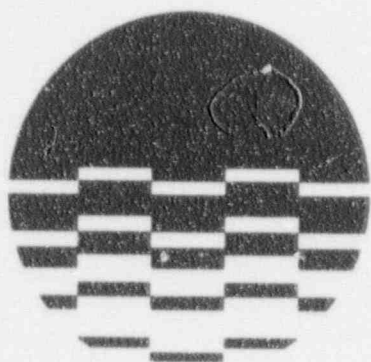


System Energy Resources, Inc./1990 Annual Report



**System
Energy**

SYSTEM ENERGY RESOURCES, INC.

System Energy Resources Inc. (System Energy), a nuclear generating company, has a 90 percent interest in the Grand Gulf Nuclear Station located near Port Gibson, Mississippi.

System Energy is a wholly-owned subsidiary of Entergy Corporation, the public utility holding company for the Entergy System. For the past 42 years, the Entergy System has been the leading electric energy supplier to a 91,000-square-mile region along the lower reaches of the Mississippi River.

The System's vast network of interconnected transmission and distribution lines and diversified grid of fossil fuel and nuclear generating plants provide electricity to more than 1.7 million retail customers in Arkansas, Louisiana, Mississippi, and Missouri.

Headquartered in New Orleans, Louisiana, Entergy Corporation includes four retail operating companies: Arkansas Power & Light Company, Louisiana Power & Light Company, Mississippi Power & Light Company, and New Orleans Public Service Inc. In June 1990, Entergy Operations, a nuclear management service company, wholly-owned by Entergy Corporation was formed and assumed operating responsibility for the Entergy System's nuclear generating units. Another subsidiary, Entergy Services, Inc., provides various technical, administrative, and corporate services to Entergy Corporation and the System companies. In August 1990, Entergy Power, another wholly-owned subsidiary of Entergy Corporation, was formed to own generating capacity and to sell such capacity and energy in the wholesale market outside Arkansas and Missouri and in markets not otherwise served presently by the Entergy System.

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SYSTEM ENERGY RESOURCES, INC.

REPORT OF MANAGEMENT

The management of System Energy Resources, Inc. has prepared and is responsible for the financial statements and related financial information included in this annual report of System Energy Resources, Inc. The financial statements are based on generally accepted accounting principles. Financial information included elsewhere in this report is consistent with the financial statements.

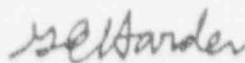
To meet its responsibilities with respect to financial information, management maintains and enforces a system of internal accounting controls which is designed to provide reasonable assurance, on a cost effective basis, as to the integrity, objectivity and reliability of the financial records, and as to the protection of assets. This system is also tested by a comprehensive internal audit program.

The independent public accountants provide an objective assessment of the degree to which management meets its responsibility for fairness of financial reporting. They regularly evaluate the system of internal accounting controls and perform such tests and other procedures as they deem necessary to reach and express an opinion on the fairness of the financial statements.

Management believes that these policies and procedures provide reasonable assurance that its operations are carried out with a high standard of business conduct.



William Cavanaugh, III
President and Chief Executive Officer

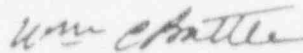


Glenn E. Harder
Vice President and Treasurer

SYSTEM ENERGY RESOURCES, INC.
AUDIT COMMITTEE CHAIRMAN'S LETTER

The Entergy Corporation Board of Directors' Audit Committee functions as the Audit Committee for System Energy. The Audit Committee is comprised of five directors, who are not officers of System Energy or Entergy Corporation: William C. Battle (Chairman), James B. Campbell, John A. Cooper, Jr., Kaneaster Hodges, Jr., and Admiral Kinnaird R. McKee. The committee held three meetings during 1990.

The Audit Committee oversees the Entergy Corporation consolidated financial reporting process, which includes System Energy, on behalf of the Entergy Corporation Board of Directors. The Audit Committee discussed with System Energy's internal auditor and the independent public accountants (Deloitte & Touche) the overall scope and plans for their respective audits, as well as the financial statements and the adequacy of System Energy's internal controls. The committee met with the independent public accountants, without management present, to discuss the results of their examinations, their evaluations of System Energy's internal controls, and the overall quality of financial reporting. The meetings were designed to facilitate and encourage any private communications between the committee and the independent public accountants.



William C. Battle
Chairman, Audit Committee

SYSTEM ENERGY RESOURCES, INC.

DEFINITIONS

Certain abbreviations or acronyms used in the text and notes are defined below:

<u>Abbreviation or Acronym</u>	<u>Term</u>
AFUDC	Allowance for Funds Used During Construction
ALJ	Administrative Law Judge
ANO	AF&L's Arkansas Nuclear One Steam Electric Generating Station (nuclear)
AP&L	Arkansas Power & Light Company
APSC	Arkansas Public Service Commission
Capital Funds Agreement	Agreement, dated as of June 21, 1974, as amended, between System Energy and Entergy Corporation, and the assignments thereof
City of New Orleans or City ..	New Orleans, Louisiana
Council	Council of the City of New Orleans, Louisiana
D.C. Circuit	United States Court of Appeals for the District of Columbia Circuit
Entergy Operations	Entergy Operations, Inc.
FASB	Financial Accounting Standards Board
February 4 Resolution	The Resolution (including the Determinations and Order referred to therein) adopted by the Council on February 4, 1988 disallowing the recovery by NOPSI of \$135 million of previously deferred Grand Gulf 1-related costs
FERC	Federal Energy Regulatory Commission
FERC Settlement	Settlement offer filed with the FERC on June 9, 1989, by AP&L, LP&L, MP&L, NOPSI and System Energy and approved by the FERC on July 21, 1989, to settle, among other things, certain then pending Grand Gulf Station-related issues, litigation and other rate matters
Grand Gulf Station	Grand Gulf Steam Electric Generating Station (nuclear)
Grand Gulf 1	Unit No. 1 of the Grand Gulf Station
Grand Gulf 2	Unit No. 2 of the Grand Gulf Station
June 13 Decision	An order issued by the FERC on June 13, 1985 (Opinion No. 234) relating to the Unit Power Sales Agreement
KWH	Kilowatt-Hours
LP&L	Louisiana Power & Light Company
LPSC	Louisiana Public Service Commission
Money Pool	Entergy System Money Pool which allows certain System companies to borrow from, or lend to, certain other System companies
MP&L	Mississippi Power & Light Company
MPSC	Mississippi Public Service Commission
NOPSI	New Orleans Public Service Inc.
November 30 Order	An order issued by the FERC on November 30, 1987 (Opinion No. 292) which reaffirmed and reinstated the June 13 Decision
NRC	Nuclear Regulatory Commission
PCRBs	Pollution Control Revenue Bonds
SEC	Securities and Exchange Commission
SFAS	Statement of Financial Accounting Standards promulgated by the FASB
SMEPA	South Mississippi Electric Power Association
System or Entergy System	Entergy Corporation and its various direct and indirect subsidiaries
System Energy	System Energy Resources, Inc.
System Fuels	System Fuels, Inc.
System operating companies ..	AP&L, LP&L, MP&L and NOPSI, collectively
Waterford 3	Unit No. 3 (nuclear) of LP&L's Waterford Steam Electric Generating Station

SYSTEM ENERGY RESOURCES, INC.
MANAGEMENT'S FINANCIAL DISCUSSION AND ANALYSIS
RESULTS OF OPERATIONS

Grand Gulf 1 was on-line for 282 of 365 days in 1990 as compared to 284 of 365 days in 1989. Grand Gulf 1 returned to power from its fourth refueling outage on November 26, 1990. The outage began September 30, 1990 and required approximately 57 days to complete, the second shortest refueling outage since the unit began commercial operation. Grand Gulf 1 was shut down due to an unplanned outage from December 18 to December 31, 1990 in order to replace two reactor recirculation pumps. In addition, Grand Gulf 1 encountered three brief unplanned outages during the last half of 1990. The capacity factor, which is a measure of the unit's performance (based on a ratio of net electrical generation to maximum dependable capacity), was 73.9% for 1990 as compared to 78.2% for 1989. Grand Gulf 1's third refueling outage occurred in 1989.

Listed below are selected factors affecting results of operations for which changes have occurred for the year 1990 as compared to 1989 and for the year 1989 as compared to 1988. The principal reasons for the changes from period to period are discussed following the table.

	1990	1989	1988	1990 vs 1989		1989 vs 1988	
				Increase/ (Decrease)	Percent Change	Increase/ (Decrease)	Percent Change
				(Dollars In Millions)			
Net income (loss)	\$168.7	\$ (655.5)	\$180.3	\$824.2	—	\$ (835.8)	(463.5)
Operating revenues	\$801.6	\$ 837.3	\$933.8	\$ (35.7)	(4.3)	\$ (96.5)	(10.3)
Fuel expense	\$ 79.0	\$ 88.3	\$129.4	\$ (9.3)	(10.5)	\$ (41.1)	(31.7)
Maintenance expense	\$ 31.6	\$ 29.8	\$ 14.1	\$ 1.8	0.1	\$ 15.7	111.3
Depreciation, amortization and decommissioning expense	\$ 75.8	\$ 103.1	\$ 96.9	\$ (27.3)	(26.5)	\$ 6.2	6.4
Miscellaneous — net	\$ 25.1	\$ 11.0	\$ 29.2	\$ 14.1	128.2	\$ (18.2)	(62.3)
Gain on disposition of property	\$ 7.2	—	—	\$ 7.2	—	—	—
Total interest expense (excluding AFUDC)	\$242.6	\$ 249.8	\$287.3	\$ (7.2)	(2.9)	\$ (37.5)	(13.1)
Total income taxes	\$113.9	\$ (89.7)	\$120.8	\$203.6	—	\$ (210.5)	(174.3)

Net Income

The increase in 1990 net income was primarily due to the implementation in 1989 of the terms of the FERC Settlement, including the cancellation and write-off of System Energy's investment in Grand Gulf 2, the write-off of \$43 million of Grand Gulf 1 AFUDC and a \$50 million one-time credit to the System operating companies. Net income was also affected to a lesser extent by a number of other factors, including changes in interest income, income taxes, depreciation expense and a lower return on System Energy's investment in Grand Gulf 1, each of which are discussed below.

The decrease in 1989 net income was primarily due to the implementation of the terms of the FERC Settlement discussed above. System Energy's 1989 net income would have been approximately \$156 million absent the impact of the FERC Settlement. 1989 net income was also affected to a lesser extent by a number of other factors, including changes in interest income, interest expense, AFUDC, income taxes on other income and a lower return on System Energy's investment in Grand Gulf 1.

Operating Revenues

System Energy's operating revenues recover operating expenses, depreciation and capital costs attributable to Grand Gulf 1. The capital costs are computed by allowing a return (currently set at a

SYSTEM ENERGY RESOURCES, INC.

MANAGEMENT'S FINANCIAL DISCUSSION AND ANALYSIS — (Continued)

rate of 14 percent) on System Energy's common equity funds allocable to its investment in Grand Gulf 1 and adding to such amount System Energy's effective interest cost for its debt allocable to its investment in Grand Gulf 1. System Energy's operating revenues decreased approximately \$35.7 million during 1990 primarily due to a decrease in System Energy's return on its investment in Grand Gulf 1 resulting from (1) a decrease in the equity portion of its capital structure due to the impact of the write-offs associated with the FERC Settlement and (2) a decrease in net unit investment. Future revenues attributable to the return on investment are expected to decrease by approximately \$18 million in 1991 and by declining amounts each year thereafter as a result of the depreciation of System Energy's investment in Grand Gulf 1.

System Energy's return on its investment in Grand Gulf 1 decreased in 1989 primarily due to a lower net unit investment resulting from the 1988 sale and leaseback transactions and a lower equity return during the fourth quarter of 1989 due to the impact of the write-offs associated with the FERC Settlement on capitalization ratios and net unit investment. Consequently, 1989 operating revenues decreased primarily as a result of a lower return on System Energy's investment in Grand Gulf 1, and lower fuel and other operating expenses, offset in part by higher maintenance expenses.

