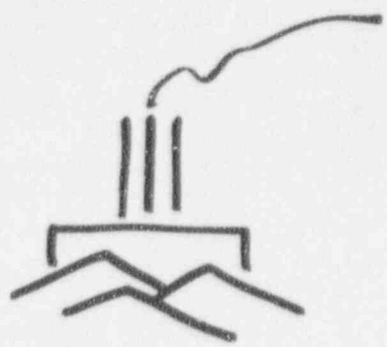
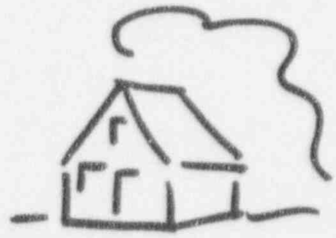
CENTERIOR ENERGY



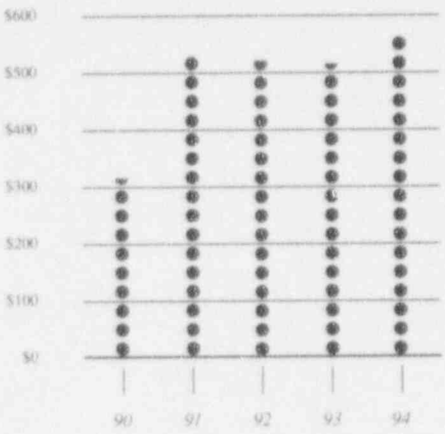


# Annual Report 1994

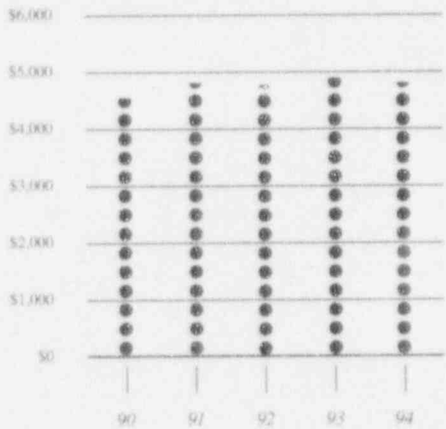
# Contents



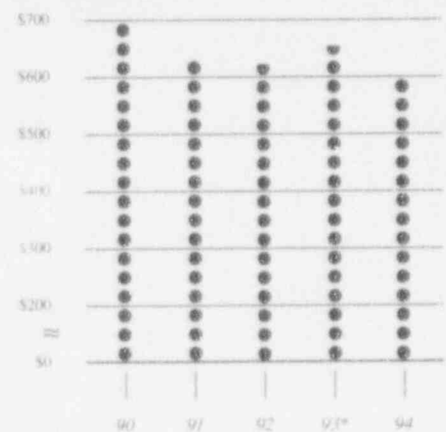
*Net Cash from Operating Activities (in millions)*




*Debt and Preferred Stock Outstanding at Year End (in millions)*




*Operation and Maintenance Excluding Fuel and Lease Expense (in millions)*




* Excludes early retirement program expenses and other charges of $272 million.

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# Financial Summary

| | 1994 | 1993 | % Change |
|---|---|---|---|
| Earnings (Loss) Per Share of Common Stock | $ 1.38 | $ (6.51) | — |
| Write-Offs and Other Charges Per Share of Common Stock | $ — | $ 7.95 | — |
| Earnings Per Share of Common Stock | | | |
| Excluding Write-Offs and Other Charges | $ 1.38 | $ 1.44 | (4) |
| Dividends Declared Per Share of Common Stock | $ .80 | $ 1.60 | (50) |
| Book Value Per Share of Common Stock at Year End | $ 12.71 | $ 12.14 | 5 |
| Closing Common Stock Price at Year End | $ 8⅞ | $ 13¼ | (33) |
| Common Stock Share Owners at Year End | 149,237 | 163,602 | (9) |
| Common Stock Shares Outstanding at Year End (millions) | 148 | 147 | 1 |
| | | | |
| Operating Revenues (millions) | $ 2,421 | $ 2,474 | (2) |
| Operating Expenses (millions) | $ 1,843 | $ 2,161 | (15) |
| Net Income (Loss) (millions) | $ 204 | $ (943) | — |
| Return on Average Common Stock Equity | 11.1% | (40.3)% | — |
| Return on Average Common Stock Equity | | | |
| Excluding Write-Offs and Other Charges | 11.1% | 7.1% | — |
| | | | |
| Kilowatt-hour Sales (Millions of Kilowatt-hours) | | | |
| Residential | 6,980 | 6,974 | 0 |
| Commercial | 7,481 | 7,306 | 2 |
| Industrial | 12,069 | 11,687 | 3 |
| Wholesale | 1,842 | 3,027 | (39) |
| Other | 1,074 | 1,022 | 5 |
| Total | 29,446 | 30,016 | (2) |
| | | | |
| Employees at Year End | 6,767 | 6,748 | 0 |

## *Quarterly Range Of Common Stock Prices*

| 1994 | High | Low |
|---|---|---|
| 1st Quarter | $13⅜ | $10⅝ |
| 2nd Quarter | 11¾ | 9⅝ |
| 3rd Quarter | 10⅝ | 8⅞ |
| 4th Quarter | 9½ | 8 |

| 1993 | High | Low |
|---|---|---|
| 1st Quarter | $20 | $18⅝ |
| 2nd Quarter | 19⅞ | 17⅜ |
| 3rd Quarter | 18⅞ | 17⅛ |
| 4th Quarter | 17⅞ | 12 |

# Dear Fellow Share Owner:

The electric utility industry, the markets served by that industry, Centerior Energy itself—everything is changing rapidly and profoundly.

Our industry is becoming more competitive, more varied, and far less predictable.

Our customers, themselves faced with sweeping change in an increasingly global economy, are becoming far more demanding where both price and service are concerned.

And in response to all this Centerior is transforming itself, committing itself to dealing aggressively with the challenges that face us.

We took our first major steps toward meeting these challenges in January 1994, cutting our common stock dividend in half, writing off assets of $1.023 billion after taxes, and announcing a multi-faceted strategic plan. Though the months since then have not been free of problems—unexpected repair needs greatly increased the cost of a refueling and maintenance outage at our Perry Nuclear Power Plant, for example—they have been months of progress overall. We met our 1994 goals for nonfuel retail revenues and, most importantly, for cash flow. We kept within our target for construction expenditures and came very close to our target for operation and maintenance expenses despite the unexpectedly high costs of the Perry outage.

This progress was just a start, however, and it had little impact on the price of our common stock. The disappointing performance of our stock in 1994 was largely a reflection of industry-wide conditions. Concern about rising interest rates, along with general industry uncertainty, contributed to a 21% drop in the Dow Jones Utility Average—the biggest decline in eight years. But investors also had specific concerns about Centerior: the decline in our stock price was 33%. We are addressing such concerns by implementing the strategic plan and demonstrating its ability to augment revenues and reduce costs, thereby increasing cash flow and ultimately rebuilding share owner value.

It was in pursuit of this strategy that we cut our common stock dividend a year ago, and this made it possible for us to retire fixed-income obligations of $136 million during 1994. Our goal is to reduce such obligations by a cumulative total of $1.3 billion by 2001. This is essential to our future competitiveness. It's why the dividend cut was not only necessary but in the best interests of share owners over the long term.

One of the keys to sustained cash flow, nonfuel retail revenues, increased slightly in 1994 despite the fact that milder weather had a significantly negative impact on residential sales. Strong growth in industrial revenues made this possible, which means that if the weather factor had remained constant, nonfuel retail revenues would have been up substantially. Contracts have become an important factor in our industrial market, helping us to build stronger relationships with major customers. We now have contracts with customers accounting for two-thirds of our industrial sales; among these customers are our 20 largest. More than 80% of our industrial contracts will not be up for renewal until 1997 or later, and increasing numbers of our largest commercial customers also are signing contracts.

Consistent cash flow growth will require not only retaining present customers but increasing revenues year by year. This key strategic objective will become especially important in 1996, when our earnings will be measured almost entirely in cash terms and deferrals will no longer be a significant factor.

In 1994, in pursuit of new revenues, we developed and launched an ambitious marketing

plan. One of the purposes of this plan is to broaden the ways in which our present residential, commercial and industrial customers use electricity. Another is to foster economic development in our service area, which after years of recession now has low unemployment along with robust activity in a variety of major industries.

Another source of revenue growth is the restructuring of rates. Our rates have not changed since 1991, but the Rate Stabilization Program approved by the Public Utilities Commission of Ohio in 1992 permits us to apply for new tariffs that would become effective in 1996. New tariffs are justified by our current return on investment, and could provide us with the kind of pricing flexibility needed in an increasingly competitive market.

We're making progress in cost reduction. Operation and maintenance expenses exclusive of fuel and purchased power were 13% lower in 1994 than in 1990. The fact that 1994's O&M expenses were $108 million lower than those for 1990, and $56 million lower than those for 1993 when one-time charges are excluded, is especially significant in light of the costs of the Perry outage.

The improvements made to the Perry plant during its outage have already contributed to better performance. They also constitute an important step in the necessarily gradual process of turning Perry into what our Davis-Besse Nuclear Power Station already is: a world-class generating facility. We expect to complete that process by 1998, when Perry will have undergone two more scheduled outages.

O&M expenses both at Davis-Besse and at our fossil-fueled plants have been reduced significantly over the past several years. Davis-Besse completed the shortest refueling and maintenance outage in its history in 1994, returning to service just 46 days after shutting down. The one scheduled outage aside, its availability rate in 1994 was 100%.

All these positive developments—good cash generation, debt and cost reduction, preparations for further change—are steps toward the achievement of the strategic plan. The ultimate purpose of that plan is to repay our share owners for their support and for their patience in challenging times. Everything being done at and by Centerior is aimed at building share owner value over the long term.

It is for this reason that we have established an incentive compensation program that rewards our work force when—but only when—key objectives are achieved. For the same reason we have frozen the base salaries of our top executives for the next three years, linking their opportunities for increased compensation directly to the performance of our common stock. This assures that our leadership team will win only if our share owners win first.

The following pages are a brief report on progress to date in the achievement of our strategic objectives, and on where we intend to go from here. We believe we have made a good beginning, but we know it is nothing more than a beginning. The strategic plan is a guide that covers eight years, and seven of those years are still ahead of us. They will bring many additional changes, some of which may require adjustments of our plan. An immense amount of work, including almost all the work of achieving our objectives, still lies ahead. In 1994 we built the foundation on which that work can and will be done.

As we move into year two, I am grateful for the support (and, yes, for the patience) of our share owners. I am likewise grateful for the immense contributions of the talented and committed men and women who make up the Centerior work force. It is the quality of our team, more than any other single thing, that makes me confident about the future.

Sincerely,

Robert J. Farling

Robert J. Farling

Chairman, President and
Chief Executive Officer

February 24, 1995

# Finance

***Provide share owners a total return—dividends plus price appreciation—exceeding that of the Standard & Poor's 500 Index.***

"Cash is king—cash is the key to everything we're trying to do," says Gary Leidich, Centerior's chief financial officer.

"Our long-term goal is to rebuild the corporation's financial strength by reducing our debt, and doing that requires cash. We want to position ourselves to compete effectively, and to do that we have to reduce our fixed costs. Again, what it takes is cash."

In 1994 the total return for the Standard & Poor's 500 Index was 1.3%. The return for Centerior share owners, by contrast, was -27%. We're still a long way, clearly, from achieving our first objective.

We did, however, make progress toward that objective. And we did so in the ways that matter most: by keeping spending under control and using available cash for the gradual reduction of debt and preferred stock.

Of the $569 million in cash that Centerior generated from operating activities in 1994, $118 million went for common stock dividend payments. Another $205 million in cash was used for capital expenditures. The balance—the part that demonstrates most clearly the importance of our focus on cash—was used to retire nuclear fuel lease obligations of $110 million and fixed-income obligations of $136 million.

Keeping cash flow at satisfactory levels will require two things above all. First it will require revenue growth. This is the subject of our second strategic objective, and it will become particularly important when, starting in 1996, deferrals are no longer a significant part of reported earnings. Second it will require firmness in controlling costs and aggressiveness in reducing costs wherever this can be done without damaging our ability to serve and satisfy customers. With revenues rising and costs stable, more dollars can fall to the bottom line and be used for the continuing reduction of debt and preferred stock.

Operation and maintenance expenses exclusive of fuel and purchased power but including plant leases amounted to $755 million in 1994. This total was very close to our target for the year. The comparable earlier totals were $811 million in 1993, $784 million in 1992 and $801 million in 1991. The level achieved in 1994 is especially gratifying in light of the $18 million that unanticipated repair needs added to the cost of the Perry plant's outage. Without these additional costs, we would have been $7 million below our O&M spending target in 1994.

The target for 1995 is $760 million—slightly higher than the previous year's total because of the costs of putting new marketing capabilities in place and improving customer service. From 1996 through the remaining years of the strategic plan, we will be committed to avoiding any increases in O&M spending, even adjustments for inflation. Payroll expense for

1994 was not only far below the previous year's total—an almost inevitable result of 1993's early retirement program—but also significantly below what we had planned.

Construction expenditures in 1994 totaled $257 million, $2 million under target. The target for 1995 is $260 million. The annual construction expenditures average called for in our five-year forecast is now $250 million. The comparable average two years ago was $329 million. Capital investment is being limited to projects that are necessary for system reliability or expansion.

# Revenues

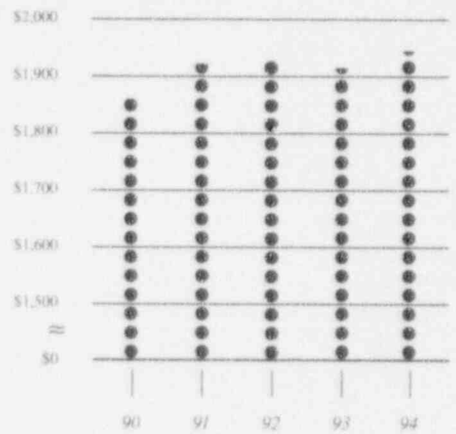
## *Increase revenues in an increasingly competitive market.*

"What we're doing," says Al Temple, who in 1994 became Centerior's vice president of sales and marketing, "is introducing highly competitive techniques for maintaining and enhancing our revenues into what was until recently a traditional utility company. This is innovative, it's necessary, and it's immensely productive."

The pursuit of higher revenues starts with maintaining our current customer base. This is achieved partly through objective number three, increased customer satisfaction.

It is achieved also through the contracts discussed in the chairman's letter—contracts which enable us to build the kinds of relationships that can be decisive in highly competitive markets. Throughout our service area a pattern is becoming apparent whenever our large industrial customers renew their contracts. The new contracts often are for longer periods of time, and often they involve increased use of electricity. More than ever before, Centerior is helping customers to use electricity as a tool for improving productivity. This in turn is leading to plant expansion and increased demand for power.

***Weather Adjusted Nonfuel Retail Revenues (in millions)***




In 1994 a growing list of established Centerior customers decided to expand their operations or make new use of innovative electrotechnologies in our service area. Each such decision brings new jobs, new economic vitality, and new demand for electricity in the years ahead.

The customer base is maintained finally through a demonstrated ability to deal with competition from municipal electric systems. Partly as a result of our actions, proposals for the study of possible municipalization were turned back in 1994 in the cities of Toledo and Garfield Heights. By the end of the year the expansion of the

Cleveland Public Power system had slowed significantly. Two of CPP's largest industrial customers, American National Can and Pierre's French Ice Cream, returned to Centerior in 1994. Late in the year CPP was reporting its expansion program to be behind schedule and over budget.

