

As filed with the Securities and Exchange Commission on December 12, 1997

Registration No. 333-33397

SECURITIES AND EXCHANGE COMMISSION  
WASHINGTON, D.C. 20549

AMENDMENT NO. 5  
TO  
FORM S-1  
REGISTRATION STATEMENT  
UNDER  
THE SECURITIES ACT OF 1933

NRG ENERGY, INC.  
(Exact Name of Registrant as specified in its charter)

DELAWARE	4911	41-1724239
(State or other jurisdiction of incorporation or organization)	(Primary Standard Industrial Classification Code Number)	(I.R.S. Employer Identification Number)

1221 NICOLLET MALL, SUITE 700  
MINNEAPOLIS, MINNESOTA 55403  
(612) 373-5300  
(Address, including zip code, and telephone number, including area code, of  
Registrant's principal executive offices)

JULIE A. JORGENSEN  
CORPORATE SECRETARY  
NRG ENERGY, INC.  
1221 NICOLLET MALL, SUITE 700  
MINNEAPOLIS, MINNESOTA 55403  
(612) 373-5300  
(Name, address, including zip code, and telephone number, including area  
code, of agent for service)

Copy to:  
STACY J. KANTER, ESQ.  
SKADDEN, ARPS, SLATE, MEAGHER & FLOM LLP  
919 THIRD AVENUE  
NEW YORK, NEW YORK 10022  
(212) 735-3000

APPROXIMATE DATE OF COMMENCEMENT OF PROPOSED SALE TO THE PUBLIC: As soon  
as practicable after this Registration Statement becomes effective.

If any of the securities being registered on this Form are to be offered  
on a delayed basis or continuous basis pursuant to Rule 415 under the  
Securities Act of 1933, check the following box. [ ]

If this form is filed to register additional securities for an offering  
pursuant to Rule 462(b) under the Securities Act, please check the following  
box and list the Securities Act registration statement number of the earlier  
effective registration statement for the same offering. [ ]

If this form is a post-effective amendment filed pursuant to Rule 462(c)  
under the Securities Act, check the following box and list the Securities Act  
registration statement number of the earlier effective registration statement  
for the same offering. [ ]

If delivery of the prospectus is expected to be made pursuant to Rule 434, please check the following box. [ ]

CALCULATION OF REGISTRATION FEE

TITLE OF EACH CLASS OF SECURITIES TO BE REGISTERED	AMOUNT TO BE REGISTERED	PROPOSED MAXIMUM OFFERING PRICE PER NOTE	PROPOSED MAXIMUM AGGREGATE OFFERING PRICE (1)	AMOUNT OF REGISTRATION FEE
7 1/2% Senior Notes due 2007 .....	\$250,000,000	100%	\$250,000,000	\$75,758 (2)

- (1) Estimated in accordance with Rule 457 (c) of the Securities Act, solely for the purpose of calculating the registration fee.  
(2) Previously paid.

THE REGISTRANT HEREBY AMENDS THIS REGISTRATION STATEMENT ON SUCH DATE OR DATES AS MAY BE NECESSARY TO DELAY ITS EFFECTIVE DATE UNTIL THE REGISTRANT SHALL FILE A FURTHER AMENDMENT WHICH SPECIFICALLY STATES THAT THIS REGISTRATION STATEMENT SHALL THEREAFTER BECOME EFFECTIVE IN ACCORDANCE WITH SECTION 8(A) OF THE SECURITIES ACT OF 1933, AS AMENDED, OR UNTIL THE REGISTRATION STATEMENT SHALL BECOME EFFECTIVE ON SUCH DATE AS THE COMMISSION, ACTING PURSUANT TO SAID SECTION 8(A), MAY DETERMINE.

INFORMATION CONTAINED HEREIN IS SUBJECT TO COMPLETION OR AMENDMENT. A REGISTRATION STATEMENT RELATING TO THESE SECURITIES HAS BEEN FILED WITH THE SECURITIES AND EXCHANGE COMMISSION. THESE SECURITIES MAY NOT BE SOLD NOR MAY OFFERS TO BUY BE ACCEPTED PRIOR TO THE TIME THE REGISTRATION STATEMENT BECOMES EFFECTIVE. THIS PROSPECTUS SHALL NOT CONSTITUTE AN OFFER TO SELL OR THE SOLICITATION OF AN OFFER TO BUY NOR SHALL THERE BE ANY SALE OF THESE SECURITIES IN ANY STATE IN WHICH SUCH OFFER, SOLICITATION OR SALE WOULD BE UNLAWFUL PRIOR TO REGISTRATION OR QUALIFICATION UNDER THE SECURITIES LAWS OF ANY SUCH STATE.

SUBJECT TO COMPLETION, DATED DECEMBER 12, 1997

PROSPECTUS

[NRG LOGO]

OFFER FOR ALL OUTSTANDING  
71/2% SENIOR NOTES DUE 2007  
IN EXCHANGE FOR  
71/2% SENIOR NOTES DUE 2007  
WHICH HAVE BEEN REGISTERED UNDER THE SECURITIES ACT OF 1933  
OF

NRG ENERGY, INC.

THE EXCHANGE OFFER WILL EXPIRE AT 5:00 P.M.,  
NEW YORK CITY TIME, ON FRIDAY, JANUARY 16, 1998,  
UNLESS EXTENDED

NRG Energy, Inc., a Delaware corporation ("NRG"), hereby offers, upon the

terms and subject to the conditions set forth in this Prospectus (as the same may be amended or supplemented from time to time, the "Prospectus") and the accompanying Letter of Transmittal (which together constitute the "Exchange Offer"), to exchange an aggregate principal amount of up to \$250,000,000 of 7 1/2% Senior Notes due 2007 which have been registered under the Securities Act of 1933 (the "New Notes") of NRG for a like principal amount of the issued and outstanding 7 1/2% Senior Notes due 2007 (the "Old Notes" and, with the New Notes, the "Notes") of NRG from the holders (the "Holders") thereof. The terms of the New Notes are identical in all material respects to the terms of the Old Notes, except for certain transfer restrictions and registration rights relating to the Old Notes.

The Notes are redeemable at any time, at the option of NRG at a redemption price equal to the principal amount thereof plus accrued interest plus a Make-Whole Premium (as defined herein). See "Description of Notes -- Optional Redemption." Upon a Change of Control (as defined herein), NRG may be required to purchase the Notes at a redemption price equal to 101% of the principal amount thereof plus accrued interest. See "Description of Notes -- Change of Control." The Notes are senior unsecured obligations of NRG, which conducts substantially all of its business through numerous project subsidiaries and project affiliates. As a result, all existing and future liabilities of the direct and indirect subsidiaries and affiliates of NRG will be effectively senior to the Notes. Because substantially all of the operations of NRG are conducted by its project subsidiaries and project affiliates, NRG's cash flow and its ability to service its indebtedness, including its ability to pay the interest on and principal of the Notes when due, are dependent upon cash dividends and distributions or other transfers from its project and other subsidiaries and project affiliates to NRG. As of September 30, 1997, NRG's project subsidiaries and project affiliates had total assets of \$8.1 billion (excluding Pacific Generation Company ("PGC") assets of \$1.2 billion acquired November 4, 1997), total indebtedness of \$4.4 billion (excluding PGC indebtedness of \$0.7 billion assumed November 4, 1997) and an aggregate debt-to-total capitalization ratio of approximately 54%. See "Risk Factors -- Holding Company Structure." The Indenture under which the Notes will be issued does not restrict the incurrence of additional indebtedness by NRG or its subsidiaries and affiliates.

For each Old Note accepted for exchange, the Holder of such Old Note will receive a New Note having a principal amount equal to that of the surrendered Old Note. The New Notes will bear interest from the most recent date to which interest has been paid on the Old Notes or, if no interest has been paid on the Old Notes, from June 17, 1997. Accordingly, registered Holders of New Notes on the relevant record date for the first interest payment date following the consummation of the Exchange Offer will receive interest accruing from the most recent date to which interest has been paid or, if no interest has been paid, from June 17, 1997. Old Notes accepted for exchange will cease to accrue interest from and after the date of consummation of the Exchange Offer. Holders of Old Notes whose Old Notes are accepted for exchange will not receive any payment in respect of accrued interest on such Old Notes.

The New Notes are being offered hereunder in order to satisfy certain obligations of NRG contained in the Registration Rights Agreement, dated as of June 12, 1997 (the "Registration Rights Agreement"), among NRG and the other signatories thereto. Based on interpretations by the staff of the Securities and Exchange Commission (the "Commission") issued to third parties, New Notes issued pursuant to the Exchange Offer in exchange for the Old Notes may be offered for resale, resold and otherwise transferred by Holders thereof (other than any such Holder which is an "affiliate" of NRG within the meaning of Rule 405 under the Securities Act of 1933, as amended (the "Securities Act")), without compliance with the registration and prospectus delivery provisions of the Securities Act, provided that such New Notes are acquired in the ordinary course of such Holders' business and such Holders have no arrangement with any person to participate in the distribution of such New Notes. Each Holder, other than a broker-dealer, must acknowledge that it is not engaged in, and does not intend to engage in, a distribution of New Notes. If any Holder is an affiliate of NRG or is engaged in or intends to engage in or has any arrangement with any person to

participate in the distribution of the New Notes to be acquired pursuant to the Exchange Offer, such Holder (i) could not rely on the applicable interpretations of the staff of the Commission and (ii) must comply with the registration and prospectus delivery requirements of the Securities Act in connection with any resale transaction, including the delivery of a prospectus which contains the information with respect to any selling holder required by the Securities Act. Each broker-dealer that receives New Notes for its own account pursuant to the Exchange Offer must represent to NRG that it will deliver a prospectus in connection with any resale of such New Notes. The Letter of Transmittal states that by so representing and by delivering a prospectus, a broker-dealer will not be deemed to admit that it is an "underwriter" within the meaning of the Securities Act. This Prospectus, as it may be amended or supplemented from time to time, may be used by a broker-dealer in connection with resales of New Notes received in exchange for Old Notes where such Old Notes were acquired by such broker-dealer as a result of market-making activities or other trading activities. NRG has agreed that, starting on the Expiration Date (as defined herein) and ending on the close of business on the 90th day following the Expiration Date, it will make this Prospectus available to any broker-dealer for use in connection with any such resale. See "Plan of Distribution."

NRG will not receive any proceeds from this Exchange Offer. NRG has agreed to bear the expenses of this Exchange Offer. Tenders of Old Notes pursuant to the Exchange Offer may be withdrawn at any time prior to the Expiration Date. In the event NRG terminates the Exchange Offer and does not accept for exchange any Old Notes, NRG will promptly return the Old Notes to the Holders thereof. See "The Exchange Offer."

Prior to the Exchange Offer, there has been no public market for the Old Notes or the New Notes. NRG does not intend to list the New Notes on any securities exchange or to seek approval for quotation through any automated quotation system. There can be no assurance that an active market for the New Notes will develop. To the extent that a market for the New Notes does develop, the New Notes could trade at a discount from their principal amount. See "Risk Factors -- Lack of a Public Market for the Notes."

SEE "RISK FACTORS" BEGINNING ON PAGE 16 FOR A DISCUSSION OF CERTAIN RISKS WHICH HOLDERS WHO TENDER THEIR OLD NOTES SHOULD CONSIDER IN CONNECTION WITH THIS EXCHANGE OFFER.

THESE SECURITIES HAVE NOT BEEN APPROVED OR DISAPPROVED BY THE SECURITIES AND EXCHANGE COMMISSION OR ANY STATE SECURITIES COMMISSION NOR HAS THE SECURITIES AND EXCHANGE COMMISSION OR ANY STATE SECURITIES COMMISSION PASSED UPON THE ACCURACY OR ADEQUACY OF THIS PROSPECTUS. ANY REPRESENTATION TO THE CONTRARY IS A CRIMINAL OFFENSE.

The date of this Prospectus is December 17, 1997

#### AVAILABLE INFORMATION

NRG has filed with the Commission a Registration Statement on Form S-1 under the Securities Act with respect to the New Notes offered hereby. As permitted by the rules and regulations of the Commission, this Prospectus omits certain information, exhibits and undertakings contained in the Registration Statement. For further information with respect to NRG and the New Notes offered hereby, reference is made to the Registration Statement, including the exhibits thereto and the financial statements, notes and schedules filed as a part thereof. Upon the effectiveness of the Registration Statement, NRG will become subject to the informational requirements of the Securities Exchange Act of 1934, as amended (the "Exchange Act"). The Registration Statement (and the exhibits and schedules thereto), as well as the periodic reports and other information filed by NRG with the Commission, may be inspected and copied at the Public Reference Section of the Commission at Room 1024, Judiciary Plaza, 450 Fifth Street, N.W., Washington, D.C. 20549 and at the regional offices of the Commission located at 7 World Trade

Center, 15th Floor, Suite 1300, New York, New York 10048 and Suite 1400, Northwestern Atrium Center, 500 West Madison Street, Chicago, Illinois 60661-2511. Copies of such materials may be obtained from the Public Reference Section of the Commission, Room 1024, Judiciary Plaza, 450 Fifth Street, N.W., Washington, D.C. 20549, and its public reference facilities in New York, New York and Chicago, Illinois at the prescribed rates. Such information may also be accessed electronically by means of the Commission's home page on the Internet (<http://www.sec.gov>). Any statements contained in this Prospectus as to the contents of any contract or document filed as an exhibit to the Registration Statement are not necessarily complete, and each such statement is qualified in all respects by such reference.

In addition, NRG has agreed to furnish or cause to be furnished to registered holders (and, at the request thereof, owners of beneficial interests in the Notes) annual consolidated financial statements of NRG prepared in accordance with United States generally accepted accounting principles ("GAAP") (together with notes thereto, a report thereon by an independent accountant of established national reputation and a management's discussion and analysis of financial condition and results of operations), such statements to be so furnished within 120 days after the end of the fiscal year covered thereby. In addition, NRG will furnish or cause to be furnished to registered holders (and, at the request thereof owners of beneficial interests in the Notes) unaudited condensed consolidated balance sheets and statements of income and cash flows of NRG for each of the first three fiscal quarters of each fiscal year and the corresponding quarter of the prior year, such statements to be so furnished within 90 days after the end of the fiscal quarter covered thereby.

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SUMMARY

The following summary is qualified in its entirety by and should be read in conjunction with the more detailed information and the consolidated financial statements of NRG, including the notes thereto, appearing elsewhere in this Prospectus. Unless the context otherwise requires, references herein to NRG mean NRG Energy, Inc. and its direct and indirect subsidiaries. The subsidiaries of NRG that are engaged in the acquisition, development and operation of, and ownership of interests in, power generation and thermal energy production and transmission facilities and other facilities described herein are sometimes referred to individually as a "project subsidiary" and collectively as NRG's "project subsidiaries." In circumstances in which NRG owns less than a majority of the interests in the joint venture, partnership or other entity that owns or leases a facility, directly or indirectly, such joint venture, partnership or other entity is referred to individually as a "project affiliate" and collectively as the "project affiliates." References herein to ownership by NRG of interests in a project or facility refer to ownership by NRG or one of its project subsidiaries of interests in such project affiliates.

THE COMPANY

NRG is one of the leading participants in the independent power generation industry. Established in 1989 and wholly-owned by Northern States Power Company ("NSP"), NRG is principally engaged in the acquisition, development and operation of, and ownership of interests in, independent power production and cogeneration facilities, thermal energy production and transmission facilities and resource recovery facilities. The power generation facilities in which NRG had interests as of November 21, 1997 (including those under construction) had a total design capacity of 7,972 megawatts ("MW"), of which NRG had or will have operational responsibility for 5,062 MW and net ownership of or leasehold interests in 2,351 MW. In addition, NRG has substantial interests in district heating and cooling systems and steam generation and transmission operations; at December 31, 1996, these thermal businesses had a steam capacity of approximately 3,550 million British thermal units ("mmBtus"). NRG's refuse-derived fuel ("RDF") plants processed more than 808,000 tons of municipal solid waste into approximately 644,000 tons of RDF in 1996.

NRG has experienced significant growth in the last three years, expanding from 33 MW of net ownership interests in power generation facilities as of December 31, 1993 to 2,351 MW of net ownership interests as of November 21, 1997. This growth resulted primarily from a number of domestic and international investments and acquisitions, principally the Gladstone Power Station ("GPS" or "Gladstone") in Australia, the Mitteldeutsche Braunkohlengesellschaft mbH ("MIBRAG") and Schkopau ("Schkopau") Projects in Germany, the Minneapolis Energy Center ("MEC"), Pacific Generation Company ("PGC") and NRG Generating (U.S.) Inc. ("NRGG"), all as described below. NRG's total operating revenues and equity in earnings of projects increased from \$91.1 million and \$27.2 million, respectively, in 1994 to \$104.5 million and \$32.8 million, respectively, in 1996. In evaluating and acquiring its project interests, NRG has a flexible, multi-disciplinary team approach that draws on its facility operations and engineering expertise, fuel procurement and management skills, environmental experience, labor and government relations expertise and legal and financial skills.

As of November 21, 1997, NRG had direct and indirect interests in 38 power generation facilities worldwide (not including those facilities in which NEO Corporation ("NEO") and the Energy Investors Funds have an interest or the El Segundo plant of Southern California Edison in which NRG signed an Asset Purchase Agreement for a 50% interest on November 21, 1997), including projects under construction. Of these facilities, 22 are located in the United States (1,275 MW design capacity, with NRG holding 378 MW net ownership), four are located in Germany (1,160 MW design capacity, with NRG holding 267 MW net ownership), four are located in Australia (4,106 MW design capacity, with NRG holding 1,270 MW net ownership), two are located in Colombia (299 MW design capacity, with NRG holding 16 MW net ownership), and one is located in each of the Czech Republic (382 MW design capacity, with NRG holding 214 MW net ownership), Jamaica (74 MW design capacity, with NRG holding 7 MW net ownership), Peru (155 MW design capacity, with NRG holding 5 MW net ownership), Honduras

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(80 MW design capacity, with NRG holding 6 MW net ownership), Canada (110 MW design capacity, with NRG holding 28 MW net ownership), and Bolivia (218 MW design capacity with NRG holding 105 MW net ownership). In December 1996, NRG and Vattenfall AB of Sweden ("Vattenfall") acquired 96.6% of the outstanding common shares of Compania Boliviana de Energia Electrica SA -- Bolivian Power Company Limited ("COBEE"), the second largest electric utility company in Bolivia, which will have a design capacity of 218 MW after a 65 MW expansion in 1998. In addition, through its wholly-owned project subsidiary, NEO, NRG had interests on November 21, 1997 in 39 small hydroelectric and landfill gas-fired power generation facilities located in the United States with total design capacity of 113 MW, of which NRG has net ownership of 55 MW.

In May 1997, NRG consummated the largest acquisition in its history, acquiring a 25.37% interest in the assets of a 2,000 MW brown coal fired thermal power station and adjacent coal mine located in Victoria, Australia and known as Loy Yang A. The State of Victoria sold the Loy Yang A assets as part of its privatization program to a partnership formed by affiliates of NRG and of CMS Generation (a wholly-owned subsidiary of CMS Enterprises), together with Horizon Energy Investment Limited (an investment vehicle of Macquarie Bank), for a total price of approximately AUS\$4.7 billion (or US\$3.7 billion as of May 12, 1997). While most of the purchase price was raised through project-financed loans and leveraged leases that are non-recourse to the sponsors, NRG's equity investment was approximately US\$257 million. NRG funded its investment and related financing costs from a bridge loan arranged by Salomon Loan Fund Inc (the "Bridge Financing"), together with an equity investment by NSP and cash on hand.

In June 1997, NRG closed the financing for the refurbishment and expansion of the Energy Center Kladno plant in Kladno, the Czech Republic ("Kladno"). NRG owns a 34% interest in the existing 28 MW coal-fired project, which also supplies thermal energy. Non-recourse project financing was provided by a consortium of Czech banks, the International Finance Corporation, Nissho Iwai

and ABB. This financing will fund the refurbishment of the existing facility as well as the construction of a new 354 MW expansion project. NRG holds a 57.85% interest in the expansion project, and El Paso Energy International and Stredoceska Energeticka ("STE"), the regional Czech electric distribution company, hold the balance. NRG's total equity commitment in this project is approximately \$53 million.

On November 4, 1997, NRG acquired 100% of the outstanding shares of PGC, a wholly-owned indirect subsidiary of PacifiCorp Company, Inc. for \$151.3 million. PGC has ownership interests in 11 projects with a total capacity of 737 MW, of which PGC has operational responsibility for 312 MW and net ownership interests of 166 MW. In addition, PGC owns a limited partnership interest in the Energy Investors Funds, through which it owns an allocated share equal to another 39MW of net ownership interests. One of PGC's projects is located in Canada and the other ten are broadly distributed throughout the United States. The three largest projects are gas-fired, but the others are fueled by coal, hydro, waste wood, refuse-derived fuel and wind. One sells only steam, while the other ten have power sales agreements with a total of seven different utilities. PGC serves a variety of roles in these facilities, ranging from operator/manager of three projects, including its largest asset, Crockett Cogeneration, to a limited partner in other projects.

In April 1996, NRG acquired a 41.86% equity interest in O'Brien Environmental Energy, Inc. ("O'Brien"), which emerged from bankruptcy and was renamed NRG Generating (U.S.) Inc. ("NRGG"). The remaining 58.14% of the common stock of NRGG continued to be held by the then-existing equity holders in O'Brien. NRG currently holds 45.21% of the common stock of NRGG and NRG employees serve as NRG's designees on NRGG's board of directors. NRGG is a public company and its shares are traded on The NASDAQ SmallCap Market under the symbol "NRGG." NRGG has interests in three domestic operating projects with an aggregate capacity of approximately 196 MW. These are: (i) sole ownership of the 52 MW Newark Boxboard Project, a gas-fired cogeneration facility that sells electricity to Jersey Central Power and Light Company ("JCP&L") and steam to Newark Boxboard Company; (ii) sole ownership of the 122 MW E.I. du Pont Parlin Project, a gas-fired cogeneration facility that sells electricity to JCP&L and steam to E.I. du Pont de Nemours and Company; and (iii) an 83% interest in a

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22 MW standby/peak sharing facility which provides electricity and standby capabilities for the Philadelphia Cogen. In addition, NRGG has a 33.33% interest in the 150 MW Grays Ferry Project, a gas-fired cogeneration project which is under construction in Philadelphia, Pennsylvania.

In addition to power generation, NRG has interests in four district heating and cooling systems, located in Minneapolis, San Francisco, Pittsburgh and San Diego, that provide steam for heating and chilled water for cooling. NRG acquired the San Diego facility in June 1997. NRG also owns or operates two steam transmission facilities and two resource recovery/RDF facilities, all located in Minnesota. In connection with the PGC acquisition, NRG also owns interests in two additional resource recovery/RDF facilities located in Maine.

At any time, NRG has a number of projects under consideration or in development and is in various stages of negotiations regarding other potential projects in the United States and abroad. NRG is currently developing a number of significant domestic and international projects. These include a 45% interest in the West Java Project, a 400 MW coal-fired project in Indonesia in partnership with Ansaldo Energia and P.T. Kiani Metra; and a 50% interest in Southern California Edison Company's El Segundo power plant, a 1020 MW power project in California which NRG and its partner, Destec Energy, have an agreement to purchase. In addition, NRG and two partners have filed a plan in federal bankruptcy court to acquire the fossil-fueled generating assets of Cajun Electric Power Cooperative of Baton Rouge, Louisiana ("Cajun"). Also, in 1996 NRG purchased, at a substantial discount, the senior secured debt of Mid-Continent Power Company, Inc. ("MCPC"). On June 18, 1997, MCPC filed a Chapter 11 petition in federal bankruptcy court

in Tulsa, Oklahoma and concurrently filed a plan of reorganization proposing to transfer ownership of all of MCPC's assets to NRG in exchange for forgiveness of debt. On October 24, 1997, the bankruptcy court entered an order confirming MCPC's plan, which provides for the transfer of MCPC's assets to a subsidiary of NRG by December 23, 1997. NRG's development partner is entitled to a 10% interest in the MCPC project, and the bankruptcy court's confirmation order effectively mandates that NRG may own no more than 50% of the project. Because of the many complexities inherent in the development, financing and acquisition of such projects, there can be no assurance that any of these transactions will be consummated.

NRG's headquarters and principal executive offices are located at 1221 Nicollet Mall, Suite 700, Minneapolis, Minnesota 55403. Its telephone number is (612) 373-5300.

#### STRATEGY

NRG intends to continue to grow through a combination of acquisitions and greenfield development of power generation and thermal energy production and transmission facilities and related assets in the United States and abroad. In the United States, NRG's near-term focus will be primarily on the acquisition of existing power generation capacity and thermal energy production and transmission facilities, particularly in situations in which its expertise can be applied to improve the operating and financial performance of the facilities. NRG is also working with several industrial companies to develop energy projects that would provide both electricity and steam for their production facilities. In addition, to the extent that the replacement of aging power generating capacity or growth in demand creates the need for new power generation facilities in the United States, NRG intends to pursue opportunities to participate in the development of such facilities. NRG is also studying the opportunities that may be created by the current restructuring of the domestic electric utility industry, particularly the divestiture by some utility companies of their generating assets.

In the international market, NRG will continue to pursue development and acquisition opportunities in those countries in which it believes that the legal, political and economic environment is conducive to increased foreign investment. NRG intends to continue to capitalize on opportunities created by the privatization of existing government-owned power generating capacity. In addition, due to the significant existing demand for new power generating capacity in the international market, NRG intends to engage in the development of international "greenfield" projects, which are projects that are developed, permitted, financed and constructed by the developer.

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Although NRG exercises flexibility in structuring its investments in projects, NRG's goal is to own a 20% to 50% equity interest in, and to have operating control or influence over, the projects in which it invests. Where appropriate, NRG will include a local or host country partner, in order to enhance its knowledge of the region or country and to leverage its human and financial resources. NRG currently holds no interest in, and has no present intention of investing in, any nuclear generating facility.

As part of NRG's global tax strategy, NRG intends to maintain its earnings from foreign investments offshore, for permanent reinvestment in other foreign projects. For this reason, NRG intends to utilize the cash in its domestic operations to make the payments with respect to the Notes. This cash is expected to include payments of interest and principal to be received from its wholly-owned Dutch subsidiary, NRGenerating International BV ("NRGBV"), with respect to loans from NRG to that company.



## THE EXCHANGE OFFER

The Exchange Offer ..... NRG is offering to exchange up to \$250,000,000 aggregate principal amount of 7-1/2% Senior Notes due 2007 (the "New Notes") for a like principal amount of its 7-1/2% Senior Notes due 2007 (the "Old Notes" and, collectively with the New Notes, the "Notes") that are properly tendered and accepted. The terms of the New Notes and the Old Notes are identical in all material respects, except for certain transfer restrictions and registration rights relating to the Old Notes described below under " -- Summary Description of the New Notes."

Tenders; Expiration Date;  
Withdrawal ..... The Exchange Offer will expire at 5:00 p.m., New York City time, on January 16, 1998, or such later date and time to which it is extended. The tender of Old Notes pursuant to the Exchange Offer may be withdrawn at any time prior to the Expiration Date. Any Old Note not accepted for exchange for any reason will be returned without expense to the tendering Holder thereof as promptly as practicable after the expiration or termination of the Exchange Offer. See "The Exchange Offer --Terms of the Exchange Offer; Period for Tendering Old Notes," and "--Withdrawal of Tenders."

Procedures for Tendering Old  
Notes ..... Certain brokers, dealers, commercial banks, trust companies and other nominees who hold Old Notes through the Depository Trust Company (the "Book-Entry Transfer Facility") must effect tenders by book-entry through the Book-Entry Transfer Facility's automated tender offer program ("ATOP"). Tendering Holders of Old Notes wishing to accept the Exchange Offer must complete, sign and date the Letter of Transmittal, or a facsimile thereof, in accordance with the instructions contained therein, and mail or otherwise deliver such Letter of Transmittal, or such facsimile together with either certificates for such Old Notes or, if tendering through ATOP, a Book-Entry Confirmation (as defined herein) of such Old Notes into the Book-Entry Transfer Facility, if such procedure is available, and any other required documentation to the exchange agent (the "Exchange Agent") at the address set forth herein. Tendering holders of Old Notes that use ATOP will, by so doing, acknowledge that they are bound by the terms of the Letter of Transmittal. See "The Exchange Offer--Book-Entry Transfer." By executing

the Letter of Transmittal, each Holder will represent to NRG, among other things, that (i) the New Notes acquired pursuant to the Exchange Offer by the Holder and any other person are being obtained in the ordinary course of business of the person receiving such New Notes, (ii) neither the Holder nor such other person is participating in, intends to participate in or has an arrangement or understanding with any person to participate in the distribution of such New Notes and (iii) neither the Holder nor such other person is an "affiliate," as defined under Rule 405 of the Securities Act, of NRG. Each broker-dealer that

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receives New Notes for its own account in exchange for Old Notes, where such Old Notes were acquired by such broker or dealer as a result of market-making activities or other trading activities, must represent that it will deliver a prospectus in connection with any resale of such New Notes and that it acquired such Old Notes as a result of market-making activities or other trading activities. The Letter of Transmittal states that by so representing and by delivering a prospectus, a broker or dealer will not be deemed to admit that it is an "underwriter" within the meaning of the Securities Act. See "The Exchange Offer -- Procedures for Tendering Old Notes" and "Plan of Distribution."

Special Procedures for  
Beneficial Owners .....

Any beneficial owner whose Old Notes are registered in the name of a broker, dealer, commercial bank, trust company or other nominee and who wishes to tender should contact such registered Holder promptly and instruct such registered Holder to tender on such beneficial owner's behalf. If such beneficial owner wishes to tender on such owner's behalf, such owner must, prior to completing and executing the Letter of Transmittal and delivering its Old Notes, either make appropriate arrangements to register ownership of the Old Notes in such owner's name or obtain a properly completed bond power from the registered Holder. The transfer of registered ownership may take considerable time. See "The Exchange Offer -- Procedures for Tendering Old Notes."

Guaranteed Delivery  
Procedures .....

Holders of Old Notes who wish to tender their Old Notes and whose Old Notes are not immediately available or who can not deliver their Old Notes or any other documents required by the Letter of Transmittal to the Exchange Agent must tender their Old Notes according to the guaranteed delivery procedures set forth in "The Exchange Offer--Guaranteed Delivery Procedures."

Federal Income Tax

Consequences .....	The exchange pursuant to the Exchange Offer should not result in any income, gain or loss to the Holders or NRG for federal income tax purposes. See "Certain Federal Income Tax Considerations."
Use of Proceeds .....	NRG will not receive any proceeds from this Exchange Offer.
Exchange Agent .....	Norwest Bank Minnesota, National Association is serving as the exchange agent (the "Exchange Agent") in connection with the Exchange Offer.

CONSEQUENCES OF EXCHANGING OLD NOTES

Holders of Old Notes who do not exchange their Old Notes for New Notes pursuant to the Exchange Offer will continue to be subject to the restrictions on transfer of such Old Notes as set forth in the legend thereon as a consequence of the issuance of the Old Notes pursuant to exemptions from, or in transactions not subject to, the registration requirements of the Securities Act and applicable state securities laws. In general, the Old Notes may not be offered or sold, unless registered under the Securities Act, except pursuant to an exemption from, or in a transaction not subject to, the Securities Act and applicable state securities laws. NRG does not currently anticipate that it will register Old Notes under the Securities Act. See "Description of Notes -- Registration Rights." Based on interpretations by the staff of the Commission issued to third parties, New Notes issued pursuant to the Exchange Offer in exchange for Old Notes may be offered for resale, resold or otherwise transferred by Holders thereof (other than any such Holder which is an "affiliate" of NRG within the meaning of Rule 405 under the Securities Act) without compliance with the registration and prospectus delivery provisions of the Securities Act, provided that such New Notes are acquired in the ordinary course of such Holders' business and such Holders have no arrangement with any person to participate in the distribution of such New Notes. Each Holder, other than a broker-dealer, must acknowledge that it is not engaged in, and does not intend to engage in, a distribution of New Notes. If any Holder is an affiliate of NRG or is engaged in or intends to engage in or has any arrangement or understanding with respect to the distribution of the New Notes to be acquired pursuant to the Exchange Offer, such Holder (i) could not rely on the applicable interpretations of the staff of the Commission and (ii) must comply with the registration and prospectus delivery requirements of the Securities Act in connection with any resale transaction. Each broker-dealer that receives New Notes for its own account pursuant to the Exchange Offer must acknowledge that it will deliver a prospectus in connection with any resale of such New Notes. The Letter of Transmittal states that by so representing and by delivering a prospectus, a broker-dealer will not be deemed to admit that it is an "underwriter" within the meaning of the Securities Act. This Prospectus, as it may be amended or supplemented from time to time, may be used by a broker-dealer in connection with resales of New Notes received in exchange for Old Notes where such Old Notes were acquired by such broker-dealer as a result of market-making activities or other trading activities. NRG has agreed that, starting on the Expiration Date and ending on the close of business on the 90th day following the Expiration Date, it will make this Prospectus available to any broker-dealer for use in connection with any such resale. See "Plan of Distribution." However, to comply with the securities laws of certain jurisdictions, if applicable, the New Notes may not be offered or sold unless they have been registered or qualified for sale in such jurisdictions or an exemption from registration or qualification is available and is complied with. NRG does not currently intend to register or qualify the sale of the New Notes in any such jurisdictions. See "The Exchange Offer -- Consequences of Failure to Exchange Old Notes."

SUMMARY DESCRIPTION OF THE NEW NOTES

The terms of the New Notes and the Old Notes are identical in all material respects, except for certain transfer restrictions and registration rights relating to the Old Notes. The New Notes will bear interest from the most recent date to which interest has been paid on the Old Notes or, if no interest has been paid on the Old Notes, from June 17, 1997. Accordingly, registered Holders of New Notes on the relevant record date for the first interest payment date following the consummation of the Exchange Offer will receive interest accruing from the most recent date to which interest has been paid or, if no interest has been paid, from June 17, 1997. Old Notes accepted for exchange will cease to accrue interest from and after the date of consummation of the Exchange Offer. Holders of Old Notes whose Old Notes are accepted for exchange will not receive any payment in respect of interest on such Old Notes otherwise payable on any interest payment date the record date for which occurs on or after consummation of the Exchange Offer. In the event of a registration default under the Registration Rights Agreement, NRG will pay special interest ("Special Interest") to each Holder of Transfer Restricted Securities (as defined herein). See "Description of Notes -- Special Interest."

Notes Offered ..... Up to \$250,000,000 principal amount of 7-1/2% Senior Notes due 2007.

Maturity Date ..... June 15, 2007.

Interest Payment Dates ..... June 15 and December 15, commencing December 15, 1997.

Ranking ..... The New Notes will be senior unsecured obligations of NRG and will rank pari passu with all other senior unsecured indebtedness of NRG. See "Description of Notes." All existing and future liabilities of the direct and indirect subsidiaries and affiliates of NRG will be effectively senior to the Notes.

Ratings ..... The Old Notes have been assigned ratings of "BBB-" by Standard & Poor's Ratings Group and "Baa3" by Moody's Investors Service, Inc. NRG expects that the New Notes would be assigned the same ratings as the Old Notes. See "Ratings."

Optional Redemption ..... The New Notes may be redeemed at the option of NRG at any time, in whole or in part, on not less than 30 nor more than 60 days notice, at a redemption price equal to the principal amount thereof plus accrued interest plus a Make-Whole Premium. See "Description of Notes -- Optional Redemption."

Sinking Fund ..... None.

Change of Control ..... Upon a Change of Control, each holder of New Notes will have the right, subject to certain conditions, to require NRG to repurchase such holder's New Notes, in whole or in part, at 101% of the principal amount thereof, plus accrued interest, if any, to the date of purchase in accordance with the procedures set forth in the Indenture pursuant to which the New Notes will be issued (the "Indenture"). A Change of Control will not be deemed to have occurred if, after giving effect thereto, the Senior

Notes are rated BBB-or better by Standard & Poor's

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Ratings Group and Baa3 or better by Moody's Investors Service, Inc. See "Description of Notes -- Change of Control."

Exchange Offer; Registration

Rights ..... Holders of New Notes (other than as set forth below) are not entitled to any registration rights with respect to the New Notes. Pursuant to the Registration Rights Agreement, NRG agreed, for the benefit of the Holders of Old Notes, to file an Exchange Offer Registration Statement (as defined). The Registration Statement of which this Prospectus is a part constitutes the Exchange Offer Registration Statement. Under certain circumstances, certain Holders of Notes (including Holders who may not participate in the Exchange Offer or who may not freely resell New Notes received in the Exchange Offer) may require NRG to file, and cause to become effective, a shelf registration statement under the Securities Act, which would cover resales of Notes by such Holders. See "Description of Notes -- Registration Rights."

Use of Proceeds ..... NRG will not receive any proceeds from this Exchange Offer. The net proceeds to NRG from the offering of the Old Notes (the "Offering"), after deducting discounts and expenses, were approximately \$246.0 million. NRG used such net proceeds to repay outstanding debt under the Bridge Financing and for other general corporate purposes. See "Use of Proceeds" and "Management's Discussion and Analysis of Financial Condition and Results of Operations -- Liquidity and Capital Resources."

RISK FACTORS

Holders of the Old Notes should consider carefully the information set forth under the caption "Risk Factors" and all other information set forth in this Prospectus before making a decision to tender their Old Notes in the Exchange Offer.

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SUMMARY CONSOLIDATED FINANCIAL DATA

The summary consolidated financial data presented below as of December 31, 1993, 1994, 1995 and 1996, and for the years then ended, have been derived from NRG's audited consolidated financial statements. The summary consolidated financial data set forth below as of September 30, 1996 and 1997, and for the nine-month periods then ended, and as of December 31, 1992 and for the year then ended, have been derived from NRG's unaudited consolidated financial statements. Certain financial information for the years ended December 31, 1993 and 1994 have been reclassified to conform to the financial presentation for the year ended December 31, 1995. Interim results and the results for 1992, in the opinion of management of NRG, include all adjustments (consisting solely of normal recurring adjustments) necessary to present fairly the financial information for such periods; however, such interim results are not necessarily indicative of the results

that may be expected for any other interim period or for a full year. The following data should be read in conjunction with the Consolidated Financial Statements and "Management's Discussion and Analysis of Financial Condition and Results of Operations" included elsewhere in this Prospectus.

CONSOLIDATED STATEMENTS OF INCOME DATA:

	YEAR ENDED DECEMBER 31,				
	1992	1993	1994	1995	1996
	(IN THOUSANDS)				
OPERATING REVENUES					
Revenues from wholly-owned operations(1)	\$39,647	\$48,529	\$63,970	\$64,180	\$ 71,649
Equity in operating earnings of unconsolidated affiliates(2)(3)	1,321	2,695	27,155	23,639	32,815
Total operating revenues	40,968	51,224	91,125	87,819	104,464
OPERATING COSTS AND EXPENSES					
Cost of operations--wholly-owned operations	22,870	27,122	34,861	32,535	36,562
Depreciation and amortization	5,060	6,475	8,675	8,283	8,378
General, administrative, and development	14,930	11,448	19,993	34,647	39,248
Total operating costs and expenses	42,860	45,045	63,529	75,465	84,188
OPERATING INCOME (LOSS)	(1,892)	6,179	27,596	12,354	20,276
OTHER INCOME (EXPENSE)					
Equity in gain from project termination settlements(4)	--	--	9,685	29,850	--
Other income (expense), net	(1,753)	1,028	1,411	4,896	9,477
Interest expense	(1,662)	(2,679)	(6,682)	(7,089)	(15,430)
Total other income (expense)	(3,415)	(1,651)	4,414	27,657	(5,953)
INCOME (LOSS) BEFORE INCOME TAXES	(5,307)	4,528	32,010	40,011	14,323
INCOME (BENEFIT) TAXES(5)	(2,187)	1,905	2,472	8,810	(5,655)
NET INCOME (LOSS)	\$ (3,120)	\$ 2,623	\$29,538	\$31,201	\$ 19,978

(RESTUBBED TABLE CONTINUED FROM ABOVE)

	NINE MONTHS ENDED SEPTEMBER 30,	
	1996	1997
OPERATING REVENUES		
Revenues from wholly-owned operations(1)	\$ 52,479	\$ 65,081
Equity in operating earnings of unconsolidated affiliates(2)(3)	19,375	17,759
Total operating revenues	71,854	82,840
OPERATING COSTS AND EXPENSES		
Cost of operations--wholly-owned operations	26,858	32,863
Depreciation and amortization	6,300	7,096
General, administrative, and development	26,599	28,402
Total operating costs and expenses	59,757	68,361
OPERATING INCOME (LOSS)	12,097	14,479
OTHER INCOME (EXPENSE)		
Equity in gain from project termination settlements(4)	--	--

Other income (expense), net .....	6,117	8,610
Interest expense .....	(11,303)	(19,815)
	-----	-----
Total other income (expense) .....	(5,186)	(11,205)
	-----	-----
INCOME (LOSS) BEFORE INCOME TAXES .....	6,911	3,274
INCOME (BENEFIT) TAXES(5) .....	(4,358)	(11,140)
	-----	-----
NET INCOME (LOSS) .....	\$ 11,269	\$ 14,414
	=====	=====

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- (1) All of these revenues are from 100% owned operations. In accordance with its strategy described herein, when NRG does not own 100% of a project, it owns 50% or less in all cases except COBEE.
  - (2) NRG accounts for its investments in projects where ownership is between 20% and 50%, and where there is no effective and legal control, using the equity method of accounting. COBEE has been accounted for using the equity method of accounting even though NRG owned more than a 50% interest in the project. However, NRG did not have control over the project due to the fact that NRG did not have the power to elect a majority of the members of the board of directors of COBEE. NRG was only entitled to appoint four out of the nine directors. Vattenfall, the other majority holder of COBEE, appointed three of the other directors, and the remaining two directors were selected jointly by NRG and Vattenfall. In addition, on October 30, 1997, NRG sold to Vattenfall part of its interest in COBEE which resulted in NRG's ownership interest declining from 57.96% to 48.3%. Also as of such date, NRG became entitled to appoint only three of the nine directors. Vattenfall appoints three directors and the remaining three are appointed jointly by NRG and Vattenfall. Equity in earnings of unconsolidated project affiliates includes NRG's proportionate share of all net income or losses attributable to project investments accounted for using the equity method.
  - (3) Includes pretax charges of \$5.0 million, \$5.0 million and \$1.5 million in the years 1994, 1995 and 1996, respectively, to write-down the carrying value of certain energy projects.
  - (4) In 1994, NRG and its partner in the Michigan Cogeneration Partners Limited Partnership agreed to terminate a power sales contract with Consumers Power Company. The contract related to a 65 MW cogeneration facility being developed in Michigan. Due to the agreement to terminate the contract, NRG recorded a one-time pre tax-gain of \$9.7 million in 1994.  
Equity in gain from project termination settlements in 1995 included a one-time pre-tax gain of \$29.9 million related to the settlement and termination of the San Joaquin Valley power purchase agreements with PG&E. See "Business--Independent Power Production and Cogeneration--Domestic Projects--San Joaquin."
  - (5) NRG is included in the consolidated federal income tax and state franchise tax returns of NSP. NRG calculates its tax position on a separate company basis under a tax sharing agreement with NSP and receives payment from NSP for tax benefits and pays NSP for tax liabilities.