Fuel Expense

Fuel expense decreased in 1989 as a result of Grand Gulf 1's third refueling outage and certain unplanned outages which occurred during the year, whereas there was no refueling outage in 1988.

Maintenance Expense

The increase in maintenance expense for 1989 was due primarily to an increase in expenses in connection with Grand Gulf 1's third refueling outage and certain unplanned outages which occurred during 1989.

Depreciation, Amortization and Decommissioning Expense

Depreciation expense decreased in 1990 due to the deferral of approximately \$30 million of depreciation expense related to the sale and leaseback property. In December 1990, consistent with a recommendation contained in a recent FERC audit report, System Energy recorded as a deferred asset the current and prior year difference between the amounts collected in revenues for lease payments and the amounts expensed for interest and depreciation on the related property. The deferral will increase in the early years of the lease term and will reverse over the later years of the lease term as the revenues associated with the leases exceed the charges for depreciation and lease interest. See Note 9, "Leases."

Decommissioning expense increased in 1990 due to an increase in annual decommissioning expense collections, subject to refund, from \$1.1 million per year to \$9.7 million effective June 1, 1990. See Note 8, "Commitments and Contingencies — *Spent Nuclear Fuel and Decommissioning Costs.*"

Miscellaneous — Net

Miscellaneous — net increased in 1990 primarily as a result of an increase in interest income on System Energy's temporary cash investments, which were maintained at higher average balances during 1990.

Miscellaneous — net decreased in 1989 primarily as a result of a reduction in interest income due to the return in the last half of 1988 of funds held in escrow to secure certain obligations of System Energy, which amounts were used during 1988 to repay outstanding indebtedness.

SYSTEM ENERGY RESOURCES, INC.

MANAGEMENT'S FINANCIAL DISCUSSION AND ANALYSIS — (Continued)

Gain on Disposition of Property

System Energy's gain on disposition of property in 1990 was due to the sale of certain Grand Gulf 2 property which was written off in 1989.

Total Interest Expense (excluding AFUDC)

Total interest expense (excluding AFUDC) declined in 1990 due to the retirement of approximately \$72.2 million of first mortgage bonds during the first half of 1990.

Total interest expense (excluding AFUDC) declined in 1989 due to the redemption of approximately \$487.7 million of System Energy's first mortgage bonds in January 1989 and due to prepayment in full of all amounts remaining outstanding under the domestic and foreign bank loan agreements in December 1988. This reduction was partially offset by interest expense related to the sales and leasebacks of an approximate 11.5% aggregate ownership interest in Grand Gulf 1 in December 1988 and by an increase in interest expense related to two series of PCRB's remarketed in December 1988 and one series remarketed in June 1989 at long-term fixed rates which were slightly higher than the previous short-term variable rates.

Total Income Taxes

Total income taxes for 1989 reflect a tax benefit resulting from the write-off of System Energy's investment in Grand Gulf 2, offset, in part, by the reversal of related deferred income taxes.

FINANCIAL CONDITION

Liquidity

For 1990, System Energy's cash requirements, which consisted primarily of ongoing operating expenses, discretionary retirement of long-term debt and common stock dividend payments, were met with internally generated funds. Net cash flow provided by operating activities totaled approximately \$369.9 million in 1990. As detailed in the Statements of Cash Flows, cash flow from operating activities was affected by a number of factors representative of normal operations. Factors of an unusual non-recurring nature were not significant.

Investing activities for the year resulted in a net utilization of cash of approximately \$185.0 million due primarily to nuclear fuel expenditures, construction expenditures and the investment of approximately \$125 million in intermediate-term investments. Investments in temporary investments other than cash equivalents are, because of their short-term nature, available for cash needs.

Financing activities in 1990 also resulted in a net utilization of cash of approximately \$302.6 million due to the retirement of approximately \$72.2 million of first mortgage bonds and the payment of approximately \$279.2 million of cash dividends on common stock to Entergy Corporation during the period. This net utilization of cash was partially offset by approximately \$48.6 million in proceeds from the sale and leaseback of nuclear fuel.

See Note 8, "Commitments and Contingencies — *FERC Complaint Case*" and "Commitments and Contingencies — *FERC Audit*," for information on uncertainties which could affect System Energy's financial condition.

Capital and Refinancing Requirements

System Energy estimates that it will require \$294 million in 1991, \$115.75 million in 1992 and \$30 million in 1993 to satisfy long-term debt maturities and to meet sinking fund requirements. Construc-

SYSTEM ENERGY RESOURCES, INC.

MANAGEMENT'S FINANCIAL DISCUSSION AND ANALYSIS — (Continued)

tion expenditures are estimated to be approximately \$24.3 million in 1991, \$26.7 million in 1992 and \$28.0 million in 1993.

System Energy anticipates that cash on hand at the beginning of the period and its projected internally generated funds for the period 1991-1993 will enable it to satisfy its capital and refinancing requirements, if System Energy does not choose to externally finance such obligations.

System Energy has received the necessary regulatory approval and is proceeding with arrangements for the possible redemption, purchase or other acquisition of all or a portion of one or more series of its outstanding first mortgage bonds. See Note 6, "Long-Term Debt," for further information.

Capital Resources

Under System Energy's mortgage, the amount of additional first mortgage bonds that System Energy can issue in the future is contingent upon earnings, the amount of unfunded bondable property available to support the issuance of additional first mortgage bonds and an equity coverage requirement contained in its Reimbursement Agreement. At December 31, 1990, the earnings coverage for System Energy's first mortgage bonds, which must be a minimum of 1.5 times the pro forma annual bond interest requirements for issuance of additional first mortgage bonds (subject to increase to two times coverage in September 1991, two years after abandonment of Grand Gulf 2), was 3.86. At December 31, 1990, based upon the most restrictive of the above tests, System Energy could have issued approximately \$93 million of additional first mortgage bonds. In addition, System Energy may, subject to meeting certain conditions, issue first mortgage bonds against the retirement of outstanding first mortgage bonds without meeting the earnings or bondable property tests. At December 31, 1990, up to \$72.2 million of first mortgage bonds could be issued on this basis without the concurrent retirement of other bonds due to purchases of bonds by System Energy in 1990.

System Energy is authorized by the SEC through November 1992 to effect short-term borrowings in an aggregate amount outstanding at any one time of up to \$125 million, subject to increase to a maximum outstanding at any one time of \$290 million with further SEC approval. At December 31, 1990, System Energy did not have any bank lines of credit. System Energy is also authorized by the SEC through November 1992 to effect short-term borrowings through the Money Pool, subject to the above limitations. System Energy's ability to borrow from the Money Pool is subject to the availability of funds, which at any particular time may be limited. At December 31, 1990, System Energy had no outstanding borrowings from the Money Pool.

In connection with the financing of Grand Gulf 1, Entergy Corporation has undertaken in the Capital Funds Agreement, in relevant part, to provide or cause to be provided to System Energy sufficient capital (1) to maintain System Energy's equity capital at an amount at least equal to 35 percent of System Energy's total capitalization (excluding short-term debt), (2) to permit the continuation of commercial operation of Grand Gulf 1 and (3) to pay in full all indebtedness for borrowed money of System Energy, whether at maturity, on prepayment, on acceleration or otherwise. In addition, Entergy Corporation has agreed in the Capital Funds Agreement to make certain cash capital contributions to enable System Energy to make payments when due on specific issues of its long-term debt.

ACCOUNTING ISSUES

SFAS No. 96

In December 1987, the FASB issued SFAS No. 96, "Accounting for Income Taxes," which was scheduled to be effective for fiscal years beginning after December 15, 1988. The FASB subsequently issued statement numbers 100 and 103, which delay the effective date of SFAS No. 96 to fiscal years

SYSTEM ENERGY RESOURCES, INC.

MANAGEMENT'S FINANCIAL DISCUSSION AND ANALYSIS — (Concluded)

beginning after December 15, 1991. The FASB is expected to issue a new exposure draft in the second quarter of 1991. This exposure draft may further delay the effective date and simplify the implementation of SFAS No. 96.

Based upon a preliminary study, System Energy expects that the adoption of SFAS No. 96 in its present form would result in a net increase in accumulated deferred income taxes with a corresponding increase in assets. It is not expected that results of operations for System Energy would be significantly impacted by the adoption of SFAS No. 96 in its present form. See Note 3, "Income Taxes."

SFAS No. 106

In December 1990, the FASB issued SFAS No. 106, "Employers' Accounting for Postretirement Benefits Other Than Pensions," which is generally effective for fiscal years beginning after December 15, 1992. The new standard requires a change in accounting requirements for postretirement benefits other than pensions from a cash method to an accrual method. The impact of this new standard has not been fully determined, but the change likely will result in significantly greater expense being recognized for provision of these benefits. The effect of the increased benefit expense on net income could be reduced to the extent such increased costs are recovered through rates or through the recording of a regulatory asset to be recovered in the future. System Energy expects to recover such increased costs under the Unit Power Sales Agreement. System Energy plans to adopt this statement in 1993. See Note 10, "Postretirement Benefits."

INDEPENDENT AUDITORS' REPORT

System Energy Resources, Inc.:

We have audited the accompanying balance sheets of System Energy Resources, Inc. (System Energy) as of December 31, 1990 and 1989, and the related statements of income (loss), retained earnings and cash flows for each of the three years in the period ended December 31, 1990. These financial statements are the responsibility of System Energy's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with generally accepted auditing standards. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, such financial statements present fairly, in all material respects, the financial position of System Energy at December 31, 1990 and 1989, and the results of its operations and its cash flows for each of the three years in the period ended December 31, 1990 in conformity with generally accepted accounting principles.

As discussed in Note 8, "Commitments and Contingencies — FERC Complaint Case and — FERC Audit" of Notes to Financial Statements, several regulatory proceedings have been initiated against System Energy seeking (1) retroactive and prospective reductions of rates charged by System Energy to the System operating companies and (2) the write off of approximately \$95 million of costs included in utility plant resulting from System Energy's accounting for certain allocated income tax charges. The ultimate outcome of these uncertainties cannot presently be determined. Accordingly, no provision for any refunds or losses that may result upon resolution of these matters has been made in the accompanying financial statements.

Deloitte + Touche

Deloitte & Touche
New Orleans, Louisiana
February 15, 1991

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SYSTEM ENERGY RESOURCES, INC.

BALANCE SHEETS

ASSETS

	December 31,	
	1990	1989
	(In Thousands)	
Utility Plant (Note 1):		
Electric	\$3,011,911	\$3,010,881
Electric plant under lease (Note 9)	438,499	435,241
Construction work in progress	26,491	14,446
Plant held for future use	4,425	5,576
Nuclear fuel under capital lease (Note 9)	133,908	150,567
Total	3,615,234	3,616,711
Less — accumulated depreciation and amortization	419,923	323,691
Utility plant — net	3,195,311	3,293,020
Other Investments:		
Decommissioning trust fund (Note 1)	11,285	5,438
Total	11,285	5,438
Current Assets:		
Cash and cash equivalents:		
Cash	58	169
Temporary investments:		
Associated companies	1,579	12,880
Other	130,361	236,610
Total cash and cash equivalents (Note 12)	131,998	249,659
Other temporary investments (Note 12)	125,225	—
Accounts receivable:		
Associated companies	56,496	69,413
Other	3,671	3,929
Materials and supplies — at average cost	76,668	70,091
Income tax benefits related to Grand Gulf 2 cancellation (Note 3)	69,600	58,000
Prepayments	2,554	2,379
Unamortized fuel expense	2,288	1,313
Other	4,542	5,423
Total	473,042	460,207
Deferred Debits:		
Future benefits related to AFUDC (Note 3)	—	9,861
Income tax benefits related to Grand Gulf 2 cancellation (Note 3)	135,489	179,335
Unamortized loss on reacquired debt	15,866	17,798
Other (Note 9)	52,248	21,396
Total	203,603	228,390
TOTAL	\$3,883,241	\$3,987,055

See Notes to Financial Statements.

