,806	1,356,806
2006.....	--	--	--	54,295	54,295
2007.....	--	--	--	59,912	59,912
2008.....	--	--	--	65,529	65,529
2009.....	--	--	--	73,018	73,018
2010.....	--	--	--	80,506	80,506
2011.....	--	--	--	87,995	87,995
2012.....	--	45,570	45,570	99,229	144,799
2013.....	450,000	--	450,000	108,590	558,590
2015.....	--	150,850	150,850	--	150,850
2017.....	--	127,385	127,385	--	127,385
2021.....	102,442	--	102,442	--	102,442
2023.....	200,000	--	200,000	--	200,000
2027.....	--	56,095	56,095	--	56,095
2028.....	--	257,500	257,500	--	257,500
2033.....	312,275	--	312,275	--	312,275
Total	\$2,374,717	\$ 654,000	\$3,028,717	\$729,426	\$3,758,143

First mortgage bonds and general mortgage bonds in aggregate principal amounts of \$302 million and \$762 million, respectively, have been issued directly to third parties. External debt of \$1.3 billion maturing in 2005 is senior and secured by general mortgage bonds. The affiliate debt is senior and unsecured.

We have outstanding approximately \$654 million aggregate principal amount of affiliate notes, which represent borrowings from our parent.

On February 28, 2003, CenterPoint Energy amended its existing \$3.85 billion bank facility. The amendment provides that proceeds from capital stock or indebtedness issued or incurred by us must be applied (subject to a \$200 million basket for CenterPoint Energy Resources Corp. (CERC) and its subsidiaries and another \$250 million basket for borrowings by us and CenterPoint Energy's other subsidiaries and other limited exceptions) to repay bank loans and reduce the bank facility. Cash proceeds from issuances of indebtedness to refinance indebtedness existing on October 10, 2002 are not subject to this limitation.

We have outstanding approximately \$699 million aggregate principal amount of first mortgage bonds and approximately \$2.6 billion aggregate principal amount of general mortgage bonds, of which approximately \$924 million combined aggregate principal amount of first mortgage bonds and general mortgage bonds collateralizes debt of CenterPoint Energy. The lien of the general mortgage indenture is junior to that of the Mortgage, pursuant to which the first mortgage bonds are issued. The aggregate amount of additional general mortgage bonds and first mortgage bonds that could be issued is approximately \$600 million based on estimates of the value of property encumbered by the general mortgage, the cost of such property and the 70% bonding ratio contained in the general mortgage. As a result of contractual limitations expiring in November 2005, the aggregate amount of first mortgage bonds and general mortgage bonds cannot currently be increased.

The following table shows the maturity dates of the \$924 million of first mortgage bonds and general mortgage bonds that we have issued as collateral for long-term debt of CenterPoint Energy. These bonds are not reflected on the financial statements of CenterPoint Houston because of the contingent nature of the obligations. Amounts are expressed in thousands.

YEAR	FIRST MORTGAGE BONDS	GENERAL MORTGAGE BONDS	TOTAL
2003.....	\$ 16,600	\$ --	\$ 16,600
2011.....	--	19,200	19,200
2012.....	45,570	--	45,570
2015.....	150,850	--	150,850
2017.....	127,385	--	127,385
2018.....	--	50,000	50,000
2019.....	--	200,000	200,000
2020.....	--	90,000	90,000
2026.....	--	100,000	100,000
2027.....	56,095	--	56,095
2028.....	--	68,000	68,000
Total	\$ 396,500	\$ 527,200	\$ 923,700

As of March 31, 2003, outstanding first mortgage bonds and general mortgage bonds aggregated approximately \$3.3 billion as shown in the following table. Amounts are expressed in thousands.

	ISSUED DIRECTLY TO THIRD PARTIES	ISSUED AS COLLATERAL FOR THE COMPANY'S DEBT	ISSUED AS COLLATERAL FOR CENTERPOINT ENERGY'S DEBT	TOTAL
First Mortgage Bonds	\$ 302,442	\$ --	\$396,500	\$ 698,942
General Mortgage Bonds	762,275	1,310,000	527,200	2,599,475
Total	\$1,064,717	\$1,310,000	\$923,700	\$3,298,417

The Bond Company has \$729 million aggregate principal amount of outstanding transition bonds that were issued in 2001 in accordance with the Texas electric restructuring law. Classes of the transition bonds have final maturity dates of September 15, 2007, September 15, 2009, September 15, 2011 and September 15, 2015 and bear interest at rates of 3.84%, 4.76%, 5.16% and 5.63%, respectively. The transition bonds are secured by "transition property," as defined in the Texas electric restructuring law, which includes the irrevocable right to recover, through non-bypassable transition charges payable by retail electric customers, qualified costs provided in the Texas electric restructuring law and a tariff issued by the Texas Utility Commission. The transition bonds are reported as our long-term debt, although the holders of the transition bonds have no recourse to any of our assets or revenues, and our creditors have no recourse to any assets or revenues (including, without limitation, the transition charges) of the transition bond company. We have no payment obligations with respect to the transition bonds except to remit collections of transition charges as set forth in a servicing agreement between us and the Bond Company and in an intercreditor agreement among us, the Bond Company and other parties.

Bank Facilities. As of March 31, 2003, we had no bank facilities available to meet our short-term liquidity needs.

In February 2003, we obtained a \$75 million revolving credit facility that terminated on March 21, 2003, following our March 2003 issuance of general mortgage bonds, which is discussed above. No borrowings were made under this facility.

Money Pool. We participate in a "money pool" through which we and certain of our affiliates can borrow or invest on a short-term basis. Funding needs are aggregated and external borrowing or investing is based on the net cash position. The money pool's net funding requirements are generally met by borrowings of CenterPoint Energy. The terms of the money pool are in accordance with requirements applicable to registered public utility holding companies under the 1935 Act. At March 31, 2003, we had borrowings of \$155 million from the money pool. The money pool may not provide sufficient funds to meet our cash needs.

Capital Requirements. We anticipate capital expenditures of up to \$1.5 billion in the years 2003 through 2007,

including \$48 million expended during the three months ended March 31, 2003. We anticipate capital expenditures to be approximately \$210 million and \$300 million in for the remainder of 2003 and 2004, respectively.

**Contractual Obligations.** Excluding long-term debt discussed above, our contractual obligations to make future payments consist of operating leases of \$5 million each in the years 2003 through 2005 and \$6 million each in the years 2006 and 2007. For a discussion of operating leases, please read Note 10(a) to the CenterPoint Houston 10-K.

**Refunds to Our Customers.** An order issued by the Texas Utility Commission on October 3, 2001 established the transmission and distribution rates that became effective in January 2002. The Texas Utility Commission determined that we had overmitigated our stranded costs by redirecting transmission and distribution depreciation and by accelerating depreciation of generation assets (an amount equal to earnings above a stated overall rate of return on rate base that was used to recover our investment in generation assets) as provided under the 1998 transition plan and the Texas electric restructuring law. In this final order, we are required to reverse the amount of redirected depreciation and accelerated depreciation taken for regulatory purposes as allowed under the transition plan and the Texas electric restructuring law. Per the October 3, 2001 order, we recorded a regulatory liability to reflect the prospective refund of the accelerated depreciation. We began refunding excess mitigation credits with the January 2002 unbundled bills, to be refunded over a seven-year period. The annual refund of excess earnings is approximately \$237 million. Under the Texas electric restructuring law, a final settlement of these stranded costs will occur in 2004.

**Cash Requirements in 2003.** Our liquidity and capital requirements are affected primarily by our results of operations, capital expenditures, debt service requirements, and working capital needs. Our principal cash requirements during the last nine months of 2003 include the following:

- approximately \$210 million of capital expenditures;
- an estimated \$185 million which we are obligated to return to customers as a result of the Texas Utility Commission's finding of over-mitigation of stranded costs;
- dividend payments to CenterPoint Energy; and
- \$17 million of maturing long-term debt to affiliate.

We expect to fund cash requirements with cash from operations, liquidations of short-term investments, short-term borrowings and to the extent permitted by our bank facility, proceeds from debt offerings. We believe that our current liquidity, along with anticipated cash flows from operations and proceeds from possible debt issuances will be sufficient to meet our cash needs. However, disruptions in our ability to access the capital markets on a timely basis could adversely affect our liquidity. Limits on our ability to issue secured debt, as described in this report, may adversely affect our ability to issue debt securities. In addition, the cost of our recent secured debt issuances has been very high. A similar cost with regard to additional issuances could significantly impact our debt service.

Prior to the Restructuring, Reliant Energy obtained an order from the SEC that granted us certain authority with respect to financing, dividends and other matters. The financing authority granted by that order will expire on June 30, 2003, and CenterPoint Energy must obtain a further order from the SEC under the 1935 Act in order for it and its subsidiaries, including us, to engage in financing activities subsequent to that date.

The amount of any debt issuance, whether registered or unregistered, or whether debt is secured or unsecured, is expected to be affected by the market's perception of our creditworthiness, market conditions and factors affecting our industry. Proceeds from the issuance of debt are expected to be used to refinance existing debt, to finance capital expenditures and to permit the payment of dividends.

**Principal Factors Affecting Cash Requirements in 2004 and 2005.** We expect to issue securitization bonds in 2004 or 2005 to monetize and recover the balance of stranded costs relating to previously owned electric generation assets and other qualified costs as determined in the 2004 true-up proceeding. The issuance will be done pursuant to a financing order to be issued by the Texas Utility Commission. As with the debt of our existing transition bond company, payments on these new securitization bonds would also be made out of funds from non-bypassable charges assessed to retail electric customers required to take delivery service from us. The holders of the



securitization bonds would not have recourse to any of our assets or revenues, and our creditors would not have recourse to any assets or revenues of the entity issuing the securitization bonds. All or a portion of the proceeds from the issuance of securitization bonds remaining after repayment of our \$1.3 billion collateralized term loan are expected to be utilized to retire affiliate debt and pay a dividend to our parent.

Impact on Liquidity of a Downgrade in Credit Ratings. As of May 1, 2003, Moody's Investors Service, Inc. (Moody's), Standard & Poor's Ratings Services, a division of The McGraw Hill Companies (S&P) and Fitch, Inc. (Fitch) had assigned the following credit ratings to our senior secured debt:

SECURITY	MOODY'S		S&P		FITCH	
	RATING	OUTLOOK(1)	RATING	OUTLOOK(2)	RATING	OUTLOOK(3)
First Mortgage Bonds.....	Baa2	Stable	BBB	Stable	BBB+	Stable
General Mortgage Bonds...	Baa2	Stable	BBB	Stable	BBB	Stable
Debt secured by General Mortgage Bonds.....	Baa2	Stable	BBB	Stable	BBB	Stable

- (1) A "stable" outlook from Moody's indicates that Moody's does not expect to put the rating on review for an upgrade or downgrade within 18 months from when the outlook was assigned or last affirmed.
- (2) A "stable" outlook from S&P indicates that the rating is not likely to change over the intermediate to longer term.
- (3) A "stable" outlook from Fitch indicates the direction a rating is likely to move over a one-to two-year period.