The struggle over municipalization continues, of course. In Toledo, advocates continue to push for voter approval of funding for a municipalization study. Centerior is among the most experienced utilities in the U.S. in dealing with such matters, and we have a long record of success in showing voters and city officials alike that municipalization is rarely if ever in the public interest.

In 1994 we also launched a marketing plan aimed partly at developing new sources of revenues, and before year-end this was producing results. In the fall, after negotiations in which Centerior played a very active role, the American Steel and Wire unit of Birmingham Steel announced its decision to build a $100 million bar mill in the Cleveland suburb of Cuyahoga Heights. Owens Corning announced that it will build a $90 million headquarters—complete with all-electric heating and cooling—in downtown Toledo.

In February 1995, Aluminum Corporation of America announced its selection of a site in the Toledo Edison service area for a new automotive supply manufacturing facility, and North Star Steel announced a site served by TE for a $450 million steel mill. North Star cited competitive electric rates as an important factor in its decision. Both companies considered locations in other states.

Centerior's economic development programs contributed significantly to all of these expansion and site selection decisions.

Overall, industrial and commercial revenues were higher in 1994 than in the previous year despite the fact that, even by year-end, our new sales and marketing capabilities were still being put into place. The increase was sufficient to offset both a 1.3% drop in residential revenues caused by last summer's generally mild temperatures and lower fuel cost recovery revenues. Toledo Edison, whose service area has long been economically sluggish, experienced a 2.8% increase in industrial revenues—solid evidence of improving business conditions.

We now have not only new sales and marketing objectives but an organization designed to achieve them. Automation and other improvements have increased the time that Centerior representatives spend actively selling by upwards of 20,000 hours per year. This translates into more calls on customers, better knowledge of customer needs and increased ability to meet those needs.

In the course of making such changes we broke down our long-term objective—$2.87 billion in retail revenues in 2001—into year-by-year goals. The goal for 1995 is $1.98 billion, weather-normalized and exclusive of fuel cost recovery, a 2% increase over 1994.

Both the marketing plan and the new organization responsible for implementing it are

focused on our three primary market segments: residential, commercial and industrial. Results-oriented research is providing valuable knowledge of the customer subgroups that are most important in each segment. This knowledge, in turn, is being used to develop marketing programs aimed at those areas where opportunities for new uses of electricity—and therefore for increased sales—appear to be greatest. These programs are producing sales. A major canned food producer, for example, chose electricity as the heat source for a new shrink-wrapping process because of its superiority to natural gas in such applications.

As part of the implementation of the marketing plan, one new program is being introduced in each segment each fiscal quarter. In the industrial segment this began with electro-technologies for non-ferrous melters and with infrared electric heat as a drying technology for customers in the metals and coatings business. The first programs introduced in the commercial sector involved exterior lighting and supplemental lighting. Each such program is aimed at a market niche where Centerior can offer a technology that provides new answers to customer needs.

# Customers

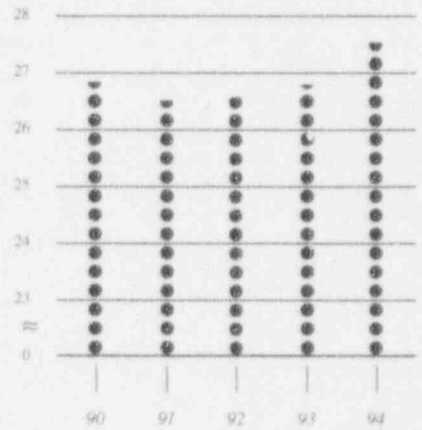
***Raise our customer satisfaction rating.***

"To fulfill our vision for the Centerior of the future, we have to be sure that our customers are happy with our service," says Murray Edelman, executive vice president.

"Accomplishing that is going to take two things: knowledge and action. We have to know enough to position ourself as the customer's partner. And we have to be constantly taking action in response to what the customer tells us."

When we launched our strategic plan early in 1994, our third objective was focused on customer favorability. Since then, we have decided that customer satisfaction is a more significant measure than favorability (the difference is somewhat technical in addition to being significant), and we have changed this objective as a result.

***Weather Adjusted Retail KWH Sales (in billions)***




Staying competitive over the long term requires competitive prices. We know that, and therefore one of the aims of our strategic plan is to assure the competitiveness of Centerior's prices. But customer satisfaction is crucial, too: whenever multiple suppliers are approximately equal in price, the one that does the best job of satisfying the customer is likely to dominate the market.

In 1994 we expanded the means by which we gather information about our customers, their

opinion of our products and services and the potential for using electricity to meet more of their wants and needs. We also broadened the range of customers about whom we systematically collect information, including commercial and industrial customers in our research for the first time. The Customer Focus 2000 program, in which executives call on large customers, served the crucial purpose of helping to keep management in direct contact with the evolving needs of the businesses we serve and the realities of a fast-changing market.

The year brought new kinds of action, too. Both in Cleveland and in Toledo, making use of lessons learned in the aftermath of a catastrophic 1993 summer storm, we opened Emergency Information Centers. Activated nearly a dozen times by year-end, these centers provided better information about outages while freeing our dispatchers and system operation personnel to work uninterrupted on power restoration. Described by the Public Utilities Commission of Ohio as a model of emergency preparedness, they will be further improved in 1995 with computerized mapping and new information links to police departments.

In 1995, with so much information now available for use, our emphasis is shifting toward action. An extensive study of Centerior's residential, commercial and industrial customers has resulted in the development of six sets of recommendations having to do with power quality, service restoration, and other key factors in customer perception of our performance. Teams have been formed to move forward with the implementation of these recommendations in each market segment.

Probably the greatest potential for radical change in our ability to satisfy the people we serve lies in the work of two teams created late in 1994 to re-engineer Centerior's financial management and customer service operations. Early in 1995 these teams converged on a single shared objective: to develop plans for making our core processes—power generation, transmission, distribution, services—the responsibility of newly created strategic business units each of which would be a distinct profit center. In the next year this study of an SBU-based structure for Centerior could open the way to unprecedented gains not only in customer satisfaction but in efficiency as well.

## Employees

### *Maximize employee commitment to corporate objectives*

"Employee commitment—real commitment that goes beyond a simple willingness to trade a day's work for a day's pay—doesn't happen automatically," says senior vice president Fred Lange.

"You have to make it happen. The two most important things we're doing to make it happen at Centerior are pay for performance, with performance measured in terms of our strategic

objectives, and the empowerment of our people."

As the chairman's letter explains on page 3, the base salary of Centerior's senior executives has been frozen and their incentive compensation has been linked to the performance of our common stock. This is pay for performance in the most basic sense of the term, starting at the top.

In 1994 the incentive compensation opportunities of the Centerior work force at large were made dependent upon ten performance measures, each of them directly connected to revenues or costs or some other aspect of our strategic plan. The achievement of each measure required superior performance, a special challenge because of the 19% decrease in our work force since 1992. At least six had to be achieved before there could be any payout. Some of these measures became even more challenging—a few, such as production unit availability and power production cost, were put out of reach—by the protracted outage at the Perry plant. Against this background it is particularly impressive that by year-end the men and women of Centerior had achieved six of the measures and in doing so had earned a cash award of $500 per eligible employee.

For 1995 the performance measures have been refined to six: revenues, customer satisfaction, power production, cash flow, expenditures, and an employee achievement index. As in 1994, the goals connected with each measure are challenging. But they are also completely achievable. The employee index, for example, encompasses absenteeism, safety, and contributions to our Bright Ideas cost-saving program and the Leads Generate Sales revenue-building program. Its safety element goes beyond accident statistics and provides rewards for actions taken to prevent accidents. Half of total incentive compensation for 1995 will be keyed to these measures, and four of them must be achieved before any payout becomes possible. The other half will depend on the achievement of each employee's group or department goals.

Empowerment at Centerior means giving employees more control over their own jobs by providing them with the means and the opportunity to do those jobs better. It means enabling them to make decisions, to utilize the training, information and communications provided by the company, and ultimately to improve service to the customer. Pay for performance, because it gives employees a bigger stake in the results of their work, is an important part of this.

## Power Supply

***Reduce variable power supply costs to a more competitive level.***

"Performance and cost reduction are closely linked in the case of a power plant," says Don Shelton, the senior vice president with responsibility for Centerior's nuclear generating

facilities. "You work to improve performance because the results show up on the bottom line. Performance improvement is the biggest driver in cost control."

Variable power production costs, though listed fifth among our prime objectives, are far from last in importance or in priority. The goal for 1995 is 2.19 cents per kilowatt-hour. Over the long term we will be pursuing various ways of reducing these costs to the lowest possible level.

The job of improving output and performance—and thereby getting better financial results—is currently at very different stages at the two nuclear plants operated by Centerior. The Davis-Besse facility, which completed a lengthy and costly upgrading in 1985 and 1986, today is widely recognized as a world-class operation—as being, in fact, one of the top-performing nuclear facilities not only in the U.S. but the world. In 1994 it met or exceeded its objectives for availability, fuel and operation and maintenance cost per kilowatt-hour, and O&M and capital expenditures.

The challenge for Davis-Besse is to keep output at its current high level while shortening refueling outages and improving processes so that greater productivity can be achieved with a progressively smaller work force. The most persuasive evidence that this challenge is being met is Davis-Besse's success in meeting its 1994 objectives and the fact that its 1994 refueling outage was, at 46 days, the shortest in its history.

The near-term objective for the Perry plant, by contrast, is to improve production performance output by means of a three-year program that will be completed in 1996 after the next refueling outage. At that point the groundwork will be prepared for raising performance to the level of Davis-Besse.

O&M spending at Centerior's fossil-fueled plants was $78 million in 1994, compared with $80 million the year before. The 1995 budget calls for another reduction. We have initiatives under way to produce continuing reductions in future years. Among our options are predictive instead of preventive maintenance, and new team-building efforts focused on greater productivity.

We achieved our 1994 fuel cost goal of 1.35 cents per kilowatt-hour. Delivered fossil fuel costs for the year were $1.44 per million BTU's—well below our $1.50 goal.

Cleveland Electric Illuminating and Toledo Edison were two of only three Ohio utilities to reduce their total delivered coal costs per million BTU's during 1994. CEI's delivered fuel costs were the lowest in the state.

Our nuclear fuel costs were 1.022 cents per kilowatt-hour in 1994, well below 1993's 1.065 cents.

# Management's Statement of Responsibility for Financial Statements

The management of Centerior Energy Corporation is responsible for the consolidated financial statements in this Annual Report. The statements were prepared in accordance with generally accepted accounting principles. Under these principles, some of the recorded amounts are estimates which are based on an analysis of the best information available.

We maintain a system of internal accounting controls designed to assure that the financial records are substantially complete and accurate. The controls also are designed to help protect the assets and their related records. We structure our control procedures such that their costs do not exceed their benefits.

Our internal audit program monitors the internal accounting controls. This program gives us the opportunity to assess the adequacy and effectiveness of existing controls and to identify and institute changes where needed. In addition, an examination of our financial statements is conducted by Arthur Andersen LLP, independent public accountants, whose report appears below.

Our Board of Directors is responsible for determining whether management and the independent public accountants are carrying out their responsibilities. The Board is also responsible for making changes in management or independent public accountants if needed.

The Board has appointed an Audit Committee, comprised entirely of outside directors, which met two times in 1994. The Committee recommends annually to the Board the firm of independent public accountants to be retained for the ensuing year and reviews the audit approach used by the accountants plus the results of their audits. It also oversees the adequacy and effectiveness of our internal accounting controls and ensures that our accounting system produces financial statements which present fairly our financial position.

Gary R. Leidich

Gary R. Leidich
*Vice President and*
*Chief Financial Officer*

E. Lyle Pepin

E. Lyle Pepin
*Controller and*
*Chief Accounting Officer*

# Report of Independent Public Accountants

To the Share Owners and
Board of Directors of
Centerior Energy Corporation:

We have audited the accompanying consolidated balance sheet and consolidated statement of preferred stock of Centerior Energy Corporation (an Ohio corporation) and subsidiaries as of December 31, 1994 and 1993, and the related consolidated statements of income, retained earnings and cash flows for each of the three years in the period ended December 31, 1994. 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 financial position of Centerior Energy Corporation and subsidiaries as of December 31, 1994 and 1993, and the results of their operations and their cash flows for each of the three years in the period ended December 31, 1994, in conformity with generally accepted accounting principles.

As discussed further in Note 9, a change was made in the method of accounting for postretirement benefits other than pensions in 1993.

Arthur Andersen LLP

Cleveland, Ohio
February 17, 1995

# Management's Financial Analysis

## *Outlook*

### Strategic Plan

We made significant strides in achieving the objectives of our comprehensive strategic action plan announced in January 1994. The strategic plan was created to strengthen our financial and competitive position through the year 2001. Its objectives are to maximize share owner return, achieve profitable revenue growth, become an industry leader in customer satisfaction, build a winning employee team and attain increasingly competitive power supply costs. To achieve these objectives, we will continue to control expenditures and reduce our outstanding debt and preferred stock. In addition, we will increase revenues by finding new uses for existing assets and resources, implementing new marketing programs and restructuring rates when appropriate. We will also improve the operating performance of our generating plants and take other appropriate actions.

During 1994, we made progress toward most of our long-term objectives. We initiated a marketing plan designed to increase our retail revenues (exclusive of fuel cost recovery revenues and weather influences) by 2-3% annually through 2001. Our new customer service activities are intended to raise our customer satisfaction rating. Our employees achieved enough of their established objectives for the year to receive a $500 per eligible employee incentive compensation award. The work undertaken during refueling outages at the Davis-Besse Nuclear Power Station (Davis-Besse) and Perry Nuclear Power Plant Unit 1 (Perry Unit 1) as well as the outage work at our fossil-fueled plants should help us achieve our long-term objective of reducing variable power costs to a more competitive level. Another long-term objective to be achieved over the planning period is to provide share owners a total annual return greater than the Standard & Poor's Corporation (S&P) 500 Index. While there was a slight gain in the S&P 500 Index in 1994, electric utility stocks in general, and Centerior Energy Corporation (Centerior Energy) common stock in particular, declined sharply. The climb in interest rates and increased investor concern about the competitiveness of the electric utility industry caused the Dow Jones Utility Average to drop 21% in 1994. The total return on our common stock in 1994, including dividends, was -27%. Investors placed a lower valuation on our stock principally because of our high retail cost structure relative to certain neighboring utilities and municipal electric systems.

As discussed below, we are taking steps to improve our competitiveness. As these efforts unfold and if interest rates decline and investor concerns about the electric utility industry diminish, the total annual return for our common stock should improve. Further improvement in several key financial measures should lead to a higher investor valuation of Centerior Energy. Substantial progress in these areas was made in 1994. Strong cash flow continued in 1994 and fixed-income obligations were reduced by $136 million. Also, total operation and maintenance expenses declined $88 million, exclusive of one-time charges in 1993.

We are taking aggressive steps to increase revenues through our enhanced marketing plan and to control costs. The full impact of these efforts will take time. In the meantime, to increase share owner value, we must raise revenues by restructuring rates. Accordingly, we are preparing to file a request with The Public Utilities Commission of Ohio (PUCO) for our two utility subsidiaries, The Cleveland Electric Illuminating Company (Cleveland Electric) and The Toledo Edison Company (Toledo Edison) (collectively, the Operating Companies) to be effective in 1996. Meaningful cost control and marketing strategies will mitigate the need for additional rate increases and help us meet competition.

### Competition

We are implementing strategies designed to create and enhance our competitive advantages and to overcome the competitive disadvantages that we face due to regulatory and tax constraints and our high retail cost structure.