SYSTEM ENERGY RESOURCES, INC.

BALANCE SHEETS

CAPITALIZATION AND LIABILITIES

	December 31,	
	1990	1989
	(In Thousands)	
Capitalization:		
Common stock, no par value, authorized 1,000,000 shares; issued and outstanding 789,350 shares	\$ 789,350	\$ 789,350
Retained earnings (Note 7)	386,469	497,022
Total common shareholder's equity	1,175,819	1,286,372
Long-term debt (Note 6)	1,795,991	2,158,455
Total	2,971,810	3,444,827
Other Noncurrent Liabilities:		
Obligations under capital lease	53,909	70,567
Total	53,909	70,567
Current Liabilities:		
Currently maturing long-term debt (Note 6)	294,000	—
Obligations under capital lease	80,000	80,000
Accounts payable:		
Associated companies	1,805	176
Other	26,475	51,736
Taxes accrued	20,730	20,256
Interest accrued	59,553	60,508
Other	121	116
Total	482,684	212,792
Deferred Credits:		
Accumulated deferred income taxes (Note 3)	282,024	236,969
Accumulated deferred investment tax credits (Note 3)	69,489	13,169
Other	23,325	8,731
Total	374,838	258,869
Commitments and Contingencies (Notes 2 and 8)		
TOTAL	\$3,883,241	\$3,987,055

See Notes to Financial Statements.

SYSTEM ENERGY RESOURCES, INC.

STATEMENTS OF INCOME (LOSS) AND RETAINED EARNINGS

STATEMENTS OF INCOME (LOSS)

	For the Years Ended December 31,		
	1990	1989	1988
	(In Thousands)		
Operating Revenues	\$801,618	\$ 837,307	\$933,828
Operating Expenses:			
Operation:			
Fuel	78,968	88,350	129,423
Other	97,133	98,647	92,859
Maintenance	31,594	29,789	14,139
Depreciation, amortization, and decommissioning (Note 9)	75,789	103,065	96,854
Taxes other than income taxes	25,879	24,350	27,571
Income taxes (Note 3)	110,227	131,225	151,997
Total	419,590	475,426	512,843
Operating Income	382,028	361,881	420,985
Other Income (Deductions):			
Project Olive Branch Settlement (Note 2)	—	(1,000,932)	—
Allowance for equity funds used during construction (Note 1)	442	985	1,112
Miscellaneous — net	25,093	11,018	29,215
Income taxes — (debit) credit (Notes 1 and 3)	(3,675)	220,937	31,226
Gain on disposition of property	7,189	—	—
Total	29,049	(767,992)	61,553
Interest Charges:			
Interest on long-term debt	230,643	239,697	279,470
Other interest — net	11,992	10,116	7,870
Allowance for borrowed funds used during construction (Note 1)	(235)	(400)	14,884
Total	242,400	249,413	302,224
Net Income (Loss)	\$168,677	\$ (655,524)	\$180,314

STATEMENTS OF RETAINED EARNINGS

	For The Years Ended December 31,		
	1990	1989	1988
	(In Thousands)		
Retained Earnings, January 1	\$497,022	\$1,240,219	\$1,359,905
Add — Net income (loss)	168,677	(655,524)	180,314
Total	665,699	584,695	1,540,219
Deduct — Cash dividends on common stock (Note 7)	279,230	87,673	300,000
Retained Earnings, December 31 (Note 7)	\$386,469	\$ 497,022	\$1,240,219

See Notes to Financial Statements.

SYSTEM ENERGY RESOURCES, INC.

STATEMENTS OF CASH FLOWS

	For The Years Ended December 31,		
	1990	1989	1988
	(In Thousands)		
Operating Activities:			
Net income (loss)	\$168,677	\$(655,524)	\$180,314
Noncash items included in net income (loss):			
Depreciation and amortization	69,653	101,952	95,741
Deferred income taxes and investment tax credits	109,282	78,727	(151,797)
Allowance for equity funds used during construction	(442)	(985)	(1,112)
Amortization of debt discount	10,532	8,069	6,643
Burnup of nuclear fuel not under lease	—	6,224	2,250
Loss on Grand Gulf 2 cancellation	—	907,932	—
Writeoff of AFUDC — equity	—	43,000	—
Changes in:			
Accounts receivable	13,175	14,077	6,175
Accounts payable	(23,632)	(7,571)	25,141
Materials and supplies	(6,577)	(27,776)	(4,519)
Taxes and interest accrued	(481)	1,142	(390)
Other current assets and liabilities	(264)	(1,020)	(500)
Income tax impact of future benefits related to AFUDC (Note 3)	9,861	69,316	258,513
Income tax benefits related to Grand Gulf 2 cancellation (Note 3)	32,246	(237,335)	—
Gain on disposition of property	(7,189)	—	—
Change in bonding trust arrangement	—	—	101,202
Change in decommissioning trust	(5,847)	(1,344)	(1,320)
Other	900	13,944	10,565
Net cash flow provided by operating activities	<u>369,894</u>	<u>312,828</u>	<u>526,906</u>
Investing Activities:			
Construction expenditures	(24,633)	(28,153)	(24,377)
Allowance for equity funds used during construction	442	985	1,112
Nuclear fuel expenditures	(48,607)	(26,672)	(103,001)
Expenditures on Grand Gulf 2	—	(7,175)	(12,194)
Proceeds from sale of assets	13,046	—	—
Investment in other temporary investments	(125,225)	—	—
Net cash flow used by investing activities	<u>(184,977)</u>	<u>(61,015)</u>	<u>(138,460)</u>
Financing Activities:			
Proceeds from issuance of long-term debt	—	—	500,000
Proceeds from sale and leaseback of nuclear fuel	48,607	44,197	129,827
Retirement of first mortgage bonds (Note 6)	(72,234)	(487,697)	—
Retirement of bank notes and other long-term debt	—	—	(374,349)
Proceeds from letter of credit escrow	—	—	192,885
Letter of credit escrow payments	—	—	(84,323)
Change in short-term borrowings	—	—	(158,000)
Common stock dividend payments (Note 7)	(279,230)	(87,673)	(300,000)
Other	279	—	—
Net cash flow used by financing activities	<u>(302,578)</u>	<u>(531,173)</u>	<u>(93,960)</u>
Net change in cash and cash equivalents	(117,661)	(279,360)	294,486
Cash and cash equivalents at beginning of period	<u>249,659</u>	<u>529,019</u>	<u>234,533</u>
Cash and cash equivalents at end of period	<u>\$131,998</u>	<u>\$ 249,659</u>	<u>\$529,019</u>

See Notes to Financial Statements.

SYSTEM ENERGY RESOURCES, INC.
NOTES TO FINANCIAL STATEMENTS

NOTE 1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Organization

System Energy, formerly Middle South Energy, Inc., is a wholly-owned subsidiary of Entergy Corporation. System Energy, created in 1974, is a generating company providing electricity to the System operating companies and has a 90% interest in Grand Gulf 1, a nuclear generating station located near Port Gibson, Mississippi. The Grand Gulf Station was originally designed as two 1250 megawatt nuclear generating units.

The NRC issued a full power operating license for Grand Gulf 1 on August 31, 1984 and the unit began commercial operation on July 1, 1985. In September 1989, System Energy canceled and wrote off its investment in Grand Gulf 2, construction on which had been suspended since September 1985. See Note 2, "Rate and Regulatory Matters — *Project Olive Branch Settlement*." On June 6, 1990, Entergy Operations assumed responsibility for the operation and maintenance of Grand Gulf 1. See Note 2, "Rate and Regulatory Matters — *Nuclear Management Consolidation*," for further information.

System Energy has a combined ownership and leasehold interest of 90% in Grand Gulf 1, and SMEPA has an undivided ownership interest of 10% in Grand Gulf 1. System Energy records its investment associated with Grand Gulf 1 to the extent to which it owns and maintains a leasehold interest in the generating station. Likewise, System Energy's operating expenses reflected in the accompanying financial statements represent 90% of such Grand Gulf 1 expenses.

System of Accounts

The accounts of System Energy are maintained in accordance with the system of accounts prescribed by the FERC. See "*Utility Plant, Depreciation and Decommissioning*" below for information on the accounting treatment of the sale and leaseback transactions.

Postretirement Benefits

System Energy participates in a postretirement plan. System Energy's policy is to fund pension costs in accordance with contribution guidelines established by the Employee Retirement Income Security Act of 1974, as amended, and the Internal Revenue Code of 1986, as amended, and to fund and record other postretirement plan costs on a cash basis. See Note 10, "Postretirement Benefits."

Income Taxes

System Energy joins its parent and affiliates in the filing of a consolidated Federal income tax return. Pursuant to an intra-System tax allocation agreement, income taxes are allocated to System Energy in proportion to its contribution to consolidated taxable income. In accordance with SEC regulations, no System company is required to pay more income tax than it would have paid had it filed a separate income tax return.

Deferred income taxes are provided for differences between book and taxable income to the extent permitted by System Energy's regulatory body for rate-making purposes. Investment tax credits allocated to System Energy are deferred and amortized based upon the average useful life of the related property in a manner consistent with rate-making treatment.

In addition, System Energy files a consolidated Mississippi state income tax return with certain other System companies.

SYSTEM ENERGY RESOURCES, INC.

NOTES TO FINANCIAL STATEMENTS — (Continued)

Allowance for Funds Used During Construction

In accordance with the regulatory system of accounts, System Energy capitalizes AFUDC as an appropriate cost of utility plant. Under this utility industry practice, construction work in progress on the balance sheet is charged and the income statement is credited for the approximate net composite interest cost of borrowed funds and for a reasonable return on the equity funds used for construction. This procedure is intended to remove from the income statement the effect of the cost of financing the construction program, and results in treating the AFUDC charges in the same manner as construction labor and material costs. As non-cash items, these credits to the income statement have no effect on current cash earnings. After the property is placed in service, the AFUDC charged to construction costs is recoverable from customers through depreciation provisions included in rates charged for utility service. System Energy's effective composite AFUDC rate was 10.2%, 10.7% and 10.4% for 1990, 1989 and 1988, respectively.

Utility Plant, Depreciation and Decommissioning

Utility plant is stated at original cost. The cost of additions to utility plant (including leasehold improvements) includes contracted work, direct labor and materials, allocable overheads and AFUDC. The costs of units of property retired are removed from utility plant and such costs plus removal costs, less salvage, are charged to accumulated depreciation. Maintenance and repairs of property, and the replacement of items determined to be less than units of property, are charged to operating expenses. Substantially all of the utility plant owned by System Energy is subject to the lien of System Energy's first mortgage bond indenture.

In accordance with SFAS No. 98, "Accounting for Leases," the sales and leasebacks of the undivided portions of Grand Gulf 1 are required to be reflected for financial reporting purposes as financing transactions in System Energy's financial statements. For financial reporting purposes, utility plant includes the portions of Grand Gulf 1 that were sold and are currently under lease. System Energy has retired such property from its continuing property records as formerly owned property released from and no longer subject to System Energy's mortgage and deed of trust. System Energy is reflecting such property on its books and records for financial reporting purposes as property under lease from others and is depreciating this leased property over the life of the basic lease term. Such depreciation is being deferred until recoverable from customers in future periods. See Note 9, "Leases."

Depreciation on Grand Gulf 1 is computed on a straight-line basis. Depreciation provisions on average depreciable property approximated 2.85% in 1990, 2.97% in 1989 and 2.85% in 1988.

Effective June 1, 1990, System Energy increased its collections, subject to refund, to \$9.7 million per year for nuclear plant decommissioning costs in connection with its combined ownership and leasehold interests of 90% in Grand Gulf 1 and is depositing these monies in a tax qualified external fund held by a trustee. See Note 8, "Commitments and Contingencies — Spent Nuclear Fuel and Decommissioning Costs."