We cannot assure you that these ratings will remain in effect for any given period of time or that one or more of these ratings will not be lowered or withdrawn entirely by a rating agency. We note that these credit ratings are not recommendations to buy, sell or hold our securities and may be revised or withdrawn at any time by the rating agency. Each rating should be evaluated independently of any other rating. Any future reduction or withdrawal of one or more of our credit ratings could have a material adverse impact on our ability to obtain short- and long-term financing, the cost of such financings and the execution of our commercial strategies. A decline in credit ratings would also increase the interest rate on long-term debt to be issued in the capital markets and would negatively impact our ability to complete capital market transactions.

Cross Defaults. The terms of our debt instruments generally provide that a default on obligations by CenterPoint Energy does not cause a default under our debt instruments. A payment default by us exceeding \$50 million will cause a default under our \$1.3 billion loan maturing in 2005.

Other Factors that Could Affect Cash Requirements. In addition to the above factors, our liquidity and capital resources could be affected by:

- various regulatory actions; and
- the ability of Reliant Resources and its subsidiaries to satisfy their obligations to us as a principal customer and in respect of its indemnity obligation to us.

Capitalization. Factors affecting our capitalization include:

- covenants in our borrowing agreements; and
- limitations imposed on us because our parent company is a registered public utility holding company.

In connection with our parent company's registration as a public utility holding company under the 1935 Act, the SEC has limited the aggregate amount of our external borrowings to \$3.55 billion. Our ability to pay dividends is restricted by the SEC's requirement that common equity as a percentage of total capitalization must be at least 30% after the payment of any dividend. In addition, the order restricts our ability to pay dividends out of capital accounts to the extent current or retained earnings are insufficient for those dividends. Under these restrictions, we are permitted to pay dividends in excess of the respective current or retained earnings in an amount up to \$200 million.

Relationship to CenterPoint Energy. We are a wholly owned subsidiary of CenterPoint Energy. As a result of this relationship, the financial condition and liquidity of our parent company could affect our access to capital, our credit standing and our financial condition.

Asset Sales. Factors affecting our ability to sell assets (including assets of our subsidiaries) or to satisfy our cash requirements include the following:

- the 1935 Act may require us to obtain prior approval of certain assets sales; and
- obligations under existing credit facilities to use certain cash received from asset sales and securities offerings to pay down debt.

Pension Plan. As discussed in Note 8(a) in the CenterPoint Houston 10-K, which is incorporated herein by reference, we participate in CenterPoint Energy's qualified non-contributory pension plan covering substantially all employees. Pension expense for 2003 is estimated to be \$26 million based on an expected return on plan assets of 9.0% and a discount rate of 6.75% as of December 31, 2002. Pension expense for the three months ended March 31, 2003 was \$6 million. Future changes in plan asset returns, assumed discount rates and various other factors related to the pension will impact our future pension expense. We cannot predict with certainty what these factors will be in the future.

#### CRITICAL ACCOUNTING POLICIES

A critical accounting policy is one that is both important to the presentation of our financial condition and results of operations and requires management to make difficult, subjective or complex accounting estimates. An accounting estimate is an approximation made by management of a financial statement element, item or account in the financial statements. Accounting estimates in our historical consolidated financial statements measure the effects of past business transactions or events, or the present status of an asset or liability. The accounting estimates described below require us to make assumptions about matters that are highly uncertain at the time the estimate is made. Additionally, different estimates that we could have used or changes in an accounting estimate that are reasonably likely to occur could have a material impact on the presentation of our financial condition or results of operations. The circumstances that make these judgments difficult, subjective and/or complex have to do with the need to make estimates about the effect of matters that are inherently uncertain. Estimates and assumptions about future events and their effects cannot be predicted with certainty. We base our estimates on historical experience and on various other assumptions that we believe to be reasonable under the circumstances, the results of which form the basis for making judgments. These estimates may change as new events occur, as more experience is acquired, as additional information is obtained and as our operating environment changes. We believe the following accounting policies involve the application of critical accounting estimates.

#### ACCOUNTING FOR RATE REGULATION

SFAS No. 71, "Accounting for the Effects of Certain Types of Regulation" (SFAS No. 71), provides that rate-regulated entities account for and report assets and liabilities consistent with the recovery of those incurred costs in rates if the rates established are designed to recover the costs of providing the regulated service and if the competitive environment makes it probable that such rates can be charged and collected. We apply SFAS No. 71, which results in our accounting for the regulatory effects of recovery of "stranded costs" and other "regulatory assets" resulting from the unbundling of the transmission and distribution business from our electric generation operations in our consolidated financial statements. Certain expenses and revenues subject to utility regulation or rate determination normally reflected in income are deferred on the balance sheet and are recognized in income as the related amounts are included in service rates and recovered from or refunded to customers. Regulatory assets reflected in our Consolidated Balance Sheets aggregated \$4.0 billion and \$4.5 billion as of December 31, 2002 and March 31, 2003, respectively. Additionally, regulatory liabilities reflected in our Consolidated Balance Sheets aggregated \$1.1 billion at both December 31, 2002 and March 31, 2003. Significant accounting estimates embedded within the application of SFAS No. 71 relate to \$2.5 billion of recoverable electric generation plant mitigation assets (stranded costs) and \$829 million of ECOM true-up. The stranded costs are comprised of \$1.1 billion of previously recorded accelerated depreciation and \$841 million of previously redirected depreciation as well as \$396 million associated with CenterPoint Energy's distribution of approximately 19% of the 80 million outstanding shares of common stock of Texas Genco to their shareholders on January 6, 2003. These stranded costs are recoverable under the provisions of the Texas electric restructuring law. The ultimate

amount of stranded cost recovery is subject to a final determination, which will occur in 2004 and is contingent upon the market value of Texas Genco. Any significant changes in our accounting estimate of stranded costs as a result of current market conditions or changes in the regulatory recovery mechanism currently in place could result in a material write-down of all or a portion of these regulatory assets. Regulatory assets related to ECOM true-up represent the regulatory assets associated with costs incurred as a result of mandated capacity auctions conducted beginning in 2002 by Texas Genco being consummated at market-based prices that have been substantially below the estimate of those prices made by the Texas Utility Commission in the spring of 2001. Any significant changes in our estimate of our regulatory asset associated with ECOM true-up could have a significant effect on our financial condition and results of operations. Additionally, any significant changes in our estimated stranded costs or ECOM true-up recovery could significantly affect our liquidity subsequent to the final true-up proceedings conducted by the Texas Utility Commission which are expected to conclude in late 2004.

#### IMPAIRMENT OF LONG-LIVED ASSETS

Long-lived assets recorded in our Consolidated Balance Sheets primarily consist of property, plant and equipment (PP&E). Net PP&E comprises \$3.8 billion or 42% of our total assets as of March 31, 2003. We make judgments and estimates in conjunction with the carrying value of these assets, including amounts to be capitalized, depreciation and amortization methods and useful lives. We evaluate our PP&E for impairment whenever indicators of impairment exist. During 2003, no such indicators of impairment existed. Accounting standards require that if the sum of the undiscounted expected future cash flows from a company's asset is less than the carrying value of the asset, an asset impairment must be recognized in the financial statements. The amount of impairment recognized is calculated by subtracting the fair value of the asset from the carrying value of the asset.

#### UNBILLED REVENUES

Revenues related to the sale and/or delivery of electricity are generally recorded when electricity is delivered to customers. However, the determination of deliveries to individual customers is based on the reading of their meters, which is performed on a systematic basis throughout the month. At the end of each month, amounts of electricity delivered to customers since the date of the last meter reading are estimated and the corresponding unbilled revenue is estimated. Unbilled electric delivery revenue is estimated each month based on daily supply volumes, applicable rates and analyses reflecting significant historical trends and experience. Accrued unbilled revenues recorded in the Consolidated Balance Sheets as of December 31, 2002 and March 31, 2003 were \$70 million and \$61 million, respectively.

#### NEW ACCOUNTING PRONOUNCEMENTS

Effective January 1, 2003, we adopted SFAS No. 143, "Accounting for Asset Retirement Obligations" (SFAS No. 143). SFAS No. 143 requires the fair value of an asset retirement obligation to be recognized as a liability is incurred and capitalized as part of the cost of the related tangible long-lived asset. Over time, the liability is accreted to its present value each period, and the capitalized cost is depreciated over the useful life of the related asset. Retirement obligations associated with long-lived assets included within the scope of SFAS No. 143 are those for which a legal obligation exists under enacted laws, statutes and written or oral contracts, including obligations arising under the doctrine of promissory estoppel.

We have not identified any asset retirement obligations; however, we have previously recognized removal costs as a component of depreciation expense in accordance with regulatory treatment. As of March 31, 2003, these previously recognized removal costs of \$254 million do not represent SFAS No. 143 asset retirement obligations, but rather embedded regulatory liabilities.

In April 2002, the Financial Accounting Standards Board (FASB) issued SFAS No. 145, "Rescission of FASB Statements No. 4, 44, and 64, Amendment of FASB Statement No. 13, and Technical Corrections" (SFAS No. 145). SFAS No. 145 eliminates the current requirement that gains and losses on debt extinguishment must be classified as extraordinary items in the income statement. Instead, such gains and losses will be classified as extraordinary items only if they are deemed to be unusual and infrequent. SFAS No. 145 also requires that capital leases that are modified so that the resulting lease agreement is classified as an operating lease be accounted for as a sale-leaseback transaction. The changes related to debt extinguishment are effective for fiscal years beginning after May 15, 2002, and the changes related to lease accounting are effective for transactions occurring after May 15, 2002. We have

applied this guidance prospectively as it relates to lease accounting and will apply the accounting provision related to debt extinguishment. Upon adoption of SFAS No. 145, any gain or loss on extinguishment of debt that was classified as an extraordinary item in prior periods presented that does not meet the criteria in APB Opinion No. 30 for classification as an extraordinary item in prior periods will be reclassified. No such reclassification was required for the three-month period ended March 31, 2002. We have reclassified the \$25 million loss on debt extinguishment related to the fourth quarter of 2002 from extraordinary item to interest expense.

In June 2002, the FASB issued SFAS No. 146, "Accounting for Costs Associated with Exit or Disposal Activities" (SFAS No. 146). SFAS No. 146 nullifies EITF Issue No. 94-3, "Liability Recognition for Certain Employee Termination Benefits and Other Costs to Exit an Activity (including Certain Costs Incurred in a Restructuring)" (EITF No. 94-3). The principal difference between SFAS No. 146 and EITF No. 94-3 relates to the requirements for recognition of a liability for costs associated with an exit or disposal activity. SFAS No. 146 requires that a liability be recognized for a cost associated with an exit or disposal activity when it is incurred. A liability is incurred when a transaction or event occurs that leaves an entity little or no discretion to avoid the future transfer or use of assets to settle the liability. Under EITF No. 94-3, a liability for an exit cost was recognized at the date of an entity's commitment to an exit plan. In addition, SFAS No. 146 also requires that a liability for a cost associated with an exit or disposal activity be recognized at its fair value when it is incurred. SFAS No. 146 is effective for exit or disposal activities that are initiated after December 31, 2002 with early application encouraged. We will apply the provisions of SFAS No. 146 to all exit or disposal activities initiated after December 31, 2002.