Currently our most pressing competition comes from municipal electric systems in our service area. Our rates are generally higher than those of municipal systems due largely to their exemption from taxation, the lower cost financing available to them, the continued availability to them of lower cost power through short-term power purchases and their access to cheaper governmental power. We are seeking to address the tax disparity through the legislative process. In 1994, the Ohio Governor's Tax Commission recommended the replacement of the gross receipts and personal property taxes currently levied only on investor-owned utilities and collected through rates with a different tax collected from customers of all electric utilities, including municipal systems. Investor-owned utilities would reduce rates upon repeal of the existing taxes. We are now working to submit this proposal to the Ohio legislature.

We face the threat that municipalities in our service area could establish new systems and continue expanding existing systems. We are responding with aggressive marketing programs and by emphasizing the value of our service and the risks of a municipal system: substantial, long-term debt; no guarantee of low-cost wholesale electricity; the difficulty of forecasting costs; and the uncertainty of market share as a result of our aggressive competition. Generally, these municipalities have determined that developing a system is not feasible or have agreed with us not to pursue development of a system at

this time. Although some communities continue to be interested in municipalization, we believe that we offer the best value and most reliable source of electric service in our territory.

The largest municipal system in our service area, Cleveland Public Power (CPP), is constructing new transmission and distribution facilities extending into eastern portions of Cleveland. CPP also plans to expand to western portions of Cleveland. CPP's expansion reduced our annual net income by about $4 million in 1993 and $3 million in 1994. We estimate our net income will continue to be reduced by an additional $4 million to $5 million each year in the 1995-1999 period because of CPP's expansion. Despite CPP's expansion efforts, we have been successful in retaining most of the large industrial and commercial customers in the expansion areas by providing economic incentives in exchange for sole-supplier contracts. We have similar contracts with customers in other parts of our service area. More than 80% of our industrial revenues under contract will not be up for renewal until 1997 or later. As these contracts expire, we expect to renegotiate them and retain the customers. In addition, an increasing number of CPP customers are converting back to our service.

The Energy Policy Act of 1992 will increase competition in the electric utility industry by allowing broader access to a utility's transmission system. It should not significantly increase the competitive threat to us since we have been required to wheel electricity to municipal systems in our service area since 1977 under operating licenses for our nuclear generating units. Further, the government could eventually require utilities to deliver power from other utilities or generation sources to their retail customers. To combat this threat, we are offering incentives such as energy-efficiency improvements and reductions in demand charges for increased electricity usage to our industrial and commercial customers in return for long-term commitments.

### Rate Matters

Under the Rate Stabilization Program discussed in Note 7, we agreed to freeze base rates until 1996 and limit rate increases through 1998. In exchange, we are permitted to defer through 1995 and subsequently recover certain costs not currently recovered in rates and to accelerate the amortization of certain benefits. Amortization and recovery of the deferrals are expected to begin in 1996 with future rate recognition and will continue over the average life of the related assets, or between 17 and 30 years. The continued use of these regulatory accounting measures in 1995 will be dependent upon our continuing assessment and conclusion that there will be probable recovery of such deferrals in future rates. Our analysis leading to certain year-end 1993 financial actions and our strategic plan also included an evaluation of our regulatory accounting measures. See Regulatory Accounting below and Note 7. We decided that, once the deferral of expenses and acceleration of benefits under the Rate Stabilization Program are completed in 1995, we should no longer plan to use these measures to the extent we have in the past.

### Regulatory Accounting

As described in Notes 1(a) and 7, the Operating Companies comply with the provisions of Statement of Financial Accounting Standards (SFAS) 71. We continually monitor changes in market and regulatory conditions and consider the effects of such changes in assessing the continuing applicability of SFAS 71. Criteria that could give rise to discontinuation of the application of SFAS 71 include: (1) increasing competition which significantly restricts the Operating Companies' ability to establish rates to recover operating costs, return requirements and the amortization of regulatory assets and (2) a significant change in the manner in which rates are set by the PUCO from cost-based regulations to some other form of regulations. In the event we determine that the Operating Companies no longer meet the criteria for following SFAS 71, we would be required to record a before-tax charge to write off the regulatory assets shown in Note 7. In addition, the Operating Companies would be required to evaluate whether the changes in the competitive and regulatory environment which led to discontinuing the application of SFAS 71 would also result in an impairment of the net book value of their property, plant and equipment.

The write-off in 1993 of the phase-in deferred operating expenses and carrying charges (phase-in deferrals) discussed in Note 7 resulted from our conclusion that projected revenues for the 1994-1998 period would not provide for recovery of such deferrals as scheduled by the PUCO orders. This short time frame for recovery of the phase-in deferrals is a requirement under the accounting standard for phase-in plans of regulated enterprises, SFAS 92. The remaining recovery periods for all remaining regulatory assets are between 17 and 34 years. We believe the Operating Companies' rates will provide for recovery of these assets over the relevant periods and SFAS 71 continues to apply.

### Nuclear Operations

We have interests in three nuclear generating units — Davis-Besse, Perry Unit 1 and Beaver Valley Power Station Unit 2 (Beaver Valley Unit 2) — and operate the first two. Davis-Besse and Beaver Valley Unit 2 have been operating extremely well, with each unit having a three-year availability average at year-end 1994 that exceeded the three-year industry average of 80% for similar reactors. However, the three-year availability av-

erage of Perry Unit 1 was below the three-year industry availability average for that reactor type.

In 1994, Davis-Besse had an availability factor of 88%. Further, Davis-Besse completed the shortest refueling and maintenance outage in its history in 1994, returning to service just 46 days after shutting down. We are in the process of upgrading Perry Unit 1 to the same level. For seven months in 1994, Perry Unit 1 was out of service for its fourth refueling and maintenance outage. Work was also performed in connection with the comprehensive course of action developed in 1993 to improve the operating performance of Perry Unit 1. Work in connection with that course of action is ongoing.

We externally fund the estimated costs for the future decommissioning of our nuclear units. In 1993 and 1994, we increased our decommissioning expense accruals because of revisions in our cost estimates. See Note 1(d).

Our nuclear units may be impacted by activities or events beyond our control. Operating nuclear units have experienced unplanned outages or extensions of scheduled outages because of equipment problems or new regulatory requirements. A major accident at a nuclear facility anywhere in the world could cause the Nuclear Regulatory Commission to limit or prohibit the operation or licensing of any domestic nuclear unit. If one of our nuclear units is taken out of service for an extended period for any reason, including an accident at such unit or any other nuclear facility, we cannot predict whether regulatory authorities would impose unfavorable rate treatment. Such treatment could include taking our affected unit out of rate base, thereby not permitting us to recover our investment in and earn a return on it, or disallowing certain construction or maintenance costs. An extended outage coupled with unfavorable rate treatment could have a material adverse effect on our financial condition and results of operations.

### Hazardous Waste Disposal Sites

The Comprehensive Environmental Response, Compensation and Liability Act of 1980 as amended (Superfund) established programs addressing the cleanup of hazardous waste disposal sites, emergency preparedness and other issues. The Operating Companies have been named as "potentially responsible parties" (PRPs) for three sites listed on the Superfund National Priorities List (Superfund List) and are aware of their potential involvement in the cleanup of several other sites. Allegations that the Operating Companies disposed of hazardous waste at these sites, and the amounts involved, are often unsubstantiated and subject to dispute. Superfund provides that all PRPs for a particular site can be held liable on a joint and several basis. If the Operating Companies were held liable for 100% of the cleanup costs of all of the sites referred to above, the cost could be as high as $500 million. However, we believe that the actual cleanup costs will be substantially lower than $500 million, that the Operating Companies' share of any cleanup costs will be substantially less than 100% and that most of the other PRPs are financially able to contribute their share. The Operating Companies have accrued a liability totaling $13 million at December 31, 1994 based on estimates of the costs of cleanup and their proportionate responsibility for such costs. We believe that the ultimate outcome of these matters will not have a material adverse effect on our financial condition or results of operations.

### Merger of the Operating Companies

We continue to seek the necessary regulatory approvals to complete the merger of the Operating Companies which we announced in 1994. The Operating Companies plan to seek preferred stock share owner approval in mid-1995. The merger is expected to be effective in 1995.

### Inflation

Although the rate of inflation has eased in recent years, we are still affected by even modest inflation which causes increases in the unit cost of labor, materials and services.

## *Capital Resources and Liquidity*

### 1992-1994 Cash Requirements

We need cash for normal corporate operations, the mandatory retirement of securities and constructing and modifying facilities. Construction is needed to meet anticipated demand for electric service, comply with government regulations and protect the environment. Over the three-year period 1992-1994, construction and mandatory retirement needs totaled approximately $1.3 billion. In addition, we exercised options to redeem and purchase approximately $900 million of our securities.

We raised $1.7 billion through security issues and term bank loans during the 1992-1994 period. The Operating Companies also utilized short-term borrowings to help meet cash needs. Although write-offs of our Perry Nuclear Power Plant Unit 2 (Perry Unit 2) investment and phase-in deferrals in 1993 negatively affected earnings, they did not adversely affect cash flow. See Notes 4(b) and 7.

### 1995 and Beyond Cash Requirements

Estimated cash requirements for 1995-1999 for Cleveland Electric and Toledo Edison, respectively, are $802 million and $288 million for construction and $832 million and $378 million for the mandatory redemption of debt and preferred stock. Cleveland Electric expects to finance externally about two-thirds of its 1995 cash requirements of approximately $451 million and about one-third of its

1996 cash requirements of approximately $320 million. Toledo Edison expects to meet nearly all of its 1995 and 1996 cash requirements of approximately $145 million and $154 million, respectively, through internal cash generation and current cash resources. The Operating Companies expect to meet nearly all of their 1997-1999 requirements through internal cash generation and current cash resources. If economical, additional securities may be redeemed under optional redemption provisions. We expect that our continued strong cash flow will reduce borrowing requirements and outstanding debt and preferred stock during this period.

Cash expenditures to comply with the Clean Air Act Amendments of 1990 (Clean Air Act) are estimated to be approximately $87 million over the 1995-1999 period. See Note 4(a).

### Liquidity

Additional first mortgage bonds may be issued by the Operating Companies under their respective mortgages on the basis of property additions, cash or refundable first mortgage bonds. If the applicable interest coverage test is met, each Operating Company may issue first mortgage bonds on the basis of property additions and, under certain circumstances, refundable bonds. At December 31, 1994, Cleveland Electric and Toledo Edison would have been permitted to issue approximately $487 million and $525 million of additional first mortgage bonds, respectively.

The Operating Companies also are able to raise funds through the sale of subordinated debt and preferred and preference stock. Under its articles of incorporation, Toledo Edison cannot issue preferred stock unless certain earnings coverage requirements are met. At December 31, 1994, Toledo Edison would have been permitted to issue approximately $28 million of additional preferred stock at an assumed dividend rate of 12%. There are no restrictions on Cleveland Electric's ability to issue preferred or preference stock or Toledo Edison's ability to issue preference stock.

Centerior Energy may raise funds through the sale of common stock under various employee and share owner plans. In 1995, the Operating Companies plan to raise funds through the sale of first mortgage bonds and the collateralization of accounts receivable.

We have a $205 million revolving credit facility which runs through mid-1996. See Note 12. We had $186 million of cash and temporary cash investments at the end of 1994. The Operating Companies are unable to issue commercial paper because of their below investment grade commercial paper ratings.

The foregoing financing resources are expected to be sufficient for the Operating Companies' needs over the next several years. However, the availability and cost of capital to meet their external financing needs also depend upon such factors as financial market conditions and their credit ratings. Current credit ratings for the Operating Companies are as follows:

| | S&P | Moody's Investors Service, Inc. |
|---|---|---|
| First mortgage bonds | BB | Ba2 |
| Unsecured notes for Cleveland Electric | B+ | Ba3 |
| Unsecured notes for Toledo Edison | B+ | B1 |
| Preferred stock | B | b2 |

In 1994, the common stock dividend was lowered which reduced our cash outflow by over $110 million annually. We are using the cash to redeem debt and preferred stock more quickly than would otherwise be the case. This has helped improve our capitalization structure and fixed charge coverage ratios, both of which are key measures considered by securities rating agencies in determining credit ratings. Improved credit ratings and less outstanding debt and preferred stock, in turn, will lower our interest costs and preferred dividends.

## *Results of Operations*

### 1994 vs. 1993

Factors contributing to the 2.1% decrease in 1994 operating revenues are as follows:

| Increase (Decrease) in Operating Revenues | Millions of Dollars |
|---|---|
| KWH Sales Volume and Mix | $ 10 |
| Wholesale Revenues | (47) |
| Fuel Cost Recovery Revenues | (22) |
| Miscellaneous Revenues | 6 |
| Total | $(53) |

Centerior Energy experienced good retail kilowatt-hour sales growth in the industrial and commercial categories in 1994; the sales growth for the residential category was lessened by weather conditions, particularly during the summer. The revenue decrease resulted primarily from milder weather conditions in 1994 and 39% lower wholesale sales. Weather reduced base rate revenues approximately $15 million from the 1993 amount. Although total sales decreased by 1.9%, industrial sales increased 3.3% on the strength of increased sales to large automotive manufacturers and the broad-based, smaller industrial customer group. This growth substantiated an economic resurgence in our service area, particularly in Northwestern Ohio. Residential and commercial sales increased 0.1% and 2.4%, respectively. Other sales decreased by 28% because of the lower sales to wholesale customers attributable to expiration of a wholesale power agreement, softer wholesale market conditions and limited power availability for bulk power transactions at certain times because of generating plant outages. Lower 1994 fuel cost recovery revenues resulted from favorable changes in the fuel cost factors. The weighted averages

of these factors dropped by 5% and 6% for Cleveland Electric and Toledo Edison, respectively.

For 1994, operating revenues were 31% residential, 30% commercial, 31% industrial and 8% other and kilowatt-hour sales were 24% residential, 25% commercial, 41% industrial and 10% other. The average prices per kilowatt-hour for residential, commercial and industrial customers were \$.11, \$.10 and \$.06, respectively.

Operating expenses were 15% lower in 1994. Operation and maintenance expenses for 1993 included \$218 million of net benefit expenses related to an early retirement program, called the Voluntary Transition Program (VTP), and other charges totaling \$54 million. Two other significant reasons for lower operation and maintenance expenses in 1994 were a smaller work force and ongoing cost reduction measures. More nuclear generation and less coal-fired generation accounted for a large part of the lower fuel and purchased power expenses in 1994. Depreciation and amortization expenses increased primarily because of higher nuclear plant decommissioning expenses as discussed in Note 1(d). Deferred operating expenses were greater primarily because of the write-off of \$172 million of phase-in deferred operating expenses in 1993 as discussed in Note 7. The 1993 deferrals also included \$84 million of postretirement benefit curtailment cost deferrals related to the VTP. See Note 9(b). Federal income taxes increased as a result of higher pretax operating income.

As discussed in Note 4(b), \$583 million of our Perry Unit 2 investment was written off in 1993. Also, as discussed in Note 7, phase-in deferred carrying charges of \$705 million were written off in 1993. The change in the federal income tax credit amounts for nonoperating income was attributable to these write-offs.

