Exhibit D

UNITED ILLUMINATING

1989 ANNUAL REPORT

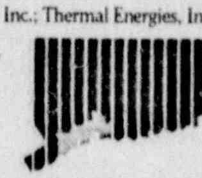
THE POWER OF PEOPLE

Contents

Cover
First
John
Celeste Robitaille, *Meter Re Reader*
Tom Dudeck, *Manager, Community*
Vivian Fripp, *Customer Services Center*
Top
Walt Booker, *Line Worker First*

The United Illuminating Company is an operating electric public utility company, incorporated in 1899. It is engaged principally in the production, purchase, transmission, distribution and sale of electricity for residential, commercial and industrial purposes in a service area of about 335 square miles in the southwestern part of the State of Connecticut. The population of this area is approximately 728,000, or 22 percent of the population of the State.

UI has three wholly owned subsidiaries. Bridgeport Electric Company, a single-purpose corporation, owns and leases to UI a coal-fired generating unit at Bridgeport Harbor Station. Research Center, Inc., has been formed to participate in the development of one or more power production ventures. United Resources, Inc., serves as the parent corporation for UI's nonutility businesses, each of which will complement and enhance UI's electric utility business and serve the interests of the Company and its shareowners and customers. Three wholly owned subsidiaries of United Resources, Inc. have been incorporated: Souwestcon Properties, Inc.; Thermal Energies, Inc.; and, Precision Power, Inc.



fourth quarter earnings were reduced by non-recurring costs of replacing siding at a generating station, costs incurred in connection with the proposal to reorganize and affiliate with Public Service Company of New Hampshire, and a write-off of the costs of a violent storm that struck our territory in July. An extended outage at the Connecticut Yankee Atomic Power Plant also had an adverse effect on earnings for the year. At year-end, the book value of UI's common stock was $26 1 per share.

Without the Seabrook write-downs, 1989 earnings would have amounted to $5.08 per share. Due to the delay in the operation of Seabrook, non-cash Allowance for Funds Used During Construction (AFUDC) continued to represent a large portion of reported earnings and returns for 1989, exclusive of write-offs. AFUDC will represent a declining portion of earnings and returns in 1990, as we begin to recover our investment in Seabrook Unit 1 through customer rates.

Cash flow from operating activities and after preferred stock dividends was $4.58 per share. Over the course of 1989, cash flow dropped off because of the increased cost of carrying the Seabrook investment and high fourth quarter costs.

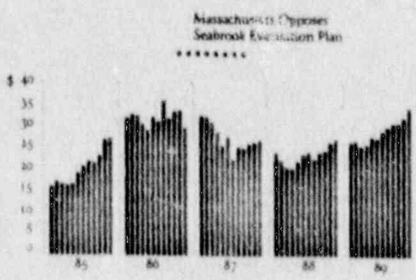
We believe that, with the anticipated commercial operation of Seabrook Unit 1 and having obtained a decision on the rate treatment of our Seabrook investment, the long-term financial outlook for UI is good. If we look beyond the write-offs in 1989 due to Seabrook and other extraordinary events, UI earnings reflect the Company's continuing efforts to improve operating efficiencies, its rigorous control over operation and maintenance budgets and its energetic pursuit of refinancing opportunities to reduce interest costs.

The expected commercial operation of Seabrook Unit 1, following the NRC's March 1, 1990 full-power licensing decision, coupled with the resolution of the unit's rate treatment, should mark the beginning of a new chapter in UI's financial history. The Company can now look to the future with renewed optimism and rededicate itself to strengthening its financial condition through the efficient operation of its core electric business and a variety of marketing and subsidiary developments.

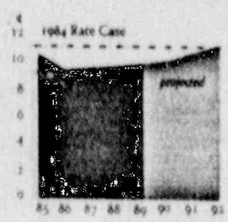
Financial Highlights

	1989	1988
Operating Revenues (000)	$ 531,181	$ 518,938
Net Income (loss) (000)	$ (73,350)	$ 78,639
Earnings per Share of Common Stock (based on average number of shares outstanding)		
Before effect of SFAS No. 90	$ 5.08	$ 7.22
After effect of SFAS No. 90	$ (5.87)	$ 4.85
Dividends Declared per Share of Common Stock	$ 2.32	$ 2.32
Utility Plant (000)	$1,725,936	$1,834,271
Sales of Energy — KWH (000)	5,307,008	5,292,157
Total Customers	307,654	307,237
Average Residential Use — KWH	6,814	6,804
Peak Load — KW	1,094,400	1,132,100
Number of Employees	1,627	1,620
Number of Common Shareowners	24,866	26,713

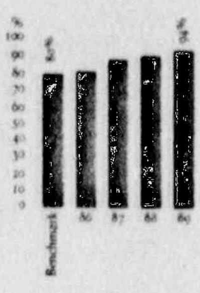
UI Common Stock Price



UI Price per KWH



Customers Rating UI Favorably



On July 6, 1989, UI reached an agreement with the Connecticut Attorney General, the Office of Consumer Counsel and the Prosecutorial Division of the Department of Public Utility Control (DPUC) on the rate treatment of UI's 17.5 percent ownership in the Seabrook plant. This historic agreement came after more than a year of difficult negotiations among the parties. It was based on the assumption that Seabrook Unit 1 will attain commercial operation in 1990, and it included settlement of many Seabrook-related issues, such as the DPUC's prudence review proceedings.

Under the agreement, which was formally approved on August 23, the amount of the Company's investment in Seabrook Unit 1 that can be recovered through customer rates was limited to $640 million, and the DPUC was to determine the Company's base rate increases for each of the next three years (1990-92). Since the recoverable investment is less than the Company's share of Connecticut's statutory "cap" on the recoverable construction costs of the unit, the settlement agreement required an additional write-down of the Company's investment in August 1989, which resulted in a net loss for the year. However, by resolving outstanding issues, including many Seabrook-related uncertainties, and by quantifying future cost recoveries within acceptable ranges, the agreement permits UI to plan effectively for the future.

Subsequently, in January 1990, the DPUC approved a $55.7 million, or 8.94 percent, increase in the Company's base rates over the next three years. The breakdown of the increases is 3.7 percent for 1990, 2.7 percent for 1991 and 2.5 percent for 1992. While the new rates took effect on February 1, 1990, UI will collect the full first year's increase over the remaining eleven months of the year.

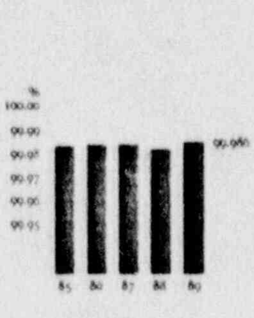
In its decision, the DPUC approved a five-year phase-in plan for the Seabrook Unit 1 investment, under which approximately $480 million, or 75 percent of the $640 million, will be phased into rate base during the first three years. The decision was based on a 12.9 percent allowed return on UI's actual equity capitalization. However, it permits the Company to earn up to 13.9 percent on a higher target equity capitalization structure of 40 percent. The DPUC also determined that the Company can retain all earnings from sales of wholesale power and property above prescribed levels, and can capitalize $35 million of the costs of conservation and load management projects, over the next three years. The investment in conservation and load management projects will be allowed to earn a premium return of up to three percent over the Company's weighted cost of capital.

In addition, the DPUC decision provides for rate design changes that encourage energy conservation and promote load management and for a sales adjustment clause to compensate for deviations from forecast sales levels. The decision also approved seasonal rates for commercial and industrial customers effective immediately, but delayed implementation of seasonal rates for residential customers until 1991.

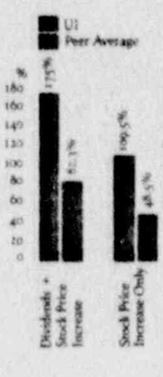
Other 1989 financial results:

In 1989, we incurred a net loss of $5.87 per share due to Seabrook Unit 1 write-downs. In addition,

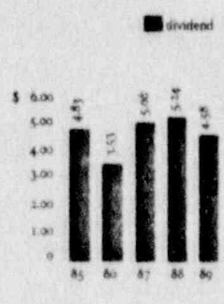
UI Reliability of Service



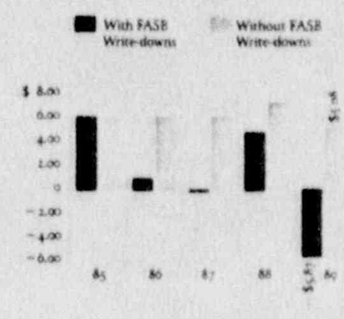
UI Shareowner Return
(April 1985 - December 1989)



UI Cash Flow per Share



UI Earnings per Share



Five years ago, when the current executive management team came together, we began a process of identifying corporate goals which, if achieved, would strengthen the Company's financial condition during the remainder of the decade and beyond and thereby increase the value of our shareowners' investment.

Beyond the immediate need to complete and secure an operating license for Seabrook Unit 1 and to resolve the financial treatment of our investment in this plant, our longer-range strategy centered on achieving high levels of customer satisfaction as the primary means of maximizing our shareowners' investment. To that end, we concluded that providing our customers with the highest value was absolutely essential. Value we defined as not only basic electric service, but also close attention to cost, courtesy, reliability and the translation of our corporate resources and expertise into service options that could be adapted to individualized customer needs. We then opened the process up to the entire Company staff for the purpose of designing and implementing programs which would help us meet these goals.

This year's Annual Report is devoted to a discussion of many of the programs which have allowed us to provide greater value to our customers. We are extremely proud of what we have achieved for our customers in five short years. We are just as proud of our success in strengthening both the present worth and future potential of our shareowners' investment.

Without question, our involvement in completing and obtaining a license for the commercial operation of the Seabrook nuclear power plant has been our central achievement. Five years ago, the plant's eventual operation was anything but a certainty. At the time, our opponents' strategy of placing every conceivable legal and regulatory obstacle in our path had put the financial viability of the project into question in the eyes of the public and even some within the financial community.

In fact, that strategy might have worked had not United Illuminating mounted one of the most ambitious and comprehensive efforts ever conducted by an electric utility at the federal level. We worked closely with everyone who would listen, convincing them of New England's severe need for additional electric capacity and the intrinsic safety of the plant.

Along the way, we won a host of important victories and, in May of 1989, the Nuclear Regulatory Commission (NRC) granted Seabrook a low-power license...a necessary step in the commercial licensing process. On March 1, 1990, over two decades after its inception, Seabrook finally obtained a full-power operating license decision from the NRC. We expect the plant to be in commercial operation by June.

Our customers, along with electric customers throughout New England, owe you, the shareowners of UI, a deep debt of gratitude. Your confidence and unswerving support were key to allowing UI management to push forward aggressively and accomplish what had to be done to get Seabrook on-line.

While Seabrook's licensing process was being played out on the federal level, there were equally important Seabrook-related developments on the local scene. On July 6, UI signed an historic agreement with Connecticut's Attorney General, the Consumer Counsel and the Prosecutorial Division of the Department of Public Utility Control (DPUC), which delineated in broad terms how UI's Seabrook investment would be treated in rates. The agreement, the first in Connecticut history, came after more than a year of negotiations and is indicative of the excellent relationships UI has forged with state regulators and elected government officials.

The agreement formed the basic framework for the rate case filed with the DPUC last September and decided in January 1990. That decision is covered in-depth in the Financial Review and Management Discussion sections of this report.

However, we had to pay a price in 1989 to free the Company from the cloud of financial uncertainty caused by Seabrook. To implement the agreement, UI reduced the recoverable cost of Seabrook Unit 1 to $640 million. This necessitated a non-cash, after tax write-off, which resulted in negative earnings for the year.

On the positive side, beginning in 1990, non-cash Allowance for Funds Used During Construction (AFUDC) will represent a declining portion of our reported earnings as the Company begins to recover its allowed Seabrook Unit 1 investment through rates. In addition, by resolving all the outstanding issues related to Seabrook, the negotiated agreement and subsequent rate increase decision by the DPUC permit UI to plan for the future with a greater degree of certainty.

It is a tribute to the strength of the Company's strategic plan and to the talents of the Company's 1,600 dedicated employees that, even under the shadow of Seabrook uncertainties, UI's record of accomplishments from 1984 through 1989 is truly impressive. These accomplishments cover the entire spectrum of Company operations and business ventures.

Since falling to a low of $9 per share during the third quarter of 1984, the market value of our stock has risen steadily, ending the year at $34.25 per share. At the same time, the Company has been successful in retiring much of the high cost debt incurred during the peak Seabrook construction phase, and has done so without having to dilute equity through the issuance of common stock.

In the Financial Review section, there appears a chart comparing the Company's shareowner return with that of 19 other electric utilities which are similar to UI. The chart shows that during the four and a half years ending in 1989, the total return (dividends plus stock price increase) to UI's shareowners was 175 percent. That ranks UI as first among all the peer group companies analyzed and is better than twice the peer group average. The increase in the price of UI stock during this same period was 109.5 percent, which is more than twice the peer group average of 48.5 percent. We believe that these numbers represent a clear expression of the growing confidence in UI's future, as we have progressively overcome obstacles and captured new opportunities.

Our total KWH sales increased by 11.5 percent during the 1984-89 time frame. UI's Business Retention and Expansion Program, along with other economic development efforts, have helped spur business growth and sales in our territory. We will continue to do everything we can to strengthen and enlarge our market.

Concurrent with a rise in sales, UI was able to offer its customers direct savings by decreasing the cost per kilowatt-hour by 6.7 percent. That decrease is in large part attributable to our diverse fuel mix, which has afforded us flexibility in using the fuels of least cost to generate power and has expanded our ability to negotiate favorable fuel contracts.

The decreased cost of electricity to our customers is also a testament to the efficiency of our system. Each year since 1984, our ranking among the nation's most efficient utilities in terms of generation has risen, to the point where, during 1989, UI's generating facilities were the fourth most efficient among those of the 100 largest utilities. We have also consistently set new Company records for heat rate and system generation. In addition, our service reliability has been exceptional and, as discussed in last year's Annual Report, we have received high public praise from the Connecticut DPUC for our commitment to customer service.

Under its present management, UI has made significant changes in its philosophy regarding energy supply and rate design. Through a sophisticated approach to conservation and load management, we have created an environment where both customers and Company benefit.

Our new-look energy programs have lowered our peak load by approximately 40 megawatts. Many of our customers, especially our commercial and industrial customers, have enjoyed substantial savings — as much as 15 percent — due to Company initiatives. We, too, have benefited through selling some of our "saved" capacity on the wholesale power market. These programs also provide a long-term benefit to both customers and the Company, since by reducing our peak load we are delaying the need for adding expensive new generation.

Central to our marketing strategies is a shift in our rate design philosophy away from a strict adherence to traditional cost-of-service rates to ones that permit customers expanded freedom in selecting the electric service options which best match their specific circumstances. To accomplish this objective, we have gradually expanded our menu of flexible rates for customers, especially business customers. In the final analysis, our optional rates help business customers to be more competitive in their own markets.

The development of subsidiaries, begun under present management in order to take full advantage of opportunities emerging within the energy marketplace, has begun to flourish and now holds significant potential for our future. With major construction projects currently underway in downtown New Haven and contracts for energy-related products and services throughout our service territory, our unregulated subsidiaries are moving toward the desired goal of representing a significant portion of total corporate revenues by the year 2000.

In the last five years, UI has come a long way toward establishing the kind of positive relationships with all our constituencies that will allow us to accomplish the things we have set out to do. There can be no question that maintaining the goodwill of our regulators, local elected officials, community leaders and, of course, customers and shareowners is central — even critical — to our success.

That is why we have been gratified by the public pronouncements of support we have received from the DPUC, officials from the cities and towns we serve, and the many groups and organizations with which we have constant interaction. That support reflects the steady rise in customers' perceptions of our service and commitment. In 1982, the overall impression that customers had of UI as a company was 80 percent favorable. By the end of 1989, that figure had risen to 94 percent. We have worked hard to gain this support. We are dedicated to maintaining it and making it even better.

The executive management of UI is prepared to explore all possibilities that have the potential of enlarging our market and strengthening our Company. One such possibility arose in 1989, involving the bankruptcy of the Public Service Company of New Hampshire (PSNH). After careful study and analysis, we put together a proposal that would have resulted in an affiliation of UI and PSNH. The proposal was an excellent one and would have benefited both UI customers and shareowners.

Unfortunately, as negotiations with PSNH creditor and equity groups developed, it became clear to us that the price of winning the competition was going to be too high. We came to the decision that to pursue the proposal further would have put our shareowners at some risk, and that was totally unacceptable to us. Therefore, we withdrew from the active bidding process in mid-November.

While we regret not being able to complete this particular venture under our preferred terms, we are confident other possibilities will arise which will provide attractive opportunities. We will pursue them aggressively, but always with the understanding that they must be related to our core expertise and present very significant opportunities for benefiting our investors.

The last five years have been good for United Illuminating and its shareowners. The years ahead will continue to present challenges as well as opportunities. We sincerely believe we have positioned the Company to meet these challenges, to seize these opportunities and to make the next five years even better.

George W. Edwards, Jr.

GEORGE W. EDWARDS, JR.
Chairman of the Board and Chief Executive Officer

Richard J. Grossi

RICHARD J. GROSSI
President and Chief Operating Officer


EXECUTIVE MANAGEMENT
Senior Vice President
Marketing
Senior Vice President
Corporate Affairs
Executive Vice President and
Chief Financial Officer
Chairman of the Board and
Chief Executive Officer
President and
Chief Operating Officer

Operations constitute the backbone of an electric utility. Broadly defined, operations consist of a company's generating facilities, its transmission and distribution system and, most importantly, the people who keep the entire network running efficiently and reliably.

By every measurement, UI's operations performance over the last five years has been a major contributing factor in providing our customers better quality service and greater value. While statistics do not tell the entire story, a few can help to give an indication of UI's success in serving its customers and its shareowners.

Last year, for example, in its annual survey of investor-owned utilities, *Electric Light & Power* magazine ranked UI's generating plants as the fourth most efficient in the nation. The ranking was based on the Company's achieved heat rate, which is determined by figuring the number of British Thermal Units (BTUs) of heat needed to produce a kilowatt-hour (KWH) of electricity; the lower the number, the greater the efficiency. UI's heat rate last year was 9,889 BTU/KWH.

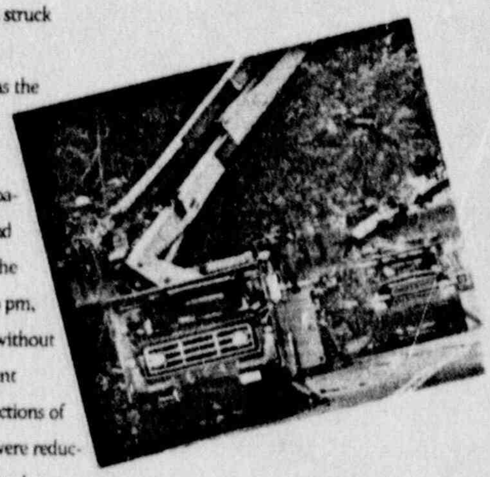
UI's success in this area was no aberration, as it marked the eighth consecutive year that UI has been ranked among the top 10 most efficient in the country and improves upon our previous fifth place standing.

There were other notable achievements as well. In 1989, the Company achieved extremely productive generation with a net output of 6,547,126,000 KWH of electricity. UI's capacity factor was a superb 63.0 percent. Even more significant for its impact on customer satisfaction was our reliability index of 99.9860 percent.

For many utilities, these numbers are mere goals. For UI they are standards of excellence that we insist on meeting or exceeding year-in and year-out. We take pride in being at the top of our industry and we are ever conscious of the important relationship between our achievements and customer satisfaction and corporate profitability.