In November 2002, the FASB issued FASB Interpretation No. (FIN) 45, "Guarantor's Accounting and Disclosure Requirements for Guarantees, Including Indirect Guarantees of Indebtedness of Others" (FIN 45). FIN 45 requires that a liability be recorded in the guarantor's balance sheet upon issuance of certain guarantees. In addition, FIN 45 requires disclosures about the guarantees that an entity has issued. The provision for initial recognition and measurement of the liability will be applied on a prospective basis to guarantees issued or modified after December 31, 2002. The disclosure provisions of FIN 45 are effective for financial statements of interim or annual periods ending after December 15, 2002. The adoption of FIN 45 did not materially affect our consolidated financial statements.

#### ITEM 4. CONTROLS AND PROCEDURES

Within the 90 days prior to the date of this report, we carried out an evaluation, under the supervision and with the participation of our management, including our Chief Executive Officer and Chief Financial Officer, of the effectiveness of the design and operation of our disclosure controls and procedures pursuant to Rule 13a-14 of the Securities Exchange Act of 1934. Based on that evaluation, the Chief Executive Officer and the Chief Financial Officer concluded that our disclosure controls and procedures are effective in timely alerting them to material information relating to us (including our consolidated subsidiaries) required to be included in our periodic SEC filings. Subsequent to the date of their evaluation, there were no significant changes in our internal controls or in other factors that could significantly affect the internal controls, including any corrective actions with regard to significant deficiencies and material weaknesses.

PART II. OTHER INFORMATION

ITEM 1. LEGAL PROCEEDINGS.

For a description of certain legal and regulatory proceedings affecting us, please review Note 9 to our Interim Financial Statements, Item 3 of the CenterPoint Houston Form 10-K and Note 10(b) to the CenterPoint Houston 10-K Notes, all of which are incorporated herein by reference.

ITEM 5. OTHER INFORMATION.

Forward-Looking Statements. From time to time, we make statements concerning our expectations, beliefs, plans, objectives, goals, strategies, future events or performance and underlying assumptions and other statements that are not historical facts. These statements are "forward-looking statements" within the meaning of the Private Securities Litigation Reform Act of 1995. Actual results may differ materially from those expressed or implied by these statements. You can generally identify the forward-looking statements by the words "anticipate," "believe," "continue," "could," "estimate," "expect," "forecast," "goal," "intend," "may," "objective," "plan," "potential," "predict," "projection," "should," or other similar words.

We have based our forward-looking statements on our management's beliefs and assumptions based on information available to our management at the time the statements are made. We caution you that assumptions, beliefs, expectations, intentions and projections about future events may and often do vary materially from actual results. Therefore, we cannot assure you that actual results will not differ materially from those expressed or implied by our forward-looking statements.

The following list identifies some of the factors that could cause actual results to differ materially from those expressed or implied in forward-looking statements:

- state and federal legislative and regulatory actions or developments, including deregulation, re-regulation and restructuring of the electric utility industry, constraints placed on our activities or business by the Public Utility Holding Company Act of 1935, changes in or application of laws or regulations applicable to other aspects of our business and actions with respect to:
  - approval of stranded costs;
  - allowed rates of return;
  - rate structures;
  - recovery of investments; and
  - operation and construction of facilities;
- non-payment for our services due to financial distress of our customers, including our largest customer, Reliant Resources;
- the successful and timely completion of our capital projects;
- industrial, commercial and residential growth in our service territory and changes in market demand and demographic patterns;
- changes in business strategy or development plans;
- changes in interest rates or rates of inflation;
- unanticipated changes in operating expenses and capital expenditures;
- weather variations and other natural phenomena, which can affect the demand for power over our transmission and distribution system;
- commercial bank and financial market conditions, our access to capital, the cost of such capital, receipt of certain approvals under the 1935 Act, and the results of our financing

and refinancing efforts, including availability of funds in the debt capital markets;

- actions by rating agencies;
- legal and administrative proceedings and settlements;
- changes in tax laws;
- inability of various counterparties to meet their obligations with respect to our financial instruments;
- any lack of effectiveness of our disclosure controls and procedures;
- changes in technology;
- significant changes in our relationship with our employees, including the availability of qualified personnel and the potential adverse effects if labor disputes or grievances were to occur;
- significant changes in accounting policies;
- acts of terrorism or war, including any direct or indirect effect on our business resulting from terrorist attacks such as occurred on September 11, 2001 or any similar incidents or responses to those incidents;
- the availability and price of insurance;
- the outcome of the pending securities lawsuits against Reliant Energy and Reliant Resources;
- the outcome of the SEC investigation relating to the treatment in our consolidated financial statements of certain activities of Reliant Resources;
- the ability of Reliant Resources to satisfy its indemnity obligations to us;
- the reliability of the systems, procedures and other infrastructure necessary to operate the retail electric business in our service territory, including the systems owned and operated by the independent system operator of the market served by the independent system operator in the market served by the Electric Reliability Council of Texas, Inc.;
- political, legal, regulatory and economic conditions and developments in the United States; and
- other factors we discuss in the CenterPoint Houston Form 10-K, including those outlined in Item 1 under "Risk Factors."

You should not place undue reliance on forward-looking statements. Each forward-looking statement speaks only as of the date of the particular statement, and we undertake no obligation to publicly update or revise any forward-looking statements.

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

(a) Exhibits.

Exhibits not incorporated by reference to a prior filing are designated by a cross (+); all exhibits not so designated are incorporated by reference to a prior filing of CenterPoint Energy Houston Electric, LLC or CenterPoint Energy, Inc. as indicated.

Exhibit Number	Description	Report or Registration Statement	SEC File or Registration Number	Exhibit References
3.1	Articles of Conversion of REI	Form 8-K dated August 31, 2002 filed with the SEC on September 3, 2002	1-3187	3(a)
3.2	Articles of Organization of CenterPoint Energy Houston Electric, LLC	Form 8-K dated August 31, 2002 filed with the SEC on September 3, 2002	1-3187	3(b)
3.3	Limited Liability Company Regulations of CenterPoint Energy Houston Electric, LLC	Form 8-K dated August 31, 2002 filed with the SEC on September 3, 2002	1-3187	3(c)
4.1	Tenth Supplemental Indenture to Exhibit 4(e)(1), dated as of March 18, 2003	CenterPoint Houston's Form 8-K dated March 13, 2003	1-31447	4.1
4.2	Officer's Certificate dated March 18, 2003 setting forth the form, terms and provisions of the Tenth Series and Eleventh Series of general mortgage bonds	CenterPoint Houston's Form 8-K dated March 13, 2003	1-31447	4.2
+99.1	Section 906 Certification of David M. McClanahan			
+99.2	Section 906 Certification of Gary L. Whitlock			
+99.3	Items incorporated by reference from the CenterPoint Houston Form 10-K. Item 1 "Business--Risk Factors," Item 3 "Legal Proceedings" and Item 7 "Management's Narrative Analysis of Results of Operations --Certain Factors Affecting Future Earnings" and Notes 3(e) (Regulatory Assets and Liabilities), 4 (Regulatory Matters), 8(a) (Pension Plans) and 10 (Commitments and Contingencies).			

(b) Reports on Form 8-K.

On March 27, 2003, we filed a Current Report on Form 8-K dated March 13, 2003, announcing the pricing and closing of \$762.275 million of general mortgage bonds in a private placement with institutions pursuant to Rule 144A under the Securities Act of 1933, as amended.



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.

CENTERPOINT ENERGY HOUSTON ELECTRIC, LLC

By: /s/ James S. Brian

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James S. Brian  
Senior Vice President and  
Chief Accounting Officer

Date: May 14, 2003

CERTIFICATIONS

I, David M. McClanahan, certify that:

1. I have reviewed this quarterly report on Form 10-Q of CenterPoint Energy Houston Electric, LLC;
2. Based on my knowledge, this quarterly report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this quarterly report;
3. Based on my knowledge, the financial statements, and other financial information included in this quarterly report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this quarterly report;
4. The registrant's other certifying officers and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-14 and 15d-14) for the registrant and we have:
  - a) designed such disclosure controls and procedures to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this quarterly report is being prepared;
  - b) evaluated the effectiveness of the registrant's disclosure controls and procedures as of a date within 90 days prior to the filing date of this quarterly report (the "Evaluation Date"); and
  - c) presented in this quarterly report our conclusions about the effectiveness of the disclosure controls and procedures based on our evaluation as of the Evaluation Date;
5. The registrant's other certifying officers and I have disclosed, based on our most recent evaluation, to the registrant's auditors and the audit committee of registrant's board of directors (or persons performing the equivalent function):
  - a) all significant deficiencies in the design or operation of internal controls which could adversely affect the registrant's ability to record, process, summarize and report financial data and have identified for the registrant's auditors any material weaknesses in internal controls; and
  - b) any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal controls; and
6. The registrant's other certifying officers and I have indicated in this quarterly report whether or not there were significant changes in internal controls or in other factors that could significantly affect internal controls subsequent to the date of our most recent evaluation, including any corrective actions with regard to significant deficiencies and material weaknesses.

Date: May 14, 2003

By /s/ David M. McClanahan

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David M. McClanahan  
Chairman and Principal Executive Officer

I, Gary L. Whitlock, certify that:

1. I have reviewed this quarterly report on Form 10-Q of CenterPoint Energy Houston Electric, LLC;
2. Based on my knowledge, this quarterly report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this quarterly report;
3. Based on my knowledge, the financial statements, and other financial information included in this quarterly report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this quarterly report;
4. The registrant's other certifying officers and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-14 and 15d-14) for the registrant and we have:
  - a) designed such disclosure controls and procedures to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this quarterly report is being prepared;
  - b) evaluated the effectiveness of the registrant's disclosure controls and procedures as of a date within 90 days prior to the filing date of this quarterly report (the "Evaluation Date"); and
  - c) presented in this quarterly report our conclusions about the effectiveness of the disclosure controls and procedures based on our evaluation as of the Evaluation Date;
5. The registrant's other certifying officers and I have disclosed, based on our most recent evaluation, to the registrant's auditors and the audit committee of registrant's board of directors (or persons performing the equivalent function):
  - a) all significant deficiencies in the design or operation of internal controls which could adversely affect the registrant's ability to record, process, summarize and report financial data and have identified for the registrant's auditors any material weaknesses in internal controls; and
  - b) any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal controls; and
6. The registrant's other certifying officers and I have indicated in this quarterly report whether or not there were significant changes in internal controls or in other factors that could significantly affect internal controls subsequent to the date of our most recent evaluation, including any corrective actions with regard to significant deficiencies and material weaknesses.

Date: May 14, 2003

By /s/ Gary L. Whitlock

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Gary L. Whitlock  
Executive Vice President and Chief Financial Officer

EXHIBIT INDEX

Exhibits not incorporated by reference to a prior filing are designated by a cross (+); all exhibits not so designated are incorporated by reference to a prior filing of CenterPoint Energy Houston Electric, LLC or CenterPoint Energy, Inc. as indicated.