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CONSOLIDATED BALANCE SHEET DATA:

	AS OF DECEMBER 31,				
	1992	1993	1994	1995	1996
	-----	-----	-----	-----	-----
	(IN THOUSANDS)				
Net property, plant and equipment	\$46,694	\$108,934	\$107,634	\$111,919	\$129,649
Net equity investments in projects .....	16,400	20,046	164,863	221,129	365,749

Total assets .....	81,091	232,888	376,570	454,589	680,809
Long-term debt, including current maturities.....	10,499	93,451(1)	93,339(1)	90,034(1)	212,141(1)
Stockholder's equity .....	40,267	97,722	234,722	319,764	421,914

(RESTUBBED TABLE CONTINUED FROM ABOVE)

	AS OF SEPTEMBER 30,	
	1996	1997
Net property, plant and equipment	\$118,189	\$ 164,915
Net equity investments in projects .....	266,504	635,047
Total assets .....	586,461	1,066,816
Long-term debt, including current maturities.....	213,298(1)	517,738(1)
Stockholder's equity .....	332,012	481,279

(1) Includes debt relating to MEC and NRG San Diego, including current maturities, which is non-recourse to NRG. As of September 30, 1997 this debt was \$77.7 million.

OTHER DATA (UNAUDITED):

	AS OF AND FOR THE YEAR ENDED DECEMBER 31,				
	1992	1993	1994	1995	1996
	(DOLLARS IN THOUSANDS)				
NRG's net power generating capacity(MW)	33	33	992	999	1,326
NRG's net thermal energy generating capacity:					
mmBtus per hour .....	695	1,865	1,961	2,318	2,654
Mwt equivalent .....	204	547	575	679	778
Consolidated EBITDA (1) .....	\$1,415	\$13,682	\$47,367	\$55,383	\$38,131
Consolidated interest expense.....	\$1,662	\$ 2,679	\$ 6,682	\$ 7,089	\$15,430
Consolidated interest expense coverage ratio (2) .....	0.85x	5.11x	7.09x	7.81x	2.47x
Consolidated debt service (3) .....	\$2,562	\$ 4,272	\$ 9,169	\$10,394	\$18,323
Consolidated debt service coverage ratio (4) .....	0.55x	3.20x	5.17x	5.33x	2.08x
Consolidated ratio of earnings to fixed charges(5).....	(6)	2.32x	2.98x	1.56x(7)	1.75x(8)

(RESTUBBED TABLE CONTINUED FROM ABOVE)

	AS OF AND FOR THE NINE MONTHS ENDED SEPTEMBER 30,	
	1996	1997
NRG's net power generating capacity(MW)	1,209	2,351
NRG's net thermal energy generating		



capacity:		
mmBtus per hour .....	1,040	2,695
MWt equivalent .....	778	789
Consolidated EBITDA (1) .....	\$24,514	\$30,185
Consolidated interest expense.....	\$11,303	\$19,815
Consolidated interest expense coverage		
ratio (2) .....	2.17x	1.52x
Consolidated debt service (3) .....	\$13,039	\$21,730
Consolidated debt service coverage		
ratio (4) .....	1.88x	1.39x
Consolidated ratio of earnings to fixed		
charges (5).....	2.19x(8)	1.03x

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- (1) EBITDA equals the sum of income (loss) before income taxes, interest expense (net of capitalized interest) and depreciation and amortization expense. EBITDA is a measure of financial performance not defined under generally accepted accounting principles and should not be considered in isolation or as a substitute for net income, cash flows from operations or other income or cash flow data prepared in accordance with generally accepted accounting principles or as a measure of a company's profitability or liquidity. In addition, EBITDA may not be comparable to similarly titled measures presented by other companies and could be misleading unless all companies and analysts calculate them in the same fashion. Management believes that some investors consider EBITDA an indicator of a company's ability to service debt. An increase in EBITDA level implies an improved ability to service debt, but does not reflect the level of debt service charges to be covered, which will change with debt levels outstanding and interest rate charges. See Statements of Cash Flows in the Consolidated Financial Statements included elsewhere in this Prospectus.
- (2) The interest expense coverage ratio equals EBITDA divided by interest expense.
- (3) Debt service consists of interest expense and principal payments on long-term debt.
- (4) The debt service coverage ratio equals EBITDA divided by debt service.
- (5) The ratio of earnings to fixed charges is calculated by dividing earnings by fixed charges. For this purpose "earnings" means income (loss) before income taxes less undistributed equity in operating earnings of unconsolidated affiliates less equity in gain from project termination settlements plus cash distributions from project termination settlements plus fixed charges. "Fixed charges" means interest expense plus interest capitalized plus amortization of debt issuance costs plus a reasonable approximation of the interest factor of rental expense.
- (6) Due primarily to the loss incurred in 1992, NRG was unable to fully cover fixed charges. Earnings did not cover fixed charges by \$5,940.
- (7) The 1995 ratio of earnings to fixed charges calculations include the effect of an equity gain and cash distribution from a project termination settlement. If the project termination had not occurred, NRG would have been unable to fully cover fixed charges and earnings would not have covered fixed charges by \$9,913.
- (8) The 1996 ratio of earnings to fixed charges calculation includes the effect of a cash distribution from a 1995 project termination settlement. If the project termination had not occurred, NRG would have been unable to fully cover fixed charges and earnings would not have covered fixed charges by \$1,497 for the nine months ended September 30, 1996, and by \$3,504 for the year ended December 31, 1996.

effect to (i) the acquisition by NRG of a 25.37% equity interest in Loy Yang A and the financing thereof and (ii) the offering of the Old Notes (the "Offering"). The pro forma statement of income data for the year ended December 31, 1996 and the nine months ended September 30, 1997 give effect to such transactions as if they had occurred on January 1, 1996. As the Loy Yang acquisition and the Offering were consummated prior to September 30, 1997, no pro forma balance sheet data is provided. The pro forma condensed financial data do not purport to be indicative of the combined financial position or results of operations of future periods or indicative of the results that would have occurred had the transactions referred to above been consummated on the dates indicated. The following data should be read in conjunction with, and are qualified in their entirety by, the Consolidated Financial Statements and "Management's Discussion and Analysis of Financial Condition and Results of Operations" included elsewhere in this Prospectus.

FOR THE YEAR ENDED DECEMBER 31, 1996

	HISTORICAL	ADJUSTMENTS (1)	PRO FORMA
	(IN THOUSANDS)		
STATEMENT OF INCOME DATA:			
Revenues from wholly-owned operations .....	\$ 71,649	--	\$ 71,649
Equity in earnings (loss) of unconsolidated affiliates .....	32,815	\$ (18,121) (2)	14,694
Operating costs and expenses .....	(84,188)	--	(84,188)
Other income (expense) .....	9,477	26,264 (3)	35,741
Interest expense .....	(15,430)	(18,750) (4)	(34,180)
Income taxes .....	5,655	4,373 (5)	10,028
Net Income.....	\$ 19,978	\$ (6,234)	\$ 13,744

(1) Adjustments were derived from Loy Yang's audited financial statements for the fiscal years ended June 30, 1996 and June 30, 1997 to conform with NRG's December 31, 1996 year-end.

	A\$000'S
(2) After-tax net income as shown in the financial statements:	120,054
Change to Depreciation/Amortization Expense.....	(316)
Change to Finance Charges.....	(164,394)
Change to Taxes.....	120,151
Other.....	(166,682)
AFTER-TAX NET INCOME (LOSS) .....	(91,187)
NRG'S 25.37%.....	(23,134)
1996 Average Exchange Rate.....	0.7833
NRG US\$ NET INCOME (LOSS).....	(18,121)

The change in depreciation is due to the increased value in assets offset by the extension of life on assets from 35 years to 50 years. Amortization expense is from the capitalized project debt fees paid to acquire the new project debt.

The change in finance charges is due to the repayment of debt to the state of Victoria (sale proceeds) netted against the new project debt. The interest rates are variable but were immediately swapped into fixed rate

debt for a period of five years. The weighted average interest rate during the first year is 7.91%.

The change to tax expense is due to reversing Loy Yang's original tax expense in 1996 and booking a deferred tax benefit based on Loy Yang's new book loss. Approximately the statutory tax rate on the other adjustments.

"Other" is composed of interest expense recorded on the note payable to the shareholders and the operating & maintenance fee expense paid to the operator shareholders.

- (3) Includes interest income and operating and maintenance fees derived from the Loy Yang project.
- (4) Represents accrued interest on \$250 million principal amount of the Old Notes for twelve months at a rate of 7.5% per annum.
- (5) Net tax benefit derived from interest expense on the Old Notes.

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AS OF AND FOR THE NINE MONTHS ENDED SEPTEMBER 30, 1997

	HISTORICAL	ADJUSTMENTS (1)	PRO FORMA
	(IN THOUSANDS)		
STATEMENT OF INCOME DATA:			
Revenues from wholly-owned operations .....	\$ 65,081	\$ --	\$ 65,081
Equity in earnings of unconsolidated affiliates	17,759	(7,945) (2)	9,814
Operating costs and expenses .....	(68,361)	--	(68,361)
Other income and (expense) .....	8,610	8,525 (3)	17,135
Interest expense .....	(19,815)	(6,883) (4)	(26,698)
Income taxes .....	11,140	1,605 (5)	12,745
Net Income.....	\$ 14,414	\$ (4,698)	\$ 9,716

- (1) Adjustments were derived from Loy Yang's audited financial statements for the fiscal year ended June 30, 1997.
- (2) Represents estimated equity earnings from Loy Yang A through May 12, 1997, based upon historical data (January 1, 1997-May 12, 1997) adjusted for differences due to acquisition accounting primarily depreciation charges, finance charges and adjustments to income tax expense. Equity earnings of Loy Yang A from May 13 until September 30 were \$1,393. This amount is included in the Historical column of Equity in earnings of unconsolidated affiliates.
- (3) Includes interest income and operating and maintenance fees derived from the Loy Yang project.
- (4) Represents interest expense on \$250 million principal amount of the Old Notes until May 12 at a rate of 7.5% per annum. Interest of \$7,140 on the Old Notes from May 13 until September 30 is in the Historical column.
- (5) Net tax benefit derived from interest expense on the Old Notes.

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#### RISK FACTORS

Holders of Old Notes should consider carefully the following risk factors as well as the other information contained in this Prospectus in evaluating an investment in the New Notes, although the risk factors set forth below (other than "--Consequences of Failure to Exchange Old Notes") are generally applicable to the Old Notes as well as the New Notes.

#### RISKS INVOLVED IN MAKING MINORITY INVESTMENTS IN PROJECTS

NRG conducts its business primarily through direct and indirect subsidiaries and joint ventures. Most of NRG's current project investments consist of minority interests in project affiliates (i.e., where NRG beneficially owns 50% or less of the ownership interests). A substantial portion of future investments in projects also may take the form of minority interests. See "Business -- Strategy." As a result, NRG's ability to control the development, construction, acquisition or operation of such projects may be limited. The Indenture does not contain any limitations on the ability of NRG to make minority investments.

Although NRG seeks to exert a degree of influence with respect to the management and operation of projects in which it is a minority investor by negotiating to receive certain limited governance rights (such as rights to veto significant actions or to obtain positions on management committees), NRG may not always succeed in such negotiations. See "Business -- Operating Arrangements." NRG may be dependent on its co-venturers to construct and operate such projects. There can be no assurance that such co-venturers would have the same level of experience, technical expertise, human resources management and other attributes that NRG possesses. Any such co-venturer may have conflicts of interest, including those relating to its status as a provider of goods or services to the project. The approval of co-venturers also may be required for distributions of funds from projects to NRG.

#### UNCERTAINTY OF ACCESS TO CAPITAL FOR FUTURE PROJECTS

Any projects that NRG develops in the future and any projects that it may seek to acquire generally will require substantial capital investment. Continued access to debt capital from outside sources on acceptable terms is necessary to assure the success of future projects and acquisitions. NRG's ability to arrange financing on a substantially non-recourse basis and the costs of such capital are dependent on numerous factors, including general economic and capital market conditions, credit availability from banks and other financial institutions, investor confidence in NRG, its partners and in the local independent power market, the success of current projects, the perceived quality of new projects and provisions of tax and securities laws that are conducive to raising capital in this manner. In order to access capital on a substantially non-recourse basis in the future, NRG may have to make larger equity investments in, or provide more financial support for, its project subsidiaries. To date, NRG's equity capital for its projects has been provided by equity contributions from NSP and, to a lesser extent, internally-generated cash flow from its projects. There can be no assurance that NRG will be successful in structuring the financing for its projects on a substantially non-recourse basis or that NRG will obtain sufficient additional equity capital from NSP, project cash flow or additional borrowings by NRG to enable it to fund the equity commitments required for future projects.

#### CONSEQUENCES OF EXCHANGING OR FAILING TO EXCHANGE OLD NOTES

Holder of Old Notes who do not exchange their Old Notes for New Notes pursuant to the Exchange Offer will continue to be subject to the restrictions on transfer of such Old Notes as set forth in the legend thereon as a consequence of the issuance of the Old Notes pursuant to exemptions from, or in transactions not subject to, the registration requirements of the Securities Act and applicable state securities laws. In general, the Old Notes may not be offered or sold, unless registered under the Securities Act, except pursuant to an exemption from, or in a transaction not subject to, the Securities Act and applicable state securities laws. NRG does not currently anticipate that it will register Old Notes under the Securities Act. See "Description of Notes -- Registration Rights." Based on interpretations by the staff of the Commission issued to third parties, New Notes issued pursuant to the Exchange Offer in exchange for Old Notes may be offered for resale, resold or otherwise transferred by Holders thereof (other than any such Holder which is an "affiliate" of NRG within the meaning of Rule 405 under the Securities Act) without compliance with the registration and prospectus delivery provisions of the Securities Act, provided that such New Notes are acquired in the ordinary course of such Holders' business and such

Holders have no arrangement with any person to participate in the distribution of such New Notes. Each Holder, other than a broker-dealer, must acknowledge that it is not engaged in, and

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does not intend to engage in, a distribution of New Notes. If any Holder is an affiliate of NRG or is engaged in or intends to engage in or has any arrangement or understanding with respect to the distribution of the New Notes to be acquired pursuant to the Exchange Offer, such Holder (i) could not rely on the applicable interpretations of the staff of the Commission and (ii) must comply with the registration and prospectus delivery requirements of the Securities Act in connection with any resale transaction. Each broker-dealer that receives New Notes for its own account pursuant to the Exchange Offer must acknowledge that it will deliver a prospectus in connection with any resale of such New Notes. The Letter of Transmittal states that by so acknowledging and by delivering a prospectus, a broker-dealer will not be deemed to admit that it is an "underwriter" within the meaning of the Securities Act. This Prospectus, as it may be amended or supplemented from time to time, may be used by a broker-dealer in connection with resales of New Notes received in exchange for Old Notes where such Old Notes were acquired by such broker-dealer as a result of market-making activities or other trading activities. NRG has agreed that, starting on the Expiration Date and ending on the close of business on the 90th day following the Expiration Date, it will make this Prospectus available to any broker-dealer for use in connection with any such resale. See "Plan of Distribution." However, to comply with the securities laws of certain jurisdictions, if applicable, the New Notes may not be offered or sold unless they have been registered or qualified for sale in such jurisdictions or an exemption from registration or qualification is available and is complied with. NRG does not currently intend to register or qualify the sale of the New Notes in any such jurisdiction. See "The Exchange Offer -- Consequences of Failure to Exchange Old Notes."

#### HOLDING COMPANY STRUCTURE; ABILITY TO SERVICE INDEBTEDNESS

The Notes will be exclusively the obligations of NRG and not of any of its project subsidiaries or project affiliates. As a result, all existing and future liabilities of the direct and indirect subsidiaries and affiliates of NRG will be effectively senior to the Notes. Because substantially all of the operations of NRG are conducted by its project subsidiaries and project affiliates, NRG's cash flow and its ability to service its indebtedness, including its ability to pay the interest on and principal of the Notes when due, are dependent upon cash dividends and distributions or other transfers from its project and other subsidiaries and project affiliates to NRG. As of September 30, 1997, NRG's project subsidiaries and project affiliates had total assets of \$8.1 billion (excluding PGC assets of \$1.2 billion acquired November 4, 1997), total indebtedness of \$4.4 billion (excluding PGC indebtedness of \$0.7 billion assumed November 4, 1997) and an aggregate debt-to-total capitalization ratio of approximately 54%. The debt agreements of NRG's project and other subsidiaries and project affiliates generally restrict their ability to pay dividends, make distributions or otherwise transfer funds to NRG. The restrictions in such agreements generally require that, prior to and after giving effect to the payment of dividends, distributions or other transfers, (i) such subsidiaries or project affiliates meet certain financial performance or coverage ratios, (ii) no default or event of default shall have occurred, and (iii) the subsidiary or project affiliate proposing to pay the dividend, distribution or other transfer must provide for the payment of other current or prospective obligations, including operating expenses, debt service and reserves. See "Business -- Project Financing." NRG's subsidiaries and project affiliates are separate and distinct legal entities that have no obligation, contingent or otherwise, to pay any amounts due pursuant to the Notes or to make any funds available therefor, whether by dividends, loans or other payments, and do not guarantee the payment of interest on, or principal of, the Notes. NRG owns a minority interest in most of its international and domestic projects, and therefore is unable unilaterally to cause dividends or distributions to be made to NRG from these operations.

Any right of NRG to receive any assets of any of its subsidiaries or project affiliates upon any liquidation or reorganization of such subsidiaries or project affiliates (and the consequent right of holders of the Senior Notes to participate in the distribution of, or to realize proceeds from, those assets) will be effectively subordinated to the claims of any such subsidiary's or project affiliate's creditors (including trade creditors and holders of debt issued by such subsidiary or project affiliate).

The Indenture imposes no limitations on the ability of subsidiaries or project affiliates to incur additional indebtedness or to permit contractual restrictions on the distribution of cash from NRG's subsidiaries or project affiliates to NRG. As part of NRG's global tax strategy, NRG intends to maintain its earnings from foreign investments offshore, for permanent reinvestment in other foreign projects. For this reason, NRG intends to utilize the cash from its domestic operations including principal and interest

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received from loans made by NRG to its foreign affiliates to make the payments with respect to the Notes. Although NRG expects that the cash available from its domestic operations and the repayment of the loans made to its foreign affiliates will be sufficient to make the payments under the Notes, there can be no assurance that these funds will be sufficient to make these payments as and when due. If NRG elects to repatriate earnings from its foreign operations to make these payments in case of such a shortfall, then NRG may incur United States taxes (net of any available foreign tax credits) on the repatriation of such foreign earnings. As a result of these additional taxes, there can be no assurance that the foreign earnings would be sufficient to make the payments on the Notes as and when due.

#### LEVERAGE; ABILITY TO REPAY NOTES

As of September 30, 1997, NRG had total indebtedness of \$517.7 million at the corporate holding company level which results in a total debt-to-capitalization ratio of 52%; the Indenture imposes no limitations on the ability of NRG to incur additional indebtedness at this level. The substantial amount of debt at the level of the corporate holding company and at the levels of the project subsidiaries and project affiliates presents the risk that NRG might not generate sufficient cash to service its indebtedness, including the Notes, or that its leveraged capital structure could limit its ability to finance the acquisition and development of additional projects, to compete effectively or to operate successfully under adverse economic conditions. See "Capitalization," "Selected Consolidated Financial Data" and "Selected Pro Forma Condensed Financial Data."

In addition, under certain of the instruments governing NRG's debt, including the credit facility described below and the 7.625% Senior Notes due 2006 (the "1996 Senior Notes"), such debt may be accelerated upon certain events of default under the Indenture or a change of control of NRG. As a result, if any such event were to occur, NRG may not have sufficient capital to fully pay Holders the amount due under the Notes or to redeem any Notes tendered pursuant to the Change of Control Offer described under "Description of Notes -- Change of Control." See "Certain Indebtedness."

NRG has entered into a \$175 million revolving credit facility with a syndicate of banks led by ABN AMRO Bank ("ABN AMRO"), which matures on March 17, 2000. It imposes certain requirements on NRG, including requirements as to the maintenance of (i) a minimum level of consolidated tangible net worth and (ii) a minimum ratio of consolidated tangible net worth to consolidated capitalization.

#### DEPENDENCE ON, AND CONTROL BY, NORTHERN STATES POWER

NSP is NRG's sole stockholder. Since NRG's formation, NSP has provided all NRG's equity funding for its business and operations. NRG's only other source

of funding has been its borrowings and internally-generated cash flow from NRG's existing projects and investments. See "Management's Discussion and Analysis of Financial Condition and Results of Operations -- Liquidity and Capital Resources." There can be no assurance that NSP will contribute additional equity capital to NRG in the future. In the absence of continued equity contributions, there can be no assurance that NRG will have access to sufficient capital to fund its obligations with respect to its existing projects or to undertake new acquisition and development projects.

As NRG's sole stockholder, NSP has the power to control the election of the directors and all other matters submitted for stockholder approval and may be deemed to have control over the management and affairs of NRG. Currently, there are no outside directors on NRG's board of directors. In circumstances involving a conflict of interest between NSP, as the sole stockholder (and, with respect to certain projects, a significant customer of and supplier to NRG, see, "Certain Transactions"), on the one hand, and the holders of the Notes as creditors of NRG on the other, there can be no assurance that NSP would not exercise its power to control NRG in a manner that would benefit NSP to the detriment of the holders of the Notes. NSP has policies in place, pursuant to applicable law, to ensure that its ratepayers are protected from affiliate transactions that may be adverse to the ratepayers' interests. The Indenture imposes no limitations on NRG's ability to pay dividends or to make other payments to NSP or on NRG's ability to enter into transactions with NSP or other affiliates of NRG.

In addition, NSP is an important customer of, and supplier to, certain of NRG's businesses in the United States. See "Certain Transactions -- Operating Agreements." NRG purchases steam production

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services from NSP for its Rock-Tenn and Washco steam transmission lines and sells RDF to NSP from its Newport resource recovery facility. NRG provides management, operation and maintenance services for the Elk River resource recovery facility and disposes of the Elk River facility's RDF ash at NSP's Becker ash landfill. See "Certain Transactions." The failure of NSP to comply with its obligations to NRG under the agreements governing such sales and services could have a material adverse effect on NRG's revenues from these projects.

#### RISKS OF DOING BUSINESS OUTSIDE THE UNITED STATES

A key component of NRG's business strategy is the development or acquisition of projects outside the United States. See "Business -- Strategy." The economic and political conditions in certain countries where NRG has interests or in which it is or could be exploring development or acquisition opportunities present risks of delays in permitting and licensing, construction delays and interruption of business, as well as risks of war, expropriation, nationalization, renegotiation or nullification of existing contracts and changes in law or tax policy, that are greater than in the United States. The uncertainty of the legal environment in certain foreign countries in which NRG may develop or acquire projects could make it more difficult to obtain non-recourse project financing on suitable terms and could impair NRG's ability to enforce its rights under agreements relating to such projects.

Operations in foreign countries also can present currency exchange, inflation, convertibility and repatriation risks. See "Business -- Strategy." In certain countries in which NRG may develop or acquire projects in the future, economic and monetary conditions and other factors could affect NRG's ability to convert its earnings to United States dollars or other hard currencies or to move funds offshore from such countries. Furthermore, the central bank of any such country may have the authority in certain circumstances to suspend, restrict or otherwise impose conditions on foreign exchange transactions or to approve distributions to foreign investors. Although NRG generally seeks to structure its power purchase agreements and other project revenue agreements to provide for payments to be made in, or indexed to, United States dollars or a currency freely convertible into

United States dollars, there can be no assurance that NRG will be able to achieve this structure in all cases or that a power purchaser or other customer will be able to obtain sufficient dollars or other hard currency to pay such obligations.

As part of privatizations or other acquisition opportunities, NRG may make investments in ancillary businesses not directly related to power generation, thermal energy production and transmission or resource recovery and in which NRG management may not have had prior experience. In such cases, NRG's policy is to attract partners with the necessary expertise. However, no assurance can be given that such persons will be available as co-venturers in every case. In addition, as a condition to participating in privatizations and refurbishments of formerly state-owned businesses, NRG may be required to undertake transitional obligations relating to union contracts, employment levels and benefits obligations for employees, which could prevent or delay the achievement of desirable operating efficiencies and financial performance.

#### ACQUISITION AND DEVELOPMENT UNCERTAINTIES

The development projects and acquisitions in which NRG may invest in the future, including those described herein, may be large and complex, and NRG may not be able to complete the development or acquisition of any such project. Development projects and acquisitions require NRG to expend significant sums for engineering, permitting, legal, financial advisory and other expenses in preparation for competitive bids that NRG may not win or before it can be determined whether a project is feasible, economically attractive or capable of being financed. There can be no assurance that the projects that NRG pursues, and on which it may spend significant sums, will prove to be desirable project investments, or that NRG will be able to win any such competitive bids, obtain new power purchase agreements, overcome any local opposition, and obtain the necessary agreements, contracts, licenses, certifications and permits necessary for the successful development of new projects and acquisition of interests in existing projects. Even if NRG is successful in the development or acquisition of an interest in a project, NRG may require substantial additional debt or equity financing for such projects, which additional financing may not be available on acceptable terms, if at all. Most acquisition agreements and

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power purchase agreements permit the seller or customer, respectively, to terminate the agreement or impose penalties if the acquisition or operation of the project (as the case may be) is not achieved by a specified date. NRG may fail to acquire or develop projects despite having incurred significant expenses.

#### COMPETITION

The independent power industry is characterized by numerous strong and capable competitors, some of which have more extensive developmental or operating experience, more extensive experience in the acquisition and development of power generation capacity, larger staffs and greater financial resources than NRG. Further, in recent years, the domestic independent power industry has been characterized by strong and increasing competition which has contributed to a reduction in prices offered by utilities for power produced by independent power producers and has resulted in lower returns to project investors. See "Risk Factors -- Effects of Ongoing Changes in the U.S. Utility Industry" and "Business -- Competition."

Many of NRG's competitors also are seeking attractive acquisition opportunities, both in the United States and abroad. This competition may adversely affect NRG's ability to make investments or acquisitions on terms favorable to NRG. Many foreign and domestic utilities are now engaging in "competitive bid" solicitations for new capacity demands or acquisitions.

#### CONSTRUCTION AND START-UP RISKS; INADEQUATE INSURANCE, WARRANTIES AND PERFORMANCE GUARANTEES



As with any major industrial construction effort, the construction, expansion or refurbishment of a power generation, thermal energy production and transmission facility or resource recovery facility involves many risks, including supply interruptions, work stoppages, labor disputes, weather interferences, unforeseen engineering, environmental and geological problems and unanticipated cost overruns. The commencement of operation of such newly-constructed, expanded or refurbished facilities also involves many risks, including the breakdown or failure of equipment or processes and test performance below expected levels of output or efficiency. New plants may employ recently developed and technologically complex equipment, especially in the case of newer environmental emission control technology. While insurance is maintained to protect against certain risks, warranties are obtained from vendors for limited periods and contractors are obligated to meet certain performance levels, the proceeds of such insurance, warranties or performance guarantees may not be adequate to cover lost revenues, increased expenses or liquidated damages payments. As a result, a project may operate at a loss and be unable to fund principal and interest payments under its project financing agreements, which may allow the affected lenders to accelerate such debt.

In addition, many power and thermal energy purchase agreements permit the customer to terminate the agreement, retain security posted by the developer as liquidated damages or change the payments to be made to the project subsidiary or the project affiliate in the event certain milestones, such as commencing commercial operation of the project, are not met by specified dates. In the event such a termination right is exercised, a project may not commence generating revenues, the default provisions in a financing agreement may be triggered (rendering such debt immediately due and payable) and the project may be rendered insolvent as a result.

#### OPERATING RISKS; INADEQUATE INSURANCE, WARRANTIES AND PERFORMANCE GUARANTEES

The operation of a power generation facility, thermal energy production and transmission facility, resource recovery facility or mining facility involves many risks, including the breakdown or failure of generation equipment or other equipment or processes, labor disputes, fuel interruption and operating performance below expected levels. Operation below expected capacity levels may result in lost revenues or increased expenses, including higher maintenance costs and penalties. As a result, a facility may be unable to perform its obligations under its purchase agreements, triggering the default provisions in a financing agreement (rendering such debt immediately due and payable) and the project may be rendered insolvent as a result.

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Certain power purchase agreements of NRG's project subsidiaries or project affiliates permit the purchaser to terminate the agreement, modify the payments required under the agreement, recover payments previously made under the agreement or require such project subsidiaries or project affiliates to pay liquidated damages under the agreement in certain circumstances. See "Business -- Independent Power Production and Cogeneration." While insurance is maintained to protect against certain risks, warranties are obtained from vendors for limited periods and contractors are obligated to meet certain performance levels, the proceeds of such insurance, warranties or performance guarantees may not be adequate to cover lost revenues, increased expenses or liquidated damages payments. As a result, default provisions in the project subsidiary's or project affiliate's financing agreements may be triggered, which might allow the affected lenders to accelerate such debt.

#### DEPENDENCE ON PROJECT AFFILIATES

Payments under power purchase agreements for domestic projects that satisfy the requirements for "qualifying facility" status under the Public Utility Regulatory Policies Act ("PURPA") and that are based upon actual short-run (as opposed to forecasted long-run) "avoided cost" (or the cost that would otherwise have been paid for power from the purchasing utility's highest-cost generating facility, see "Business"), are subject to significant

variations based upon a number of factors outside of the control of the owners of such facilities, including weather, economic conditions, and the particular operating profile and generating capacity position of the purchasing utility. A project affiliate of NRG owns a 50% interest in a joint venture that owns the Sunnyside waste coal-fired power generation facility in Carbon County, Utah. The Sunnyside facility has experienced a shortfall in project cash flow attributable primarily to decreased revenues due to avoided energy rates being significantly lower than originally forecasted. In the absence of a restructuring of the project's debt, a debt service reserve fund, which has been used to make up cash shortfalls, is expected to be depleted within twelve months. There can be no assurance as to the actions the partnership which owns the Sunnyside facility may take at that time. See "Business -- Independent Power Production and Cogeneration -- Sunnyside."

NRG has provided guarantees relating to certain equity and operating obligations of its project subsidiaries. One example is NRG's guarantee of the obligations of its project subsidiary that operates the Gladstone facility for up to AUS\$25 million, indexed to the Australian consumer price index ("ACPI") (US\$19.7 million, based on exchange rates and ACPI in effect at September 30, 1997), under the project subsidiary's operating and maintenance agreement with the owners of the facility. If NRG were required to satisfy all these guarantees and other obligations, such event would have a material adverse effect on NRG's condition, financial and otherwise. See "Business -- Description of NRG's Projects" and "Business -- Independent Power Production and Cogeneration -- Gladstone Power Station."

#### DEPENDENCE ON CERTAIN CUSTOMERS AND PROJECTS

A power generation, thermal energy production and transmission or resource recovery facility typically relies on a single supplier each for the provision of fuel, water and other services required for operation of the facility and on a single customer or a few customers to purchase all of the facility's output, in each case under long-term agreements that provide the support for any project debt used to finance such facilities. The failure of any one customer or supplier to fulfill its contractual obligations to the facility could have a material adverse effect on such facility's financial results. As a result, the financial performance of such facilities is dependent on the continued performance by customers and suppliers of their obligations under such long-term agreements and, in particular, on the credit quality of the project's customers. Each of the Rock-Tenn and Newport projects produced more than ten percent of NRG's net revenues for 1996. See "Business -- Principal Customers of Operating Subsidiaries." In addition, on a pro forma basis Loy Yang A would have produced more than ten percent of NRG's net revenues for 1996.

#### GOVERNMENTAL REGULATION

NRG is subject to a number of complex and stringent environmental and other laws and regulations affecting many aspects of its present and future operations, including the disposal of various forms of

waste and the construction or permitting of new facilities. See "Regulation." Such laws and regulations generally require NRG to obtain and comply with a wide variety of licenses, permits and other approvals, and may in some cases be enforced by both public officials and private individuals. There can be no assurance that existing laws or regulations will not be revised or that new laws or regulations will not be adopted or become applicable to NRG which could have an adverse impact on its operations. There can be no assurance that NRG will be able to recover all or any increased costs of compliance from its customers or that its business and financial condition will not be materially and adversely affected by future changes in environmental laws or regulations. In addition, regulatory compliance for the construction of new facilities is a costly and time-consuming process, and intricate and rapidly changing environmental regulations may require major expenditures for permitting and create the risk of expensive delays or material impairment of project value if projects cannot function as planned due to changing

regulatory requirements or local opposition.

PURPA and the Public Utility Holding Company Act of 1935, as amended ("PUHCA"), are two of the laws (including the regulations thereunder) that affect NRG's operations. PURPA provides to qualifying facilities ("QFs") certain exemptions from federal and state laws and regulations, including organizational, rate and financial regulation. PUHCA regulates public utility holding companies and their subsidiaries. NRG is not and will not be subject to regulation as a holding company under PUHCA as long as the domestic power plants it owns are QFs under PURPA or are exempted as exempt wholesale generators ("EWGs"), and so long as its foreign utility operations are exempted as EWGs or foreign utility companies or are otherwise exempted under PUHCA. QF status is conditioned on meeting certain criteria, and could be jeopardized, for example, by the loss of a steam customer or reduction of steam purchases below the amount required by PURPA. See "Regulation."

#### CHANGES IN STATE MUNICIPAL SOLID WASTE ("MSW") FLOW CONTROL LAWS

RDF projects, such as NRG's Newport facility and NSP's Elk River facility, which is operated by NRG, historically were assured an adequate supply of MSW through state and local flow control legislation, which directed that MSW be disposed of in certain facilities. In May 1994, the United States Supreme Court held that MSW is a commodity in interstate commerce and, accordingly, that flow control legislation that prohibited shipment of MSW out of state is unconstitutional. Since this Supreme Court holding, the RDF facilities owned or operated by NRG have faced increased competition from landfills in surrounding states. As a result of such competition, MSW processed at the Newport facility decreased approximately 5% in 1995, from approximately 378,000 tons in 1994 to 360,000 tons in 1995. In 1996, however, due to assistance from NRG and a reduction of tipping fees under contracts entered into between haulers and the Ramsey and Washington Counties, waste deliveries reversed their downward trend. However, in the absence of valid flow control legislation, there can be no assurance that this improved trend will continue. See "Business -- Resource Recover Facilities."

#### EFFECTS OF ONGOING CHANGES IN THE U.S. UTILITY INDUSTRY

The U.S. electric utility industry currently is experiencing increasing competitive pressures, primarily in wholesale markets, as a result of consumer demands, technological advances, greater availability of natural gas and other factors. The Federal Energy Regulatory Commission ("FERC") has proposed regulatory changes to increase access to the nationwide transmission grid by utility and non-utility purchasers and sellers of electricity. A number of states are considering or implementing methods to introduce and promote retail competition. Proposals have been introduced in Congress to repeal PURPA and PUHCA, and the FERC has publicly indicated support for the PUHCA repeal effort. Additionally, some utilities have brought litigation aimed at forcing the renegotiation or termination of contracts requiring payments to owners of qualifying facilities based upon past estimates of avoided cost that are now substantially in excess of market prices. There can be no assurance that, in the future, utilities, with the approval of state public utility commissions, will not seek to abrogate their existing power purchase agreements. See "Regulation."

If the repeal of PURPA or PUHCA occurs, either separately or as part of legislation designed to encourage the broader introduction of wholesale and retail competition, the significant competitive

advantages that independent power producers currently enjoy over certain regulated utility companies would be eliminated or sharply curtailed, and the ability of regulated utility companies to compete more directly with independent power companies would be increased. To the extent competitive pressures increase and the pricing and sale of electricity assumes more characteristics of a commodity business, the economics of domestic independent power generation projects may come under increasing pressure, and the availability of long-term power purchase agreements, which can serve as

the basis for project financings, may decrease. Deregulation may not only continue to fuel the current trend toward consolidation among domestic utilities but may also encourage the disaggregation of vertically-integrated utilities into separate generation, transmission and distribution businesses. As a result, additional significant competitors could become active in the independent power industry. In addition, independent power producers may find it increasingly difficult to negotiate long-term power sales agreements with solvent utilities, which may affect the profitability and financial stability of independent power projects.

#### LACK OF PUBLIC MARKET FOR THE NOTES

The New Notes are being offered to the Holders of the Old Notes. The Old Notes were issued in June 1997 to a small number of institutional investors and are eligible for trading in the Private Offering, Resale, and Trading through Automated Linkages (PORTAL) Market, the National Association of Securities Dealers' screenbased, automated market for trading of securities eligible for resale under Rule 144A. The New Notes are new securities for which there currently is no market. Although the Initial Purchasers (as defined herein) have informed NRG that they currently intend to make a market in the New Notes, they are not obligated to do so and any such market making may be discontinued at any time without notice. NRG does not intend to list the New Notes or the Old Notes on any securities exchange or to seek approval for quotation through any automated quotation system. There can be no assurance as to the development or liquidity of any market for the New Notes or the Old Notes.

#### FORWARD-LOOKING STATEMENTS

Certain statements under the captions "Offering Memorandum Summary," "Risk Factors," "Management's Discussion and Analysis of Financial Condition and Results of Operations," "Business" and elsewhere in this Offering Memorandum constitute "forward-looking statements." Such forward-looking statements involve known and unknown risks, uncertainties and other factors that may cause the actual results, performance or achievements of NRG to be materially different from any future results, performance or achievements expressed or implied by such forward-looking statements. Such factors include, among others, the following: general economic and business conditions; industry capacity; demographic changes; competition; changes in technology; changes in political, social and economic conditions; changes in local laws and regulations; changes in electricity usage patterns and practices; changes in fuel pricing, including coal, oil and oil products and natural gas; and various other factors beyond NRG's control.

#### EXCHANGE OFFER PROCEDURES

Subject to the conditions set forth under "The Exchange Offer -- Conditions to the Exchange Offer," issuance of the New Notes in exchange for Old Notes pursuant to the Exchange Offer will be made only after a timely receipt by NRG of (i) a book-entry confirmation (as defined below) evidencing the tender of such Old Notes through ATOP or (ii) certificates representing such Old Notes, a properly completed and duly executed Letter of Transmittal, with any required signature guarantees, and all other required documents. See "The Exchange Offer -- Acceptance for Exchange and Issuance of Capital Securities" and "--Procedures for Tendering Original Capital Securities." Therefore, holders of the Old Notes desiring to tender such Old Notes in exchange for New Notes should allow sufficient time to ensure timely delivery. NRG is under no duty to give notification of defects or irregularities with respect to the tenders of Old Notes for exchange.

#### USE OF PROCEEDS

NRG will not receive any proceeds from the issuance of the New Notes offered pursuant to the Exchange Offer. In consideration for issuing the New Notes as contemplated in this Prospectus, NRG will receive in exchange Old Notes in like principal amount, the terms of which are identical in all

material respects to the New Notes except for certain transfer restrictions and registration rights. The Old Notes surrendered in exchange for New Notes will be retired and cancelled and cannot be reissued. Accordingly, issuance of the New Notes will not result in any increase in the indebtedness of NRG.