Just as we are judged by our ability to sustain top-notch service over extended periods of time, we are also judged by our ability to respond effectively to unforeseen, sometimes catastrophic natural events. Such was the case for UI this past summer when an unexpected storm struck our region.

On July 10th, just as the evening rush hour was at its ebb, tornado-like winds reaching 80 m.p.h., accompanied by violent lightning and golf-ball sized hail blasted the UI service territory. By 6:30 pm, 48,000 UI customers were without electricity. Homes, apartment houses and businesses in sections of Hamden and New Haven were reduced to rubble; utility poles listed at 45 degree angles; cars were smashed; majestic old trees were completely uprooted; and large metal objects were bent at unbelievable angles and left lying in the middle of streets.



Overhead Line Supervisor, Bill Barker, gives Line Group Leader, George Hokanson, last minute instructions.

What UI accomplished over the next four days can be compared with rebuilding an entire distribution system for an extensive urban area. Working double shifts, UI line crews, with help from out-of-state crews, had full power restored by the following weekend, a remarkable achievement given the extent of damage that had been done to the system. UI's efforts in coordinating and executing the power restoration, which entailed integrated around-the-clock efforts of personnel from all departments of the Company, earned the respect and appreciation of tens of thousands of customers and elected officials of the most hard-hit communities.

Still another standard by which we are judged is our success in planning and preparing for future contingencies, so that quality service can be maintained at reasonable prices even as system demands change over time. Here, again, UI has been a consistent performer.

In 1989, UI finished its planning activities on two bulk substations to be constructed over the next four years to serve the Greater New Haven area. The two new substations will substantially increase our transmission and distribution capabilities and allow us to handle the growing demand for power as economic activity escalates. Bulk substations such as these are necessary to convert high voltages to the lower voltages which are usable in homes and businesses.

The Company has also dedicated itself to on-going studies and systems planning aimed at lowering

the amount of transmission line loss. This is a naturally occurring phenomenon, where the strength of electric power is diminished as it is transmitted over long distances. The aim here, as it is with so many of our efforts, is to run as efficient an operation as possible.

UI has become a leader in the study of another transmission phenomenon known as "galloping." Galloping is the reaction of iced conductors to moderate wind velocities, and can result in a short circuit or damage to supporting structures or transmission wires. While it is a relatively infrequent problem, when it does occur the result can be the loss of power to a significant population of customers.

In order to minimize the chance of a major outage due to galloping, UI has performed extensive studies on all the devices used to mitigate its effects and has installed the equipment most appropriate for our system. Our work in this area is among the most

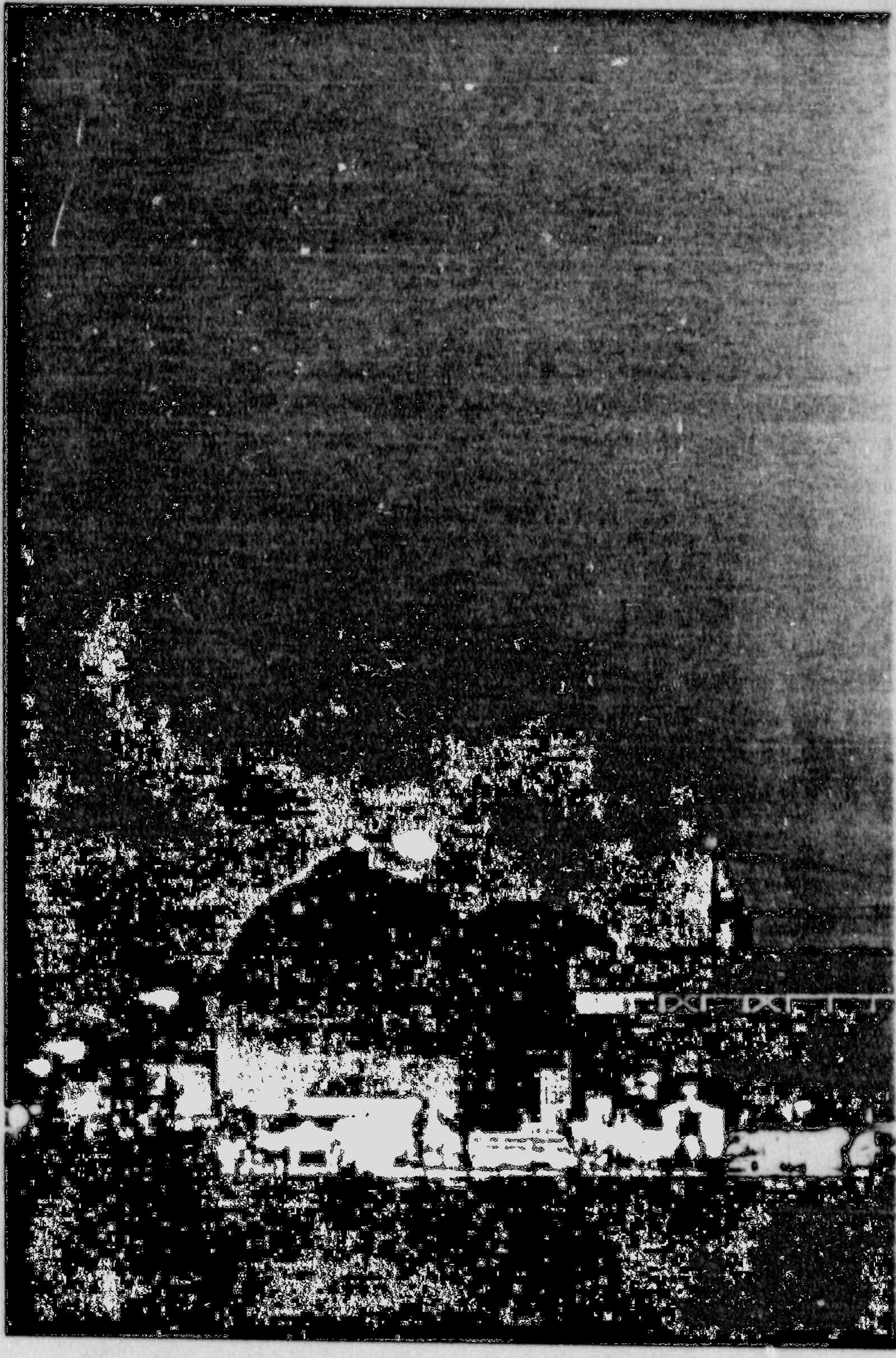
Walt Booker, Line Worker First Class.

in-depth in the industry and serves as yet another example of the Company's oft-recognized striving for the best possible customer service.

No matter whether it be planning, researching, reacting to devastating natural events, or the daily maintenance and operation of our system, UI is a leader. At UI, we take pride in our personal accomplishments but, even more, we take pride in operating a utility of which our shareowners can be proud and on which our customers can depend.

Edward Baclawski, Assistant Unit Operator, New Haven Harbor Station.

Line Worker First Class, David Bähr, selects equipment.

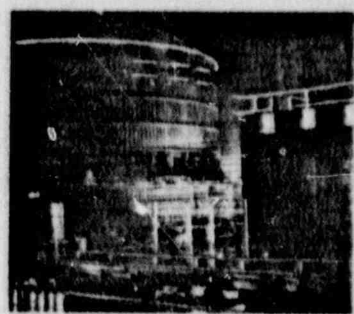


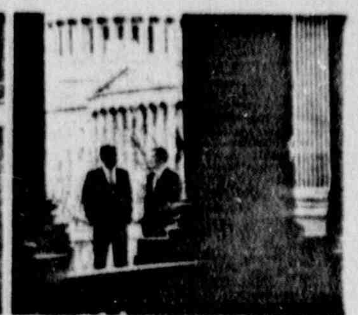
UI shareowners were first introduced to the idea of a nuclear power plant at Seabrook, New Hampshire 21 years ago in the 1968 Annual Report. During that year, the Company had dispatched a team of engineers to work with other planners at Public Service Company of New Hampshire (PSNH) in the early planning stages of the plant. Two of those engineers, current UI President and Chief Operating Officer Richard Grossi and Senior Vice President James Crowe, have stayed close to the project in its many phases ever since.

From the very beginning, the project was beset by confrontation and delays. Long before the first shovel-full of dirt was turned over, Seabrook project personnel were enmeshed in myriad siting, construction and environmental permit battles. At the same time, it was clear to those who were taking an unbiased look at the region's energy situation that New England needed this plant, that capacity problems in the region were going to grow precipitously over the next few decades and that nuclear power was the best answer. Nevertheless, because of initial conflicts, the official groundbreaking did not occur until August 1976, eight years after the project's announcement.

In one respect, construction went smoothly. Seabrook is arguably the best-designed and best constructed plant in the world. The people who oversaw the plant's construction and the workers themselves were dedi-

U.S. Senator John Breaux (Dem., La.) with George Edwards.





UI's Richard Grossi (left) and James Crowe (right) inspect construction progress.

cated to quality from the very beginning.

On other fronts, however, there were a host of difficulties. The obstacles created by Seabrook's often narrow-visioned opponents, along with countless, sometimes contradictory, regulatory revisions in construction and environmental standards, led to delays and higher costs.

Eventually, the costs that protracted legal and regulatory battles entailed began to take a toll. First, the scope of the project was cut back from two units to one. Then, on April 18, 1984, PSNH declared a temporary suspension of construction on Unit 1 because of mounting financial problems. PSNH was eventually to seek protection by filing under Chapter 11 of the U.S. bankruptcy code.

The temporary suspension could well have become a permanent cancellation if UI had not taken a leadership position at this critical juncture. John D. Fassett, who was at the time UI's Chairman and Chief Executive Officer, took personal command during the difficult weeks that followed the announcement of the construction suspension. Fassett's firm control effectively calmed the fears of the financial community and kept the project's joint owners unified. He was also instrumental in the formation of New Hampshire Yankee, which was to become Seabrook's management arm for the plant's joint owners. Under Fassett, and with the assistance of Dick Grossi and Jim Crowe, construction was restarted in an orderly fashion.

Construction finally concluded on Seabrook in 1986 and fuel was loaded in October of that year. But, the plant remained idle, trapped in a seemingly hopeless web of regulatory and litigation constraints. It was to be UI's current Chairman and Chief Executive Officer, George Edwards, who would guide the project step-by-step through the labyrinth of legal and political obstructions created almost entirely by the refusal of Massachusetts authorities to participate in emergency planning for the six Commonwealth communities that lie within Seabrook's ten-mile emergency planning zone.

Under the stewardship of Edwards and his team of Senior Vice President Roland Comstock and Vice President Richard Bornemann, UI undertook a major campaign on the federal level to keep the plant's licensing process on course. One-by-one, victories were won in the courts, on the floor of Congress and in regulatory chambers until, finally, on March 1, 1990, the NRC decided to grant Seabrook a license for commercial operation.

In the end, UI customers, along with electric consumers throughout much of New England, are the true beneficiaries. Seabrook represents 1,150 MW (UI's share is 201.3 MW) of desperately needed electric power. The plant is a tribute to the expertise and dedication of the people who designed and built it. Its double containment structure has been rated as the strongest in the world, able to withstand a major earthquake or even the direct impact of a jet aircraft. Its intricate safety in-depth systems protect against any conceivable equipment failures or human errors and provide multiple backups. So ingrained was safety in the consciousness of Seabrook's design engineers that approximately 60 percent of the total construction costs were safety-related.

There have been many heroes in the Seabrook saga, and a good many of them are still affiliated with UI. Seabrook would not be a reality today if it were not for the hard work, vision and unique talents and creativity of UI people. With the tortuous road to full licensing now behind them, many of these people can now turn their considerable talents to the goal of making UI a highly successful and profitable company in the years ahead. We can never forget, however, everything these people did to save Seabrook and help ease the electric supply situation in New England.

The key to success for any business is satisfying its customers. At UI, we not only see it as the key to our success, but necessary for achieving all we want for our shareowners.

As we have already stated, the fundamental way in which UI seeks to satisfy its customers is by providing reliable electric service and by providing maximum value for every dollar spent by our customers.

A couple of decades ago, value was narrowly defined within the electric industry. Basically, from the utility perspective, providing value meant getting the power from generating plants to the consumers' homes or businesses. Any further definition of value was pretty much left up to consumers to define in terms of their individual abilities to utilize the electricity they received.

Twenty years later, the landscape has changed drastically. As energy prices have risen to where they now have a more noticeable impact on household or business budgets, UI, as an energy company, has broadened its definition of value.

No longer does value end at the meter box. It has become an all-encompassing term which includes providing reliable electric service; giving customers enough information in a usable form to allow them to make informed energy decisions; handling promptly and courteously all customer questions and problems; listening to customers, so that we can determine what they really want and need; reviewing our programs and services continually to guarantee that they are up-to-date and helpful; and treating each customer with the attention and respect he or she deserves.

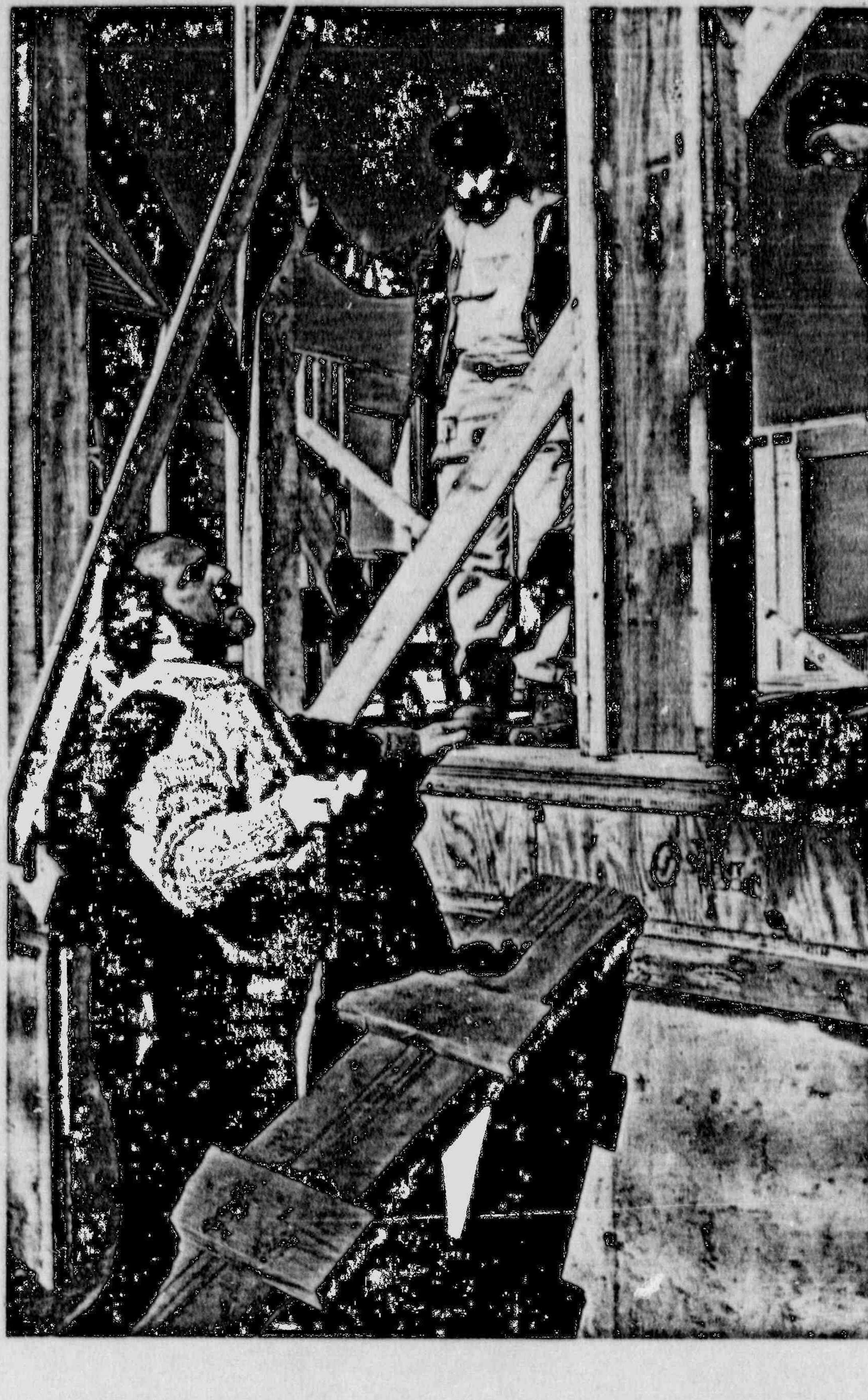
In its broadest sense, value means helping our customers maximize their utilization of our product while minimizing associated costs. Essentially, our goal is to help customers use electricity wisely, efficiently and productively.

The service we render is an important part of the value our customers receive from UI. In order to facilitate their interaction, UI has expanded its energy-related products and services for both residential and commercial/industrial customers.

The centerpiece of our residential effort is our Good Cents program. Good Cents is an umbrella term for a host of conservation programs and energy efficient technologies and building standards all targeted toward helping the consumer gain greater control over electricity usage and costs.

In 1989, the most active component of our effort was the Good Cents Home. Here, UI is working closely with contractors, construction companies and developers in its service area to integrate the very latest in energy efficient design, construction and technology into new home construction. The effort represents the most ambitious undertaking of its kind in Connecticut history.

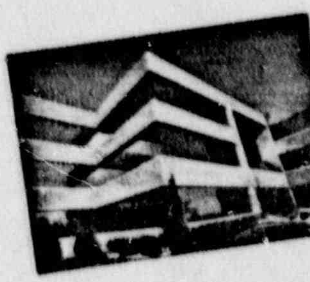
Joe D'Albero, head of the carpentry department at Eli Whitney Vocational-Regional Technical School, gives instruction to students working on UI's Good Cents duplex construction in Hamden.



Our success in gaining the cooperation of developers and builders has substantially exceeded our initial expectations. Last year alone, 740 contracts were signed for new dwellings which will comply with UI's stringent Good Cents standards.

The importance of the program did not escape the attention of top federal officials. United States Senators Joseph Lieberman and Christopher Dodd spoke at ceremonies involving two of our Good Cents model home sites. Each praised UI's initiative in undertaking a program that helps customers save money on their energy bills while addressing the State of Connecticut's stated policy of seeking greater conservation of energy resources.

UI also promoted the utilization of energy efficient appliances and heating and cooling equipment in homes. Our room and central air conditioning tune-up and rebate program allowed 5,152 customers to save money through greater efficiency. In addition, 401 customers took advantage of the Company's Good Cents Heat Pump program. Heat pumps are a cost-efficient alternative to conventional heating and cooling.



The Enterprise II commercial building, Shelton, one of a number of offices utilizing cool storage technology.

The Company also reshaped its working relations with commercial and industrial customers. We believe that value for our business customers means helping them to use electricity in ways that enable them to be more competitive in their own markets. UI does this by working alongside its customers, first, to learn the specifics of their business and then analyzing how, by modifying areas of their operations or utilizing more efficient equipment, they can exercise greater control over their energy expenditures.

Importantly, our involvement does not end at this point. Instead of handing them a report and feeling that we have met our responsibility, we walk them through the whole process, sometimes even helping to secure financing for changes that include finding, installing and even operating new equipment.

These efforts bore impressive results in 1989. Some business customers were able to reduce their energy bills by as much as 15 percent. In one case, UI's leadership was critical to the survival of a manufacturing facility which had been targeted for closure, thus saving not only 420 jobs, but also the revenue the plant contributes to UI.

UI also benefited from efforts that led to a 40 MW reduction in our peak load. This allowed us to sell more power on the wholesale market. In the long run, both customers and Company will benefit from these reductions in another way: namely, through the postponement of the need to build additional generation facilities to meet our load.