### 1993 vs. 1992

Factors contributing to the 1.5% increase in 1993 operating revenues are as follows:

| Increase (Decrease) in Operating Revenues | Millions of Dollars |
|---|---|
| KWH Sales Volume and Mix | \$ 65 |
| Base Rates and Miscellaneous | (18) |
| Fuel Cost Recovery Revenues | (11) |
| Total | \$ 36 |

The revenue increase resulted primarily from the different weather conditions and the changes in the composition of the sales mix among customer categories. Weather accounted for approximately \$47 million of higher 1993 base rate revenues. Hot summer weather in 1993 boosted residential, commercial and wholesale kilowatt-hour sales. In contrast, the 1992 summer was the coolest in 56 years for Northern Ohio. Residential and commercial sales also increased as a result of colder late-winter temperatures in 1993 which increased electric heating-related demand. As a result, total sales increased 3.1% in 1993. Residential and commercial sales increased 4.6% and 3.1%, respectively. Industrial sales increased 1.2%. Increased sales to large automotive manufacturers, petroleum refiners and the broad-based, smaller industrial customer group were partially offset by lower sales to large steel industry customers. Other sales increased 5.9% because of increased sales to wholesale customers. Base rates and miscellaneous revenues decreased in 1993 primarily from lower revenues under contracts having reduced rates with certain large customers and a declining rate structure tied to usage. The contracts have been negotiated to meet competition and encourage economic growth. The decrease in 1993 fuel cost recovery revenues resulted from changes in the fuel cost factors. The weighted average of these factors increased slightly for Toledo Edison but decreased 5% for Cleveland Electric.

For 1993, operating revenues were 31% residential, 29% commercial, 30% industrial and 10% other and kilowatt-hour sales were 23% residential, 24% commercial, 39% industrial and 14% other. The average prices per kilowatt-hour for residential, commercial and industrial customers were \$.11, \$.10 and \$.06, respectively. The changes from 1992 were not significant.

Operating expenses increased 14% in 1993. The increase in total operation and maintenance expenses resulted from the \$218 million of net benefit expenses related to the VTP, other charges totaling \$54 million and an increase in other operation and maintenance expenses. The increase in other operation and maintenance expenses resulted from higher environmental expenses, power restoration and repair expenses following a July 1993 storm in the Cleveland area, and an increase in other postretirement benefit expenses. See Note 9 for information on retirement benefits. Deferred operating expenses decreased because of the write-off of the phase-in deferred operating expenses in 1993. Federal income taxes decreased as a result of lower pretax operating income.

As mentioned above, \$583 million of our Perry Unit 2 investment was written off in 1993. Credits for carrying charges recorded in nonoperating income decreased because of the write-off of the phase-in deferred carrying charges in 1993. The federal income tax credit for nonoperating income in 1993 resulted from the write-offs.

# Income Statement

*Centerior Energy Corporation and Subsidiaries*

| | For the years ended December 31, 1994 | 1993 | 1992 |
|---|---|---|---|
| | (millions of dollars, except per share amounts) | | |
| **Operating Revenues** | $2,421 | $2,474 | $2,438 |
| **Operating Expenses** | | | |
| Fuel and purchased power | 442 | 474 | 473 |
| Other operation and maintenance | 595 | 652 | 623 |
| Generation facilities rental expense, net | 160 | 159 | 161 |
| Early retirement program expenses and other | — | 272 | — |
| Total operation and maintenance | 1,197 | 1,557 | 1,257 |
| Depreciation and amortization | 278 | 258 | 256 |
| Taxes, other than federal income taxes | 309 | 312 | 318 |
| Deferred operating expenses, net | (55) | 23 | (52) |
| Federal income taxes | 114 | 11 | 122 |
| | 1,843 | 2,161 | 1,901 |
| **Operating Income** | 578 | 313 | 537 |
| **Nonoperating Income (Loss)** | | | |
| Allowance for equity funds used during construction | 5 | 5 | 2 |
| Other income and deductions, net | 8 | (6) | 9 |
| Write-off of Perry Unit 2 | — | (583) | — |
| Deferred carrying charges, net | 40 | (649) | 100 |
| Federal income taxes — credit (expense) | (6) | 398 | (7) |
| | 47 | (835) | 104 |
| **Income (Loss) Before Interest Charges and Preferred Dividends** | 625 | (522) | 641 |
| **Interest Charges and Preferred Dividends** | | | |
| Debt interest | 361 | 359 | 365 |
| Allowance for borrowed funds used during construction | (6) | (5) | (1) |
| Preferred dividend requirements of subsidiaries | 66 | 67 | 65 |
| | 421 | 421 | 429 |
| **Net Income (Loss)** | $ 204 | $ (943) | $ 212 |
| **Average Number of Common Shares Outstanding (millions)** | 147.8 | 144.9 | 141.7 |
| **Earnings (Loss) Per Common Share** | $ 1.38 | $(6.51) | $ 1.50 |
| **Dividends Declared Per Common Share** | $ .80 | $ 1.60 | $ 1.60 |

# Retained Earnings

| | For the years ended December 31, 1994 | 1993 | 1992 |
|---|---|---|---|
| | (millions of dollars) | | |
| **Retained Earnings (Deficit) at Beginning of Year** | $(523) | $ 652 | $ 669 |
| **Additions** | | | |
| Net income (loss) | 204 | (943) | 212 |
| **Deductions** | | | |
| Common stock dividends | (118) | (231) | (226) |
| Other, primarily preferred stock redemption expenses of subsidiaries | (1) | (1) | (3) |
| Net Increase (Decrease) | 85 | (1,175) | (17) |
| **Retained Earnings (Deficit) at End of Year** | $(438) | $ (523) | $ 652 |

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

# Balance Sheet

| | December 31, 1994 | December 31, 1993 |
|---|---|---|
| | (millions of dollars) | |
| *ASSETS* | | |
| **Property, Plant and Equipment** | | |
| Utility plant in service | $ 9,770 | $ 9,571 |
| Less: accumulated depreciation and amortization | 2,906 | 2,677 |
| | 6,864 | 6,894 |
| Construction work in progress | 129 | 181 |
| | 6,993 | 7,075 |
| Nuclear fuel, net of amortization | 293 | 344 |
| Other property, less accumulated depreciation | 50 | 41 |
| | 7,336 | 7,460 |
| **Current Assets** | | |
| Cash and temporary cash investments | 186 | 225 |
| Amounts due from customers and others, net | 211 | 221 |
| Unbilled revenues | 93 | 124 |
| Materials and supplies, at average cost | 139 | 136 |
| Fossil fuel inventory, at average cost | 29 | 32 |
| Taxes applicable to succeeding years | 252 | 250 |
| Other | 16 | 5 |
| | 926 | 993 |
| **Deferred Charges and Other Assets** | | |
| Amounts due from customers for future federal income taxes | 1,046 | 968 |
| Unamortized loss from Beaver Valley Unit 2 sale | 101 | 105 |
| Unamortized loss on reacquired debt | 86 | 92 |
| Carrying charges and operating expenses | 957 | 862 |
| Nuclear plant decommissioning trusts | 82 | 56 |
| Other | 157 | 174 |
| | 2,429 | 2,257 |
| Total Assets | $10,691 | $10,710 |

*The accompanying notes are an integral part of this statement.*

| | December 31, 1994 | December 31, 1993 |
|---|---|---|
| | (millions of dollars) | |
| *CAPITALIZATION AND LIABILITIES* | | |
| **Capitalization** | | |
| Common shares, without par value (stated value of $357 million and $345 million for 1994 and 1993, respectively): 180 million authorized; 148 million (excluding 2.7 million shares in Treasury) and 147 million (excluding 2.7 million shares in Treasury) outstanding in 1994 and 1993, respectively | $ 2,320 | $ 2,308 |
| Retained earnings (deficit) | (438) | (523) |
| Common stock equity | 1,882 | 1,785 |
| Preferred stock | | |
| With mandatory redemption provisions | 253 | 313 |
| Without mandatory redemption provisions | 451 | 451 |
| Long-term debt | 3,697 | 4,019 |
| | 6,283 | 6,568 |
| **Current Liabilities** | | |
| Current portion of long-term debt and preferred stock | 373 | 127 |
| Current portion of nuclear fuel lease obligations | 83 | 111 |
| Accounts payable | 144 | 188 |
| Accrued taxes | 384 | 378 |
| Accrued interest | 90 | 87 |
| Other | 75 | 75 |
| | 1,149 | 966 |
| **Deferred Credits and Other Liabilities** | | |
| Unamortized investment tax credits | 279 | 329 |
| Accumulated deferred federal income taxes | 1,778 | 1,579 |
| Unamortized gain from Bruce Mansfield Plant sale | 525 | 551 |
| Accumulated deferred rents for Bruce Mansfield Plant and Beaver Valley Unit 2 | 139 | 128 |
| Nuclear fuel lease obligations | 219 | 254 |
| Retirement benefits | 176 | 160 |
| Other | 143 | 175 |
| | 3,259 | 3,176 |
| Total Capitalization and Liabilities | $10,691 | $10,710 |

# Cash Flows

Centerior Energy Corporation and Subsidiaries

| | For the years ended December 31, | | |
|---|---|---|---|
| | 1994 | 1993 | 1992 |
| | (millions of dollars) | | |
| **Cash Flows from Operating Activities (1)** | | | |
| Net Income (Loss) | $ 204 | $ (943) | $ 212 |
| Adjustments to Reconcile Net Income (Loss) to Cash from Operating Activities: | | | |
| Depreciation and amortization | 278 | 258 | 256 |
| Deferred federal income taxes | 95 | (452) | 95 |
| Investment tax credits, net | — | — | (14) |
| Unbilled revenues | 31 | (10) | (6) |
| Deferred fuel | (17) | 5 | 1 |
| Deferred carrying charges, net | (40) | 649 | (100) |
| Leased nuclear fuel amortization | 98 | 86 | 126 |
| Deferred operating expenses, net | (55) | 23 | (52) |
| Allowance for equity funds used during construction | (5) | (5) | (2) |
| Noncash early retirement program expenses, net | — | 208 | — |
| Write-off of Perry Unit 2 | — | 583 | — |
| Changes in amounts due from customers and others, net | 10 | 1 | 7 |
| Changes in inventories | — | 26 | (10) |
| Changes in accounts payable | (44) | 45 | (5) |
| Changes in working capital affecting operations | — | 25 | 8 |
| Other noncash items | 14 | 18 | 3 |
| Total Adjustments | 365 | 1,460 | 307 |
| Net Cash from Operating Activities | 569 | 517 | 519 |
| **Cash Flows from Financing Activities (2)** | | | |
| Bank loans, commercial paper and other short-term debt | — | (50) | 50 |
| First mortgage bond issues | 77 | 300 | 600 |
| Secured medium-term note issues | — | 128 | 138 |
| Term bank loans and other long-term debt issues | — | 40 | 135 |
| Preferred stock issues | — | 100 | 74 |
| Common stock issues | 12 | 71 | 53 |
| Reacquired common stock | — | 1 | (3) |
| Maturities, redemptions and sinking funds | (214) | (434) | (1,013) |
| Nuclear fuel lease obligations | (110) | (106) | (117) |
| Common stock dividends paid | (118) | (231) | (226) |
| Premiums, discounts and expenses | (1) | (13) | (14) |
| Net Cash from Financing Activities | (354) | (194) | (323) |
| **Cash Flows from Investing Activities (2)** | | | |
| Cash applied to construction | (205) | (209) | (200) |
| Interest capitalized as allowance for borrowed funds used during construction | (6) | (5) | (1) |
| Sale and leaseback restructuring fees | — | — | (43) |
| Contributions to nuclear plant decommissioning trusts | (26) | (9) | (8) |
| Other cash received (applied) | (17) | 32 | (28) |
| Net Cash from Investing Activities | (254) | (191) | (280) |
| **Net Change in Cash and Temporary Cash Investments** | (39) | 132 | (84) |
| **Cash and Temporary Cash Investments at Beginning of Year** | 225 | 93 | 177 |
| **Cash and Temporary Cash Investments at End of Year** | $ 186 | $ 225 | $ 93 |

*(1) Interest paid (net of amounts capitalized) was $300 million, $295 million and $299 million in 1994, 1993 and 1992, respectively. Income taxes paid were $6 million, $50 million and $32 million in 1994, 1993 and 1992, respectively.*

*(2) Increases in Nuclear Fuel and Nuclear Fuel Lease Obligations in the Balance Sheet resulting from the noncash capitalizations under nuclear fuel agreements are excluded from this statement.*

*The accompanying notes are an integral part of this statement.*

# Statement of Preferred Stock



| | 1994 Shares Outstanding | Current Call Price Per Share | December 31, 1994 | December 31, 1993 |
|---|---|---|---|---|
| | | | (millions of dollars) | |
| **CLEVELAND ELECTRIC** | | | | |
| Without par value, 4,000,000 preferred shares authorized | | | | |
| Subject to mandatory redemption: | | | | |
| $ 7.35 Series C | 140,000 | $ 101.00 | $ 14 | $ 15 |
| 88.00 Series E | 18,000 | 1,019.13 | 18 | 21 |
| Adjustable Series M | 100,000 | 100.00 | 10 | 20 |
| 9.125 Series N | 410,766 | 102.03 | 41 | 59 |
| 91.50 Series Q | 75,000 | — | 75 | 75 |
| 88.00 Series R | 50,000 | — | 50 | 50 |
| 90.00 Series S | 75,000 | — | 74 | 74 |
| | | | 282 | 314 |
| Less: Current maturities | | | 36 | 29 |
| | | | 246 | 285 |
| Not subject to mandatory redemption: | | | | |
| $ 7.40 Series A | 500,000 | 101.00 | 50 | 50 |
| 7.56 Series B | 450,000 | 102.26 | 45 | 45 |
| Adjustable Series L | 500,000 | 100.00 | 49 | 49 |
| 42.40 Series T | 200,000 | — | 97 | 97 |
| | | | 241 | 241 |
| **TOLEDO EDISON** | | | | |
| $100 par value, 3,000,000 preferred shares authorized and $25 par value, 12,000,000 preferred shares authorized | | | | |
| Subject to mandatory redemption: | | | | |
| $100 par $9.375 | 83,500 | 101.98 | 8 | 10 |
| 25 par 2.81 | 400,000 | 25.62 | 10 | 30 |
| | | | 18 | 40 |
| Less: Current maturities | | | 11 | 12 |
| | | | 7 | 28 |
| Not subject to mandatory redemption: | | | | |
| $100 par $ 4.25 | 160,000 | 104.625 | 16 | 16 |
| 4.56 | 50,000 | 101.00 | 5 | 5 |
| 4.25 | 100,000 | 102.00 | 10 | 10 |
| 8.32 | 100,000 | 102.46 | 10 | 10 |
| 7.76 | 150,000 | 102.437 | 15 | 15 |
| 7.80 | 150,000 | 101.65 | 15 | 15 |
| 10.00 | 190,000 | 101.00 | 19 | 19 |
| 25 par 2.21 | 1,000,000 | 25.25 | 25 | 25 |
| 2.365 | 1,400,000 | 27.75 | 35 | 35 |
| Series A Adjustable | 1,200,000 | 25.75 | 30 | 30 |
| Series B Adjustable | 1,200,000 | 25.75 | 30 | 30 |
| | | | 210 | 210 |
| **CENTERIOR ENERGY** | | | | |
| Without par value, 5,000,000 preferred shares authorized, none outstanding | | | — | — |
| **Total Preferred Stock, with Mandatory Redemption Provisions** | | | $253 | $313 |
| **Total Preferred Stock, without Mandatory Redemption Provisions** | | | $451 | $451 |

*The accompanying notes are an integral part of this statement.*

# Notes to the Financial Statements

## *(1) Summary of Significant Accounting Policies*

### (a) General

Centerior Energy is a holding company with two electric utility subsidiaries, Cleveland Electric and Toledo Edison. The consolidated financial statements also include the accounts of Centerior Energy's wholly owned subsidiary, Centerior Service Company (Service Company), and Centerior Energy's four other wholly owned subsidiaries, which in the aggregate are not material. During 1994, Cleveland Electric transferred its common stock investments in three wholly owned subsidiaries to Centerior Energy via property dividends and Centerior Energy formed the fourth wholly owned subsidiary. The Service Company provides management, financial, administrative, engineering, legal and other services at cost to Centerior Energy, the Operating Companies and the other subsidiaries. The Operating Companies operate as separate companies, each serving the customers in its service area. The preferred stock, first mortgage bonds and other debt obligations of the Operating Companies are outstanding securities of the issuing utility. All significant intercompany items have been eliminated in consolidation.