The net proceeds to NRG from the offering of the Old Notes, after deducting discounts and expenses, were approximately \$246.0 million. NRG used those net proceeds to repay outstanding debt under the Bridge Financing and for other general corporate purposes. The Bridge Financing was used for the acquisition of NRG's interest in the Loy Yang Project. See "Management's Discussion and Analysis of Financial Condition and Results of Operations -- Liquidity and Capital Resources" and "Certain Indebtedness."

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#### THE EXCHANGE OFFER

##### TERMS OF THE EXCHANGE OFFER; PERIOD FOR TENDERING OLD NOTES

The Old Notes were sold by NRG on June 17, 1997 (the "Closing Date") to Salomon Brothers Inc, ABN AMRO Chicago Corporation and Chase Securities Inc. (the "Initial Purchasers") pursuant to a Purchase Agreement, dated June 12, 1997, entered into by and among NRG and the Initial Purchasers (the "Purchase Agreement"). Upon the terms and subject to the conditions set forth in this Prospectus and in the accompanying Letter of Transmittal (which together constitute the Exchange Offer), NRG will accept for exchange Old Notes which are properly tendered on or prior to the Expiration Date and not withdrawn as permitted below. As used herein, the term "Expiration Date" means 5:00 p.m., New York City time on January 16, 1998; provided, however, that if NRG, in its sole discretion, has extended the period of time for which the Exchange Offer is open, the term "Expiration Date" means the latest time and date to which the Exchange Offer is extended.

As of the date of this Prospectus, \$250,000,000 aggregate principal amount of the Old Notes is outstanding. This Prospectus, together with the Letter of Transmittal, is first being sent on or about December 17, 1997, to all Holders of Old Notes known to NRG. NRG's obligation to accept Old Notes for exchange pursuant to the Exchange Offer is subject to certain conditions as set forth under "--Conditions to the Exchange Offer" below.

NRG expressly reserves the right, at any time or from time to time, to extend the period of time during which the Exchange Offer is open, and thereby delay acceptance for exchange of any Old Notes, by giving oral or written notice of such extension to the Holders thereof as described below. During any such extension, all Old Notes previously tendered will remain subject to the Exchange Offer and may be accepted for exchange by NRG. Any Old Notes not accepted for exchange for any reason will be returned without expense to the tendering Holder thereof as promptly as practicable after the expiration or termination of the Exchange Offer.

Old Notes tendered in the Exchange Offer must be in denominations of principal amount of \$1,000 or any integral multiple thereof.

NRG expressly reserves the right to amend or terminate the Exchange Offer, and not to accept for exchange any Old Notes not theretofore accepted for exchange, upon the occurrence of any of the conditions of the Exchange Offer specified below under "--Conditions to the Exchange Offer." NRG will give oral or written notice of any extension, amendment, non-acceptance or termination to the Holders of the Old Notes as promptly as practicable, such notice in the case of any extension to be issued by means of a press release or other public announcement no later than 9:00 a.m., New York City time, on the next business day after the previously scheduled Expiration Date.

## PROCEDURES FOR TENDERING

The tender to NRG of Old Notes by a Holder thereof as set forth below and the acceptance thereof by NRG will constitute a binding agreement between the tendering Holder and NRG upon the terms and subject to the conditions set forth in this Prospectus and in the accompanying Letter of Transmittal. Except as set forth below, a Holder who wishes to tender Old Notes for exchange pursuant to the Exchange Offer must transmit a properly completed and duly executed Letter of Transmittal, including all other documents required by such Letter of Transmittal, to Norwest Bank Minnesota, National Association (the "Exchange Agent") at one of the addresses set forth below under "--Exchange Agent" for receipt on or prior to the Expiration Date. In addition, either (i) certificates for such Old Notes must be received by the Exchange Agent along with the Letter of Transmittal or (ii) if using ATOP, a timely confirmation of a book-entry transfer (a "Book-Entry Confirmation") of such Old Notes, if such procedure is available, into the Exchange Agent's account at The Depository Trust Company (the "Book-Entry Transfer Facility") pursuant to the procedure for book-entry transfer described below, must be received by the Exchange Agent prior to the Expiration Date or (iii) the Holder must comply with the guaranteed delivery procedures described below.

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THE METHOD OF DELIVERY OF OLD NOTES AND THE LETTER OF TRANSMITTAL AND ALL OTHER REQUIRED DOCUMENTS TO THE EXCHANGE AGENT IS AT THE ELECTION AND RISK OF THE HOLDERS. IF SUCH DELIVERY IS BY MAIL, IT IS RECOMMENDED THAT REGISTERED MAIL, PROPERLY INSURED, WITH RETURN RECEIPT REQUESTED, BE USED. IN ALL CASES, SUFFICIENT TIME SHOULD BE ALLOWED TO ASSURE TIMELY DELIVERY. NO LETTER OF TRANSMITTAL OR OLD NOTES SHOULD BE SENT TO NRG.

Any beneficial owner whose Old Notes are registered in the name of a broker, dealer, commercial bank, trust company or other nominee and who wishes to tender should contact the registered Holder promptly and instruct such registered Holder to tender on such beneficial owner's behalf. If such beneficial owner wishes to tender on such owner's own behalf, such owner must, prior to completing and executing the Letter of Transmittal and delivering such owner's Old Notes, either make appropriate arrangements to register ownership of the Old Notes in such owner's name or obtain a properly completed bond power from the registered Holder. The transfer of registered ownership may take considerable time.

Signatures on a Letter of Transmittal or a notice of withdrawal described below (see "--Withdrawal of Tenders"), as the case may be, must be guaranteed as described below (see "--Guaranteed Delivery Procedures") unless the Old Notes tendered pursuant thereto are tendered (i) by a registered Holder who has not completed the box entitled "Special Issuance Instructions" or "Special Delivery Instructions" on the Letter of Transmittal or (ii) for the account of an Eligible Institution (as defined below). In the event that signatures of a Letter of Transmittal or a notice of withdrawal, as the case may be, are required to be guaranteed, such guarantee must be made by a financial institution (including most banks, savings and loan associations and brokerage houses) that is a participant in the Securities Transfer Agents Medallion Program, the New York Stock Exchange Medallion Signature Program or the Stock Exchange Medallion Program (collectively, "Eligible Institutions"). If Old Notes are registered in the name of a person other than a signer of the Letter of Transmittal, the Old Notes surrendered for exchange must be endorsed by, or be accompanied by a written instrument or instruments of transfer or exchange, in satisfactory form as determined by NRG, duly executed by the registered Holder with the signature thereon guaranteed by an Eligible Institution.

All questions as to the validity, form, eligibility (including time of receipt) and acceptance of tendered Old Notes will be determined by NRG in its sole discretion, which determination will be final and binding. NRG reserves the absolute right to reject any and all tenders of any particular Old Notes not properly tendered or to not accept any particular Old Note if acceptance would, in the judgment of NRG or its counsel, be unlawful. NRG also reserves the absolute right to waive any defects, irregularities or

conditions of the Exchange Offer as to any particular Old Notes either before or after the Expiration Date (including the right to waive the ineligibility of any Holder who seeks to tender Old Notes in the Exchange Offer). The interpretation of the terms and conditions of the Exchange Offer as to any particular Old Notes either before or after the Expiration Date (including the Letter of Transmittal and the instructions thereto) by NRG will be final and binding on all parties. Unless waived, any defects or irregularities in connection with tenders of Old Notes for exchange must be cured within such reasonable period of time as NRG may determine. None of NRG, the Exchange Agent or any other person will be under any duty to give notification of any defect or irregularity with respect to any tender of Old Notes for exchange, nor will any of them incur any liability for failure to give such notification.

If the Letter of Transmittal is signed by a person or persons other than the registered Holder or Holders of Old Notes, such Old Notes must be endorsed or accompanied by appropriate powers of attorney, in either case signed exactly as the name or names of the registered Holder or Holders that appear on the Old Notes.

If the Letter of Transmittal or any Old Note or powers of attorney are signed by trustees, executors, administrators, guardians, attorneys-in-fact, officers of corporations or others acting in a fiduciary or representative capacity, such persons should so indicate when signing, and, unless waived by NRG, proper evidence satisfactory to NRG of their authority to so act must be submitted with the Letter of Transmittal.

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By tendering, each Holder, other than a broker-dealer, must acknowledge that it is not engaged in, and does not intend to engage in, a distribution of New Notes. If any Holder is an affiliate of NRG, is engaged in or intends to engage in or has any arrangement with any person to participate in the distribution of the New Notes to be acquired pursuant to the Exchange Offer, such Holder (i) could not rely on the applicable interpretations of the staff of the Commission and (ii) must comply with the registration and prospectus delivery requirements of the Securities Act in connection with any resale transaction, including the delivery of a prospectus which contains the information with respect to any selling holder required by the Securities Act. Each broker-dealer that receives New Notes for its own account in exchange for Old Notes, where such Old Notes were acquired by such broker-dealer as a result of market-making activities or other trading activities, must represent to NRG that it will deliver a prospectus in connection with any resale of such New Notes and that it acquired such Old Notes as a result of market-making activities or other trading activities. See "Plan of Distribution." The Letter of Transmittal states that by so representing and by delivering a prospectus, a broker-dealer will not be deemed to admit that it is an "underwriter" within the meaning of the Securities Act.

#### ACCEPTANCE OF OLD NOTES FOR EXCHANGE; DELIVERY OF NEW NOTES

Upon satisfaction or waiver of all of the conditions to the Exchange Offer, NRG will accept, promptly after the Expiration Date, all Old Notes properly tendered and will issue the New Notes promptly after acceptance of the Old Notes. See "--Conditions to the Exchange Offer" below. For purposes of the Exchange Offer, NRG will be deemed to have accepted properly tendered Old Notes for exchange, when, as and if NRG has given oral or written notice thereof to the Exchange Agent.

For each Old Note accepted for exchange, the Holder of such Old Note will receive a new Note having a principal amount equal to that of the surrendered Old Note. Accordingly, registered Holders of New Notes on the relevant record date for the first interest payment date following the consummation of the Exchange Offer will receive interest accruing from the most recent date to which interest has been paid or, if no interest has been paid, from June 17, 1997. Old Notes accepted for exchange will cease to accrue interest from and after the date of consummation of the Exchange Offer. Holders of Old Notes

whose Old Notes are accepted for exchange will not receive any payment in respect of accrued interest on such Old Notes otherwise payable on any interest payment date the record date for which occurs on or after consummation of the Exchange Offer. In the event of a Registration Default under and as defined in the Registration Rights Agreement, NRG will pay Special Interest to each Holder of Transfer Restricted Securities (as defined herein). See "Description of Notes -- Special Interest."

In all cases, issuance of New Notes for Old Notes that are accepted for exchange pursuant to the Exchange Offer will be made only after timely receipt by the Exchange Agent of certificates for such Old Notes or, if using ATOP, a timely Book-Entry Confirmation of such Old Notes into the Exchange Agent's account at the Book-Entry Transfer Facility, a properly completed and duly executed Letter of Transmittal and all other required documents. If any tendered Old Notes are not accepted for any reason set forth in the terms and conditions of the Exchange Offer or if Old Notes are submitted for a greater principal amount than the Holder desires to exchange, such unaccepted or non-exchanged Old Notes will be returned without expense to the tendering Holder thereof (or, in the case of Old Notes tendered by book-entry transfer into the Exchange Agent's account at the Book-Entry Transfer Facility pursuant to the book-entry procedures described below, such non-exchanged Old Notes will be credited to an account maintained with such Book-Entry Transfer Facility) as promptly as practicable after the expiration or termination of the Exchange Offer.

#### BOOK-ENTRY TRANSFER

The Exchange Agent will make a request to establish an account with respect to the Old Notes at the Book-Entry Transfer Facility for purposes of the Exchange Offer within two business days after the date of this Prospectus, and any tendering financial institution that is a participant in the Book-Entry Transfer Facility's systems must make book-entry delivery of Old Notes by causing the Book-Entry Transfer Facility to transfer such Old Notes into the Exchange Agent's account at the Book-Entry Transfer Facility in accordance with the Book-Entry Transfer Facility's ATOP procedures for transfer.

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Such holder of Old Notes using ATOP should transmit its acceptance to the Book-Entry Transfer Facility on or prior to the Expiration Date (or comply with the guaranteed delivery procedures set forth below). The Book-Entry Transfer Facility will verify such acceptance, execute a book-entry transfer of the tendered Old Notes into the Exchange Agent's account at the Book-Entry Transfer Facility and then send to the Exchange Agent confirmation of such book-entry transfer, including an Agent's Message confirming that the Book-Entry Transfer Facility has received an express acknowledgement from such holder that such holder has received and agrees to be bound by this Letter of Transmittal and that NRG may enforce this Letter of Transmittal against such Holder (a "Book-Entry Confirmation").

#### GUARANTEED DELIVERY PROCEDURES

If a registered Holder of the Old Notes desires to tender such Old Notes and the Old Notes are not immediately available, or time will not permit such Holder's Old Notes or other required documents to reach the Exchange Agent before the Expiration Date, or the procedure for book-entry transfer cannot be completed on a timely basis, a tender may be effected if (i) the tender is made through an Eligible Institution, (ii) prior to the Expiration Date, the Exchange Agent receives from such Eligible Institution a properly completed and duly executed Letter of Transmittal (or a facsimile thereof) and Notice of Guaranteed Delivery, substantially in the form provided by NRG (by telegram, telex, facsimile transmission, mail or hand delivery), setting forth the name and address of the Holder of Old Notes and the principal amount of Old Notes tendered, stating that the tender is being made thereby and guaranteeing that, within three New York Stock Exchange, Inc. ("NYSE") trading days after the date of execution of the Notice of Guaranteed Delivery, the certificates for all physically tendered Old Notes, in proper



form for transfer, or a Book-Entry Confirmation, as the case may be, and any other documents required by the Letter of Transmittal will be deposited by the Eligible Institution with the Exchange Agent, and (iii) the certificates for all physically tendered Old Notes, in proper form for transfer, or a Book-Entry Confirmation, as the case may be, and all other documents required by the Letter of Transmittal, are received by the Exchange Agent within three NYSE trading days after the date of execution of the Notice of Guaranteed Delivery.

#### WITHDRAWAL OF TENDERS

Tenders of Old Notes may be withdrawn at any time prior to the Expiration Date.

For a withdrawal to be effective, a written notice of withdrawal must be received by the Exchange Agent at one of its addresses set forth below under "--Exchange Agent" prior to the Expiration Date. Any such notice of withdrawal must (i) specify the name of the person having deposited the Old Notes to be withdrawn (the "Depositor"), (ii) identify the Old Notes to be withdrawn (including the principal amount of such Old Notes), and (iii) (where certificates for Old Notes have been transmitted) specify the name in which such Old Notes are registered, if different from that of the withdrawing Holder. If certificates for Old Notes have been delivered or otherwise identified to the Exchange Agent, then, prior to the release of such certificates the withdrawing Holder must also submit the serial numbers of the particular certificates to be withdrawn and a signed notice of withdrawal with signatures guaranteed by an Eligible Institution unless such Holder is an Eligible Institution. If Old Notes have been tendered pursuant to the procedure for book-entry transfer described above, any notice of withdrawal must specify the name and number of the account at the Book-Entry Transfer Facility to be credited with the withdrawn Old Notes and otherwise comply with the procedures of such facility. All questions as to the validity, form and eligibility (including time of receipt) of such notices will be determined by NRG, whose determination shall be final and binding on all parties. Any Old Note so withdrawn will be deemed not to have been validly tendered for exchange for purposes of the Exchange Offer. Any Old Note which has been tendered for exchange but which is not exchanged for any reason will be returned to the Holder thereof without cost to such Holder (or, in the case of Old Notes tendered by book-entry transfer procedures described above, such Old Notes will be credited to an account maintained with such Book-Entry Transfer Facility for the Old Notes) as soon as practicable after withdrawal, rejection of tender or termination of the Exchange Offer. Properly withdrawn Old Notes may be retendered by following one of the procedures described under "--Procedures for Tendering Old Notes" above at any time on or prior to the Expiration Date.

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#### CONDITIONS TO THE EXCHANGE OFFER

Notwithstanding any other provision of the Exchange Offer, NRG will not be required to accept for exchange, or issue New Notes in exchange for, any Old Notes and may terminate or amend the Exchange Offer if at any time before the acceptance of such Old Notes for exchange or the exchange of the New Notes for such Old Notes, any of the following events occur:

(a) there shall be threatened, instituted or pending any action or proceeding before, or any injunction, order or decree shall have been issued by, any court or governmental agency or other governmental regulatory or administrative agency or commission, (i) seeking to restrain or prohibit the making or consummation of the Exchange Offer or any other transaction contemplated by the Exchange Offer, or assessing or seeking any damages as a result thereof, or (ii) resulting in a material delay in the ability of NRG to accept for exchange or exchange some or all of the Old Notes pursuant to the Exchange Offer, or any statute, rule, regulation, order or injunction shall be sought, proposed, introduced, enacted, promulgated or deemed applicable to the Exchange Offer or any of the transactions contemplated by the Exchange Offer by any government or

governmental authority, domestic or foreign, or any action shall have been taken, proposed or threatened, by any government or governmental authority, agency or court, domestic or foreign, that in the reasonable judgment of NRG might directly or indirectly result in any of the consequences referred to in clauses (i) or (ii) above or, in the reasonable judgment of NRG, might result in the Holders of New Notes having obligations with respect to resales and transfers of New Notes which are greater than those described in the interpretation of the Commission referred to on the cover page of this Prospectus, or would otherwise make it inadvisable to proceed with the Exchange Offer; or

(b) there shall have occurred (i) any general suspension of or general limitation on prices for, or trading in, securities on any national securities exchange or in the over-the-counter market, (ii) any limitation by any governmental agency or authority which may adversely affect the ability of NRG to complete the transactions contemplated by the Exchange Offer, (iii) a declaration of a banking moratorium or any suspension of payments in respect of banks in the United States or any limitation by any governmental agency or authority which adversely affects the extension of credit or (iv) a commencement of a war, armed hostilities or other similar international calamity directly or indirectly involving the United States, or, in the case of any of the foregoing existing at the time of the commencement of the Exchange Offer, a material acceleration or worsening thereof; or

(c) any change (or any development involving a prospective change) shall have occurred or be threatened in the business, properties, assets, liabilities, financial condition, operations, results of operations or prospects of NRG and its subsidiaries taken as a whole that, in the reasonable judgment of NRG, is or may be adverse to NRG, or NRG shall have become aware of facts that, in the reasonable judgment of NRG, have or may have adverse significance with respect to the value of the Old Notes or the New Notes;

which, in the reasonable judgment of NRG in any case, and regardless of the circumstances (including any action by NRG) giving rise to any such condition, makes it inadvisable to proceed with the Exchange Offer and/or with such acceptance for exchange or with such exchange.

The foregoing conditions are for the sole benefit of NRG and may be asserted by NRG regardless of the circumstances giving rise to any such condition or may be waived by NRG in whole or in part at any time and from time to time in its sole discretion. The failure by NRG at any time to exercise any of the foregoing rights shall not be deemed a waiver of any such right and each such right shall be deemed an ongoing right which may be asserted at any time and from time to time.

In addition, NRG will not accept for exchange any Old Note tendered, and no New Notes will be issued in exchange for any such Old Note, if at such time any stop order shall be threatened or in effect with respect to the Registration Statement of which this Prospectus constitutes a part or the qualification of the Indenture under the Trust Indenture Act of 1939.

#### EXCHANGE AGENT

Norwest Bank Minnesota, National Association has been appointed as the Exchange Agent of the Exchange Offer. All executed Letters of Transmittal should be directed to the Exchange Agent at one of the addresses set forth below. Questions and requests for assistance, requests for additional copies of this Prospectus or of the Letter of Transmittal and requests for Notice of Guaranteed Delivery should be directed to the Exchange Agent addressed as follows:

By Registered or Certified Mail:  
Norwest Bank Minnesota, National Association  
P.O. Box 1517  
Minneapolis, Minnesota 55480-1517  
Attention: Corporate Trust Operations

By Hand Delivery:  
Norwest Bank Minnesota National Association  
Northstar East 12th Floor  
608 2nd Avenue  
Minneapolis, Minnesota 55479-0113  
Attention: Corporate Trust Operations

By Overnight Delivery:  
Norwest Bank Minnesota National Association  
Norwest Center  
6th and Marquette Avenue  
Minneapolis, Minnesota 55479-0069  
Attention: Corporate Trust Operations

By Facsimile:  
(612) 667-4927  
Confirm by Telephone:  
(612) 667-9764

DELIVERY TO AN ADDRESS OTHER THAN AS SET FORTH ABOVE OR TRANSMISSION OF INSTRUCTIONS VIA FACSIMILE OTHER THAN AS SET FORTH ABOVE DOES NOT CONSTITUTE A VALID DELIVERY.

#### FEES AND EXPENSES

NRG will not make any payment to brokers, dealers or others soliciting acceptances of the Exchange Offer.

The estimated cash expenses to be incurred in connection with the Exchange Offer will be paid by NRG and are estimated in the aggregate to be \$400,000.

#### TRANSFER TAXES

Holdes who tender their Old Notes for exchange will not be obligated to pay any transfer tax in connection therewith, except that Holdes who instruct NRG to register New Notes in the name of, or request that Old Notes not tendered or not accepted in the Exchange Offer be returned to, a person other than the registered tendering Holder will be responsible for the payment of any applicable transfer tax thereon.

#### CONSEQUENCES OF FAILURE TO EXCHANGE OLD NOTES

Holdes of Old Notes who do not exchange their Old Notes for New Notes pursuant to the Exchange Offer will continue to be subject to the restrictions on transfer of such Old Notes as set forth in the legend thereon as a consequence of the issuance of the Old Notes pursuant to exemptions from, or in transactions not subject to, the registration requirements of the Securities Act and applicable state securities laws. In general, the Old Notes may not be offered or sold, unless registered under the Securities Act, except pursuant to an exemption from, or in a transaction not subject to, the registration requirements of the Securities Act and applicable state securities laws. NRG does not currently anticipate that it will register Old Notes under the Securities Act. See "Description of Notes -- Registration Rights." Based on interpretations by the staff of the Commission issued to third parties,

New Notes issued pursuant to the Exchange Offer in exchange for Old Notes may be offered for resale, resold or otherwise transferred by Holdes thereof (other than any Holder which is an "affiliate" of NRG within the meaning of Rule 405 under the Securities Act) without compliance with the registration and prospectus delivery provisions of the Securities Act, provided that such New Notes are acquired in the ordinary course of such Holdes' business and such Holdes have no arrangement with any person to participate in the distribution of such New Notes. Each Holder, other than a broker-dealer, must acknowledge that it is not engaged in, and does not intend to engage in, a distribution of New Notes. If any Holder is an affiliate of NRG, is engaged in or intends to engage in or has any arrangement or understanding with respect to the distribution of the New Notes to be acquired pursuant to the Exchange Offer, such Holder (i) could not rely on the applicable interpretations of the staff of the Commission and (ii) must comply with the registration and prospectus delivery requirements of the Securities Act in connection with any resale transaction. Each broker-dealer that receives New Notes for its own account in exchange for Old Notes must acknowledge that

such Old Notes were acquired by such broker-dealer as a result of market-making activities or other trading activities and that it will deliver a prospectus in connection with any resale of such New Notes. See "Plan of Distribution." In addition, to comply with the securities laws of certain jurisdictions, if applicable, the New Notes may not be offered or sold unless they have been registered or qualified for sale in such jurisdiction or an exemption from registration or qualification is available and is complied with. NRG does not currently intend to register or qualify the sale of the New Notes in any such jurisdictions.

CAPITALIZATION

The following table sets forth the unaudited consolidated capitalization of NRG as of September 30, 1997.

	SEPTEMBER 30, 1997
	(DOLLARS IN THOUSANDS) (UNAUDITED)
Long-term debt:	
Existing funded debt(1).....	\$142,738
1996 Senior Notes.....	125,000
1997 Senior Notes .....	250,000
	-----
Total long-term debt.....	517,738
	-----
Stockholder's equity:	
Common stock; \$1 par value; 1,000 shares authorized; 1,000 shares issued and outstanding .....	1
Additional paid-in capital(2) .....	431,374
Retained earnings .....	80,715
Currency translation adjustments .....	(30,811)
	-----
Total stockholder's equity .....	481,279
	-----
Total capitalization .....	\$999,017
	=====

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- (1) Includes \$43.3 million of current portion of long-term debt and \$77.7 million of debt relating to MEC and NRG San Diego, including current maturities, which is non-recourse to NRG.
  - (2) Includes the \$60.9 million contribution by NSP in connection with the acquisition of Loy Yang A.

SELECTED CONSOLIDATED FINANCIAL DATA

The selected consolidated financial data set forth below as of December 31, 1993, 1994, 1995 and 1996 and for the years then ended, have been derived from the audited consolidated financial statements of NRG. Certain financial information for the years ended December 31, 1993 and 1994 have been reclassified to conform to the financial presentation for the year ended

December 31, 1995. The selected consolidated financial data set forth below as of September 30, 1996 and 1997, and for the nine-month periods then ended, and as of December 31, 1992 and for the year then ended, have been derived from the unaudited consolidated financial statements of NRG. Interim results and the results for 1992, in the opinion of management of NRG, include all adjustments (consisting solely of normal recurring adjustments) necessary to present fairly the financial information for such periods; however, such interim results are not necessarily indicative of the results that may be expected for any other interim period or for a full year. The following data should be read in conjunction with the Consolidated Financial Statements and "Management's Discussion and Analysis of Financial Condition and Results of Operations" included elsewhere in this Prospectus.

CONSOLIDATED STATEMENTS OF INCOME DATA:

	YEAR ENDED DECEMBER 31,				
	1992	1993	1994	1995	1996
	(IN THOUSANDS)				
OPERATING REVENUES					
Revenues from wholly-owned operations(1) .	\$39,647	\$48,529	\$63,970	\$64,180	\$ 71,649
Equity in operating earnings of unconsolidated affiliates(2) (3).....	1,321	2,695	27,155	23,639	32,815
Total operating revenues .....	40,968	51,224	91,125	87,819	104,464
OPERATING COSTS AND EXPENSES					
Cost of operations--wholly-owned operations .....	22,870	27,122	34,861	32,535	36,562
Depreciation and amortization .....	5,060	6,475	8,675	8,283	8,378
General, administrative, and development	14,930	11,448	19,993	34,647	39,248
Total operating costs and expenses .....	42,860	45,045	63,529	75,465	84,188
OPERATING INCOME (LOSS) .....	(1,892)	6,179	27,596	12,354	20,276
OTHER INCOME (EXPENSE)					
Equity in gain from project termination settlements(4) .....	--	--	9,685	29,850	--
Other income (expense), net .....	(1,753)	1,028	1,411	4,896	9,477
Interest expense .....	(1,662)	(2,679)	(6,682)	(7,089)	(15,430)
Total other income (expense) .....	(3,415)	(1,651)	4,414	27,657	(5,953)
INCOME (LOSS) BEFORE INCOME TAXES .....	(5,307)	4,528	32,010	40,011	14,323
INCOME (BENEFIT) TAXES(5) .....	(2,187)	1,905	2,472	8,810	(5,655)
NET INCOME (LOSS).....	\$ (3,120)	\$ 2,623	\$29,538	\$31,201	\$ 19,978

(RESTUBBED TABLE CONTINUED FROM ABOVE)

	NINE MONTHS ENDED SEPTEMBER 30,	
	1996	1997
OPERATING REVENUES		
Revenues from wholly-owned operations(1) .	\$ 52,479	\$ 65,081
Equity in operating earnings of unconsolidated affiliates(2) (3).....	19,375	17,759
Total operating revenues .....	71,854	82,840
OPERATING COSTS AND EXPENSES		
Cost of operations--wholly-owned operations .....	26,858	32,863
Depreciation and amortization .....	6,300	7,096

General, administrative, and development	26,599	28,402
	-----	-----
Total operating costs and expenses .....	59,757	68,361
	-----	-----
OPERATING INCOME (LOSS) .....	12,097	14,479
OTHER INCOME (EXPENSE)		
Equity in gain from project termination settlements(4) .....	--	--
Other income (expense), net .....	6,117	8,610
Interest expense .....	(11,303)	(19,815)
	-----	-----
Total other income (expense) .....	(5,186)	(11,205)
	-----	-----
INCOME (LOSS) BEFORE INCOME TAXES .....	6,911	3,274
INCOME (BENEFIT) TAXES (5) .....	(4,358)	(11,140)
	-----	-----
NET INCOME (LOSS) .....	\$ 11,269	\$ 14,414
	=====	=====

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- (1) All of these revenues are from 100% owned operations. In accordance with its strategy described herein, when NRG does not own 100% of a project, it owns 50% or less in all cases except COBEE.
- (2) NRG accounts for its investments in projects where ownership is between 20% and 50%, and where there is no effective and legal control, using the equity method of accounting; COBEE has been accounted for using the equity method of accounting even though NRG owned more than a 50% interest in the project. However, NRG did not have control over the project due to the fact that NRG did not have the power to elect a majority of the members of the board of directors of COBEE. NRG was only entitled to appoint four out of the nine directors. Vattenfall, the other majority holder of COBEE, appointed three of the other directors, and the remaining two directors were selected jointly by NRG and Vattenfall. In addition, on October 30, 1997, NRG sold to Vattenfall part of its interest in COBEE which resulted in NRG's ownership interest declining from 57.96% to 48.3%. Also as of such date, NRG became entitled to appoint only three of the nine directors. Vattenfall appoints three directors and the remaining three are appointed jointly by NRG and Vattenfall. Equity in earnings of unconsolidated project affiliates includes NRG's proportionate share of all net income or losses attributable to project investments accounted for using the equity method.

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- (3) Includes pretax charges of \$5.0 million, \$5.0 million and \$1.5 million in the years 1994, 1995 and 1996, respectively, to write-down the carrying value of certain energy projects.
- (4) In 1994, NRG and its partner in the Michigan Cogeneration Partners Limited Partnership agreed to terminate a power sales contract with Consumers Power Company. The contract related to a 65 MW cogeneration facility being developed in Michigan. Due to the agreement to terminate the contract, NRG recorded a one-time pre-tax gain of \$9.7 million in 1994. Equity in gain from project termination settlements in 1995 included a one-time pre-tax gain of \$29.9 million related to the settlement and termination of the San Joaquin Valley power purchase agreements with PG&E. See "Business -- Independent Power Production and Cogeneration -- Domestic Projects -- San Joaquin."
- (5) NRG is included in the consolidated federal income tax and state franchise tax returns of NSP. NRG calculates its tax position on a separate company basis under a tax sharing agreement with NSP and receives payment from NSP for tax benefits and pays NSP for tax liabilities.

CONSOLIDATED BALANCE SHEET DATA:

	AS OF DECEMBER 31,				
	1992	1993	1994	1995	1996
	(IN THOUSANDS)				
Net property, plant and equipment .	\$46,694	\$108,934	\$107,634	\$111,919	\$129,649
Net equity investments in projects	16,400	20,046	164,863	221,129	365,749
Total assets.....	81,091	232,888	376,570	454,589	680,809
Long-term debt, including current maturities .....	10,499	93,451 (1)	93,339 (1)	90,034 (1)	212,141 (1)
Stockholder's equity .....	40,267	97,722	234,722	319,764	421,914

(RESTUBBED TABLE CONTINUED FROM ABOVE)

	AS OF SEPTEMBER 30,	
	1996	1997
Net property, plant and equipment .	\$118,109	\$ 164,915
Net equity investments in projects	266,504	635,047
Total assets.....	586,461	1,066,816
Long-term debt, including current maturities .....	213,298 (1)	517,738 (1)
Stockholder's equity .....	332,012	481,279

(1) Includes debt relating to MEC and NRG San Diego, including current maturities, which is non-recourse to NRG. As of September 30, 1997 this debt was \$77.7 million.

OTHER DATA (UNAUDITED):

	AS OF AND FOR THE YEAR ENDED DECEMBER 31,				
	1992	1993	1994	1995	1996
	(DOLLARS IN THOUSANDS)				
NRG's net power generating capacity (MW).....	33	33	992	999	1,326
NRG's net thermal energy generating capacity:					
mmBtus per hour .....	695	1,865	1,961	2,318	2,654
Mwt .....	204	547	575	679	778
Consolidated EBITDA (1) .....	\$1,415	\$13,682	\$47,367	\$55,383	\$38,131
Consolidated interest expense .....	\$1,662	\$ 2,679	\$ 6,682	\$ 7,089	\$15,430
Consolidated interest expense coverage ratio (2) .....	0.85x	5.11x	7.09x	7.81x	2.47x
Consolidated debt service (3) .....	\$2,562	\$ 4,272	\$ 9,169	\$10,394	\$18,323
Consolidated debt service coverage ratio (4) .....	0.55x	3.20x	5.17x	5.33x	2.08x
Consolidated ratio of earnings to fixed charges (5).....	(6)	2.32x	2.98x	1.56x (7)	1.75x (8)

(RESTUBBED TABLE CONTINUED FROM ABOVE)

AS OF AND FOR THE  
NINE MONTHS ENDED  
SEPTEMBER 30,

	1996	1997
NRG's net power generating capacity (MW).....	1,209	2,351
NRG's net thermal energy generating capacity:		
mmBtus per hour .....	1,040	2,695
Mwt .....	778	789
Consolidated EBITDA (1) .....	\$24,514	\$30,185
Consolidated interest expense .....	\$11,303	\$19,815
Consolidated interest expense coverage ratio (2) .....	2.17x	1.52x
Consolidated debt service (3) .....	\$13,039	\$21,730
Consolidated debt service coverage ratio (4) .....	1.88x	1.39x
Consolidated ratio of earnings to fixed charges (5).....	2.19x(8)	1.03x

(1) EBITDA equals the sum of income (loss) before income taxes, interest expense (net of capitalized interest) and depreciation and amortization expense. EBITDA is a measure of financial performance not defined under generally accepted accounting principles and should not be considered in isolation or as a substitute for net income, cash flows from operations or other income or cash flow data prepared in accordance with generally accepted accounting principles or as a measure of a company's profitability or liquidity. In addition, EBITDA may not be comparable to similarly titled measures presented by other companies and could be misleading unless all companies and analysts calculate them in the same fashion. Management believes that some investors consider EBITDA an indicator of a company's ability to service debt. An increase in EBITDA level implies an improved ability to service debt, but does not reflect the level of debt service charges to be covered, which will change with debt levels outstanding and interest rate charges. See Statements of Cash Flows in the Consolidated Financial Statements included elsewhere in this Prospectus.

(2) The interest expense coverage ratio equals EBITDA divided by interest expense.

(3) Debt service consists of the previous twelve months of interest expense and principal payments on long-term debt.

(4) The debt service coverage ratio equals EBITDA divided by debt service.

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(5) The ratio of earnings to fixed charges is calculated by dividing earnings by fixed charges. For this purpose "earnings" means income (loss) before income taxes less undistributed equity in operating earnings of unconsolidated affiliates less equity in gain from project termination settlements plus cash distributions from project termination settlements plus fixed charges. "Fixed charges" means interest expense plus interest capitalized plus amortization of debt issuance costs plus a reasonable approximation of the interest factor of rental expense.

(6) Due primarily to the loss incurred in 1992, NRG was unable to fully cover fixed charges. Earnings did not cover fixed charges by \$5,940.

(7) The 1995 ratio of earnings to fixed charges calculation includes the effect of an equity gain and cash distribution from a project termination settlement. If the project termination had not occurred, NRG would have been unable to fully cover fixed charges and earnings



would not have covered fixed charges by \$9,913.

- (8) The 1996 ratio of earnings to fixed charges calculations include the effect of a cash distribution from a 1995 project termination settlement. If the project termination had not occurred, NRG would have been unable to fully cover fixed charges and earnings would not have covered fixed charges by \$1,497 for the nine months ended September 30, 1996, and by \$3,504 for the year ended December 31, 1996.

SELECTED PRO FORMA CONDENSED FINANCIAL DATA

The unaudited pro forma condensed financial data set forth below give effect to (i) the acquisition by NRG of a 25.37% equity interest in Loy Yang A and the financing thereof and (ii) the Offering. The pro forma statement of income data for the year ended December 31, 1996 and the nine months ended September 30, 1997 gives effect to such transactions as if they had occurred on January 1, 1996. As the Loy Yang acquisition and the Offering were consummated prior to September 30, 1997, no pro forma balance sheet data is provided. The pro forma condensed financial data do not purport to be indicative of the combined financial position or results of operations of future periods or indicative of the results that would have occurred had the transactions referred to above been consummated on the dates indicated. The following data should be read in conjunction with, and are qualified in their entirety by, the Consolidated Financial Statements and "Management's Discussion and Analysis of Financial Condition and Results of Operations" included elsewhere in this Prospectus.

FOR THE YEAR ENDED DECEMBER 31, 1996

	HISTORICAL	ADJUSTMENTS (1)	PRO FORMA
	(IN THOUSANDS)		
STATEMENT OF INCOME DATA:			
Revenues from wholly-owned operations .....	\$ 71,649	--	\$ 71,649
Equity in earnings (loss) of unconsolidated affiliates .....	32,815	\$ (18,121) (2)	14,694
Operating costs and expenses .....	(84,188)	--	(84,188)
Other income (expense) .....	9,477	26,264 (3)	35,741
Interest expense .....	(15,430)	(18,750) (4)	(34,180)
Income taxes .....	5,655	4,373 (5)	10,028
Net Income.....	\$ 19,978	\$ (6,234)	\$ 13,744

- (1) Adjustments were derived from Loy Yang's audited financial statements for the fiscal years ended June 30, 1996 and June 30, 1997 to conform with NRG's December 31, 1996 year-end.

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- (2) After-tax net income as shown in the financial

statements:	120,054
Change to Depreciation/Amortization Expense.....	(316)
Change to Finance Charges.....	(164,394)
Change to Taxes.....	120,151
Other.....	(166,682)
	-----
AFTER-TAX NET INCOME (LOSS) .....	(91,187)
	-----
NRG'S 25.37%.....	(23,134)
1996 Average Exchange Rate.....	0.7833
	-----
NRG US\$ NET INCOME (LOSS) .....	(18,121)
	=====

The change in depreciation is due to the increased value in assets offset by the extension of life on assets from 35 years to 50 years. Amortization expense is from the capitalized project debt fees paid to acquire the new project debt.

The change in finance charges is due to the repayment of debt to the state of Victoria (sale proceeds) netted against the new project debt. The interest rates are variable but were immediately swapped into fixed rate debt for a period of five years. The weighted average interest rate during the first year is 7.91%.

The change to tax expense is due to reversing Loy Yang's original tax expense in 1996 and booking a deferred tax benefit based on Loy Yang's new book loss. Approximately the statutory tax rate on the other adjustments.

"Other" is composed of interest expense recorded on the note payable to the shareholders and the operating & maintenance fee expense paid to the operator shareholders.

- (3) Includes interest income and operating and maintenance fees derived from the Loy Yang project.
- (4) Represents accrued interest on \$250 million principal amount of the Old Notes for twelve months at a rate of 7.5% per annum.
- (5) Net tax benefit derived from interest expense on the Old Notes.

AS OF AND FOR THE NINE MONTHS ENDED SEPTEMBER 30, 1997

	HISTORICAL	ADJUSTMENTS	PRO FORMA
	-----	-----	-----
	(IN THOUSANDS)		
STATEMENT OF INCOME DATA:			
Revenues from wholly-owned operations .....	\$ 65,081	\$ --	\$ 65,081
Equity in earnings of unconsolidated affiliates	17,759	(7,945) (1)	9,814
Operating costs and expenses .....	(68,361)	--	(68,361)
Other income and (expense) .....	8,610	8,525 (3)	17,135
Interest expense .....	(19,815)	(6,883) (4)	(26,698)
Income taxes .....	11,140	1,605 (5)	12,745
	-----	-----	-----
Net Income.....	\$ 14,414	\$ (4,698)	\$ 9,716
	=====	=====	=====

- (1) Adjustments were derived from Loy Yang's audited financial statements for the fiscal year ended June 30, 1997.
- (2) Represents estimated equity earnings from Loy Yang A through May 12, 1997, based upon historical data (January 1, 1997 -- May 12, 1997) adjusted for differences due to acquisition accounting primarily

depreciation charges, finance charges and adjustments to income tax expense. Equity earnings of Loy Yang A from May 13 until September 30 were \$1,393. This amount is included in the Historical column of Equity in earnings of unconsolidated affiliates.

- (3) Includes interest income and operating and maintenance fees derived from the Loy Yang project.
- (4) Represents interest expense on \$250 million principal amount of the Old Notes until May 12 at a rate of 7.5% per annum. Interest of \$7,140 on the Old Notes from May 13 until September 30 is in the Historical column.
- (5) Net tax benefit derived from interest expense on the Old Notes.

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#### MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

The following Management's Discussion and Analysis of Financial Condition and Results of Operations should be read in conjunction with NRG's consolidated financial statements appearing elsewhere in this Offering Memorandum. In addition, as a result of the recent Loy Yang acquisition, NRG's future results could differ significantly from NRG's historical results. See "Selected Pro Forma Condensed Financial Data" and "Business."