Exhibit Number	Description	Report or Registration Statement	SEC File or Registration Number	Exhibit References
3.1	Articles of Conversion of REI	Form 8-K dated August 31, 2002 filed with the SEC on September 3, 2002	1-3187	3(a)
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CERTIFICATION PURSUANT TO  
SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002  
(SUBSECTIONS (a) AND (b) OF SECTION 1350, CHAPTER 63 OF TITLE 18,  
UNITED STATES CODE)

Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 (Subsections (a) and (b) of Section 1350, Chapter 63 of Title 18, United States Code) (the "Act"), I, David M. McClanahan, Manager (Principal Executive Officer) of CenterPoint Energy Houston Electric, LLC (the "Company"), hereby certify, to the best of my knowledge:

- (1) The Company's Quarterly Report on Form 10-Q for the quarter ended March 31, 2003 (the "Report"), fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934; and
- (2) The information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

Dated: May 14, 2003

/s/ DAVID M. McCLANAHAN

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David M. McClanahan  
Manager (Principal Executive Officer)

A signed original of this written statement required by Section 906 has been provided to the Company and will be retained by the Company and furnished to the Securities and Exchange Commission or its staff upon request.

The foregoing certification is being furnished solely pursuant to Section 906 of the Act and is not being filed as part of the Report or as a separate disclosure document.

CERTIFICATION PURSUANT TO  
SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002  
(SUBSECTIONS (a) AND (b) OF SECTION 1350, CHAPTER 63 OF TITLE 18,  
UNITED STATES CODE)

Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 (Subsections (a) and (b) of Section 1350, Chapter 63 of Title 18, United States Code) (the "Act"), I, Gary L. Whitlock, Executive Vice President and Chief Financial Officer of CenterPoint Energy Houston Electric, LLC (the "Company"), hereby certify, to the best of my knowledge:

- (1) The Company's Quarterly Report on Form 10-Q for the quarter ended March 31, 2003 (the "Report"), fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934; and
- (2) The information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

Dated: May 14, 2003

/s/ GARY L. WHITLOCK

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Gary L. Whitlock  
Executive Vice President and  
Chief Financial Officer

A signed original of this written statement required by Section 906 has been provided to the Company and will be retained by the Company and furnished to the Securities and Exchange Commission or its staff upon request.

The foregoing certification is being furnished solely pursuant to Section 906 of the Act and is not being filed as part of the Report or as a separate disclosure document.

## ITEM 1. BUSINESS

## RISK FACTORS

## RISK FACTORS ASSOCIATED WITH FINANCIAL CONDITION AND OTHER RISKS

IF WE ARE UNABLE TO ARRANGE FUTURE FINANCINGS ON ACCEPTABLE TERMS, OUR ABILITY TO FUND FUTURE CAPITAL EXPENDITURES AND REFINANCE EXISTING INDEBTEDNESS COULD BE LIMITED.

As a result of events occurring in 2001 and 2002, including the September 11, 2001 terrorist attacks, the bankruptcy of Enron Corp., the downgrading of our credit ratings and the credit ratings of several energy companies, the general downturn in the utility industry and the unusual volatility in the U.S. financial markets, the availability and cost of capital for our business have been adversely affected. If we are unable to obtain external financing to meet our future capital requirements on terms that are acceptable to us, our financial condition and future results of operations could be materially adversely affected. As of December 31, 2002, we had \$3.7 billion of outstanding indebtedness, including a \$1.3 billion collateralized term loan that will expire in 2005. In addition, the capital constraints currently impacting our business may require our future indebtedness to include terms that are more restrictive or burdensome than those of our current indebtedness. These terms may negatively impact our ability to operate our business. The success of our future financing efforts may depend, at least in part, on:

- general economic and capital market conditions;
- credit availability from financial institutions and other lenders;
- investor confidence in us and the market in which we operate;
- maintenance of acceptable credit ratings by us and by CenterPoint Energy;
- market expectations regarding our future earnings and probable cash flows;
- market perceptions of our ability to access capital markets on reasonable terms;
- our exposure to Reliant Resources as our customer and in connection with its indemnification obligations arising in connection with its separation from CenterPoint Energy;
- provisions of relevant tax and securities laws; and
- our ability to obtain approval of specific financing transactions under the 1935 Act.

As of December 31, 2002, we had \$1.8 billion of general mortgage bonds outstanding. We may issue additional general mortgage bonds on the basis of retired bonds, 70% of property additions or cash deposited with the trustee. Although approximately \$900 million of additional general mortgage bonds could be issued on the basis of property additions as of December 31, 2002, we have agreed contractually to limit incremental secured debt to \$300 million. In addition, we are contractually prohibited, subject to certain exceptions, from issuing additional first mortgage bonds.

Our current credit ratings are discussed in "Management's Narrative Analysis of Results of Operations -- Liquidity -- Impact on Liquidity of a Downgrade in Credit Ratings" in Item 7 of this report. We cannot assure you that these credit ratings will remain in effect for any given period of time or that one or more of these ratings will not be lowered or withdrawn entirely by a rating agency. We note that these credit ratings are not recommendations to buy, sell or hold our securities. Each rating should be evaluated independently of any other rating. Any future reduction or withdrawal of one or more of our credit ratings could have a material adverse impact on our ability to access capital on acceptable terms.

THE FINANCIAL CONDITION AND LIQUIDITY OF OUR PARENT COMPANY COULD AFFECT OUR ACCESS TO CAPITAL, OUR CREDIT STANDING AND OUR FINANCIAL CONDITION.

Our ratings and credit may be impacted by CenterPoint Energy's credit standing. CenterPoint Energy and its subsidiaries other than us have approximately \$1.0 billion of debt that must be refinanced in 2003. We cannot assure you that CenterPoint Energy and its other subsidiaries will be able to pay or refinance these

amounts. If CenterPoint Energy were to experience a deterioration in its credit standing or liquidity difficulties, our access to credit and our ratings could be adversely affected and the repayment of \$815 million demand notes receivable from CenterPoint Energy could be adversely affected.

WE ARE A WHOLLY OWNED SUBSIDIARY OF CENTERPOINT ENERGY. CENTERPOINT ENERGY CAN EXERCISE SUBSTANTIAL CONTROL OVER OUR DIVIDEND POLICY AND BUSINESS AND OPERATIONS AND COULD DO SO IN A MANNER THAT IS ADVERSE TO OUR INTERESTS.

We are managed by officers and employees of CenterPoint Energy. Our management will make determinations with respect to the following:

- our payment of dividends;
- decisions on our financings and our capital raising activities;
- mergers or other business combinations; and
- our acquisition or disposition of assets.

There are no contractual restrictions on our ability to pay dividends to CenterPoint Energy. Our management could decide to increase our dividends to CenterPoint Energy to support its cash needs. This could adversely affect our liquidity. Under the 1935 Act, our ability to pay dividends is restricted by the SEC's requirement that common equity as a percentage of total capitalization must be at least 30% after the payment of any dividend. In addition, the order restricts our ability to pay dividends out of capital accounts to the extent current or retained earnings are insufficient for those dividends. Under these restrictions, we are permitted to pay dividends in excess of the respective current or retained earnings in an amount up to \$200 million.

AN INCREASE IN SHORT-TERM INTEREST RATES COULD ADVERSELY AFFECT OUR CASH FLOWS.

As of December 31, 2002, we had \$1.3 billion of outstanding floating-rate debt. Because of capital constraints impacting our business at the time this floating-rate debt was entered into, the interest rates are substantially above our historical borrowing rates. In addition, any floating-rate debt issued by us in the future could be at interest rates substantially above our historical borrowing rates. While we may seek to use interest rate swaps in order to hedge portions of our floating-rate debt, we may not be successful in obtaining hedges on acceptable terms. Any increase in short-term interest rates would result in higher interest costs and could adversely affect our results of operations, financial condition and cash flows.

OUR REVENUES AND RESULTS OF OPERATIONS ARE SUBJECT TO RISKS THAT ARE BEYOND OUR CONTROL, INCLUDING BUT NOT LIMITED TO FUTURE TERRORIST ATTACKS OR RELATED ACTS OF WAR.

The cost of repairing damage to our facilities due to storms, natural disasters, wars, terrorist acts and other catastrophic events, in excess of reserves established for such repairs, may adversely impact our results of operations, financial condition and cash flows. The occurrence or risk of occurrence of future terrorist activity may impact our results of operations, financial condition and cash flows in unpredictable ways. These actions could also result in adverse changes in the insurance markets and disruptions of power and fuel markets. In addition, our transmission and distribution facilities could be directly or indirectly harmed by future terrorist activity. The occurrence or risk of occurrence of future terrorist attacks or related acts of war could also adversely affect the United States economy. A lower level of economic activity could result in a decline in energy consumption, which could adversely affect our revenues and margins and limit our future growth prospects. Also, these risks could cause instability in the financial markets and adversely affect our ability to access capital.



WE COULD INCUR LIABILITIES ASSOCIATED WITH BUSINESS AND ASSETS WE HAVE TRANSFERRED TO OTHERS.

Under some circumstances, we could incur liabilities associated with assets and businesses we no longer own. These assets and businesses include:

- those transferred to Reliant Resources or its subsidiaries in connection with the organization and capitalization of Reliant Resources prior to its initial public offering in 2001;
- those transferred to Texas Genco in connection with its organization and capitalization; and
- those transferred to CenterPoint Energy in connection with the Restructuring.

In connection with the organization and capitalization of Reliant Resources, Reliant Resources and its subsidiaries assumed liabilities associated with various assets and businesses Reliant Energy transferred to them. Reliant Resources also agreed to indemnify, and cause the applicable transferee subsidiaries to indemnify, CenterPoint Energy and its subsidiaries, including us, with respect to liabilities associated with the transferred assets and businesses. The indemnity provisions were intended to place sole financial responsibility on Reliant Resources and its subsidiaries for all liabilities associated with the current and historical businesses and operations of Reliant Resources, regardless of the time those liabilities arose. If Reliant Resources is unable to satisfy a liability that has been so assumed in circumstances in which Reliant Energy has not been released from the liability in connection with the transfer, we, as successor to Reliant Energy, could be responsible for satisfying the liability.

Reliant Resources has reported that it is facing large maturities of its debt over the next year. If Reliant Resources is unable to meet its obligations, it would need to consider, among various options, restructuring under the bankruptcy laws, in which event Reliant Resources might not honor its indemnification obligations and claims by Reliant Resources' creditors might be made against us as its former owner.

As described in Note 10(b) to our consolidated financial statements, Reliant Energy and Reliant Resources are named as defendants in a number of lawsuits arising out of power sales in California and other West Coast markets and financial reporting matters. Although these matters relate to the business and operations of Reliant Resources, claims against Reliant Energy have been made on grounds that include the effect of Reliant Resources' financial results on Reliant Energy's historical financial statements and liability of Reliant Energy as a controlling shareholder of Reliant Resources. As Reliant Energy's successor, we could incur liability if claims in one or more of these lawsuits were successfully asserted against us and indemnification from Reliant Resources were determined to be unavailable or if Reliant Resources were unable to satisfy indemnification obligations owed to us with respect to those claims.