Centerior Energy and the Operating Companies follow the Uniform System of Accounts prescribed by the Federal Energy Regulatory Commission and adopted by the PUCO. Rate-regulated utilities are subject to SFAS 71 which governs accounting for the effects of certain types of rate regulation. Pursuant to SFAS 71, certain incurred costs are deferred for recovery in future rates. See Note 7. The Service Company follows the Uniform System of Accounts for Mutual Service Companies prescribed by the Securities and Exchange Commission (SEC) under the Public Utility Holding Company Act of 1935.

The Operating Companies are members of the Central Area Power Coordination Group (CAPCO). Other members are Duquesne Light Company, Ohio Edison Company and its wholly owned subsidiary, Pennsylvania Power Company. The members have constructed and operate generation and transmission facilities for their use.

### (b) Revenues

Customers are billed on a monthly cycle basis for their energy consumption based on rate schedules or contracts authorized by the PUCO or on ordinances of individual municipalities. An accrual is made at the end of each month to record the estimated amount of unbilled revenues for kilowatt-hours sold in the current month but not billed by the end of that month.

A fuel factor is added to the base rates for electric service. This factor is designed to recover from customers the costs of fuel and most purchased power. It is reviewed and adjusted semiannually in a PUCO proceeding.

### (c) Fuel Expense

The cost of fossil fuel is charged to fuel expense based on inventory usage. The cost of nuclear fuel, including an interest component, is charged to fuel expense based on the rate of consumption. Estimated future nuclear fuel disposal costs are being recovered through base rates.

The Operating Companies defer the differences between actual fuel costs and estimated fuel costs currently being recovered from customers through the fuel factor. This matches fuel expenses with fuel-related revenues.

Owners of nuclear generating plants are assessed by the federal government for the cost of decontamination and decommissioning of nuclear enrichment facilities operated by the United States Department of Energy. The assessments are based upon the amount of enrichment services used in prior years and cannot be imposed for more than 15 years (to 2007). The Operating Companies have accrued the liability for their share of the total assessments. These costs have been recorded in a deferred charge account since the PUCO is allowing the Operating Companies to recover the assessments through their fuel cost factors.

### (d) Depreciation and Amortization

The cost of property, plant and equipment is depreciated over their estimated useful lives on a straight-line basis. The annual straight-line depreciation provision for nonnuclear property expressed as a percent of average depreciable utility plant in service was 3.4% in 1994, 3.5% in 1993 and 3.4% in 1992. The annual straight-line depreciation rate for nuclear property is 2.5%.

The Operating Companies accrue the estimated costs of decommissioning their three nuclear generating units. The accruals are required to be funded in an external trust. The PUCO requires that the expense and payments to the external trusts be determined on a levelized basis by dividing the unrecovered decommissioning costs in current dollars by the remaining years in the licensing period of each unit. This methodology requires that the net earnings on the trusts be reinvested therein with the intent of allowing net earnings to offset inflation. The PUCO requires that the estimated costs of decommissioning and the funding level be reviewed at least every five years.

In 1994, the Operating Companies increased their annual decommissioning expense accruals to $24 million from the $8 million level in 1992. The accruals are reflected in current rates. The increased accruals were derived from recently updated, site-specific studies for each of the units. The revised estimates reflect the DECON method of decommissioning (prompt decontamination), and the locations and cost characteristics specific to the units, and include costs associated with decontamination, dismantlement and site restoration.

The revised estimates for the units in 1993 and 1992 dollars and in dollars at the time of license expiration, assuming a 4% annual inflation rate, are as follows:

| Generating Unit | License Expiration Year | Amount | Future Amount |
|---|---|---|---|
| | | (millions of dollars) | |
| Davis-Besse | 2017 | $346(1) | $ 862 |
| Perry Unit 1 | 2026 | 256(1) | 908 |
| Beaver Valley Unit 2 | 2027 | 114(2) | 423 |
| Total | | $716 | $2,193 |

(1) Dollar amounts in 1993 dollars.
(2) Dollar amounts in 1992 dollars.

The updated estimates reflect substantial increases from the prior PUCO-recognized aggregate estimates of $257 million in 1987 and 1986 dollars.

The classification, Accumulated Depreciation and Amortization, in the Balance Sheet at December 31, 1994 includes $98 million of decommissioning costs previously expensed and the earnings on the external trust funding. This amount exceeds the Balance Sheet amount of the external Nuclear Plant Decommissioning Trusts because the reserve began prior to the external trust funding. The trust earnings are recorded as an increase to the trust assets and the related component of the decommissioning reserve (included in Accumulated Depreciation and Amortization).

The staff of the SEC has questioned certain of the current accounting practices of the electric utility industry, including those of the Operating Companies, regarding the recognition, measurement and classification of decommissioning costs for nuclear generating stations in the financial statements. In response to these questions, the Financial Accounting Standards Board is reviewing the accounting for removal costs, including decommissioning. If such current accounting practices are changed, the annual provision for decommissioning could increase; the estimated cost for decommissioning could be recorded as a liability rather than as accumulated depreciation; and trust fund income from the external decommissioning trusts could be reported as investment income rather than as a reduction to decommissioning expense.

### (e) Property, Plant and Equipment

Property, plant and equipment are stated at original cost less amounts ordered by the PUCO to be written off. Construction costs include related payroll taxes, retirement benefits, fringe benefits, management and general overheads and allowance for funds used during construction (AFUDC). AFUDC represents the estimated composite debt and equity cost of funds used to finance construction. This noncash allowance is credited to income. The AFUDC rates averaged 9.8% in 1994, 9.9% in 1993 and 10.8% in 1992.

Maintenance and repairs for plant and equipment are charged to expense as incurred. The cost of replacing plant and equipment is charged to the utility plant accounts. The cost of property retired plus removal costs, after deducting any salvage value, is charged to the accumulated provision for depreciation.

### (f) Deferred Gain and Loss from Sales of Utility Plant

The sale and leaseback transactions discussed in Note 2 resulted in a net gain for the sale of the Bruce Mansfield Generating Plant (Mansfield Plant) and a net loss for the sale of Beaver Valley Unit 2. The net gain and net loss were deferred and are being amortized over the terms of leases. See Note 7. These amortizations and the lease expense amounts are reported in the Income Statement as Generation Facilities Rental Expense, Net.

### (g) Interest Charges

Debt Interest reported in the Income Statement does not include interest on obligations for nuclear fuel under construction. That interest is capitalized. See Note 6.

Losses and gains realized upon the reacquisition or redemption of long-term debt are deferred, consistent with the regulatory rate treatment. See Note 7. Such losses and gains are either amortized over the remainder of the original life of the debt issue retired or amortized over the life of the new debt issue when the proceeds of a new issue are used for the debt redemption. The amortizations are included in debt interest expense.

### (h) Federal Income Taxes

We use the liability method of accounting for income taxes in accordance with SFAS 109. See Note 8. This method requires that deferred taxes be recorded for all temporary differences between the book and tax bases of assets and liabilities. The majority of these temporary differences are attributable to property-related basis differences. Included in these basis differences is the equity component of AFUDC, which will increase future tax expense when it is recovered through rates. Since this

component is not recognized for tax purposes, we must record a liability for our tax obligation. The PUCO permits recovery of such taxes from customers when they become payable. Therefore, the net amount due from customers through rates has been recorded as a deferred charge and will be recovered over the lives of the related assets. See Note 7.

Investment tax credits are deferred and amortized over the lives of the applicable property as a reduction of depreciation expense. See Note 7 for a discussion of the amortization of certain unrestricted excess deferred taxes and unrestricted investment tax credits under the Rate Stabilization Program.

## *(2) Utility Plant Sale and Leaseback Transactions*

The Operating Companies are co-lessees of 18.26% (150 megawatts) of Beaver Valley Unit 2 and 6.5% (51 megawatts), 45.9% (358 megawatts) and 44.38% (355 megawatts) of Units 1, 2 and 3 of the Mansfield Plant, respectively, all for terms of about 29½ years. These leases are the result of sale and leaseback transactions completed in 1987.

Under these leases, the Operating Companies are responsible for paying all taxes, insurance premiums, operation and maintenance expenses and all other similar costs for their interests in the units sold and leased back. They may incur additional costs in connection with capital improvements to the units. The Operating Companies have options to buy the interests back at the end of the leases for the fair market value at that time or renew the leases. Additional lease provisions provide other purchase options along with conditions for mandatory termination of the leases (and possible repurchase of the leasehold interests) for events of default. These events include noncompliance with several financial covenants discussed in Note 11(d).

In April 1992, nearly all of the outstanding Secured Lease Obligation Bonds (SLOBs) issued by a special purpose corporation in connection with financing the sale and leaseback of Beaver Valley Unit 2 were refinanced through a tender offer and the sale of new bonds having a lower interest rate. As part of the refinancing transaction, Toledo Edison paid $43 million as supplemental rent to fund transaction expenses and part of the tender premium. This amount has been deferred and is being amortized over the remaining lease term. The refinancing transaction reduced the annual rental expense for the Beaver Valley Unit 2 lease by $9 million.

Future minimum lease payments under the operating leases at December 31, 1994 are summarized as follows:

| Year | Amount (millions of dollars) |
|---|---|
| 1995 | $ 166 |
| 1996 | 188 |
| 1997 | 165 |
| 1998 | 165 |
| 1999 | 178 |
| Later Years | 3,239 |
| Total Future Minimum Lease Payments | $4,101 |

Rental expense is accrued on a straight-line basis over the terms of the leases. The amount recorded in 1994, 1993 and 1992 as annual rental expense for the Mansfield Plant leases was $115 million. The amounts recorded in 1994, 1993 and 1992 as annual rental expense for the Beaver Valley Unit 2 lease were $64 million, $63 million and $66 million, respectively. Amounts charged to expense in excess of the lease payments are classified as Accumulated Deferred Rents in the Balance Sheet.

Toledo Edison is selling 150 megawatts of its Beaver Valley Unit 2 leased capacity entitlement to Cleveland Electric. We anticipate that this sale will continue indefinitely.

## *(3) Property Owned with Other Utilities and Investors*

The Operating Companies own, as tenants in common with other utilities and those investors who are owner-participants in various sale and leaseback transactions (Lessors), certain generating units as listed below. Each owner owns an undivided share in the entire unit. Each owner has the right to a percentage of the generating capability of each unit equal to its ownership share. Each utility owner is obligated to pay for only its respective share of the construction costs and operating expenses. Each Lessor has leased its capacity rights to a utility which is obligated to pay for such Lessor's share of the construction costs and operating expenses. The Operating Companies' share of the operating expenses of these generating units is included in the Income Statement. The Balance Sheet classification of Property, Plant and Equipment at December 31, 1994 includes the following facilities owned by the Operating Companies as tenants in common with other utilities and Lessors:

| Generating Unit | In-Service Date | Ownership Share | Ownership Megawatts | Power Source | Plant in Service | Construction Work in Progress | Accumulated Depreciation |
|---|---|---|---|---|---|---|---|
| | | | | | | (millions of dollars) | |
| Seneca Pumped Storage | 1970 | 80.00% | 351 | Hydro | $ 66 | $— | $ 22 |
| Eastlake Unit 5 | 1972 | 68.80 | 411 | Coal | 156 | 1 | — |
| Perry Unit 1 | 1987 | 51.02 | 609 | Nuclear | 2,817 | 9 | 511 |
| Beaver Valley Unit 2 and Common Facilities (Note 2) | 1987 | 26.12 | 214 | Nuclear | 1,480 | 4 | 292 |
| Total | | | | | $4,519 | $14 | $825 |

Depreciation for Eastlake Unit 5 has been accumulated with all other nonnuclear depreciable property rather than by specific units of depreciable property.

## *(4) Construction and Contingencies*

### (a) Construction Program

The estimated cost of our construction program for the 1995-1999 period is $1.154 billion, including AFUDC of $64 million and excluding nuclear fuel.

The Clean Air Act requires, among other things, significant reductions in the emission of sulfur dioxide and nitrogen oxides by fossil-fueled generating units. Our strategy provides for compliance primarily through greater use of low-sulfur coal at some of our units and the use of emission allowances. Total capital expenditures from 1991 through 1994 in connection with Clean Air Act compliance amounted to $35 million. The plan will require additional capital expenditures over the 1995-2004 period of approximately $157 million for nitrogen oxide control equipment and plant modifications. In addition, higher fuel and other operation and maintenance expenses will be incurred. The anticipated rate increase associated with the capital expenditures and higher expenses would be about 1-2% in the late 1990s. Cleveland Electric may need to install sulfur emission control technology at one of its generating plants after 2005 which could require additional expenditures at that time.

### (b) Perry Unit 2

Perry Unit 2, including its share of the facilities common with Perry Unit 1, was approximately 50% complete when construction was suspended in 1985 pending consideration of various options. We wrote off our investment in Perry Unit 2 at December 31, 1993 after we determined that it would not be completed or sold. The write-off totaled $583 million ($425 million after taxes) for our 64.76% ownership share of the unit. See Note 14.

### (c) Hazardous Waste Disposal Sites

The Operating Companies are aware of their potential involvement in the cleanup of three sites listed on the Superfund List and several other waste sites not on such list. The Operating Companies have accrued a liability totaling $13 million at December 31, 1994 based on estimates of the costs of cleanup and their proportionate responsibility for such costs. We believe that the ultimate outcome of these matters will not have a material adverse effect on our financial condition or results of operations. See Management's Financial Analysis — Outlook-Hazardous Waste Disposal Sites.

## *(5) Nuclear Operations and Contingencies*

### (a) Operating Nuclear Units

Our three nuclear units may be impacted by activities or events beyond our control. An extended outage of one of our nuclear units for any reason, coupled with any unfavorable rate treatment, could have a material adverse effect on our financial condition and results of operations. See discussion of these risks in Management's Financial Analysis — Outlook-Nuclear Operations.

**(b) Nuclear Insurance**

The Price-Anderson Act limits the public liability of the owners of a nuclear power plant to the amount provided by private insurance and an industry assessment plan. In the event of a nuclear incident at any unit in the United States resulting in losses in excess of the level of private insurance (currently $200 million), our maximum potential assessment under that plan would be $155 million (plus any inflation adjustment) per incident. The assessment is limited to $20 million per year for each nuclear incident. These assessment limits assume the other CAPCO companies contribute their proportionate share of any assessment.

The utility owners and lessees of Davis-Besse, Perry and Beaver Valley also have insurance coverage for damage to property at these sites (including leased fuel and cleanup costs). Coverage amounted to $2.75 billion for each site as of January 1, 1995. Damage to property could exceed the insurance coverage by a substantial amount. If it does, our share of such excess amount could have a material adverse effect on our financial condition and results of operations. Under these policies, we can be assessed a maximum of $22 million during a policy year if the reserves available to the insurer are inadequate to pay claims arising out of an accident at any nuclear facility covered by the insurer.

We also have extra expense insurance coverage. It includes the incremental cost of any replacement power purchased (over the costs which would have been incurred had the units been operating) and other incidental expenses after the occurrence of certain types of accidents at our nuclear units. The amounts of the coverage are 100% of the estimated extra expense per week during the 52-week period starting 21 weeks after an accident and 80% of such estimate per week for the next 104 weeks. The amount and duration of extra expense could substantially exceed the insurance coverage.

## *(6) Nuclear Fuel*

Nuclear fuel is financed for the Operating Companies through leases with a special-purpose corporation. At December 31, 1994, $307 million of nuclear fuel was financed ($157 million from intermediate-term notes and $150 million from bank credit arrangements). The intermediate-term notes mature in 1996 and 1997. The Operating Companies severally lease their respective portions of the nuclear fuel and are obligated to pay for the fuel as it is consumed in a reactor. The lease rates are based on various intermediate-term note rates, bank rates and commercial paper rates.