Rate design is another tool that UI is employing effectively to enhance customer value. Five years ago, UI began a push toward a rate design philosophy which would give customers the freedom to choose, from a "menu" of different rate options, the best match for their specific circumstances. Our innovative rate packages have had a significant positive impact on lowering peak loads, reducing our customers' bills and also providing an effective inducement to business development in our territory. Moreover, the January 1990 rate decision by the DPUC significantly extended the scope of our menu of options.

Finally, UI is also enhancing both customer and shareowner value by broadening its corporate horizons. The more committed we have become to providing energy-related services to our customers, the more we have come to understand that some of these services can best be enhanced through entities whose primary responsibilities are not the generation, transmission and distribution of electricity. Therefore, the Company has created subsidiaries which, while taking full advantage of UI's technical and financial expertise,

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Chief Operating Officer
Ansonia Copper & Bra
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Vallillo, Director — Sales a
Marketing Developme

The Governme
Center, New Haven. UI w
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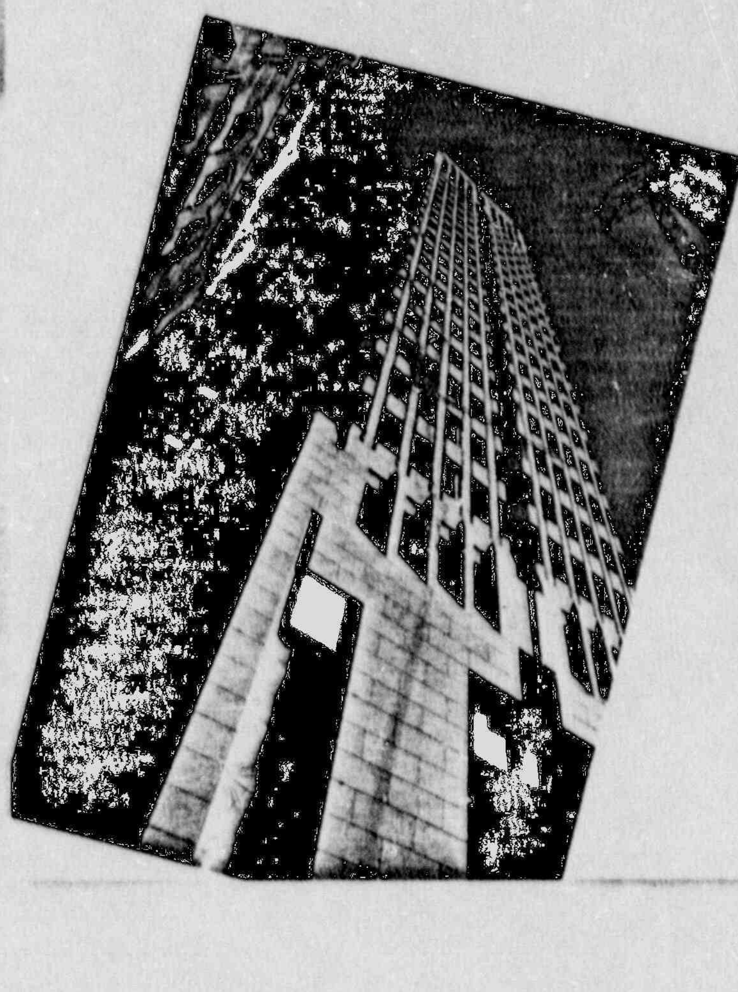


have the freedom to explore emerging new opportunities within the energy marketplace.

In 1989, three subsidiaries were especially active. Souwestcon Properties, Inc. is a partner in a medical hotel being constructed adjacent to UI's corporate headquarters in downtown New Haven. Thermal Energies, Inc. is overseeing the construction of two energy centers and will eventually operate these facilities to provide all the heating and cooling needs of two large office buildings, New Haven's Government Center and Century Tower. A third subsidiary, Precision Power, Inc., has been established to help local businesses address special electrical needs within their premises. By the year 2000, it is projected that a significant portion of total corporate revenues will come from our subsidiaries.

Because in the last analysis, success or failure is determined by customers, we have been gratified by the strong loyalty we have enjoyed from our customer base. Our approval rating in terms of the impression our customers have of the Company climbed steadily through the 1980s, reaching a high of 94 percent favorable last year. This is a rating to be envied by every company, especially those in the electric industry. To us this means that we are on the right track and that our dedication to our customers is being recognized and appreciated.

Corporate commitment encompasses two areas at UI. First, to be a friend and partner in the communities we serve and second, to maintain constructive working relationships with regulators, elected officials and key decisionmakers at local, state and federal levels.

We are dedicated to fulfilling our obligations in these areas, because we feel a sincere social responsibility to the people and institutions in our service territory, and because we are convinced that maintaining positive relationships with our constituencies is an essential ingredient in our overall effort to provide service and value. We cannot succeed unless they succeed. The future welfare of UI is inextricably linked to the welfare of the communities we serve.

On both counts, 1989 was an exceptional year. In terms of social commitment, UI directed a great deal of attention to the issue of drug and alcohol abuse and embarked on a number of initiatives directed at mobilizing community support for confronting the problem.

Substance abuse is a cancer eating away at the health of our society. It threatens nearly everything we hold dear...our families, education, economy and the quality of our life in general. Moreover, it is a problem that has grown so in magnitude that government by itself can no longer be expected to develop and implement all the solutions. Any effective response must be multi-dimensional, calling on the strengths and resources of both public and private parties.

This past year, UI teamed up with New Haven's ABC television affiliate, WTNH, in a year-long series of programs chronicling the many different faces of substance abuse. UI Chairman and Chief Executive Officer George Edwards personally appeared in four UI-produced television commercials on the subject, which were broadcast repeatedly throughout the year. We also made available, through a "hot-line" number, an informative booklet about how and where to seek help for friends or relatives with substance abuse problems.

• UI also hosted an organizational meeting of "Drugs Don't Work," which is the Connecticut Governor's own program designed to bring business and government together to fight the problem. In addition, we sponsored "Dribble Against Drugs," an effort which brought professional basketball players to Bridgeport to serve as positive role models to boys susceptible to negative peer pressures. The Company also participated in the "Youth At Risk" program by sponsoring a young person at an intense two-week camp for teenagers with significant drug and behavioral problems.

Hamden Mayor John Carusone and UI's John Nutcher, Manager of Business Services inspect construction progress in the town's hardest hit area

A Hamden resident pours through the wreckage of her home destroyed by July's violent storm.

So comprehensive was UI's total involvement, both internally and externally, that the Company was singled out by the Connecticut Legislature and given a special citation for its superlative efforts in combatting substance abuse. State Senator Gary Hale of the 17th District, which includes part of UI's service territory, was instrumental in our gaining the recognition and has been a strong partner with the Company on many social, energy and economic issues.

It is a credit to the commitment to social responsibility of both UI's executive management and its employees that, while substance abuse was given special attention in 1989, participation in other social programs also reached new heights.

For many years, the Company has been at the forefront of efforts to help customers at the lower end of the economic scale cope with their energy bills. In 1989, UI customers, bolstered by a matching grant from the Company, established a new record for contributions to Operation Fuel, the statewide energy assistance program. The combined total of $123,078 exceeded our previous high recorded in 1988.

In addition, UI continued to administer the Southern Connecticut Action Team (SCAT) program. SCAT is a public-private partnership which provides state funds for the weatherization of qualifying households. Since 1984, 565 dwellings have been weatherized through the SCAT program.

George W. Edwards, UI's Chairman and CEO, takes a break from filming a drug abuse commercial to talk to children.

UI continued its full support of United Way. Both employee and corporate donations set new highs, with the total of $242,863 representing nearly a 7 percent increase over our 1988 record. The Company also coordinated a "Scouting for Food Drive" for a local council of the Boy Scouts, which provided tons of canned goods for area food banks.

Again this past year, the Company worked with groups and organizations throughout its service territory on programs to help senior citizens, disabled persons and the economically disadvantaged. UI's educational services program, recognized as one of the best of its kind in the nation, offered energy curricula

UI supported the "Youth At Risk" program in 1989.

and support for students in kindergarten through 12th grade in 21 school districts. In addition to its energy components, the Company's "Adopt-a-School," Black History, Mini-Grant, Ocean Classroom and other programs have gained the respect of educators throughout the region.

UI's dedication to social responsibility is equaled in intensity by its commitment to nurture and maintain those relationships which help create an operating and regulatory atmosphere conducive to providing excellent service and value. There is really only one way for this commitment to be played out successfully, and that is by working closely with regulators, elected and government officials, key decision-makers and opinion leaders and other important constituents. Our objective is to work one-on-one with these people to learn more about their needs and agenda, so that we can help develop programs which satisfy both their mandates and our goals.

While UI has been pursuing this course actively for the past five years, it was in 1989 that our labors really began to bear fruit. Certainly, the negotiated agreement regarding our Seabrook investment, discussed earlier in this Report, stands as a prime example. UI could not have reached agreement with the state's Attorney General, the Consumer Counsel and the Prosecutorial Division of the DPUC if it had not already established a foundation of mutual respect and trust. Besides paving the way for the final resolution of issues involving the Company's Seabrook investment, the agreement directly saved customers and shareowners an estimated $10 million in avoided regulatory and litigation costs.

The positive reaction of public officials and customers throughout our service territory to the agreement and subsequent rate case decision also evidences the extraordinarily high regard in which UI is held. They have come to recognize UI's commitment to this region and, in turn, have publicly supported our efforts to insure continued exceptional electric power service...even when that means higher rates.

Expressions of public support were also freely given during and after the restoration effort which followed last July's violent storm. Power outages that persist for an extended period can severely test the patience of community officials responsible for public welfare. This instance had the potential of being particularly volatile, because so many people lost their homes and most of their possessions.

All this makes the overwhelmingly positive support UI received all the more impressive. Impressive, but not surprising, because UI people had already established strong relationships with community officials and stayed in continuous contact with them throughout the difficult ordeal. Furthermore, after full power was restored, we did not walk away. We stayed on to help rebuild the most devastated areas.

UI representatives attend all the aldermanic and common council meetings in the principal cities in the Company's franchise area; they meet regularly with elected officials in all 17 municipalities; they work on the state level, paying particularly close attention to legislative initiatives that pertain to energy, business development and the economy; and they interact with regulators and public interest groups to develop joint efforts in support of state energy policy. In short, UI is always there and willing to help. Our goal is always to be part of the solution, not part of the problem.

The ultimate beneficiaries of our many involvements are UI's customers and shareowners. Taking an active positive interest in the affairs of many of our key constituencies serves to strengthen our business. For customers, a stronger UI means maximum value-added service. For shareowners, a stronger UI means a greater return on their investment.

That's the way it should be and, with United Illuminating, that's the way it will always be.

UI-sponsored Ocean Classroom program.

Stephen F. Goldschmidt
Vice President
Planning

Robert H. Hyde
Vice President
Customer Services

James F. Crowe
Senior Vice President
Marketing

David W. Hoskinson
Senior Vice President
Operations

Albert N. Henricksen
Vice President
Engineering

Charles W. Cook, Jr.
Senior Vice President
Corporate Development

Richard J. Grossi
President and
Chief Operating Officer

Harold J. Moore, Jr.
Vice President
Human Resources

E. Jon Majkowski
Vice President
Public Affairs

Roland W. Comstock
Senior Vice President
Corporate Affairs

Richard H. Bornemann
Vice-President
Governmental Affairs and
Corporate Communications

William A. Elder
Treasurer

James L. Benjamin
Controller

Robert L. Fiscus
Executive Vice President and
Chief Financial Officer

Mary Ellen Manthey
Corporate Secretary

Albert Harary
Vice President
Management Services

Leon A. Morgan
Senior Vice President
Finance and Accounting

F. Patrick McFadden, Jr.
Chairman of the Board and Chief Executive Officer, The Bank of New Haven and BNH Bancshares, Inc.

George W. Edwards, Jr.
Chairman of the Board and Chief Executive Officer, UI

Norwick R. Goodspeed
Chairman of the Board, People's Mutual Holdings

Richard J. Grossi
President and Chief Operating Officer, UI

John F. Croweak
Chairman of the Board, President and Chief Executive Officer, Blue Cross & Blue Shield of Connecticut, Inc.

Betsy Henley-Cohn
Chairman of the Board, Joseph Cohn & Son, Inc., and President, Atlantic Floor Company, Inc.

J. Hugh Devlin
Advisory Director, Morgan Stanley & Co., Inc.

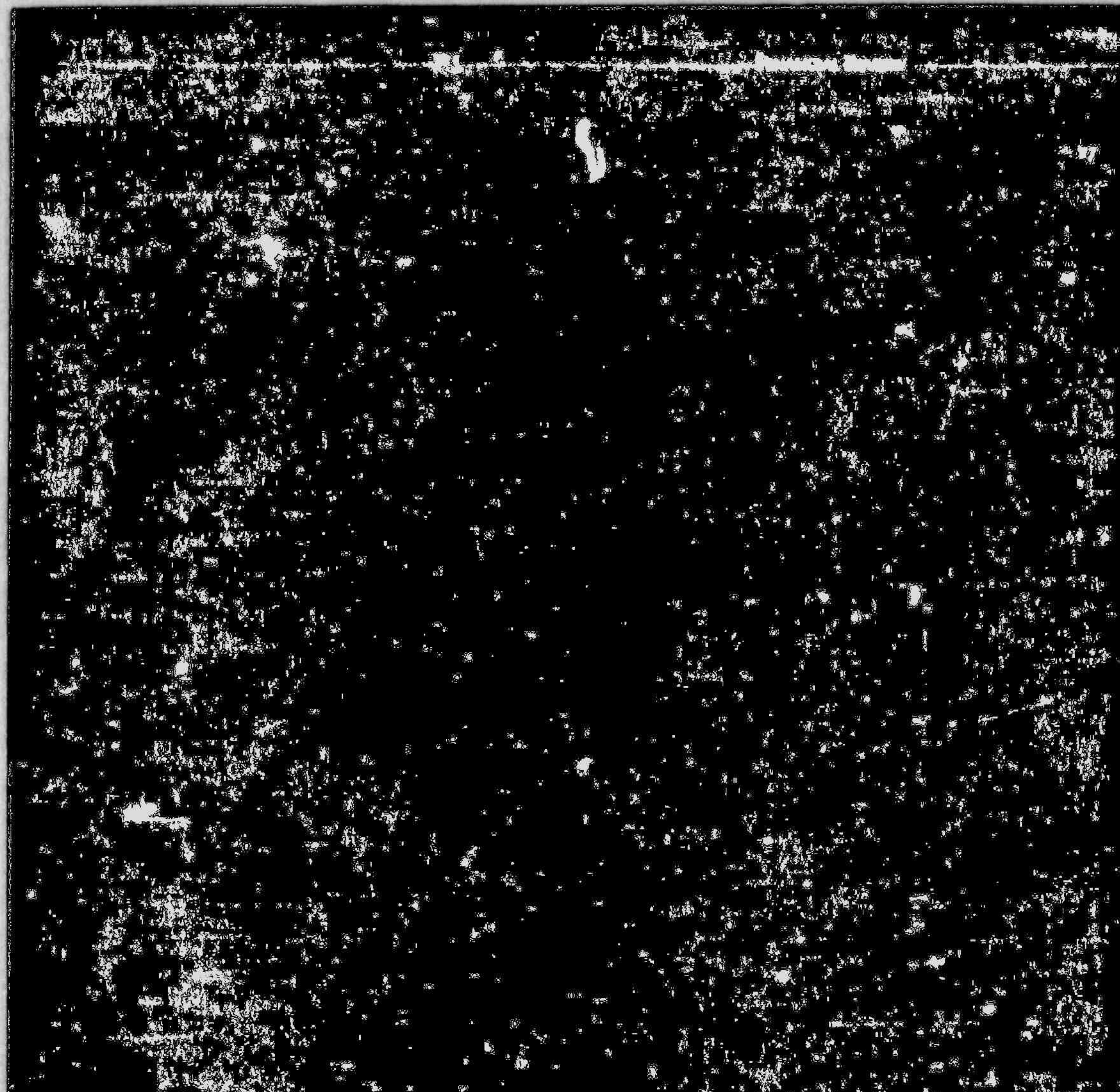
J. Robert Gunther
Chairman of the Board, George Schmitt & Co., Inc. and President, Palmas Printing Company

William S. Warner
Chairman of the Board, The Hydraulic Company

Frank R. O'Keefe, Jr.
President, Long Wharf Capital Partners, Inc.

Leland W. Miles
President Emeritus, University of Bridgeport

John D. Fassett
Former Chairman of the Board, UI



Ten-Year Summary Of Selected Financial And Statistical Data

	1989	1988	1987
Kilowatt-Hour Sales (000)			
Residential	1,883,363	1,870,318	1,780,333
Commercial	2,254,099	2,174,200	2,046,289
Industrial	1,109,119	1,186,336	1,236,151
Other	60,427	61,303	62,246
Total	5,307,008	5,292,157	5,125,019
Financial Results (000)			
Sales of electricity — Residential	$ 205,183	$ 200,170	$ 188,740
Commercial	219,852	208,801	195,972
Industrial	92,855	96,665	100,354
Other	9,943	9,732	9,480
Other operating revenues	3,348	3,570	3,077
Total operating revenues	531,181	518,938	497,623
Operating expenses, excluding income tax expense	309,429	360,998	361,586
Income tax expense (credit)	37,963	44,045	50,633
Allowance for funds used during construction	65,443	75,656	81,419
Net effect of SFAS No. 90	(152,147)	(32,914)	(86,528)
Other income	33,540	24,093	26,282
Interest charges	113,975	102,091	97,028
Net income (loss)	(73,350)	78,639	8,649
Preferred and preference stock dividends	8,233	11,348	11,953
Income applicable to common stock	$ (81,583)	$ 67,291	$ (3,304)
Capitalization (000)			
Long-term debt	$ 887,551	$ 865,954	$ 796,226
Preferred and preference stock			
Not subject to mandatory redemption	70,000	70,000	70,000
Subject to mandatory redemption	—	34,000	40,000
Common stock equity	362,584	473,674	438,564
Total	$ 1,320,135	$1,443,628	$1,344,790
Common Stock			
Number of shares outstanding at year-end	13,887,748	13,887,748	13,887,748
Average number of shares outstanding	13,887,748	13,887,748	13,887,654
Earnings (loss) per share (a)			
Before effect of SFAS No. 90	$5.08	$7.22	$5.99
After effect of SFAS No. 90	$(5.87)	$4.85	$(.24)
Dividends declared per share	$2.32	$2.32	$2.32
Book value per share	$26.11	$34.11	$31.58
Shareowners — Total	24,866	26,713	28,157
In Connecticut	11,741	12,482	13,265
In Company territory	7,391	7,827	8,301
General			
Peak load — kilowatts	1,094,400	1,132,100	1,039,600
Generating capability at year-end — kilowatts (b)	1,257,610	1,256,710	1,240,500
Number of customers	307,654	307,237	303,794
Kilowatt-hours per residential customer	6,814	6,804	6,562
Number of employees	1,627	1,620	1,604
Total payroll (000)	$ 65,175	$ 62,387	$ 57,207
Total taxes (000)	$ (37,732)	$ 66,714	$ 33,224
Utility plant at year-end (000)	$ 1,725,936	$1,834,271	$1,718,300
Gross property additions (000)	$ 142,485	$ 159,391	$ 154,672
Total assets at year-end (000)	$ 2,188,239	$2,365,063	$2,178,002

(a) Earnings per share based on the average number of shares outstanding.
(b) Represents maximum dependable net load-carrying ability during the winter period for New England Power Pool purposes, including UI's share of capacity in Connecticut Yankee Atomic Power Company (55,770 KW).