#### GENERAL

NRG has developed a complex organizational structure involving foreign holding companies, corporations, partnerships and joint ventures through which NRG holds interests in its international projects. These entities are organized to maximize available cash flows (by reducing and deferring foreign and U.S. taxes) and to reduce current and deferred taxes. As part of NRG's global tax strategy, NRG intends to maintain offshore, for permanent reinvestment in other projects, its dividends and distributions from foreign investments, except to the limited extent required to make payments of interest or principal on loans from NRG. Any repatriation of dividends from foreign investments may result in adverse U.S. income tax consequences.

NRG's policy is to pay for offshore development expenses from available offshore cash. NRG generally funds offshore investments as equity, which can come from a variety of sources, including capital infusions from NSP, borrowings by NRG and internal cash generation. In certain circumstances, a portion of project equity funding is treated as a loan by NRG to the project subsidiary or affiliate on market-based interest rate and repayment terms.

In light of NRG's global tax policy as described above, cash flows from ongoing domestic operations and repayments of principal and interest by foreign project subsidiaries and project affiliates to NRG are expected to be the primary source of cash to service NRG's corporate obligations, including with respect to the Notes. To date, NRG's consolidated operating revenues from domestic operations have been derived primarily from the production and transmission of thermal energy (steam and chilled water) and from the operation of resource recovery facilities that process MSW into RDF. Other operating revenues arose from fees earned in providing management and engineering services to a number of operating facilities. NRG's operating expenses also are largely attributable to domestic activities except for general, administrative and development expenses, which in 1994, 1995 and 1996 were incurred primarily in pursuit of international investment and acquisition activities.

NRG accounts for investments in projects where ownership is between 20% and 50%, and where there is no effective and legal control, using the equity method of accounting. Under the equity method, NRG's investment in an entity is recorded on the balance sheet at cost and is adjusted to recognize NRG's proportional share of all earnings or losses of the entity. Distributions received reduce the carrying amount of NRG's investment in the entity. For income statement purposes, NRG records as equity in earnings its proportional share of net income or losses which are attributable to those projects that are accounted for using the equity method. Certain reclassifications have

been made to the 1994 financial data included herein to conform to the 1995 and 1996 presentation. These reclassifications had no effect on net income or stockholder's equity as previously reported.

The costs of developing a project are expensed until the project meets the major milestones of (1) a signed power purchase agreement or the equivalent and (2) approval by the Board of Directors of NRG. There were several projects under development at September 30, 1997 that met NRG's policy for capitalization of development costs. At September 30, 1997, NRG had \$21.1 million in capitalized costs related to Alto Cachopoal (\$2.6 million), Collinsville (\$1.9 million), Kladno (\$9.5 million), Millenium-Morris (\$6.0 million) and West Java (\$1.1 million).

#### RESULTS OF OPERATIONS

NINE MONTHS ENDED SEPTEMBER 30, 1997 COMPARED TO NINE MONTHS ENDED SEPTEMBER 30, 1996

For the nine months ended September 30, 1997, NRG had operating revenues of \$82.8 million, compared to operating revenues of \$71.8 million for the nine months ended September 30, 1996, an

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increase of 15%. NRG's operating revenues from wholly-owned operations for the period ended September 30, 1997 were \$65.1 million, an increase of \$12.6 million, or 24%, over the same period in 1996. The increase was primarily attributable to increases in MEC sales volume, rates charged to customers and pass-through fuel costs, management fee and cost reimbursement revenues from NRG's wholly-owned service subsidiaries, and technical service fees. Revenues from the RDF business increased \$3.1 million, due to increases in MSW deliveries at the Newport Facility. For the nine months ended September 30, 1997, revenues from wholly-owned operations consisted primarily of revenue from district heating and cooling (39%), resource recovery activities (32%), other thermal projects (16%), technical service fees (6%), management fees (5%), and NEO (2%).

Equity in earnings of unconsolidated project affiliates was \$17.8 million for the nine months ended September 30, 1997 compared to \$19.4 million for the nine months ended September 30, 1996, a decline of 8%. Lower earnings in MIBRAG, Latin Power and Kladno offset the new revenue sources for NRG and COBEE.

Cost of operations in wholly-owned operations was \$32.9 million for the nine months ended September 30, 1997, an increase of \$6.0 million, or 22%, over the same period in 1996. The increase is due primarily to increased MEC sales volume, service labor costs and fuel costs. Cost of operations as a percentage of revenues from wholly-owned operations is 50% which is identical to the same period in 1996.

General, administrative and development costs were \$28.4 million for the nine months ended September 30, 1997, compared to \$26.6 million for the nine months ended September 30, 1996. The \$1.8 million increase is due primarily to increased business development, associated legal, technical, and accounting expenses, headcount and equipment. General, administrative and development costs as a percent of revenues from wholly-owned operations declined from 51% to 44%.

Interest expense for the nine months ended September 30, 1997, as compared with the same period in 1996, increased by \$8.5 million, from \$11.3 million to \$19.8 million. This increase was due to the issuance of \$250 million aggregate principal amount of Old Notes at the end of June 1997, an additional month of interest associated with the issuance of 7.625%, \$125 million Senior Notes due 2006; bridge financing, and \$0.2 million of interest on the Company's \$175 million revolver.

The Company has recognized an income tax benefit due to domestic income tax losses and due to the recognition of certain tax credits. The income tax

benefit for the nine months ended September 30, 1997 increased as compared to the benefit for the nine months ended September 30, 1996 due primarily to increased tax credits and higher interest expense.

Net income for the nine months ended September 30, 1997, was \$14.4 million, an increase of \$3.1 million or 28%, compared to net income of \$11.3 million in the same period in 1996. This increase was due to the factors described above.

#### YEAR ENDED DECEMBER 31, 1996 COMPARED TO YEAR ENDED DECEMBER 31, 1995

For the year ended December 31, 1996, NRG had operating revenues of \$104.5 million, compared to operating revenues of \$87.8 million in 1995, an increase of 19%. NRG's operating revenues from wholly-owned operations for the year ended December 31, 1996 were \$71.6 million, an increase of \$7.5 million, or 12%, over the prior year. The increase was primarily attributable to continued expansion of NEO's methane gas business and increased revenues from MEC. For the year ended December 31, 1996, revenues from wholly-owned operations consisted primarily of revenue from district heating and cooling (39%), resource recovery activities (33%), other thermal projects (19%) and NEO (5%).

Equity in earnings of unconsolidated project affiliates, excluding gains on project termination settlements, was \$32.8 million for the year ended December 31, 1996, compared to \$23.6 million for the year ended December 31, 1995, an increase of 39%. In 1996, new revenue sources from the Schkopau and NRGG projects provided equity earnings of \$6.4 million and \$2.3 million, respectively. Additionally, Latin Power provided \$1.6 million of increased equity earnings in 1996 as compared to 1995 because of the startup of a new project. These were offset by an expected decrease in equity earnings of \$9.2

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million for the MIBRAG mining and power generation project, primarily due to expected decreases in coal and briquette sales. Equity in earnings of Gladstone was \$10.8 million in 1996, down slightly from 1995 earnings of \$11.2 million. Equity in earnings in 1996 and 1995 reflect an investment write-down of \$1.5 million and \$5.0 million, respectively, relating to the enhanced coal project of NRG's wholly-owned subsidiary, Scoria, Inc. ("Scoria"). On December 31, 1996, NRG's investment balance in the Scoria project was reduced to zero. Scoria Incorporated and Western SynCoal Co., a subsidiary of Montana Power Co., completed construction in January 1992 of a demonstration coal conversion plant designed to improve the heating value of coal by removing moisture, sulfur and ash. The plant, located in Montana, has the ability to produce 300,000 tons of clean coal annually which, when burned, produces emissions in compliance with the Clean Air Act. The fuel may be an alternative to scrubbers for some energy companies. Testing of the plant ended in August 1993 and commercial operations began at that time. NRG's net capitalized investment in the Scoria coal project was written down by \$3.5 million in 1994, \$5.0 million in 1995 and final write-off of \$1.5 million in 1996. The write-downs were due to reductions in expected future operating cash flows from the project and an overall economic assessment of the project. On August 31, 1997, Scoria's 50% interest in the project was liquidated by the project partnership in exchange for a liquidation payment of \$100.

Cost of operations in wholly-owned operations was \$36.6 million in 1996, an increase of \$4.1 million, or 12.6%, compared to 1995, due primarily to increased fuel costs resulting from increased MEC sales volume and per unit fuel prices. Cost of operations as a percentage of revenues from wholly-owned operations remained constant at 51% for 1995 and 1996.

General, administrative and development costs were \$39.2 million in 1996, compared to \$34.6 million in 1995, an increase of \$4.6 million, or 12.9%. The majority of the increase from 1995 to 1996 was due to additional general and administrative expenses incurred in the growth and development of NEO totaling \$5.8 million, in contrast with NEO's general and administrative expenses of \$1.8 million for the prior year. Business development expenses

for the year ended December 31, 1996 totaled \$19.4 million, as compared with \$17.6 million for the same period in 1995.

Other income, net increased by \$4.6 million in 1996 due primarily to additional interest income earned from investing the proceeds of the 1996 Senior Note Offering, which was completed in January 1996.

The effective tax rate (benefit) for the year ended December 31, 1996 was (39.5%), as compared to 22% for the same period ended December 31, 1995. The decrease in the effective tax rate in 1996 was due to a change in NRG's income sources, with more earnings derived from U.S. operations in 1995, primarily the \$29.9 million pre-tax gain on the disposition of the San Joaquin power purchase agreements. Because of NRG's intention to reinvest earnings of foreign operations offshore, no provision was recorded for income taxes due upon repatriation.

Net income for the year ended December 31, 1996 was \$20.0 million, a decrease of \$11.2 million, or 36%, compared to net income of \$31.2 million in 1995. This decrease was due to the fact that \$29.9 million of that 1995 net income was attributable to the one-time payment for the buy-out of the San Joaquin power sales contract in that year, as well as to the other factors described above.

#### YEAR ENDED DECEMBER 31, 1995 COMPARED TO YEAR ENDED DECEMBER 31, 1994

For the year ended December 31, 1995, NRG had operating revenues of \$87.8 million, compared to operating revenues of \$91.1 million in 1994, a decrease of 4%. NRG's operating revenues from wholly-owned operations for the year ended December 31, 1995, were \$64.2 million, essentially unchanged from \$64.0 million in the prior year. Revenues from wholly-owned operations consisted primarily of revenue from district heating and cooling (39%), resource recovery activities (36%), other thermal projects (21%) and NEO (1%).

Equity in earnings of unconsolidated project affiliates was \$23.6 million for the year ended December 31, 1995, compared to \$27.2 million for the year ended December 31, 1994, a decrease of 13%. Equity in earnings of \$22.2 million from the MIBRAG mining and power generation project increased \$2.8 million in 1995 primarily due to increased power and coal sales. Equity in earnings of

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Gladstone was \$11.2 million in 1995 as compared to \$7.7 million for the prior year, due to the inclusion of a full year's earnings in 1995 compared to nine months of the prior year. San Joaquin Cogeneration earnings decreased from \$6.1 million in 1994 to \$2.0 million in equity earnings in 1995 because of the shutdown of the facilities at the end of February 1995, and the termination of the power purchase agreements with Pacific Gas & Electric ("PG&E"). The Sunnyside waste coal facility acquired in late 1994 experienced initial operating problems, a six-week shutdown for major repairs and refurbishments, and a reduction in power revenue due to lower than anticipated avoided costs of the power purchaser, PacifiCorp, resulting in a loss of \$2.7 million in 1995 equity in earnings. Finally, equity in earnings in 1995 reflects an investment write-down of \$5.0 million related to Scoria while 1994 equity in earnings reflects investment write-downs of \$3.5 million for Scoria and \$1.5 million related to the proposed Louisiana Energy Services ("LES") uranium enrichment facility in which NRG owns a 6.73% interest. NRG's investment in LES has been reduced to zero.

Cost of operations in wholly-owned operations was \$32.5 million in 1995, a decrease of \$2.3 million, or 6.7%, compared to 1994, due primarily to lower resource recovery landfill charges and reduced district heating fuel costs. Cost of operations as a percentage of revenues from wholly-owned operations decreased to 51% in 1995 from 55% in 1994.

General, administrative and development costs were \$34.6 million in 1995, as compared to \$20.0 million in 1994, an increase of \$14.6 million, or 73.0%. Business development expenses made up approximately \$8.8 million of this

increase. The balance of the increase was attributable to establishing and maintaining NRG's foreign offices and domestic support functions. In 1995, NRG aggressively expanded staff and activity in seeking new projects. Project development activity was redirected and expanded in 1995 as NRG completed its initial investments in the MIBRAG, Gladstone and Schkopau projects in 1994. During 1994, some development costs were capitalized in these projects until financial close was achieved. Conversely, during 1995, NRG expensed the costs of pursuing a number of projects requiring the payment of significant upfront fees and expenses, including an investment opportunity that required expenditure of significant legal fees to submit a competing plan of reorganization in the bankruptcy court proceeding for O'Brien Energy (in which NRG acquired a 41.86% interest in 1996). Most of these costs were expensed because these projects did not meet NRG's requirements for capitalization.

Equity in gain from project termination settlements in 1995 included a one-time pre-tax gain of \$29.9 million related to the settlement and termination of the San Joaquin Valley power purchase agreements with PG&E. In 1994, NRG and its partner in the Michigan Cogeneration Partners Limited Partnership agreed to terminate a power sales contract with Consumers Power Company. The contract related to a 65 MW cogeneration facility being developed in Michigan. Due to the agreement to terminate the contract, NRG recorded a one-time pre-tax gain of \$9.7 million in 1994.

Other income, net increased \$3.5 million in 1995 due primarily to additional interest income from project notes receivable and short-term investments.

The effective tax rate for the year ended December 31, 1995 was 22%, as compared to 7.7% for the same period ended December 31, 1994. This increase from 1994 to 1995 was primarily due to the fact that a greater portion of NRG's income was derived from United States sources in 1995, primarily as a result of the \$29.9 million pre-tax gain on the disposition of the San Joaquin power purchase agreements. Because of NRG's intent to reinvest earnings of foreign operations offshore, no provision was recorded for income taxes that would be due on repatriation.

Net income for the year ended December 31, 1995, was \$31.2 million, an increase of \$1.7 million, or 6%, compared to net income of \$29.5 million in 1994. This increase was due to the factors described above.

FINANCIAL RESULTS OF INVESTMENTS IN PRINCIPAL PROJECTS

The following sets forth certain information with respect to the results of investments in principal projects. For a description of these projects, see "Business -- Description of NRG's Projects."

PROJECT	EQUITY IN EARNINGS					PERCENTAGE OWNERSHIP INTEREST
	YEAR ENDED DECEMBER 31,			NINE MONTHS ENDED SEPTEMBER 30,		
	1994	1995	1996	1996	1997	
	(DOLLARS IN MILLIONS)					
MIBRAG (1) ....	\$19.4	\$22.2	\$13.1	\$ 7.6	\$ 7.0	33.3
Gladstone .....	7.7 (2)	11.2	10.8	8.5	8.7	37.5
Schkopau .....	0.0	0.0 (3)	4.6	4.5	3.8	20.6
Latin Power....	(0.3)	0.0	1.6	1.4	0.1	4 -9
NRGG.....	*	*	2.3	1.3(5)	2.3	41.9

Scoria.....	(3.0)	(3.0)	(3.3)	(2.4)	0	50.0
San Joaquin....	8.1	-- (4)	2.7	(0.5)	(0.8)	45.0
Jackson						
Valley.....	1.0	--	3.3	--	(0.3)	50.0
Sunnyside.....	*	(2.4)	0.6	0.6	0	50.0
Other.....	(0.7)	0.6	(1.4)	(1.6)	(3.0)	
Write-off (6)	(5.0)	(5.0)	(1.5)	--	--	

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\* Not owned during this period.

- (1) Earnings are expected to decrease in 1997 and 1998 due to mine refurbishment and reduced coal sales. However, in 1999, coal sales are expected to increase with the expected startup of the first of two 800 MW generating units being constructed nearby at Lippendorf. Contracts to supply coal to new Lippendorf facility have been executed as part of the MIBRAG transaction.
- (2) Purchased in March 1994.
- (3) Earnings commenced in the first quarter of 1996 when the first unit was brought on-line.
- (4) In June 1995, a power sales contract was terminated and a pre-tax gain of \$29.9 million was recognized by NRG for its share of the termination settlement.
- (5) Purchased in April 1996.
- (6) In 1994, 1995 and 1996, NRG recorded a pre-tax charge to write down the carrying value of certain energy projects. See "--Results of Operations."

#### LIQUIDITY AND CAPITAL RESOURCES

Net cash provided by operating activities was \$27.4 million for the nine months ended September 30, 1997, as compared to \$2.4 million cash used by operating activities for the same period of 1996, a change of \$29.8 million. The primary differences between the nine months ended September 30, 1997 and the same period in 1996 were increased net income of \$3.1 million, undistributed equity in operating earnings of affiliates of \$5.7, working capital items of \$13.7 million, and an increase in other assets of \$4.6 million.

Net cash flow from operating activities was \$4.1 million for the year ended December 31, 1996. Principal components of cash flow from operating activities were net income of \$20.0 million, depreciation and amortization of \$8.4 million and changes in working capital of (\$4.3) million. Non-cash adjustments that reduced cash flow from operating activities consisted primarily of \$17.8 million of undistributed equity in operating earnings of unconsolidated project affiliates.

Net cash flow used by operating activities was \$5.1 million for the year ended December 31, 1995. Principal components of cash flow from operating activities were net income of \$31.2 million, depreciation and amortization of \$8.3 million and changes in working capital items of \$9.0 million. Non-cash adjustments that reduced cash flow from operating activities consisted primarily of \$29.9 million of undistributed equity in gain from the San Joaquin project termination settlement.

Net cash flow from operating activities was \$12.4 million for the year ended December 31, 1994. Principal components of cash flow from operating activities were net income of \$29.5 million, depreciation and amortization of \$8.7 million and changes in working capital items of (\$6.1) million. Other adjustments that reduced cash flow from operating activities consisted primarily of \$18.5 million of undistributed equity in operating earnings of unconsolidated project affiliates and \$1.1 million of cash related to deferred taxes and cash used by changes in other assets.

Net cash used for investing activities for the nine months ended September 30, 1997 was \$402.5 million as compared to \$70.8 million for the same period



in 1996. The primary reason for the increase was due to \$326.9 million being invested in projects in the nine months ended September 30, 1997 as compared to \$53.4 million in the same period in 1996.

NRG's project investments in the nine months ended September 30, 1997 included \$264.3 million in Loy Yang, \$6.7 million in NRG San Diego, \$23.5 million in Energy Development Limited ("EDL"), \$3.7 million in Latin Power, \$2.3 million in Scoria, \$1.9 million in NRG Cadillac, \$4.5 million in Kladno, and \$16.9 million in capital development costs. NRG also increased its outstanding notes receivable by \$67.0 million. Of this amount \$42.9 million went to international projects (a \$9.4 million note to Enfield, \$1.7 million in various international notes, and \$31.8 million in notes to COBEE) and \$21.7 million went to domestic projects (\$15.2 million in notes to NEO, \$1.6 million to MEC, and \$4.9 million to Grays Ferry). Capital expenditures totaled \$41.1 million for the nine months ended September 30, 1997, as compared to \$11.4 million in the same period one year earlier. This amount is primarily attributable to capital investments in NEO of \$21.0 million, in the MEC Fairview Plant and the MEC Federal Reserve Plant of \$3.0 million, and in the Company's new investments in San Diego Power & Cooling of \$6.0 million and Millennium of \$10.3 million. At September 30, 1997, NRG's restricted cash balance was \$0.3 million, while at September 30, 1996, it was \$23.6 million. The decline in restricted cash is due to a change in the market value of the company's foreign exchange swaps, and the posting of an \$8 million letter of credit which replaced the collateral requirement. The restricted cash balance charge for the periods ended September 30, 1997 and 1996 impacted cash flow by \$17.3 million and (\$13.9) million, respectively. For the period ended September 30, 1997, NRG received \$6.7 million from its sale of a portion of its investment in COBEE. On October 30, 1997, NRG subsequently received \$14.5 million for a sale of an additional portion of its COBEE investment. For the same period in 1996, NRG received \$15.7 million of proceeds related to the termination of the SJVEP Facilities (as hereinafter defined) power purchase agreement.

Cash used for investing activities for the year ended December 31, 1996 included \$140.6 million in equity investments in projects, \$36.6 million in loans to projects, and \$24.6 million in capital expenditures related to wholly-owned operations. The primary components of NRG's 1996 project investments include \$81.8 million for its investment in COBEE, \$28.8 million for its investment in NRGG and \$7.5 million for the purchase of certain biomass assets from O'Brien (subsequently NRGG). NRG's net increase in loans to projects of \$36.6 million was primarily due to a loan to NRGG of \$14.4 million and the purchase of the senior debt of MCPC. NRG made total capital expenditures in 1996 of \$24.6 million. Additionally, cash flows from investing activities in 1996 included \$15.7 million of cash distributed from SJVEP related to the project termination settlement. The project termination resulted in a pre-tax gain of \$29.9 million in 1995, at which time NRG received a \$14.2 million distribution. All other cash distributions from the project are included in operating cash flow, while the distributions from project termination are included as cash flow from investing activities.

Cash used for investing activities for the year ended December 31, 1995 included \$25.8 million in equity investments in projects, \$35.4 million in loans to projects, and \$11.0 million in capital expenditures related to wholly-owned operations. In 1995 NRG invested \$25.8 million in several projects, including \$11.0 million in the Schkopau project, \$4.1 million in the Latin Power Project, \$3.8 million in the Kladno project, and \$3.3 million in the North America Thermal project. In addition, NRG loaned additional funds of \$35.4 million to operating projects, including a \$27.9 million loan to the Schkopau project.

Cash used for investing activities for the year ended December 31, 1994 included \$102.1 million in equity investment in projects and \$4.4 million in loans to projects, and \$5.8 million in capital expenditures related to wholly-owned operations. In 1994, NRG invested this \$102.1 million in several projects including, \$64.9 million in the Gladstone project, \$18.2 million in the Schkopau project, \$11.5 million in the Sunnyside project, and \$10.6 million in the MIBRAG project. In addition, NRG provided \$13.8 million of restricted cash deposits to collateralize foreign currency hedging activities

and letters of credit issued in connection with competitive bids.

Net cash provided from financing activities for the nine months ended September 30, 1997 was \$382.0 million as compared to \$120.9 million in the same period of the prior year. The cash provided from

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financing activities includes \$80.4 million equity investment by NRG's parent company, NSP, to fund NRG's investment in EDL and Loy Yang. Proceeds from the issuance of long-term debt were \$303.5 million which included \$16.9 million used to finance Millennium, \$2.6 million to finance San Diego Power & Cooling, \$38.0 million on the Company's line of credit, and \$250.0 million on the 1997 Senior Notes, all of which was offset by \$4.0 million of debt issuance costs. For the nine months ended September 30, 1996, the Company received \$125.0 million in cash proceeds from the issuance of the 1996 Senior Notes which was partially offset by \$2.4 million in financing costs. For the balance of 1996, cash flows from financing activities included an \$80 million equity contribution from NSP to NRG for the purchase of COBEE. In 1994, cash flows from financing included an investment of \$103.9 million from NSP. The proceeds of the capital infusion were used for investment in Gladstone (\$64.9 million), Schkopau (\$18.2 million), MIBRAG (\$10.6 million) and Sunnyside (\$11.5 million).

On January 29, 1996, NRG issued the 1996 Senior Notes in a transaction exempt from registration under the Securities Act. The 1996 Senior Notes were issued to fund some or all of NRG's equity investments in Schkopau and Latin Power, to pay a portion of the consideration for NRG's acquisition of interests in Collinsville and in O'Brien (for reorganization as NRGG), to make equity investments in Kladno and West Java, and for general corporate purposes, including investments in new projects. The 1996 Senior Notes are senior unsecured obligations of NRG and rank pari passu with all other senior unsecured indebtedness of NRG, including the Notes. The 1996 Senior Notes have terms similar to the Notes. See "Certain Indebtedness" and "Description of Notes."

As of September 30, 1997, NRG's consolidated financial statements contained long-term debt (excluding current maturities) of \$474.4 million, \$375 million of which is represented by the 1996 Senior Notes and the Notes. The 1996 Senior Notes have terms substantially similar to the Notes, except the maturity date is in January 2006. The \$265.0 million increase from the same period one year earlier is due to \$250.0 million from the 1997 Senior Notes, \$2.2 million for San Diego Power & Cooling, \$16.9 million for Millennium less \$4.1 million consisting primarily of debt issuance costs. As of September 30, 1997, annual maturities of long-term debt ranged from \$3.9 million to \$5.0 million in the five-year period ending December 31, 2001. In addition, \$38.0 million is due under NRG's revolving credit facility. See "Certain Indebtedness" and "Description of Notes."

NRG is committed to additional equity investments of approximately \$226 million for 1997-2001, approximately \$49 million of which is committed for 1997, for various international power generation projects. In September 1997, NRG committed to funding up to \$22 million in Millennium on or before the end of the construction period estimated to be May 1999. In addition, in 1996, NRG provided a \$10 million loan commitment to a wholly-owned project subsidiary of NRGG in order for the NRGG project subsidiary to fund its capital contribution to Grays Ferry, a cogeneration project currently under construction. As of October 31, 1997, NRG lent Grays Ferry \$6.3 million as part of its loan commitment. As part of the 1996 loan agreement, NRG was granted the option to convert \$3 million of the loan into common equity of NRGG. NRG exercised this option and on November 25, 1997, received 396,255 shares of NRGG's common stock. In addition, NRG has committed to finance NRGG's investment in projects transferred to NRGG under the Co-Investment Agreement between NRG and NRGG to the extent funds are not available to NRGG on comparable terms from other sources. (See Note 13 of Notes to Consolidated Financial Statements for further discussion of NRG's commitments.) NRG expects to meet these cash requirements with proceeds from the issuance of debt or equity, including equity contributions from NSP, and internally

generated cash.

In May 1997, NRG acquired a 25.37% equity interest in Loy Yang A. See "Business -- Independent Power Production and Cogeneration--International Projects--Loy Yang Power." In order to finance its equity investment in this acquisition and related financing costs, NRG borrowed \$200 million in short-term debt pursuant to the Bridge Financing, which it used together with an investment of \$60.9 million from NSP and cash on hand. The net proceeds from the Offering were used to refinance the Bridge Financing. See "Use of Proceeds."

In addition to the Loy Yang acquisition, NRG purchased San Diego Power & Cooling on June 25, 1997. The purchase price was \$6.7 million, including a note from the seller for \$2.7 million. In July 1997,

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NRG acquired a 50% interest in Cadillac Renewable Energy, a 34 MW steam turbine power plant located in Cadillac, Michigan for \$1.9 million. In September 1997, NRG Morris Cogen, LLC, (formerly Millennium-Morris), an NRG affiliate, entered into a Construction and Term Loan Agreement to finance the construction of a 117 MW cogeneration plant in Morris, Illinois. NRG has entered into a \$22 million equity commitment and a \$1.2 million guaranty of certain obligations of NRG Morris Operation, Inc., an NRG affiliate that will operate the project.

On November 4, 1997, NRG acquired 100% of the outstanding shares of Pacific Generation Company for \$151.3 million. Pacific Generation has ownership interests in 11 projects with a total capacity of 737 MW, with operational responsibility for 312 MW and net ownership interests of 166 MW. The acquisition was financed primarily through the use of NRG's revolving credit facility.

On November 21, 1997, a consortium including NRG signed an Asset Sale Agreement to acquire the El Segundo Generating Station, a 1,020 MW gas-fired project, from Southern California Edison. NRG and Destec Energy, Inc. are jointly and severally liable under the agreement for the payment of the \$87.75 million purchase price. Consummation of the transaction is scheduled for January 1, 1998, but it is contingent on receipt of regulatory approvals and consents from a number of governmental and private parties. There can be no assurance that all of these approvals and consents will be received.

NRG has entered into a \$175 million revolving credit facility with a syndicate of banks led by ABN AMRO, which matures on March 17, 2000. Proceeds from the facility will be used for general corporate purposes, including letters of credit and interim funding for NRG project investments.

The facility allows for LIBOR and Base rate borrowing depending upon the days notice required and the term of drawing. The applicable margin is based upon the rate option selected and the assigned ratings of NRG. Pursuant to the terms of the agreement, NRG is restricted from creating liens on its assets, is prohibited from merging except under certain circumstances and must maintain a specified minimum net worth. Failure to comply with these restrictive covenants could result in an event of default. Other events of default include nonpayment of principal or interest, NSP's failure to own majority of outstanding voting stock of NRG, certain cross-defaults, and certain events of bankruptcy. As of September 30, 1997, \$38.0 million was outstanding from the revolving credit facility.

As part of NRG's global tax strategy, NRG intends to maintain offshore, for permanent reinvestment in other foreign projects, earnings from foreign investments. For this reason, NRG intends to utilize the earnings in its domestic operations to make the payments of principal and interest on the Senior Notes. These earnings will include payments of interest and principal to be received from its wholly-owned Dutch project subsidiary, NRGenerating International, B.V., with respect to loans from NRG. Although dividends and management fees to NRG and its subsidiaries from partnerships in which NRG invests are subject to restrictions in some cases, NRG currently expects that

cash generated internally and funds from borrowings described above will provide sufficient funds for operating activities. However, there can be no assurance that available funds will be sufficient for such purposes. Because substantially all of the operations of NRG are conducted by its project subsidiaries and project affiliates, NRG's cash flow and its ability to service its indebtedness, including its ability to pay the interest on and principal of the Senior Notes when due, are dependent upon cash dividends and distributions or other transfers from its project and other subsidiaries and project affiliates to NRG.

#### IMPACT OF INFLATION, INTEREST RATES, EXCHANGE RATES AND ENERGY PRICES

NRG attempts, whenever practicable, to hedge certain aspects of its international project investments against the effects of inflation and fluctuations in interest rates and energy prices. To date, NRG has generally structured the energy payments of its power purchase agreements to adjust with the same price indices as contained in its contracts with the fuel suppliers for the corresponding projects. In some cases, a portion of revenues is associated with operation and maintenance and is indexed to adjust with inflation.

In July 1997, NRG changed its policy of hedging foreign currency denominated investments as they were made, to a policy of hedging foreign currency denominated cash flows, over a projected 12-month period. As a result of this change in hedging policy, NRG terminated the seven foreign currency swap

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agreements on July 29, 1997. Such terminations resulted in cash payments to NRG without any earnings impact. Consistent with prior policies, NRG is not hedging future earnings and does not speculate in foreign currencies.

#### RECENTLY ISSUED ACCOUNTING STANDARDS

In June 1997, Statement of Financial Accounting Standards (SFAS) No. 130, "Reporting Comprehensive Income," was issued. In addition, in June 1997 SFAS No. 131, "Disclosures about Segments of an Enterprise and Related Information," was also issued. As both SFAS No. 130 and No. 131 are effective for fiscal years beginning after December 15, 1997, NRG's 1998 annual report to shareholders will include the disclosures required by these new standards. Management believes the adoption of SFAS No. 130 and SFAS No. 131 will not have a material effect on NRG's financial statements.

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#### BUSINESS

##### INTRODUCTION

NRG is one of the leading participants in the independent power generation industry. Established in 1989 and wholly-owned by Northern States Power Company ("NSP"), NRG is principally engaged in the acquisition, development and operation of, and ownership of interests in, independent power production and cogeneration facilities, thermal energy production and transmission facilities and resource recovery facilities. The power generation facilities in which NRG currently has interests (including those under construction and Loy Yang A) as of November 21, 1997 have a total design capacity of 7,972

megawatts ("MW"), of which NRG has or will have operational responsibility for 5,062 MW and net ownership of or leasehold interests in 2,351 MW. In addition, NRG has substantial interests in district heating and cooling systems and steam generation and transmission operations; as of December 31, 1996, these thermal businesses had a steam capacity of approximately 3,550 million British thermal units ("mmBtus"). NRG's refuse-derived fuel ("RDF") plants processed more than 808,000 tons of municipal solid waste into approximately 644,000 tons of RDF in 1996.

#### STRATEGY

NRG intends to continue to grow through a combination of acquisitions and greenfield development of power generation and thermal energy production and transmission facilities and related assets in the United States and abroad. NRG believes that its facility operations and engineering expertise, fuel and environmental strategies, labor and government relations expertise and legal and financial skills give NRG a competitive advantage in the independent power market. NRG also believes that its policy of meeting or exceeding applicable environmental regulatory standards and its environmental compliance record will give it an advantage as regulators continue to impose increasingly stringent environmental requirements on the operation of power generation facilities. In addition, NRG continues to have access to technical and administrative support from NSP on a contract basis to augment its own expertise. NRG believes the knowledge and expertise it has gained in the financial and legal restructuring of its existing facilities, as well as its reputation with respect to environmental compliance and labor relations, can be effectively employed in the development of both domestic and international greenfield projects.

In the United States, NRG's near-term focus will be primarily on the acquisition of existing power generation capacity and thermal energy production and transmission facilities, particularly in situations in which its expertise can be applied to improve the operating and financial performance of the facilities. NRG intends to focus its domestic development activities primarily on the acquisition or development of facilities in excess of 100 MW and to pursue smaller projects when it has the opportunity to combine several smaller projects into a larger transaction. NRG is also working with several industrial companies to develop energy projects that would provide both electricity and steam for their production facilities. In addition, to the extent that the replacement of aging power generating capacity or growth in demand creates the need for new power generation facilities in the United States, NRG intends to pursue opportunities to participate in the development of such facilities. NRG is also studying the opportunities that may be created by the current restructuring of the domestic electric utility industry, particularly the divestiture by some utility companies of their generating assets.

In the international market, NRG will continue to pursue development and acquisition opportunities in those countries in which it believes that the legal, political and economic environment is conducive to increased foreign investment. Once it has developed one project in a country, NRG uses that as a base to develop other projects in that same country or region, leveraging its experience and knowledge to enhance its likelihood of success in the area. NRG intends to continue to capitalize on opportunities created by the privatization of existing government-owned generating capacity. In addition, due to the significant existing demand for new power generating capacity in the international market, NRG intends to engage in the development of international greenfield projects. NRG intends to focus its international development activities primarily on the acquisition or development of facilities with capacity in excess of 100 MW and to pursue smaller projects when it has the opportunity to combine several smaller projects into a larger transaction. NRG believes that the global market will continue to provide attractive

investment opportunities to NRG as the countries that have initiated the privatization of their power generation capacity and have solicited bids from

private companies to purchase existing facilities or to develop new capacity continue their privatization programs and other countries begin similar privatization efforts.

NRG's acquisition and development strategy is based upon the pursuit of opportunities located in countries that are expected to meet certain project-specific and market criteria. These criteria include fuel type, facility size, form of ownership or control, type of transaction (privatization or greenfield) and committed capacity compared to projected market demand. The evaluation process also incorporates political and business climate criteria that include a favorable legal and regulatory environment, ability to attract financing and economic outlook. NRG's goal is to focus on countries that provide a combination of need for additional generation capacity and positive political, business and economic factors.

NRG expects to acquire or develop most domestic and international projects on a joint venture basis. Where appropriate, NRG will include a local or host country partner or a partner with substantial experience in or connections to the area. By doing so, NRG expects to gain a number of advantages, including technical expertise possessed by others, greater knowledge of and experience with the political, economic, cultural and social conditions and commercial practices of the region or country where the project is being developed, and the ability to leverage NRG's human and financial resources. A local partner also may, among other things, assist in obtaining financing from local capital markets as well as building political and community support for the project. NRG expects such joint ventures will enable it to share the risks associated with the acquisition and development of larger projects. Joint acquisition and development of future projects also should further reduce NRG's financial risk by building a more diversified portfolio of projects.

Although NRG exercises flexibility in structuring its investments in projects, NRG's goal is to own a 20% to 50% equity interest in, and have operating control or influence over, the projects in which it invests. However, NRG may in some instances be willing to modify these targets for a particular project if it determines that strategic considerations and anticipated returns, when combined with other factors, such as the ability to exercise "negative control" (i.e., the ability to control material project decisions by exercising a veto right) or the ability to exercise oversight authority in the development or operation of a project, justify an investment in that project. Alternatively, NRG may consider investments or projects in which it is the sole or a majority owner or in which it owns less than a 20% equity interest. See "Risk Factors -- Risks Involved in Making Minority Investments in Projects."

NRG intends to pursue the acquisition and development of natural gas-fired power generation facilities where appropriate, to complement its existing and anticipated future investments in coal and other solid fuel-fired facilities. NRG currently holds no interest in, and has no present intention of investing in, any nuclear generating facility.

As part of NRG's global tax strategy, NRG intends to maintain its earnings from foreign investments offshore, for permanent reinvestment in other foreign projects. For this reason, NRG intends to utilize the earnings in its domestic operations to make the payments with respect to the Notes. These earnings are expected to include payments of interest and principal to be received from its wholly-owned Dutch subsidiary, NRGenerating International, B.V. ("NRGBV") with respect to loans from NRG to that company.

#### COMPETITION

The demand for power in the United States traditionally has been met by utilities constructing large-scale electric generating plants under cost-of-service based regulation. The enactment of PURPA in 1978 spawned the growth of the independent power industry which expanded rapidly in the 1980s. The initial independent power producers to enter the market were an entrepreneurial group of cogenerators and small power producers who recognized the business opportunities offered by PURPA. This initial group of independent power producers was later joined by larger, better capitalized

companies, such as subsidiaries of fuel supply companies, engineering companies, equipment manufacturers and affiliates of other industrial companies. In addition, a number of regulated utilities

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created subsidiaries (such as NRG) which compete with the independent power producers. Some independent power producers specialize in market niches, such as a specific technology or fuel (for example, gas-fired cogeneration, waste-to-energy, hydropower, geothermal, wind, solar, wood, coal and conservation) or a specific region of the country where they believe they have a market advantage.

Although NRG is one of the leading participants in the independent power industry, certain other independent power producers and utility affiliates have significantly larger capital resources available to them on a stand-alone basis than NRG. NRG's competitors are major international independent power producers worldwide, which include, among others, CalEnergy, CMS Generation Co., Cogentrix Energy, Inc., Dominion Energy, Enron Development Corp., Edison Mission, Inc., National Power plc, PowerGen plc, Southern Electric International, Inc. and The AES Corporation. Such competitors compete with NRG with regard to pricing terms, quality of service and experience.

#### PENDING ACQUISITIONS AND PROJECTS UNDER DEVELOPMENT

NRG has a number of projects in development and is in various stages of negotiations for the acquisition of power and steam generating capacity in the United States and abroad. There can be no assurance that the acquisition or development of any or all of these projects will in fact be consummated, or if consummated, that the projects will remain in the form or occur in the manner described in this Prospectus.

#### WEST JAVA

A joint venture among NRG, Ansaldo Energia SpA, a major Italian industrial company ("Ansaldo"), and P.T. Kiani Metra, an Indonesian industrial company ("PTKM"), is developing a 400 MW coal-fired power generation facility in West Java, Indonesia through P.T. Dayalistrik Pratama ("PTDP"), a limited liability company created by the joint venturers. Each of NRG and Ansaldo have an ownership interest of 45% in PTDP and PTKM has an ownership interest of 10%.

PTDP signed a Power Purchase Agreement (the "PPA") with P.T. PLN (Persero) ("P.T. PLN"), an instrumentality of the Government of Indonesia, on November 13, 1996. Under the PPA, PTDP must close and draw on construction financing no later than January 12, 1998 or be subject to termination. Furthermore, in certain circumstances of default the PPA gives P.T. PLN an option to purchase the project prior to commercial operation at a price designed to give NRG and its partners a fixed rate of return on their committed equity investments and, after commercial operation, at a price based on the net present value of future project cash flows.

PTDP has executed construction contracts pursuant to which Ansaldo will construct the project for a fixed price on a fixed schedule (subject to customary adjustments). Ansaldo is liable for liquidated damages in the event of certain construction delays or defaults. An NRG affiliate will be the operator of the project pursuant to an 18 year operating and maintenance agreement, which provides for reimbursement of the actual operating costs and payment of an annual fee. NRG will guarantee the operator's obligations under this agreement. In June 1997, PTDP signed a coal supply agreement for the project and acquired the land for the plant site.

NRG expects that, upon closing of financing, its total committed equity in PTDP will be approximately \$65 million. As of September 15, 1997, NRG has made capital infusions into PTDP totalling \$5.63 million. The total project cost is approximately \$560 million, which is to be financed by a combination of equity investments, commercial bank debt and capital markets funding. The

project is currently expected to be ready for financial closing by the end of 1997, however, in September 1997 the Government of Indonesia announced that the project had been "postponed" and there can be no assurance as to when or whether the Government will allow the project to go forward. If the project does not go forward, NRG will be required to write-off its investment of approximately \$6 million, which has been capitalized.