The amounts financed include nuclear fuel in the Davis-Besse, Perry Unit 1 and Beaver Valley Unit 2 reactors with remaining lease payments of $128 million, $91 million and $24 million, respectively, at December 31, 1994. The nuclear fuel amounts financed and capitalized also included interest charges incurred by the lessors amounting to $11 million in 1994, $14 million in 1993 and $15 million in 1992. The estimated future lease amortization payments based on projected consumption are $99 million in 1995, $91 million in 1996, $80 million in 1997, $73 million in 1998 and $62 million in 1999.

## *(7) Regulatory Matters*

The Operating Companies are subject to the provisions of SFAS 71. Regulatory assets represent probable future revenues to the Operating Companies associated with certain incurred costs, which they will recover from customers through the ratemaking process. Regulatory assets in the Balance Sheet are as follows:

| | December 31, 1994 | December 31, 1993 |
|---|---|---|
| | (millions of dollars) | |
| Amounts due from customers for future federal income taxes | $1,046 | $ 968 |
| Unamortized loss from Beaver Valley Unit 2 sale | 101 | 105 |
| Unamortized loss on reacquired debt | 86 | 92 |
| Pre-phase-in deferrals* | 570 | 587 |
| Rate Stabilization Program deferrals | 387 | 275 |
| Total | $2,190 | $2,027 |

* Represent deferrals of operating expenses and carrying charges for Perry Unit 1 and Beaver Valley Unit 2 in 1987 and 1988 which are being amortized over the lives of the related property.

As of December 31, 1994, customer rates provide for recovery of all the above regulatory assets, except those related to the Rate Stabilization Program discussed below. The remaining recovery periods for all of the regulatory assets listed above range from 17 to 34 years. The Operating Companies continually assess the effects of competition and the changing industry and regulatory environment on operations and their ability to recover the regulatory assets. In the event that the Operating Companies determine that future revenues would not be provided for recovery of any regulatory asset, such asset would be required to be written off. See Management's Financial Analysis — Outlook-Regulatory Accounting.

The Operating Companies will file a request with the PUCO to restructure rates to increase revenues to be effective in 1996 which will include provision for recovery of the Rate Stabilization Program deferrals. We believe that rates will be set at a level consistent with cost-based regulations and will provide revenues to recover the then-current operating costs, return requirements and amortization of all regulatory assets listed above.

The Rate Stabilization Program that the PUCO approved in October 1992 was designed to encourage economic

growth in our service area by freezing base rates until 1996 and limiting subsequent rate increases to specified annual amounts not to exceed $216 million for Cleveland Electric and $89 million for Toledo Edison over the 1996-1998 period.

As part of the Rate Stabilization Program, during the 1992-1995 period the Operating Companies are allowed to defer and subsequently recover certain costs not currently recovered in rates and to accelerate amortization of certain benefits. The continued use of these regulatory accounting measures will be dependent upon our continuing assessment and conclusion that there will be probable recovery of such deferrals in future rates.

The regulatory accounting measures we are eligible to record through December 31, 1995 include the deferral of post-in-service interest carrying charges, depreciation expense and property taxes on assets placed in service after February 29, 1988 and the deferral of Toledo Edison operating expenses equivalent to an accumulated excess rent reserve for Beaver Valley Unit 2 (which resulted from the April 1992 refinancing of SLOBs as discussed in Note 2). The cost deferrals recorded in 1994, 1993 and 1992 pursuant to these provisions were $106 million, $95 million and $84 million, respectively. The regulatory accounting measures also provide for the accelerated amortization of certain unrestricted excess deferred tax and unrestricted investment tax credit balances and interim spent fuel storage accrual balances for Davis-Besse. The total amount of such regulatory benefits recognized pursuant to these provisions was $46 million in both 1994 and 1993 and $12 million in 1992.

The Rate Stabilization Program also authorized the Operating Companies to defer and subsequently recover the incremental expenses associated with the adoption of the accounting standard for postretirement benefits other than pensions (SFAS 106). In 1994 and 1993, we deferred $6 million and $96 million, respectively, pursuant to this provision. Amortization and recovery of these deferrals are expected to commence in 1996 and to be completed by no later than 2012. See Note 9(b).

In 1993, upon completing a comprehensive study which led to our current strategic plan, we concluded that projected revenues would not provide for recovery of deferrals recorded pursuant to phase-in plans approved by the PUCO in 1989. Such deferrals were scheduled to be recovered over the 1994 through 1998 period. The total phase-in deferred operating expenses and carrying charges written off at December 31, 1993 were $172 million and $705 million, respectively (totaling $598 million after taxes). See Note 14. Additionally, based on our assessment of business conditions, we concluded that, once the deferral of expenses and acceleration of benefits under our Rate Stabilization Program are completed in 1995, we should no longer plan to use regulatory accounting measures to the extent we have in the past.

## *(8) Federal Income Tax*

The components of federal income tax expense (credit) recorded in the Income Statement were as follows:

| | 1994 | 1993 | 1992 |
|---|---|---|---|
| | (millions of dollars) | | |
| Operating Expenses: | | | |
| Current | $ 70 | $ 99 | $ 71 |
| Deferred | 44 | (88) | 51 |
| Total Charged to Operating Expenses | 114 | 11 | 122 |
| Nonoperating Income: | | | |
| Current | (45) | (34) | (38) |
| Deferred | 51 | (364) | 45 |
| Total Expense (Credit) to Nonoperating Income | 6 | (398) | 7 |
| Total Federal Income Tax Expense (Credit) | $120 | $(387) | $129 |

The deferred federal income tax expense results from the temporary differences that arise from the different years certain expenses are recognized for tax purposes as opposed to financial reporting purposes. Such temporary differences affecting operating expenses relate principally to depreciation and deferred operating expenses whereas those affecting nonoperating income principally relate to deferred carrying charges and the 1993 write-offs.

Federal income tax, computed by multiplying the income before taxes and preferred dividend requirements of subsidiaries by the statutory rate (35% in 1994 and 1993 and 34% in 1992), is reconciled to the amount of federal income tax recorded on the books as follows:

| | 1994 | 1993 | 1992 |
|---|---|---|---|
| | (millions of dollars) | | |
| Book Income (Loss) Before Federal Income Tax | $390 | $(1,263) | $406 |
| Tax (Credit) on Book Income (Loss) at Statutory Rate | $137 | $ (442) | $138 |
| Increase (Decrease) in Tax: | | | |
| Write-off of Perry Unit 2 | — | 46 | — |
| Write-off of phase-in deferrals | — | 28 | — |
| Depreciation | 3 | (6) | (9) |
| Rate Stabilization Program | (27) | (30) | (7) |
| Other items | 7 | 17 | 7 |
| Total Federal Income Tax Expense (Credit) | $120 | $ (387) | $129 |

For tax reporting purposes, the Perry Unit 2 abandonment was recognized in 1994 and resulted in a $307 million loss with a corresponding $107 million reduction in federal income tax liability. Because of the alternative minimum tax (AMT), $62 million of the $107 million was realized in 1994. The remaining $45 million will not be realized until 1999. Additionally, a repayment of approximately $32 million of previously allowed investment tax credits was recognized in 1994.

In August 1993, the Revenue Reconciliation Act of 1993 was enacted. Retroactive to January 1, 1993, the top marginal corporate income tax rate increased to 35%. The change in tax rate did not materially impact the results of operations for 1993, but increased Accumulated Deferred Federal Income Taxes for the future tax obligation by approximately $90 million. Since the PUCO has historically permitted recovery of such taxes from customers when they become payable, the deferred charge, Amounts Due from Customers for Future Federal Income Taxes, also was increased by $90 million.

Under SFAS 109, temporary differences and carryforwards resulted in deferred tax assets of $596 million and deferred tax liabilities of $2.374 billion at December 31, 1994 and deferred tax assets of $619 million and deferred tax liabilities of $2.198 billion at December 31, 1993. These are summarized as follows:

| | December 31, 1994 | December 31, 1993 |
|---|---|---|
| | (millions of dollars) | |
| Property, plant and equipment | $2,035 | $1,845 |
| Deferred carrying charges and operating expenses | 215 | 206 |
| Net operating loss carryforwards | (144) | (108) |
| Investment tax credits | (156) | (183) |
| Sale and leaseback transactions | (128) | (127) |
| Other | (44) | (54) |
| Net deferred tax liability | $1,778 | $1,579 |

For tax purposes, net operating loss (NOL) carryforwards of approximately $412 million are available to reduce future taxable income and will expire in 2003 through 2009. The 35% tax effect of the NOLs is $144 million. Additionally, AMT credits of $168 million that may be carried forward indefinitely are available to reduce future regular tax.

## *(9) Retirement Benefits*

### (a) Retirement Income Plan

We sponsor a noncontributing pension plan which covers all employee groups. The amount of retirement benefits generally depends upon the length of service. Under certain circumstances, benefits can begin as early as age 55. Our funding policy is to comply with the Employee Retirement Income Security Act of 1974 guidelines.

In 1993, we offered the VTP, an early retirement program. Operating expenses for 1993 included $205 million of pension plan accruals to cover enhanced VTP benefits and an additional $10 million of pension costs for VTP benefits paid to retirees from corporate funds. The $10 million is not included in the pension data reported in the following table. A credit of $81 million resulting from a settlement of pension obligations through lump sum payments to almost all the VTP retirees partially offset the VTP expenses.

Pension and VTP costs (credits) for 1992 through 1994 were comprised of the following components:

| | 1994 | 1993 | 1992 |
|---|---|---|---|
| | (millions of dollars) | | |
| Pension Costs (Credits): | | | |
| Service cost for benefits earned during the period | $ 13 | $ 15 | $ 15 |
| Interest cost on projected benefit obligation | 26 | 37 | 38 |
| Actual return on plan assets | (2) | (65) | (24) |
| Net amortization and deferral | (34) | 4 | (45) |
| Net pension costs (credits) | 3 | (9) | (16) |
| VTP cost | — | 205 | — |
| Settlement gain | — | (81) | — |
| Net costs (credits) | $ 3 | $115 | $(16) |

The following table presents a reconciliation of the funded status of the plan.

| | December 31, 1994 | December 31, 1993 |
|---|---|---|
| | (millions of dollars) | |
| Actuarial present value of benefit obligations: | | |
| Vested benefits | $278 | $333 |
| Nonvested benefits | 2 | 37 |
| Accumulated benefit obligation | 280 | 370 |
| Effect of future compensation levels | 37 | 53 |
| Total projected benefit obligation | 317 | 423 |
| Plan assets at fair market value | 362 | 386 |
| Funded status | 45 | (37) |
| Unrecognized net loss (gain) from variance between assumptions and experience | (79) | 11 |
| Unrecognized prior service cost | 10 | 10 |
| Transition asset at January 1, 1987 being amortized over 19 years | (39) | (43) |
| Net accrued pension liability included in Retirement Benefits in the Balance Sheet | $(63) | $(59) |

A September 30, 1994 measurement date was used for 1994 reporting. At December 31, 1994, the settlement (discount) rate and long-term rate of return on plan assets assumptions were 8.5% and 10%, respectively. The long-term rate of annual compensation increase assumption was 3.5% for 1995 and 1996 and 4% thereafter. At December 31, 1993, the settlement rate and long-term rate of return on plan assets assumptions were 7.25% and 8.75%, respectively. The long-term rate of annual compensation increase assumption was 4.25%.

Plan assets consist primarily of investments in common stock, bonds, guaranteed investment contracts, cash equivalent securities and real estate.

### (b) Other Postretirement Benefits

We sponsor a postretirement benefit plan which provides all employee groups certain health care, death and other postretirement benefits other than pensions. The plan is contributory, with retiree contributions adjusted annually. The plan is not funded. We adopted SFAS 106, the accounting standard for postretirement benefits other than pensions, effective January 1, 1993. The standard requires the accrual of the expected costs of such benefits

during the employees' years of service. Prior to 1993, the costs of these benefits were expensed as paid, which was consistent with ratemaking practices.

The components of the total postretirement benefit costs for 1994 and 1993 were as follows:

| | 1994 | 1993 |
|---|---|---|
| | (millions of dollars) | |
| Service cost for benefits earned during the period | $ 2 | $ 3 |
| Interest cost on accumulated postretirement benefit obligation | 18 | 16 |
| Amortization of transition obligation at January 1, 1993 of $167 million over 20 years | 8 | 8 |
| VTP curtailment cost (includes $16 million transition obligation adjustment) | — | 84 |
| Total costs | $28 | $111 |

In 1994 and 1993, we deferred incremental SFAS 106 expenses (in excess of the amounts paid) of $6 million and $96 million, respectively, pursuant to a provision of the Rate Stabilization Program. See Note 7.

The accumulated postretirement benefit obligation and accrued postretirement benefit cost are as follows:

| | December 31, | |
|---|---|---|
| | 1994 | 1993 |
| | (millions of dollars) | |
| Accumulated postretirement benefit obligation attributable to: | | |
| Retired participants | $(203) | $(229) |
| Fully eligible active plan participants | (1) | (1) |
| Other active plan participants | (21) | (28) |
| Accumulated postretirement benefit obligation | (225) | (258) |
| Unrecognized net loss (gain) from variance between assumptions and experience | (23) | 14 |
| Unamortized transition obligation | 135 | 143 |
| Accrued postretirement benefit cost included in Retirement Benefits in the Balance Sheet | $(113) | $(101) |

A September 30, 1994 measurement date was used for 1994 reporting. At December 31, 1994 and 1993, the settlement rate and the long-term rate of annual compensation increase assumptions were the same as those discussed for pension reporting in Note 9(a). At December 31, 1994, the assumed annual health care cost trend rates (applicable to gross eligible charges) are 8.5% for medical and 8% for dental in 1995. Both rates reduce gradually to a fixed rate of 4.75% by 2003. Elements of the obligation affected by contribution caps are significantly less sensitive to the health care cost trend rate than other elements. If the assumed health care cost trend rates were increased by one percentage point in each future year, the accumulated postretirement benefit obligation as of December 31, 1994 would increase by $7 million and the aggregate of the service and interest cost components of the annual postretirement benefit cost would increase by $0.5 million.

## (10) Guarantees

Cleveland Electric has guaranteed certain loan and lease obligations of two coal suppliers under two long-term coal supply contracts. Toledo Edison is a party to one of these contracts. At December 31, 1994, the principal amount of the loan and lease obligations guaranteed by the Operating Companies under both contracts was $67 million. In addition, under the contract to which Toledo Edison is not a party, Cleveland Electric may be responsible for mine closing costs when the contract is terminated. At December 31, 1994, the unfunded costs of closing this mine as estimated by the supplier were $54 million.

The prices under both contracts which include certain minimum payments are sufficient to satisfy the loan and lease obligations and mine closing costs over the lives of the contracts. If either contract is terminated early for any reason, the Operating Companies would attempt to reduce the termination charges and would ask the PUCO to allow recovery of such charges from customers through the fuel factor of the respective Operating Company.