NOTE 2. RATE AND REGULATORY MATTERS

Unit Power Sales Agreement

In June 1982, System Energy and the System operating companies entered into a Unit Power Sales Agreement pursuant to which System Energy agreed to sell all of the capacity and energy available to it from its 90% share of Grand Gulf 1 and Grand Gulf 2 to LP&L, MP&L and NPSI in accordance with percentages specified therein, which conformed with the percentages set forth in the Reallocation Agreement described in Note 8, "Commitments and Contingencies — Capital Funds, Availability and

SYSTEM ENERGY RESOURCES, INC.

NOTES TO FINANCIAL STATEMENTS — (Continued)

Reallocation Agreements." The Unit Power Sales Agreement was, with certain modifications (capacity and energy from Grand Gulf 1 was allocated in the following percentages: AP&L, 36%; LP&L, 14%; MP&L, 33%; and NOPSI, 17%), approved by the FERC in its June 13 Decision and ordered to become effective upon the initiation of service of Grand Gulf 1, which occurred on July 1, 1985. The Unit Power Sales Agreement will remain in effect until terminated by the parties and approved by the FERC, which most likely would occur after Grand Gulf 1 is retired from service. In its June 13 Decision, the FERC did not rule on the Grand Gulf 2 allocation and ordered System Energy to remove the proposed Grand Gulf 2 percentage allocation from the Unit Power Sales Agreement.

The June 13 Decision was reaffirmed by the FERC in the November 30 Order. The challenges to this decision terminated on April 16, 1990, when the United States Supreme Court denied a petition for writ of certiorari seeking review of the D.C. Circuit's affirmance of the November 30 Order, thereby ending the appeals process with respect to the June 13 Decision.

The Unit Power Sales Agreement specifies the rates to be charged to the System operating companies for their respective entitlements to receive capacity and energy from Grand Gulf 1. Such rates are computed monthly on the basis of System Energy's total cost of service, which is based on System Energy's operating expenses, depreciation and capital costs attributable to the unit for the month. These rates are paid in consideration for the respective entitlements of the System operating companies to receive such capacity and energy, and are payable irrespective of the quantity of energy delivered so long as the unit remains in commercial operation. Generally, operating expenses are computed by reference to allocable amounts chargeable to System Energy's operating expense accounts, and capital costs are computed by allowing a return, currently set at a rate of 14%, on System Energy's common equity funds allocable to its investment in the unit and adding to such amount the effective interest and dividend cost to System Energy during the billing period for its respective debt and preferred stock, if any, allocable to its investment in the unit. The current monthly obligation for payments from the System operating companies to System Energy for Grand Gulf 1 capacity and energy is approximately \$67 million.

On February 1, 1990, the APSC, the LPSC, the MPSC, the Mississippi Attorney General and the City of New Orleans (Complainants) filed a complaint with the FERC against System Energy alleging that the rates currently being charged to the System operating companies by System Energy for capacity and energy from Grand Gulf 1 are not just and reasonable. See Note 8, "Commitments and Contingencies — FERC Complaint Case" and "Commitments and Contingencies — FERC Audit."

Grand Gulf 1 — Rate Activity — System Operating Companies

A disallowance by the Council in the February 4 Resolution of \$135 million of NOPSI's previously deferred Grand Gulf 1-related costs is still being litigated by NOPSI in both federal and state courts. NOPSI believes that the February 4 Resolution is contrary to the evidence presented to the Council. However, NOPSI cannot predict the outcome of the federal and state court proceedings or whether the February 4 Resolution will ultimately be overturned by the courts.

In the meantime, NOPSI is maintaining in effect a series of cash conservation measures to mitigate the negative effects upon its cash flow caused by the February 4 Resolution and to preserve its stable financial condition. While the February 4 Resolution continues to have an adverse effect upon NOPSI's financial condition and to constrain NOPSI's ability, over the near term, to raise funds from external sources, NOPSI believes that even if there were no judicial reversal of the February 4 Resolution, but assuming no catastrophic or other extraordinary event occurs, NOPSI's projected cash flow will be sufficient to permit NOPSI to meet its monthly payment obligations to System Energy under the Unit Power Sales Agreement, its projected regularly scheduled debt service obligations and its continuing preferred stock dividend and sinking fund requirements for the foreseeable future.

SYSTEM ENERGY RESOURCES, INC.

NOTES TO FINANCIAL STATEMENTS — (Continued)

On September 16, 1986, the MPSC issued an initial order establishing Docket No. U-4900 for the stated purposes, among other things, of examining the prudence of actions of System Energy relating to the construction and operation of the Grand Gulf Station and the appropriate regulatory treatment of the associated costs; obtaining FERC review of System Energy's rate of return on common equity; and performing a detailed audit of the books and records of System Energy. This docket has been inactive since mid-1987. However, since the time the docket was opened, several of the issues raised by the MPSC in the initial order either have been settled at the FERC (see "Project Olive Branch Settlement" below) or are being litigated by the MPSC and others at the FERC (see Note 8, "Commitments and Contingencies — FERC Complaint Case" and "Commitments and Contingencies — FERC Audit"). System Energy remains a party to Docket No. U-4900.

Furthermore, on February 3, 1987, the MPSC issued an order in this docket directing System Energy to show cause why its Certificate of Public Convenience and Necessity relating to the construction and operation of the Grand Gulf Station should not be canceled for the failure of System Energy to allow the MPSC to audit its books and records. System Energy had objected to the MPSC auditing its books and records on jurisdictional and other grounds. In April 1987, System Energy sought declaratory and injunctive relief against the MPSC in the United States District Court for the Southern District of Mississippi in connection with the MPSC's attempt to conduct a detailed audit of the books and records of System Energy. Following the Mississippi District Court's denial of System Energy's Motion for Preliminary Injunction, System Energy agreed to cooperate with the MPSC staff in an audit of the books and records of System Energy relating to Grand Gulf 1 wholesale rates approved by the FERC. System Energy later filed a Motion for Voluntary Dismissal of the Mississippi District Court action, which motion was approved on April 6, 1990. The Mississippi District Court's April 6, 1990 order was not appealed.

Project Olive Branch Settlement

In the FERC Settlement, System Energy and the System operating companies agreed with the FERC staff, state and local regulators and officials, and other interested parties to resolve a number of Grand Gulf Station-related and other rate matters that had been adversely affecting the System for a number of years. Implementation of the FERC Settlement in 1989 resulted in, among other things, the following:

- 1) a \$900 million pre-tax write-off of System Energy's investment in Grand Gulf 2;
- 2) a \$50 million one-time credit by System Energy to the System operating companies (which was substantially refunded to ratepayers); and
- 3) a \$43 million write-off by System Energy of Grand Gulf 1 AFUDC-equity.

The after tax impact on System Energy's 1989 net income was a reduction of approximately \$803 million. However, System Energy's cash position was not materially affected.

While all parties to the FERC Settlement agreed not to pursue any prudence disallowance of Grand Gulf 1 construction costs and operating and maintenance expenses recorded through June 9, 1989, the FERC Settlement, among other things, does not prejudice any party's right to seek disallowance of such costs recorded after that date or the right of the parties to seek future changes to the Unit Power Sales Agreement that are not inconsistent with the FERC Settlement. In addition, the FERC Settlement did not prejudice the right of any party to further pursue litigation with respect to the February 4 Resolution. See Note 8, "Commitments and Contingencies — FERC Complaint Case" and "Commitments and Contingencies — FERC Audit."

SYSTEM ENERGY RESOURCES, INC.

NOTES TO FINANCIAL STATEMENTS — (Continued)

Nuclear Management Consolidation

In June 1989, plans were announced whereby a nuclear management service company, Entergy Operations, would assume operating responsibility for ANO, Waterford 3, and Grand Gulf 1, subject, respectively, to AP&L's, LP&L's, and System Energy's oversight. Under the proposal, AP&L, LP&L, System Energy, and the other Grand Gulf 1 and Waterford 3 co-owner, would retain their ownership interests in the respective nuclear generating units. Further, AP&L, LP&L, and System Energy would retain their associated capacity and energy entitlements and would pay directly or reimburse Entergy Operations at cost for service associated with the operation and maintenance of these units. Applications for approval of or non-opposition to, as applicable, the proposed arrangements were filed with the NRC, the LTSC, the APSC, the Council, and the SEC, and all such approvals were received by June 5, 1990. However, the APSC's order is being appealed by the Arkansas Electric Energy Consumers, an intervenor in the APSC proceeding. On June 6, 1990, an organizational meeting of the board of directors of Entergy Operations was held to form Entergy Operations as a new subsidiary of Entergy Corporation, and Entergy Operations assumed responsibility for the operation of ANO, Waterford 3, and Grand Gulf 1.

NOTE 3. INCOME TAXES

Income tax expense (credit) consists of the following:

	For the Years Ended December 31,		
	1990	1989	1988
	(In Thousands)		
Current:			
Federal	\$ (4,176)	\$ (145,012)	\$264,514
State	8,796	(23,427)	8,054
Total	4,620	(168,439)	272,568
Deferred — net:			
Liberalized depreciation	46,825	43,290	49,195
Nuclear fuel	1,424	(1,336)	(9,491)
Capitalized interest	(721)	(13,674)	(60,510)
Taxes capitalized	(1,154)	(672)	(2,043)
Tax gain on sale and leaseback transactions	—	—	(126,243)
Grand Gulf 2 cancellation	2,363	55,892	—
Alternative minimum tax	(189)	7,807	(20,452)
Other	4,414	1,741	2,085
Total	52,962	93,048	(167,459)
Investment tax credit adjustments — net	56,320	(14,321)	15,662
Recorded income tax expense (credit)	\$113,902	\$ (80,712)	\$120,771
Charged to operations	\$110,227	\$ 131,225	\$ 51,997
Charged (credited) to other income	3,675	(220,937)	31,226
Recorded income tax expense (credit)	113,902	(89,712)	120,771
Income taxes applied against the debt component of AFUDC	(140)	(238)	(8,855)
Total income tax expense (credit)	\$113,762	\$ (89,950)	\$111,916

Deferred income taxes are provided for differences between book and taxable income to the extent permitted by the FERC for rate-making purposes.

SYSTEM ENERGY RESOURCES, INC.

NOTES TO FINANCIAL STATEMENTS — (Continued)

The balance sheet account described as "income tax benefits related to Grand Gulf 2 cancellation" represents the tax effects of the substantial tax loss generated in September 1989 by the Grand Gulf 2 write-off. The loss was recognized in 1989 and increased System Energy's net operating loss carryforwards, to a total of approximately \$674 million as of December 31, 1990, which may be utilized in the future to offset taxable income. If not utilized to offset consolidated Federal taxable income, income tax benefits related to the net operating loss carryforwards will expire in the years 2000 through 2004.

System Energy's tax benefits reflected in the balance sheet account, "future benefits related to AFUDC," were fully utilized during 1990. The future benefits related to AFUDC realized in 1990, 1989 and 1988 amounted to approximately \$10 million, \$69 million, and \$259 million, respectively.

Investment tax credits allocated to System Energy have been deferred and are being amortized based upon the average useful life of the related property. Unused investment tax credits at December 31, 1990, amounted to \$47.3 million. These credits may be applied against Federal income tax liabilities in future years. If not used, they will expire in the years 1999 through 2002.

The alternative minimum tax credit at December 31, 1990 was \$18.9 million. The credit can be carried forward indefinitely and will reduce regular income tax in the future.

In December 1987, the FASB issued SFAS No. 96, "Accounting for Income Taxes," which was scheduled to be effective for fiscal years beginning after December 15, 1988. The FASB subsequently issued statement numbers 100 and 103, which delay the effective date of SFAS No. 96 to fiscal years beginning after December 15, 1991. The FASB is expected to issue a new exposure draft in the second quarter of 1991. This exposure draft may further delay the effective date and simplify the implementation of SFAS No. 96. SFAS No. 96 expands the requirements to record deferred income taxes for all temporary differences that are reported in one year for financial reporting purposes and a different year for tax purposes. This will require the recognition of deferred tax balances for certain items not previously reflected in the financial statements, such as a deferred tax liability relating to AFUDC. Under the liability method adopted by SFAS No. 96, deferred tax balances will be based on enacted tax laws at tax rates that are expected to be in effect when the temporary differences reverse.