#### ENFIELD

In December 1996, NRG reached agreement with Indeck Energy Services (Europe) ("Indeck") to take a 50% interest in the Enfield Energy Centre, a 350 MW gas-fired power project in the North London

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borough of Enfield. The power station is planned to begin commercial operations in the end of 1999 and is being jointly developed by NRG and Indeck. This power station, like Loy Yang A, will not have a long-term power sales contract, which is no longer available under the current United Kingdom regulatory system. Instead, it will sell its output to the U.K. grid. NRG expects that upon closing of financing, its total committed equity in the Enfield Energy Center will be approximately GBP 17 million.

#### ESTONIA

On December 20, 1996 representatives of the Estonian Government, the state-owned Eesti Energia ("EE"), and NRG signed a Development and Cooperation Agreement ("DCA"). The DCA defines the terms under which the parties are to establish a plan to develop and refurbish the Balti and Eesti Power Plants. Pursuant to the DCA, a business plan for the joint project was submitted in June, 1997. NRG has stated its willingness to invest up to \$67.25 million of equity in this project and to assist the joint project in obtaining non-recourse debt in an amount necessary to fund the required capital improvements to the Balti and Eesti Power Plants. Recently the Estonian government announced that it had rejected the business plan of NRG and EE. NRG has a policy of expensing all costs until there is a signed contract and Board of Directors approval. All such costs with respect to Estonia have been expensed. Discussions are continuing with the Estonian Government as management continues to evaluate the Estonian situation as well as other opportunities around the world.

#### CAJUN

NRG, together with two other parties, and the Chapter 11 trustee has filed a plan with the United States Bankruptcy Court for the Middle District of Louisiana, to acquire the fossil generating assets of Cajun Electric Power Cooperative of Baton Rouge, Louisiana ("Cajun") for approximately \$1.1 billion. The NRG consortium has the support of the Chapter 11 trustee and Cajun's secured creditors. The Court has also received two other competing plans of reorganization for Cajun. All three plans of reorganization are the subject of a confirmation hearing which began on December 15, 1996. NRG expects the confirmation process to conclude in 1997. Under the plan filed with the Court, NRG would hold a 30% equity interest in Louisiana Generating LLC, which would acquire Cajun's 1760 MW of non-nuclear generating assets. NRG's plan of reorganization for Cajun includes an equity investment from NRG of approximately \$55 million.

#### MCPC

In September 1996, through its subsidiary, Oklahoma Loan Acquisition Corp. ("OLAC"), NRG acquired all right, title and interest in the existing senior secured debt of Mid-Continent Power Company, Inc. ("MCPC") from Barclays Bank and The Nippon Credit Bank, at a substantial discount. On June 18, 1997, MCPC filed a Chapter 11 petition in federal bankruptcy court in Tulsa, Oklahoma, and concurrently filed a plan of reorganization proposing to transfer ownership of substantially all of MCPC's assets to OLAC in exchange for forgiveness of debt. On October 24, 1997, the bankruptcy court entered an order confirming MCPC's plan which provides for the transfer of MCPC's assets



to a subsidiary of NRG by December 23, 1997. NRG's development partner is entitled to a 10% interest in the MCPC project, and the bankruptcy court's confirmation order effectively mandates that NRG may own no more than 50% of the project. NRG is not obligated to make any further investments in MCPC. The project is a gas-fired cogeneration plant with a rated capacity of 110 MW, located in Pryor, Oklahoma. The project sells steam to several industrial customers located in the Mid-America Industrial Park and sells electricity to two Oklahoma utilities.

#### EL SEGUNDO

On November 21, 1997, a consortium including NRG signed an Asset Sale Agreement to acquire the El Segundo Generating Station, a 1,020 MW gas-fired project, from Southern California Edison. NRG and Destec Energy, Inc. are jointly and severally liable under the agreement for the payment of the \$87.75 million purchase price. Consummation of the transaction is expected to occur on or before January 1, 1998, but it is contingent on receipt of regulatory approvals and consents from a number of governmental and private parties. There can be no assurance that all of these approvals and consents will be received.

#### DESCRIPTION OF NRG'S PROJECTS

NRG owns interests in power generation and thermal generation projects and other facilities described herein either directly or through project subsidiaries or project affiliates. Each project is located on a site that is owned or leased on a long-term basis by NRG, a project subsidiary or a project affiliate. The ownership or leasehold interest generally is mortgaged to secure project financing obligations, and, in certain instances, to secure the project subsidiary's or project affiliate's obligations under its power purchase agreement.

#### PROJECT AGREEMENTS

In the past, virtually all of NRG's operating power generation facilities have sold electricity under long-term power purchase agreements. A facility's revenue from a power purchase agreement usually consists of two components: energy payments and capacity payments. Energy payments, which are intended to cover the variable costs of electric generation (such as fuel costs and variable operation and maintenance expense), are normally based on a facility's net electrical output measured in kilowatt hours, with payment rates either fixed or indexed to the fuel costs of the power purchaser. Capacity payments, which are generally intended to provide funds for the fixed costs incurred by the project subsidiary or project affiliate (such as debt service on the project financing and the equity return), are normally calculated based on the net electrical output or the declared capacity of a facility and its availability.

The power purchase agreements for NRG's international projects generally require that payments under such agreements be made in or indexed to United States dollars or a currency freely convertible to United States dollars, such as the Australian dollar or the German mark. NRG currently does not have political risk or currency convertibility and repatriation risk insurance coverage with respect to any of its existing project interests (other than Latin Power project investments). However, where appropriate and if available at reasonable premiums with respect to future project investments, NRG intends to procure insurance against currency inconvertibility and repatriation risks for its equity interests in projects.

A number of the more recent projects in which NRG has acquired or is acquiring an interest do not have long-term power purchase agreements. For example, Loy Yang A does not have such agreements because under the new Australian regulatory scheme, all generators must sell their output to a grid, where the price is established by a neutral regulator based on the

market prices during each defined period. The same will be true of Enfield, since the United Kingdom has adopted a similar regulatory scheme. Similarly, the SJVEP Facilities accepted a buy-out of their long-term contracts, so if they recommence operations, it is anticipated that they will be merchant plants. In the case of the Kladno project, where there is a long-term agreement, the energy price is tied to the market price of electricity rather than to the costs incurred by the project, so the contract does not provide the traditional level of certainty and protection. While these "merchant" projects introduce new risks and uncertainties, and require careful advance analysis of the local power markets, NRG believes that they are becoming increasingly accepted in the independent power market.

Generally, NRG's project subsidiaries and project affiliates that own operating power generation or steam generation facilities purchase fuel under long-term supply agreements or have ownership interests in the fuel source. Of the power generation projects in which NRG has an ownership interest, ten are fueled with coal or waste coal, four are fueled with biomass, three are fueled with oil, eight are fueled with natural gas, one is fueled with hydro-power and one is fueled with landfill gas and coal seam methane. Through NEO, NRG also has interests in 39 small hydroelectric or landfill gas-fired power generation facilities.

#### PROJECT FINANCING

As with its existing facilities, NRG expects to finance most of its future projects with some type of debt as well as equity. Leveraged financing permits the development of projects with a limited equity base but also increases the risk that a reduction in revenues could adversely affect a particular project's ability to meet its debt or lease obligations.

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NRG has financed its principal power generation facilities (other than Schkopau) primarily with non-recourse debt that is repaid solely from the project's revenues and generally is secured by interests in the physical assets, major project contracts and agreements, cash accounts and, in certain cases, the ownership interest, in that project subsidiary. This type of financing is referred to as "project financing." True project financing is not available for all projects, including some assets purchased out of bankruptcy (such as NRGG), some merchant plants, some purchases of minority stock positions in publicly traded companies (such as EDL) and plants in certain countries that lack a sufficiently well-developed legal system. But even in those instances, NRG may be able to finance a smaller proportion of the total project cost with project financing or may employ debt that is either raised or supported at the corporate level.

Project financing transactions generally are structured so that all revenues of a project are deposited directly with a bank or other financial institution acting as escrow or security deposit agent. These funds then are payable in a specified order of priority set forth in the financing documents to ensure that, to the extent available, they are used first to pay operating expenses, senior debt service and taxes and to fund reserve accounts. Thereafter, subject to satisfying debt service coverage ratios and certain other conditions, available funds may be disbursed for management fees or dividends or, where there are subordinated lenders, to the payment of subordinated debt service.

In the event of a foreclosure after a default, NRG's project subsidiary or project affiliate owning the facility would only retain an interest in the assets, if any, remaining after all debts and obligations were paid. In addition, the debt of each operating project may reduce the liquidity of NRG's equity interest in that project because the interest is typically subject both to a pledge securing the project's debt and to transfer restrictions set forth in the relevant financing agreements. Also, NRG's ability to transfer or sell its interest in certain projects is restricted by certain purchase options or rights of first refusal in favor of its partners or the project's power and steam purchasers and certain change of control restrictions in the project financing documents.

These project financing structures are designed to prevent the lenders from looking to NRG or its other projects for repayment (that is, they are "non-recourse" to NRG and its other project subsidiaries and project affiliates not involved in the project), unless NRG or another project subsidiary or project affiliate expressly agrees to undertake liability. NRG has agreed to undertake limited financial support for certain of its project subsidiaries in the form of certain limited obligations and contingent liabilities. These obligations and contingent liabilities take the form of guarantees of certain specified obligations, indemnities, capital infusions and agreements to pay certain debt service deficiencies. To the extent NRG becomes liable under such guarantees and other agreements in respect of a particular project, distributions received by NRG from other projects may be used by NRG to satisfy these obligations. To the extent of these obligations, creditors of a project financing may have recourse to NRG. The project financing structures therefore generally are described throughout this Offering Memorandum as being "substantially non-recourse" to NRG and its other projects.

NRG's facilities are insured in accordance with covenants in each project's debt financing agreements (if any) and in accordance with NRG's risk management policies. Coverage for each facility generally include workers' compensation, commercial general liability supplemented by primary and excess umbrella liability, and a master property insurance program including property, boiler and machinery (at replacement cost) and business interruption.

#### OPERATING ARRANGEMENTS

NRG operates each of the projects that it wholly owns or controls. Where NRG has only a minority interest and is not the operator of a project, NRG generally seeks the ability to exert a degree of influence with respect to operation of the project through its joint venture or similar agreement with its partners.

As a condition to participating in privatizations and refurbishments of formerly state-owned businesses, NRG may be required to undertake transitional obligations relating to union contracts, employment levels and benefits obligations for employees, which could delay the achievement of desirable operating efficiencies and financial performance.

#### SUMMARY OF NRG PROJECTS

As of November 21, 1997, NRG had interests in 38 operating power generation facilities worldwide (not including NEO and Energy Investors Funds or the El Segundo plant of Southern California Edison in which NRG signed an Asset Purchase Agreement for a 50% interest on November 21, 1997), including projects under construction. Of these facilities, 22 are located in the United States (1,275 MW design capacity, with NRG holding 378 MW net ownership), four are located in Germany (1,160 MW design capacity, with NRG holding 267 MW net ownership), four are located in Australia (4,106 MW design capacity, with NRG holding 1,270 MW net ownership), and two are located in Colombia (299 MW design capacity, with NRG holding 16 MW net ownership), and one is located in each of the Czech Republic (382 MW design capacity, with NRG holding 214 MW net ownership), Jamaica (74 MW design capacity, with NRG holding 7 MW net ownership), Peru (155 MW design capacity, with NRG holding 5 MW net ownership), Honduras (80 MW design capacity, with NRG holding 6 MW net ownership), Canada (110 MW design capacity, with NRG holding 28 MW net ownership), and Bolivia (218 MW design capacity, with NRG holding 126 MW net ownership). In December 1996, NRG and Vattenfall AB of Sweden acquired 96.6% of the outstanding common shares of Compania Boliviana de Energia Electrica SA -- Boliviana Power Company Limited ("COBEE"), the second largest electric utility company in Bolivia, which will have a design capacity of 218 MW after a 65 MW expansion in 1998. In addition, through its wholly-owned project subsidiary, NEO Corporation ("NEO"), NRG also had interests on November 21, 1997 in 39 small hydroelectric and landfill

gas-fired power generation facilities located in the United States with total design capacity of 113 MW, of which NRG has net ownership of 55 MW.

In addition to power generation, NRG has interests in four district heating and cooling systems, located in Minneapolis, San Francisco, Pittsburgh and San Diego, that provide steam for heating and chilled water for cooling. NRG also owns or operates two steam transmission facilities and two resource recovery/RDF facilities, all located in Minnesota. In connection with the PGC acquisition, NRG also owns interests in two additional resource recovery/RDF facilities in Maine. NRG also owns or leases interests in lignite mines in Germany estimated to contain reserves of approximately 789 million metric tons and in Australia estimated to contain resources equal to 2 billion tons.

Set forth in the two tables and the text below are descriptions of NRG's facilities in operation or under construction as of November 21, 1997.

INDEPENDENT POWER PRODUCTION AND COGENERATION FACILITIES(1)

NAME AND LOCATION OF FACILITY	DESIGN CAPACITY (MW) (2)	POWER PURCHASER
Loy Yang Power(4), Australia.....	2000	Victorian Pool
Gladstone Power Station, Australia.....	1680	QTSC; BSL
Collinsville, Australia.....	189	QTSC
Energy Development Limited, Australia.....	237	Various
Kladno Czech Republic, existing project.....	28	STE/Industrials
expansion project.....	354	STE
Schkopau Power Station, Germany.....	960	VEAG
MIBRAG mbH(4), (Mummsdorf) Germany.....	100	WESAG
MIBRAG mbH(4), (Deuben) Germany.....	60	WESAG
MIBRAG mbH(4), (Wahlitz) Germany.....	40	WESAG
COBEE, Bolivia.....	218 (9)	Electropaz/ELF
Latin Power (Mamonal), Colombia.....	100	Proelectrica
Latin Power (Termovalle), Colombia.....	199	EPSA
Latin Power (ELCOSA), Honduras .....	80	Empresa Nacional de Energia Electrica
Latin Power (Dr. Bird), Jamaica.....	74	Jamaica Public Service Company, Ltd.
Latin Power (Aguaytia), Peru .....	155	Central Peruvian Electricity Grid
NRGG (Parlin), New Jersey.....	122	Jersey Central Power & Light Company
NRGG (Newark), New Jersey.....	52	Jersey Central Power & Light Company
NRGG (Grays Ferry), Pennsylvania.....	150	PECO Energy Company
NRGG (Philadelphia Cogen),		Philadelphia

Pennsylvania.....	22	Municipal Authority
Pacific Generation Company (10) ...	737	
Camas Power .....	25 (12)	NA
Crockett Cogeneration .....	240	PG&E
Curtis-Palmer Hydro .....	58	NIMO
Kingston Cogeneration.....	110	Ontario Hydro
Maine Energy Recovery .....	22	CMP
Penobscot Energy Recovery .....	22	Bangor Hydroelectric Company
Mt. Poso Cogeneration .....	50	PG&E
PowerSmith Cogeneration .....	110	Oklahoma Gas & Electric
WindPower Partners 1987 .....	50	PG&E
WindPower Partners 1988.....	30	PG&E
Turners Falls .....	20	Unitil Power Company(13)
San Joaquin Valley (Madera), California.....	23	NA(14) (15)
San Joaquin Valley (Chowchilla II), California.....	10	NA(14) (15)
San Joaquin Valley (El Nido), California.....	10	NA(14) (15)

(RESTUBBED TABLE CONTINUED FROM ABOVE)

NAME AND LOCATION OF FACILITY	LATER OF DATE OF ACQUISITION OR DATE OF COMMERCIAL OPERATION	NRG'S PERCENTAGE OWNERSHIP INTEREST	TOTAL FACILITY COST (3) (IN \$ MILLIONS)
Loy Yang Power(4), Australia.....	1997	25.37	3,700 (5)
Gladstone Power Station, Australia.....	1994	37.50	532.0 (6)
Collinsville, Australia.....	1998	50.00	154.0
Energy Development Limited, Australia.....	1997	15.9	Listed company
Kladno Czech Republic, existing project.....	1994	34.00	NA(7)
expansion project.....	1999	57.85	401.0
Schkopau Power Station, Germany.....	1996	20.55	1,094.0 (6)
MIBRAG mbH(4), (Mumsdorf) Germany.....	1994	33.33	468.0 (4) (8)
MIBRAG mbH(4), (Deuben) Germany.....	1994	33.33	(8)
MIBRAG mbH(4), (Wahlitz) Germany.....	1994	33.33	(8)
COBEE, Bolivia.....	1996	48.30	174.6
Latin Power (Mamonal), Colombia.....	1994	6.45	71.0
Latin Power (Termovalle), Colombia.....	1998	4.88	145.6
Latin Power (ELCOSA), Honduras .....	1994	7.65	93.0
Latin Power (Dr. Bird), Jamaica.....	1995	8.78	98.0
Latin Power (Aguaytia), Peru .....	1998	3.28	256.0
NRGG (Parlin), New Jersey.....	1996	45.21	Listed company
NRGG (Newark), New Jersey.....	1996	45.21	Listed company
NRGG (Grays Ferry), Pennsylvania.....	1996	15.07	Listed company
NRGG (Philadelphia Cogen), Pennsylvania.....	1996	37.52	Listed company
Pacific Generation Company (10) ...	1997	100.00	151.3 (11)
Camas Power .....	1997	100.00	

Crockett Cogeneration .....	1997	24.87	
Curtis-Palmer Hydro .....	1997	8.50	
Kingston Cogeneration.....	1997	25.00	
Maine Energy Recovery .....	1997	16.25	
Penobscot Energy Recovery .....	1997	28.70	
Mt. Poso Cogeneration .....	1997	21.90	
PowerSmith Cogeneration .....	1997	8.75	
WindPower Partners 1987 .....	1997	17.00	
WindPower Partners 1988.....	1997	18.54	
Turners Falls .....	1997	8.90	
San Joaquin Valley (Madera), California.....	1992	45.00	45.8
San Joaquin Valley (Chowchilla II), California.....	1992	45.00	
San Joaquin Valley (El Nido), California.....	1992	45.00	

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NAME AND LOCATION OF FACILITY	DESIGN CAPACITY (MW) (2)	POWER PURCHASER
Jackson Valley Energy Partners, California(16).....	16	PG&E
Sunnyside Cogeneration Associates, Utah.....	58	PacifiCorp
Artesia, California.....	34	Southern California Edison
Cadillac Renewable Energy, Michigan.....	34	Consumers Energy
Millennium, Illinois.....	117	Millenium Petrochemicals, Inc.

(RESTUBBED TABLE CONTINUED FROM ABOVE)

NAME AND LOCATION OF FACILITY	LATER OF DATE OF ACQUISITION OR DATE OF COMMERCIAL OPERATION	NRG'S PERCENTAGE OWNERSHIP INTEREST	TOTAL FACILITY COST (3) (IN \$ MILLIONS)
Jackson Valley Energy Partners, California(16).....	1991	50.00	28.0
Sunnyside Cogeneration Associates, Utah.....	1994	50.00	139.4
Artesia, California.....	1996	2.96	40.0
Cadillac Renewable Energy, Michigan.....	1997	50.00	5.0 (17)
Millennium, Illinois(18).....	1998	50.00	91.0

- (1) Does not include the small hydroelectric and landfill gas-fired power generation facilities owned by NEO with an aggregate capacity of 72 MW, of which NEO has net ownership of 35 MW. In addition, NEO has landfill gas projects under construction with an aggregate capacity of 23.5 MW, of which NEO has net ownership of 11.8 MW.
- (2) Design capacity is without deduction for internally consumed power.
- (3) Except as otherwise indicated, total facility cost includes the total acquisition cost (purchase price plus assumed debt) where NRG has acquired an interest in an existing facility or the total construction

cost where NRG has acquired an interest in a facility under construction.

- (4) Each of Loy Yang and MIBRAG also owns coal mines which sell coal both to its respective power plant and to third parties.
- (5) Figures based on an acquisition cost of AUS\$4.7 billion, converted at an exchange rate of 0.7767.
- (6) Based on exchange rates in effect at the time of acquisition.
- (7) The existing Kladno facility was constructed over a number of years in former Czechoslovakia and no meaningful cost data are available.
- (8) This figure represents the total cost for the 3 generation facilities and the lignite mine reserves owned by MIBRAG. The purchase price includes a commitment to contribute DM 1 billion of additional capital made by MIBRAG at the time of the acquisition. In addition to the price stated above, MIBRAG is required to pay premiums to the German government based on the quantity of lignite and briquettes sold.
- (9) Includes the Zongo 65 MW expansion which will be operational in 1998.
- (10) In addition to the projects listed, PGC owns a limited partnership interest in the Energy Investors Funds through which it owns an allocated share equal to another 39 MW.
- (11) Figure based on total purchase price for PGC, not allocated between projects. Approxiamtely \$18 million of the purchase price is subject to confirmation by a post-closing audit.
- (12) The project does not generate electricity but its steam sales are the equivalent of 25 MW of electric power.
- (13) Operations of the project are currently suspended pursuant to an agreement with this power purchaser but it retains the right to require the project to start-up on six months' notice.
- (14) Operations suspended following buy-out of power purchase contracts and pending negotiation of new power purchase agreements or sale of such facilities.
- (15) PG&E has agreed to a buy-out of related power purchase agreements, but retains a right of first refusal with respect to output of facilities.
- (16) Operations were suspended during 1995 and 1996 pursuant to a restructuring of the power purchase agreement. Operations restarted on May 1, 1997.
- (17) In addition, NRG pays GE Credit Corporation rent under an operating lease for the facility.
- (18) In December 1997, NRG entered into an agreement to transfer this project to NRGG, subject to certain conditions precedent.

THERMAL ENERGY PRODUCTION AND TRANSMISSION FACILITIES  
AND RESOURCE RECOVERY FACILITIES

NAME AND LOCATION OF FACILITY	DESIGN CAPACITY(1)	THERMAL ENERGY PURCHASER/MSW SUPPLIER
Thermal Energy Production and Transmission Facilities Minneapolis Energy Center (MEC), Minnesota.....	Steam: 1,323 mmBtu/hr. (388 MWt) Chilled water: 35,550 tons/hr.	Approximately 90 steam customers and 30 chilled water customers
North American Thermal Systems (NATS), Pennsylvania; California.....	Pittsburgh: steam-- 240 mmBtu/hr. (70 MWt) chilled water-- 10,180 tons/hr. San Francisco: steam-- 490 mmBtu/hr. (144 MWt)	Approximately 24 customers in Pittsburgh and 210 customers in San Francisco
San Diego Power & Cooling..... Rock-Tenn Minnesota.....	Chilled Water: 5,250 tons/hr. Steam: 430 mmBtu/hr. (126 MWt)	Approximately 14 customers Rock-Tenn Company
Washco,	160 mmBtu/hr.	Andersen Corporation

Minnesota.....	(47 MWt)	Minnesota Correctional Facility
Grand Forks Air Force Base, North Dakota.....	105 mmBtu/hr. (31 MWt)	Grand Forks Air Force Base
Energy Center Kladno, Czech Republic(4) .....	512 mmBtu/hr. (150 MWt)	City of Kladno
Resource Recovery Facilities Newport, Minnesota.....	MSW: 1,500 tons/day	Ramsey and Washington Counties
Elk River, Minnesota(5).....	MSW: 1,500 tons/day	Anoka, Hennepin, and Sherburne Counties; Tri-County Solid Waste Management Commission

(RESTUBBED TABLE CONTINUED FROM ABOVE)

NAME AND LOCATION OF FACILITY	DATE OF ACQUISITION	NRG'S PERCENTAGE OWNERSHIP INTEREST	TOTAL FACILITY COST(2) (IN \$ MILLIONS)
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Thermal Energy Production and Transmission Facilities			
Minneapolis Energy Center (MEC), Minnesota.....	1993	100.00	110.0
North American Thermal Systems (NATS), Pennsylvania; California.....	1995	49.40 (3)	6.8
San Diego Power & Cooling.....	1997	100.00	6.7
Rock-Tenn Minnesota.....	1992	100.00	14.2
Washco, Minnesota.....	1992	100.00	5.2
Grand Forks Air Force Base, North Dakota.....	1992	100.00	2.2
Energy Center Kladno, Czech Republic(4) .....	1994	34.00	NA(4)
Resource Recovery Facilities Newport, Minnesota.....	1993	100.00	17.1
Elk River, Minnesota(5).....	NA(6)	0.00	NA(5)

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- (1) Thermal production and transmission capacity is based on 1,000 Btus per pound of steam production or transmission capacity. The unit mmBtu is equal to one million Btus.
  - (2) Total facility cost includes the total acquisition cost (purchase price plus assumed debt).
  - (3) Includes 0.5% general partnership interests in each of PTLP and SFTLP.
  - (4) Kladno also is included in the Independent Power Production and Cogeneration Facilities table on the preceding page.
  - (5) NRG operates the Elk River resource recovery facility on behalf of NSP.
  - (6) Not owned during this period.

INDEPENDENT POWER PRODUCTION AND COGENERATION

INTERNATIONAL PROJECTS

LOY YANG POWER



In May 1997, NRG consummated the largest acquisition in its history, acquiring a 25.37% interest in the assets of a 2,000 MW brown coal fired thermal power station and adjacent coal mine located in Victoria, Australia and known as Loy Yang A. The State of Victoria sold the Loy Yang A assets as part of its privatization program to a partnership called Horizon Energy Partnership ("HEP"), formed by affiliates of NRG and of CMS Generation (a wholly-owned subsidiary of CMS Enterprises), together with Horizon Energy Investment Limited (an investment vehicle of Macquarie Bank). NRG has a 25.37% interest in HEP through its wholly-owned project subsidiary, NRGenerating Holdings (No.4) B.V.

HEP purchased the Loy Yang A assets for a total price of approximately AUS\$4.7 billion (US\$3.7 billion, as of May 12, 1997). While most of that amount was raised through project-financed loans and leveraged leases that are non-recourse to the sponsors, NRG's equity investment was approximately US\$257 million. NRG provided that amount and related financing costs from the Bridge Financing, the equity investment by NSP and cash on hand. After the acquisition, HEP changed its name to "Loy Yang Power" ("Loy Yang").

Loy Yang owns and operates a 2,000 MW brown coal fired thermal power station (the "Power Station") and the adjacent Loy Yang coal mine (the "Mine") located in the Latrobe Valley, Victoria, Australia. The Power Station has four generating units, each with a 500 MW boiler and turbo generator, which commenced commercial operation between July 1984 and December 1988. In addition, Loy Yang manages the common infrastructure facilities which are located on the Loy Yang site, which service not only the Power Station, but also the adjacent Loy Yang B 1000 MW power station ("Loy Yang B"), a pulverized dried brown coal ("PDBC") plant, and several other nearby power stations.

Loy Yang is required by law to sell its entire output of electricity (subject to certain narrow exemptions, including output used in the Power Station and the Mine) through the competitive wholesale market for electricity operated and administered by the Victorian Power Exchange (the "Pool"). There are two components to the wholesale electricity market in Victoria. The first is the Pool. The second is the price hedging contracts, known as Contracts for Differences (or "CFDs"), that are entered into between electricity sellers and buyers in lieu of traditional power purchase agreements, which are not available in Victoria because of the Pool system.

Under the Victorian regulatory system, all electricity generated in Victoria must be sold and purchased through the Pool. All licensed generators and suppliers, including Loy Yang, are signatories to a pooling and settlement agreement, which governs the constitution and operation of the Pool and the calculation of payments due to and from generators and suppliers. The Pool also provides centralized settlement of accounts and clearing. Prices for electricity are set by the Pool daily for each half-hour of the following day based on the bids of the generators and a complex set of calculations matching supply and demand and taking account of system stability, security and other costs. Under a new national electricity market, the grid in Victoria has been interconnected with that of New South Wales and limited trading is already taking place between those states. Over the long term, there are plans for the interconnection of the eastern seaboard states to establish what will be known as a national power pool. There can be no assurance that NRG's assumptions concerning future market pricing will in fact be realized under this new system.

In a Pool system, it is not possible for a generator such as Loy Yang to enter into traditional power purchase agreements. In order to provide a hedge against Pool price volatility and also to support their financings, most of the Victorian generators have entered into CFDs with the Victorian distribution companies, Victorian government entities and industrial users ("customers"). These CFDs are financial hedging instruments which have the effect of fixing the price for a specified quantity of electricity for a particular seller and purchaser over a defined period. They establish a "strike price" for a certain volume of electricity purchased by the user during a specified period; differences between that "strike price" and

the actual price set by the Pool give rise to "difference payments" between the parties at the end of the period. Even if Loy Yang is producing less than its contracted quantity it will still be required to make and will be entitled to receive difference payments for the amounts set forth in its CFDs.

Loy Yang's current CFDs with the Victorian distribution companies and other Victorian government entities in respect of regulated customer load (which are called its "vesting contracts") cover approximately 73% of Loy Yang's forecast revenue from generation in the year ending June 30, 1997, thus providing considerable stability in its income over that period. Loy Yang also enters into CFDs with its unregulated or "contestable" customers; these CFDs are known as "hedging contracts" and, together with the vesting contracts with the regulated customers, they cover approximately 93% of Loy Yang's forecast load for the year ending June 30, 1997. Each of the vesting contracts expires at the end of the franchise period (December 31, 2000), by which time all retail customers will have become "contestable customers" by operation of law. Loy Yang's hedging contracts are generally for a term of one to two years, and the volume of load covered will increase as retail customers progressively become contestable. Loy Yang's goal is to cover 85% of its forecast load with these hedging contracts.

Loy Yang and the State Electricity Commission of Victoria (the "SECV") have been issued with a joint mining license for the Mine. Under the terms of the privatization, Loy Yang is required to mine coal to supply not only its own Power Station but also the neighboring Loy Yang B, a nearby PDBC plant, and an additional future power station that could be developed on a nearby site. This requirement extends to 2027, but may be extended for an additional 30 years at the SECV's option. Loy Yang receives a fixed capacity charge and a variable energy charge for these services, coupled with a system of initiatives and penalties. Loy Yang has over 70 years of economically viable coal supply at current usage rates within its mine license area, even assuming that it is required to continue supplying coal to the other parties beyond 2026.

As noted above, Loy Yang also manages certain common infrastructure facilities located on Loy Yang's site that service not only Loy Yang, but also Loy Yang B, the PDBC plant, and several other nearby power plants. These services provided include the supply of high quality water, low quality water, ash and waste disposal, drainage and steam.

#### GLADSTONE POWER STATION

Gladstone is a 1,680 MW coal-fired power generation facility located in Gladstone, Australia. NRG acquired a 37.5% ownership interest in Gladstone when the facility was privatized in March 1994. The other participants in this acquisition are subsidiaries or affiliates of Comalco Limited, Marubeni Corporation, Sumitomo Corporation and Sumitomo Light Metal Industries, Mitsubishi Corporation and Mitsubishi Materials Corporation, and Yoshida Kogyo (the "Participants"). NRG Gladstone Operating Services Pty. Ltd., another wholly-owned subsidiary of NRG ("NRG Gladstone"), operates the Gladstone Power Station under an operations and maintenance agreement expiring in 2011.

Gladstone sells electricity to the Queensland Transmission and Supply Corporation ("QTSC") and also to the Boyne Smelters Limited located at Boyne Island, Queensland ("Smelter"). Pursuant to an Interconnection and Power Pooling Agreement (the "IPPA"), the Participants have the right to interconnect Gladstone to the QTSC system and QTSC is obligated to accept all electricity generated by the facility (subject to merit order dispatch), for an initial term of 35 years. QTSC also has agreed under the IPPA to permit the Smelter to interconnect to the QTSC system and to provide sufficient generating capacity on its system in order to provide an uninterrupted supply of power to the Smelter in most circumstances. The Participants are obligated to maintain a 35% reserve margin for the Smelter design load, but the QTSC is

obligated to provide capacity support to the Participants to make up any shortfall between the available capacity from the GPS and the Smelter demand at any given time.

The QTSC also entered into a 35-year Capacity Purchase Agreement (a "CPA") with each of the Participants for its percentage of the capacity of Gladstone, excluding that sold directly to the Smelter. Under the CPAs, the Participants are paid both a capacity and an energy charge by the QTSC. The capacity charge is designed to cover the projected fixed costs allocable to the QTSC, including debt service and an equity return, and is adjusted to reflect variations in interest rates. A capacity bonus is also

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available if the Equivalent Availability Factor exceeds 88% on a rolling average basis, and damages are payable by the Participants if it is less than 82% on that same basis. As of September 30, 1997, the two-year average Equivalent Availability Factor was 88.4%. The QTSC also pays an energy charge, which is intended to cover fuel costs.

The owners of the Smelter ("BSL") have also entered into a Block A PPA with each Participant, providing for the sale and purchase of such Participant's percentage share of capacity allocated to the existing Smelter. BSL has also entered into a Block B PPA with each Participant, providing for the sale and purchase of such Participant's percentage share of capacity allocated to the third production line of the Smelter which is currently being commissioned. The term of each of these PPAs is 35 years. BSL is obligated to pay to each Participant a demand charge that is intended to cover the fixed costs of supplying capacity to the existing Smelter and the Smelter expansion, including debt service and return on equity. BSL also is obligated to pay an energy charge based on the fuel cost associated with the production of energy from the facility. NRG anticipates that the Smelter expansion will result in an increase in Gladstone capacity utilization from approximately 41% in 1994 to an estimated 70% in 1998.

NRG Gladstone is responsible for operation and maintenance of Gladstone pursuant to a 17-year Operation and Maintenance Agreement that commenced in 1994. NRG Gladstone is entitled to a base fee of AUS\$1.25 million per year indexed in accordance with Australian CPI (approximately \$1.0 million, based on exchange rates and ACPI in effect at September 30, 1997), and an annual bonus based on the capacity bonuses to which the Participants are entitled under the CPAs. NRG Gladstone is obligated to pay liquidated damages for shortfalls in availability in an amount calculated by reference to the liquidated damages payable by the Participants under the CPAs and the PPAs. NRG Gladstone's obligations under the Operation and Maintenance Agreement are unconditionally guaranteed by NRG, subject to an aggregate liability cap of AUS\$25 million indexed in accordance with ACPI (approximately \$19.7 million, based on exchange rates and ACPI in effect at September 30, 1997).

In the event the Gladstone facility fails to deliver sufficient power for the Smelter and no back up power is available from the QTSC, molten aluminum in the Smelter can solidify, resulting in a shutdown of the Smelter for a substantial period of time. If the failure to deliver power to the Smelter is caused by the willful default of QTSC or the Participants (but not NRG Gladstone), the Participants may become liable to pay liquidated damages, including compensation to BSL for lost profits, which are not capped. QTSC has agreed to indemnify NRG's project subsidiaries and the other Participants for any liability to the owners of the Smelter arising as the result of a willful default by QTSC with regard to its obligations to deliver power to the Smelter, subject to certain mitigation obligations of NRG's project subsidiaries and the other Participants. If such failure is due to the willful default of NRG Gladstone, NRG may become liable, under its guarantee of NRG Gladstone's obligations, to pay liquidated damages up to AUS\$25 million indexed in accordance with ACPI (approximately \$19.7 million, based on exchange rates and ACPI in effect at September 30, 1997). In addition, in the event NRG Gladstone is terminated for cause under the Operation and Maintenance Agreement, the other Participants can require a sale of NRG's equity interest.

Coal costs for operation of Gladstone generally are passed through to QTSC and BSL via the energy charges under the IPPA and the BSL Power Purchase Agreements. Until 2005, coal will be supplied to Gladstone by QTSC through on-sale agreements between QTSC and the Participants. An umbrella coal haulage agreement between the Participants and Queensland Railways provides for the transportation of coal by rail from the existing sources and from future coal sources for 30 years, with rail freight costs generally being passed through to QTSC and BSL via the energy charge payable to the Participants. The Participants have arranged for ash disposal from the facility pursuant to an ash management agreement with the Gladstone Port Authority, the City of Gladstone and Queensland Railways.

The acquisition of the GPS by the Participants was financed pursuant to an AUS\$625 million (US\$443 million at exchange rates in effect at the time) secured term loan and letter of credit facility provided by a consortium of international banks arranged by Barclay's Bank plc. The debt is non-recourse to NRG and the other owners of the Participants.

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Queensland is in the process of converting its electricity generation system in order to participate in the national power pool under development in Australia. In connection with that conversion, the Participants have engaged in discussions with BSL and various Queensland governmental entities regarding a restructuring of the project to make it more compatible with the new electricity market. Those negotiations are in an intermediary stage, and NRG expects the restructuring to take several months. Meanwhile, NRG, the Participants and BSL have agreed on certain principles regarding restructuring, including the following principles: (a) none of the parties will be any worse off as a result of the restructuring, taking into account all risk and financial perspectives; (b) it is preferable to have restructuring outcomes that are consistent with the operation of the new electricity market, rather than outcomes that are exceptions; (c) where opportunities arise in the restructuring, the benefits from superior management of risk will be recognized; and (d) benefits arising from the restructuring will be shared equitably after taking into account any reallocation of risk.

NRG's equity in earnings from its 37.5% interest in the GPS was \$7.7 million for the nine months of ownership in 1994. Equity in earnings for the twelve months ended December 30, 1995, was \$11.2 million, and for the same period in 1996 was \$10.8 million. For the nine months ending September 30, 1997, equity in earnings was \$8.7 million and for the same period in 1996 was \$8.5 million.

#### COLLINSVILLE POWER STATION

The Collinville Power Station ("Collinville") is a 189 MW coal-fired power generation facility located in Collinville, Australia. In March 1996, NRG acquired a 50% ownership interest in Collinville when the facility was privatized by the Queensland State government. NRG's partner in this acquisition is Transfield Holdings Pty Ltd, an Australian infrastructure contractor, with which NRG formed an unincorporated joint venture to refurbish this plant. The operation and maintenance of the facility will be undertaken by Collinville Operations Pty Ltd, a 50% owned subsidiary of NRG which has entered into a technical services agreement with NRG for some staffing and assistance with certain operational and maintenance functions.

Both NRG and Transfield have entered into an 18-year PPA with the QTSC, each agreeing to make available and sell to the QTSC its respective proportion of the capacity of Collinville. Under the PPA, NRG is paid both a capacity and an energy charge by the QTSC. The capacity charge is designed to cover the projected fixed costs allocable to the QTSC, including debt service, permitted capital costs incurred by NRG in carrying out additional works on the facility and an equity return. The capacity charge is adjusted to reflect variations in interest rates. A capacity bonus is also available. The QTSC also pays NRG an energy charge, which is intended to cover fuel

costs. Further, in accordance with its take-or-pay obligations, the QTSC must pay NRG its energy charges for an annual minimum quantity of energy in each year, less energy taken by the QTSC in that relevant year.

As of September 1997, the refurbishment of the Collinsville Project is on schedule and within the budget. For each day the capacity test of the facility is delayed past March 1, 1998, NRG and Transfield must pay liquidated damages to the QTSC. Liquidated damages will also be payable if the capacity of the power plant is determined to be less than 177.25 MW. Total liquidated damages which NRG and Transfield can be required to pay to the QTSC under the PPA are limited to AUS\$5 million (indexed in April 1995 dollars).

The refurbishment of the Collinsville Power Station has been financed with nonrecourse commercial project financed bank debt. NRG has guaranteed to the QTSC that its Collinsville project subsidiary will satisfy its equity contribution obligations to the project lenders. This \$13.4 million equity contribution is expected to be made in the second quarter of 1998.

#### ENERGY DEVELOPMENTS LIMITED

On February 6, 1997, NRG, through its wholly-owned subsidiary NRG Victoria III Pty Ltd., signed a subscription agreement with EDL to acquire up to 20% of EDL's common stock at AUS\$2.20 (US\$1.71 as of May 22, 1997) per share, and was granted an option to acquire 16.8 million convertible non-voting

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preference shares at AUS\$2.20 per share. The preference shares do not become convertible into EDL's common stock unless a takeover bid is made for EDL by a person who is not an affiliate of the owner of the preference shares and such person is, or becomes, entitled to purchase more than 35% of EDL's outstanding common stock. In such event, if EDL fails to comply with an obligation to appoint directors nominated by the owner of the preference shares, the preference shares convert at the option of the owner to common shares of EDL on a share-for-share basis. On February 11, 1997, NRG made an initial purchase of 7.2% (4.5 million shares) of EDL's common stock for AUS\$9.9 million (US\$7.9 million on that date). On September 24, 1997, NRG purchased an additional 10,109,670 shares of common stock of EDL for an aggregate purchase price of AUS\$22.2 million (US\$16.1 million on that date), bringing NRG's ownership level to 20% of the outstanding shares of EDL.

EDL, an Australian company, is engaged in independent power generation from landfill gas, coal seam methane, and natural gas (including projects that utilize the latest combined cycle technology). EDL currently owns approximately 149 MW of operating projects and operates over 200 MW of generation capacity across five states and territories of Australia. EDL has commenced the development of new projects in the United Kingdom, Asia and New Zealand. EDL is a publicly traded company listed on the Australian Stock Exchange. Its share price as of December 1, 1997 was AUS\$2.60 (US\$1.76 as of September 24, 1997).