	1986	1985	1984	1983	1982	1981	1980
	1,700,302	1,654,591	1,642,564	1,637,581	1,593,854	1,611,212	1,660,353
	1,914,889	1,810,192	1,729,027	1,657,518	1,578,433	1,551,228	1,568,638
	1,232,209	1,286,402	1,314,328	1,255,824	1,232,942	1,315,172	1,415,274
	65,533	68,064	71,998	71,085	69,935	70,299	70,813
	4,912,933	4,819,249	4,757,917	4,622,008	4,475,164	4,547,911	4,715,078
	$ 178,268	$ 190,880	$ 185,209	$ 16[illegible],350	$ 161,237	$ 164,595	$ 133,763
	180,888	192,058	187,112	163,458	156,902	157,386	122,904
	99,939	118,637	124,118	107,724	106,788	117,624	98,303
	9,516	10,367	10,664	9,771	9,652	9,613	7,697
	2,508	2,394	2,367	2,283	2,151	1,804	1,455
	471,119	514,036	509,470	449,586	436,730	451,022	364,122
	333,651	368,260	400,773	356,380	353,070	386,279	328,253
	51,419	62,047	44,371	37,746	31,81[illegible]	22,454	(387)
	78,044	62,623	57,242	52,407	40,349	28,113	27,555
	(69,785)	3,400	(19,889)	—	—	—	—
	28,290	29,755	19,083	13,981	8,595	9,040	710
	90,833	77,402	52,351	41,345	35,039	29,904	30,055
	31,765	103,005	68,411	80,503	65,755	49,538	34,466
	18,969	20,339	16,883	14,084	14,084	12,351	9,296
	$ 12,796	$ 82,666	$ 51,528	$ 66,419	$ 51,671	$ 37,187	$ 25,170
	$ 680,215	$ 668,315	$ 571,403	$ 394,115	$ 373,015	$ 303,648	$ 295,581
	70,000	70,000	70,000	70,000	70,000	70,000	70,000
	63,000	96,000	90,000	65,000	65,000	65,000	45,000
	476,108	493,261	434,030	408,331	319,720	262,198	222,861
	$1,289,323	$1,327,576	$1,174,433	$ 937,446	$ 827,735	$ 700,846	$ 633,442
	13,886,566	13,720,050	13,429,443	12,972,344	10,693,605	9,154,578	7,660,132
	13,827,431	13,623,093	13,213,526	11,708,570	9,579,312	8,775,667	7,061,241
	$5.97	$5.82	$5.41	$5.67	$5.39	$4.24	$3.56
	$.93	$6.07	$3.90	—	—	—	—
	$2.32	$2.08	$2.30	$3.08	$2.92	$2.76	$2.68
	$34.29	$35.95	$32.32	$31.48	$29.90	$28.64	$29.09
	29,888	35,426	38,848	41,067	39,213	37,868	36,447
	14,008	15,606	16,774	17,862	17,750	17,765	18,372
	9,282	10,056	13,539	13,742	13,439	11,815	12,456
	985,710	1,019,980	998,910	969,500	951,700	949,100	971,100
	1,239,530	1,197,150	1,229,440	1,235,850	1,235,850	1,281,050	1,299,360
	298,484	294,320	290,591	287,370	284,586	282,890	280,800
	6,356	6,265	6,293	6,336	6,213	6,312	6,545
	1,576	1,501	1,559	1,569	1,517	1,514	1,481
	$ 52,782	$ 49,150	$ 46,911	$ 44,114	$ 40,310	$ 35,581	$ 31,653
	$ 38,724	$ 86,038	$ 62,122	$ 66,300	$ 64,319	$ 54,510	$ 34,777
	$1,681,986	$1,555,883	$1,385,672	$1,274,477	$1,080,810	$ 922,734	$ 830,034
	$ 194,168	$ 179,528	$ 210,378	$ 197,412	$ 167,924	$ 115,540	$ 98,413
	$2,155,251	$1,638,519	$1,466,704	$1,179,409	$ 982,852	$ 836,508	$ 739,027

Major Influences on Financial Condition

The Company's financial condition has been heavily influenced by both the size and the cost of financing its accumulated investment in the construction of Seabrook Unit 1, a nuclear generating unit in Seabrook, New Hampshire, in which the Company has a 17.5% ownership share. To the extent that this investment has not been included in rate base, cash recovery applicable to the investment has been limited to the income tax benefits of construction. However, from an earnings standpoint, the cost of financing construction balances has been offset by a non-cash credit to allowance for funds used during construction (AFUDC).

The Company's primary financial concerns have been the achievement of commercial operation status for Seabrook Unit 1 and, more particularly, obtaining a Connecticut Department of Public Utility Control (DPUC) rate decision that will permit a return on, and recovery of, UI's investment in this unit.

On July 6, 1989, the Company reached a settlement agreement with Connecticut officials representing the public regarding the Company's recoverable investment in Seabrook Unit 1, amounting to $640 million, and the resolution of all outstanding Seabrook-related issues, assuming that the unit achieves commercial operation by the end of 1990. This agreement, which was approved by the DPUC on August 23, 1989, provided for moderate rate increases over the years 1990 through 1992 totaling between 5% and 11%.

On September 1, 1989, the Company filed a rate application in accordance with the agreement, requesting base rate increases of 5%, 3% and 3%, effective for the years 1990, 1991 and 1992, respectively. The DPUC commenced hearings on the rate proposal on November 20, 1989 and, in a decision dated January 24, 1990, granted base rate increases of 3.72%, 2.69% and 2.53% for the three years. These increases are designed to raise revenues by $22.1 million in 1990, $16.9 million in 1991 and $16.7 million in 1992. While the rate increases granted were based on a 12.9% return on equity, the Company is authorized to earn up to a 13.9% return on equity under the terms of the settlement agreement. The DPUC decision also provides, among other things, for phasing-in the Company's recoverable Seabrook investment into rate base over a 5-year period commencing January 1, 1990, for recovery of deferred phase-in costs during the subsequent 5-year period consistent with Statement of Financial Accounting Standards No. 92 (SFAS No. 92), "Regulated Enterprises — Accounting for Phase-in Plans," for rate design changes designed to encourage energy conservation, and for a sales adjustment clause designed to compensate for deviations from forecast sales levels, within prescribed limits and subject to DPUC approval. The decision permits the Company to retain the benefits of wholesale power sales above prescribed levels, and allows the Company to capitalize conservation projects. These capitalized conservation investments will be allowed to earn a premium return of up to 3% over the Company's weighted cost of capital.

Since the recoverable investment in Seabrook Unit 1 is less than the Company's share of Connecticut's statutory recoverable cost "cap", the settlement agreement required an additional write-down of the Company's investment in Seabrook Unit 1 in August 1989. This write-down was necessary in order to comply with SFAS No. 90, "Regulated Enterprises — Accounting for Abandonments and Disallowances of Plant Costs," which the Company adopted in 1988, and resulted in a net loss for the year 1989. However, by resolving outstanding issues and quantifying future cost recoveries within acceptable ranges, the agreement permits UI to plan effectively for the future.

While construction of Seabrook Unit 1 is complete and a 40-year conditional operating license has been received from the Nuclear Regulatory Commission (NRC), the resolution of issues related to the off-site emergency response plans for the emergency response and evacuation planning zone surrounding the plant continues to prevent the unit from achieving commercial operation status. Primarily as a result of the delay in resolving emergency response plan issues, Public Service Company of New Hampshire (PSNH), which holds the largest ownership interest in the Seabrook project, has had to seek protection under Chapter 11 of the Bankruptcy Code. Although the bankruptcy court has approved PSNH's continuing participation in the Seabrook project, and the NRC has issued a low-power license and low-power testing has been completed, the Company cannot predict at this time what impact these bankruptcy proceedings may have on the remaining NRC licensing proceedings and if or when commercial operation of the unit will be permitted. In any event, primarily as a result of the delay in resolving emergency response plan issues, the unit is not likely to achieve commercial operation prior to the second quarter of 1990.

Liquidity and Capital Resources

At the beginning of 1989, the Company had $60 million of cash and temporary cash investments. During 1989, operating activities provided net cash of $73 million. Financing activities provided $70 million from short-term borrowings and new long-term debt, but required the use of $87 million principally for dividend payments, preferred stock redemptions and net lease obligation transactions. Cash available after the net addition of $56 million from operating and financing activities for the period was $116 million. Plant investment required $77 million of these resources, leaving a cash balance of $39 million at December 31, 1989.

The Company has had a revolving credit agreement with a group of banks since 1984. On April 15, 1989, the Company reduced the borrowing limit of the revolving credit agreement then in effect from $160 million to $100 million. This agreement was replaced by a new $100 million revolving credit agreement on December 21, 1989. The new agreement, which currently extends to October 30, 1990, affords the banks an opportunity to decline to lend funds if any one of several conditions is not satisfied at the date of a requested borrowing. The conditions include, among others, the absence of a determination by the banks that the PSNH bankruptcy proceedings have increased the risk that the Company will not be able to perform its obligations under the agreement.

The Company has sale and leaseback arrangements with a financial institution providing for nuclear fuel financing up to $70 million for Seabrook Unit 1 and up to $10 million for Millstone Unit 3. Under these arrangements, the Company is paying rent for the Millstone Unit 3 fuel based on the direct costs to the lessor of the fuel, plus the lessor's financing costs. In addition, a fuel reserve and supply agreement with the same financial institution provides for financing fossil fuel purchases up to an aggregate of $165 million, less the outstanding nuclear fuel lease obligations and all other outstanding obligations to the financial institution. The $165 million aggregate limit on all outstanding obligations to the financial institution will decrease to $135 million on March 16, 1990 unless Seabrook Unit 1 has, by then, received a full-power operating license and made satisfactory progress towards achieving commercial operation. The term of the fuel reserve and supply agreement extends to December 31, 1990. At December 31, 1989, approximately $74 million of nuclear fuel and $28 million of fossil fuel purchases, includi coal, were being financed under these arrangements. On April 29, 1987, the Company entered into a lease with the same financial institution providing for the financing of $3.7 million, representing the purchase price and capitalized carrying charges of real property on which the Company plans to construct a service center facility. On September 26, 1988, the Company entered into a revolving credit agreement with the same financial institution. This revolving credit agreement enables the Company to borrow up to $45 million until August 31, 1990, for general corporate purposes and within the aggregate $165 million limit on all outstanding financing obligations to the financial institution. The financial institution may decline to lend funds under the revolving credit agreement if any one of several conditions is not satisfied at the time of a requested borrowing.

The Company presently estimates that its capital requirements will exceed its net cash provided by operating activities for the next several years. All of the excess capital requirements will have to be provided by external financing, and there is no assurance that such financing can be effected. The Company's ability to incur additional indebtedness will be restricted by the earnings coverage provision of the Trust Indenture under which the Company has issued all of its long-term Debentures. The absence of a return on the disallowed portion of the Company's Seabrook Unit 1 investment and the increased depreciation charges against income related to Seabrook Unit 1 can be expected to cause the Company's earnings for the next several years to fall below the interest coverage level specified in the Trust Indenture as a prerequisite to any increase in short-term or long-term indebtedness (except for $2 million of short-term borrowings incurred for operating expense purposes, and except for borrowings which are expressly subordinated to the Company's Debentures and are limited to an aggregate amount not exceeding 10% of the Company's debt limit under the Trust Indenture — 62½% of the cost of the Company's properties less depreciation thereon (the Company's debt limit under the Trust Indenture was $1.024 billion at December 31, 1989)). The Company estimates that its aggregate capital requirements will exceed cash provided by operations by $295 million during this period. The Company expects to meet these requirements by a combination of pre-financing, subordinated borrowings and financings that are not subject to the Trust Indenture's restrictions. However, there is currently no assurance that this expectation will be met.

The Company has formed several subsidiary companies for the purpose of entering into nonutility, power-related business ventures which will complement and enhance its electric utility business and serve the interests of the Company and its shareholders and customers. The Directors of the Company have authorized the investment of up to $10 million in one or more subsidiary or affiliated corporations for this purpose.

Results of Operations

Due to non-cash write-offs in March, June and August 1989, to recognize reductions in the recoverable cost of Seabrook Unit 1, the Company incurred a loss of $5.87 per share for the year 1989, as compared to earnings per share of $4.85 for 1988. The largest of such write-offs, $8.08 per share, was recorded in August 1989 to reflect disallowances due to a reduction in the recoverable amount of the Company's investment in Seabrook Unit 1 and other provisions of the Seabrook Settlement Agreement.

Earnings per share for 1989, before giving effect to the write-offs that resulted from the adoption in 1988 of SFAS No. 90, were $5.08 per share, a decrease of $2.14 from 1988. This decrease was due principally to higher fuel and energy costs, higher maintenance expense, lower non-cash allowance for funds used during construction and non-cash charges that were ordered by the DPUC to reduce UI's projected 1989 regulated earnings to the 16.4% level authorized in its last rate decision in 1984 without affecting current revenues or cash flows. In accordance with this DPUC order, in 1989 the Company wrote off a total of $14.8 million, consisting of bond repurchase premiums amounting to $4.6 million, net of income taxes, and $10.2 million of additional depreciation charges related to Millstone Unit 3.

Earnings per share for 1988, before giving effect to changes arising from the adoption of SFAS No. 90, were $7.22 per share, an increase of $1.23 over 1987. This increase was due principally to higher kilowatt-hour sales, higher capacity sales, lower income taxes and the absence of additional depreciation and other non-cash charges recorded in 1987.

Kilowatt-hour sales for both 1989 and 1988 increased over prior years, due to improved commercial activity and higher residential use; but the effect of substantial decreases in industrial activity in both years limited the net increases to less than 1% in 1989 and 3.3% in 1988.

Operating revenues for 1989 and 1988 increased by $12.2 million and $21.3 million, respectively, over the prior years, due to higher sales volume and higher fossil fuel and energy costs which were passed on to customers through the fossil fuel adjustment clause. The more modest increase for 1989 reflects relatively moderate summer weather compared to the prior years.

Fuel and interchange energy expense in 1989 increased over 1988, due to higher kilowatt-hour sales and an increase in purchases of power generated by a regional waste-burning facility at prices considerably higher than the Company's average cost per kilowatt-hour. Reduced availability due to scheduled outages for overhaul of the Company's two most efficient fossil-fired generating units also contributed to higher energy costs in 1989. Fuel and interchange energy expense in 1988 increased over 1987, due primarily to higher kilowatt-hour sales and increased purchases of power from the regional waste-burning facility, which more than offset reductions due to the benefits of continuing operating efficiencies and increased nuclear generation.

Other operation and maintenance expenses increased in 1989 over 1988, due principally to a non-recurring expense of $3.5 million to replace defective building siding at a generating station, storm damage repair expense of $2.7 million, and higher payroll costs. Other operation and maintenance expenses increased in 1988 over 1987, due principally to higher payroll costs.

Depreciation expense increased in 1989 over 1988, due primarily to the additional Millstone Unit 3 depreciation charges recorded pursuant to the DPUC's order of February 22, 1989. Depreciation expense decreased in 1988 from the 1987 level, due primarily to the absence in 1988 of the additional depreciation for Millstone Unit 3 recorded in 1987 as a result of stipulated earnings agreements approved by the DPUC.

Income taxes charged to operating expense decreased in 1989 compared to 1988, principally as a result of lower taxable income. The decrease in 1988 income tax expense from the 1987 level was due principally to a lower tax rate.

The allowance for equity funds used during construction decreased in both 1989 and 1988 below the preceding years, due primarily to lower rates and lower CWIP balances in both years resulting from SFAS No. 90 write-downs.

Other income and deductions, excluding the allowance for equity funds used during construction, increased in 1989 over 1988, mainly as a result of Seabrook Unit 1 investment tax credits of $21.7 million that were recorded as income in accordance with the terms of the Seabrook Settlement Agreement that more than offset deductions which included primarily the write-off of Seabrook prudence audit expenses. The increase in 1988 over 1987 was due to higher interest income as a result of higher average balances in temporary cash investments.

Other interest charges increased in 1988 over the prior year, due primarily to the amortization of bond redemption premiums. In 1989 the increase in other interest charges primarily reflects the accelerated amortization of bond redemption premiums pursuant to the DPUC's order of February 22, 1989.

Dividends on preferred stock decreased in 1989 by $3.1 million and in 1988 by $605,000 as a result of redemptions. These redemptions were made as part of the Company's program of refinancing high cost securities at lower rates.

Outlook

In recent years, the Company's earnings have included a large amount of AFUDC. As a result of the January 24, 1990 rate decision and beginning January 1, 1990, the Company's Seabrook Unit 1-related AFUDC will decline to a level reflecting a deferred return on the portion of the recoverable Seabrook Unit 1 investment that is excluded from rate base due to the phase-in plan. Concurrently, the Company's earnings will begin to reflect the recovery of the investment in Seabrook Unit 1 through increased charges to customers resulting from the base rate increases allowed by the DPUC.

The Company's financial condition will be heavily influenced by the timing of commercial operation of Seabrook Unit 1. The achievement of commercial operation of Seabrook Unit 1, which will trigger the commencement of significant additional wholesale power sales, is chiefly dependent on events that are largely beyond the Company's control, especially the timely and successful resolution of a proceeding in which the NRC is considering objections to off-site emergency response and evacuation plans for the unit's emergency response and evacuation planning zone. While there have been recent positive developments, including NRC staff recommendations that the plans be approved and a full-power operating license granted, the Company is unable to predict if or when the plans will be finally approved and a full-power license granted, since the NRC proceedings continue to be contested vigorously by opponents of the unit. Nor can the Company predict what impact the proceedings under the Bankruptcy Code by PSNH will have on the NRC operating license proceedings for the unit. However, delays in achieving commercial operation may negatively impact 1990 earnings by deferring the commencement of wholesale power sales that are conditioned on commercial operation of the unit. Moreover, in accordance with the Seabrook Settlement Agreement, a delay of commercial operation beyond 1990 will require that the rate base treatment and rate making provisions of the agreement be renegotiated and, in the event new terms can not be negotiated, will leave those issues for DPUC decision. However, in any event, revenues to which the Company is entitled prior to December 31, 1990 will not be refundable.

The Company's financial condition will also be influenced by the level of success of its efforts to satisfy its external financing requirements for the period when it will be precluded by restrictions in its Trust Indenture from borrowing on an unsubordinated basis. While the Company expects to be able to meet its financing requirements for this period, there is currently no assurance that this expectation will be met.

Although developments with respect to Seabrook Unit 1 can be expected to continue to dominate the Company's financing outlook and plans, such matters are also sensitive to many other factors, including conditions in the securities markets, economics conditions, the level of the Company's sales, and legislative and regulatory developments. The latter include the cost of compliance with increasingly stringent environmental regulations and increased liability for post-retirement employee benefits.

Inflation

As a result of inflation and increased environmental and regulatory requirements, the estimated cost of replacing the Company's productive capacity today would substantially exceed the historical cost of such facilities reported in the financial statements. Since the Company's rates for service to its customers have been based in the past on the cost of providing such service and have been revised from time to time to reflect increased costs of service, the Company believes that any higher replacement costs it may experience in the future will be recovered through the normal regulatory process.