It is expected that reductions in deferred taxes resulting from the lower corporate Federal income tax rates will be reflected as liabilities to customers since the regulators may require any such savings to be passed through to ratepayers. However, based on a preliminary study, System Energy expects that the adoption of SFAS No. 96 in its present form would result in a net increase in accumulated deferred income taxes with a corresponding increase in assets. It is not expected that results of operations for System Energy would be significantly impacted by the adoption of SFAS No. 96 in its present form.

SYSTEM ENERGY RESOURCES, INC.

NOTES TO FINANCIAL STATEMENTS — (Continued)

Total income taxes differ from the amounts computed by applying the statutory Federal income tax rate to income or loss before taxes. The reasons for the differences are as follows (dollars in thousands):

	For the Years Ended December 31,					
	1990		1989		1988	
	Amount	% of Pre-Tax Income	Amount	% of Pre-Tax Loss	Amount	% of Pre-Tax Income
Computed at statutory rate	\$ 96,077	34.0	\$ (253,380)	34.0	\$102,369	34.0
Increases (reductions) in tax resulting from:						
Depreciation	8,326	2.9	14,874	(2.0)	16,931	5.5
State income taxes net of federal income tax effect....	10,115	3.6	(7,695)	1.0	(3,428)	(1.1)
Project Olive Branch Settlement/Loss on Grand Gulf 2 cancellation	—	—	154,995	(20.8)	—	—
Other	(616)	(6.2)	1,494	(0.2)	4,899	1.6
Recorded income tax expense	113,902	40.3	(89,712)	12.0	120,771	40.1
Income taxes applied against debt component of AFUDC ..	(140)	(0.1)	(238)	0.1	(8,855)	(1.8)
Total income tax expense (credit)	<u>\$113,762</u>	<u>40.2</u>	<u>\$ (89,950)</u>	<u>12.1</u>	<u>\$111,916</u>	<u>38.3</u>

NOTE 4. LINES OF CREDIT AND SHORT-TERM BORROWINGS

System Energy is authorized by the SEC through November 1992 to effect short-term borrowings in an aggregate amount outstanding at any one time or up to \$125 million, subject to increase to a maximum of \$290 million with further SEC approval. At December 31, 1990, System Energy did not have any bank lines of credit. System Energy is also authorized by the SEC through November 1992 to effect short-term borrowings through the Money Pool, subject to the above limitations. System Energy's ability to borrow from the Money Pool is subject to the availability of funds, which at any particular time may be limited. At December 31, 1990, System Energy had no outstanding borrowings from the Money Pool.

System Energy had no short-term borrowings during 1990, 1989 and at year end 1988. However, during 1988 its short-term borrowings and the interest rate (determined by dividing applicable interest expense by the average amount borrowed) were: maximum borrowing of \$158 million; average borrowing of \$10.533 million; and an average interest rate of 9.7%.

NOTE 5. COMMON STOCK

There were no changes in the number of shares of System Energy's common stock during the years 1990, 1989 and 1988.

SYSTEM ENERGY RESOURCES, INC.
NOTES TO FINANCIAL STATEMENTS — (Continued)

NOTE 6. LONG-TERM DEBT

The long-term debt of System Energy at December 31, 1990 and 1989 was as follows:

	1990	1989
	(In Thousands)	
First Mortgage Bonds:		
Due 2000, 11% Series	\$ 255,750	\$ 300,000
Due 1991, 9% Series	294,000	300,000
Due 1996, 10 3/8% Series	250,000	250,000
Due 2016, 11 3/8% Series	90,319	112,303
Due 1991, 14% Series	200,000	200,000
Due 1992, 14.34% Series	100,000	100,000
Total	<u>1,190,069</u>	<u>1,262,303</u>
Pollution Control Revenue Bonds:		
Claiborne County, Mississippi —		
Due 2013, at 9 1/4%	49,500	49,500
Due 2014, at 8.25%	27,100	27,100
Due 2014, at 9%	206,000	206,000
Due 2015, at 12.5%	44,000	44,000
Due 2016, at 9.5%	90,000	90,000
Total	<u>416,600</u>	<u>416,600</u>
Other:		
Grand Gulf 1 Lease Obligations (Note 9)	500,000	500,000
Miscellaneous	279	—
Total	<u>500,279</u>	<u>500,000</u>
Unamortized discount on debt	(16,957)	(20,448)
Total long-term debt	<u>2,089,991</u>	<u>2,158,455</u>
Less — Amount due within one year	<u>294,000</u>	<u>—</u>
Long-term debt excluding amount due within one year	<u>\$1,795,991</u>	<u>\$2,158,455</u>

System Energy has received the necessary regulatory approval and is proceeding with arrangements for the possible redemption, purchase or other acquisition of all or a portion of one or more series of its outstanding first mortgage bonds up to an aggregate amount of \$400 million through December 1992. During 1990, System Energy reacquired in aggregate principal amount \$72.234 million of its outstanding first mortgage bonds, resulting in approval to reacquire up to approximately \$328 million as of December 31, 1990.

The PCRBs due 2015 at 12.50% and those due 2016 at 9.50% are collateralized by \$47.2 million and \$95.6 million, respectively, of non-interest bearing first mortgage bonds.

Sinking fund requirements and maturities for the ensuing five years for System Energy's long-term debt at December 31, 1990 were as follows:

	Cash Sinking Fund	Maturities
	(In Thousands)	
1991	—	\$294,000
1992	\$15,750	\$100,000
1993	\$30,000	—
1994	\$30,000	\$200,000
1995	\$30,000	—

SYSTEM ENERGY RESOURCES, INC.

NOTES TO FINANCIAL STATEMENTS — (Continued)

NOTE 7. RETAINED EARNINGS

The provisions of System Energy's first mortgage bond indenture restrict the amount of retained earnings available for cash dividends on common stock. Under its mortgage, System Energy may not declare dividends, other than stock dividends, or make other distributions on or acquisitions of its stock (except where concurrently certain contributions or stock proceeds are received) unless System Energy is not in default under certain of its financing agreements, and the sum of certain indebtedness does not exceed 65% of adjusted capitalization. However, at December 31, 1990, System Energy's most limiting restriction on dividends resulted from its reimbursement agreement equity coverage ratio, discussed below.

In connection with the 1988 sale and leaseback transactions, System Energy agreed, under the provisions of the letters of credit and reimbursement agreement, to maintain its equity at not less than 35% of its adjusted capitalization, (as defined in the agreement) and to maintain its common equity at not less than 29% of such amount. In December, 1990, a reimbursement agreement waiver was executed which reduced System Energy's required equity ratio from 35% to 33% of its adjusted capitalization (as defined in the agreement). See Note 5, "Commitments and Contingencies — Reimbursement Agreement," for more information. As of December 31, 1990, System Energy could have paid a dividend on its common stock of approximately \$46 million without violating its reimbursement agreement equity coverage ratio.

On January 23, 1991, System Energy's Board of Directors declared a dividend of \$40 million which was paid to Entergy Corporation on February 14, 1991.

NOTE 8. COMMITMENTS AND CONTINGENCIES

FERC Complaint Case

On February 1, 1990, the APSC, the LPSC, the MPSC, the Mississippi Attorney General and the City of New Orleans (Complainants) filed a complaint with the FERC against System Energy and Entergy Services, Inc. (as agent for Entergy Corporation and the System operating companies), alleging that the rates currently being charged to the System operating companies by System Energy for capacity and energy from Grand Gulf 1 are not just and reasonable. The issues raised in the complaint involve: (1) reducing System Energy's rate of return on common equity from 14%; (2) placing a ceiling for rate-making purposes on System Energy's common equity ratio; (3) reducing System Energy's cash working capital allowance; (4) investigating the transfer of certain Grand Gulf 2 assets to Grand Gulf 1; and (5) investigating plant costs related to income tax accounting issues. See "FERC Audit" below for further information on income tax accounting issues.

A reduction in System Energy's rate of return on common equity by 1% would cause annual revenues to be reduced by approximately \$16 million. System Energy's cash working capital allowance currently produces annual revenues of approximately \$4 million. Revenues currently being collected relative to equipment determined to be useful and transferred to Grand Gulf 1 at the time of the Grand Gulf 2 write-off are approximately \$3 million annually.

On May 1, 1990, the FERC issued an order which, among other things, set these matters for investigation, consolidated these issues with System Energy's decommissioning filing (see "Spent Nuclear Fuel and Decommissioning Costs" below), and established April 2, 1990 as the refund effective date. Any adjustments to System Energy's rates found necessary by the FERC pursuant to this complaint would be effective retroactively to the refund effective date. In addition to the issues mentioned above, testimony has been filed by the Complainants and the FERC staff proposing certain modifications to System Energy's rate accounting for the portion of Grand Gulf 1 sold and leased back. Such modifications, if adopted by the FERC, would reduce System Energy's revenues approximately

SYSTEM ENERGY RESOURCES, INC.

NOTES TO FINANCIAL STATEMENTS — (Continued)

\$1.5 million annually. A public hearing is scheduled to commence on September 11, 1991. System Energy cannot predict the ultimate outcome of this case. Accordingly, no provision has been made in the accompanying financial statements for the possible effects of a decision adverse to System Energy with respect to any of the issues raised in the complaint.

FERC Audit

On December 21, 1990, the FERC Division of Audits issued an audit report for System Energy for the years 1986 through 1988. The report recommends that System Energy (1) write off and not recover in its rates approximately \$95 million of Grand Gulf 1 costs included in utility plant related to the System's income tax allocation procedures (and System Energy's accounting resulting from certain allocated income tax charges) alleged to be inconsistent with FERC's accounting requirements and (2) compute refunds for the years 1987 to date to correct for overcollections of depreciation and return on rate base related thereto from the System operating companies. System Energy believes the System's income tax allocation procedures are consistent with the SEC's rules and that System Energy's accounting for allocated benefits and costs pursuant thereto are just and reasonable under the FERC's accounting rules and rate-making policies.

Should this recommendation be adopted, System Energy would have a refund obligation to the System operating companies, which, as of December 31, 1990 would have been approximately \$40 million (including interest). The ongoing effect of this change, if adopted, would be to reduce System Energy's 1991 revenues by approximately \$19 million and subsequent years' revenues by a comparable amount, but decreasing at the rate of approximately \$0.5 million in each year thereafter.

System Energy intends to vigorously contest this issue through a hearing, scheduled for August 13, 1991, before a FERC ALJ and believes that its income tax accounting procedures are in compliance with FERC and SEC requirements. However, the ultimate resolution of this issue is uncertain. Accordingly, no provision has been made in the accompanying financial statements for the possible effects of a decision adverse to System Energy.

Proposed NOPSI Negotiated Buy-out and Other Considerations

On March 29, 1988, the Council proposed to Entergy Corporation to discuss a negotiated buy-out of NOPSI (and of LP&L's electric distribution facilities in Algiers) by the City. Entergy Corporation responded by indicating a willingness to consider any alternatives that the Council might propose if they are in the best interests of its stockholders, customers and employees. In early March 1990, discussions by the City and Entergy Corporation culminated in a conceptual proposal setting forth the terms and conditions of the negotiated buy-out proposal. This proposal was the subject of public hearings by the Council in April 1990, and at a Council public meeting held on May 17, 1990, the Council voted against the adoption of a resolution to proceed with the buy-out proposal.

In July 1990 the Council adopted a resolution that provided a framework for further discussions and research concerning several issues of interest to the Council, NOPSI and LP&L. Each of the three members of the Utility Committee of the Council were assigned specific areas of study, i.e., rate matters including rate disparity, deferral collection and consolidation; capacity matters, including least cost planning, and the gas distribution properties; and socio-economic development, including industrial development. Each working group is meeting with NOPSI and LP&L and discussions are continuing with regard to all three areas of study.