#### SCHKOPAU POWER STATION

In 1993, NRG and PowerGen plc of the United Kingdom each acquired a 50% interest in a German limited liability company, Saale Energie GmbH ("Saale"). Saale then acquired a 41.1% interest in a 960 MW coal-fired power plant that was under construction in Schkopau, which is located in the former East Germany. A German energy company, VEBA Kraftwerke Ruhr AG ("VKR"), owns the remaining 58.9% interest in Schkopau and operates the plant. The partnership of Saale and VKR that owns the plant is called Kraftwerk Schkopau GbR ("KS").

The first 425 MW unit of the Schkopau plant began operation in January 1996, the 110 MW turbine went into commercial operation in February 1996, and the second 425 MW unit came on line in July 1996. Acceptance testing of all of the individual pieces of equipment has been completed. The plant has generally experienced good availability since the beginning of commercial operation and is expected to continue meeting its design reliability and

efficiency requirements.

VKR operates and maintains the Schkopau facility under an operation and maintenance contract with Kraftwerk Schkopau Betriebsgesellschaft mbH, a German limited liability company ("KSB"), in which Saale and VKR hold interests of 44.4% and 55.6% respectively, and which is responsible for the operation and maintenance of the facility pursuant to certain agreements with each of Saale and VKR. VKR is paid a management fee for such services made up of several variable components that will be adjusted according to changes in, among other things, labor costs, producer prices for light fuel oil and prices for electricity. Pursuant to the KSB partnership agreement between Saale and VKR and the Saale shareholders agreement between NRG and PowerGen, NRG has the right to participate in the oversight of facility operations and in the approval and oversight of facility budgets and policies.

The plant is fueled by brown coal (lignite) which will be provided under a long-term contract by MIBRAG's Profen lignite mine. For a description of the coal supply agreement between MIBRAG and the Schkopau project, see "MIBRAG", below.

Pursuant to the KS partnership agreement between Saale and VKR, each partner has been allocated a share of capacity and energy generated by the facility. Saale sells its allocated 400 MW portion of the plant's capacity under a 25-year contract with VEAG, a major German utility which controls the high-voltage transmission of electricity in the former East Germany. VEAG pays a price that is made up of three components, the first of which is designed to recover installation and capital costs, the second to recover operating and other variable costs, and the third to cover fuel supply and transportation costs. NRG receives 50% of the net profits from these VEAG payments through its ownership interest in Saale.

The construction of the Schkopau facility was financed through a combination of capital contributions from Saale and VKR, and borrowings by KS from VKR and from third party lenders, which are

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non-recourse to NRG. Saale financed a portion of its capital contributions through a line of credit from VKR. Saale's interests in KS and the facility are pledged as security for, among other obligations, the repayment of these borrowings by Saale from VKR. As of September 30, 1997, KS had borrowed an aggregate of DM 1.5 billion (approximately \$852.4 million based on exchange rates in effect as of September 30, 1997) and Saale had borrowed an aggregate of DM 34.2 million (approximately \$19.4 million, based on exchange rates in effect as of September 30, 1997).

NRG, PowerGen and VKR have also entered into a cooperation agreement concerning the participation of VKR in the acquisition or construction of certain large power station projects involving NRG and/or PowerGen in the Federal Republic of Germany.

Earnings from the Schkopau facility commenced in the first quarter of 1996 when the first unit was brought on-line. Equity in Schkopau earnings was \$4.6 million for the year ended December 31, 1996 and \$3.8 million for the nine months ended September 30, 1997.

#### MIBRAG

In 1994, NRG, Morrison Knudsen Corporation and PowerGen plc each acquired a 33% interest in a Dutch holding company which then acquired the equity of Mitteldeutsche Braunkohlengesellschaft mbH ("MIBRAG") which owns the coal mining, power generation and associated operations of MIBRAG, all of which are located south of Leipzig, Germany. The German government retained a 1% interest in MIBRAG until December 1996, when each of the three original investor parties were permitted to purchase one third of that interest. The investor partners began operating MIBRAG effective January 1, 1994, and the legal closing occurred August 11, 1994.

MIBRAG is a corporation formed by the German government following the reunification of East and West Germany, to hold two open-cast brown coal (lignite) mining operations, a lease on an additional mine, three lignite-fired industrial cogeneration facilities and briquette manufacturing and coal dust plants, all located in the former East Germany. In connection with the acquisition, NRG and its partners agreed to invest (from cash flow from MIBRAG operations) in excess of DM 1 billion (US\$568 million based on the exchange rate as of September 30, 1997) by December 31, 2004 to modernize the existing mines and power generation facilities and to develop new open-pit mines. The German government is obligated to provide certain guarantees of bank loans to MIBRAG relating to capital improvements to the Schleenhain mine. MIBRAG also agreed to operate the three power generation facilities until 2005, to operate the briquette plants in accordance with market demand until 2005, and to operate the lignite mines until continued operation of the mines is no longer economically justifiable. In addition, MIBRAG has made certain employee retention commitments until 2000. Under the provisions of the sale and purchase agreement, NRG and its partners agreed to make a deferred payment of DM 40 million to the German government in the year 2009. This obligation will be reduced by certain costs incurred by MIBRAG. The remaining obligation at September 30, 1997 was DM 22.0 million (or US\$12.5 million based on the exchange rate on September 30, 1997). NRG expects the entire obligation will be offset by ongoing costs prior to the year 2009.

MIBRAG's cogeneration operations consist of the 100 MW Mumsdorf facility, the 60 MW Deuben facility and the 40 MW Wahllitz facility. These facilities provide power and thermal energy for MIBRAG's coal mining operations and its briquette manufacturing plants. All power not consumed by MIBRAG's internal operations is sold under an eight-year power purchase agreement with Westsächsische Energie Aktiengesellschaft ("WESAG"), a recently privatized German electric utility. NRG and PowerGen jointly, through Saale, provide consulting services for a fee for the operation of the MIBRAG steam and power generation facilities, the associated electrical and thermal transmission and distribution system and the briquette manufacturing plants, under a power consultancy agreement with MIBRAG for the life of the facilities. After some retrofitting was completed by MIBRAG, all three of these cogeneration facilities now satisfy the current European Union environmental regulations. MIBRAG leases these cogeneration facilities under a 13-year lease pursuant to which MIBRAG has operating control of and a 1% interest in the facilities.

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MIBRAG's lignite mine operations include Profen, Zwenkau and Schleenhain (which is under construction but has not yet commenced operations), with total estimated reserves of 776 million metric tons. Morrison Knudsen, an international mining company, provides consulting services to mines under a consultancy agreement with MIBRAG for the life of the mines. In addition to providing approximately 3 million tons of lignite per year for MIBRAG's three cogeneration facilities and one briquette facility, output from these mines supply lignite to the Schkopau power station and other facilities. The total output of the new Schleenhain mine will be dedicated to the new 1600 MW Lippendorf power station. MIBRAG is currently supplying coal for the existing Lippendorf and Thierbach power generation facilities, but they are expected to close in 1999 when the new Lippendorf facility is scheduled to commence operations.

In addition to its power generation and coal mining operations, MIBRAG owns and operates two briquette manufacturing plants and a coal dust plant. Operations at the Deuben briquette plant were phased out as anticipated in 1996 due to reduced market demand for briquettes. MIBRAG also partially owns and is the principal customer of a transportation company, an insurance brokerage firm, a briquette marketer, a waste disposal and management company, a ground water consulting company and an environmental consulting company.

MIBRAG is restricted from selling or transferring certain assets without the consent of the German government, generally for a period ending not earlier than January 2004. Even if consent is obtained, MIBRAG is obligated

to pay a portion of the proceeds of any sale or transfer of such assets consummated before January 2004 to the German government.

To the extent liabilities arise with respect to environmental conditions existing at the time of the acquisition, MIBRAG is indemnified by the German government, subject to certain limitations. The German government has also agreed to indemnify MIBRAG in respect of certain liabilities arising from claims for the restitution of property allocated to MIBRAG.

MIBRAG has entered into several long-term loan agreements with the Kreditanstalt fur Wiederaufbau ("KfW"), which is the German government economic development bank. Approximately DM 126.7 million (\$72.0 million as of September 30, 1997) of these loans relate to the construction of the Wahlitz power station and were assumed as part of the MIBRAG acquisition on January 1, 1994. In January 1996, MIBRAG borrowed an additional DM 94.5 million (\$53.7 million as of September 30, 1997) from KfW and DM 112.5 million (\$113.4 million as of September 30, 1997) from a group of private investors. The proceeds from these loans are being used in respect of the refurbishment of the Schleenhain mine. These loans are payable out of project revenues over a period of 13 years and are non-recourse to the three sponsors. Additional acquisition payments are due to the German government in the form of premiums based on the quantity of lignite and briquettes sold. MIBRAG has also borrowed an additional DM 90 million (\$51.1 million as of September 30, 1997) from the KfW to partially finance the modernization and refurbishment of the Deuben and Mumsdorf plants, particularly the cost of bringing them into compliance with environmental requirements. This loan is also non-recourse to the sponsors.

NRG's equity in earnings from its interest in MIBRAG was \$19.4 million in the year ended December 31, 1994 (reflecting a full twelve months of operations). NRG's equity in earnings in MIBRAG for the twelve months ended December 31, 1995, was \$22.2 million, and for the same period in 1996 was \$13.1 million. Similarly, for the nine months ending September 30, 1997 was \$7.0 million, and for the same period in 1996 was \$7.6 million. Earnings from MIBRAG decreased in 1996 and are expected to continue to decrease in 1997 and 1998 due to mine refurbishments and reduced coal sales. However, in 1999, coal sales are expected to increase substantially with the scheduled startup of the first of two 800 MW Lippendorf generating units.

MIBRAG's results of operations, which are reported under German accounting rules, are adjusted for purposes of NRG's financial statements to reflect GAAP. Such adjustments include, among others, adjustments for differences in reporting of depreciation expense, mining reserves, vacation reserves and maintenance reserves.

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The following chart represents the ownership structure of MIBRAG and Schkopau:

[CHART OF OWNERSHIP STRUCTURE OF MIBRAG AND SCHKOPAU]

COBEE

In December 1996, NRG acquired an interest in Compañia Boliviana de Energia Electrica S.A. -- Bolivian Power Company Limited ("COBEE"), the second largest generator of electricity in Bolivia. The acquisition was consummated through a Netherlands corporation, Tosli Investments B.V. ("Tosli"), which is jointly owned by subsidiaries of NRG (60%) and Vattenfall AB of Sweden (40%). As of October 30, 1997, the ownership of Tosli changed to 50% for each of NRG and Vattenfall AB due to the sale of 10% of Tosli to Vattenfall AB from NRG. On December 19, 1996, Tosli completed a successful tender offer for the shares of COBEE, which were listed on the New York Stock Exchange, acquiring 96.6% of COBEE's outstanding common shares for a total of \$175 million. COBEE shares were delisted in January 1997.



Tosli financed its acquisition of COBEE in part using the proceeds of a \$49.6 million bridge loan arranged by Morgan Grenfell & Co. Limited, as administrative agent. The unpaid principal amount of that loan of \$30 million was repaid in full on June 19, 1997 using the proceeds of a loan from NRG to Tosli. On August 13, 1997, COBEE entered into a Credit Agreement with Corporacion Andina de Fomento (the "CAF Financing") for \$75 million to fund the completion of the Zongo Project, as described below. Upon funding of the CAF Financing, COBEE will declare and pay a dividend to Tosli and COBEE's minority shareholders. The dividend received by Tosli will be used to pay the amounts due on the NRG loan.

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Upon Tosli's acquisition of COBEE, the COBEE board of directors was reconstituted to include nine members, including four designees of NRG, three designees of Vattenfall and two outside directors. On October 30, 1997 the membership of the COBEE board of directors was adjusted to reflect the equal ownership of COBEE by NRG and Vattenfall. The COBEE board of directors now consists of three designees of NRG, three designees of Vattenfall and three directors appointed jointly by NRG and Vattenfall. In addition, in December 1996, the Chief Executive Officer of NRG was elected as chairman of the board of directors and chief executive officer of COBEE.

COBEE generates and transmits electricity in La Paz and Oruro, Bolivia, and owns 14 generating facilities representing an installed capacity of approximately 153 MW. These facilities consist of 136 MW of hydroelectric capacity and 17 MW of gas peaking capacity. During 1996, COBEE had electricity sales of \$20 million. In 1996, two distribution companies, Electropaz and ELF, accounted for approximately 69% and 16%, respectively, of COBEE's revenues. The remaining COBEE revenues are derived from sales on the spot market.

COBEE has entered into an Electricity Supply Contract with Electropaz which provides that COBEE shall supply Electropaz with all of the electricity that COBEE can supply, up to the maximum amount of electricity required by Electropaz to supply the requirements of its distribution concession. This Electricity Supply Contract expires in December 2008. COBEE has entered into a substantially similar contract with ELF. Electropaz and ELF are both wholly-owned subsidiaries of Ibedrola S.A., a Spanish utility company. All payments by Electropaz and ELF are in local currency, tied to the value of the U.S. dollar.

COBEE operates its electric generation business under a 40-year Concession granted by the Government of Bolivia in 1990, as most recently amended in March 1995. Under this Concession, COBEE is entitled to earn a return of 9% after all operating expenses, depreciation, taxes and interest expense, calculated on its U.S. dollar rate base, consisting of net fixed assets at historical cost in U.S. dollars and working capital and materials up to certain limits. The Bolivian Electricity Code also provides for the adjustment of rates to compensate COBEE for any shortfall or to recapture any excess in COBEE's actual rate of return during the previous year. COBEE periodically applies to the Superintendent of Electricity for rate increases sufficient to provide its 9% rate of return based on COBEE's current operating results and its projection of future revenues and expenses.

Its Concession also obligates COBEE to expand its hydroelectric generation capacity. As a result, COBEE has an additional 65 MW of new hydroelectric facilities under construction in the Zongo Valley. This expansion, which COBEE refers to as the "Zongo Project," consists of adding new generation facilities and modernizing existing facilities in the Zongo Valley and constructing transmission lines to transmit the increased generation capacity. The Zongo Project is scheduled to be completed in 1998 and is expected to add a total of 65 MW to COBEE's generating capacity.

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Under the terms of the Concession, COBEE also has the right to expand its facilities in the Miguillas Basin (the "Miguillas Project") which, if

completed, may add up to 200 MW of generation capacity. In accordance with its obligations under the Concession, in late 1995 COBEE presented to the Government a technical-economic feasibility study. COBEE fully expects to proceed with the construction of Miguillas in accordance with a proposal and schedule submitted to the Bolivian government in December 1996. COBEE's proposal still awaits regulatory approval from the Superintendent of Electricity in Bolivia.

There can be no assurance that any or all of the projects under development by COBEE will be completed.

Equity in earnings from COBEE were \$0.1 million for the twelve days ended December 31, 1996 and \$1.3 million for the nine months ended September 30, 1997. Also, on October 30, 1997, NRG recorded the sale of a portion of its investment in COBEE reducing its ownership to 48.3%.

#### KLADNO

The Energy Center Kladno project, located in Kladno, the Czech Republic, consists of two distinct phases. In 1994, NRG acquired an interest in the existing coal-fired electricity and thermal energy generation facility that can supply 28 MW of electrical energy and 150 MWT of steam and heated water. This plant has historically supplied electrical energy to a nearby industrial complex which includes the Poldi Steel works (which is currently shut down and undergoing reorganization), and to Stredoceska Energeticka ("STE"), the local regional electric distribution company. In addition, the existing plant supplies steam and heated water to the industrial complex and to the City of Kladno. NRG's interest in the existing project is 34%.

The second phase is the expansion of the existing project by the addition of 354 MW of new capacity, 282 MW of which will be coal-fired and 72 MW of which will be gas-fired. As a part of this effort, the existing plant will be refurbished.

The existing project is owned by a company called Energy Center Kladno ("ECK"), in which NRG owns 34%, El Paso Energy International Company ("El Paso") owns 19% and local partners own the balance of 47%. The expansion project is held separately through ECK Generating ("ECKG"), a Czech limited liability company of which 89% is owned by a Netherlands company called Matra Powerplant Holding B.V. ("Matra") and 11% is owned by STE. NRG owns 65% of Matra and El Paso owns the remaining 35%. As a result, NRG has a net ownership interest in the expansion plant of 57.85%. Each of NRG and El Paso has granted Nations Energy (a subsidiary of Tucson Electric) an option to acquire 15% of Matra at any time before May 1998. If Nations Energy does not exercise its option with NRG, NRG intends to sell down its interest in Matra until its ownership interest in ECKG is less than 50%. The following charts represent the ownership structure of ECK and ECKG:

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[CHART OF ECK]

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ECK has leased all of the existing power generation facilities to ECKG pursuant to a 40-year lease. NRG, through a wholly-owned subsidiary, has responsibility for operating both the ECK assets and the new facilities. During construction ECKG will continue to service ECK's existing customers. When the new facilities are built ECKG will sell the additional capacity to

STE under a 20 year power sales agreement, at a price tied to STE's cost of purchasing power from CEZ, the state-owned power generation entity.

Construction of the new facilities started in early 1997, and in May 1997 ECKG signed loan documents to provide financing for the project. Construction is currently scheduled to be completed in 1999. All project debt is nonrecourse to NRG.

As of September 30, 1997, the Company has incurred \$9.5 million of development costs for the ECKG project. In addition, the purchase price paid by NRG for the acquisition of its interest in ECK has been capitalized to investments in projects.

#### LATIN POWER

Latin Power is an investment fund that was formed in July 1993 to make equity investments in independent power projects in Latin America and the Caribbean. NRG, the International Finance Corporation (a member of the World Bank Group), Corporation Andina de Fomento (a multilateral institution for the Andean region headquartered in Caracas, Venezuela) and CMS Generation Co. (the independent power subsidiary of CMS Energy) are the four lead investors in Latin Power. Each of the four lead investors has committed \$25 million to Latin Power and has designated Scudder, Stevens & Clark, Inc. ("Scudder") as the investment manager of the fund.

As of September 30, 1997, NRG had invested \$14.7 million of its \$25 million commitment in Latin Power portfolio project investments. NRG has also committed to fund projects in Peru and Colombia, which will be drawn down during 1997 and 1998. For the balance of the \$25 million the Latin Power project committee recently approved two investments in power generation facilities in Guatemala and Brazil. NRG's proportional investments in these projects, which have not yet commenced construction, will be approximately \$1.9 million and \$550,000 respectively.

Latin Power generally makes equity investments in private sector independent power projects located in Latin America and the Caribbean that sell power under long-term contracts to industrial users or to distribution and transmission companies. The fund also may invest in transmission, distribution or related operations. Latin Power currently holds investments in five projects. The Mamonal project is a 100 MW combined-cycle natural gas-fired power generation facility plant operating near Cartagena, Colombia. The facility is owned by K&M Engineering and Consulting, Bank of Boston, Rockefeller Group and Latin Power, which purchased a limited partnership interest in the partnership that owns the facility in 1994 for \$7.6 million. Total project debt is \$57 million, which is non-recourse to the facility owners. The Overseas Private Investment Corporation ("OPIC") insurance covers certain political and currency risks.

In November 1994, Latin Power purchased a 31% interest in the ELCOSA power generation facility in Puerto Cortes, Honduras. ELCOSA is an oil-fired facility with 80 MW of generating capacity, which the facility sells pursuant to a 15-year power purchase agreement to Empresa Nacional de Energia Electrica. The Honduran government has guaranteed the utility's obligations under the power purchase agreement. The Multilateral Investment Guarantee Association is providing insurance for Latin Power's equity investment against expropriation, political violence and certain currency risks.

In December 1995, Latin Power purchased a 35.1% interest in Jamaica Energy Partners, which owns the 74 MW Dr. Bird floating diesel-fired power generation facility. The facility is installed and operating at Old Harbour on the southern coast of Jamaica near Kingston. Jamaica Public Service Company, Ltd. has signed a 20-year power purchase agreement with Jamaica Energy Partners.

In July 1996, Latin Power assumed a 14.5% ownership interest in the Aguaytia power project in Peru which, when constructed, will be a 155 MW gas-fired power plant. When completed, Aguaytia will sell its output to the Peruvian power pool.

In October 1996, Latin Power purchased a 19.5% limited partnership interest in the 199 MW combined cycle Termovalle project near Cali, Colombia. Commercial operation of Phase I (130 MW simple cycle) is expected in August 1997 and of Phase II (199 MW combined cycle) in May 1998. Empresa de Energia del Pacifico (EPSA), a state-owned generation, transmission and distribution company, has entered into a PPA for 160 MW of generating capacity from the project. Industrial purchasers in the Cali area have committed to purchase the remaining power capacity.

In late 1996, NRG expressed an interest in making an additional investment in Latin Power II, a new Latin Power fund. Assuming NRG formally commits to the Latin Power II investment, NRG's aggregate commitment in Latin Power from \$25 million to \$32.5 million.

NRG's equity in earnings from its interest in Latin Power was \$1.6 million for the year ended December 31, 1996. For the nine months ended September 30, of 1997, equity in earnings were \$0.1 million compared with \$1.4 million for the nine months ended September 30, 1996.

#### DOMESTIC PROJECTS

#### PACIFIC GENERATION COMPANY

On November 4, 1997, NRG acquired 100% of the outstanding shares of Pacific Generation Company ("PGC"), a wholly-owned indirect subsidiary of PacifiCorp Company, Inc. for \$151.3 million and the assumption of debt of \$13.2 million. PGC has ownership interests in 11 projects with a total capacity of 737 MW, with operational responsibility for 312 MW and net ownership interests of 166 MW. In addition, PGC owns a 3.1% limited partnership interest in the Energy Investors Funds, through which it owns an additional allocated share equal to another 39MW.

One of PGC's projects is located in Canada and the other ten are broadly distributed throughout the United States. The three largest projects are gas-fired, but the others are fueled by coal, hydro, waste wood, refuse-derived fuel and wind. One sells only steam, while the other ten have power sales agreements with a total of seven different utilities. PGC serves a variety of roles in these facilities, ranging from operator/manager of three projects, including its largest asset, Crockett Cogeneration, to a limited partner in other projects.

Crockett Cogeneration. PGC is the sole general partner in and the operator of the 240 MW Crockett Cogeneration project ("Crockett"), which commenced operations in May, 1996. The project sells 240 MW of capacity and electric power to Pacific Gas & Electric Company under a power purchase agreement extending to 2026. The agreement provides for a fixed capacity payment and a variable energy payment based on the market price of gas. A Third Amendment to this agreement was executed this year, and is awaiting approval by the CPUC; this amendment resolved certain disputes that had arisen between the parties relating to: (i) the required level of delivery if Pacific Gas & Electric Company dispatches the facility at 100% and (ii) the right to dispatch under principles of economic dispatch. In addition, Crockett provides up to 450,000 lbs/hr. of steam to the C&H sugar refinery under a steam sales agreement that does not expire until 2026.

Natural gas is supplied to the Project by Amoco Canada Marketing Corp. under a fifteen year contract, with performance guaranteed by Amoco Canada Petroleum Company Ltd. PGC operates the Project under a 15 year contract that provides for reimbursement of all costs within an approved budget, plus a fee and the possibility of a performance bonus.

PGC holds the sole one percent general partnership interest in the Crockett Project, as well as a 23.87 percent limited partnership interest, which will increase to 56.68 percent after certain conditions of payment to the other limited partners have been satisfied. Those partners are the Energy

Investors Fund and Tomen Investments. The Crockett Project was financed with a \$278 million construction and term loan facility provided by a commercial bank syndicate led by ABN-AMRO, which will mature on December 31, 2010.

Kingston Cogeneration. Kingston, the only PGC project located outside of the United States, is a 110 MW combined cycle gas turbine project in Ontario, Canada. The Project commenced operation in

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1996. It sells power to Ontario Hydro under a 20-year PPA, which provides for a fixed capacity payment and a variable energy payment, provided the plant meets certain operating targets. Up to 150,000 lbs/hr. of thermal energy is sold to Hoechst-Celanese and gas is supplied under a 20-year agreement with PanCanadian Petroleum Limited.

PGC has a 25% general partnership interest in this project, but it is operated by AES. The Project was financed with a C\$193.6 million construction and term loan led by Bank of Nova Scotia and Credit Suisse, which will mature in March 2013.

PowerSmith Cogeneration. The third PGC gas-fired project is PowerSmith Cogeneration, a 110 MW combined cycle gas turbine project. Smith Cogeneration is the managing general partner of the project and GE is the operator. The PowerSmith Project sells its power to Oklahoma Gas and Electric under a contract expiring in 2004, and its steam to Dayton Tire for the same term. PGC has a total of 8.75% general and limited partnership interests until 2003, which is then decreased automatically to a 6.25% ownership interest thereafter.

Maine Energy Recovery Project ("MERC"). MERC is a 680 ton per day waste-to-energy facility located in Biddeford, Maine. The annual throughput of municipal solid waste is approximately 200,000 tons and income is received from the disposal or "tipping" fees paid by communities utilizing this service. The facility sells its 22 MW output to Central Maine Power under a 20-year PPA, which was restructured in May 1996 to provide for energy-only rates until 2007, after which all sales will be at market-based capacity and energy rates. The new PPA also extended its term through 2012.

PGC owns a 16.25% limited partnership interest in MERC with no operating responsibilities. All of the senior debt on the Project was repaid with funds received from the renegotiation of the power contract, but there is still some subordinated debt outstanding to certain partners (including PGC) in the amount of \$14.1 million.

Penobscot Energy Recovery Project (PERC). PERC is an 800 tons per day waste-to-energy facility located in Orrington, Maine, which began operations in 1988. The minimum annual throughput is about 175,000 tons under a series of agreements with Maine communities that pay "tipping" fees for waste disposal services. The Project's 22 MW electric power output is sold to Bangor Hydroelectric Company pursuant to a 30-year PPA. PERC, Bangor Hydro and the affected communities have reached an agreement in principle to restructure the terms of this PPA and are seeking the approvals required to do so. If approved, this restructuring is expected to result, among other things, in a substantial cash payment to PERC from the utility.

PGC owns 28.7 percent of the general and limited partnership interests in PERC and NRG has become the operator of the Project under the terms of the acquisition. PERC was financed with \$108.6 million of tax-exempt bonds, supported by a letter of credit from Bankers Trust. It is expected that this financing would be replaced by bonds issued by the Finance Authority of Maine as a part of the restructuring of the PPA.

Mt. Poso Cogeneration Facility. Mt. Poso is one of two coal-fired cogeneration plants owned by PGC. It is a 49.5 MW circulating fluidized bed facility located near Bakersfield, California. The project sells electricity to Pacific Gas & Electric under an SO4 contract which extends to 2009. However, the fixed price period of the agreement terminates on April 1, 1999,

and there can be no assurances concerning the likely income from this project following that date. The project also supplies up to 45,000 lbs./hr. of steam to an adjacent oil field owned by the Project for enhanced oil recovery. Coal has been supplied to the project by ARCO Coal Company and the project recently negotiated the terms of that contract.

PGC owns a 21.50% general partnership interest in Mt. Poso itself, and in addition, owns a 47.5% interest in the company that operates the Project, Pyro-Pacific Operating Company.

Turners Falls Cogeneration. The second PGC coal-fired cogeneration facility, Turners Falls, is in cold shut-down as a result of a PPA Termination Agreement entered into in 1996 at the request of the power purchaser, Unitil Power Company. Turners Falls is a 20.1 MW coal-fired facility that had been

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placed into service in 1989. Under the terms of the PPA Termination Agreement, Unitil will make monthly payments to Turners Falls until 2009, and the project must be ready to resume operations on six months notice. PGC owns an 8.9% limited partnership interest in Turners Falls.

Wind Power Partners. The wind projects consist of one 50 MW project (500 wind turbines) and one 30 MW project (300 wind turbines), both located in California. PGC has a one percent general partnership interest in each project, and a 16% and a 17.54% limited partnership interest in them, respectively. Power is sold from both projects to Pacific Gas & Electric under 30-year S04 PPAs, but the fixed price periods have already ended for the first project and will do so for the final increment in 1998. After the expiration of that period, power is sold at a variable, short-run avoided cost rate with a reduced capacity payment. PGC also owns half of the \$7.6 million senior debt on the 50 MW project and all of the \$4.4 million senior debt on the 30 MW project.

Curtis Palmer Hydroelectric Project. Curtis Palmer is the only hydroelectric project in the PGC portfolio. It is a 58 MW project located at two dams on the Hudson River near the town of Corinth, New York. The project recently entered into a renegotiated power purchase agreement with Niagara Mohawk Power Corp. for a term that is projected to expire in 2027. PGC has only an 8.5% limited partnership interest in this project.

Camas Power Boiler. Camas is a 200,000 lbs./hr. wood and natural gas fired boiler which supplies steam to the Fort James Paper Mill in Camas, Washington. Under the Steam Sales Agreement, which expires in 2007, Fort James makes fixed and variable payments to Camas for this supply. The project does not generate electricity or make any power sales, but its steam sales are the equivalent of 25 MW of electric power.

PGC owns 100% of the Camas project, but Fort James has an option to buy the project at various prices determined in accordance with the Agreement during its term. The project was financed with \$15 million of tax-exempt bonds and \$22.8 million in taxable debt, all supported by a letter of credit from HelebaBank.

NRG GENERATING (U.S.) INC. ("NRGG")

On January 18, 1996, the U.S. Bankruptcy Court for the District of New Jersey awarded NRG the right to acquire a 41.86% equity interest in O'Brien Environmental Energy, Inc. ("O'Brien"), which emerged from bankruptcy on April 30, 1996 and was renamed NRGG. NRG currently holds 45.21% of the common stock of NRGG. The remaining 54.79% of the common stock continues to be held publicly. NRGG has interests in three domestic operating projects with an aggregate capacity of approximately 196 MW. NRGG's principal operating projects include: (a) the 52 MW Newark Boxboard Project (which is owned 100% by a wholly-owned project subsidiary of NRGG), a gas-fired cogeneration facility that sells electricity to JCP&L and steam to Newark Group

Industries, Inc.; (b) the 122 MW E.I. du Pont Parlin Project (which is owned 100% by a wholly-owned project subsidiary of NREGG), a gas-fired cogeneration facility that sells electricity to JCP&L and steam to E.I. du Pont de Nemours and Company ("E.I. du Pont"); and (c) an 83% interest in a 22 MW standby/peak sharing facility which provides electricity and standby capabilities for the Philadelphia Municipal Authority. In addition, NREGG has a 33.33% interest in the 150 MW Grays Ferry Project, a gas-fired cogeneration project which is under construction in Philadelphia, Pennsylvania. In December 1997, NREGG entered into an agreement, subject to certain conditions precedent, to acquire NRG's 117 MW Millennium project and to assume certain of NRG's obligations with respect to such project. See "--Millennium" below.

NRG provides NREGG with management and administrative services in connection with day-to-day operations. NRG employees serve as NRG's designees on the board of directors of NREGG. NRG and NREGG also entered into a "Co-Investment Agreement," pursuant to which NRG grants NREGG a right of first offer to acquire from NRG each energy development project first developed or acquired by NRG for which a co-investor is required because of federal or state regulatory restrictions on NRG's ownership. NRG has agreed that, within the three-year period following the closing date of the acquisition of NREGG, a minimum of one or more such projects, having an aggregate equity value of at least \$60 million or a minimum power generation capacity of 150 MW, will be so offered. To facilitate NREGG's ability to acquire projects under the Co-Investment Agreement, NRG is obligated to provide financing to NREGG to the extent that NREGG is unable to obtain funds on comparable terms from other sources.

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NRG has also agreed to certain provisions designed to protect the rights of the holders of the equity in NREGG that is not owned by NRG. These provisions include super-majority voting requirements with respect to a merger or sale of all or substantially all of NREGG's assets and certain additional issuances of NREGG stock, the creation of an independent committee of the board of directors of NREGG with authority to, among other things, determine whether NREGG will exercise its right of first offer under the Co-Investment Agreement and a commitment that, for a seven-year period following NRG's investment in NREGG, NRG will not remove or vote against the re-election to NREGG's board of directors of any of the three directors (appointed by Wexford Management Corp. and the Committee of Equity Security Holders) who constitute the independent directors committee.

NREGG and NRG have entered into various loan agreements. At December 31, 1996, the loan balance due to NRG was \$14,388,000 with a maturity date of April 30, 2001.

NREGG's shares are traded on The NASDAQ SmallCap Market under the symbol "NRGG". NREGG's closing share price as of September 30, 1997 was \$20.75.

Newark. The 52 MW Newark project, which commenced operation in November 1990, is 100%-owned by NRG Generating (Newark) Cogeneration Inc. ("NRGGN"), a wholly-owned project subsidiary of NREGG. NRGGN is designed to operate continuously and to provide up to 75,000 lbs./hr. of steam to a recycled paper boxboard manufacturing plant owned by Newark Boxboard Company, a subsidiary of Newark Group Industries, Inc., and 52 MW of electricity to JCP&L, each under agreements extending into the year 2015. The power contract provides fixed on-peak and off-peak energy and capacity payments for the base electrical power and fixed capital, fixed operation and maintenance and variable operation and maintenance payments for the dispatchable power. The facility availability in 1996 was in excess of 95%.

Natural gas for the project is supplied and paid for by JCP&L as a part of its obligations under the terms of the power purchase agreement.

Parlin. The 122 MW Parlin project, which commenced operation in June 1991, is 100% owned by NRG Generating (Parlin) Cogeneration Inc. ("NRGGP"), a wholly-owned project subsidiary of NREGG. NRGGP provides up to 120,000

lbs./hr. of steam to a manufacturing plant in Parlin, New Jersey owned by E.I. du Pont, under an agreement extending until 2021. In addition, the project sells 41 MW of base electric power and up to 73 MW of dispatchable power to JCP&L, under an agreement with an initial term until 2011. The power contract provides fixed on-peak and off-peak energy and capacity payments for the base electrical power and fixed capital, fixed operation and maintenance and variable operation and maintenance payments for the dispatchable power. Finally, the projects sells up to 9 MW of power to NRG Parlin, Inc. ("NPI"), a wholly-owned subsidiary of NRG Energy, Inc. NPI resells this power at retail to E.I. du Pont under an agreement extending until 2011. The facility availability in 1996 was in excess of 95%.

Natural gas for the project is supplied and paid for by JCP&L as part of its obligations under the terms of the power purchase agreement.

Both the Newark and the Parlin projects are being operated by Power Operations, Inc., a wholly-owned subsidiary of NRG which assumed the operations and maintenance responsibilities on December 31, 1996, under a six-year operating agreement providing for reimbursement of the operator's costs plus a fee.

Financing for Newark and Parlin. On May 17, 1996, NRG's wholly-owned project subsidiaries, NRGGN and NRGGP entered into a Credit Agreement (the "Credit Agreement") with Credit Suisse. The Credit Agreement established provisions for a \$155,000,000 15-year loan and a \$5,000,000 five-year debt service reserve line of credit. Pursuant to borrowings in May and July of 1996, NRGGN and NRGGP drew the full \$155,000,000 available under the Credit Agreement, which is a joint and several liability of NRGGN and NRGGP and will be amortized over a 15-year period as specified under the terms of the Credit Agreement.

Grays Ferry. NRGG has a 33.3% interest in the 150 MW Grays Ferry Project, which is currently under construction and will, when completed, sell electricity to PECO Energy Company ("PECO") and

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district heating steam to Trigen-Philadelphia Energy Corporation ("Trigen"). The Grays Ferry Project is being constructed by Westinghouse Electric Corporation ("WEC") pursuant to a fixed price turnkey construction contract. WEC has also made available \$15 million in subordinated debt to the project, payable semi-annually after commercial operation and to be repaid in full no later than March 2005. The project is scheduled to go into commercial operation in December 1997. Once in operation, it will be operated by an affiliate of Trigen pursuant to a 25-year operating agreement providing for reimbursement of the operator's costs plus a fee.

PECO will purchase energy and capacity from the project pursuant to two energy purchase agreements and two capacity purchase agreements, each having a term of 20 years. Gas for the Project will be provided by Aquila Energy Marketing Corporation. The gas sales agreement is tailored so that the project's fuel expenses will track its revenues from sales of electricity. To the extent the actual cost of fuel exceeds revenues received, a tracking account has been established which is payable by the project out of distributable cash flow.

Construction and term loan project financing for the project and certain letters of credit to support project agreements were provided by The Chase Manhattan Bank, N.A., as agent. This financing is non-recourse to NRG. The maturity date for the term loan is the earlier of March 6, 2013 or the fifteenth anniversary of the term loan conversion date.

NRG has agreed to fund NRGG's \$10 million equity obligation for the Grays Ferry Project. As of October 31, 1997, \$6.3 million had been advanced to NRGG by NRG for the Grays Ferry Project. In addition, on October 28, 1997, NRG converted \$3 million of its loan to NRGG into 396,255 shares of NRGG common stock. NRG owns 45.21% of the common stock of NRGG.



## MILLENNIUM

On September 19, 1997, NRG (Morris) Cogen, LLC ("NRGM"), an NRG affiliate, entered into a Construction and Term Loan Agreement with The Chase Manhattan Bank to finance the construction of a 117 MW cogeneration plant in Morris, Illinois. The project is being developed pursuant to a 25-year Energy Services Agreement between NRGM and Millennium Petrochemicals Inc. ("Millennium") pursuant to which NRGM will supply all of the external steam requirements and substantially all of the electricity requirements for Millennium's polyethylene manufacturing facility in Morris. Millennium has the right to buy out the cogeneration plant for fair market value at certain defined points in the contract term. The project is being constructed by Kiewit Industrial Co. and is projected to be completed by December 1, 1998. In connection with the financing of this project, NRG has entered into a \$22 million equity commitment and a \$1.2 million guaranty of certain obligations of Millennium Operations, Inc., an NRG subsidiary which will operate the project. In December 1997, NRGM entered into an agreement, subject to certain conditions precedent, with NRG to acquire this project and assume certain of NRG's obligations with respect to such project.

## NEO CORPORATION

NEO is a wholly-owned project subsidiary of NRG that was formed to develop small power generation facilities, ranging in size from 1 to 50 MW, in the United States. NEO is currently focusing on the development and acquisition of landfill gas projects and the acquisition of hydroelectric projects.

Through the investment vehicle Northbrook Energy, L.L.C. ("Northbrook"), NEO presently has a 50% interest in nineteen small operating hydroelectric projects, ranging in size from 1 MW to 6 MW and having a total capacity of 39.3 MW. As of March 31, 1997, NEO's total investment in these projects is \$4.0 million. NEO also has loaned \$3.7 million to Omega Energy Partners, L.L.C. ("Omega") to fund Omega's 50% equity interest in Northbrook. This loan is secured by Omega's project ownership interest.

NEO also has a 50% interest in twelve operating landfill gas projects, as of September 1, 1997, ranging in size from 1 MW to 8.4 MW and having a total capacity of 40 MW. As of June 30, 1997, NEO's investment in these projects totals \$1.9 million. In addition, NEO has ten landfill gas projects in varying phases of development: these projects will range in size from 1 MW to 10 MW and will have a total capacity of approximately 60 MW that is expected to go into commercial operation in 1997 and 1998. NEO expects its total equity requirements for these development projects to be approximately

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\$55 million. NEO also has twenty-one other landfill gas projects in development that it expects to go into commercial operation in 1998. There can be no assurance that the development of any or all of these projects will in fact be successfully completed.

On September 24, 1997, certain affiliates of NEO entered into a Construction, Acquisition and Term Loan Agreement with Lyon Credit Corporation ("Lyon") for \$92 million to fund the construction of the landfill gas collection system and generation facility for certain NEO landfill gas projects in development. The construction loan for each project will convert to a term loan containing a maximum maturity date of ten (10) years. NRG has agreed to provide Lyon with a guarantee during the construction loan period. In addition, NRG has agreed to guarantee the monetization and use of the Section 29 tax credits generated from the landfill gas projects financed by Lyon through the year 2007.

An important factor in the after tax return of the landfill gas projects is the eligibility of these projects for Section 29 tax credits. The Section 29 tax credit is available only to projects that produce gas from biomass or synthetic fuels from coal. Landfill gas is produced from biomass for purposes

of the Section 29 credit. To qualify for the credit, the facility for producing gas must be placed in service no later than June 30, 1998.

NEO generated after tax losses of \$520,000 in 1996, reflecting heavy development activity. For the nine months ended September 30, 1997, NEO has generated after tax earnings of \$3.6 million as compared to \$191,000 for the same nine month period in 1996.

#### CADILLAC RENEWABLE ENERGY

In July 1997, NRG, together with its partner, Decker Energy International, Inc. ("Decker"), acquired a 34 MW wood-fired steam turbine power plant, located in Cadillac, Wexford County, Michigan ("Cadillac"). NRG and Decker acquired the facility and certain other assets from Beaver Michigan Associates Limited Partnership. Electricity from the plant is sold to Consumers Energy under a long-term power purchase agreement. NRG immediately assumed operation of the 20-employee plant, now named Cadillac Renewable Energy, through a wholly-owned subsidiary.

#### SUNNYSIDE

The Sunnyside facility, located in Carbon County, Utah, is a 58 MW waste coal-fired facility that utilizes circulating fluidized bed technology. The Sunnyside facility is owned by Sunnyside Cogeneration Associates ("SCA"), a Utah joint venture, 50% of which is owned by NRG Sunnyside Inc. and 50% of which is owned by B&W Sunnyside L.P., an affiliate of Babcock & Wilcox. Sunnyside Operations Associates, in which affiliates of NRG and Babcock & Wilcox each hold 50% of the partnership interests, performs operations and maintenance services on behalf of SCA. As of December 31, 1996, NRG's investment in SCA was \$12.5 million.