## (11) Capitalization

### (a) Capital Stock Transactions and Common Shares Reserved for Issue

Shares sold, retired and purchased for treasury during the three years ended December 31, 1994 are listed in the following table.

| | 1994 | 1993 | 1992 |
|---|---|---|---|
| | (thousands of shares) | | |
| Centerior Energy Common Stock: | | | |
| Dividend Reinvestment and Stock Purchase Plan | 683 | 3,542 | 2,570 |
| Employee Savings Plan | 259 | 544 | 322 |
| Employee Purchase Plan | 46 | 52 | — |
| Total Common Stock Sales | 988 | 4,138 | 2,892 |
| Treasury Shares | — | 26 | (172) |
| Net Increase | 988 | 4,164 | 2,720 |
| Preferred Stock of Subsidiaries Subject to Mandatory Redemption: | | | |
| Cleveland Electric Sales | | | |
| $90.00 Series S | — | — | 75 |
| Cleveland Electric Retirements | | | |
| $ 7.35 Series C | (10) | (10) | (10) |
| 88.00 Series E | (3) | (3) | (3) |
| Adjustable Series M | (100) | (100) | (100) |
| 9.125 Series N | (189) | (150) | — |
| Toledo Edison Retirements | | | |
| $100 par $11.00 | — | — | (25) |
| 9.375 | (17) | (17) | (17) |
| 25 par 2.81 | (800) | (800) | — |
| Preferred Stock of Subsidiaries Not Subject to Mandatory Redemption: | | | |
| Cleveland Electric Sales | | | |
| $42.40 Series T | — | 200 | — |
| Cleveland Electric Retirements | | | |
| Remarketed Series P | — | — | (1) |
| Net (Decrease) | (1,119) | (880) | (81) |

Shares of common stock required for our stock plans in 1994 were either acquired in the open market or issued as new shares.

The Board of Directors has authorized the purchase in the open market of up to 1,500,000 shares of our common stock until June 30, 1996. As of December 31, 1994, 225,500 shares had been purchased at a total cost of $4 million. Such shares are being held as treasury stock.

The number of common stock shares reserved for issue under the Employee Savings Plan and the Employee Purchase Plan was 1,702,849 and 423,797, respectively, at December 31, 1994.

Under an Equity Compensation Plan (Plan) adopted in 1994, options to purchase shares of common stock and restricted common stock awards were granted to management employees. Options were issued for 264,900 shares at an exercise price of $13.20. The options expire 10 years from the date of the grant and vest over four years. The number of shares available for issuance under the Plan each year is determined by formula, generally 0.5% of outstanding shares. The options and stock grants for 1994 are conditioned upon the approval of the Plan by Centerior Energy common stock share owners at their April 1995 annual meeting. Shares of common stock required for the Plan may be either issued as new shares, issued from treasury stock or acquired in the open market specifically for distribution under the Plan.

### (b) Equity Distribution Restrictions

The Operating Companies make cash available for the funding of Centerior Energy's common stock dividends by paying dividends on their respective common stock, which are held solely by Centerior Energy. Federal law prohibits the Operating Companies from paying dividends out of capital accounts. However, the Operating Companies may pay preferred and common stock dividends out of appropriated retained earnings and current earnings. At December 31, 1994, Cleveland Electric and Toledo Edison had $144 million and $104 million, respectively, of appropriated retained earnings for the payment of dividends. However, Toledo Edison is prohibited from paying a common stock dividend by a provision in its mortgage that essentially requires such dividends to be paid out of the total balance of retained earnings, which currently is a deficit.

### (c) Preferred and Preference Stock

Amounts to be paid for preferred stock which must be redeemed during the next five years are $47 million in 1995, $31 million in both 1996 and 1997, $16 million in 1998 and $35 million in 1999.

The annual mandatory redemption provisions are as follows:

| | Shares To Be Redeemed | Beginning in | Price Per Share |
|---|---|---|---|
| Cleveland Electric Preferred: | | | |
| $ 7.35 Series C | 10,000 | 1984 | $ 100 |
| 88.00 Series E | 3,000 | 1981 | 1,000 |
| Adjustable Series M | 100,000 | 1991 | 100 |
| 9.125 Series N | 150,000 | 1993 | 100 |
| 91.50 Series Q | 10,714 | 1995 | 1,000 |
| 88.00 Series R | 50,000 | 2001* | 1,000 |
| 90.00 Series S | 18,750 | 1999 | 1,000 |
| Toledo Edison Preferred: | | | |
| $100 par $9.375 | 16,650 | 1985 | 100 |
| 25 par 2.81 | 400,000 | 1993 | 25 |

* All outstanding shares to be redeemed on December 1, 2001.

In 1993, Cleveland Electric issued $100 million principal amount of Serial Preferred Stock, $42.40 Series T. The Series T stock was deposited with an agent which issued Depositary Receipts, each representing 1/20 of a share of the Series T stock.

The annualized preferred dividend requirement for the Operating Companies at December 31, 1994 was $63 million.

The preferred dividend rates on Cleveland Electric's Series L and M and Toledo Edison's Series A and B fluctuate based on prevailing interest rates and market conditions. The dividend rates for these issues averaged 7.17%, 7.01%, 7.66% and 8.44%, respectively, in 1994.

Preference stock authorized for the Operating Companies are 3,000,000 shares without par value for Cleveland Electric and 5,000,000 shares with a $25 par value for Toledo Edison. No preference shares are currently outstanding for either company.

With respect to dividend and liquidation rights, each Operating Company's preferred stock is prior to its preference stock and common stock, and each Operating Company's preference stock is prior to its common stock.

### (d) Long-Term Debt and Other Borrowing Arrangements

Long-term debt, less current maturities, for the Operating Companies was as follows:

| Year of Maturity | Actual or Average Interest Rate at December 31, 1994 | December 31, 1994 | December 31, 1993 |
|---|---|---|---|
| | | (millions of dollars) | |
| First mortgage bonds: | | | |
| 1996-1999 | 13.75 % | $ 17 | $ 21 |
| 1996-1999 | 7.00 | 3 | 4 |
| 1997-1999 | 10.88 | 18 | 18 |
| 1997 | 6.125 | 31 | 31 |
| 1998 | 10.00 | 1 | 1 |
| 1999 | 6.20 | 2 | 2 |
| 1999 | 7.25 | 100 | 100 |
| 2000-2004 | 7.89 | 603 | 607 |
| 2005-2009 | 8.33 | 202 | 202 |
| 2010-2014 | 8.13 | 396 | 396 |
| 2015-2019 | 8.00 | 526 | 526 |
| 2020-2023 | 8.53 | 666 | 666 |
| | | 2,565 | 2,574 |
| Secured medium term notes due 1996-2021 | 8.60 | 766 | 963 |
| Term bank loans due 1996 | 9.07 | 63 | 154 |
| Notes due 1996-1997 | 9.49 | 25 | 43 |
| Debentures due 2002 | 8.70 | 135 | 135 |
| Pollution control notes due 1996-2015 | 10.30 | 151 | 158 |
| Other — net | — | (8) | (8) |
| Total Long-Term Debt | | $3,697 | $4,019 |

Long-term debt matures during the next five years as follows: $326 million in 1995, $243 million in 1996, $95 million in 1997, $117 million in 1998 and $277 million in 1999.

The Operating Companies issued $266 million aggregate principal amount of secured medium-term notes in 1992 and 1993. The notes are secured by first mortgage bonds.

The mortgages of the Operating Companies constitute direct first liens on substantially all property owned and franchises held by them. Excluded from the liens, among other things, are cash, securities, accounts receivable, fuel, supplies and, in the case of Toledo Edison, automotive equipment.

Certain unsecured loan agreements of the Operating Companies contain covenants relating to capitalization ratios, fixed charge coverage ratios and limitations on secured financing other than through first mortgage bonds or certain other transactions. Two reimbursement agreements relating to separate letters of credit issued in connection with the sale and leaseback of Beaver Valley Unit 2 contain several financial covenants affecting Centerior Energy and the Operating Companies. Among these are covenants relating to fixed charge coverage ratios and capitalization ratios. The write-offs recorded at December 31, 1993 caused Centerior Energy and the Operating Companies to violate certain covenants contained in a Cleveland Electric loan agreement and the two reimbursement agreements. The affected creditors waived those violations in exchange for a subordinate mortgage security interest on the Operating Companies' properties. We provided the same security interest to certain other creditors because their agreements require equal treatment. At December 31, 1994, the Operating Companies provided subordinate mortgage collateral for $197 million of unsecured debt, $228 million of bank letters of credit and a $205 million revolving credit facility.

## *(12) Short-Term Borrowing Arrangements*

Centerior Energy has a $205 million revolving credit facility through May 1996. Centerior Energy and the Service Company may borrow under the facility, with all borrowings jointly and severally guaranteed by the Operating Companies. Centerior Energy plans to transfer any of its borrowed funds to the Operating Companies. The facility agreement as amended provides the participating banks with a subordinate mortgage security interest on the Operating Companies' properties. The banks' fee is 0.625% per annum payable quarterly in addition to interest on any borrowings. There were no borrowings under the facility at December 31, 1994. The facility agreement contains covenants relating to capitalization and fixed charge coverage ratios.

Short-term borrowing capacity authorized by the PUCO annually is $300 million for Cleveland Electric and $150 million for Toledo Edison. The Operating Companies are authorized by the PUCO to borrow from each other on a short-term basis.

## (13) Financial Instruments

Except for the Nuclear Plant Decommissioning Trusts at December 31 1994, as discussed below, the estimated fair values at December 31, 1994 and 1993 of financial instruments that do not approximate their carrying amounts in the Balance Sheet are as follows:

| | December 31, | | | |
|---|---|---|---|---|
| | 1994 | | 1993 | |
| | Carrying Amount | Fair Value | Carrying Amount | Fair Value |
| | (millions of dollars) | | | |
| Assets: | | | | |
| Nuclear Plant Decommissioning Trusts | $ 82 | $ 82 | $ 56 | $ 59 |
| Capitalization and Liabilities: | | | | |
| Preferred Stock, with Mandatory Redemption Provisions (including current portion) | 300 | 264 | 354 | 349 |
| Long-Term Debt (including current portion) | 4,031 | 3,628 | 4,113 | 4,260 |

The Nuclear Plant Decommissioning Trusts at December 31, 1994 included $46 million of federal governmental securities and $31 million of municipal securities. The securities had the following maturities: $19 million due within one year; $16 million due in one to five years; $17 million due in six to 10 years; and $25 million due after 10 years. The fair value of these trusts is estimated based on the quoted market prices for the investment securities. As a result of adopting the new accounting standard for certain investments in debt and equity securities, SFAS 115, in 1994, the carrying amount of these trusts is equal to the fair value. The fair value of the Operating Companies' preferred stock, with mandatory redemption provisions, and long-term debt is estimated based on the quoted market prices for the respective or similar issues or on the basis of the discounted value of future cash flows. The discounted value used current dividend or interest rates (or other appropriate rates) for similar issues and loans with the same remaining maturities.

The estimated fair values of all other financial instruments approximate their carrying amounts in the Balance Sheet at December 31, 1994 and 1993 because of their short-term nature.

## (14) Quarterly Results of Operations (Unaudited)

The following is a tabulation of the unaudited quarterly results of operations for the two years ended December 31, 1994.

| | Quarters Ended | | | |
|---|---|---|---|---|
| | March 31, | June 30, | Sept. 30, | Dec. 31, |
| | (millions of dollars, except per share amounts) | | | |
| 1994 | | | | |
| Operating Revenues | $588 | $596 | $667 | $ 570 |
| Operating Income | $129 | $134 | $186 | $ 129 |
| Net Income | $ 35 | $ 42 | $ 92 | $ 35 |
| Average Common Shares (millions) | 147.4 | 147.9 | 148.0 | 148.0 |
| Earnings Per Common Share | $ .24 | $ .28 | $ .62 | $ .24 |
| Dividends Paid Per Common Share | $ .20 | $ .20 | $ .20 | $ .20 |
| 1993 | | | | |
| Operating Revenues | $598 | $589 | $709 | $ 578 |
| Operating Income (Loss) | $122 | $126 | $106 | $ (42) |
| Net Income (Loss) | $ 35 | $ 34 | $ 17 | $(1,029) |
| Average Common Shares (millions) | 143.4 | 144.4 | 145.3 | 146.4 |
| Earnings (Loss) Per Common Share | $ .25 | $ .23 | $ .12 | $ (7.02) |
| Dividends Paid Per Common Share | $ .40 | $ .40 | $ .40 | $ .40 |

Earnings for the quarter ended September 30, 1993 were decreased by $81 million, or $.56 per share, as a result of the recording of $125 million of VTP pension-related benefits.

Earnings for the quarter ended December 31, 1993 were decreased as a result of year-end adjustments for the $583 million write-off of Perry Unit 2 (see Note 4(b)), the $877 million write-off of the phase-in deferrals (see Note 7) and $58 million of other charges. These adjustments decreased quarterly earnings by $1.06 billion, or $7.24 per share.

# Executives Of Centerior Energy Corporation

| | |
|---|---|
| Chairman, President and Chief Executive Officer | *Robert J. Farling (58)* |
| Executive Vice President | *Murray R. Edelman (55)* |
| Senior Vice President | *Fred J. Lange, Jr. (45)* |
| Vice President | *Gary R. Leidich (44)* |
| Vice President | *Terrence G. Linnert (48)* |
| Controller | *E. Lyle Pepin (53)* |
| Treasurer | *David M. Blank (46)* |
| Secretary | *Janis T. Percio (42)* |

# Executives Of Centerior Service Company

| | |
|---|---|
| Chairman, President and Chief Executive Officer (and Chairman & CEO of Cleveland Electric and Toledo Edison) | *Robert J. Farling (58)* |
| Executive Vice President – Operations & Engineering (and Vice Chairman of Toledo Edison and President of Cleveland Electric) | *Murray R. Edelman (55)* |
| Senior Vice President – Fossil & Transmission and Distribution Operations (and President of Toledo Edison) | *Fred J. Lange, Jr. (45)* |
| Senior Vice President – Nuclear (and Vice President – Nuclear-Perry) | *Donald C. Shelton (61)* |
| Vice President – Customer Support | *Jacquita K. Hauserman (52)* |
| Vice President – Finance & Administration | *Gary R. Leidich (44)* |
| Vice President – Legal & Governmental Affairs and General Counsel | *Terrence G. Linnert (48)* |
| Vice President – Transmission & Distribution Operations | *David L. Monseau (54)* |
| Vice President – Nuclear-Davis-Besse | *John P. Stetz (49)* |
| Vice President – Sales & Marketing | *Al R. Temple (49)* |
| Controller | *E. Lyle Pepin (53)* |
| Treasurer | *David M. Blank (46)* |
| Secretary | *Janis T. Percio (42)* |

*Number in parentheses indicates age.*

# Financial and Statistical Review

**Operating Revenues** (millions of dollars)

| Year | Residential | Commercial | Industrial | Other | Total Retail | Wholesale | Total Electric | Steam Heating & Gas | Total Operating Revenues |
|---|---|---|---|---|---|---|---|---|---|
| *1994* | $758 | 722 | 758 | 137 | 2 375 | 46 | 2 421 | — | $2 421 |
| *1993* | 768 | 716 | 754 | 143 | 2 381 | 93 | 2 474 | — | 2 474 |
| *1992* | 732 | 706 | 766 | 143 | 2 347 | 91 | 2 438 | — | 2 438 |
| *1991* | 777 | 723 | 783 | 188 | 2 471 | 89 | 2 560 | — | 2 560 |
| *1990* | 719 | 669 | 779 | 190 | 2 357 | 70 | 2 427 | — | 2 427 |
| *1984* | 548 | 454 | 636 | 88 | 1 726 | 24 | 1 750 | 24 | 1 774 |