In connection with the organization and capitalization of Texas Genco, Texas Genco and its subsidiaries assumed liabilities associated with the electric generation assets Reliant Energy transferred to it. Texas Genco also agreed to indemnify, and cause the applicable transferee subsidiaries to indemnify, CenterPoint Energy and its subsidiaries, including us, with respect to liabilities associated with the transferred assets and businesses. In many cases the liabilities assumed were held by us and we were not released by third parties from these liabilities. The indemnity provisions were intended to place sole financial responsibility on Texas Genco and its subsidiaries for all liabilities associated with the current and historical businesses and operations of Texas Genco, regardless of the time those liabilities arose. If Texas Genco were unable to satisfy a liability that had been so assumed or indemnified against, and provided Reliant Energy had not been released from the liability in connection with the transfer, we could be responsible for satisfying the liability.

OUR HISTORICAL FINANCIAL RESULTS AS THE UNINCORPORATED ELECTRIC TRANSMISSION AND DISTRIBUTION DIVISION OF RELIANT ENERGY ARE NOT REPRESENTATIVE OF OUR EXPECTED FUTURE RESULTS AS CENTERPOINT HOUSTON.

We have limited experience operating as a transmission and distribution utility in a deregulated electricity market in which we are subject to rate regulation, although our transmission and distribution business had a significant operating history at the time of the Restructuring of Reliant Energy, this business was operated until January 1, 2002 as part of a vertically integrated utility company. Our historical costs and expenses reflect charges from Reliant Energy for centralized corporate services and infrastructure costs. These

allocations have been determined based on what we and Reliant Energy considered to be reasonable reflections of the utilization of services provided to us or for the benefits received by us. We may experience significant changes in our cost structure, funding and operations as a result of the restructuring of Reliant Energy, including increased costs associated with reduced economies of scale. In addition, since January 1, 2002, we have transmitted and distributed electricity at rates regulated by the Texas Utility Commission. Therefore, the historical financial information presented in or incorporated by reference into this report prior to January 1, 2002 is not indicative of our future performance and does not reflect what our results of operations, financial position, and cash flows would have been had we operated as a separate stand-alone, rate-regulated transmission and distribution utility in a deregulated market during the periods presented.

IF CENTERPOINT ENERGY IS UNABLE TO OBTAIN AN EXTENSION OF ITS FINANCING ORDER UNDER THE 1935 ACT, WE WILL NOT BE ABLE TO ENGAGE IN FINANCING TRANSACTIONS AFTER JUNE 30, 2003.

In connection with CenterPoint Energy's registration as a public utility holding company under the 1935 Act, the SEC issued a financing order which authorizes us to enter into a wide range of financing transactions. This financing order expires on June 30, 2003. If CenterPoint Energy is unable to obtain an extension of the financing order, we would generally be unable to engage in any financing transactions, including the refinancing of existing obligations after June 30, 2003.

#### RISK FACTORS ASSOCIATED WITH OUR BUSINESS

WE MAY NOT BE SUCCESSFUL IN RECOVERING THE FULL VALUE OF OUR STRANDED COSTS AND REGULATORY ASSETS RELATED TO GENERATION.

We are entitled to recover our stranded costs (the excess of regulatory net book value of generation assets, as defined by the Texas electric restructuring law, over the market value of those assets) and our regulatory assets related to generation. We expect to make a filing in January 2004 in a true-up proceeding provided for by the Texas electric restructuring law. The purpose of this proceeding will be to quantify and reconcile:

- the amount of stranded costs;
- differences in the prices achieved in the auctions of Texas Genco's generation capacity mandated by the Texas electric restructuring law and Texas Utility Commission estimates (ECOM true-up);
- fuel over- or under-recovery;
- the "price to beat" clawback; and
- other regulatory assets associated with CenterPoint Energy's former generation business that were not previously recovered through the issuance of securitization bonds by a subsidiary.

We will be required to establish and support the amounts of these costs in order to recover them. We expect these costs to be substantial. We cannot assure you that we will be able to successfully establish and support our estimates of the amount of these costs. For more information about the true-up proceeding, please read "-- Electric Transmission and Distribution -- Stranded Costs and Regulatory Assets Recovery" above and Note 4 to our consolidated financial statements.

In addition, our \$1.3 billion collateralized term loan matures on November 11, 2005 and is expected to be repaid or refinanced with the proceeds from the recovery of these costs. To the extent we have not received the proceeds by November 11, 2005, our ability to repay or refinance our \$1.3 billion term loan will be adversely affected.

OUR RECEIVABLES ARE CONCENTRATED IN A SMALL NUMBER OF RETAIL ELECTRIC PROVIDERS.

Our receivables from the distribution of electricity are collected from retail electric providers that supply the electricity we distribute to their customers. Currently, we do business with approximately 31 retail electric providers. Adverse economic conditions, structural problems in the new ERCOT market or financial

difficulties of one or more retail electric providers could impair the ability of these retail providers to pay for our services or could cause them to delay such payments. We depend on these retail electric providers to remit payments timely to us. Any delay or default in payment could adversely affect our cash flows, financial condition and results of operations. Our receivables balance from retail electric providers at December 31, 2002 was \$85 million. Approximately 72% of our receivables from retail electric providers at December 31, 2002, was owed by subsidiaries of Reliant Resources. Our financial condition may be adversely affected if Reliant Resources is unable to meet its obligations to us.

Reliant Resources, through its subsidiaries, is our largest customer. Pursuant to the Texas electric restructuring law, Reliant Resources may be obligated to make a large "price to beat" clawback payment to us in 2004. We expect the clawback, if any, to be applied against any stranded cost recovery to which we are entitled or, if no stranded costs are recoverable, to be refunded to retail electric providers. Also, as discussed in "Risk Factors Associated with Financial Condition and Other Risks -- We could incur liabilities associated with business and assets we have transferred to others," Reliant Resources is obligated to indemnify us for other potential liabilities. Reliant Resources has reported that it is facing large maturities of its debt over the next year and thus its ability to satisfy its obligations to us cannot be assured.

#### RATE REGULATION OF OUR BUSINESS MAY DELAY OR DENY OUR FULL RECOVERY OF OUR COSTS.

Our rates are regulated by certain municipalities and the Texas Utility Commission based on an analysis of our invested capital and expenses incurred in a test year. Thus, the rates we are allowed to charge may not match our expenses at any given time. While rate regulation in Texas is premised on providing a reasonable opportunity to recover reasonable and necessary operating expenses and to earn a reasonable return on invested capital, there can be no assurance that the Texas Utility Commission will judge all of our costs to be reasonable or necessary or that the regulatory process in which rates are determined will always result in rates that will produce full recovery of our costs.

#### WE ARE OPERATING IN A RELATIVELY NEW MARKET ENVIRONMENT IN WHICH WE AND OTHERS HAVE LITTLE OPERATING EXPERIENCE.

The competitive electric market in Texas became fully operational in January 2002. Neither we nor any of the Texas Utility Commission, ERCOT or other market participants has any significant operating history under the market framework created by the Texas electric restructuring law. Some operational difficulties were encountered in the pilot program conducted in 2001 and continue to be experienced now. These difficulties include delays in the switching of some customers from one retail electric provider to another. These difficulties create uncertainty as to the amount of transmission and distribution charges owed by each retail electric provider, which may cause payment of those amounts to be delayed. While to date these difficulties have not been material, these operating difficulties could become material or structural changes adopted to address these difficulties could materially adversely affect our results of operations, financial condition and cash flows.

#### DISRUPTIONS AT POWER GENERATION FACILITIES OWNED BY THIRD PARTIES COULD INTERRUPT OUR SALES OF TRANSMISSION AND DISTRIBUTION SERVICES.

We depend on power generation facilities owned by third parties to provide retail electric providers with electric power which we transmit and distribute to their customers. We do not own or operate any power generation facilities. If power generation is disrupted or if power generation capacity is inadequate, our services may be interrupted, and our results of operations, financial condition and cash flows may be adversely affected.

#### OUR REVENUES AND RESULTS OF OPERATIONS ARE SEASONAL.

A portion of our revenues is derived from rates that we collect from each retail electric provider based on the amount of electricity we distribute on behalf of each retail electric provider. Thus, our revenues and results of operations are subject to seasonality, weather conditions and other changes in electricity usage, with revenues being higher during the warmer months.

WE DO NOT MAINTAIN INSURANCE COVERAGE ON OUR TRANSMISSION AND DISTRIBUTION SYSTEM.

In common with other companies in our line of business that serve coastal regions, we do not have insurance covering our transmission and distribution system because we believe it to be cost prohibitive. If we were to sustain any loss of or damage to our transmission and distribution properties, we would be entitled to seek to recover such loss or damage through a change in our regulated rates, although there is no assurance that we would ultimately obtain any such rate recovery or that any such rate recovery would be timely granted. Therefore, we cannot assure you that we will be able to restore any loss of or damage to any of our transmission and distribution properties without negative impact on our results of operations, financial condition and cash flows.

TECHNOLOGICAL CHANGE MAY MAKE ALTERNATIVE ENERGY SOURCES MORE ATTRACTIVE AND MAY ADVERSELY AFFECT OUR REVENUES AND RESULTS OF OPERATIONS.

The continuous process of technological development may result in the introduction to retail customers of economically attractive alternatives to purchasing electricity through our distribution facilities. Manufacturers of self-generation facilities continue to develop smaller-scale, more-fuel-efficient generating units that can be cost-effective options for some retail customers with smaller electric energy requirements. Any reduction in the amount of electric energy we distribute as a result of these technologies may have an adverse impact on our results of operations, financial condition and cash flows in the future.

### ITEM 3. LEGAL PROCEEDINGS

For a brief description of certain legal and regulatory proceedings affecting us, see Note 10(b) to our consolidated financial statements, which note is incorporated herein by reference.

### ITEM 7. MANAGEMENT'S NARRATIVE ANALYSIS OF RESULTS OF OPERATIONS

#### CERTAIN FACTORS AFFECTING FUTURE EARNINGS

Our past earnings are not necessarily indicative of our future earnings and results of operations. The magnitude of our future earnings and results of our operations will depend on numerous factors including:

- state and federal legislative and regulatory actions or developments, including deregulation, re-regulation and restructuring of the electric utility industry, constraints placed on our activities or business by the 1935 Act, changes in or application of laws or regulations applicable to other aspects of our business and actions with respect to:
- approval of stranded costs;
- allowed rates of return;
- rate structures;
- recovery of investments; and
- operation and construction of facilities;
- non-payment for our services due to financial distress of our customers, including our largest customer, Reliant Resources;
- the successful and timely completion of our capital projects;
- industrial, commercial and residential growth in our service territory and changes in market demand and demographic patterns;
- changes in business strategy or development plans;
- changes in interest rates or rates of inflation;
- unanticipated changes in operating expenses and capital expenditures;
- weather variations and other natural phenomena, which can affect the demand for power over our transmission and distribution system;

- commercial bank and financial market conditions, our access to capital, the cost of such capital, receipt of certain approvals under the 1935 Act, and the results of our financing and refinancing efforts, including availability of funds in the debt capital markets for transmission and distribution companies;
- actions by rating agencies;
- legal and administrative proceedings and settlements;
- changes in tax laws;
- inability of various counterparties to meet their obligations with respect to our financial instruments;
- any lack of effectiveness of our disclosure controls and procedures;
- changes in technology;
- significant changes in our relationship with our employees, including the availability of qualified personnel and the potential adverse effects if labor disputes or grievances were to occur;
- significant changes in critical accounting policies;
- acts of terrorism or war, including any direct or indirect effect on our business resulting from terrorist attacks such as occurred on September 11, 2001 or any similar incidents or responses to those incidents;
- the availability and price of insurance;
- the outcome of the pending securities lawsuits against Reliant Energy and Reliant Resources;
- the outcome of the Securities and Exchange Commission investigation relating to the treatment in our consolidated financial statements of certain activities of Reliant Resources;
- the ability of Reliant Resources to satisfy its indemnity obligations to us;
- the reliability of the systems, procedures and other infrastructure necessary to operate the retail electric business in our service territory, including the systems owned and operated by the ERCOT ISO;
- political, legal, regulatory and economic conditions and developments in the United States; and
- other factors discussed in Item 1 of this report under "Risk Factors."