In addition to the negotiated buy-out, the Council has also considered the involuntary municipalization of NOPSI's electric and gas utility properties. Such municipalization is not under active consideration at this time. Nevertheless, certain ordinances and permits under which NOPSI operates

SYSTEM ENERGY RESOURCES, INC.

NOTES TO FINANCIAL STATEMENTS — (Continued)

state, among other things, that the City has a continuing option to purchase NOPSI's electric and gas utility properties.

As provided in System Energy's mortgage and deed of trust, the condemnation or other involuntary taking of substantially all of NOPSI's property might cause acceleration of a substantial portion of System Energy's indebtedness, unless waivers were obtained, the debt were restructured or other arrangements were made.

Capital Requirements and Financing

System Energy estimates that it will require \$294 million in 1991, \$115.75 million in 1992 and \$30 million in 1993 to satisfy long-term debt maturities and to meet sinking fund requirements. Construction expenditures are estimated to be approximately \$24.3 million in 1991, \$26.7 million in 1992 and \$28.0 million in 1993.

System Energy anticipates that cash on hand at the beginning of the period and its projected internally generated funds for the period 1991-1993 will enable it to meet its capital and refinancing requirements, if System Energy does not choose to externally finance its obligations.

System Energy has received the necessary regulatory approval and is proceeding with arrangements for the possible redemption, purchase or other acquisition of all or a portion of one or more series of its outstanding first mortgage bonds. See Note 6, "Long-Term Debt," for further information.

On October 3, 1989, System Fuels entered into a revolving credit agreement with banks that provides for up to \$45 million of borrowings to finance System Fuels' nuclear materials and services inventory. In connection with these arrangements, System Energy, AP&L, and LP&L, as purchasers from System Fuels of the nuclear materials and services, agreed to purchase from System Fuels the nuclear materials and services financed under the agreement if System Fuels should default in its obligations thereunder. The purchases under these circumstances would be of percentages agreed upon between the parties but, in the absence of such agreement, System Energy, AP&L, and LP&L would each be obligated to purchase one-third of System Fuels' nuclear materials and services.

Shareholder Litigation

Entergy Corporation and certain other System companies (including System Energy) and individuals were defendants in a consolidated purported class action suit filed in the United States District Court for the Eastern District of Louisiana (District Court) in 1985 by Entergy Corporation shareholders (purporting to represent classes that purchased Entergy Corporation common stock). On October 5, 1990, the parties to the suit entered into a settlement agreement, subject to the approval of the District Court, providing for, among other things, payment to the members of the asserted plaintiff classes from an interest-bearing \$15.3 million settlement fund established by Entergy Corporation. On January 31, 1991, the District Court entered an order and final judgment approving the settlement agreement and dismissing the suit with prejudice. The time for filing appeals of this order expired with no such appeals being filed.

Bondholder Litigation

On September 29, 1989, two former holders of System Energy's First Mortgage Bonds, 16% Series Due 2000 (16% Bonds), filed a class action complaint, purporting to represent a class comprised of all former holders of the 16% Bonds, against System Energy in the United States District Court for the Southern District of New York, alleging that System Energy's redemption of the 16% Bonds in January 1989 violated the Securities Exchange Act of 1934 (Exchange Act) and New York common law. System Energy redeemed the 16% Bonds on January 22, 1989, at a price equal to the principal amount thereof

SYSTEM ENERGY RESOURCES, INC.

NOTES TO FINANCIAL STATEMENTS — (Continued)

plus accrued interest, with the proceeds of the sale of a portion of its interest in Grand Gulf 1. Such redemption was made pursuant to a provision in System Energy's Mortgage and Deed of Trust permitting redemption of bonds at the special redemption price (100% of principal amount in the case of the 16% Bonds) with the proceeds of the sale of property released from the mortgage. The complaint alleges that the 16% Bonds were not redeemable at the special redemption price, that System Energy should have paid the holders of the 16% Bonds a redemption premium of 16% of the principal amount thereof (aggregating \$48 million), and that System Energy's redemption of the 16% Bonds at par constitutes fraud under the Exchange Act, breach of System Energy's contract with the 16% bondholders and unjust enrichment of System Energy at the expense of the 16% bondholders. The complaint seeks compensatory damages, interest, costs and fees. On November 8, 1989, the plaintiffs filed a Motion For Plaintiff Class Certification. On December 12, 1989, System Energy filed an Answer denying the substantive allegations of the complaint. On December 18, 1989, System Energy moved to transfer the action to the United States District Court for the Southern District of Mississippi (Mississippi District Court). System Energy's motion to transfer was granted on March 20, 1990. On February 14, 1990, one of the two named plaintiffs withdrew from the proceeding. On October 5, 1990, the remaining plaintiff and System Energy filed a motion with the Mississippi District Court requesting a hearing to approve a proposed settlement, under which, among other things, the class action allegations would be dropped, the remaining plaintiff's claims would be dismissed and System Energy, without admitting to any liability, would reimburse the remaining plaintiff for certain litigation expenses and attorney fees up to an aggregate of \$90,000. Plaintiff would receive nothing on its claim for damages. On November 15, 1990, the Mississippi District Court, after a hearing, approved the proposed settlement, and System Energy has reimbursed the plaintiff for the agreed to litigation expenses and attorney fees. The litigation has thus terminated, but without prejudice to the right of any former bondholder not affiliated with the settling plaintiff to bring its own action to challenge the redemption in question.

Unit Power Sales Agreement

See Note 2, "Rate and Regulatory Matters — Unit Power Sales Agreement" for a description of the Unit Power Sales Agreement and for further information with respect to litigation and proceedings related to the Unit Power Sales Agreement. The financial condition of System Energy significantly depends upon the continued commercial operation of Grand Gulf 1 and upon its receipt of payments from the System operating companies.

Capital Funds, Availability and Reallocation Agreements

Under the Capital Funds Agreement, as supplemented, Entergy Corporation has agreed to supply or cause to be supplied to System Energy (1) such amounts of capital as may be required in order to maintain System Energy's equity capital at an amount equal to at least 35% of System Energy's total capitalization (excluding short-term debt) and (2) such amounts of capital as shall be required in order (a) to permit the continuation of commercial operation of Grand Gulf 1 and (b) to pay in full all indebtedness for borrowed money of System Energy whether at maturity, on prepayment, on acceleration or otherwise. In addition, Entergy Corporation has agreed to make cash capital contributions to enable System Energy to make payments when due on its long-term debt, as specified therein. System Energy has, with the consent of Entergy Corporation, assigned its rights under the Capital Funds Agreement to certain creditors.

The System operating companies are severally obligated under the Availability Agreement in accordance with stated percentages (AP&L, 17.1%; LP&L, 26.9%; MP&L, 31.3%; NOPSI, 24.7%) to make payments or subordinated advances in amounts which, when added to any amounts received by System Energy under the Unit Power Sales Agreement or otherwise, are adequate to cover all of the

SYSTEM ENERGY RESOURCES, INC.

NOTES TO FINANCIAL STATEMENTS — (Continued)

operating expenses, including depreciation and interest charges, of System Energy. System Energy has, with the consent of the System operating companies, assigned its rights to payments and advances from the System operating companies under the Availability Agreement to certain creditors. Payments or advances under the Availability Agreement are only required to be made to the extent System Energy's receipts from all sources, including under the Unit Power Sales Agreement approved by the FERC, are less than the amount required under the Availability Agreement.

In June 1989, System Energy and the System operating companies, with the prior consent of such creditors, amended the Availability Agreement so that the Grand Gulf 2 write-off would be amortized for Availability Agreement purposes over 27 years rather than in the month the write-off was recognized on System Energy's books. This amendment was made so that the write-off of System Energy's investment in Grand Gulf 2 in September 1989 would not cause a payment by the System operating companies to be required under the Availability Agreement.

Since commercial operation of Grand Gulf 1, amounts received by System Energy under the Unit Power Sales Agreement (which include a return on equity) have exceeded the amounts payable under the Availability Agreement (which does not provide for a return on equity), which is expected to be the case for the foreseeable future. Consequently, no payments under the Availability Agreement have ever been required. Should there be a shortfall in any month as a result of the inability of any System operating company to make a payment under the Unit Power Sales Agreement, amounts received by System Energy from any other sources (including financings, sales of property and the like) and available at that time would be credited toward the obligations owing under the Availability Agreement.

In November 1981, the System operating companies entered into a Reallocation Agreement which would have allocated the capacity and energy available to System Energy from the Grand Gulf Station and the related costs to LP&L, MP&L and NOPSI. These companies thus agreed to assume all the responsibilities and obligations of AP&L with respect to the Grand Gulf Station under the Availability Agreement, with AP&L relinquishing its rights to capacity and energy from the Grand Gulf Station. Each of the System operating companies, including AP&L, would have remained primarily liable to System Energy and its assignees for payments or advances under the Availability Agreement and assignments thereof. AP&L was obligated to make its share of the payments or advances only if the other System operating companies were unable to meet their contractual obligations. However, the FERC's June 13 Decision allocating a portion of Grand Gulf 1 capacity and energy to AP&L supersedes the Reallocation Agreement insofar as it relates to Grand Gulf 1. However, under certain circumstances, responsibility for Grand Gulf 2 amortization amounts could be allocated to LP&L, MP&L and NOPSI under the terms of the Reallocation Agreement.

Reimbursement Agreement

On December 28, 1988, System Energy entered into two entirely separate, but identical, arrangements for the sales and leasebacks of an approximate aggregate 11.5% ownership interest in Grand Gulf 1 (as discussed in Note 9, "Leases"). In connection with the equity funding of the sale and leaseback arrangements, letters of credit are required to be maintained to secure certain amounts payable for the benefit of the equity investors by System Energy under the leases. The initial letters of credit, which were scheduled to expire on December 28, 1991, were replaced on January 14, 1991 with new letters of credit that are scheduled to expire on January 15, 1994.

Under the provisions of the reimbursement agreement, dated December 1, 1988, entered into by System Energy and various banks in connection with the sale and leaseback arrangements ("Reimbursement Agreement") related to the letters of credit, System Energy has agreed to a number of covenants relating to, among other things, the maintenance of certain capitalization and fixed charge

SYSTEM ENERGY RESOURCES, INC.

NOTES TO FINANCIAL STATEMENTS — (Continued)

coverage ratios. In this connection, System Energy agreed, during the term of the Reimbursement Agreement, to maintain its equity at not less than 35% of its adjusted capitalization (as defined in the Reimbursement Agreement) and to maintain its common equity at not less than 29% of such amount. However, in December 1990, a Reimbursement Agreement waiver was executed which reduced System Energy's required equity ratio from 35% to 33% of its adjusted capitalization (as defined in the Reimbursement Agreement). In the first amendment to the Reimbursement Agreement, executed on January 14, 1991 in connection with the issuance of the new letters of credit, System Energy was also permitted to maintain its equity, during the term of the Reimbursement Agreement, at not less than 33% of its adjusted capitalization. In addition, System Energy must maintain, with respect to each fiscal quarter during the term of the Reimbursement Agreement, a ratio of adjusted net income to interest expense (calculated, in each case, as specified in the Reimbursement Agreement) of at least 1.60. At December 31, 1990, System Energy's equity and common equity in each case approximated 33.89% of its adjusted capitalization, and its fixed charge coverage ratio was 2.11. The letters of credit may be terminated by the banks under certain circumstances as a result of any change in applicable law or governmental action which adversely affects the obligations or ability of System Energy and certain other participants in the sale and leaseback transactions to make required payments or otherwise perform under the transaction documents.

Failure by System Energy to perform its covenants under the Reimbursement Agreement could give rise to a draw under the letters of credit and/or an early termination of the letters of credit, and, if such letters of credit were not replaced in a timely manner, could result in a default under, or other early termination of, System Energy's leases. Draws under the letters of credit must be repaid by System Energy within 5 days (and, in some cases, 90 days) following the date of drawing.