Consolidated Statement of Income
For the Years Ended December 31, 1989, 1988 and 1987

(Thousands except per share amounts)	1989	1988	1987
Operating Revenues	$531,181	$518,938	$497,623
Operating Expenses			
Operation			
Fuel and interchange energy — net	153,919	140,973	131,471
Capacity purchased — net	9,810	6,491	14,449
Other	105,441	102,715	96,045
Maintenance	39,426	30,692	31,855
Depreciation	35,618	24,069	37,160
Amortization of cancelled nuclear projects	10,415	10,415	10,415
Income taxes	37,963	44,045	50,633
Other taxes	44,800	45,643	40,191
Total	437,392	405,043	412,219
Operating Income	93,789	113,895	85,404
Other Income and Deductions			
Allowance for equity funds used during construction	38,968	48,605	54,933
Other — net	13,936	5,011	3,092
Total	52,904	53,616	58,025
Application of SFAS No. 90			
Disallowed plant costs	(217,503)	(50,595)	(125,228)
Accretion of Seabrook Unit 2 disallowed return	4,129	4,419	4,922
Applicable income taxes	61,227	13,262	33,778
Net Effect of SFAS No. 90	(152,147)	(32,914)	(86,528)
Income (Loss) Before Interest Charges	(5,454)	134,597	56,901
Interest Charges			
Interest on long-term debt	91,126	90,022	88,700
Other interest	22,849	12,069	9,228
Allowance for borrowed funds used during construction	(26,475)	(27,051)	(26,486)
Income tax benefits attributable to the allowance for borrowed funds	(19,604)	(19,082)	(23,190)
Net Interest Charges	67,896	55,958	48,252
Net Income (Loss)	(73,350)	78,639	8,649
Dividends on Preferred Stock	8,233	11,348	11,953
Income (Loss) Applicable to Common Stock	$(81,583)	$ 67,291	$ (3,304)
Average Number of Common Shares Outstanding	13,888	13,888	13,888
Earnings (Loss) per Share of Common Stock	$(5.87)	$4.85	$(.24)
Cash Dividends Declared per Share of Common Stock	$2.32	$2.32	$2.32

Consolidated Statement of Retained Earnings
For the Years Ended December 31, 1989, 1988 and 1987

(Thousands of Dollars)	1989	1988	1987
Balance January 1	$201,371	$166,303	$204,947
Net Income (Loss)	(73,350)	78,639	8,649
Premium applicable to redemption of preferred stock	—	—	(2,200)
Expenses associated with preferred stock redeemed	—	(4)	(921)
	128,021	244,938	210,475
Deduct Cash Dividends Declared			
Preferred Stock	7,982	11,348	11,953
Common Stock	32,219	32,219	32,219
Total	40,201	43,567	44,172
Balance December 31	$ 87,820	$201,371	$166,303

The accompanying Statement of Accounting Policies and Notes to Consolidated Financial Statements are integral parts of the financial statements.

Consolidated Statement of Cash Flows

For the Years Ended December 31, 1989, 1988 and 1987

(Thousands of Dollars)	1989	1988	1987
Cash Flows From Operating Activities			
Net Income (Loss)	$ (73,350)	$ 78,639	$ 8,649
Adjustments to reconcile net income to net cash provided by operating activities:			
Depreciation and amortization	68,977	43,781	52,581
Deferred income taxes	(6,154)	4,135	9,998
SFAS No. 90 writeoffs — net	152,147	32,914	86,528
Seabrook prudence audit costs (thru 1988)	21,237	—	—
Deferred investment tax credits — net	(22,758)	(1,029)	3,383
Allowance for funds used during construction	(65,444)	(75,656)	(81,419)
Changes in current assets and liabilities:			
Accounts receivable	(16,865)	(10,360)	(5,794)
Accrued utility revenues	(3,032)	(588)	(1,895)
Fuel, materials and supplies	(4,463)	12	(6,635)
Accounts payable	17,124	(10,487)	13,138
Taxes accrued	663	(652)	(2,175)
Interest accrued	403	11,464	4,509
Other — net	928	6,054	1,116
Changes in noncurrent balance sheets items	3,840	6,084	917
Total Adjustments	146,603	5,672	74,252
Net cash provided by Operating Activities	73,253	84,311	82,901
Cash Flows from Financing Activities			
Common stock	—	—	36
Long-term debt	25,000	170,000	328,500
Lease obligations	(3,040)	16,722	13,856
Securities retired and redeemed, including premiums			
Preferred stock	(37,400)	(6,000)	(25,200)
Long-term debt	(3,667)	(98,667)	(251,727)
Notes payable	45,000	—	(25,675)
Expenses of issues	(1,440)	(4,096)	(3,877)
Dividends			
Preferred stock	(9,597)	(11,485)	(12,696)
Common stock	(32,219)	(32,219)	(32,219)
Net cash provided by (used in) Financing Activities	(17,363)	34,255	(9,002)
Net cash flows from Operating and Financing Activities	55,890	118,566	73,899
Cash Invested in Plant, including nuclear fuel	(77,041)	(83,735)	(73,253)
Cash and Temporary Cash Investments:			
Net change for the period	(21,151)	34,831	646
Balance at beginning of period	59,918	25,087	24,441
Balance at end of period	$ 38,767	$ 59,918	$ 25,087
Cash paid during the period for:			
Interest (net of amount capitalized)	$ 67,656	$ 49,673	$ 46,028
Income Taxes	$ 21,715	$ 14,881	$ 13,341

For cash flow purposes, the Company considers all highly liquid debt instruments with a maturity of three months or less at purchase date to be cash equivalents.

The accompanying Statement of Accounting Policies and Notes to Consolidated Financial Statements are integral parts of the financial statements.

Consolidated Balance Sheet
December 31, 1989, 1988 and 1987

Assets (Thousands of Dollars)	1989	1988	1987
Utility Plant at Original Cost			
In service	$ 894,608	$ 858,702	$ 844,989
Less accumulated provision for depreciation	323,837	297,772	281,779
	570,771	560,930	563,210
Construction work in progress	675,831	812,246	737,169
Nuclear fuel	73,729	74,984	67,539
Plant-related regulatory assets	81,768	88,339	68,603
Net Utility Plant	1,402,099	1,536,499	1,436,521
Other Property and Investments	9,621	8,876	8,493
Current Assets			
Cash and temporary cash investments	38,767	59,918	25,087
Accounts receivable			
Customers, less allowance for doubtful accounts of $2,130, $1,580 and $1,600	54,309	50,665	43,827
Other	24,346	11,125	7,603
Accrued utility revenues	24,912	21,880	21,292
Fuel, materials and supplies, at average cost	24,709	20,246	20,258
Prepayments	3,780	2,436	4,008
Total	170,823	166,270	122,075
Deferred Debits			
Unfunded deferred income taxes	334,292	383,476	338,708
Unamortized cancelled nuclear projects	53,461	59,970	65,710
Unamortized bond redemption costs	31,524	47,996	54,850
Deferred income taxes	176,821	145,771	141,642
Other	9,598	16,205	10,003
Total	605,696	653,418	610,913
	$2,188,239	$2,365,063	$2,178,002

The accompanying Statement of Accounting Policies and Notes to Consolidated Financial Statements are integral parts of the financial statements.

Consolidated Balance Sheet

December 31, 1989, 1988 and 1987

Capitalization and Liabilities (Thousands of Dollars)	1989	1988	1987
Capitalization			
Common stock equity			
Common stock	$ 277,968	$ 277,968	$ 277,968
Capital stock expense	(3,204)	(5,665)	(5,707)
Retained earnings	87,820	201,371	166,303
	362,584	473,674	438,564
Preferred stock			
Not subject to mandatory redemption	70,000	70,000	70,000
Subject to mandatory redemption	—	34,000	40,000
Long-term debt	868,884	862,287	767,559
Total	1,301,468	1,439,961	1,316,123
Noncurrent Liabilities			
Obligations under capital leases	106,831	111,171	94,870
Other	950	800	200
Total	107,781	111,971	95,070
Current Liabilities			
Current portion of long-term debt	18,667	3,667	28,667
Accounts payable	60,077	42,953	53,440
Notes payable	45,000	—	—
Dividends payable	9,243	10,858	10,994
Taxes accrued	22,592	21,929	22,581
Pensions accrued	9,086	7,194	5,751
Interest accrued	27,715	27,312	15,848
Obligations under capital leases	3,015	1,714	1,293
Other accrued liabilities	11,150	10,277	7,102
Total	206,545	125,904	145,676
Deferred Credits			
Customers' advances for construction	3,114	2,840	2,346
Accumulated deferred investment tax credits	21,773	52,125	54,954
Unfunded deferred income taxes	53,902	87,554	86,779
Deferred income taxes	474,593	526,329	466,133
Deferred gain on sale of utility plant	10,437	10,230	2,802
Deferred fossil fuel costs	8,626	8,149	8,119
Total	572,445	687,227	621,133
Commitments and Contingencies	—	—	—
	$2,188,230	$2,365,063	$2,178,002

The accompanying Statement of Accounting Policies and Notes to Consolidated Financial Statements are integral parts of the financial statements.

Accounting Records

The accounting records are maintained in accordance with the uniform systems of accounts prescribed by the Federal Energy Regulatory Commission (FERC) and the Connecticut Department of Public Utility Control (DPUC).

Principles of Consolidation

The consolidated financial statements include the accounts of the Company and its wholly-owned subsidiaries, Bridgeport Electric Company (BEC), United Resources Inc. (URI) and Research Center, Inc. (RCI). Intercompany accounts and transactions have been eliminated in consolidation.

Utility Plant

The cost of additions to utility plant and the cost of renewals and betterments are capitalized. Cost consists of labor, materials, services and certain indirect construction costs, including an allowance for funds used during construction. The cost of current repairs and minor replacements is charged to appropriate operating expense accounts. The original cost of utility plant retired or otherwise disposed of and the cost of removal less salvage are charged to the accumulated provision for depreciation.

Phase-in Plan

The Company is phasing into rate base its allowable investment in Seabrook Unit 1, amounting to $640 million. The phase-in plan allows the Company to record a deferred return on the portion of allowable investment excluded from rate base during the phase-in period. At December 31, 1989 the Company's rate base included $48 million of its allowable investment in Seabrook Unit 1. In accordance with the phase-in plan, commencing January 1, 1990, the Company began phasing in the balance of its allowable investment over a five-year period. Commencing January 1, 1991, the deferred return will be added to rate base at the beginning of each year over a four-year period in the same proportion as the phase-in installment for that year bears to the remainder of the $640 million yet to be phased-in. This phase-in plan, which was approved by the DPUC in a January 24, 1990 rate decision that granted the Company base rate increases for the next three years, is in compliance with Statement of Financial Accounting Standards No. 92 (SFAS No. 92), "Regulated Enterprises — Accounting for Phase-in Plans". The rate decision allows the Company to phase-in $480 million, or 75% of its allowable investment, plus a portion of the deferred return that will be accumulated during 1990 and 1991 into rate base by January 1, 1992. The remaining $160 million of allowable investment plus the remaining accumulated deferred return will be phased into rate base in approximately equal amounts on January 1, 1993 and January 1, 1994. The Company will be allowed to recover the deferred return over a five-year period commencing January 1, 1995.

Allowance for Funds Used During Construction

In accordance with the applicable regulatory systems of accounts, the Company capitalizes an allowance for funds used during construction (AFUDC), which represents the approximate cost of debt and equity capital devoted to plant under construction. In accordance with FERC prescribed accounting, the portion of the allowance applicable to borrowed funds is presented in the Consolidated Statement of Income as a reduction of interest charges, while the portion of the allowance applicable to equity funds is presented as other income. Although the allowance does not represent current cash income, it has historically been recoverable under the rate-making process over the service lives of the related properties. The Company compounds semi-annually the allowance applicable to major construction projects.

Prior to 1987, the Company accounted for the portion of the allowance applicable to borrowed funds on a net-of-tax basis for all construction projects because interest charges associated with construction projects were expensed currently for tax purposes. However, effective January 1, 1987, the Tax Reform Act of 1986 requires the capitalization for tax purposes of interest charges associated with construction projects, except for projects such as Seabrook Unit 1 that were begun prior to March 1, 1986. Therefore, in 1987, 1988 and 1989, AFUDC for Seabrook Unit 1, which accounted for over 90% of the Company's AFUDC in those years, was computed on a net-of-tax basis, and AFUDC for all other projects was computed on a before-tax basis.

AFUDC rates in effect during 1987-1989 are shown below:

	Before-Tax Basis	Net-of-Tax Basis
1987	13.0%	10.25%
1988	12.7%	10.0%
1989	12.3%	9.5%

Depreciation

Provisions for depreciation on utility plant for book purposes, excluding costs associated with the 1984 reconversion of BEC's plant to a dual-fired capability, are computed on a straight-line basis, using estimated service lives determined by independent engineers. One-half year's depreciation is taken in the year of addition and disposition of utility plant, except in the case of major operating units on which depreciation commences in the month they are placed in service and ceases in the month they are removed from service. During the years 1985-1989, depreciation associated with BEC's reconversion costs was computed on an annuity

basis over the original ten-year period that this plant was being leased to the Company by BEC. Commencing January 1, 1990, the reconversion costs will be depreciated on a straight-line basis over a period ending July 2000. The aggregate annual provisions for depreciation for the years 1987, 1988 and 1989 were equivalent to approximately 4.77%, 2.09%, and 4.31%, respectively, of the original cost of depreciable property, as restated for the effect of SFAS No. 90. The aggregate provisions for 1987 and 1989 include one-time increases of $12.5 million and $10.2 million, respectively, in Millstone Unit No. 3 depreciation charges as prescribed in DPUC-approved stipulated earnings agreements in 1987 and in a 1989 DPUC order. These earnings reduction measures were initiated in order to lower the Company's return on Common Stock equity for rate-making purposes without impacting revenues or cash flows. See Note (C), "Rate-related Regulatory Proceedings".

Income Taxes

In accordance with Statement of Financial Accounting Standards No. 96, "Accounting for Income Taxes" (SFAS No. 96), which was adopted in the first quarter of 1988, the Company has provided deferred taxes for all temporary book-tax differences using the liability method. The liability method requires that deferred tax balances be adjusted to reflect enacted future tax rates that are anticipated to be in effect when the temporary differences reverse. In accordance with generally accepted accounting principles for regulated industries, the Company has established assets and liabilities that reflect anticipated future ratemaking effects of deferred tax provisions arising from the implementation of SFAS No. 96. The Company has restated the deferred tax balances in its financial statements for prior periods to reflect the adoption of SFAS No. 96.

Previously, income taxes were accounted for by the deferred method. Under that method, deferred taxes were recognized at current tax rates and regulated enterprises did not record deferred taxes for realized tax benefits when regulators used these benefits to reduce current rates.

The Company has elected to take investment tax credits (ITC) applicable to long-term construction projects on a progress-of-construction basis, which has accounted for the major portion of the ITC generated. For accounting purposes, the Company practices full normalization for all ITC related to recoverable plant investments except for the ITC related to the recoverable plant investment in Seabrook Unit 1. ITC related to nonrecoverable plant investments, i.e. those investments written off in accordance with the provisions of SFAS No. 90, were taken into income when the related SFAS No. 90 write-offs were recorded, while ITC, amounting to approximately $21.7 million, related to the recoverable Seabrook investment was taken into income in 1989 in accordance with the Seabrook Settlement Agreement.

Accrued Utility Revenues

The estimated amount of utility revenues (less related expenses and applicable taxes) for service rendered but not billed is accrued at the end of each accounting period.

Investments

The Company's investment in the Connecticut Yankee Atomic Power Company joint venture, a nuclear generating company in which the Company has a 9[illegible]% stock interest, is accounted for on an equity basis.

Fossil Fuel Costs

The amount of fossil fuel costs that can not be reflected currently in customers' bills pursuant to the fuel adjustment clause in the Company's rates is deferred at the end of each accounting period. Since adoption of the deferred accounting procedure in 1974, rate decisions by the DPUC and its predecessors have consistently made specific provision for amortization and rate-making treatment of the Company's existing deferred fossil fuel cost balances.

Research and Development Costs

Research and development costs, including environmental studies, are capitalized if related to specific construction projects and depreciated over the lives of the related assets. Other research and development costs are charged to expense as incurred.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
(Dollar amounts, except per share amounts, are in thousands unless otherwise indicated)

(A) Capitalization at December 31, 1989

Common Stock Equity (a)		
Common stock, no par value		$ 277,968
Shares authorized	17,500,000	
Shares outstanding at December 31:		
1987	13,887,748	
1988	13,887,748	
1989	13,887,748	
Capital stock expense		(3,204)
Retained earnings (b)		87,820
Total common stock equity		362,584
Preferred and Preference Stock (c)		
Authorized:		
Cumulative preferred stock:		
$100 par value, 1,350,000 shares		
$25 par value, 2,400,000 shares		
Cumulative preference stock:		
$25 par value, 5,000,000 shares		
Outstanding at December 31, 1989:		
Cumulative preferred stock, $100 par value:		
4.35%, Series A, 50,000 shares		5,000
4.72%, Series B, 75,000 shares		7,500
4.64%, Series C, 75,000 shares		7,500
5 5/8%, Series D, 75,000 shares		7,500
7.60%, Series E, 125,000 shares		12,500
7.60%, Series F, 150,000 shares		15,000
Cumulative preferred stock, $25 par value, 8.80%, 1976 Series, 600,000 shares		15,000
Total preferred stock not subject to mandatory redemption		70,000
Long-term Debt (d)		
Long-term debentures:		
4.65%, 1990 Series, due August 15, 1990		15,000
4 7/8%, 1991 Series, due July 15, 1991		10,000
10 1/2%, 1995 Series, due October 1, 1995		150,000
5 3/4%, 1996 Series, due August 15, 1996		15,000
6%, 1997 Series, due June 15, 1997		22,500
7%, 1999 Series, due January 15, 1999		15,000
10 1/4%, 2000 Series, due June 15, 2000		30,000
7 3/4%, 2002 Series, due October 1, 2002		25,000
8 1/4%, 2003 Series, due December 15, 2003		30,000
12%, 2017 Series, due August 1, 2017		100,000
Serial debentures:		
8 1/2%, maturing serially as to $1,667 principal amount on November 15 in each of the years 1990 to 1997, inclusive ($1,667 matured in 198[illegible])		$ 13,333
11%, maturing serially as to $2,000 principal amount on November 15 in each of the years 1990 to 1999, inclusive ($2,000 matured in 1989)		20,000
		445,833
First Mortgage Bonds-Bridgeport Electric Company:		
9.44%, Series B, maturing serially as to $10,800 principal amount on February 15 in each of the years 1995 to 1999		54,000
10.32%, Series C, maturing serially as to $60,000 principal amount on January 15 in each of the years 1993 to 1995		180,000
Other:		
Pollution Control Revenue Bonds:		
14 1/2%, 1984 Series, due October 1, 2009		40,000
14 1/2%, 1984 Series B, due December 1, 2009		28,400
9 1/2%, 1986 Series, due June 1, 2016		7,500
9 3/8%, 1987 Series, due July 1, 2012		25,000
10 3/4%, 1987 Series, due November 1, 2012		43,500
8%, 1989 Series A, due December 1, 2014 (issued in December 1989)		25,000
Long-term bank loans:		
12.9% ($20,000), and 13.1% ($20,000), maturing as to $15,000 in 1992, $15,000 in 1993 and $10,000 in 1994		40,000
		889,233
Unamortized debt discount less premium at December 31, 1989		(1,682)
Total long-term debt		887,551
Less current portion included in Current Liabilities		18,667
Total long-term debt included in Capitalization		868,884
Total Capitalization		$1,301,468

(a) Common Stock

Common stock, no par value, authorized at December 31, 1989, included 400,000 shares reserved for the Company's Employee Stock Ownership Plan (ESOP).

Shares issued during 1989, 1988 and 1987 and increases to the common stock account from the proceeds of these issues were as follows:

	1989		1988		1987	
	Amount	**Shares (000)**	**Amount**	**Shares (000)**	**Amount**	**Shares (000)**
Balance, January 1	$277,968	13,888	$277,968	13,888	$277,932	13,887
Additions resulting from:						
DRP*	—	—	—	—	—	—
ESOP**	—	—	—	—	36	1
Balance, December 31	$277,968	13,888	$277,968	13,888	$277,968	13,888

*The Company purchased on the open market, on behalf of shareholders participating in the Dividend Reinvestment Plan (DRP), 158,474 shares in 1987, 192,152 shares in 1988 and 156,683 shares in 1989.