CENTERPOINT ENERGY HOUSTON ELECTRIC, LLC AND SUBSIDIARIES  
 (AN INDIRECT WHOLLY OWNED SUBSIDIARY OF CENTERPOINT ENERGY, INC.)  
 NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(3) SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

(e) REGULATORY ASSETS AND LIABILITIES

The Company applies the accounting policies established in SFAS No. 71, "Accounting for the Effects of Certain Types of Regulation" (SFAS No. 71).

The following is a list of regulatory assets/liabilities reflected on the Company's Consolidated Balance Sheets as of December 31, 2001 and 2002:

DECEMBER 31, -----	2001	2002	-----
(IN MILLIONS) Excess cost over market (ECOM) true-up.....	\$ --	\$ 697	Recoverable electric generation related regulatory assets,
net.....	160	100	Securitized regulatory asset.....
tax asset, net.....	740	706	Regulatory tax asset, net.....
debt.....	62	58	Recoverable electric generation plant mitigation.....
liability.....	(1,126)	(969)	Excess mitigation Other long-term
assets/liabilities.....	28	40	-----
Total.....	\$ 1,942	\$ 2,861	=====

If events were to occur that would make the recovery of these assets and liabilities no longer probable, the Company would be required to write off or write down these regulatory assets and liabilities. In addition, the Company would be required to determine any impairment of the carrying costs of plant and inventory assets.

Through December 31, 2001, the Public Utility Commission of Texas (Texas Utility Commission) provided for the recovery of most of the Company's fuel and purchased power costs from customers through a fixed fuel factor included in electric rates. Included in the above table in recoverable electric generation-related regulatory assets, net are \$126 million and \$66 million of regulatory assets related to the recovery of fuel costs as of December 31, 2001 and 2002, respectively. For additional information regarding our fuel filings, see Note 4(c).

In 2001, the Company monetized \$738 million of regulatory assets in a securitization financing authorized by the Texas Utility Commission pursuant to the Texas electric restructuring law. The securitized regulatory assets are being amortized ratably as transition charges are collected over the life of the outstanding transition bonds. For additional information regarding the securitization financing, see Note 6.

#### (4) REGULATORY MATTERS

##### (a) TEXAS ELECTRIC RESTRUCTURING LAW AND DISCONTINUANCE OF SFAS NO. 71 FOR ELECTRIC GENERATION OPERATIONS

In June 1999, the Texas legislature adopted the Texas electric restructuring law, which substantially amended the regulatory structure governing electric utilities in Texas in order to allow retail electric competition. Retail pilot projects allowing competition for up to 5% of each utility's load in all customer classes began in the third quarter of 2001, and retail electric competition for all other customers began in January 2002. In preparation for competition, CenterPoint Energy made significant changes in the electric utility operations it conducts through the Company. In addition, the Texas Utility Commission issued a number of new rules and determinations in implementing the Texas electric restructuring law.

The Texas electric restructuring law defined the process for competition and created a transition period during which most utility rates were frozen at rates not in excess of their then-current levels. The Texas electric restructuring law provided for utilities to recover their generation related stranded costs and regulatory assets (as defined in the Texas electric restructuring law).

Unbundling. As of January 1, 2002, electric utilities in Texas such as the Company unbundled their businesses in order to separate power generation, transmission and distribution, and retail activities into different units. Pursuant to the Texas electric restructuring law, CenterPoint Energy submitted a plan in January 2000 that was later amended and updated to accomplish the required separation (the business separation plan). The Company continues to be subject to cost-of-service rate regulation and is responsible for the transmission and distribution of electricity to retail customers. The Company transferred its Texas generation facilities that were formerly part of Reliant Energy HL&P (Texas generation business) to Texas Genco in connection with the Restructuring.

Transmission and Distribution Rates. All retail electric providers in the Company's service area pay the same rates and other charges for transmission and distribution services.

The Company's distribution rates charged to retail electric providers are generally based on amounts of energy delivered. The Company's transmission rates charged to other distribution companies are based on amounts of energy transmitted under "postage stamp" rates that do not vary with the distance the energy is being transmitted. All distribution companies in ERCOT pay the Company the same rates and other charges for transmission services. The transmission and distribution rates for the Company have been in effect since January 1, 2002, when electric competition began. This regulated delivery charge includes the transmission and distribution rate (which includes costs for nuclear decommissioning and municipal franchise fees), a system benefit fund fee imposed by the Texas electric restructuring law, a transition charge associated with securitization of regulatory assets and an excess mitigation credit imposed by the Texas Utility Commission.

Stranded Costs. The Company will be entitled to recover its stranded costs (the excess of net regulatory book value of historical generation assets (as defined by the Texas electric restructuring law) over the market value of those assets) and its regulatory assets related to generation. The Texas electric restructuring law prescribes specific methods for determining the amount of stranded costs and the details for their recovery. During the transition period to deregulation (the Transition Period), which included 1998 and the first six months of 1999, and extending through the base rate freeze period from July 1999 through 2001, the Texas electric restructuring law provided that earnings above a stated overall annual rate of return on invested capital be used to recover CenterPoint Energy's investment in generation assets (Accelerated Depreciation). In addition, during the Transition Period, the redirection of depreciation expense to generation assets that the Company would otherwise apply to transmission, distribution and general plant assets was permitted for regulatory purposes (Redirected Depreciation). Please read the discussion of the accounting treatment for depreciation for financial reporting purposes below under "-- Accounting." The Company cannot predict the amount, if any, of these costs that may not be recovered.

In accordance with the Texas electric restructuring law, beginning on January 1, 2002, and ending December 31, 2003, any difference between market power prices received in Texas Genco's generation capacity auctions mandated by the Texas electric restructuring law and the Texas Utility Commission's earlier estimates of those prices will be included in the 2004 stranded cost true-up proceeding, as further discussed below. This component of the true-up is intended to ensure that neither the customers nor CenterPoint Energy is disadvantaged economically as a result of the two-year transition period by providing this pricing structure.

On October 24, 2001, CenterPoint Energy Transition Bond Company, LLC (Bond Company), a Delaware limited liability company and wholly owned subsidiary of the Company, issued \$749 million aggregate principal amount of its Series 2001-1 Transition Bonds (Transition Bonds) pursuant to a financing order of the Texas Utility Commission. Classes of the bonds have final maturity dates of September 15, 2007, September 15, 2009, September 15, 2011 and September 15, 2015, and bear interest at rates of 3.84%, 4.76%, 5.16% and 5.63%, respectively. Scheduled payments on the bonds are from 2002 through 2013. Net proceeds to the Bond Company from the issuance were \$738 million. The Bond Company paid the Company \$738 million for the transition property. Proceeds were used for general corporate purposes, including the repayment of indebtedness.

The Transition Bonds are secured primarily by the "transition property," which includes the irrevocable right to recover, through non-bypassable transition charges payable by certain retail electric customers, the qualified costs of the Company authorized by the financing order. The holders of the Bond Company's bonds have no recourse to any assets or revenues of the Company, and the creditors of the Company have no recourse to any assets or revenues (including, without limitation, the transition charges) of the Bond Company. The Company has no payment obligations with respect to the Transition Bonds except to remit collections of transition charges as set forth in a servicing agreement between the Company and the Bond Company and in an intercreditor agreement among the Company, the Bond Company and other parties.

The non-bypassable transition charges are required by the financing order to be true-up annually, effective November 1, for the term of the transition charge. The Company filed an annual true-up with the Texas Utility Commission on August 2, 2002 for transition charges that became effective November 1, 2002.

Costs associated with nuclear decommissioning will continue to be subject to cost-of-service rate regulation and are included in a charge to transmission and distribution customers. For further discussion of the effect of the business separation plan on funding of the nuclear decommissioning trust fund, see Note 4(b).

**True-Up Proceeding.** The Texas electric restructuring law and current Texas Utility Commission implementation guidance provide for a true-up proceeding to be initiated in or after January 2004. The purpose of the true-up proceeding is to quantify and reconcile the amount of stranded costs, the capacity auction true-up, unreconciled fuel costs (see Note 3(e)), and other regulatory assets associated with the Company's former electric generating operations that were not previously securitized through the Transition Bonds. The 2004 true-up proceeding will result in either additional charges being assessed on or credits being issued to certain retail electric customers. CenterPoint Energy appealed the Texas Utility Commission's true-up rule on the basis that there are no negative stranded costs, that CenterPoint Energy should be allowed to collect interest on stranded costs, and that the premium on the partial stock valuation applies to only the equity of Texas Genco, not equity plus debt. The Texas court of appeals issued a decision on February 6, 2003 upholding the rule in part and reversing in part. The court ruled that there are no negative stranded costs and that the premium on the partial stock valuation applies only to equity. The court upheld the Texas Utility Commission's rule that interest on stranded costs begins upon the date of the final true-up order. On February 21, 2003, CenterPoint Energy filed a motion for rehearing on the issue that interest on amounts determined in the true-up proceeding should accrue from an earlier date. CenterPoint Energy has not accrued interest in its consolidated financial statements, but estimates that interest could be material. If the court of appeals denies CenterPoint Energy's motion, then CenterPoint Energy will have 45 days to appeal to the Texas Supreme Court. CenterPoint Energy has not decided what action, if any, it will take if the motion for rehearing is denied.

**Accounting.** Historically, CenterPoint Energy has applied the accounting policies established in SFAS No. 71. Effective June 30, 1999, CenterPoint Energy applied SFAS No. 101 to Texas Genco.



In 1999, CenterPoint Energy evaluated the effects that the Texas electric restructuring law would have on the recovery of its generation related regulatory assets and liabilities. CenterPoint Energy determined that a pre-tax accounting loss of \$282 million existed because it believes only the economic value of its generation related regulatory assets (as defined by the Texas electric restructuring law) will be recoverable. Therefore, the Company recorded a \$183 million after-tax extraordinary loss in the fourth quarter of 1999. Pursuant to EITF Issue No. 97-4 "Deregulation of the Pricing of Electricity -- Issues Related to the Application of FASB Statements No. 71 and No. 101" (EITF No. 97-4), the remaining recoverable regulatory assets are now associated with the Company. For details regarding the Company's regulatory assets, see Note 3(e).