Nuclear Insurance

The Price-Anderson Act provides for a limit of public liability for a single nuclear incident. As of December 31, 1990, the limit of public liability for such type of incident was approximately \$7.807 billion. System Energy has protection with respect to this liability through a combination of private insurance (currently \$200 million) and an industry assessment program. Under the assessment program, the maximum amount System Energy would be required to pay, with respect to each nuclear incident at a licensed nuclear facility, would be \$66.15 million per reactor (such amount to be indexed every five years for inflation and includes a 5% surcharge in the event the total public liability claims and legal costs approach or exceed the limit of protection otherwise established), payable at a rate of \$10 million per licensed reactor per incident per year. As a co-licensee of Grand Gulf 1 with System Energy, SMEPA would share in this assessment obligation. System Energy is an owner of one licensed reactor, and the Entergy System has four licensed reactors.

System Energy, on behalf of itself and other insured interests (including other co-owners of Grand Gulf 1), is a member of certain insurance programs that provide coverage for property damage, including decontamination expense, for the Grand Gulf facility. At December 31, 1990, System Energy was insured against such losses up to \$2.185 billion with a \$200 million sublimit for premature decommissioning coverage. Under the property damage insurance programs, System Energy could be subject to assessments if losses exceed the accumulated funds available to the insurers. At December 31, 1990, the maximum amount of such possible assessments to System Energy was \$17.91 million. Under its agreement with System Energy, SMEPA would share in System Energy's assessment obligation.

The amount of property insurance presently carried by System Energy exceeds the NRC's minimum requirement for nuclear power plant licensees of \$1.06 billion per site. Effective April 2, 1990, NRC regulations provide that the proceeds of this insurance must be used, first, to place and

SYSTEM ENERGY RESOURCES, INC.

NOTES TO FINANCIAL STATEMENTS — (Continued)

maintain the reactor in a safe and stable condition and, second, to complete required decontamination operations. Only after proceeds are used or dedicated for such use and appropriate regulatory approval is obtained would the balance of these proceeds, if any, be available for plant owners' or their creditors' benefit.

Spent Nuclear Fuel and Decommissioning Costs

Under the terms of its nuclear fuel lease, System Energy is responsible for the disposal of spent nuclear fuel. System Energy has executed a contract with the U.S. Department of Energy (DOE) whereby the DOE will furnish disposal service for System Energy's spent nuclear fuel at a cost of one mill per kilowatt-hour of net generation. System Energy includes this one mill per kilowatt-hour cost as a component of its nuclear fuel expense. A 1989 federal court ruling effectively changed the basis for the fee to one mill per net KWH sold, rather than generated, which could reduce System Energy's payments.

Under the Nuclear Waste Policy Act of 1982, the DOE was to begin accepting spent fuel in 1998 and to continue accepting spent fuel until the disposal of all fuel from reactor sites is accomplished. However, the DOE's repository program has been delayed. Based on the DOE's current schedule for acceptance of spent nuclear fuel, initial shipments of spent fuel from Grand Gulf 1 to the DOE's storage facilities will occur in 2016. In the meantime, System Energy will be responsible for storage of spent fuel. System Energy estimates that current on-site spent fuel storage capacity will be sufficient to store fuel from normal operations until 2004. It is expected that any additional storage capacity required due to, among other things, delay of the DOE repository program will have to be provided by System Energy. The cost of providing the additional on-site spent fuel storage capability required at Grand Gulf 1 by 2004 is estimated to be approximately \$10 to \$15 million (in 1990 dollars). In addition, approximately \$5 to \$10 million (in 1990 dollars) will be required every two to three years subsequent to 2004 until DOE's repository begins accepting Grand Gulf 1 spent fuel.

In addition to the recovery of costs associated with the disposal of spent nuclear fuel, System Energy is recovering nuclear plant decommissioning costs in connection with its combined ownership and leasehold interest of 90% in Grand Gulf 1. System Energy regularly reviews and updates estimated decommissioning costs to reflect inflation and changes in regulatory requirements and technology. An outside engineering firm completed a new decommissioning cost study for Grand Gulf 1 in 1989. Based upon the study, System Energy estimates that the costs of decommissioning System Energy's 90% interest in Grand Gulf 1 would approximate \$248.7 million in 1989 dollars. In a petition filed with the FERC on September 29, 1989, System Energy requested an increase in annual decommissioning expense collections from \$1.1 million per year to \$9.7 million per year to become effective January 1990. The FERC accepted System Energy's proposed rates for filing and suspended the proposed rates for five months, to become effective June 1, 1990, subject to refund. On May 24, 1990 the FERC issued an order which consolidated System Energy's decommissioning filing with the FERC Complaint Case. See the "FERC Complaint Case" discussed above.

Other Commitments and Contingencies

See Note 2, "Rate and Regulatory Matters," for information on the status of certain other contingencies.

SYSTEM ENERGY RESOURCES, INC.

NOTES TO FINANCIAL STATEMENTS — (Continued)

NOTE 9. LEASES

Nuclear Fuel Leases

In February 1989, System Energy entered into an arrangement whereby System Energy may lease up to \$185 million of nuclear fuel. The lessor finances its acquisition and ownership of nuclear fuel under a credit agreement and through the issuance of intermediate term notes. The credit agreement has a term of five years and the intermediate term notes have varying maturities of 1½ to 10 years. It is contemplated that these credit arrangements will be extended or alternative financing will be secured by the lessor upon the maturity of the current arrangements, based on System Energy's nuclear fuel requirements. If the lessor cannot arrange for alternative financing upon the regularly scheduled maturity of its borrowings, System Energy must purchase nuclear fuel in an amount equal to the amount required by the lessor to retire such borrowings. System Energy had prior nuclear fuel leasing arrangements that were effectively cancelled with the start of the new nuclear fuel leasing arrangement.

Lease payments, based upon nuclear fuel use, are treated as a cost of fuel. Lease expense charged to operations for the years ended December 31, 1990, 1989 and 1988 was approximately \$72.4 million, \$75.3 million, and \$115.4 million, respectively. The unrecovered cost base of System Energy's leases at December 31, 1990 and 1989 was approximately \$134 million and \$151 million, respectively.

Sale and Leaseback Transactions

On December 28, 1988, System Energy entered into two entirely separate, but identical, arrangements for the sales and leasebacks of an approximate aggregate 11.5% undivided ownership interest in Grand Gulf 1 for an aggregate cash consideration of \$500 million. System Energy is leasing back the undivided interest on a net lease basis over a 26½ year basic lease term. System Energy has options to terminate the leases and to repurchase the undivided interest in Grand Gulf 1 at certain intervals during the basic lease term. Further, at the end of the basic lease term, System Energy has an option to renew the leases or to repurchase the undivided interest in Grand Gulf 1. See Note 8, "Commitments and Contingencies — Reimbursement Agreement," with respect to certain other terms of the transaction.

In accordance with SFAS No. 98, "Accounting for Leases," due to "continuing involvement" by System Energy, the sales and leasebacks of the undivided portions of Grand Gulf 1, as described above, are required to be reflected for financial reporting purposes as financing transactions in System Energy's financial statements. The amounts charged for financial reporting purposes to expense include the interest portion of the lease obligations and depreciation of the plant. However, operating revenues include the recovery of the lease payments since the transactions are accounted for as sales and leasebacks for rate-making purposes. The total of interest and depreciation expense exceeds the corresponding revenues realized during the early part of the lease term. In December 1990, consistent with a recommendation contained in a recent FERC audit report, System Energy recorded as a deferred asset the current and prior year difference between the recovery of the lease payments and the amounts expensed for interest and depreciation, resulting in an increase in net income of approximately \$24 million in 1990. The effect of the deferral was to decrease depreciation expense and interest expense by approximately \$30 million and \$2 million, respectively, and to increase related taxes by approximately \$8 million. The deferral will reverse over the later years of the lease term as the revenues associated with the leases exceed the charges for depreciation and lease interest.

See Note 1, "Summary of Significant Accounting Policies — Utility Plant, Depreciation and Decommissioning" for further information regarding the accounting for the sale and leaseback transactions.

SYSTEM ENERGY RESOURCES, INC.
NOTES TO FINANCIAL STATEMENTS — (Continued)

At December 31, 1990, System Energy had future minimum lease payments (reflecting an overall implicit rate of 9.86%) in connection with the sale and leaseback transactions as listed in the following table:

	Minimum Lease Payments (In Thousands)
1991	\$ 49,333
1992	49,333
1993	49,333
1994	51,295
1995	52,247
For years thereafter	<u>1,195,873</u>
Total	<u>\$1,447,414</u>

NOTE 10. POSTRETIREMENT BENEFITS

System Energy participates in a postretirement plan sponsored by Entergy Corporation. The pension plan is noncontributory and provides pension benefits that are based on employees' credited service and average compensation, generally during the last five years before retirement. System Energy's policy is to fund pension costs in accordance with contribution guidelines established by the Employee Retirement Income Security Act of 1974, as amended.

The pension plan is administered by a trustee who is responsible for pension payments to retirees. Various investment managers have responsibility for management of the plan's assets. In addition, an independent actuary performs the necessary actuarial valuations for System Energy's plan.

Effective June 6, 1990 all of System Energy's employees became employees of Entergy Operations. However, the employees still remain under System Energy's plan and no transfers of related pension liabilities and assets have been made.

The components of System Energy's total 1990, 1989 and 1988 pension cost (income), including amounts capitalized, were as follows:

	1990	1989	1988
	(In Thousands)		
Service cost-benefits earned during the period	\$ 1,398	\$1,073	\$ 937
Interest cost on projected benefit obligation	762	559	421
Actual return on plan assets	48	(3,992)	(1,883)
Net amortization and deferral	<u>(2,402)</u>	<u>1,759</u>	<u>(36)</u>
Net pension cost (income)	<u>\$ (194)</u>	<u>\$ (601)</u>	<u>\$ (561)</u>

The assets of the plan consist primarily of common and preferred stocks, fixed income securities and insurance contracts.

SYSTEM ENERGY RESOURCES, INC.
NOTES TO FINANCIAL STATEMENTS — (Continued)

The funded status of System Energy's pension plan at December 31, 1990 and 1989 was as follows:

	1990	1989
	(In Thousands)	
Actuarial present value of accumulated pension plan benefits:		
Vested	\$ 4,036	\$ 1,386
Nonvested	982	2,594
Accumulated benefit obligation	<u>\$ 5,018</u>	<u>\$ 3,980</u>
Projected benefit obligation	\$10,478	\$ 8,861
Plan assets at fair value	<u>22,797</u>	<u>22,860</u>
Plan assets in excess of projected benefit obligation	12,319	13,999
Unrecognized prior service cost	156	165
Unrecognized transition asset	(8,871)	(9,467)
Unrecognized net gain	(1,667)	(2,954)
Accrued pension asset	<u>\$ 1,937</u>	<u>\$ 1,743</u>

Transition assets are being amortized over the average remaining service period of active participants.

The measurement of the items listed above is based on the following assumptions:

	1990	1989	1988
Weighted average discount rate	8.75%	8.5%	9.0%
Rate of increase in future compensation	5.6%	5.6%	5.6%
Expected long-term rate of return on plan assets	8.5%	8.5%	8.5%

System Energy also provides certain health care and life insurance benefits. Substantially all employees may become eligible for these benefits if they reach retirement age while still working for the Entergy System. These benefits and similar benefits for active employees are provided through payments of premiums to insurance companies, and System Energy recognizes the cost of providing these benefits by expensing the amounts as incurred. System Energy had four retirees as of December 31, 1990, three retirees as of December 31, 1989, and one retiree as of December 31, 1988. The cost of providing these benefits for retirees is not separable from the cost of providing benefits for active employees. The cost of providing these benefits for 1990, 1989, and 1988 was approximately \$2,845,000, \$1,865,000, and \$1,658,000, respectively.