**Shares contributed to ESOP include additional purchases for the plan on the open market of 9,407 shares in 1987. There were no additions to ESOP in 1988 or 1989, since income tax credits allowable for ESOP ended at December 31, 1987.

Expenses related to the new issuances were charged to capital stock expense.

On January 22, 1990, the Company's Board of Directors approved a stock option plan for officers and key employees of the Company. This plan is subject to both shareowner and DPUC approvals. The plan provides for the awarding of options to purchase up to 750,000 shares of the Company's common stock over periods of from one to ten years following the dates when the options are granted. The exercise price of each option cannot be less than the market value of the common stock on the date of the grant. Options to purchase 596,000 shares of common stock at an exercise price of $30.75 per share have been granted by the Board of Directors to date.

In addition, certain executive officers can earn shares of the Company's common stock based upon the dividend and market performance of the common stock compared to a peer group of electric utilities over four-year periods, under the Company's long-term incentive program. This plan is subject to DPUC approval. The total number of shares of common stock that may be earned under the long-term incentive program is limited to 100,000. No long-term incentive awards have been earned to date.

(b) Retained Earnings Restriction

The indenture under which all of the Company's debentures are issued places limitations on the payment of cash dividends on the common stock of the Company and on the amounts that can be expended to purchase or redeem shares of common stock. However, an amount equal to the Company's retained earnings at December 31, 1989 can be used for the payment of cash dividends and the purchase or redemption of shares of stock, without exceeding these limitations.

(c) Preferred and Preference Stock

The par value of each of these issues was credited to the appropriate stock account and expenses related to these issues were charged to capital stock expense.

On July 15, 1989, the Company redeemed all of the 340,000 shares outstanding of its $100 par value 19% Preferred Stock, 1984 Series, at $110.00 per share, plus accrued dividends to the date of redemption of $4.75 per share. These shares were scheduled for mandatory redemption of 68,000 shares each year, commencing July 15, 1990, at $100.00 per share, plus accrued dividends.

There are no redemption requirements for preferred stock outstanding at December 31, 1989.

Preference stock is a form of stock that is junior to preferred stock but senior to common stock. It is not subject to the earnings coverage requirements or minimum capital and surplus requirements governing the issuance of preferred stock. There were no shares of preference stock outstanding at December 31, 1989.

Shares of preferred stock have preferential dividend and liquidation rights over shares of common stock. Preferred shareholders are not entitled to general voting rights. However, if any preferred dividends are in arrears for six or more quarters, or if some other event of default occurs, preferred shareholders are entitled to elect a majority of the Board of Directors, until all preferred dividend arrears are paid and any event of default is terminated.

(d) Long-Term Debt

On December 20, 1989, the Company borrowed from the Industrial Development Authority of the State of New Hampshire the proceeds of the Authority's issuance of $25 million of tax exempt 8% Pollution Control Revenue Bonds. The net proceeds of approximately $24.5 million were used to reimburse the Company for its share of expenditures, including financing costs, relating to certain pollution control facilities constructed and required for the operation of Seabrook Unit 1.

The aggregate maturities of long-term debt during each of the five years 1990-1994 are: 1990 — $18,667; 1991 — $13,667; 1992 — $18,667; 1993 — $78,667; 1994 — $73,667.

(B) Accounting For Abandonments and Disallowances of Plant Costs and Phase-in Plans

Accounting for Abandonments and Disallowances of Plant Costs

In 1988, the Company adopted Statement of Financial Accounting Standards No. 90, "Regulated Enterprises — Accounting for Abandonments and Disallowances of Plant Costs" (SFAS No. 90), and elected to restate prior

periods. SFAS No. 90 requires that, for completed plant facilities, all costs disallowed for rate-making purposes must be recognized as losses against income as soon as the disallowance becomes probable and can be reasonably estimated. SFAS No. 90 also requires that a loss be recorded for any disallowance of the investment in an abandoned plant facility, and for the disallowance of a return on investment, regardless of the fact that regulators have provided for recovery of the full investment. The loss to be recorded for the disallowance of a return is measured by the difference between the recoverable investment and the present value of such investment. As this difference decreases over the period of recovery of the original investment, the loss is reversed through accretion, which is recognized as income.

Pursuant to SFAS No. 90, the Company recorded losses in 1988 for disallowed costs of its investment in Millstone Unit 3, for the amount by which the Company's investment in Seabrook Unit 1 was then projected to exceed the $832 million Connecticut statutory "cap" on the recoverable construction costs of the unit, and for the disallowance of a return on the recovery of the Company's investment in the abandoned Seabrook Unit 2. These losses were recorded by restating the financial results of prior periods when the write-offs would have been recorded if SFAS No. 90 had been in effect in those periods. In March and June 1989, the Company recorded additional write-offs of $16.1 million and $17.5 million, respectively, net of related income tax effects, to recognize disallowances due to successive extensions, to at least January 1, 1990, of the estimated commercial operation date of Seabrook Unit 1. An additional write-off of $121.2 million, net of related income tax effects, was recorded in August 1989 to reflect the write-down of the Seabrook Unit 1 investment from the statutory "cap" to the allowed recoverable amount of $640 million, as provided in the Seabrook Settlement Agreement, and to recognize the disallowance of a return on the Company's additional $11 million of costs associated with Seabrook Unit 2 for which recovery has not yet been approved. See Note (C) Rate-Related Regulatory Proceedings. The following table illustrates the effect on net income of the SFAS No. 90 write-offs and accretion transactions through December 31, 1989:

Accounting for Phase-in Plans

In order to ease the impact on rates that may result from the addition to rate base of the cost of major new facilities, such additions may be added to rate base by regulatory authorities gradually via a phase-in plan. SFAS No. 92, "Regulated Enterprises -- Accounting for Phase-in Plans", establishes criteria for a phase-in plan and requires, among other things, that costs deferred for future recovery under a phase-in plan can be capitalized for financial reporting purposes only if the rate regulators allow recovery of these deferred costs within a ten-year period of time, and that the percentage increase in rates scheduled under the plan can be no greater than the percentage increase in rates scheduled under the plan for each preceding year. The January 24, 1990 decision of the DPUC implementing the Seabrook Settlement Agreement includes a phase-in plan for recovery of the Company's investment in Seabrook Unit 1 that complies with SFAS No. 92.

(C) Rate-Related Regulatory Proceedings

On October 1, 1986, the DPUC issued a notice that it would conduct a general review of financial and operational results of the State's major public service companies, including UI. UI projected a return on equity, as calculated for rate-making purposes, of over 18% for the year 1987 and offered several alternative ways of reducing its earnings to or below the allowed level of 16.4% without reducing rates and revenues. The DPUC, recognizing UI's cash-flow needs, accepted the concept of non-rate actions to reduce the equity return, and initiated a proceeding to examine the appropriateness of non-cash adjustment actions such as accelerated depreciation of facilities and shorter amortization periods for premium costs associated with redemption of high-cost securities as a means of lowering UI's projected equity return.

As a result of this proceeding, on April 4, 1987, the DPUC approved a stipulated earnings agreement among the Company, the DPUC's Prosecutorial Division, the Division of Consumer Counsel and the Connecticut Attorney General. Under the terms of this agreement, the Company

Years Ended December 31,	1989	1984-1988	Total
(Thousands of dollars)			
Disallowed Costs:			
Millstone Unit 3	$ —	$ (17,472)	$ (17,472)
Seabrook Unit 1	(212,859)	(265,409)	(478,268)
Disallowed Return on Seabrook Unit 2	(4,644)	(34,051)	(38,695)
Total disallowances	(217,503)	(316,932)	(534,435)
Related Income Taxes	62,705	99,213	161,918
Net disallowances	(154,798)	(217,719)	(372,517)
Accretion of Disallowed Return on Seabrook Unit 2	4,129	20,549	24,678
Related Income Taxes	(1,478)	(8,546)	(10,024)
Net accretion	2,651	12,003	14,654
Effect of application of SFAS No. 90 — net	$(152,147)	$(205,716)	$(357,863)

was required to continue its cash conservation practices while reducing its non-cash earnings for 1987 by approximately $16 million through various accounting procedures. Such procedures included the recording of additional depreciation on its ownership interest in Millstone Unit 3, the use of lower AFUDC rates and the write-off against income of issue expenses, including debt discount, associated with certain 1987 long-term debt issuances. The intent of the agreement was to lower the Company's rate of return on common stock equity for 1987 to a level comparable with the average of the electric utility industry, without affecting the level of the Company's cash flow. A condition of the agreement was that if these measures proved to be insufficient to achieve the rate of return prescribed in the stipulated agreement, further adjustments of this nature would be required. Accordingly, on October 29, 1987, the DPUC issued an order requiring the Company to show cause why it should not be ordered to decrease non-cash earnings by an additional $5.6 million, by recording additional depreciation of $4.7 million and by writing off against income debt issue expenses of $900,000 associated with the $43.5 million borrowing from the New Hampshire Industrial Development Authority in November. The Company did not contest this show cause order and in the fourth quarter of 1987 recorded these earnings reductions that were prescribed in a second stipulated earnings agreement among the parties to the earlier agreement.

On February 22, 1989, the DPUC issued a decision in a proceeding that it commenced on October 11, 1988 to investigate the operational and financial status of the Company. The decision ordered the Company to reduce its 1989 return on equity for rate-making purposes to 16.4%, the level authorized in its last rate case in 1984. Accordingly, in 1989, the Company wrote off a total of $14.8 million, consisting of bond repurchase premiums amounting to $4.6 million, net of related income taxes, and $10.2 million of additional depreciation charges related to Millstone Unit 3. In its decision, the DPUC stated that it continues to be sensitive to the need to maintain the Company's financial integrity and therefore had approved earnings reduction measures that did not affect revenues or current cash flows.

On August 23, 1989, the DPUC approved the July 6, 1989 Seabrook Settlement Agreement among the Company and the "Connecticut Public Parties" (consisting of the Connecticut Office of Consumer Counsel, the Connecticut Attorney General and the Prosecutorial Division of the DPUC) on the rate treatment of the Company's 17.5% ownership in the Seabrook nuclear plant. This agreement settled many pending Seabrook-related issues including: termination of the DPUC's prudence audit of the planning and construction of Seabrook Units 1 and 2, the Company's then pending application to increase its rates by approximately 9.3% in 1990 by phasing-in $832 million of its investment in Seabrook Unit 1 over four years, the Connecticut statutory issues relative to an appropriate phase-in period for Seabrook Unit 1, the Company's having excess generating capacity, and the exclusion from rates of revenues equal to Seabrook Unit 1 CWIP revenues collected by the Company since 1983. This agreement also resolved DPUC accounting and tax issues with respect to Seabrook Unit 1 and terminated several DPUC directives in other proceedings and all of the lawsuits pending in the Connecticut Superior Court among the parties and the DPUC. It stipulated that the Company would receive base rate increases to customers totalling between 6% and 11% over the three-year period 1990 through 1992, with the DPUC subsequently determining the actual rate increase for each year, taking into account the appropriate level of financial health for the Company and the effect of the increases on the Company's customers and shareholders. Under the agreement, the amount of the Company's Seabrook Unit 1 investment that can be recovered through customer rates will be limited to $640 million, phased-in to rate base over a five-year period beginning in 1990. The agreement was based on the assumption that Seabrook Unit 1 will attain commercial operation by the end of 1990. If this assumption proves incorrect, the Seabrook Settlement Agreement will be reopened and the appropriate ratemaking and investment recovery treatment for Seabrook Units 1 and 2 for subsequent years will be determined after further negotiations among the parties and determinations by the DPUC. However, during renegotiations, the agreement may be extended up to one year by the DPUC. In any case, revenues to which UI has become entitled prior to December 31, 1990 will not be refundable. The agreement further provides that the Company's rate-making rate of return on Common Stock equity (ROE) during the three years 1990-1992 will be limited to a ceiling of 13.9%, with a floor of 9%. If the actual ROE exceeds 13.9%, the amount of earnings in excess of the ceiling will be applied against deferred revenues related to the Seabrook 1 phase-in. The Company may request additional rate relief if the ROE falls below 9%.

On September 1, 1989, the Company filed a rate application in accordance with the agreement, requesting base rate increases of 5%, 3% and 3%, effective for the years 1990, 1991 and 1992, respectively. The DPUC commenced hearings on the rate proposal on November 20, 1989 and, in a decision dated January 24, 1990, granted base rate increases of 3.72%, 2.69% and 2.53% for the three years. These increases are designed to raise revenues by $22.1 million in 1990, $16.9 million in 1991 and $16.7 million in 1992. While the rate increases granted were based on a 12.9% ROE, the Company is authorized to earn up to a 13.9% ROE in accordance with the settlement agreement. The decision also provides, among other things, for phasing-in the Company's recoverable Seabrook investment into rate base over a 5-year period commencing January 1, 1990, for recovery of deferred phase-in costs during the subsequent 5-year period consistent with SFAS No. 92 criteria, for rate design changes designed to encourage energy conservation, and for a sales adjustment clause designed to compensate for deviations from forecast sales levels, within prescribed limits and subject to DPUC approval. The decision permits the Company to retain the benefits of wholesale power sales above prescribed levels, and allows the Company to capitalize conservation projects. These capitalized conservation investments will be allowed to earn a premium return of up to 3% over the Company's weighted cost of capital.

In recent years, the Company's earnings have included a large amount of AFUDC. As a result of the January 24, 1990 rate decision and beginning January 1,

1990, the Company's Seabrook Unit 1-related AFUDC will decline to a level reflecting a deferred return on the portion of the recoverable Seabrook Unit 1 investment that is excluded from rate base due to the phase-in plan. Concurrently, the Company's earnings will begin to reflect the recovery of the investment in Seabrook Unit 1 through increased charges to customers resulting from the base rate increases allowed by the DPUC.

(D) Income Taxes

Income tax expense consists of:

	1989	1988	1987
Operating expenses:			
Current	$ 25,681	$22,313	$18,536
Deferred:			
Income tax attributable to the allowance for borrowed funds	19,604	19,082	23,190
Alternative minimum tax	4,535	6,913	(10,670)
Accelerated depreciation	5,025	5,308	8,171
Construction overheads	(994)	1,609	1,378
Deferred fossil fuel costs	(208)	(20)	546
Pension costs	(441)	(665)	(636)
Investment tax credits — amortization	(1,029)	(1,029)	(1,091)
Premium on BEC bond redemption	(7,402)	(3,306)	17,532
Cancelled nuclear projects	(3,795)	(6,359)	(3,795)
Gain on sale of utility plant	(520)	—	29
Other — net	(2,493)	199	(2,557)
Total deferred	12,282	21,732	32,097
Total operating income tax expense	37,963	44,045	50,633
Other income and deductions:			
Current	(17,422)	(1,408)	(10,521)
Deferred:			
Investment tax credits	(21,729)	—	—
Other — net	(757)	122	6,859
Total other income and deductions	(39,908)	(1,286)	(3,662)
SFAS No. 90 write-offs:			
Plant abandonment	1,466	1,838	2,047
Construction overheads	(1,013)	(647)	(1,009)
Investment tax credits	(7,594)	(1,800)	(4,353)
Plant disallowances	(54,086)	(12,653)	(30,463)
Total SFAS No. 90 write-offs	(61,227)	(13,262)	(33,778)
Total income tax expense	$(63,172)	$29,497	$13,193

Accumulated deferred income tax assets at December 31:	1989	1988	1987
Plant disallowances	$123,087	$ 69,565	$ 57,474
SFAS No. 96 adjustments	33,139	57,643	64,655
Plant abandonment	4,003	5,615	7,453
Deferred fossil fuel costs	4,520	4,312	4,292
Pension costs	4,060	3,619	2,954
Gain on sale of utility plant	1,637	1,117	1,117
Other	6,375	3,900	3,697
	$176,821	$145,771	$141,642
Accumulated deferred income tax liabilities at December 31:			
SFAS No. 96 adjustments	$395,056	$441,904	$385,187
Accelerated depreciation	31,951	26,981	21,886
Cancelled Seabrook Unit 2	21,742	25,537	31,722
Unamortized bond redemption costs	15,427	23,240	26,546
Construction overheads	10,417	12,424	11,462
Alternative minimum tax carryforward	—	(3,757)	(10,670)
	$474,593	$526,329	$466,133
Accumulated deferred investment tax credits	$ 21,773	$ 52,125	$ 54,954

As a result of the adoption of SFAS No. 96 and the restatement of the financial results of prior periods to reflect such adoption, the Company has adjusted its deferred tax asset and liability balances as indicated in the table above. In accordance with SFAS No. 96, the Company has also recorded Unfunded Deferred Income Tax regulatory assets and liabilities as shown in the Consolidated Balance Sheet.

The amounts reported for federal income tax expense for the years 1989, 1988 and 1987 differed from the amounts computed by applying the federal income tax statutory rates

to book income before federal income taxes. The reasons for such differences are as follows:

	1989	1988	1987
Net income	$(73,350)	$78,639	$ 8,649
Total income tax expense	(63,172)	29,497	13,193
Less state income tax expense	(12,284)	9,325	3,803
Federal income tax expense	(50,888)	20,172	9,390
Book income before federal income taxes	(124,238)	98,811	18,039
Federal income tax statutory rates	34%	34%	40%
Federal income tax at statutory rate	(42,240)	33,596	7,216
Effect on taxes of:			
Deferred investment tax credits recorded as income per Seabrook Settlement Agreement	(21,729)	—	—
Allowance for equity funds used during construction capitalized for book purposes, not taxable income	(13,249)	(16,526)	(21,973)
Amortization of deferred investment tax credits	(1,029)	(1,029)	(1,091)
Equity in earnings of subsidiary companies for book purposes, not taxable income	(506)	(560)	(759)
Tax depreciation less than book depreciation applicable to pre-1981 property additions	516	84	505
Amortization of allowance for funds used during construction applicable to cancelled nuclear projects	1,070	1,070	1,259
Application of SFAS No. 90:			
Book/tax basis differentials	32,304	6,318	23,552
Investment tax credits	(7,594)	(1,800)	(4,353)
Additional book depreciation applicable to Millstone Unit 3	3,447	—	4,995
Other items — net	(1,878)	(981)	39
Federal income tax expense	$(50,888)	$20,172	$ 9,390
Effective federal income tax rates	40.9%	20.4%	52.1%

The Tax Reform Act of 1986 provides for a more comprehensive corporate alternative minimum tax (AMT) for years beginning after 1986. To the extent that the AMT exceeds the federal income tax computed at statutory rates, the excess must be paid in addition to the regular tax liability. For tax purposes, the excess paid in any year can be carried forward indefinitely and offset against any future year's regular tax liability in excess of that year's tentative AMT. In 1987, the Company paid additional taxes of $10,670 due to the AMT, which amount was carried forward for tax purposes and deferred on the Consolidated Statement of Income for book purposes. Since the Company's regular tax liability exceeded its tentative AMT liability by $6,913 in 1988, the Company's tax payments for that year were reduced accordingly and the AMT carryforward at December 31, 1988 was reduced to $3,757. During 1989, the Company's regular tax liability exceeded its tentative AMT liability by an amount greater than $3,757. As a result, there is no AMT being carried forward at December 31, 1989.