At June 30, 1999, CenterPoint Energy performed an impairment test of its previously regulated electric generation assets pursuant to SFAS No. 121 on a plant specific basis. Under SFAS No. 121, an asset is considered impaired, and should be written down to fair value, if the future undiscounted net cash flows expected to be generated by the use of the asset are insufficient to recover the carrying amount of the asset. For assets that are impaired pursuant to SFAS No. 121, CenterPoint Energy determined the fair value for each generating plant by estimating the net present value of future cash flows over the estimated life of each plant. CenterPoint Energy determined that \$797 million of electric generation assets was impaired in 1999. The Texas electric restructuring law provides for recovery of this impairment through regulated cash flows during the transition period and through charges to transmission and distribution customers. As such, a regulatory asset for an amount equal to Texas Genco's impairment loss and was included on the Company's Consolidated Balance Sheets as a regulatory asset. The Company recorded amortization expense related to the recoverable impaired plant costs and other assets created from discontinuing SFAS No. 71 of \$221 million during the six months ended December 31, 1999, \$329 million in 2000 and \$247 million in 2001.

The impairment analysis requires estimates of possible future market prices, load growth, competition and many other factors over the lives of the plants. The resulting impairment loss is highly dependent on these underlying assumptions. In addition, after January 10, 2004, the Company must finalize and reconcile stranded costs (as defined by the Texas electric restructuring law) in a filing with the Texas Utility Commission. Any positive difference between the regulatory net book value and the fair market value of the generation assets (as defined by the Texas electric restructuring law) will be collected through future charges. Any overmitigation of stranded costs may be refunded by a reduction in future charges. This final reconciliation allows alternative methods of third party valuation of the fair market value of these assets, including outright sale, stock valuations and asset exchanges.

In order to reduce potential exposure to stranded costs related to generation assets, the Company recognized Redirected Depreciation of \$195 million and \$99 million 1998 and for the six months ended June 30, 1999, respectively, for regulatory and financial reporting purposes. This redirection was in accordance with the Company's Transition Plan. Subsequent to June 30, 1999, Redirected Depreciation expense could no longer be recorded by CenterPoint Energy's electric generation business for financial reporting purposes as these operations are no longer accounted for under SFAS No. 71. During the six months ended December 31, 1999 and during 2000 and 2001, \$99 million, \$218 million and \$230 million in depreciation expense, respectively, was redirected from transmission and distribution for regulatory and financial reporting purposes and was established as an embedded regulatory asset included in transmission and distribution related plant and equipment balances. As of December 31, 2001, the cumulative amount of Redirected Depreciation for regulatory purposes was \$841 million, prior to the effects of the October 3, 2001 order discussed below.

Additionally, as allowed by the Texas Utility Commission, in an effort to further reduce potential exposure to stranded costs related to generation assets, the Company recorded Accelerated Depreciation of \$194 million and \$104 million in 1998 and for the six months ended June 30, 1999, respectively, for regulatory and financial reporting purposes. Accelerated Depreciation expense was recorded in accordance with the Company's Transition Plan during this period. Subsequent to June 30, 1999, Accelerated Depreciation

expense could no longer be recorded by CenterPoint Energy's electric generation business for financial reporting purposes, as these operations are no longer accounted for under SFAS No. 71. During the six months ended December 31, 1999 and during 2000 and 2001, \$179 million, \$385 million and \$264 million, respectively, of Accelerated Depreciation was recorded for regulatory reporting purposes, reducing the regulatory book value of the Company's stranded costs recovery.

The Texas Utility Commission issued a final order on October 3, 2001 (October 3, 2001 Order) that established the transmission and distribution utility rates that became effective in January 2002. In this Order, the Texas Utility Commission found that the Company had overmitigated its stranded costs by redirecting transmission and distribution depreciation and by accelerating depreciation of generation assets as provided under the Transition Plan and Texas electric restructuring law. As a result of the October 3, 2001 Order, the Company was required to reverse the \$841 million embedded regulatory asset related to Redirected Depreciation, thereby reducing the net book value of transmission and distribution assets. The Company was required to record a regulatory liability of \$1.1 billion related to Accelerated Depreciation. The October 3, 2001 Order requires this amount to be refunded through excess mitigation credits to certain retail electric customers during a seven-year period which began in January 2002.

As of December 31, 2002, in contemplation of the 2004 true-up proceeding, the Company has recorded a regulatory asset of \$2.0 billion representing the estimated future recovery of previously incurred stranded costs, which includes \$1.1 billion of previously recorded Accelerated Depreciation plus Redirected Depreciation, both reversed in 2001. Offsetting this regulatory asset is a \$969 million regulatory liability to refund the excess mitigation to ratepayers. This estimated recovery is based upon current projections of the market value of CenterPoint Energy's Texas generation assets to be covered by the 2004 true-up proceeding calculations. The regulatory liability reflects a current refund obligation arising from prior mitigation of stranded costs deemed excessive by the Texas Utility Commission. The Company began refunding excess mitigation credits with January 2002 bills. These credits are to be refunded over a seven-year period. Because accounting principles generally accepted in the United States of America require the Company to estimate fair market values in advance of the final reconciliation, the financial impacts of the Texas electric restructuring law with respect to the final determination of stranded costs in the 2004 true-up proceeding are subject to material changes. Factors affecting such changes may include estimation risk, uncertainty of future energy and commodity prices and the economic lives of the plants. If events were to occur that made the recovery of some of the remaining generation related regulatory assets no longer probable, the Company would write off the unrecoverable balance of such assets as a charge against earnings.

#### (b) AGREEMENTS RELATED TO TEXAS GENERATING ASSETS

Texas Genco is the beneficiary of the decommissioning trust that has been established to provide funding for decontamination and decommissioning of the South Texas Project in which Texas Genco owns a 30.8% interest. The Company collects through rates or other authorized charges to its electric utility customers amounts designated for funding the decommissioning trust, and pays the amounts to Texas Genco. Texas Genco in turn deposits these amounts into the decommissioning trust. Upon decommissioning of the facility, in the event funds from the trust are inadequate, the Company or its successor will be required to collect through rates or other authorized charges to customers as contemplated by the Texas Utilities Code all additional amounts required to fund Texas Genco's obligations relating to the decommissioning of the facility. Following the completion of the decommissioning, if surplus funds remain in the decommissioning trust, the excess will be refunded to the ratepayers of the Company or its successor.

#### (c) CENTERPOINT HOUSTON REGULATORY FILINGS

Texas Genco and the Company filed their joint application to reconcile fuel revenues and expenses with the Texas Utility Commission on July 1, 2002. This final fuel reconciliation filing covers reconcilable fuel revenue, fuel expense and interest of approximately \$8.5 billion incurred from August 1, 1997 through January 30, 2002. Also included in this amount is an under-recovery of \$94 million, which was the balance at July 31, 1997 as approved in the Company's last fuel reconciliation. On January 28, 2003, a settlement agreement was reached under which it was agreed that certain items totaling \$24 million were written off during the fourth quarter of 2002 and items totaling \$203 million will be carried forward for resolution by the Texas Utility Commission in late 2003 or early 2004.

(8) EMPLOYEE BENEFIT PLANS

(a) PENSION PLANS

Substantially all of the Company's employees participate in CenterPoint Energy's qualified non-contributory pension plan. Under the cash balance formula, participants accumulate a retirement benefit based upon 4% of eligible earnings and accrued interest. Prior to 1999, the pension plan accrued benefits based on years of service, final average pay and covered compensation. As a result, certain employees participating in the plan as of December 31, 1998 are eligible to receive the greater of the accrued benefit calculated under the prior plan through 2008 or the cash balance formula.

CenterPoint Energy's funding policy is to review amounts annually in accordance with applicable regulations in order to achieve adequate funding of projected benefit obligations. Pension expense is allocated to the Company based on covered employees. This calculation is intended to allocate pension costs in the same manner as a separate employer plan. Assets of the plan are not segregated or restricted by CenterPoint Energy's participating subsidiaries. Pension benefit was \$10 million and \$6 million for the years ended December 31, 2000 and 2001, respectively. The Company recognized pension expense of \$7 million for the year ended December 31, 2002.

In addition to the Plan, the Company participates in CenterPoint Energy's non-qualified pension plan, which allows participants to retain the benefits to which they would have been entitled under the qualified pension plan except for federally mandated limits on these benefits or on the level of salary on which these benefits may be calculated. The expense associated with the non-qualified pension plan was \$3 million in 2000 and less than \$1 million in 2001 and 2002.

As of December 31, 2001, CenterPoint Energy allocated \$83 million of pension assets, \$7 million of non-qualified pension liabilities and \$2 million of minimum pension liabilities to the Company. As of December 31, 2002, CenterPoint Energy has not allocated such pension assets or liabilities to the Company. This change in method of allocation had no impact on pension expense recorded for the year ended December 31, 2002.

(10) COMMITMENTS AND CONTINGENCIES

(a) LEASE COMMITMENTS

The following table sets forth information concerning the Company's obligations under non-cancelable long-term operating leases at December 31, 2002, which primarily consist of rental agreements for building space, data processing equipment and vehicles, including major work equipment (in millions).

2003.....	\$ 5
2004.....	5
2005.....	5
2006.....	6
2007.....	6
	---
Total	\$27
	===

Total lease expense for all operating leases was \$3 million during 2000 and \$5 million during 2001 and 2002, respectively.

(b) LEGAL MATTERS

The Company's predecessor, Reliant Energy, and certain of its former subsidiaries are named as defendants in several lawsuits described below. Under a master separation agreement between Reliant Energy and Reliant Resources, CenterPoint Energy and its subsidiaries, including the Company, are entitled to be indemnified by Reliant Resources for any losses arising out of the lawsuits described under "California Class Actions and Attorney General Cases," "Long-Term Contract Class Action," "Washington and Oregon Class Actions," "Bustamante Price Reporting Class Action" and "Trading and Marketing Activities," including attorneys' fees and other costs. Pursuant to the indemnification obligation, Reliant Resources is defending CenterPoint Energy and its subsidiaries, including the Company, to the extent named in these lawsuits. The ultimate outcome of these matters cannot be predicted at this time.

California Class Actions and Attorney General Cases. Reliant Energy, Reliant Resources, Reliant Energy Services, Inc. (Reliant Energy Services), Reliant Energy Power Generation, Inc. (REPG) and several other subsidiaries of Reliant Resources, as well as two former officers and one present officer of some of these companies, have been named as defendants in class action lawsuits and other lawsuits filed against a number of companies that own generation plants in California and other sellers of electricity in California markets. While the plaintiffs allege various violations by the defendants of antitrust laws and state laws against unfair and unlawful business practices, each of the lawsuits is grounded on the central allegation that the defendants conspired to drive up the wholesale price of electricity. In addition to injunctive relief, the plaintiffs in these lawsuits seek treble the amount of damages alleged, restitution of alleged overpayments, disgorgement of alleged unlawful profits for sales of electricity, costs of suit and attorneys' fees. All of these suits originally were filed in state courts in San Diego, San Francisco and Los Angeles Counties. The suits in San Diego and Los Angeles Counties were consolidated and removed to the federal district court in San Diego, but on December 13, 2002, that court remanded the suits to the state courts. Prior to the remand, Reliant Energy was voluntarily dismissed from two of the suits.

Several parties, including the Reliant defendants, have appealed the judge's remand decision. The United States court of appeals has entered a briefing schedule that could result in oral arguments by summer of 2003. Proceedings before the state court are expected to resume during the first quarter of 2003.