**Operating Expenses** (millions of dollars)

| Year | Fuel & Purchased Power | Other Operation & Maintenance | Generation Facilities Rental Expense, Net | Depreciation & Amortization | Taxes, Other Than FIT | Deferred Operating Expenses, Net | Federal Income Taxes | Total Operating Expenses |
|---|---|---|---|---|---|---|---|---|
| *1994* | $442 | 595 | 160 | 278 | 309 | (55) | 114 | $1 843 |
| *1993* | 474 | 924*(a)* | 159 | 258 | 312 | 23*(b)* | 11 | 2 161 |
| *1992* | 473 | 623 | 161 | 256 | 318 | (52) | 122 | 1 901 |
| *1991* | 500 | 633 | 168 | 243*(c)* | 305 | (6) | 138 | 1 981 |
| *1990* | 472 | 698 | 165 | 242 | 283 | (34) | 96 | 1 922 |
| *1984* | 463 | 404 | — | 145 | 179 | — | 198 | 1 389 |

**Income (Loss)** (millions of dollars)

| Year | Operating Income | AFUDC—Equity | Other Income & Deductions, Net | Deferred Carrying Charges, Net | Federal Income Taxes—Credit (Expense) | Income (Loss) Before Interest Charges | Debt Interest |
|---|---|---|---|---|---|---|---|
| *1994* | $578 | 5 | 8 | 40 | (6) | 625 | 361 |
| *1993* | 313 | 5 | (589)*(d)* | (649)*(b)* | 398 | (522) | 359 |
| *1992* | 537 | 2 | 9 | 100 | (7) | 641 | 365 |
| *1991* | 579 | 9 | 6 | 110 | (30) | 674 | 381 |
| *1990* | 505 | 8 | (1) | 205 | (13) | 704 | 384 |
| *1984* | 385 | 213 | 12 | — | 69 | 679 | 310 |

**Income (Loss)** (millions of dollars) **Common Stock** (dollars per share & %)

| Year | AFUDC—Debt | Preferred & Preference Stock Dividends | Net Income (Loss) | Average Shares Outstanding (millions) | Earnings (Loss) | Return on Average Common Stock Equity | Dividends Declared | Book Value |
|---|---|---|---|---|---|---|---|---|
| *1994* | $ (6) | 66 | $ 204 | 147.8 | $ 1.38 | 11.1 % | $ .80 | $12.71 |
| *1993* | (5) | 67 | (943) | 144.9 | (6.51) | (40.3) | 1.60 | 12.14 |
| *1992* | (1) | 65 | 212 | 141.7 | 1.50 | 7.4 | 1.60 | 20.22 |
| *1991* | (5) | 61 | 237 | 139.1 | 1.71 | 8.4 | 1.60 | 20.37 |
| *1990* | (6) | 62 | 264 | 138.9 | 1.90 | 9.4 | 1.60 | 20.30 |
| *1984* | (76) | 78 | 367 | 107.6*(e)* | 3.41*(e)* | 16.4 | 2.29*(e)* | 20.64*(e)* |

*NOTE: 1984 data is the result of combining and restating data for the Operating Companies.*

*(a) Includes early retirement program expenses and other charges of $272 million in 1993.*

*(b) Includes write-off of phase-in deferrals of $877 million in 1993, consisting of $172 million of deferred operating expenses and $705 million of deferred carrying charges.*

*(c) In 1991, the Operating Companies adopted a change in accounting for nuclear plant depreciation, changing from the units-of-production method to the straight-line method at a 2.5% rate.*

| Year | **Electric Sales** (millions of KWH) | | | | | | **Electric Customers** (year end) | | | | **Residential Usage** | | |
|---|---|---|---|---|---|---|---|---|---|---|---|---|---|
| | Residential | Commercial | Industrial | Wholesale | Other | Total | Residential | Commercial | Industrial & Other | Total | Average KWH Per Customer | Average Price Per KWH | Average Revenue Per Customer |
| *1994* | 6 980 | 7 481 | 12 069 | 1 842 | 1 074 | 29 446 | 925 344 | 97 530 | 11 360 | 1 034 234 | 7 556 | 10.86¢ | $820.89 |
| *1993* | 6 974 | 7 306 | 11 687 | 3 027 | 1 022 | 30 016 | 924 227 | 96 491 | 12 219 | 1 032 937 | 7 546 | 11.01 | 830.99 |
| *1992* | 6 666 | 7 086 | 11 551 | 2 814 | 1 011 | 29 128 | 925 099 | 96 813 | 12 741 | 1 034 653 | 7 227 | 10.98 | 793.68 |
| *1991* | 6 981 | 7 176 | 11 559 | 2 690 | 1 048 | 29 454 | 921 995 | 96 449 | 12 843 | 1 031 287 | 7 410 | 11.16 | 827.10 |
| *1990* | 6 666 | 6 848 | 12 168 | 2 487 | 959 | 29 128 | 918 965 | 94 522 | 12 906 | 1 026 393 | 7 079 | 10.82 | 765.93 |
| *1984* | 6 404 | 5 794 | 11 441 | 578 | 871 | 25 088 | 888 816 | 85 825 | 11 850 | 986 491 | 7 035 | 8.56 | 603.92 |

| Year | **Load** (MW & %) | | | | **Energy** (millions of KWH) | | | | | **Fuel** | |
|---|---|---|---|---|---|---|---|---|---|---|---|
| | | | | | Company Generated | | | | | | |
| | Net Seasonal Capability | Peak Load | Capacity Margin | Load Factor | Fossil | Nuclear | Total | Purchased Power | Total | Fuel Cost Per KWH | Efficiency— BTU Per KWH |
| *1994* | 6 226 | 5 291 | 15.0% | 63.9% | 18 146 | 11 824 | 29 970 | 922 | 30 892 | 1.35¢ | 10 454 |
| *1993* | 6 226 | 5 397 | 13.3 | 61.6 | 21 105 | 10 435 | 31 540 | 273 | 31 813 | 1.39 | 10 276 |
| *1992* | 6 463 | 5 091 | 21.2 | 63.4 | 17 371 | 13 814 | 31 185 | (122) | 31 063 | 1.45 | 10 395 |
| *1991* | 6 460 | 5 361 | 17.0 | 62.9 | 18 041 | 13 454 | 31 495 | 40 | 31 535 | 1.48 | 10 442 |
| *1990* | 6 437 | 5 261 | 18.3 | 63.6 | 21 114 | 9 481 | 30 595 | 413 | 31 008 | 1.52 | 10 354 |
| *1984* | 5 384 | 4 659 | 13.5 | 66.1 | 19 930 | 4 303 | 24 233 | 2 621 | 26 854 | 1.71 | 10 349 |

**Investment** (millions of dollars)

| Year | Utility Plant In Service | Accumulated Depreciation & Amortization | Net Plant | Construction Work In Progress & Perry Unit 2 | Nuclear Fuel and Other | Total Property, Plant and Equipment | Utility Plant Additions | Total Assets |
|---|---|---|---|---|---|---|---|---|
| *1994* | $9 770 | 2 906 | 6 864 | 129 | 343 | $7 336 | $197 | $10 691 |
| *1993* | 9 571 | 2 677 | 6 894 | 181 | 385 | 7 460 | 218 | 10 710 |
| *1992* | 9 449 | 2 488 | 6 961 | 781 | 424 | 8 166 | 200 | 12 071 |
| *1991* | 8 888 | 2 274 | 6 614 | 853 | 503 | 7 970 | 204 | 11 829 |
| *1990* | 8 636 | 2 039 | 6 597 | 921 | 568 | 8 086 | 251 | 11 681 |
| *1984* | 4 282 | 1 164 | 3 118 | 3 527 | 485 *(f)* | 7 130 | 939 | 8 050 |

**Capitalization** (millions of dollars & %)

| Year | Common Stock Equity | | Preferred & Preference Stock, with Mandatory Redemption Provisions | | Preferred Stock, without Mandatory Redemption Provisions | | Long-Term Debt | | Total |
|---|---|---|---|---|---|---|---|---|---|
| *1994* | $1 882 | 30% | 253 | 4% | 451 | 7% | 3 697 | 59% | $6 283 |
| *1993* | 1 785 | 27 | 313 | 5 | 451 | 7 | 4 019 | 61 | 6 568 |
| *1992* | 2 889 | 39 | 364 | 5 | 354 | 5 | 3 694 | 51 | 7 301 |
| *1991* | 2 855 | 38 | 332 | 4 | 427 | 6 | 3 841 | 52 | 7 455 |
| *1990* | 2 810 | 39 | 237 | 3 | 427 | 6 | 3 729 | 52 | 7 203 |
| *1984* | 2 403 | 39 | 451 | 7 | 344 | 6 | 2 994 | 48 | 6 192 |

*(d) Includes write-off of Perry Unit 2 of $583 million in 1993.*

*(e) Average shares outstanding and related per share computations reflect the Cleveland Electric 1.11-for-one exchange ratio and the Toledo Edison one-for-one exchange ratio for Centerior Energy shares at the date of affiliation, April 29, 1986.*

*(f) Restated for effects of capitalization of nuclear fuel lease and financing arrangements pursuant to Statement of Financial Accounting Standards 71.*

# Board Of Directors

***Richard P. Anderson*** *(65)* President and Chief Executive Officer of The Andersons Management Corporation, a grain, farm supply and retailing firm. 1986

***Albert C. Bersticker*** *(60)* President and Chief Executive Officer of Ferro Corporation, a producer of specialty chemical materials for manufactured products. 1990

***Leigh Carter*** *(69)* Retired President and Chief Operating Officer of The BFGoodrich Company, a producer of chemicals, plastics and aerospace products. Retired Chairman of Tremco, Incorporated, a manufacturer of specialty chemical products and a wholly owned subsidiary of The BFGoodrich Company. 1986

***Thomas A. Commes*** *(52)* President and Chief Operating Officer of The Sherwin-Williams Company, a manufacturer of paints and painting supplies. 1987

***William F. Conway*** *(64)* President of William F. Conway & Associates, Inc., a management consulting firm. Retired Executive Vice President–Nuclear of Arizona Public Service Company, an electric utility. 1994

***Wayne R. Embry*** *(57)* President and Chief Operating Officer of the Cleveland Cavaliers, a professional basketball team. Chairman of M.A.L. Co., a fabricator of hardboard, fiberglass and carpeting materials for the automotive industry. 1991

*Number in parentheses indicates age.*
*Date indicates first year in which elected to Board.*

***Robert J. Farling*** *(58)* Chairman, President and Chief Executive Officer of the Company and Centerior Service Company. 1988

***George H. Kaull*** *(63)* Retired Chairman of Premix, Inc., a developer, manufacturer and fabricator of thermoset reinforced composite materials. 1987

***Richard A. Miller*** *(68)* Retired Chairman and Chief Executive Officer of the Company and Centerior Service Company. 1986

***Frank E. Mosier*** *(64)* Retired Vice Chairman of the Advisory Board of BP America Inc., a producer and refiner of petroleum products. 1986

***Sister Mary Marthe Reinhard, SND*** *(65)* Director of Development for the Sisters of Notre Dame of Cleveland, Ohio. Former President of Notre Dame College of Ohio. 1986

***Robert C. Savage*** *(57)* President and Chief Executive Officer of Savage & Associates, Inc., an insurance, financial planning and estate planning firm. 1990

***William J. Williams*** *(66)* Retired Chairman of Huntington National Bank. 1986

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***Robert M. Ginn*** Chairman Emeritus
***John P. Williamson*** Chairman Emeritus

# Committees Of The Board

| *Audit* | *Capital Expenditures* | *Environmental and Community Responsibility* | *Executive and Nominating* | *Finance* | *Human Resources* | *Nuclear* |
|---|---|---|---|---|---|---|
| T.A. Commes, Chairman | G.H. Kaull, Chairman | Sr. M.M. Reinhard, Chairman | R.J. Farling, Chairman | R.A. Miller, Chairman | F.E. Mosier, Chairman | R.P. Anderson, Chairman |
| R.P. Anderson | A.C. Bersticker | W.R. Embry | L. Carter | L. Carter | W.R. Embry | A.C. Bersticker |
| L. Carter | W.F. Conway | R.A. Miller | T.A. Commes | T.A. Commes | G.H. Kaull | W.F. Conway |
| W.R. Embry | R.A. Miller | F.E. Mosier | R.A. Miller | R.J. Farling | R.C. Savage | R.J. Farling |
| Sr. M.M. Reinhard | F.E. Mosier | R.C. Savage | W.J. Williams | F.E. Mosier | W.J. Williams | Sr. M.M. Reinhard |
| | | | | R.C. Savage | | W.J. Williams |

# Share Owner Information

### *Dividend Reinvestment and Stock Purchase Plan and Individual Retirement Account (CX•IRA)*

The Company has a Dividend Reinvestment and Stock Purchase Plan which provides share owners of record and customers of the Company's subsidiaries a convenient means of purchasing shares of Company common stock by investing all or a part of their quarterly dividends as well as making cash investments. In addition, individuals may establish an individual retirement account (IRA) which invests in Company common stock through the Plan. Information relating to the Plan and the CX•IRA may be obtained from Share Owner Services at the Company.

### *CX•IRA Custodian*

All communications about an existing CX•IRA should be directed to the Custodian at the address or telephone numbers listed below:

Society National Bank
Custodian, CX•IRA
P.O. Box 6477
Cleveland, OH 44101

In Cleveland area 737-5745

Elsewhere in Ohio 1-800-362-0697, Extension 5745

Outside Ohio 1-800-321-1355, Extension 5745

### *Share Owner Services*

Communications regarding stock transfer requirements, lost certificates, dividends and changes of address should be directed to Share Owner Services at the Company. To reach Share Owner Services by phone, call:

In Cleveland area 642-6900 or 447-2400

Outside Cleveland area 1-800-433-7794

Please have your account number ready when calling.

### *Investor Relations*

Inquiries from security analysts and institutional investors should be directed to Terrence R. Moran, Manager-Investor Relations, at the Company's mail address or by telephone at (216) 447-2882.

### *Transfer Agent*

Centerior Energy Corporation
Share Owner Services
P.O. Box 94661
Cleveland, OH 44101-4661

Stock transfers may be presented at
Society Trust Company of New York
5 Hanover Square, 10th Floor
New York, NY 10004

### *Registrar*

Society National Bank
Corporate Trust Division
P.O. Box 6477
Cleveland, OH 44101

### *Executive Offices*

Centerior Energy Corporation
6200 Oak Tree Boulevard
Independence, OH
Telephone: (216) 447-3100
FAX: (216) 447-3240

### *Mail Address*

Centerior Energy Corporation
P.O. Box 94661
Cleveland, OH 44101-4661

### *Independent Accountants*

Arthur Andersen LLP
1717 East Ninth Street
Cleveland, OH 44114

### *Common Stock*

Listed on the New York, Chicago and Pacific Stock Exchanges. Options are traded on The Pacific Stock Exchange. New York Stock Exchange symbol–CX. Newspaper abbreviation–CentEn or CentrEngy.

### *Annual Meeting*

The 1995 annual meeting of the share owners of the Company will be held on April 25, 1995. Owners of common stock as of February 24, 1995, the record date for the meeting, will be eligible to vote on matters brought up for share owners' consideration.

### *Environmental Report*

The Company will furnish to share owners, without charge, a copy of a report on its environmental performance. Requests should be directed to Share Owner Services.

### *Form 10-K*

The Company will furnish to share owners, without charge, a copy of its most recent annual report to the Securities and Exchange Commission. Requests should be directed to Share Owner Services.

### *Audio Cassettes*

Share owners with impaired vision may obtain audio cassettes of the Company's Quarterly Reports and Annual Report. To obtain a cassette, simply write or call Share Owner Services. There is no charge for this service.


Ohio

*Centerior Energy Corporation was formed in April 1986 upon the affiliation of The Cleveland Electric Illuminating Company and The Toledo Edison Company. With assets of about $11 billion, Centerior Energy is one of the largest electric utility systems in the nation. The Centerior operating companies serve 2.6 million people in a combined service area of 4,200 square miles in Northern Ohio. Centerior Energy is an equal opportunity employer.*

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