(E) Short-Term Credit Arrangements

On April 15, 1989, the Company reduced, from $160 million to $100 million, the borrowing limit of the revolving credit agreement that the Company has had with a group of banks since September 1984. This agreement was replaced by a new $100 million revolving credit agreement on December 21, 1989. The new agreement, which currently extends to October 30, 1990, affords the banks an opportunity to decline to lend funds if any one of several conditions is not satisfied at the date of a requested borrowing. These conditions include, among others, the absence of a determination by the banks that the Public Service Company of New Hampshire (PSNH) bankruptcy proceedings have increased the risk that the Company will not be able to perform its obligations under the agreement. As of December 31, 1989, $25 million of borrowings were outstanding under this agreement.

In September 1988, the Company entered into a revolving credit agreement with the same financial institution with which its has a sale and leaseback arrangement for nuclear fuel and a fossil fuel reserve and supply agreement. See Note (J), "Fuel Financing Obligations and Other Lease Obligations". This revolving credit agreement enables the Company to borrow up to a total $45 million, until August 31, 1990, for general corporate purposes and within an aggregate $165 million limit for all outstanding financing obligations to the financial institution. The aggregate limit is subject to being decreased to $135 million on March 16, 1990 unless Seabrook Unit 1 has, by that date, received a full-power operating license and made satisfactory progress towards achieving commercial operation. The financial institution may decline to lend funds under the revolving credit agreement if any one of several conditions is not satisfied at the time of a requested borrowing. As of December 31, 1989, $20 million of borrowings were outstanding under this agreement.

Information with respect to short-term borrowings is as follows:

	1989	1988	1987
Maximum aggregate principal amount of short-term borrowings outstanding at any month-end	$70,000	—	$60,000
Average aggregate short-term borrowings outstanding during the year*	26,068	—	27,848
Weighted average interest rate*	10.5%	—	7.5%
Principal amounts outstanding at year-end	$45,000	—	—
Annualized interest rate on principal amounts outstanding at year-end	10.4%	—	—

*Average short-term borrowings represent the sum of daily borrowings outstanding, weighted for the number of days outstanding and divided by the number of days in the period. The weighted average interest rate is determined by dividing interest expense by the amount of average borrowings. Commitment fees of $700, $830 and $800 paid during 1989, 1988 and 1987, respectively, are excluded from the calculation of the weighted average interest rate.

(F) Supplementary Information

The amount of maintenance, advertising costs, and the provisions for depreciation and amortization, other than set forth in the Consolidated Statement of Income, are not significant, and there are no royalties.

Taxes, other than income taxes charged to costs and expenses, are set forth below:

	1989	1988	1987
State gross earnings	$24,508	$23,950	$22,999
Local real estate and personal property	15,706	20,226	16,199
Other, principally payroll	4,830	6,123	4,024
	$45,044	$50,299	$43,222
Charged to:			
Tax expense	$44,800	$45,643	$40,191
Other accounts	244	4,656	3,031
	$45,044	$50,299	$43,222

(G) Pension Plan and Retirement Benefits

The Company's pension plan, which is based on final average pay, covers substantially all of its employees and its entire cost is borne by the Company. Net pension costs for 1987, 1988 and 1989 were $1,255, $1,443 and $1,892.

For funding purposes, the Company uses the Entry Age Normal Cost methodology. Due to the experience of the plan and the fund in recent years, no funding contribution has been required since 1985.

The plan's irrevocable trust fund consists principally of equity and fixed-income securities and real estate investments in approximately the following percentages:

Asset Category	Percentage of Total Fund
Equity Securities	60
Fixed-income Securities	30
Real Estate	10

The components of net pension costs were as follows:

	1989	1988
Service cost of benefits earned during the period	$ 3,544	$ 2,795
Interest cost on projected benefit obligation	9,482	8,647
Actual return on plan assets	(18,445)	(19,545)
Net amortization and deferral	7,311	9,546
Net pension cost	$ 1,892	$ 1,443
Assumptions used to determine pension costs were:		
Discount rate	7.75%	8.25%
Average wage increase	6.00%	6.00%
Expected long-term rate of plan assets	8.00%	8.00%
The funded status and amounts recognized in the balance sheet at December 31 were as follows:		
Actuarial present value of benefit obligations:		
Vested benefit obligation	$83,375	$70,272
Accumulated benefit obligation	$85,425	$78,555
Reconciliation of Accrued Pension Liability:		
Projected benefit obligation	$137,432	$123,540
Less: Plan assets (fair value)	142,653	128,540
Projected benefit obligation less than plan assets	(5,221)	(5,000)
Unrecognized prior service cost	(4,942)	(61)
Unrecognized gain (loss) from past experience	1,940	(6,357)
Unrecognized net asset (obligation) at date of initial application	17,309	18,612
Accrued pension liability at December 31	$ 9,086	$ 7,194

In addition to providing pension benefits, the Company provides certain health care and life insurance benefits for retired employees. Substantially all of the Company's employees become eligible for these benefits when they reach retirement age while working for the Company. These and similar benefits for active employees are provided through insurance companies and Health Maintenance Organizations whose premiums and membership fees are

based on the benefits provided and the claims experienced during the immediately preceding rating year. The Company recognizes the cost of providing these benefits to retired and active employees on a pay-as-you-go basis by expensing the annual insurance premiums, which were $5,282, $5,117 and $6,487 for the years 1987, 1988 and 1989, respectively. At December 31, 1989, the Company was providing these benefits for 1,623 active employees and approximately 548 retirees or their beneficiaries. The cost of providing these benefits for retirees is not now readily separable from the cost of providing benefits for active employees.

The FASB is currently deliberating proposed changes in the accounting for post-retirement benefits other than pensions. If these proposed changes are approved, commencing in 1992, the Company would be required to accrue such post-retirement benefits over a period starting with an employee's employment date until the date that the employee becomes eligible for retirement. At this time, the Company is unable to predict the outcome of these deliberations, but it is expected that the Company would be required to recognize substantial additional annual expense if the proposals were to be accepted.

(H) Jointly Owned Plant

The Company's 93.7% ownership share of the New Haven Harbor Station generating unit represented $129 million of utility plant in service and $45 million of accumulated provision for depreciation at December 31, 1989. The Company's 3.685% ownership share of the Millstone Unit 3 nuclear generating unit represented $133 million in plant in service and $36 million in accumulated provision for depreciation at December 31, 1989. The accumulated provision for depreciation for Millstone Unit 3 includes one-time increases of $12.5 million and $10.2 million recorded in 1987 and 1989, respectively, as provided in DPUC-approved stipulated earnings agreements in 1987 and a 1989 DPUC order. The Company's share of the operating costs is included in the appropriate expense captions in the Consolidated Statement of Income.

The Company also has a 17.5% ownership share in Seabrook Unit 1, a nuclear generating unit not yet in service. See Note (K), "Commitments and Contingencies".

(I) Unamortized Cancelled Nuclear Project

Since the Company has not been allowed a return on the Seabrook Unit 2 investment that it is recovering through rates, it recorded, in the first quarter of 1988, a non-cash write-off of approximately $10 million, net of related income tax effects, by restating the financial results for the years 1984 through 1987.

In August 1989, the Company recorded an additional non-cash write-off of approximately $2.6 million, net of related income tax effects, to recognize the probable disallowance of an allowed return on additional costs associated with Seabrook Unit 2 for which recovery has not yet been approved. See Note (B) "Accounting for Abandonments and Disallowances of Plant Costs and Phase-In Plans".

(J) Fuel Financing Obligations and Other Lease Obligations

The Company has a fuel reserve and supply agreement with a financial institution providing for the financing of up to $165 million in fossil fuel purchases, less the amount of the Company's outstanding obligations to the same financial institution for other corporate purposes. The dollar limit in the agreement, which was extended to December 31, 1990 in December of 1989, is subject to a reduction to $135 million on March 16, 1990 unless certain conditions are met. See Note (E), "Short-Term Credit Arrangements." At December 31, 1989, approximately $18 million of oil and $10 million of coal were being financed under this agreement.

The Company also has sale and leaseback arrangements with the same financial institution providing for nuclear fuel financing up to $70 million for Seabrook Unit 1 and up to $10 million for Millstone Unit 3. Under these arrangements, the Company is paying rent for the Millstone Unit 3 fuel based on the direct costs to the lessor of the fuel, plus the lessor's financing costs. At December 31, 1989, approximately $74 million of nuclear fuel was being financed under this agreement.

In addition to the nuclear fuel leases described above, the Company has entered into other leases (some of which are capital leases), including arrangements for the use of data processing and office equipment, vehicles, office space and oil tanks. The gross amount of assets recorded under capital leases and the related obligations of those leases as of December 31, 1989 are recorded on the balance sheet.

Future minimum lease payments under capital leases are estimated to be as follows:

Next five years:	
1990	$ 6,897
1991	6,405
1992	5,510
1993	5,416
1994	5,685
After 1994	72,773
Total minimum capital lease payments	102,686
Less: Amount representing interest	66,843
Present value of minimum capital lease payments	35,843
Present value of future nuclear fuel lease payments	74,003
Total lease obligations	$109,846

Capitalization of leases has no impact on income since the sum of the amortization of a leased asset and the interest on the lease obligation equals the rental expense allowed for rate-making purposes.

Rental payments charged to operating expenses in 1987, 1988 and 1989 amounted to $10,838, $12,821 and $13,780, respectively.

Operating leases, which account for the largest part of rental and lease payments charged to operating expense, consist of a large number of small, relatively short-term, renewable agreements for a wide variety of equipment.

(K) Commitments and Contingencies

The Company has entered into substantial commitments in connection with its continuing construction program, which is presently estimated at approximately $350 million, including AFUDC and excluding nuclear fuel costs, for 1990 through 1994. While this program was dominated by costs related to the construction of Seabrook Unit 1 prior to 1990, the above estimate includes only costs related to new construction commencing after January 1, 1990 for this unit. Since the Seabrook Settlement Agreement and the January 24, 1990 rate decision of the DPUC described at Note (C), "Rate-Related Regulatory Proceedings", provides for phasing-in the Company's $640 million investment in the unit and recovery of all on-going costs, the Company's primary concern is the achievement of commercial operation status. Although Seabrook Unit 1 has successfully completed low-power testing, its full-power operation is the subject of continuing Nuclear Regulatory Commission (NRC) proceedings and commercial operation can not be predicted. However, due primarily to delays in resolving emergency response plan issues, the unit is not likely to achieve commercial operation before the second quarter of 1990. See "Licensing Proceedings".

Seabrook Unit 1

The economic viability of Seabrook Unit 1 was seriously jeopardized in the Spring of 1984 by substantial increases in cost estimates and by the attendant financial problems of Public Service Company of New Hampshire (PSNH), which holds the largest ownership share (35.6%) in the Seabrook project. Since that time substantial progress has been made, due in part to the greater participation of other joint owners, including the Company. Construction of the unit has been completed, lengthy and costly proceedings to resolve controversies over licensing requirements and interventions and appeals by opponents of nuclear power have been successfully concluded, and low-power testing has been performed. While the risk of cancellation of the unit has been reduced by this record of progress, both the occurrence and timing of commercial operation of the unit continue to be dependent on accomplishment of remaining steps that are largely beyond the Company's control. The most difficult step is obtaining NRC approval of an off-site emergency response and evacuation plan for six communities in Massachusetts, which is being challenged by intervenors, including Massachusetts public officials. NRC licensing proceedings in this matter are in progress and are expected to conclude during the first quarter of 1990. See "Financing Concerns" and "Licensing Proceedings". However, there is no assurance that Seabrook Unit 1 will be placed in service; and if the unit were cancelled or abandoned, UI's financial viability and business operations could be jeopardized. See "Financial Consequences if Seabrook Unit 1 were Cancelled".

Financing Concerns

PSNH experienced increasing financial stress beginning in May 1987. On January 26, 1988, the Supreme Court of New Hampshire upheld the constitutionality of a New Hampshire statute that prohibits the inclusion of construction work in progress (CWIP) in a utility's rate base, thereby effectively precluding PSNH from obtaining a 15% emergency rate increase, which PSNH had stated was integral to a financial restructuring plan it had proposed in an effort to avoid proceedings under the Bankruptcy Code.

On January 28, 1988, PSNH commenced a proceeding under Chapter 11 of the Bankruptcy Code. Under this statute, PSNH is continuing its operations while seeking a financial reorganization. Several competing reorganization plans for PSNH have been filed with the bankruptcy court, including plans submitted by UI, PSNH and Northeast Utilities (NU). As revised through November 20, 1989, the UI plan provided for the payment of all of PSNH's debts and for merger transactions in which UI and PSNH would become wholly-owned subsidiaries of a public utility holding company owned by the existing creditors and shareholders of PSNH and UI's shareholders. Sufficient cash for the implementation of this plan would be obtained through a $1.6 billion sale-and-leaseback financing of PSNH's ownership interest in Seabrook Unit 1, and PSNH would also issue approximately $700 million of new stock and new debt securities to existing creditors and shareholders of PSNH in exchange for their existing claims and equity interests. As revised through November 20, 1989, the plan proposed by PSNH would involve an internally-recapitalized PSNH, which would retain all of its existing assets and distribute to existing creditors and shareholders of PSNH cash, new PSNH stock and new PSNH debt securities in exchange for their existing claims and equity interests. NU and the official committees of unsecured creditors and equity security holders in the bankruptcy proceeding have jointly proposed a plan pursuant to which PSNH would become a subsidiary of NU, PSNH's interest in the Seabrook plant would be transferred to a new subsidiary of NU, and the Seabrook subsidiary would contract to sell Seabrook power to PSNH. Under this plan, existing creditors and shareholders of PSNH would receive cash, new PSNH stock, new PSNH contingent debt securities and warrants to purchase NU stock. On November 20, 1989, UI announced that it expected to withdraw its reorganization plan for PSNH when the NU reorganization plan was properly documented and supported by an agreement with the State of New Hampshire relative to future electric rates for PSNH. Thereafter, NU filed with the bankruptcy court a revised joint plan of reorganization and an agreement with the State of New Hampshire relative to future electric rates for PSNH. Although the NU reorganization plan for PSNH, by reason of its joint sponsorship with the two official committees in the bankruptcy proceeding, is expected to be confirmed by the bankruptcy court, UI is unable to predict that the NU plan will be the plan confirmed. In the confirmation and implementation process, a plan is subject to obtaining approvals from affected shareholders, creditors and regulatory agencies, as well as the bankruptcy court. UI continues to expect that it will withdraw its reorganization plan for PSNH when NU's plan has been approved.

On June 1, 1988, Massachusetts Municipal Wholesale Electric Company (MMWEC), which holds an 11.59% ownership share of the Seabrook project, adopted a plan of action to withdraw from the project, including cessation of payment of its share, approximately $2 million, of total monthly project costs. Subsequent to that date, the shortfall in monthly payments was met by a combination of MMWEC's prepayments, payments by NU in return for wholesale power sales to other participants in the project, including the Company, and withdrawals from project cash balances and advances by other participants in anticipation of the implementation of a November 4, 1988 agreement between PSNH and MMWEC under which MMWEC continues to participate in the project. The agreement includes a provision pursuant to which PSNH advanced funds to reimburse the project cash balance withdrawals and advances by other participants, and has paid and will pay MMWEC's share of monthly project costs until commercial operation or cancellation of Seabrook Unit 1, in an aggregate amount not exceeding $30 million. This agreement received bankruptcy court approval, and it became effective on August 1, 1989. The financing arrangements for the agreement required that the present and former Seabrook participants exchange mutual releases of claims arising out of the construction of the project.

A Vermont participant in the Seabrook project, Vermont Electric Generation and Transmission Cooperative, Inc. (Vt Coop), which holds a 0.4% ownership share, has failed to make construction funding payments due since January 1986. However, the deficiency in project construction funding on account of Vt Coop's delinquencies has been and is being made up by advance payments by the Company and some of the other participants or their affiliates. The Company's share of advance payments on account of these delinquencies amounted to approximately $995,000 at December 31, 1989.

On December 21, 1988, the NRC decided all of the financial qualification issues that had been admitted for consideration in connection with low-power testing of Seabrook Unit 1, including the bankruptcy of PSNH, the effect of New Hampshire's anti-CWIP statute, and the cessation of, or arrears in, project payments by MMWEC and Vt Coop. The NRC concluded that no significant low-power testing safety problem was presented by these financial qualification concerns. After several minor on-site emergency planning issues were resolved and the joint owners had provided for a sum of $72.1 million to be available for decommissioning Seabrook Unit 1 in the event that low-power testing was conducted but commercial operation never achieved, low power testing was conducted in May and June of 1989. On October 19, 1989, the NRC denied a petition by intervenors in the pending full-power licensing proceeding for Seabrook Unit 1 to consider the financial qualification of PSNH to operate the unit safely. However, a court challenge to this decision of the NRC is pending.

Although it now appears likely that PSNH will be successfully reorganized under the Bankruptcy Code and that its bankruptcy proceedings will not materially adversely affect the NRC's full-power operating licensing proceeding for Seabrook Unit 1, the outcome of bankruptcy proceedings is unpredictable and the Company is unable to predict what impact, if any, that these proceedings will have on the NRC licensing proceeding or on the Company's financial condition.

Licensing Proceedings

Nuclear generating units are subject to the licensing requirements of the NRC under the Atomic Energy Act of 1954, as amended, and a variety of other state and federal requirements. It has been the experience of the electric utility industry that the construction and initial operation of these units are subject to increasingly stringent licensing requirements that, with other factors, have tended to increase the costs of and delay completion dates for the units, in some instances precipitating cancellations of projects after the expenditure of large amounts of money.

The licensing of Seabrook Unit 1 has been plagued by lengthy delays and has been repeatedly opposed by a number of intervening groups who have participated actively in administrative proceedings, filed numerous lawsuits and demonstrated at the construction site. On October 17, 1986, the NRC issued a full 40-year operating license for Seabrook Unit 1, permitting fuel loading. However, this license is subject to several conditions that must be satisfied to permit an orderly progression from fuel loading, which was completed on October 29, 1986, through low-power testing, which was conducted during May and June of 1989, and finally to full-power operation.

The principal remaining issues that have been identified to date and must be resolved prior to commercial operation relate to the development of satisfactory off-site emergency response and evacuation plans for the ten-mile emergency response and evacuation planning zone surrounding the plant. In this regard, the State of New Hampshire prepared and filed a plan for the seventeen New Hampshire communities within the ten-mile planning zone in 1985. The Atomic Safety and Licensing Board (ASLB) of the NRC held public hearings on the plan from October 1987 to June 1988, and the ASLB approved the plan on December 30, 1988, as described below, although an appeal is pending before the NRC and additional appeals to the courts are anticipated. However, the state government of Massachusetts, which is responsible for the development of such a plan for Massachusetts, has not filed a plan for the six Massachusetts communities within the ten-mile planning zone and, in a statement issued September 20, 1986, Governor Michael Dukakis stated that he does not intend to do so because he does not believe it is possible to develop a plan that would adequately protect public health and safety if an accident were to occur.

On October 29, 1987, the NRC unanimously adopted a licensing rule change that allows full-power operation of a nuclear plant to begin where there is a lack of participation in the development and implementation of emergency response and evacuation planning by state or local governments. This rule change requires the plant's owners to dem-

onstrate to the NRC's satisfaction that (1) the planning deficiency is wholly or substantially the result of the non-participation of state and/or local governments, (2) plans prepared by the owners provide reasonable assurance that public health and safety are not endangered by operation of the plant, and (3) the owners have made a sustained, good faith effort to secure and retain the participation of the pertinent state and/or local governmental authorities, including the furnishing to them of copies of the plans. The Commonwealth of Massachusetts, the State of New York and several private parties have challenged this rule change in court proceedings; and, although a federal appeals court in Boston has upheld the rule change and the Seabrook owners have attempted to demonstrate that the utility-sponsored emergency response plan that they have filed for Massachusetts satifies the requirements of the revised rule, there can be no assurance that the NRC's rule change will survive additional legal challenges or that the owners' plan will satisfy its requirements.