In March and April 2002, the California Attorney General filed three complaints, two in state court in San Francisco and one in the federal district court in San Francisco, against Reliant Energy, Reliant

Resources, Reliant Energy Services and other subsidiaries of Reliant Resources alleging, among other matters, violations by the defendants of state laws against unfair and unlawful business practices arising out of transactions in the markets for ancillary services run by the California independent systems operator, charging unjust and unreasonable prices for electricity, in violation of antitrust laws in connection with the acquisition in 1998 of electric generating facilities located in California. The complaints variously seek restitution and disgorgement of alleged unlawful profits for sales of electricity, civil penalties and fines, injunctive relief against unfair competition, and undefined equitable relief. Reliant Resources has removed the two state court cases to the federal district court in San Francisco where all three cases are now pending.

Following the filing of the Attorney General cases, seven additional class action cases were filed in state courts in Northern California. Each of these purports to represent the same class of California ratepayers, assert the same claims as asserted in the other California class action cases, and in some instances repeat as well the allegations in the Attorney General cases. All of these cases have been removed to federal district court in San Diego. Reliant Resources has not filed an answer in any of these cases. The plaintiffs have agreed to a stipulated order that would require the filing of a consolidated complaint by early March 2003 and the filing of the defendants' initial response to the complaint within 60 days after the consolidated complaint is filed. In all of these cases before the federal and state courts in California, the Reliant defendants have filed or intend to file motions to dismiss on grounds that the claims are barred by federal preemption and the filed rate doctrine.

**Long-Term Contract Class Action.** In October 2002, a class action was filed in state court in Los Angeles against Reliant Energy and several subsidiaries of Reliant Resources. The complaint in this case repeats the allegations asserted in the California class actions as well as the Attorney General cases and also alleges misconduct related to long-term contracts purportedly entered into by the California Department of Water Resources. None of the Reliant entities, however, has a long-term contract with the Department of Water Resources. This case has been removed to federal district court in San Diego.

**Washington and Oregon Class Actions.** In December 2002, a lawsuit was filed in Circuit Court of the State of Oregon for the County of Multnomah on behalf of a class of all Oregon purchasers of electricity and natural gas. Reliant Energy, Reliant Resources and several Reliant Resources subsidiaries are named as defendants, along with many other electricity generators and marketers. Like the other lawsuits filed in California, the plaintiffs claim the defendants manipulated wholesale power prices in violation of state and federal law. The plaintiffs seek injunctive relief and payment of damages based on alleged overcharges for electricity. Also in December 2002, a nearly identical lawsuit on behalf of consumers in the State of Washington was filed in federal district court in Seattle. Reliant Resources has removed the Oregon suit to federal district court in Portland. It is anticipated that before answering the lawsuits, the defendants will file motions to dismiss on the grounds that the claims are barred by federal preemption and by the filed rate doctrine.

**Bustamante Price Reporting Class Action.** In November 2002, California Lieutenant Governor Cruz Bustamante filed a lawsuit in state court in Los Angeles on behalf of a class of purchasers of gas and power alleging violations of state antitrust laws and state laws against unfair and unlawful business practices based on an alleged conspiracy to report and publish false and fraudulent natural gas prices with an intent to affect the market prices of natural gas and electricity in California. Reliant Energy, Reliant Resources and several Reliant Resources subsidiaries are named as defendants, along with other market participants and publishers of some of the price indices. The complaint seeks injunctive relief, compensatory and punitive damages, restitution of alleged overpayment, disgorgement of all profits and funds acquired by the alleged unlawful conduct, costs of suit and attorneys' fees. The parties have stipulated to a schedule that would require the defendants to respond to the complaint by March 31, 2003. The Reliant defendants intend to deny both their alleged violation of any laws and their alleged participation in any conspiracy.

Trading and Marketing Activities. Reliant Energy has been named as a party in several lawsuits and regulatory proceedings relating to the trading and marketing activities of its former subsidiary, Reliant Resources.

In June 2002, the SEC advised Reliant Resources and Reliant Energy that it had issued a formal order in connection with its investigation of Reliant Resources' financial reporting, internal controls and related matters. The Company understands that the investigation is focused on Reliant Resources' same-day commodity trading transactions involving purchases and sales with the same counterparty for the same volume at substantially the same price and certain structured transactions. These matters were previously the subject of an informal inquiry by the SEC. Reliant Resources and CenterPoint Energy are cooperating with the SEC staff.

In connection with the Texas Utility Commission's industry-wide investigation into potential manipulation of the ERCOT market on and after July 31, 2001, Reliant Energy and Reliant Resources have provided information to the Texas Utility Commission concerning their scheduling and trading activities.

Fifteen class action lawsuits filed in May, June and July 2002 on behalf of purchasers of securities of Reliant Resources and/or Reliant Energy have been consolidated in federal district court in Houston. Reliant Resources and certain of its executive officers are named as defendants. Reliant Energy is also named as a defendant in seven of the lawsuits. Two of the lawsuits also name as defendants the underwriters of the May 2001 initial public offering of approximately 20% of the common stock of Reliant Resources (Reliant Resources Offering). One lawsuit names Reliant Resources' and Reliant Energy's independent auditors as a defendant. The consolidated amended complaint seeks monetary relief purportedly on behalf of three classes: (1) purchasers of Reliant Energy common stock from February 3, 2000 to May 13, 2002; (2) purchasers of Reliant Resources common stock on the open market from May 1, 2001 to May 13, 2002; and (3) purchasers of Reliant Resources common stock in the Reliant Resources Offering or purchasers of shares that are traceable to the Reliant Resources Offering. The plaintiffs allege, among other things, that the defendants misrepresented their revenues and trading volumes by engaging in round-trip trades and improperly accounted for certain structured transactions as cash-flow hedges, which resulted in earnings from these transactions being accounted for as future earnings rather than being accounted for as earnings in fiscal year 2001.

In February 2003, a lawsuit was filed by three individuals in federal district court in Chicago against CenterPoint Energy and certain former and current officers of Reliant Resources for alleged violations of federal securities laws. The plaintiffs in this lawsuit allege that the defendants violated federal securities laws by issuing false and misleading statements to the public, and that the defendants made false and misleading statements as part of an alleged scheme to inflate artificially trading volumes and revenues. In addition, the plaintiffs assert claims of fraudulent and negligent misrepresentation and violations of Illinois consumer law. The defendants expect to file a motion to transfer this lawsuit to the federal district court in Houston and to consolidate this lawsuit with the consolidated lawsuits described above.

The Company believes that none of these lawsuits has merit because, among other reasons, the alleged misstatements and omissions were not material and did not result in any damages to any of the plaintiffs.

In May 2002, three class action lawsuits were filed in federal district court in Houston on behalf of participants in various employee benefits plans sponsored by Reliant Energy. Reliant Energy and its directors are named as defendants in all of the lawsuits. Two of the lawsuits have been dismissed without prejudice. The remaining lawsuit alleges that the defendants breached their fiduciary duties to various employee benefits plans, directly or indirectly sponsored by Reliant Energy, in violation of the Employee Retirement Income Security Act. The plaintiffs allege that the defendants permitted the plans to purchase or hold securities issued by Reliant Energy when it was imprudent to do so, including after the prices for such securities became artificially inflated because of alleged securities fraud engaged in by the defendants. The complaints seek

monetary damages for losses suffered by a putative class of plan participants whose accounts held Reliant Energy or Reliant Resources securities, as well as equitable relief in the form of restitution.

In October 2002, a derivative action was filed in the federal district court in Houston, against the directors and officers of CenterPoint Energy. The complaint sets forth claims for breach of fiduciary duty, waste of corporate assets, abuse of control and gross mismanagement. Specifically, the shareholder plaintiff alleges that the defendants caused CenterPoint Energy to overstate its revenues through so-called "round trip" transactions. The plaintiff also alleges breach of fiduciary duty in connection with the spin-off and the Reliant Resources Offering. The complaint seeks monetary damages on behalf of CenterPoint Energy as well as equitable relief in the form of a constructive trust on the compensation paid to the defendants. The defendants have filed a motion to dismiss this case on the ground that the plaintiff did not make an adequate demand on CenterPoint Energy before filing suit.

A Special Litigation Committee appointed by CenterPoint Energy's Board of Directors is investigating similar allegations made in a June 28, 2002 demand letter sent on behalf of a CenterPoint Energy shareholder. The letter states that the shareholder and other shareholders are considering filing a derivative suit on behalf of CenterPoint Energy and demands that CenterPoint Energy take several actions in response to alleged round-trip trades occurring in 1999, 2000, and 2001. The Special Litigation Committee is reviewing the demands made by the shareholder to determine if these proposed actions are in the best interests of CenterPoint Energy.

Reliant Energy Municipal Franchise Fee Lawsuits. In February 1996, the cities of Wharton, Galveston and Pasadena filed suit, for themselves and a proposed class of all similarly situated cities in Reliant Energy's electric service area, against Reliant Energy and Houston Industries Finance, Inc. (formerly a wholly owned subsidiary of Reliant Energy) alleging underpayment of municipal franchise fees. The plaintiffs claim that they are entitled to 4% of all receipts of any kind for business conducted within these cities over the previous four decades. A jury trial of the original claimant cities (but not the class of cities) in the 269th Judicial District Court for Harris County, Texas, ended in April 2000 (the Three Cities case). Although the jury found for Reliant Energy on many issues, it found in favor of the original claimant cities on three issues, and assessed a total of \$4 million in actual and \$30 million in punitive damages. However, the jury also found in favor of Reliant Energy on the affirmative defense of laches, a defense similar to a statute of limitations defense, due to the original claimant cities having unreasonably delayed bringing their claims during the 43 years since the alleged wrongs began. The trial court in the Three Cities case granted most of Reliant Energy's motions to disregard the jury's findings. The trial court's rulings reduced the judgment to \$1.7 million, including interest, plus an award of \$13.7 million in legal fees. In addition, the trial court granted Reliant Energy's motion to decertify the class. Following this ruling, 45 cities filed individual suits against Reliant Energy in the District Court of Harris County.

On February 27, 2003, the state court of appeals in Houston rendered an opinion reversing the judgment against CenterPoint Energy and rendering judgment that the Three Cities take nothing by their claims. The court of appeals found that the jury's finding of laches barred all of the Three Cities' claims and that the Three Cities were not entitled to recovery of any attorneys' fees. The judgment of the court of appeals is subject to motions for rehearing and an appeal to the Texas Supreme Court.

The extent to which issues in the Three Cities case may affect the claims of the other cities served by Reliant Energy cannot be assessed until judgments are final and no longer subject to appeal. However, the court of appeals' ruling appears to be consistent with Texas Supreme Court opinions. The Company estimates the range of possible outcomes for recovery by the plaintiffs in the Three Cities case to be between \$0 and \$18 million inclusive of interest and attorneys' fees.

#### Other Matters

The Company is involved in other legal, environmental, tax and regulatory proceedings before various courts, regulatory commissions and governmental agencies regarding matters arising in the ordinary course of business. Some of these proceedings involve substantial amounts. The Company's management regularly analyzes current information and, as necessary, provides accruals for probable liabilities on the eventual disposition of these matters. The Company's management believes that the disposition of these matters will not have a material adverse effect on the Company's financial condition, results of operations or cash flows.