PacifiCorp purchases the energy and capacity generated by the Sunnyside facility pursuant to a power purchase agreement with an initial term expiring in 2023. PacifiCorp is obligated to pay for energy at prices based on PacifiCorp's avoided cost. PacifiCorp is obligated to pay for base capacity, up to 45 MW, at a levelized fixed price, and for additional capacity up to 53 MW, at escalating fixed prices. The Sunnyside facility has experienced a shortfall in project cash flow attributable primarily to decreased revenues due to avoided energy rates being significantly lower than originally forecasted. In addition, higher fuel costs than originally forecasted may be incurred in the future.

These changes in the economic performance of the Sunnyside project have caused NRG to explore options for restoring the Sunnyside project to financial health. In particular, SCA has negotiated with PacifiCorp regarding a potential restructuring of payments under the power purchase agreement, and SCA has discussed a restructuring of the project debt with its bondholders. In the absence of a restructuring of the project's debt, a debt service reserve fund, which has been used to make up cash shortfalls, is expected to be depleted at the end of 1997. There can be no assurances that either PacifiCorp or the bondholders will agree to any restructuring, nor can there be any assurances as to the actions SCA may take when and if the debt service reserve fund is depleted.

#### JACKSON VALLEY

The Jackson Valley cogeneration facility ("Jackson Valley"), located near Ione, California is a 16 MW fluidized bed power generation facility fueled by waste lignite. The Jackson Valley facility is owned and operated by Jackson Valley Energy Partners, L.P., a California limited partnership ("JVEP") in which NRG owns a 2% general partnership interest and a 48% limited partnership interest. The remaining 2% general partnership interest and 48% limited partnership interest are owned by partnerships formed by two individuals. The facility began operation in 1987 and has had a lifetime operating availability in excess of 90%. NRG acquired its interest in Jackson Valley in July 1991.

Jackson Valley has a long-term power sales agreement with PG&E through to 2016. On April 1, 1995, JVEP reached an agreement with PG&E regarding the partial buy-out of the capacity payments under the PPA. The plant, which had been idle since that date, restarted operations on May 1, 1997, at which time the sale of energy to PG&E recommenced under the amended PPA.

In connection with its acquisition of the Jackson Valley facility in July 1991, JVEP also acquired a montan wax manufacturing plant, three mineral leases and rights to mine lignite on property near the facility. During the period while the JVEP facility was down, the montan wax plant maintained production by receiving its power requirements from an auxiliary boiler. Litigation is pending with respect to defining the nature and extent of JVEP's rights to waste lignite from one of the several mines that supplies the project with fuel but recent negotiations appear to favor a settlement. However, since the plant is currently receiving and will for the foreseeable future receive its waste lignite from several other mines, management believes that it is unlikely that this litigation will have a material adverse effect on the JVEP Partnership.

JVEP's acquisition of the power generation facility, the montan wax plant and the mineral rights was financed partially through the assumption of indebtedness under a financing facility that was outstanding at the time of the acquisition. The financing facility, which was restructured in 1995 in connection with the partial buyout, and the obligations of JVEP under the PPA, are non-recourse to NRG. The project debt was again restructured in September 1997, providing additional project capital for permitting, litigation and restart expenditures.

#### SAN JOAQUIN

NRG holds a 2% general partnership interest and a 43% limited partnership interest in San Joaquin Valley Energy Partners I L.P. and San Joaquin Energy Partners IV L.P. (together, the "SJVEP Partnerships"). The SJVEP Partnerships separately own the Chowchilla I, Chowchilla II, El Nido and Madera power generation facilities (the "SJVEP Facilities").

The PPAs with PG&E in respect of the SJVEP Facilities were bought-out by PG&E as part of its program of trying to end long-term power purchase agreements that impose above-market costs. The SJVEP contracts and many others like them were entered into at rates established by the California Public Utilities Commission in the early 1980's, which by 1995 were substantially above the market cost of power. PG&E has tried to buy-out a number of these contracts in order to save money for its ratepayers; the price of each buy-out has been negotiated based on the savings that PG&E will realize from terminating that contract. The SJVEP Partnerships agreed to terminate these power purchase contracts in exchange for the payment by PG&E of approximately \$116 million. NRG received total pre-tax cash distributions of \$41.8 million in 1995 and 1996 after retiring debt on the Facilities and making appropriate reserves. The project termination agreement resulted in a pretax gain of \$29.9 million in 1995, at which time NRG received a \$14.2 million distribution. An additional \$15.7 million of cash was received in 1996. PG&E also paid the Facilities' on-going operating expenses during the time that the buyout was in progress, which accounted for \$4.7 million of the total \$29.9 million gain in 1995. The distributions to NRG of \$14.2 million and \$15.7 million were included as cash flow from investing activities in 1995 and 1996, respectively, while all other cash distributions from the project were included in operating cash flow. Litigation is pending regarding the termination of a bio-fuel supply contract in connection with the buy-out. Appropriate reserves have been made and management believes that it is unlikely that this litigation will have a material adverse effect on the SJVEP Partnerships.

As a result of this buy-out, the SJVEP Facilities have been taken out of service. On December 31, 1996, a contractor for a NEO project purchased the mechanical equipment from the Chowchilla I power generation facility. The

SJVEP Partnerships' objective with respect to the other Facilities is to enter into replacement PPAs for the sale of energy and capacity and to resume operation by the end of 1997 or to sell the remaining SJVEP Facilities. No assurance can be given as to whether replacement agreements will be obtained or, if obtained, whether such agreements will be on terms favorable to the SJVEP Partnerships, or if purchasers for the SJVEP Facilities can be secured, or, if secured, whether the terms of their purchases will be favorable to the SJVEP Partnerships.

#### STEAM AND CHILLED WATER PRODUCTION, TRANSMISSION AND RELATED SERVICES

##### MINNEAPOLIS ENERGY CENTER ("MEC")

MEC provides steam and chilled water to customers in downtown Minneapolis, Minnesota. MEC currently provides 90 customers with 1.5 billion pounds of steam per year and 30 customers with 37.0 million ton hours of chilled water per year. NRG, through its wholly-owned project subsidiary NRG Energy Center, Inc. ("NRG Energy Center"), acquired MEC in August 1993 for approximately \$110 million. MEC's assets include two steam and chilled water plants, three chilled water plants, two steam plants, six miles of steam and two miles of chilled water distribution lines. The MEC plants have a combined steam capacity of 1,323 mmBtus per hour (388 MWT) and cooling capacity of 35,550 tons per hour.

MEC provides steam and chilled water to its customers pursuant to energy supply agreements which expire at varying dates from December 1997 to March 2017. Historically, MEC has renewed its energy supply agreements as they near expiration. With minor exceptions, these agreements are standard form contracts providing for a uniform rate structure consisting of three components: a demand charge designed to recover MEC's fixed capital costs, a consumption charge designed to provide a per unit margin, and an operating charge designed to pass through to customers all fuel, labor, maintenance, electricity and other operating costs. The demand and consumption charges are adjusted in accordance with the Consumer Price Index ("CPI") every five years.

NRG Energy Center's acquisition of MEC was financed pursuant to an \$84 million senior secured note facility. The notes are 7.31% fixed rate obligations due in 2013, with the principal amortized over the life of the loan and paid quarterly.

On January 9, 1996, two NRG employees were killed in an accident at MEC that occurred while two steam pipes were being connected. NRG believes that any liability relating to this accident will be adequately covered by insurance policies (which contain customary deductibles).

##### NATS

In August 1995, NRG purchased from Thermal Ventures, Inc. ("TVI"), a 49% limited partnership interest in each of two district heating and cooling projects, one in San Francisco (San Francisco Thermal Limited Partnership or "SFTLP") and the other in Pittsburgh (Pittsburgh Thermal Limited Partnership or "PTLP"). NRG and TVI then established North American Thermal Systems LLC ("NATS") for the purpose of jointly owning their respective general partnership interests in these two district heating and cooling companies. In 1996, NRG paid \$2.8 million to the owners of TVI and made a capital contribution of \$500,000 to NATS in exchange for the sale of the 1% general partnership interests in each of PTLP and SFTLP to NATS. NRG and TVI participate equally in SFTLP and in PTLP and each owns 50% of the membership interests in NATS. As of September 1997, NRG's investment in PTLP was \$4.0 million and NRG's investment in SFTLP was \$5.1 million.

PTLP and SFTLP are both regulated utilities that operate under tariffs and are rate-regulated. PTLP owns and operates a district heating and cooling system that serves part of downtown Pittsburgh and has peak steam capacity of 240 mmBtus per hour (70 MWT) and 10,180 tons of chilled water per year. PTLP serves 24 customers with 300 million pounds of steam per year and 21 million ton hours of chilled water per year. SFTLP is the sole supplier of steam to

downtown San Francisco, which it serves through its

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district heating system that has steam capacity of 490 mmBtu per hour (144 MWt). SFTLP serves approximately 210 customers with approximately 700 million pounds of steam per year that is used primarily for space and domestic heating and absorption air-conditioning.

NATS is currently considering the acquisition of several other district heating and cooling companies. NRG has agreed to make additional payments to the principals of TVI of up to an aggregate of \$7 million until January 1, 2003 for reaching performance benchmarks of current and future NATS operating entities. There is no assurance that NATS will consummate any additional acquisition.

#### SAN DIEGO POWER & COOLING

NRG purchased the San Diego Power & Cooling Company ("SDPC") on June 25, 1997. The purchase price was \$6.7 million, including a note from the seller for \$2.7 million, payable over 72 months. The remaining amount, with the exception of a \$50,000 contingency, was paid in cash. SDPC serves the cooling needs of fourteen major customers in the downtown San Diego central business district through an underground piping system. SDPC's chilled water capacity is 5,250 tons/hour.

#### ROCK-TENN

Rock-Tenn process steam operation, which is owned and operated by NRG, consists of a five-mile closed-loop steam/condensate line that delivers steam to the Rock-Tenn Company (formerly Waldorf Corporation), a paper manufacturer in St. Paul, Minnesota and has a peak steam capacity of 430 mmBtus per hour (126 MWt). Upon settlement of a 1987 dispute between NORENCO Corporation (a predecessor of NRG) and Waldorf, Waldorf elected to prepay revenues for future steam service. As of September 30, 1997, deferred revenues remaining were \$5.1 million. Rock-Tenn's corrugated medium operations are on 24 hour a day, 7 day a week schedule. The corrugated medium operations represent approximately 40% of normal steam sales.

NRG delivers steam to Rock-Tenn pursuant to a steam sales agreement which expires in 2007. Under the agreement Rock-Tenn is obligated to purchase its total energy needs for its St. Paul, Minnesota facility through June 30, 2007. The agreement does not obligate Rock-Tenn to purchase a minimum quantity of energy. Instead, Rock-Tenn's failure to acquire a certain quantity of energy during a given contract year triggers an NRG right to terminate the agreement, unless Rock-Tenn elects to compensate NRG for the deficit energy usage amount.

All project debt incurred with respect to the Rock-Tenn line has been repaid. NRG maintains a \$1.5 million performance bond with respect to the Rock-Tenn steam line.

#### WASHCO

NRG's Washco steam operation consists primarily of two steam lines and a back-up boiler facility, which were placed in service in 1986. The system has a peak steam capacity of 160 mmBtus per hour (47 MWt).

Andersen Corporation, a window manufacturer based in Bayport, Minnesota ("Andersen"), purchases approximately 200,000 mmBtus of thermal energy annually pursuant to a new ten-year agreement that expires in April 2007. Andersen is obligated to take or pay for an annual quantity of steam equal to 60% of its total of purchased and self-generated steam, on a cost plus fixed fee basis. The Minnesota Correctional Facility ("MCF"), located at Oak Park Heights, Minnesota, purchases approximately 130,000 mmBtus of thermal energy annually pursuant to an agreement that expires in December 2006. MCF purchases steam based on a fixed facility charge plus an energy charge that escalates annually in accordance with an NSP coal fuel and labor index.

## GRAND FORKS

NRG's Grand Forks boiler plant facility consists of seven boilers located in Grand Forks, North Dakota that were acquired from NSP in 1990. The system has a peak steam capacity of 105 mmBtus per hour (31 Mwt).

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The Grand Forks facility provides approximately 400,000 mmBtus of high temperature water annually to the Grand Forks Air Force Base pursuant to an agreement that expires in September 2000. NRG is paid a fixed capacity price component, a variable price component adjusted annually based on changes in CPI and a fuel component that is a pass-through of the facility's fuel costs for high temperature water sold under the agreement.

## RESOURCE RECOVERY FACILITIES

RDF projects, such as NRG's Newport facility and NSP's Elk River facility, historically were assured adequate supply of waste through state and local flow control legislation, which directed that waste be disposed of in certain facilities. In May 1994, the United States Supreme Court held that such waste was a commodity in interstate commerce and, accordingly, that flow control legislation that prohibited shipment of waste out of state was unconstitutional. Since this ruling, the RDF facilities owned or operated by NRG have faced increased competition from landfills in surrounding states. As a result of such competition, MSW processed at the Newport facility decreased by approximately 5% in 1995, from approximately 378,000 tons in 1994 to 360,000 tons in 1995. In 1996, however, due to assistance from NRG and a reduction in tipping fees under contracts entered into between haulers and Ramsey and Washington Counties (the "Counties"), waste deliveries reversed their downward trend. In the absence of valid flow control legislation, there can be no assurance that this improved trend will continue. Various legislative proposals have been considered, including legislation that would provide relief to existing RDF facilities. No assurance can be given that such legislation will be adopted.

## NEWPORT

NRG's Newport resource recovery facility, located in Newport, Minnesota, can process over 1,500 tons of MSW per day, 92% of which is recovered as RDF or other recyclables and reused in power generation facilities in Red Wing and Mankato, Minnesota. The Newport facility, which was originally constructed and operated by NSP, was transferred to NRG in 1994. NRG owns 100% of and operates and maintains the Newport facility.

The construction of the Newport facility was financed through the issuance by the Counties of tax exempt variable rate resource recovery revenue bonds, which have subsequently been converted to fixed rate resource recovery revenue bonds with annual maturities each December through to 2006. The proceeds of such bond issuance were loaned by the Counties to NSP, which agreed to pay to the Counties amounts sufficient to pay the debt service on the bonds. NRG issued a separate note to NSP in an original principal amount of approximately \$10 million as part of the consideration for the purchase of the facility from NSP. As of September 30, 1997, \$19.8 million was outstanding on the Counties' loan to NSP and \$8.4 million was outstanding under NRG's note to NSP.

Pursuant to service agreements with the Counties, which expire in 2007, NRG processes a minimum of 280,800 tons of MSW per year and receives service fees based on the amount of waste processed, pass-through costs and certain other factors. NRG is also entitled to an operation and maintenance fee, which is designed to recover fixed costs and to provide NRG a guaranteed amount for operating and maintaining the facility for the processing of 750 tons per day of MSW, whether or not the Counties deliver such waste for processing.

To increase MSW flows and improve facility competitiveness, the Counties

reduced tipping fees charged to haulers under long-term delivery contracts. The tip fee reduction became effective as of June 1, 1996 and is effective under those contracts until the end of 1998. MSW deliveries for the nine months ended September 30, 1997 were 16% higher than the same period in 1996.

Minnesota Waste Processors L.L.C. ("Minnesota Waste Processors"), a limited liability company which is 50% owned by each of NRG and LJP Enterprises, Inc., collects MSW from several cities in southern Minnesota for processing at the Newport facility. NRG also uses Minnesota Waste Processors' primary asset, a large warehouse, as a temporary RDF storage facility to enable more efficient utilization

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of RDF as a feedstock to NSP's Wilmarth generating plant. The \$2 million storage and transfer warehouse owned by Minnesota Waste Processors has been financed through a loan from NRG to Minnesota Waste Processors. In the event of a default on such loan, NRG's recourse likely would be limited to foreclosure on the warehouse.

#### ELK RIVER

Since 1989, NRG has operated the Elk River resource recovery facility located in Elk River, Minnesota, which can process over 1,500 tons of MSW per day, 90% of which is recovered as RDF or other recyclables and reused in power generation facilities in Elk River and Mankato, Minnesota. NSP owns 85% of the Elk River facility, and United Power Association owns the remaining 15%.

Pursuant to service agreements between NSP and each of Anoka County, Hennepin County, Sherburne County in Minnesota and the Tri-County Solid Waste Management Commission in Minnesota (the "NSP Service Counties"), all of which expire in 2009, NSP is obligated to process a maximum of 450,000 tons of MSW per year and is entitled to receive service fees based on the amount of waste processed, pass-through costs, revenues credited to the NSP Service Counties and certain other factors. NSP is also entitled to an operation and maintenance fee, which is designed to recover fixed costs and to provide NSP a guaranteed amount for operating and maintaining the facility for the processing of 214,900 tons of waste, whether or not the NSP Service Counties deliver such waste for processing.

NRG also provides ash storage and disposal for the Elk River facility at NSP's Becker ash disposal facility, an approved ash deposit site adjacent to NSP's Sherburne County generating facility near Becker, Minnesota. NRG operates the Becker facility on behalf of NSP. Pursuant to an ash management services agreement between NSP and the NSP Service Counties, the NSP Service Counties pay an ash disposal fee based on the amount of ash disposal, pass-through costs and certain other factors.

Prior to 1996, NRG managed Elk River and Becker Ash on behalf of NSP under a cost reimbursement arrangement. NRG did not earn a profit with respect to providing such services. As of January 1, 1996, NRG entered into an operation and maintenance agreement with NSP with respect to the Elk River Facilities, under which NRG receives a base management fee and is reimbursed for costs it has incurred. The operation and maintenance agreement also provides for a management incentive fee payable to NRG, based upon the financial performance of the Elk River Facilities.

In 1996 NRG earned a total management fee of \$1.5 million, in addition to reimbursed expenses. Management fees for the nine months ended September 30, 1997, totalled \$776,000 compared to \$761,000 for the same period in 1996.

#### PRINCIPAL CUSTOMERS OF OPERATING SUBSIDIARIES

Customers accounting for more than 10% of NRG's operating revenues (which exclude equity in earnings of projects) in each of the last two fiscal years were as follows:

YEAR ENDED  
DECEMBER 31,  
-----  
1995      1996  
-----  
(IN MILLIONS)

Ramsey and Washington Counties, Minnesota (Resource Recovery) ..	\$20.6	\$20.8
Rock-Tenn Company (Thermal Energy).....	10.0	10.1

PROPERTIES

In addition to NRG's properties listed under the heading "Business -- Description of NRG's Projects," NRG leases its offices at 1221 Nicollet Mall, Suite 700, Minneapolis, Minnesota 55403, under a five-year lease that expires in June 2002.

NRG believes that its facilities and properties have been satisfactorily maintained, are in good condition, and are suitable for NRG's operations.

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LEGAL AND ADMINISTRATIVE PROCEEDINGS

NRG experiences routine litigation in the course of its business. Management is of the opinion that none of this routine litigation will have a material adverse effect on the consolidated financial condition of NRG.

EMPLOYEES

At September 30, 1997, NRG employed 850 people, approximately 313 of whom are employed directly by NRG and approximately 537 of whom are employed by its wholly-owned subsidiaries. Approximately 550 employees are covered by collective bargaining agreements.

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REGULATION

NRG is subject to a broad range of federal, state and local energy and environmental laws and regulations applicable to the development, ownership and operation of its United States and international projects. These laws and regulations generally require that a wide variety of permits and other approvals be obtained before construction or operation of a power plant commences and that, after completion, the facility operate in compliance with their requirements. NRG strives to comply with the terms of all such laws, regulations, permits and licenses and believes that all of its operating plants are in material compliance with all such applicable requirements. No assurance can be given, however, that in the future all necessary permits and approvals will be obtained and all applicable statutes and regulations



complied with. In addition, regulatory compliance for the construction of new facilities is a costly and time-consuming process, and intricate and rapidly changing environmental regulations may require major expenditures for permitting and create the risk of expensive delays or material impairment of project value if projects cannot function as planned due to changing regulatory requirements or local opposition. Furthermore, there can be no assurance that existing regulations will not be revised or that new regulations will not be adopted or become applicable to NRG which could have an adverse impact on its operations.

In particular, the independent power market in the United States, Australia and other countries is dependent on the existing regulatory and ownership structure, and while NRG strives to take advantage of the opportunities created by such changes, it is impossible to predict the impact of those changes on NRG's operations. Further, NRG believes that the level of environmental awareness and enforcement is growing in most countries, including most of the countries in which NRG intends to develop and operate new projects. Therefore, based on current trends, NRG believes that the nature and level of environmental regulation to which it is subject will become increasingly stringent. NRG's policy is therefore to operate its projects in accordance with environmental guidelines adopted by the World Bank and applicable local law.

#### ENERGY REGULATION IN THE UNITED STATES

The enactment of PURPA in 1978 provided incentives for the development of Qualifying Facilities or "QFs", which were basically cogeneration facilities and small power production facilities that utilized certain alternative or renewable fuels. The passage of the Energy Policy Act in 1992 further encouraged independent power production by providing certain exemptions from regulation for EWGs and "foreign utility companies" ("FUCOs").

All of NRG's domestic projects are currently Qualifying Facilities under PURPA, except for Parlin which is an EWG. These QF projects are as follows: Sunnyside, Jackson Valley, Artesia, all of the NRGG Facilities (except for Parlin) and all of the NEO Facilities. QF status conveys two primary benefits. First, regulations under PURPA exempt Qualifying Facilities from PUHCA, most provisions of the Federal Power Act and the state laws concerning rates of electric utilities, and financial and organizational regulations of electric utilities. Second, FERC's regulations under PURPA require that (1) electric utilities purchase electricity generated by QFs at a price based on the purchasing utility's full avoided cost of producing power, (2) the electric utilities must sell back-up, interruptible, maintenance and supplemental power to the QF on a non-discriminatory basis, and (3) the electric utilities must interconnect with any QF in its service territory, and if required transmit power if they do not purchase it.

NRG endeavors to acquire, develop and operate its domestic plants, monitor regulatory compliance by such plants and choose its customers in a manner that minimizes the risk of those plants losing their QF status. However, the occurrence of events outside NRG's control, such as loss of a cogeneration plant's steam customer, could jeopardize QF status. While a plant usually would be able to react in a manner to avoid the loss of QF status by, for example, replacing the steam customer or finding another use for the steam which meets PURPA's requirements, there is no certainty that such action, if possible, would be practicable or economic. In the alternative, NRG could attempt to avoid regulation under PUHCA by qualifying the project as an EWG, as is the case with the NRGG Parlin cogeneration facility. However, this change may not be permitted under the terms of the applicable power purchase agreement, and even if it were, the plant would then be subject to rate approval from the FERC.

While it is unlikely that one of NRG's plants would actually lose its status as a QF and not become an EWG, if that did occur, NRG would in all likelihood have to cease operation of that plant or sell the

plant to an unaffiliated third party if NRG could not restore QF status after a reasonable cure period. If it continued to operate, the project subsidiary holding that plant would lose the exemptions outlined above and would become an electric utility or EWG. This could result in NRG inadvertently becoming a "public utility holding company" under PUHCA by owning more than 10% of the voting securities of an electric utility. Loss of QF status on a retroactive basis could also lead to, among other things, fines and penalties being levied against NRG and its project subsidiaries, defaults under the power purchase agreement and resulting claims by the utility customer for the refund of previous payments, and defaults under financing agreements.

Currently, Congress is considering proposed legislation that would amend PURPA by eliminating the requirement that utilities purchase electricity from QFs at prices based on the purchasing utility's avoided cost. NRG does not know whether such legislation will be passed or what form it may take. NRG believes that if any such legislation is passed, it would apply to new projects only and thus, although potentially impacting NRG's ability to develop new domestic QF projects, it would not affect NRG's existing QF projects. There can be no assurance, however, that any legislation passed would not adversely impact NRG's existing domestic projects.

In any case, NRG anticipates that most of its future domestic development activities will focus on the development of EWGs rather than QFs. An EWG is an entity that is exclusively engaged, directly or indirectly, in the business of owning or operating facilities which are exclusively engaged in generating and selling electric energy at wholesale. An EWG will not be regulated under PUHCA, but is subject to FERC and state public utility commission regulatory reviews, including rate approval.

In its future development and acquisition of domestic projects, NRG may also be subject to regulation by the FERC if NRG wheels electricity to purchasers other than the local utility to which the plant is interconnected. Although wheeling arrangements are generally voluntary, the FERC regulates the rates, terms and conditions for electricity transmission in interstate commerce. Currently, none of NRG's projects requires the wheeling of electricity over power lines owned by others.

If it develops or acquires domestic EWGs rather than QF's in the future, NRG may also be subject to some regulation by state public utility commissions ("PUCs"), because EWGs do not enjoy the same statutory and regulatory exemptions from state regulation as was granted to QF's. In fact, however, since EWGs are only allowed to sell power at wholesale, their rates must receive initial approval from the FERC rather than the states. But in areas outside of rate regulation (such as financial or organizational regulation), some state utility laws may give their PUCs broad jurisdiction over non-QF independent power projects that sell power in their service territories, including EWGs. The actual scope of that jurisdiction over independent power projects varies significantly from state to state, depending on the law of that state. In addition, many states are implementing or considering regulatory initiatives designed to increase competition in the domestic power generating industry and increase access to electric utilities' transmission and distribution systems for independent power producers and electricity consumers. At the same time, electric utility companies themselves are considering a variety of restructuring proposals, including mergers, acquisitions and divestitures of one or more lines of business. NRG believes that the training and experience of many of its employees in the electric utility industry have prepared it to take advantage of these many changes in the industry. However, NRG cannot predict the final form or timing of these changes in the domestic utility industry or the results of these changes on its operations.

#### ENVIRONMENTAL REGULATIONS -- UNITED STATES

The construction and operation of power projects are subject to extensive environmental protection and land use regulation in the United States. These laws and regulations often require a lengthy and complex process of obtaining licenses, permits and approvals from federal, state and local agencies. If

such laws and regulations are changed and NRG's facilities are not grandfathered, extensive modifications to project technologies and facilities could be required.

Based on current trends, NRG expects that environmental and land use regulation will continue to be stringent. Accordingly, NRG plans to continue a strong emphasis on the development and use of "best-available" control technology, as required under the Clean Air Act and Clean Water Act, to minimize the environmental impact of its operations.

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All of NRG's domestic facilities perform at levels equal to or better than applicable federal performance standards mandated for such plants under the Clean Air Act. NRG believes that technology currently installed at NRG's projects should uniformly meet or exceed reasonably available control technology (RACT). In addition, all of NRG's current domestic operating plants are by statute generally exempt from or unaffected by the provision of the 1990 amendments to the Clean Air Act (the "1990 Amendments"), which require most power plants to purchase sulphur dioxide allowances. In the future, the plants NRG expects to develop in the United States will continue to rely on "clean (low sulfur) coal," sulphur dioxide removal technology or natural gas technology. Accordingly, NRG believes that the additional costs of obtaining the number of allowances needed for future projects should not materially affect NRG's ability to develop such projects.

The 1990 Amendments also provide an extensive new operating permit program for existing sources. Because all of the existing NRG facilities (with the exception of the NATS facilities) were permitted under the Prevention of Significant Deterioration or other New Source Review program, NRG currently expects that the permitting impact under the 1990 Amendments to be minimal. NATS currently is evaluating whether any of its facilities will require modification. NRG anticipates that the costs of applying for and obtaining operating air permits will not be material. NRG may need to upgrade continuous emission monitoring systems at some plants, however, and permit fees will increase operating expenses.

The hazardous air pollutant provisions of the 1990 Amendments presently exclude electric steam generating facilities, such as NRG's plants. Until studies of the emissions from such facilities are completed and Congress either amends the Clean Air Act further or the EPA promulgates regulations in connection therewith, the nature and extent of federal hazardous air pollutants emissions restrictions which will be applied to NRG's plants and other electric steam generating facilities will remain uncertain.

NRG has received notices of violation and fines totaling approximately \$250,000 from the New Jersey Department of Environmental Protection ("NJDEP") in connection with certain technical and record keeping violations under the Clean Air Act at the former O'Brien Energy facilities in New Jersey. NRG detected and voluntarily disclosed these violations to the NJDEP shortly after NRG's acquisition of its interest in the O'Brien facilities. Because NRG did not receive any economic advantage from these violations and disclosed them promptly and voluntarily, NRG has recently filed administrative proceedings seeking forgiveness of the fines. In addition, NRG believes that the former operator of these facilities is contractually responsible for payment of any fines that are assessed, because the violations occurred during a time when that third-party operator managed the facilities.

Existing NRG facilities are also subject to a variety of state and federal regulations governing existing and potential water/wastewater discharges from the facilities. Generally, federal regulations promulgated through the Clean Water Act govern overall water/wastewater discharges, through NPDES permits. Under current provisions of the Clean Water Act, existing permits must be renewed every five years, at which time permit limits are extensively reviewed and can be modified to account for changes in regulations. In addition, the permits have re-opener clauses which the federal government can use to modify a permit at any time. NRG does not anticipate, however, that

any change in permit limits pursuant to these provisions of the Clean Water Act would affect significantly the profitability of NRG's facilities.

Congress is considering whether to re-authorize the Clean Water Act, with reauthorization focusing on toxic discharges, receiving water body biological monitoring requirements, bioassay requirements, additional controls on stormwater runoff, and water quality standards and enforcement provisions. It is uncertain whether the Clean Water Act will become more or less stringent after re-authorization. If the Clean Water Act becomes more stringent, NRG facilities may be required to retrofit existing wastewater treatment facilities for metals removal and to budget for additional monitoring requirements and toxicity reduction evaluations. NRG does not expect the impact of these additional expenses to affect significantly the profitability of the facilities.

There can be no assurance that existing laws and regulations will not be revised or that new regulations will not be adopted or become applicable to NRG which could have an adverse impact on its operations.

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#### ENVIRONMENTAL REGULATIONS -- INTERNATIONAL

Although the type of environmental laws and regulations applicable to independent power producers and developers varies widely from country to country, many foreign countries have laws and regulations relating to the protection of the environment and land use which are similar to those found in the United States. Laws applicable to the construction and operation of electric power generation facilities in foreign countries generally regulate discharges and emissions into water and air, and also regulate noise levels. Air pollution laws in foreign jurisdictions often limit the emissions of particles, dust, smoke, carbon monoxide, sulfur dioxide, nitrogen oxides and other pollutants. Water pollution laws in foreign countries generally limit wastewater discharges into municipal sewer systems and require treatment of wastewater so that it meets established standards. New projects and modifications to existing projects are also subject, in many cases, to land use and zoning restrictions imposed in the foreign country. In addition to the requirements currently imposed by a particular country, certain lenders to international development projects may impose their own requirements relating to the protection of the environment.

NRG believes that the level of environmental awareness and enforcement is growing in most countries, including most of the countries in which NRG intends to develop and operate new projects. Therefore, based on current trends, NRG believes that the nature and level of environmental regulation to which it is subject will become increasingly stringent. NRG's policy is to operate its projects at least in accordance with environmental guidelines adopted by the World Bank and applicable local law.

#### GERMAN REGULATIONS

Both the Schkopau Power Station and MIBRAG are subject to the energy and environmental laws and regulations of Germany. German environmental laws conform to European Union standards. In addition, MIBRAG is governed by German mining laws and regulations.

#### ENVIRONMENTAL REGULATIONS

The Schkopau facility is designed to comply with all applicable German laws and regulations, including, without limitation, environmental and land use laws and regulations. The power purchase agreement between Saale Energie and VEAG provides that any future changes in law that may affect the cost of providing the contracted capacity will lead to adjustment of the price.

In the case of existing power generating facilities located in eastern Germany, current German environmental laws and regulations are being phased-in in a manner that provides for a gradual step-up of the environmental standards applicable to such facilities. All east German power

generating facilities were required to be in full compliance with German environmental laws and regulations by July 1, 1996. MIBRAG's Wif3hlitz, Mumsdorf and Deuben facilities have been retrofitted and are presently in full compliance with these laws and regulations. The power purchase agreement between MIBRAG and WESAG provides that any future changes in the law that may materially affect the cost of generating power will reopen the price.

#### ENERGY REGULATIONS

The Schkopau facility and all three power generating facilities of MIBRAG are permitted to generate and sell energy to their present customers pursuant to current German energy laws and regulations. Should the Schkopau facility or any of the MIBRAG power generating facilities wish to sell to additional customers, this would require further regulatory approval.

The German government currently is considering substantially amending the German Energy Resources Act of 1936. The bill currently before the German Parliament will not affect the regulatory status of the Schkopau or MIBRAG facilities. However, it is not possible at present to determine whether the bill will be enacted in its current form or whether an amendment, if enacted, would have an adverse effect on the regulatory status of those facilities.

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The current German government has dismissed plans to enact an energy related tax or other surcharge. However, certain political factions in Germany and within the European Union continue to press for such a tax or surcharge. There can be no assurance that such a tax or surcharge will not be enacted in the future.

#### MINING REGULATIONS

MIBRAG owns the mining rights to the Profen and Schleenhain mines and leases mining rights to the Zwenkau mine. MIBRAG currently is operating all three of its mines in compliance with current German mining regulations.

#### AUSTRALIAN REGULATIONS

The electricity sector in Queensland is regulated primarily under the Electricity Act. The Electricity Act was recently amended to provide for independent generation and the licensing of independent generators by the Regulator General. Pursuant to the Electricity Act, the State Minister for Energy and the Regulator General have the authority to promulgate regulations governing the Queensland electricity industry.

In Victoria, the primary laws providing for the economic regulation of the Victorian electricity industry are the Electricity Industry Act 1993 (Vic) and the Office of the Regulator-General Act 1994 (Vic). The ongoing regulation of the Victorian electricity industry is the responsibility of the Office of the Regulator-General, an independent regulatory body established under the Office of the Regulator-General Act.

Environmental management in Victoria is primarily governed by the Environment Protection Act 1970 (Vic). The primary control instruments under the EPA are licenses issued by the Environment Protection Authority (the environmental regulatory agency established under the EPA). The EPA was amended in 1990 and now provides for severe penalties for company directors, managers and employees in cases of gross environmental misconduct.

Although discussed in Victoria, it is considered unlikely that a carbon tax will be introduced in the foreseeable future. Even if one is introduced, the tax would have to operate at very high levels before it could significantly affect Loy Yang's competitiveness in the wholesale electricity market.

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#### MANAGEMENT

The name, age and title of each of the directors and executive officers of NRG as of November 1, 1997 are as set forth below.

NAME	AGE	TITLE
David H. Peterson ...	56	Chairman of the Board, President, Chief Executive Officer and Director
Gary R. Johnson .....	50	Director
Cynthia L. Leshner ...	49	Director
Edward J. McIntyre ..	46	Director
John A. Noer.....	52	Director
Leonard A. Bluhm ....	51	Executive Vice President and Chief Financial Officer
James J. Bender .....	40	Vice President and General Counsel
Valorie A. Knudsen ..	41	Vice President, Finance
Craig A. Mataczynski	37	Vice President, U.S. Business Development
Robert McClenachan ..	46	Vice President, International Business Development
Louise T. Routhe ....	41	Vice President, Human Resources and Administration
Ronald J. Will .....	57	Vice President, Operations and Engineering
Brian B. Bird.....	35	Treasurer
David E. Ripka .....	48	Controller
Julie A. Jorgensen ..	35	Corporate Secretary

David H. Peterson has been Chairman of the Board of NRG since January 1994, Chief Executive Officer since November 1993, President since 1989 and a Director since 1989. Mr. Peterson was also Chief Operating Officer of NRG from June 1992 to November 1993. Prior to joining NRG, Mr. Peterson was Vice President, Non-Regulated Generation for NSP, and he has served in various other management positions with NSP during the last 20 years.

Cynthia L. Leshner has been a Director of NRG since July 1996 and became President of NSP Gas in July 1997. Prior to July 1997, Ms. Leshner was Vice President-Human Resources of NSP since March 1992 after serving as Director of Power Supply-Human Resources since 1991. Ms. Leshner became Area Manager, Electric Utility Operations, in 1990, and previously served as Manager, Metro Credit, and Manager, Occupational Health and Safety. Prior to joining NSP, Ms. Leshner was a training and development consultant at the Center for Continuing Education in Minneapolis. From 1970 to 1977, she held a variety of positions with Multi Resource Centers, Inc., also in Minneapolis.

Gary R. Johnson has been a Director of NRG since February 1993, Corporate Secretary of NSP from April 1994 until July 1997 and Vice President and General Counsel of NSP since October 1991. Prior to October 1991, Mr. Johnson was Vice President-Law of NSP from December 1988, acting Vice President from September 1988 and Director of Law from February 1987.

Edward J. McIntyre has been a Director of NRG since May 1992 and Vice President and Chief Financial Officer of NSP since January 1993. Mr. McIntyre has also been a director of NSP subsidiaries Viking Gas Transmission Company since June 1993, Eloigne Company since August 1993 and First Midwest Auto Park, Inc. since September 1993, and Cenerprise since September 1994, where he served as Chairman from 1994 to 1996. Mr. McIntyre served as President and Chief Executive Officer of NSP-Wisconsin, a wholly owned subsidiary of NSP, from July 1990 to December 1992, and he has served in various other management positions with NSP during the last 20 years.

John A. Noer has been a director of NRG since June 1997 and President and CEO of NSP Wisconsin, a wholly owned subsidiary of NSP, since January 1993. Prior to joining NSP Wisconsin, Mr. Noer was President of Cypress Energy Partners, a wholly-owned project subsidiary of NRG, from March 1992 to January 1993. Prior to joining Cypress Energy Partners, Mr. Noer held various management positions with NSP since joining the company in September 1968.

Leonard A. Bluhm has been Executive Vice President and Chief Financial Officer of NRG since January 1997. Immediately prior to that, he served as the first President and Chief Executive Officer of NRGG, of which he is now Chairman. Mr. Bluhm was Vice President of NRG from January 1993 and Chief Financial Officer May 1993 until assuming his NRGG position. Mr. Bluhm was Chief Financial Officer of Cypress Energy Partners, a wholly-owned project subsidiary of NRG, from April 1992 to January 1993, prior to which he was Director, International Operations and Manager, Acquisitions and Special Projects of NRG from 1991. Mr. Bluhm previously served for over 20 years in various financial positions with NSP.

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James J. Bender has been Vice President and General Counsel of NRG since June 1997. He served as the General Counsel of the Polymers Division of Allied Signal Inc. from May 1996 until June 1997. From June 1994 to May 1996 Mr. Bender was employed at NRG, acting as Senior Counsel until December 1994 and as Assistant General Counsel and Corporate Secretary from December 1994 to May 1996. Prior to joining NRG in 1994, Mr. Bender was a partner at the Minneapolis law firm of Leonard, Street and Deinard from April 1993 to June 1994 and he served as Corporate Counsel for Pfizer Inc. from August 1989 to April 1993.

Valorie A. Knudsen has been Vice President, Finance since April 1996, prior to which she served as Controller since August 1993. Prior to joining NRG, Ms. Knudsen served in various managerial accounting positions from November 1987 to July 1993 with Carlson Companies, Inc., where she was responsible for various types of accounting and reporting.

Craig A. Mataczynski has been Vice President, U.S. Business Development of NRG since December 1994. Mr. Mataczynski served as President of NEO Corporation, NRG's wholly-owned subsidiary that develops small electric generation projects within the United States, from May 1993 to January 1995. Prior to joining NRG, Mr. Mataczynski worked for NSP from 1982 to 1994 in various positions, including Director, Strategy and Development and Director, Power Supply Finance.

Robert McClenachan has been Vice President, International Business Development of NRG since September 1995, prior to which he was Managing Director, Business Development from June 1992 to September 1995. Mr. McClenachan was also President of NRG Australia, a wholly-owned project subsidiary of NRG, from April 1993 to October 1995. Prior to joining NRG, Mr. McClenachan served as Development Director for Bonneville Pacific Corporation, an independent power production company in Salt Lake City, Utah, from January 1991 to December 1991, and he worked from 1983 to 1991 in various positions for Central Vermont Public Service Corporation, including Vice President, Corporate Development.

Louise T. Routhe has been Vice President, Human Resources and Administration of NRG since June 1992, prior to which she served as Human Resources Director from January 1992. Prior to joining NRG, Ms. Routhe was self-employed as a Human Resources and Management Consultant from December 1990 to January 1992 and worked as Vice President, Human Resources with First Trust Company, a wholly-owned subsidiary of First Bank System, Inc., from 1987 to 1990. Ms. Routhe held various other Human Resources management positions at First Bank System from 1979 to 1987.

Ronald J. Will has been Vice President, Operations and Engineering of NRG since March 1994, prior to which he served as Vice President, Operations from June 1992. Prior to joining NRG, he served as President and Chief Executive Officer of NRG Thermal, a wholly-owned subsidiary of NRG that provides customers with thermal services, from February 1991 to June 1993. Prior to February 1991, Mr. Will served in a variety of positions with Norengo, a wholly-owned thermal services subsidiary of NRG, including Vice President and General Manager from August 1989 to February 1991.