On April 8, 1987, the New Hampshire Yankee Division of PSNH (NHY) filed an emergency response and evacuation plan for the six Massachusetts communities within the ten-mile planning zone. On June 11, 1987, the NRC determined that this plan was inadequate; and on September 21, 1987, NHY filed a new utility-sponsored plan for the Massachusetts communities. On October 20, 1987, the staff of the NRC concluded that the new plan is a "bona fide utility plan" that compensates for the absence of participation by the governmental entities in Massachusetts. In a November 25, 1987 decision, the NRC agreed with this analysis of its staff.

On June 28 and 29, 1988, a full-scale, graded emergency preparedness exercise was conducted at Seabrook for both the Massachusetts and New Hampshire emergency response and evacuation plans. Preliminary reviews by the Federal Emergency Management Agency (FEMA) and NRC officials indicated that all participating organizations had demonstrated that they could adequately protect the public health and safety. On July 6, 1988, the NRC issued an inspection report on the exercise that confirmed its preliminary conclusions. A final report from FEMA on September 6, 1988 stated that it found no deficiencies in the plans.

On November 18, 1988, the President of the United States issued an Executive Order covering FEMA's assistance in emergency preparedness planning at commercial nuclear power plants. This order enables the federal government to participate in such planning and to delegate federal authority to a utility or other entity to carry out an emergency response and evacuation plan.

On December 14, 1988, FEMA issued the results of its integrated review and evaluation of all off-site emergency response and evacuation plans for Seabrook Station. FEMA determined that the plan for the State of Maine was adequate to protect public health and safety, and that the New Hampshire plan would also meet FEMA approval after proposed enhancements to the alert and notification systems are complete. FEMA further determined that the utility-sponsored plan for the Massachusetts communities would also provide for adequate protection of public health and safety when a vehicular alert and notification system for that area is operational. On December 30, 1988, the ASLB issued a Partial Initial Decision on the New Hampshire portion of the Seabrook Station Emergency Response Plan. In this decision, the ASLB found reasonable assurance that adequate protective measures can and will be taken within the New Hampshire portion of the ten-mile emergency planning zone in the event of a radiological emergency at Seabrook, subject to the satisfaction of several specified conditions, which have since been satisfactorily resolved. However, several intervenors, including the Commonwealth of Massachusetts, appealed to the Atomic Safety and Licensing Appeal Board (ASLAB) from the ASLB's decision and, on November 7, 1989, the ASLAB remanded four issues to the ASLB for further consideration and the correction of deficiencies. On November 16, 1989, the NRC decided that these issues should be resolved by it, rather than the ASLB, in conjunction with the proceeding described in the following sentences. The ASLB's public hearings on the utility-sponsored plan for the Massachusetts communities began on March 21, 1989 and were completed on June 30, 1989. Public hearings on the June 28 and 29, 1988 graded emergency preparedness exercise were conducted concurrently. On November 9, 1989, the ASLB issued a Partial Initial Decision in which it found that the June 1989 graded emergency exercise was adequate in scope and revealed no fundamental flaw in either the New Hampshire or the Massachusetts emergency response and evacuation plan, that the Massachusetts plan is adequate and implementable, and that a full-power license should be issued for Seabrook Unit 1. Although intervenors commenced appeals to the ASLAB from this decision of the ASLB, as stated above, the NRC decided on November 16, 1989 that it, rather than the ASLAB, would consider all appeals from the ASLB's November 9, 1989 decision. A final decision by the NRC is expected during the first quarter of 1990; but appeals to the courts by intervenors, including the Commonwealth of Massachusetts, are anticipated.

Regulatory proceedings with respect to the transfer of responsibility for management of construction and for operation of Seabrook Unit 1 to New Hampshire Yankee Electric Corporation, an entity that has been created by the Seabrook joint owners for these express purposes, are pending before the Masachusetts Department of Public Utilities. Approval of this transfer by the NRC and the PSNH bankruptcy court will also be required. On September 2, 1988, the bankruptcy court refused to approve the transfer, finding that evidence submitted was insufficient to justify approval at that time. The joint owners will continue to seek the required regulatory approvals, but the Company cannot predict when or if the approvals will be obtained. The latest reorganization plan filed by NU in PSNH's bankruptcy proceeding (see "Financing Concerns") proposes the transfer of responsibility for management and operation of Seabrook Unit 1 to a new subsidiary of NU.

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Financial Consequences If Seabrook Unit 1 were Cancelled

The outcome of the proceedings described at "Financing Concerns" and "Licensing Proceedings" is of particular significance in assessing the risk that Seabrook Unit 1 will not be placed in commercial operation despite the several favorable developments noted above. The Company is unable to predict either the outcome of these proceedings or the nature or scope of any action that might be taken by the other Seabrook participants if the outcome is unfavorable.

If Seabrook Unit 1 were cancelled, it would have a material adverse impact on the Company's financial condition and its ability to meet the long-term needs of its customers, and the Company's financial viability and business operations could be jeopardized. The provisions of the Seabrook Settlement Agreement, described at Note (C), "Rate-Related Regulatory Proceedings," that cover rate base treatment and rate increases associated with Seabrook Unit 1 would require the parties to attempt to renegotiate this agreement and, in the event new terms could not be negotiated, would leave the issues for DPUC decision. At December 31, 1989, the Company's investment in Seabrook Unit 1, after giving effect to SFAS No. 90 write-offs described at Note (B), "Accounting for Abandonments and Disallowances of Plant Costs and Phase-in Plans", amounted to $640 million, including a non-cash allowance for funds used during construction (AFUDC) but excluding approximately $78 million of nuclear fuel. This investment exceeds the net book value of the Company's utility plant in service. Although the Company would seek approval to amortize its investment over an appropriate period of time and to recover the investment through rates, there would be no assurance as to whether or to what extent the DPUC would grant such recovery. Consequently, although the Company is unable to predict the outcome of renegotiation of the Seabrook Settlement Agreement and regulatory proceedings in which these matters would be determined if Seabrook Unit 1 were cancelled, adverse decisions in these proceedings could jeopardize the Company's financial viability and business operations. However, the Seabrook Settlement Agreement provides that the Company will be entitled to retain revenues, including CWIP revenues, to which it has become entitled prior to December 31, 1990, whether or not Seabrook Unit 1 is cancelled.

Cancellation of Seabrook Unit 1 would remove all of the Company's investment in the unit from the calculation of the limit on the aggregate amount of the Company's unsubordinated short-term and long-term borrowings prescribed by the Trust Indenture under which all of the Company's Debentures are issued. The Company's borrowing limit would be reduced thereby to a level substantially below its outstanding borrowings, precluding further unsubordinated borrowings by the Company and obligating it to reduce its outstanding borrowings to the new lower borrowing limit prior to May 1 of the succeeding year. In such an event, in order to preserve its financial viability and business operations, the Company would be compelled to attempt to sell securities that are junior to the Company's Debentures and to seek a waiver of the Trust Indenture borrowing limit from the holders of all outstanding series of its Debentures issued prior to July 1, 1987. Approval of the holders of two-thirds of the principal amount of all such Debentures would be required to obtain such a waiver. The Company is unable to predict whether it would be successful in either of these endeavors.

Nuclear Insurance Contingencies

The Price-Anderson Act, currently extended through August 1, 2002, limits public liability from a single incident at a nuclear power plant. The first $160 million of this liability would be provided by purchasing the maximum amount of commercially available insurance. Additional liability would be provided by an assessment of $63 million per incident, levied on each of the nuclear units licensed to operate in the United States, subject to a maximum assessment of $10 million per incident per nuclear unit in any year. In addition, if the sum of all public liability claims and legal costs arising from any nuclear incident exceeds the maximum amount of financial protection, each reactor operator can be assessed an additional 5% of $63 million or $3.2 million. The maximum assessment is adjusted at least every five years to reflect the impact of inflation. Based on its ownership interest in nuclear units, including Seabrook Unit 1, the Company estimates its maximum liability would be $20.3 million per incident. However, assessments would be limited to $3.1 million per incident, per year.

With respect to each of the operating nuclear generating units in which the Company has an interest, the Company will be obligated to pay its ownership share of any statutory assessment resulting from a nuclear incident at any nuclear generating unit.

The NRC requires nuclear generating units to obtain property insurance coverage in a minimum amount of $1.06 billion and to establish a system of prioritized use of the insurance proceeds in the event of a nuclear incident. The system requires that the first $1.06 billion of insurance proceeds be placed in a trust beyond the reach of creditors of the unit's owners and used to stabilize the nuclear reactor to prevent any significant risk to public health and safety and then for decontamination and cleanup operations. Only following completion of these tasks would the balance, if any, of the segregated insurance proceeds become available to the unit's owners.

For each of the nuclear generating units in which the Company has an ownership interest, the Company is required to pay its ownership share of the cost of purchasing such insurance.

Other Commitments and Contingencies

An additional financial problem that will arise if and when Seabrook Unit 1 achieves commercial operation concerns the Company's ability to incur indebtedness under the earnings coverage provisions of the Trust Indenture under which the Company has issued all of its long-term Debentures. The absence of a return on the disallowed portion of the Company's Seabrook Unit 1 investment and the increased depreciation charges against income related to

Seabrook Unit 1 can be expected to cause the Company's earnings for the next several years to fall below the interest coverage level specified in the Trust Indenture as a prerequisite to any increase in short-term or long-term indebtedness (except for $2 million of short-term borrowings incurred for operating expense purposes, and except for borrowings which are expressly subordinated to the Company's Debentures and are limited to an aggregate amount not exceeding 10% of the Company's debt limit under the Trust Indenture — 62½% of the cost of the Company's properties less depreciation thereon (the Company's debt limit under the Trust Indenture was $1.024 billion at December 31, 1989)). The Company estimates that its aggregate capital requirements will exceed cash provided by operations by $295 million during this period. The Company expects to meet these requirements by a combination of pre-financing, subordinated borrowings and financings that are not subject to the Trust Indenture's restrictions. However, there is currently no assurance that this expectation will be met.

The Company has a 9.5% common stock ownership share in Connecticut Yankee Atomic Power Company (Connecticut Yankee), which owns and operates a nuclear electric generating station in Haddam Neck, Connecticut. Connecticut Yankee has been engaged in a construction program that is essential to maintain its station as a dependable source of low-cost electric power in New England. As a condition of the debt financing arrangements for this construction program, the lenders from time to time have required guarantees from the shareowners of Connecticut Yankee. In this regard, the Company is obligated to furnish 9.5% of Connecticut Yankee's capital requirements within specified limits. Currently, the Company's liability for its share of Connecticut Yankee's long-term debt issues amounts to approximately $2.2 million. During a scheduled refueling and maintenance outage that began on September 2, 1989, Connecticut Yankee management completed an assessment of fuel damage and presently estimates that the total cost of fuel repairs, including the cost of eight new fuel assemblies, will be approximately $8 million. During the outage, Connecticut Yankee's thermal shield is being removed at an estimated cost of $25 million. The Company may be required to furnish additional guarantees to finance its portion of costs incurred during this outage. Connecticut Yankee's management presently estimates that the Connecticut Yankee unit will not be returned to service until April 1990, five months later than the originally scheduled date.

The Company claimed abandonment losses for tax purposes with respect to Seabrook Unit 2 of approximately $72.7 million in 1984 and $10.2 million in 1986. During 1988, the Internal Revenue Service (IRS) commenced an examination of the Seabrook project expenditures on Seabrook Unit 2 that were claimed as abandonment losses by several of the joint owners of the project, including the Company, in the years 1984 and/or 1985. On March 20, 1989, the IRS case manager issued a notice of proposed adjustment setting forth the IRS position that there was no abandonment of Seabrook Unit 2 in the years under audit. It is also the IRS position that, in the event new facts and circumstances beyond the examination level reveal that an abandonment loss did occur in 1984 and/or 1985, the claimed losses must be reduced by the salvage value of Seabrook Unit 2 assets. In a letter dated July 17, 1989, the IRS District Director notified the Company of proposed tax assessments for the years 1981, 1984, and 1985 arising from a disallowance of the abandonment loss deduction claimed by the Company in 1984. The Company responded to this notice, disagreeing with the proposed assessments and requesting a conference with the IRS appellate division. If this matter is not resolved at the appellate division level, the Company will contest the proposed assessments vigorously in Tax Court proceedings.

The Company is a party to a ten-year contract for the purchase of seven billion kilowatt-hours per year of firm energy from Hydro-Quebec by the New England participants in Phase II of a transmission intertie project linking New England and Quebec, Canada. The Company has a 5.45% share in this phase of the project, which participation was authorized by the Connecticut DPUC in April 1987. The Phase II agreements provide for expansion of the capacity of this transmission intertie from 690 megawatts to 2,000 megawatts in the early 1990's.

On May 2, 1990, a pumping error at the Company's Bridgeport Harbor Station caused an overflow of approximately 800,000 gallons of fuel oil into the diked containment area surrounding the station's oil storage tanks. Approximately 90% of the spilled oil was reclaimed and the remainder was consolidated with approximately 1,200 cubic yards of contaminated soil and removed to a location approved for disposal by the Connecticut Department of Environmental Protection. The estimated cost of this accident is not expected to exceed $700,000, of which approximately $655,000 was charged against current income as of December 31, 1989.

In complying with existing environmental statutes and regulations and further developments in these and other areas of environmental concern, including legislation that is receiving serious consideration at federal and state levels in the fields of water and air quality (particularly "acid rain", "air toxics", "ozone non-attainment", and "global warming"), hazardous waste handling and disposal and toxic substances, the Company may incur substantial capital expenditures for equipment modifications and additions, monitoring equipment and recording devices, and it may incur additional operating expenses. The total amount of these expenditures is not now determinable.

(L) Nuclear Fuel Disposal and Nuclear Plant Decommissioning

Under the Nuclear Waste Policy Act of 1982, the federal government is responsible for the disposal of spent nuclear fuel. The Department of Energy (DOE) has established disposal fees which are payable to the federal government on the basis of net generation by electric utilities owning or operating nuclear generating units. UI recovers such fees as a part of nuclear fuel expense charged to customers through electric service rates.

The Company is also recovering through electric service rates its share of the estimated decommissioning costs for Seabrook Unit 1 and Millstone Unit 3. In January 1989, the New Hampshire Nuclear Decommissioning Financing Committee established the cost of decommissioning Seabrook Unit 1 upon its retirement at $242.4 million (in 1987 dollars). This amount is to be increased each year after 1987 by a 4% annual inflation factor until Seabrook Unit 1 begins commercial operation. Upon operation of Seabrook Unit 1, the Company will be required to make monthly payments of its share of the estimated decommissioning costs into a state-managed trust fund. The DPUC has established a decommissioning estimate of $194 million for Millstone Unit 3 (in 1987 dollars), and the Company is currently funding its share of such estimated decommissioning costs monthly. Although such amounts will be reviewed and revised from time to time during the life of the units, there is no guarantee that such funding will be sufficient to cover actual decommissioning costs upon retirement.

(M) Quarterly Financial Data (Unaudited)

Selected quarterly financial data for 1989 and 1988 are set forth below:

Quarter	Operating Revenues	Operating Income	Net Income (Loss)	Earnings (Loss) Per Share of Common Stock (1) (2)
1989				
First	$128,864	$32,228	$ 9,737	$ .50
Second	127,697	18,366	690	(.15)
Third	144,155	26,914	(90,773)	(6.64)
Fourth	130,465	16,281	6,996	.42(3)
1988				
First	$126,712	$27,605	$32,478	$2.13
Second	120,465	25,476	24,911	1.59
Third	144,638	34,317	(2,342)	(.37)
Fourth	127,123	26,497	23,592	1.50

(1) Based on weighted average number of shares outstanding each quarter.

(2) Earnings for 1989 and 1988 include the net effects of SFAS No. 90 write-offs and accretion transactions in the following amounts for the first through fourth quarters, respectively:

1989: $(1.12) $(1.20) $(8.77) $.13
1988: $ .05 $ .05 $(2.51) $.04

(3) Earnings for the fourth quarter of 1989 include one-time expenses associated with replacing defective siding at a generating station, costs in connection with the effort to affiliate with PSNH through its bankruptcy reorganization proceedings and storm costs. Also included are costs associated with an extended maintenance outage of the Connecticut Yankee power plant and substantially lower AFUDC due to SFAS No. 90 write-offs in 1989. The aggregate reduction due to these factors was approximately $.85 per share.

Market for the Company's Common Equity and Related Stockholder Matters.

UI's Common Stock is traded on the New York Stock Exchange, where the high and low sale prices during 1989 and 1988 were as follows:

	1989 Sale Price		1988 Sale Price	
	High	Low	High	Low
First Quarter	25 1/4	24 1/4	27 1/4	19 3/4
Second Quarter	27 1/4	26 3/8	23	19 5/8
Third Quarter	29 3/8	28 3/8	24 1/4	21 3/4
Fourth Quarter	34 1/4	30	27 1/2	23 1/4

UI has paid quarterly dividends on its Common Stock since 1900. The quarterly dividends declared in 1988 and 1989 were at a rate of 58 cents per share.

The Trust Indenture under which all of the Company's Debentures are issued places limitations on the payment of cash dividends on the Common Stock of the Company and on the amounts that can be expended to purchase or redeem shares of Common Stock. However, all the Company's retained earnings at December 31, 1989 were free of such limitations.

As of January 31, 1990, there were 24,728 Common Stock shareowners of record.

TO THE SHAREOWNERS AND DIRECTORS OF
THE UNITED ILLUMINATING COMPANY:

We have audited the accompanying consolidated balance sheets of The United Illuminating Company as of December 31, 1989, 1988 and 1987, and related consolidated statements of income, retained earnings and cash flows for the years then ended. These financial statements are the responsibility of the Company'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, the financial statements referred to above present fairly, in all material respects, the consolidated financial position of The United Illuminating Company as of December 31, 1989, 1988 and 1987, and the consolidated results of its operations and its cash flows for the years then ended in conformity with generally accepted accounting principles.

The Company is a 17.5% participant in the Seabrook Unit 1 Nuclear Project (the Unit). As more fully described in Note (K) in the "Notes to Consolidated Financial Statements", there are uncertainties relating to those events necessary for the Unit to achieve commercial operations and, therefore, the ability of the Company to ultimately recover, in rates, their investment in the Unit. The outcome of these uncertainties could have a material effect on the financial position and results of operations of the Company, and it is uncertain whether such material effects would permit the realization of assets and liquidation of liabilities in the ordinary course of business operations.

COOPERS & LYBRAND

New York, New York
January 24, 1990

[illegible] Information

General Counsel
Wiggin & Dana

Independent Accountants
Coopers & Lybrand

Co-Transfer And Dividend Disbursing Agent:
The United Illuminating Company
80 Temple Street
P.O. Box 1564
New Haven, Connecticut
06506-1564
Attention: Shareholder Services
Telephone: (203) 777-[illegible]

Registrar And Co-Transfer Agent:
Continental Stock Transfer & Trust Company
[illegible] Street
New York, New York [illegible]
Attention: Stock Transfer Department
Telephone: (212) [illegible]

Stock Listing:
New York Stock Exchange
Common Stock
[illegible] Preferred Stock, [illegible] Series

[illegible] Common Stock Shareholders of record interested in obtaining information regarding the benefits of participating in UI's dividend reinvestment plan may write or call: [illegible]
Shareholder Services
P.O. Box 1564
New Haven, CT [illegible]
Telephone: (203) [illegible]

Annual Meeting Date:
The Company's Annual Meeting will be held at the New Haven Lawn Club, 193 Whitney Avenue, New Haven, CT on Wednesday, May [illegible], beginning at [illegible]

UI United Illuminating

80 Temple Street
New Haven, Connecticut 06506

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