In December 1990, the FASB issued SFAS No. 106, "Employers' Accounting for Postretirement Benefits Other Than Pensions," which is generally effective for fiscal years beginning after December 15, 1992. The new standard requires a change in accounting requirements for postretirement benefits other than pensions from a cash method to an accrual method. The impact of this new standard has not been fully determined, but the change likely will result in significantly greater expense being recognized for provision of these benefits. The effect of the increased benefit expense on net income could be reduced to the extent such increased costs are recovered through rates or through the recording of a regulatory asset to be recovered in the future. System Energy expects to recover such increased costs under the Unit Power Sales Agreement. System Energy plans to adopt this statement in 1993.

SYSTEM ENERGY RESOURCES, INC.

NOTES TO FINANCIAL STATEMENTS — (Continued)

NOTE 11. TRANSACTIONS WITH AFFILIATES

System Energy sells all of the capacity and energy from its share of Grand Gulf 1 to the System operating companies under rate schedules approved by the FERC in its June 13 Decision regarding the Unit Power Sales Agreement. Accordingly, all of System Energy's operating revenues consist of billings to the System operating companies.

MP&L provides a minimal amount of technical and advisory services and other miscellaneous services to System Energy. In addition, pursuant to a service agreement, System Energy receives technical and advisory services from Entergy Services, Inc. Charges from MP&L and Entergy Services, Inc. for technical, advisory and miscellaneous services amounted to approximately \$10.6 million in 1990, \$12.3 million in 1989 and \$12.1 million in 1988. Also, pursuant to an operating agreement, effective June 6, 1990, Entergy Operations has been authorized to act as general agent for System Energy and has assumed operating responsibility for, but not ownership of Grand Gulf 1. In return, System Energy pays directly or reimburses Entergy Operations for the costs associated with operating Grand Gulf 1. In 1990, direct payments totaled approximately \$141.0 million and reimbursements totaled approximately \$17.6 million.

In addition, certain materials and services required for fabrication of nuclear fuel are acquired and financed by System Fuels and then sold to System Energy, as needed. Charges for these materials and services, which represent additions to nuclear fuel, amounted to approximately \$34.3 million in 1990, \$0.06 million in 1989 and \$93.7 million in 1988.

NOTE 12. CASH AND CASH EQUIVALENTS

For purposes of the Statements of Cash Flows, System Energy generally considers all unrestricted highly liquid debt instruments, purchased with a maturity of three months or less, to be cash equivalents. The supplemental disclosures required by SFAS No. 95, "Statement of Cash Flows," were as follows:

	For the years ended December 31,		
	1990	1989	1988
	(In Thousands)		
Cash Paid (Received) During the Period for:			
Interest (net of amount capitalized of \$451 thousand in 1990; \$638 thousand in 1989 and \$674 thousand in 1988) ..	\$246,280	\$244,129	\$310,708
Income taxes	\$ (37,383)	\$ 11,741	\$ 6,543
Noncash Investing and Financing:			
Capital lease obligations incurred (Note 9)	—	\$185,000	\$ 50,000
Plant impact of future benefits related to AFUDC	—	\$ 69,593	\$ 85,472

All temporary investments are stated at cost, which approximates market.

SYSTEM ENERGY RESOURCES, INC.
NOTES TO FINANCIAL STATEMENTS — (Concluded)

NOTE 13. QUARTERLY RESULTS (Unaudited)

Operating results for the four quarters of 1990 and 1989 were as follows:

Quarter Ended	March	June	September	December
	(In Thousands)			
1990:				
Operating Revenues	\$201,660	\$197,992	\$ 204,583	\$197,383
Operating Income	\$ 88,955	\$ 86,431	\$ 88,280	\$118,362
Net Income	\$ 38,487	\$ 36,122	\$ 36,569	\$ 57,499**
1989:				
Operating Revenues	\$215,867	\$218,687	\$ 200,634	\$202,119
Operating Income	\$ 95,834	\$ 95,825	\$ 80,624	\$ 89,598
Net Income (Loss)	\$ 40,341	\$ 42,168	\$(771,085)*	\$ 33,052

* See Note 2, "Rate and Regulatory Matters — Project Olive Branch Settlement."

** See Note 9, "Leases — Sale and Leaseback Transactions."

SYSTEM ENERGY RESOURCES, INC.
RECORD OF PROGRESS 1985-1990

	1990	1989	1988	1987	1986	1985(2)
	(In Thousands)					
Selected Financial Data:						
Operating revenues	\$ 801,618	\$ 837,307	\$ 933,828	\$ 962,549	\$ 959,737	\$ 524,012
Net income (loss)	\$ 168,677	\$ (655,524)	\$ 180,314	\$ 198,801	\$ 189,135	\$ 218,067
Total assets	\$3,883,241	\$3,987,055	\$5,160,249	\$5,422,329	\$4,950,118	\$4,947,418
Long-term obligations(1)	\$1,849,900	\$2,229,022	\$2,553,002	\$2,245,155	\$2,266,824	\$2,317,225
Capitalization:						
Long-term debt (excluding currently maturing debt)	\$1,795,991	\$2,158,455	\$2,553,002	\$2,245,155	\$2,266,824	\$2,317,225
Common stock and paid-in capital	789,350	789,350	789,350	789,350	789,350	789,350
Retained earnings	386,469	497,022	1,240,219	1,359,905	1,161,104	971,969
Total capitalization	\$2,971,810	\$3,444,827	\$4,582,571	\$4,394,410	\$4,217,278	\$4,078,544
Utility Plant	\$3,615,234	\$3,616,711	\$3,653,645	\$3,602,466	\$3,357,628	\$3,322,360
Less — accumulated depreciation	419,923	323,691	245,444	170,880	95,988	37,856
Net utility plant	\$3,195,311	\$3,293,020	\$3,408,201	\$3,431,586	\$3,261,640	\$3,284,504
Electric Revenues (Dollars in Thousands):						
Sales for resale	\$ 801,618	\$ 837,307	\$ 933,828	\$ 962,549	\$ 959,737	\$ 524,012
Energy Sales (Millions of KWH):						
Sales for resale	6,666	7,064	8,632	6,954	3,696	2,403
Number of Customers (At December 31):						
Sales for resale	4	4	4	4	4	4

(1) Includes long-term debt, excluding current maturities, and non-current capital lease obligations.

(2) Commercial operation of Grand Gulf 1 commenced on July 1, 1985.

DIRECTORS

Edwin Lupberger

Chairman of the Board of System Energy and Entergy Operations, Inc.
Chairman of the Board and Chief Executive Officer of Entergy Corporation

William Cavanaugh, III

President and Chief Executive Officer of System Energy and Entergy Operations, Inc.
Senior Vice President, System Executive-Nuclear of Entergy Corporation and Entergy Services, Inc.
Executive Vice President and Chief Nuclear Officer of Arkansas Power & Light Company and Louisiana Power & Light Company

James M. Cain

Vice Chairman of Entergy Corporation and Entergy Services, Inc.

Jerry L. Maulden

Chairman of the Board and Chief Executive Officer of Arkansas Power & Light Company, Mississippi Power & Light Company, Louisiana Power & Light Company, and New Orleans Public Service Inc.
Group President, System Executive — Distribution/Customer Service of Entergy Corporation and Entergy Services, Inc.

EXECUTIVE OFFICERS

Edwin Lupberger

Chairman of the Board

William Cavanaugh, III

President and Chief Executive Officer

Glenn E. Harder

Vice President and Treasurer

Dan E. Stapp

Secretary

The 1990 Annual Report to the Securities and Exchange Commission on Form 10-K (including financial statement schedules) is available to any interested parties without charge. Interested parties can obtain a copy by calling or writing to:

Glenn E. Harder

Vice President and Treasurer
System Energy Resources, Inc.
P.O. Box 31995
Jackson, MS 39286-1995
Telephone (601) 984-9000

To request a copy of the 1990 Entergy Corporation Annual Report, call or write to:

Entergy Corporation
System Investor Relations
P.O. Box 61005
New Orleans, LA 70161
Telephone (800) 292-9960

FORM 8-K

SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, D.C. 20549

CURRENT REPORT

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

DATE OF REPORT (Date of earliest event reported): April 4, 1991

SYSTEM ENERGY RESOURCES, INC.
(Exact name of registrant as specified in its charter)

ARKANSAS	1-9067	72-0752777
(State or other jurisdiction of Incorporation)	(Commission File Number)	(IRS Employer Identification Number)

Echelon One, 1340 Echelon Parkway, Jackson, Mississippi 39213
(Address of principal executive offices)

Registrant's telephone number, including area code: (601) 984-9000

Item 5. Other Events.

As discussed on pages 14-16, 76, 236-239 and 270 of the Annual Report on Form 10-K for the fiscal year ended December 31, 1990, on February 4, 1988, after a lengthy prudence investigation that was contested by New Orleans Public Service Inc. ("NOPSI"), the Council of the City of New Orleans, Louisiana ("Council") adopted a resolution ("February 4 Resolution") that required NOPSI to write off, and not recover from its retail electric customers, \$135 million of its previously deferred costs associated with Unit No. 1 of the Grand Gulf Steam Electric Generating Station (nuclear) ("Grand Gulf 1"). This write-off, which was recorded in 1987, was in addition to \$51 million of Grand Gulf 1-related costs originally absorbed and not recovered by NOPSI. The February 4 Resolution has resulted in extensive litigation.

On February 4, 1988, the Council and other parties filed in the Civil District Court for the Parish of Orleans, Louisiana ("State Court") a petition for declaratory and injunctive relief seeking a judgment, among other things, declaring that the February 4 Resolution is valid and enforceable. Furthermore, on February 4, 1988, a suit was filed in the State Court by the Alliance for Affordable Energy, Inc. and others ("Alliance") asking that the February 4 Resolution be amended to order a significantly greater disallowance of Grand Gulf 1-related costs from NOPSI's electric rates, and NOPSI subsequently was named a party to this suit. On March 7, 1988, NOPSI also filed a petition in the State Court seeking reversal of the February 4 Resolution. These three cases were consolidated and, on November 15, 1989, the State Court rendered a judgment in favor of the Council, affirming the February 4 Resolution, and against the petitions of NOPSI and the Alliance.

On appeal, the Fourth Circuit Court of Appeal for the State of Louisiana ("Fourth Circuit") issued a decision on April 4, 1991 that rejected NOPSI's federal preemption claims and affirmed the findings of the Council, embodied in the February 4 Resolution, that NOPSI had imprudently incurred approximately \$477 million of Grand Gulf 1-related costs. However, the Fourth Circuit concluded that the Council acted contrary to law and public policy when, in weighing the effect of its ruling upon NOPSI's financial condition, it decided to disallow only a portion of the Grand Gulf 1-related costs found imprudent. The Fourth Circuit purported to amend the February 4 Resolution to disallow the recovery by NOPSI from its retail electric customers of any costs found to have been imprudently incurred, including an additional \$290 million not previously disallowed.

NOPSI intends to vigorously contest the Fourth Circuit's decision. The ruling is subject to further discretionary review in the Louisiana courts. In related proceedings before federal courts, NOPSI has petitioned the United States Supreme Court for a writ of certiorari seeking a review of lower federal court rulings rejecting NOPSI's facial preemption claims and staying the remaining portions of the federal proceedings. A ruling from the United States Supreme Court on whether to review the decisions staying federal court proceedings is expected as early as the middle of April 1991.

The ultimate outcome of these various federal and state court proceedings cannot be predicted. Entergy Corporation and NOPSI are in the process of assessing the potential impact of the Fourth Circuit decision upon NOPSI and the Entergy System as a whole. However, if the Fourth Circuit decision were ultimately sustained, NOPSI's earnings, liquidity and financial condition would be materially adversely affected and NOPSI could be rendered insolvent.

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.

SYSTEM ENERGY RESOURCES, INC.
(REGISTRANT)

By /s/ C. J. Dudenhefer
C. J. Dudenhefer
Assistant Secretary

Date: April 8, 1991