Brian B. Bird has been Treasurer of NRG since June 1997, prior to which he

was Director of Corporate Finance for Deluxe Corporation in Shoreview, Minnesota from September 1994 to May 1997. Mr. Bird was Manager of Finance for the Minnesota Vikings Professional Football Team from March 1993 to September 1994. Mr. Bird held several financial management positions with Northwest Airlines in Minneapolis, Minnesota from 1988 to March 1993.

David E. Ripka has been Controller of NRG since March 3, 1997. Prior to joining NRG, Mr. Ripka held a variety of positions with NSP for over 20 years, including Assistant Controller and General Manager of Accounting Operations and Director of Audit Services.

Julie A. Jorgensen has been Corporate Secretary of NRG since October 1997 and Senior Counsel since June 1997. She was Vice President and General Counsel of NRG from December 1994 until June 1997, prior to which she was Assistant General Counsel from January 1994 to December 1994 and Counsel from January 1993 to January 1994. Prior to joining NRG in 1993, Ms. Jorgensen worked as an associate with Morrison & Foerster, a private law firm in Los Angeles, California.

EXECUTIVE COMPENSATION AND OTHER INFORMATION

Compensation. The following table sets forth the compensation paid or awarded to David H. Peterson, Chairman, President and Chief Executive Officer of NRG, and the other four most highly compensated executive officers of NRG during the last fiscal year (collectively, the "Named Executives") for services rendered in all capacities for the last fiscal year.

SUMMARY COMPENSATION TABLE

NAME AND PRINCIPAL POSITION	YEAR	ANNUAL COMPENSATION		
		SALARY	BONUS	OTHER ANNUAL COMPENSATION (1)
		(\$)	(\$)	(\$)
David H. Peterson Chairman, President & Chief Executive Officer .....	1996	250,000	81,000	
Leonard A. Bluhm (3) Executive Vice President & CFO .....	1996	152,333	53,630	
Robert McClenachan Vice President, International Business Development .....	1996	150,000	36,201	37,410
Ronald J. Will Vice President, Operations & Engineering .....	1996	147,000	38,667	
Craig A. Mataczynski Vice President, U.S. Business Development .....	1996	145,000	40,343	

(RESTUBBED TABLE CONTINUED FROM ABOVE)

NAME AND PRINCIPAL POSITION	SECURITIES UNDERLYING OPTIONS	ALL OTHER COMPENSATION (2)
	(#)	(\$)
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David H. Peterson Chairman, President & Chief Executive Officer .....		3,637
Leonard A. Bluhm (3) Executive Vice President & CFO .....	105,000 (4)	2,712
Robert McClenachan Vice President, International Business Development .....		2,712
Ronald J. Will Vice President, Operations & Engineering .....		2,712
Craig A. Mataczynski Vice President, U.S. Business Development .....		2,712

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- (1) The amount shown in this column for Mr. McClenachan includes a relocation and foreign assignment premium bonus (\$19,616) and the value of the personal use of a company-provided automobile (\$7,986).
  - (2) This column consists of the amounts contributed by NRG to the NSP Retirement Savings Plan (\$900) and the Employee Stock Ownership Plan (\$1,812.89) for each Named Executive. The column also reflects the value to Mr. Peterson of the remainder of insurance premiums paid under the NSP Officer Survivor Benefit Plan by NRG (\$925).
  - (3) Mr. Bluhm's salary and bonus include amounts paid for his service with NRG.
  - (4) These options relate to NRG common stock. See "Option Grants in Last Fiscal Year."

The following table sets forth information concerning the exercise of stock options and stock appreciation rights during fiscal 1996 by each of the Named Executives and the fiscal year-end value of unexercised options. Prior to the existence of the NRG Equity Plan, NRG executives participated in the NSP Executive Stock Option program. The following table reflects the Named Executive's participation in the NSP Executive Stock Option Program.

AGGREGATED OPTION/SAR EXERCISES IN LAST FISCAL YEAR, AND FY-END OPTION/SAR VALUE (1)

NAME	NUMBER OF SECURITIES UNDERLYING UNEXERCISED OPTIONS/SARS AT FY-END		VALUE OF UNEXERCISED IN-THE-MONEY OPTIONS/SARS AT FY-END (\$) (2)
	EXERCISABLE/ UNEXERCISABLE	(#)	
David H. Peterson .	8,415/0		44,213/0
Leonard A. Bluhm ..	2,840/0		18,117/0
Robert McClenachan	0/105,000 (3)		0/610,313 (3)
Ronald J. Will .....	859/0		2,048/0
	2,723/0		17,839/0

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- (1) These options to acquire NSP Stock were granted to the Named Executives for services rendered to NRG and its subsidiaries.
  - (2) NSP's share price on December 31, 1996 was \$45.875.
  - (3) These options relate to NRG common stock. The options were granted at an exercise price of \$5.4375. The price per share of NRG common stock on December 31, 1996 was \$11.25. 75,000 of these options were cancelled in January, 1997. See "Option Grants in Last Fiscal Year."

NAME	NUMBER OF SECURITIES UNDERLYING OPTIONS GRANTED	% OF TOTAL OPTIONS GRANTED TO EMPLOYEES IN FISCAL YEAR	EXERCISE PRICE (\$/SH)	EXPIRATION DATE
LEONARD A. BLUHM.....	105,000 (2)	26	5.4375	10/21/2006

(RESTUBBED TABLE CONTINUED FROM ABOVE)

OPTION GRANTS IN LAST FISCAL YEAR (1)

NAME	POTENTIAL REALIZABLE VALUE AT ASSUMED ANNUAL RATES OF STOCK PRICE APPRECIATION FOR OPTION TERM	
	5% (\$)(3)	10% (\$)(3)
LEONARD A. BLUHM.....	359,100	909,930

- (1) These options relate to NRGG common stock. Options were granted to Mr. Bluhm under the NRG Generating (U.S.) Inc. 1996 Stock Option Plan. The options vest one-third annually on each of the first, second and third anniversaries of grant.
- (2) By agreement with NRGG, options to acquire 75,000 of these shares were withdrawn in January, 1997.
- (3) Amounts set forth in these columns reflect rates of appreciation required by Securities and Exchange Commission rules and are not intended to predict the future value of NRGG common stock.

PENSION PLAN TABLE

The following table illustrates the approximate retirement benefits payable to employees retiring at the normal retirement age of 65 years:

AVERAGE COMPENSATION (4 YEARS)	ESTIMATED ANNUAL BENEFITS FOR YEARS OF SERVICE INDICATED					
	YEARS OF SERVICE					
	5	10	15	20	25	30
\$ 50,000 .....	\$ 3,500	\$ 7,000	\$ 10,500	\$ 14,000	\$ 18,000	\$ 21,500
100,000 .....	7,500	15,500	23,000	30,500	38,000	46,000
150,000 .....	11,500	23,500	35,000	47,000	58,500	70,500
200,000 .....	16,000	31,500	47,500	63,000	79,000	95,000
250,000 .....	20,000	40,000	59,500	79,500	99,500	119,500
300,000 .....	24,000	48,000	72,000	96,000	120,000	144,000
350,000 .....	28,000	56,000	84,000	112,500	140,500	168,500
400,000 .....	32,000	64,500	96,500	128,500	160,500	193,000
450,000 .....	36,000	72,500	108,500	145,000	181,000	217,500
wage base:	\$62,700					

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 After an employee has reached 30 years of service, no additional years are used in determining pension benefits. The annual compensation used to calculate the average compensation shown in this table is based on the participant's base salary for the year (as shown on the Summary Compensation Table) and bonus compensation paid in that same year (as shown on the Summary Compensation Table). The benefit amounts shown are amounts computed in the form of a straight-life annuity. The amounts are not subject to offset for social security or otherwise.

As of September 30, 1997, each of the Named Executives had the following credited service: Mr. Peterson, 33.7 years, Mr. Bluhm, 26.3 years, Mr. McClenachan, 5.3 years, Mr. Will, 37.4 years, Mr. Mataczynski, 15.3 years.

LONG-TERM INCENTIVE PLAN COMPENSATION

The following table sets forth information concerning awards during fiscal 1996 to each of the Named Executives under the NRG Equity Plan.

LONG-TERM INCENTIVE PLAN AWARDS IN LAST FISCAL YEAR(1)

NAME	NUMBER OF SHARES, UNITS OR OTHER RIGHTS (#)	PERFORMANCE OR OTHER
		PERIOD UNTIL MATURATION OR PAYOUT(2)
David H. Peterson ...	5,500 (3)	7 years
	18,200 (4)	7 years
Leonard A. Bluhm ....	1,300 (3)	7 years
	1,700 (4)	7 years
Robert McClenachan ..	3,400 (3)	7 years
	4,500 (4)	7 years
Ronald J. Will.....	3,600 (3)	7 years
	4,800 (4)	7 years
Craig A. Mataczynski.....	3,800 (3)	7 years
	5,000 (4)	7 years

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- (1) Participants in the NRG Equity Plan are granted Equity Units, each of which is assigned a "Grant Price" at the discretion of the Chief Executive Officer and the Compensation Committee of the Board. Equity Units are valued upon vesting under a formula which takes into account the Company's cash flow, revenue growth, total debt and equity investment, among others. The amount of payment (if any) with respect to an Equity Unit is determined by the extent to which the value of the Equity Unit exceeds the Grant Price. The NRG Equity Plan does not contain threshold levels of performance or maximum payment amounts (or equivalent items).
  - (2) Equity Units vest annually in 20% increments, beginning on the third anniversary of the grant date of the Equity Unit. Participants are paid the value (if any) of Equity Units as soon as practicable following the end of year in which the Equity Unit vests.
  - (3) These Equity Units were granted at a Grant Price equal to the valuation of the Equity Unit on the date of grant. Such Equity Units will have value to the holders upon any increase in the valuation of the Equity Unit.
  - (4) These Equity Units were granted at a premium Grant Price (greater than the valuation of the Equity Unit on the date of grant). Such Equity Units will only have value to the holder after the valuation of the Equity Unit reaches the premium Grant Price.

## Compensation of Directors.

Directors receive no compensation for service as directors.

## Employment Contracts.

NRG has entered into an employment agreement with Mr. Peterson providing that Mr. Peterson will be employed as the highest level executive officer of NRG. The term of the agreement expires June 27, 2000. During the term of the agreement, Mr. Peterson's base salary will be reviewed at least annually by the Compensation Committee of the Board for possible increase. The agreement provides that Mr. Peterson will receive retirement and welfare benefits no less favorable than those provided to any other officer of NRG. In addition, the employment agreement provides for participation in a supplemental executive retirement plan such that the aggregate value of the retirement benefits that Mr. Peterson and his spouse will receive at the end of the term of the agreement under all the defined benefit pension plans of NRG and its affiliates will not be less than the aggregate value of the benefits he would have received had he continued, through the end of the term of the agreement, to participate in the NSP Deferred Compensation Plan, the NSP Excess Benefit Plan and the NSP Pension Plan, including amounts to compensate Mr. Peterson for the monthly defined benefit payments he would have received during the term of the employment agreement and prior to the date of his termination of employment if monthly benefit payments had commenced following the month in which he first became eligible for early retirement under the NSP Pension Plan. The employment agreement also provides for certain additional benefits to be paid upon Mr. Peterson's death. If Mr. Peterson's employment is terminated by the company without Cause or by Mr. Peterson with Good Reason (in each case as defined in the

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employment agreement), Mr. Peterson will continue to receive his salary, bonus (at greater of target bonus and actual bonus for the last plan year prior to termination), incentive compensation (with cash replacing equity based awards) and benefits under the agreement as if he had remained employed until the end of the term of the employment agreement and then retired (at which time he will be treated as eligible for retiree welfare benefits and other benefits provided to the retired senior executives).

## COMPENSATION COMMITTEE INTERLOCKS AND INSIDER PARTICIPATION

The compensation committee is comprised of Ms. Leshner and Mr. McIntyre. There are no compensation committee interlocks and no insider participation.

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## OWNERSHIP OF CAPITAL STOCK

Northern States Power Company, 414 Nicollet Mall, Minneapolis, Minnesota 55401, owns all of the outstanding capital stock of NRG.

## CERTAIN TRANSACTIONS

The transactions described or referred to below were entered into between related parties prior to the offering of the Senior Notes and were not the result of arms-length negotiations. Accordingly, the terms of these transactions may be more or less favorable to NRG than if they had been entered into on an arms-length basis.

As NRG's sole stockholder, NSP has the power to control the election of the directors and all other matters submitted for stockholder approval and may be deemed to have control over the management and affairs of NRG. Currently, there are no outside directors on NRG's board of directors. In circumstances involving a conflict of interest between NSP, as the sole stockholder and a significant customer of and supplier to NRG, and the holders of the Senior Notes as creditors of NRG, there can be no assurance that NSP would not exercise its power to control NRG in a manner that would benefit NSP to the detriment of the holders of the Senior Notes. NSP has policies in place, pursuant to applicable law, to ensure that its ratepayers are protected from affiliate transactions that may be adverse to the ratepayers' interests. The Indenture imposes no limitations on NRG's ability to pay dividends or to make other payments to NSP or on NRG's ability to enter into transactions with NSP or other affiliates of NRG.

## OPERATING AGREEMENTS

NRG has two agreements with NSP for the purchase of thermal energy. Under the terms of the agreements, NSP charges NRG for certain incremental costs (fuel, labor, plant maintenance and auxiliary power) incurred by NSP to produce the thermal energy. NRG paid NSP \$6 million in 1996, \$3.7 million in 1995 and \$6.6 million in 1994 under these agreements; NRG has paid \$3.5 million under them in the first nine months of 1997.

NRG has a renewable 10-year agreement with NSP, expiring on December 31, 2001, whereby NSP agrees to purchase RDF for use in certain of its boilers and NRG agrees to pay NSP an incentive fee to use RDF. Under this agreement, NRG received \$1.9 million and \$1.7 million from NSP and paid \$2.3 million and \$2.2 million to NSP in 1995 and 1994, respectively. In 1996, NRG received \$1.5 million and paid \$2.2 million. For the nine months ended September 30, 1997, NRG received \$1.3 million and paid \$2.3 million.

As of January 1, 1996, NRG entered into an operation and maintenance agreement with NSP with respect to the Elk River Facilities, under which NRG receives a base management fee and is reimbursed for costs it has incurred. The operation and maintenance agreement also provides for a management incentive fee payable to NRG, based upon the financial performance of the Elk River Facilities. In 1996 NRG earned a total management fee of \$1.5 million, in addition to reimbursed expenses. Management fees for the nine months ended September 30, 1997, totalled \$776,000 compared to \$761,000 for the same period in 1996.

## ADMINISTRATIVE SERVICES AGREEMENT

NRG and NSP have entered into an agreement to provide for the reimbursement of actual administrative services provided to each other, an allocation of NSP administrative costs and a working capital fee. Services provided by NSP to NRG are principally for cash management, accounting, employee relations and engineering. In addition, NRG employees participate in certain employee benefit plans of NSP. Also, in 1993 NSP employees assisted in operating certain NRG facilities for which NRG reimbursed NSP for gross wages plus an amount to cover employee benefits. During 1995 and 1994, NRG paid NSP \$6.8 million and \$6.2 million, respectively, as reimbursement for the cost of services provided. In 1996, NRG paid \$7.2 million and in the first nine months of 1997, NRG paid \$2.8 million for these services. Allocation is on a direct charge, actual cost basis where possible. When this is not possible, an allocation is made based upon employee headcounts, operating revenues and investment in fixed assets. Management believes that "allocated" costs approximate expenses that would be incurred on a stand alone basis.

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#### TAX SHARING AGREEMENT

NRG is included in the consolidated federal income tax and state franchise tax returns of NSP. NRG calculates its tax position on a separate company basis under a tax sharing agreement with NSP and receives payment from NSP for tax benefits and pays NSP for tax liabilities.

#### LONG-TERM DEBT

The construction cost of the Newport facility was financed through tax exempt variable rate resource recovery revenue bonds issued by the Counties, which have subsequently been converted to fixed rate resource recovery revenue bonds with an effective interest rate of 6.57% per annum and annual maturities each December through 2006. The proceeds of such bond issuance were loaned by the counties to NSP, which agreed under a loan agreement to pay to the counties amounts sufficient to pay debt service on the bonds. NRG issued a separate note to NSP in an original principal amount of approximately \$10 million as part of the consideration for the purchase of the facility from NSP.

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#### CERTAIN INDEBTEDNESS

NRG has funded investments and intends to fund future investments from certain outside sources, including those described below.

#### 1996 SENIOR NOTES

On January 29, 1996, NRG issued the 1996 Senior Notes in a transaction exempt from registration under the Securities Act. The 1996 Senior Notes were issued to fund some or all of NRG's equity investments in Schkopau and Latin Power, to pay a portion of the consideration for NRG's acquisition of interests in Collinsville and in O'Brien (for reorganization as NRGG), to make equity investments in Kladno and West Java, and for general corporate purposes, including investments in new projects. The 1996 Senior Notes are senior unsecured obligations of NRG and rank pari passu with all other senior unsecured indebtedness of NRG, including the Notes. The 1996 Senior Notes were assigned ratings of BBB-by S&P's Rating Group and Baa3 by Moody's. Redemption of the 1996 Senior Notes is not permitted prior to February 1, 2001. However, upon a change of control of NRG, each holder of the 1996 Senior Notes will have the right to require NRG to repurchase such holder's 1996 Senior Notes. Pursuant to the Indenture (the "1996 Indenture") under which the 1996 Senior Notes were issued, NRG is restricted from creating liens on its assets, is prohibited from merging except under certain circumstances and must maintain a specified minimum net worth. Failure to comply with these restrictive covenants could result in an event of default under the Indenture. Other events of default include nonpayment of principal or interest, certain cross-defaults, judgment decrees aggregating over \$20 million and certain events of bankruptcy.

#### REVOLVER

NRG has entered into a \$175 million revolving credit facility with a syndicate of banks led by ABN AMRO, which matures on March 17, 2000. Proceeds from the facility will be used for general corporate purposes, including letters of credit and interim funding for NRG project investments.

The facility allows for LIBOR and Base rate borrowing depending upon the days notice required and the term of drawing. The applicable margin is based upon the rate option selected and the assigned ratings of NRG. Pursuant to the terms of the agreement, NRG is restricted from creating liens on its assets, is prohibited from merging except under certain circumstances and must maintain a specified minimum net worth. Failure to comply with these restrictive covenants could result in an event of default. Other events of default include nonpayment of principal or interest, NSP's failure to own majority of outstanding voting stock of NRG, certain cross-defaults, and certain events of bankruptcy. At September 30, 1997, the Company had borrowed \$38 million against its revolving credit facility.

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#### DESCRIPTION OF NOTES

##### GENERAL

The Old Notes were issued, and the New Notes will be issued, under an Indenture, dated as of June 1, 1997 (the "Indenture"), between NRG and Norwest Bank Minnesota, National Association, as trustee (the "Trustee"). The following summaries of the material provisions of the Notes and the Indenture do not purport to be complete and are subject, and qualified in their entirety by reference, to all of the provisions of the Notes and the Indenture, including the definitions of certain terms therein. The definitions of certain capitalized terms used in the following summary are set forth below under " -- Certain Definitions." As used in this section, unless otherwise indicated, "NRG" refers solely to NRG Energy, Inc. and does not include any of its subsidiaries or affiliates.

The Notes are senior unsecured obligations of NRG, which conducts substantially all of its business through numerous subsidiaries and affiliates. As a result, all existing and future liabilities of the direct and indirect subsidiaries and affiliates of NRG will be effectively senior to the Notes. The Notes will not be guaranteed by, or otherwise be obligations of, NRG's project subsidiaries and project affiliates, NRG's other direct and indirect subsidiaries and affiliates or NSP.

##### PRINCIPAL, MATURITY AND INTEREST

The Notes are limited in aggregate principal amount to \$250,000,000 and will mature on June 15, 2007. Interest is payable on the Notes semiannually on June 15 and December 15 of each year, commencing December 15, 1997, until the principal is paid or made available for payment. Interest on the Notes will accrue from the most recent date to which interest has been paid or, if no interest has been paid, from the date of issuance. Interest will be computed on the basis of a 360-day year comprised of twelve 30-day months.

Payment of principal of the Notes will be made against surrender of such Notes at the office or agency of the Trustee in the Borough of Manhattan, The City of New York. Payment of interest on the Notes will be made to the person in whose name such Notes are registered at the close of business on the June 1 or December 1 immediately preceding the relevant interest payment date. For so long as the Notes are issued in book-entry form, payments of principal and interest shall be made in immediately available funds by wire transfer to DTC or its nominee. If the Notes are issued in certificated form to a Holder (as defined below) other than DTC, payments of principal and interest shall be made by check mailed to such Holder at such Holder's registered address or, upon written application by a Holder of \$1,000,000 or more in aggregate principal amount of Notes to the Trustee in accordance with the terms of the Indenture, by wire transfer of immediately available funds to an account maintained by such Holder with a bank. Defaulted interest will be paid in the same manner to Holders as of a special record date established in accordance with the Indenture.

All amounts paid by NRG to the Trustee for the payment of principal of, premium, if any, or interest on any Notes that remain unclaimed at the end of two years after such payment has become due and payable will be repaid to NRG and the Holders of such Notes will thereafter look only to NRG for payment thereof.

#### OPTIONAL REDEMPTION

NRG at its option, at any time, may redeem the Notes, in whole or in part (if in part, by lot or by such other method as the Trustee shall deem fair or appropriate) at the redemption price of 100% of principal amount of such Notes, plus accrued interest on the principal amount of such Notes, if any, to the redemption date, plus the applicable Make-Whole Premium.

To determine the applicable Make-Whole Premium for any Note, an independent investment banking institution of national standing selected by NRG (the "Investment Banker") will compute, as of the third Business Day prior to the redemption date, the sum of the present values of all of the remaining scheduled payments of principal and interest from the redemption date to maturity on such Note

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computed on a semiannual basis by discounting such payments (assuming a 360-day year consisting of twelve 30-day months) using a rate equal to the Treasury Rate plus 25 basis points. If the sum of these present values of the remaining payments as computed above exceeds the aggregate unpaid principal amount of the Note to be redeemed plus any accrued but unpaid interest thereon, the difference will be payable as a premium upon redemption of such Note. If the sum is equal to or less than such principal amount plus accrued interest, there will be no premium payable with respect to such Note.

#### CERTAIN COVENANTS

##### RESTRICTIONS ON LIENS

So long as any of the Notes are outstanding, NRG has agreed not to pledge, mortgage, hypothecate or permit to exist any mortgage, pledge or other lien upon any property at any time directly owned by NRG to secure any indebtedness for money borrowed which is incurred, issued, assumed or guaranteed by NRG ("Indebtedness"), without making effective provisions whereby the Notes shall be equally and ratably secured with any and all such



Indebtedness and with any other Indebtedness similarly entitled to be equally and ratably secured; provided, however, that this restriction shall not apply to or prevent the creation or existence of: (i) liens existing at the original date of issuance of the Notes; (ii) purchase money liens which do not exceed the cost or value of the purchased property; (iii) other liens not to exceed 10% of Consolidated Net Tangible Assets and (iv) liens granted in connection with extending, renewing, replacing or refinancing in whole or in part the Indebtedness (including, without limitation, increasing the principal amount of such Indebtedness) secured by liens described in the foregoing clauses (i) through (iii).

In the event that NRG shall propose to pledge, mortgage or hypothecate any property at any time directly owned by it to secure any Indebtedness, other than as permitted by clauses (i) through (iv) of the previous paragraph, NRG has agreed to give prior written notice thereof to the Trustee, who shall give notice to the Holders, and NRG has agreed, prior to or simultaneously with such pledge, mortgage or hypothecation, effectively to secure all the Notes equally and ratably with such Indebtedness.

The foregoing covenant does not restrict the ability of NRG's subsidiaries and affiliates to pledge, mortgage, hypothecate or permit to exist any mortgage, pledge or lien upon their assets, in connection with project financings or otherwise.

#### CONSOLIDATION, MERGER, SALE OF ASSETS

Without the consent of any Holder, NRG may consolidate with or merge into any other person, or convey, transfer or lease its properties and assets substantially as an entirety to any person, or permit any person to merge into or consolidate with NRG, if (i) NRG is the surviving or continuing corporation or the surviving or continuing corporation or purchaser or lessee is a corporation incorporated under the laws of the United States of America or Canada and assumes NRG's obligations under the Notes and under the Indenture and (ii) immediately before and after such transaction, no Event of Default (as defined herein) shall have occurred and be continuing.

Except for a sale of the assets of NRG substantially as an entirety as provided above, and other than assets required to be sold to conform with governmental regulations, the Indenture provides that NRG may not sell or otherwise dispose of any assets (other than short-term, readily marketable investments purchased for cash management purposes with funds not representing the proceeds of other asset sales) if on a pro forma basis, the aggregate net book value of all such sales during the most recent 12-month period would exceed 10% of Consolidated Net Tangible Assets computed as of the end of the most recent quarter preceding such sale; provided, however, that any such sales shall be disregarded for purposes of this 10% limitation if the proceeds are invested in assets in similar or related lines of business of NRG and, provided further, that NRG may sell or otherwise dispose of assets in excess of such 10% if the proceeds from such sales or dispositions, which are not reinvested as provided above, are retained by NRG as cash or cash equivalents or are used to purchase and retire Notes or 1996 Notes.

#### CHANGE OF CONTROL

Upon a Change of Control, each Holder shall have the right to require that NRG repurchase such Holder's Notes at a repurchase price in cash equal to 101% of the principal amount thereof plus accrued interest, if any, to the date of repurchase. A Change of Control shall not be deemed to have occurred if, after giving effect thereto, the Notes are rated BBB-or better by Standard & Poor's Ratings Group and Baa3 or better by Moody's Investors Service, Inc.

The Change of Control provisions may not be waived by the Trustee or the Board of Directors, and any modification thereof must be approved by each Holder. Nevertheless, the Change of Control provisions will not only afford

protection to holders of Notes, including protection against an adverse effect on the value of the Notes, in the event that NRG or its subsidiaries and affiliates incur additional Indebtedness, whether through recapitalizations or otherwise. Moreover, no assurance can be given that NRG would have sufficient liquidity to effectuate any required repurchase of Notes upon a Change of Control.

Within 30 days following any Change of Control, NRG will be required to mail a notice to each Holder (with a copy to the Trustee) stating (1) that a Change of Control has occurred and that such Holder has the right to require NRG to repurchase such Holder's Notes at a repurchase price in cash equal to 101% of the principal amount thereof plus accrued interest, if any, to the date of repurchase (the "Change of Control Offer"); (2) the circumstances and relevant facts regarding such Change of Control (including information with respect to pro forma historical income, cash flow and capitalization after giving effect to such Change of Control); (3) the repurchase date (which shall be a Business Day and be not earlier than 30 days or later than 60 days from the date such notice is mailed (the "Repurchase Date"); (4) that interest on any Senior Note tendered will continue to accrue; (5) that interest on any Senior Note accepted for payment pursuant to the Change of Control Offer shall cease to accrue after the Repurchase Date; (6) that Holders electing to have a Senior Note purchased pursuant to a Change of Control Offer will be required to surrender the Senior Note, with the form entitled "Option to Elect Purchase" on the reverse of the Senior Note completed, to the Trustee at the address specified in the notice prior to the close of business on the Repurchase Date; (7) that Holders will be entitled to withdraw their election if the Trustee receives, not later than the close of business on the third Business Day (or such shorter periods as may be required by applicable law) preceding the Repurchase Date, a telegram, telex, facsimile or letter setting forth the name of the Holder, the principal amount of Notes the Holder delivered for purchase and a statement that such Holder is withdrawing its election to have such Notes purchased; and (8) that Holders that elect to have their Notes purchased only in part will be issued new Notes in a principal amount equal to the unpurchased portion of the Notes surrendered.

For so long as the Notes are in global form, upon a Change of Control NRG will be required to deliver to DTC, for re-transmittal to its participants, a notice substantially to the effect specified in clauses (1) through (5) and (7) of the previous paragraph. Such notice shall also specify the required procedures for holders of interests in the Global Notes to tender the Notes (including the DTC Repayment Option Procedures to the extent applicable).

On the Repurchase Date, NRG shall (i) accept for payment such surrendered Notes or portions thereof tendered pursuant to the Change of Control and (ii) deposit with the Trustee money sufficient to pay the purchase price of all Notes or portions thereof so tendered. NRG will publicly announce the result of the Change of Control Offer as soon as practicable after the Repurchase Date.

NRG has agreed to comply with all applicable tender offer rules, including, without limitation, Rule 14e-1 under the Exchange Act in connection with a Change of Control Offer.

#### REPORTING OBLIGATIONS

NRG has agreed to furnish or cause to be furnished to Holders (and, at the request thereof, beneficial holders of Notes) annual consolidated financial statements of NRG prepared in accordance with GAAP (together with notes thereto, a report thereon by an independent accountant of established national reputation and a management's discussion and analysis of financial condition and results of operations). In addition, NRG will furnish or cause to be furnished to Holders (and, at the request thereof,

beneficial holders of Notes) unaudited condensed consolidated comparative balance sheets and statements of income and cash flows of NRG for each of the

first three fiscal quarters of each fiscal year and the corresponding quarter of the prior year, such statements to be furnished within 90 days after the end of the fiscal quarter covered thereby.

#### CERTAIN DEFINITIONS

"Business Day" means a day which is neither a legal holiday or a day on which banking institutions (including, without limitation, the Federal Reserve System) are authorized or required by law or regulation to close in The City of New York or Minneapolis, Minnesota.

"Change of Control" means the occurrence of one or more of the following events: (a) NSP (or its successors) ceases to own a majority of NRG's outstanding voting stock, (b) at any time following the occurrence of the event described in clause (a) above, a person or group of persons (other than NSP) becomes the beneficial owner, directly or indirectly, or has the absolute power to direct the vote of more than 35% of NRG's voting stock or (c) during any one year period, individuals who at the beginning of such period constitute NRG's Board of Directors cease to be a majority of the Board of Directors (unless approved by a majority of the current directors then in office who were either directors at the beginning of such period or who were previously so approved). A Change of Control shall be deemed not to have occurred if, following such an event described above, the Notes are rated BBB-or better by Standard & Poor's Ratings Group and Baa3 or better by Moody's Investors Service, Inc.

"Consolidated Net Tangible Assets" means, as of the date of any determination thereof, the total amount of all assets of NRG determined on a consolidated basis in accordance with GAAP as of such date less the sum of (a) the consolidated current liabilities of NRG determined in accordance with GAAP and (b) assets properly classified as Intangible Assets.

"Holder" means a registered holder of a Senior Note.

"Intangible Assets" means, as of the date of any determination thereof, with respect to any person, all assets properly classified as intangible assets in accordance with GAAP.

"Treasury Rate" means, with respect to each Note to be redeemed, a per annum rate (expressed as a semiannual equivalent and as a decimal and, in the case of United States Treasury bills, converted to a bond equivalent yield) determined by the Investment Banker to be the per annum rate equal to the semiannual yield to maturity of United States Treasury securities maturing on the Average Life Date (as defined below) of such Note, as determined by interpolation between the most recent weekly average yields to maturity for two series of Treasury securities, (A) one maturing as close as possible to, but earlier than, the Average Life Date of such Note and (B) the other maturing as close as possible to, but later than, the Average Life Date of such Note, in each case as published in the most recent H.15(519) (or, if a weekly average yield to maturity for United States Treasury securities maturing on the Average Life Date of such Note is reported in the most recent H.15(519), as published in H.15(519)). "H.15(519)" means "Statistical Release H.15(519), Selected Interest Rates," or any successor publication, published by the Board of Governors of the Federal Reserve System. The "most recent H.15(519)" means the latest H.15(519) which is published prior to the close of business on the third Business Day prior to the applicable redemption date. The "Average Life Date" for any Note to be redeemed shall be the date which follows the redemption date by a period equal to the Remaining Weighted Average Life of such Note. The "Remaining Weighted Average Life" of such Note with respect to the redemption of such Note is the number of days equal to the quotient obtained by dividing (A) the sum of the products obtained by multiplying (1) the amount of each remaining principal payment on such Note by (2) the number of days from and including the redemption date, to but excluding the scheduled payment date of such principal payment by (B) the unpaid principal amount of such Note.

#### EVENTS OF DEFAULT

The following constitute Events of Default under the Notes:

(a) failure to pay any interest on any Senior Note when due, which failure continues for 30 days;

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(b) failure to pay principal or premium (including in connection with a Change of Control) when due;

(c) failure of NRG to perform any other covenant in the Notes or the Indenture for a period of 30 days after written notice to NRG by the Trustee or by the Holders of at least 25% in aggregate principal amount of the Notes;

(d) an event of default occurring under any instrument of NRG under which there may be issued, or by which there may be secured or evidenced, any indebtedness for money borrowed that has resulted in the acceleration of such indebtedness, or any default occurring in payment of any such indebtedness at final maturity (and after the expiration of any applicable grace periods), other than (i) indebtedness which is payable solely out of the property or assets of a partnership, joint venture or similar entity of which NRG or any of its subsidiaries or affiliates is a participant, or which is secured by a lien on the property or assets owned or held by such entity, without further recourse to NRG or (ii) such indebtedness of NRG not exceeding \$20,000,000;

(e) one or more final judgments, decrees or orders of any court, tribunal, arbitrator, administrative or other governmental body or similar entity for the payment of money aggregating more than \$20,000,000 shall be rendered against NRG (excluding the amount thereof covered by insurance) and shall remain undischarged, unvacated and unstayed for more than 90 days, except while being contested in good faith by appropriate proceedings; and

(f) certain events of bankruptcy, insolvency or reorganization in respect of NRG.

The Indenture provides that if an Event of Default (other than an Event of Default based on an event of bankruptcy, insolvency or reorganization of NRG) shall occur and be continuing, either the Trustee or the Holders of not less than 25% in aggregate principal amount of the Notes may, by written notice to NRG (and to the Trustee if given by Holders), declare the principal of all Notes to be immediately due and payable, but upon certain conditions such declaration may be annulled and past defaults (except, unless theretofore cured, a default in payment of principal, premium or interest) may be waived by the Holders of a majority in aggregate principal amount of Notes then outstanding. Notwithstanding the foregoing, any Holder shall have the right to institute suit to enforcement of any overdue payment owing to such Holder pursuant to the Notes. If an Event of Default due to the bankruptcy, insolvency or reorganization of NRG occurs, all unpaid principal, premium, if any, and interest in respect of the Notes will automatically become due and payable. Pursuant to the Indenture NRG is required to provide an annual statement of compliance with the terms of the Indenture.

The Holders of a majority in principal amount of the Notes then outstanding shall have the right to direct the time, method and place of conducting any proceeding for any remedy available to the Trustee under the Indenture, provided that the Holders shall have offered to the Trustee reasonable indemnity against expenses and liabilities. Notwithstanding the foregoing, the Trustee shall have the right to decline to follow any such direction if the Trustee and its counsel shall determine that the action requested is unlawful, would involve the Trustee in personal liability or will be unduly prejudicial to the interests of Holders not joining in the giving of such direction.

MODIFICATION OF THE INDENTURE

The Indenture contains provisions permitting NRG and the Trustee, with the consent of the Holders of not less than a majority in principal amount of the Notes then outstanding, to modify the Indenture or the rights of the Holders, except that no such modification may, without the consent of each Holder, (i) extend the final maturity of any of the Notes or reduce the principal amount thereof, or reduce the rate or extend the time of payment of interest thereon, or reduce any amount payable on redemption thereof, or impair or affect the right of any Holder to institute suit for the payment thereof or make any change in the covenant regarding a Change of Control or (ii) reduce the percentage of Notes, the consent of the Holders of which is required for any such modification.

NRG and the Trustee without the consent of any Holder may amend the Indenture and the Notes for the purpose of curing any ambiguity, or of curing, correcting or supplementing any defective provision

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thereof, or in any manner which NRG and the Trustee may determine is not inconsistent with the Notes and will not adversely affect the interest of any Holder.

#### DEFEASANCE AND COVENANT DEFEASANCE

##### DEFEASANCE

The Indenture provides that NRG will be deemed to have paid and will be discharged from any and all obligations in respect of the Notes, on the 123rd day after the deposit referred to below has been made, and the provisions of the Indenture will cease to be applicable with respect to the Notes (except for, among other matters, certain obligations to register the transfer of or exchange of the Notes, to replace stolen, lost or mutilated Notes, to maintain paying agencies and to hold funds for payment in trust) if (A) NRG has deposited with the Trustee, in trust, money and/or U.S. Government Obligations (as defined in the Indenture) that, through the payment of interest and principal in respect thereof in accordance with their terms will provide money in an amount sufficient to pay the principal of, premium, if any, and accrued interest on the Notes, at the time such payments are due in accordance with the terms of the Indenture, (B) NRG has delivered to the Trustee (i) an opinion of counsel to the effect that Holders will not recognize income, gain or loss for federal income tax purposes as a result of NRG's exercise of its option under the defeasance provisions of the Indenture and will be subject to federal income tax on the same amount and in the same manner and at the same times as would have been the case if such deposit, defeasance and discharge had not occurred, which opinion of counsel must be based upon a ruling of the Internal Revenue Service to the same effect or a change in applicable federal income tax law or related treasury regulations after the date of the Indenture and (ii) an opinion of counsel to the effect that the defeasance trust does not constitute an "investment company" within the meaning of the Investment Company Act of 1940, as amended, and after the passage of 123 days following the deposit, the trust fund will not be subject to the effect of Section 547 of the U.S. Bankruptcy Code or Section 15 of the New York Debtor and Creditor Law, (C) immediately after giving effect to such deposit, no Event of Default, or event that after the giving of notice or lapse of time or both would become an Event of Default, shall have occurred and be continuing on the date of such deposit or during the period ending on the 123rd day after the date of such deposit, and such deposit shall not result in a breach or violation of, or constitute a default under, any other agreement or instrument to which NRG is a party or by which NRG is bound and (D) if at such time the Notes are listed on a national securities exchange, NRG has delivered to the Trustee an opinion of counsel to the effect that the Notes will not be delisted as a result of such deposit and discharge.

##### DEFEASANCE OF CERTAIN COVENANTS AND CERTAIN EVENTS OF DEFAULT

The Indenture further provides that the provisions of the Indenture will cease to be applicable with respect to (i) the covenants described under "Certain Covenants -- Restrictions on Liens" and "Change of Control" and (ii)

clause (c) under "Events of Default" with respect to such covenants and clauses (d) and (e) under "--Events of Default" upon the deposit with the Trustee, in trust, of money and/or U.S. Government Obligations that through the payment of interest and principal in respect thereof in accordance with their terms will provide money in an amount sufficient to pay the principal of, premium, if any, and accrued interest on the Notes, the satisfaction of the conditions described in clauses (B)(ii), (C) and (D) of the preceding paragraph and the delivery by NRG to the Trustee of an opinion of counsel to the effect that, among other things, the Holders of the Notes will not recognize income, gain or loss for federal income tax purposes as a result of such deposit and defeasance of certain covenants and Events of Default and will be subject to federal income tax on the same amount and in the same manner and at the same times as would have been the case if such deposit and defeasance had not occurred.

#### DEFEASANCE AND CERTAIN OTHER EVENTS OF DEFAULT

If NRG exercises its option to omit compliance with certain covenants and provisions of the Indenture with respect to the Notes as described in the immediately preceding paragraph and the Notes are declared due and payable because of the occurrence of an Event of Default that remains applicable,

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the amount of money and/or U.S. Government Obligations on deposit with the Trustee will be sufficient to pay amounts due on the Notes at the time of their stated maturity, but may not be sufficient to pay amounts due on the Notes at the time of acceleration resulting from such Event of Default. NRG shall remain liable for such payments.

#### FORM, DENOMINATION, BOOK-ENTRY PROCEDURES AND TRANSFER

The Old Notes were initially represented by two Notes in registered, global form (collectively, the "Old Global Notes"). The New Notes will initially be represented by a Note in registered, global form (the "New Global Note" and together with the Old Global Notes, the "Global Notes"). The Old Global Notes were, and the New Global Note will be, deposited upon issuance with the Trustee as custodian for DTC and registered in the name of Cede & Co., DTC's nominee, for credit to any account of a direct or indirect participant in DTC as described below.

Except as set forth below, the Global Notes may be transferred, in whole or in part, only to another nominee of DTC or to a successor of DTC or its nominee. Beneficial interests in the Global Notes may not be exchanged for Senior Notes in certificated forms except in the limited circumstances described under "--Exchange of Book-Entry Notes for Certificated Notes" below.

#### DEPOSITARY PROCEDURES

DTC has advised NRG that DTC is a limited-purpose trust company created to hold securities for its Participants and to facilitate the clearance and settlement of transactions in those securities between Participants through electronic book-entry changes in accounts of the Participants. The Participants include securities brokers and dealers (including the Initial Purchasers), banks, trust companies, clearing corporations and certain other organizations. Access to DTC's system is also available to other entities such as banks, brokers, dealers and trust companies that clear through or maintain a custodial relationship with a Participant, either directly or indirectly (collectively, the "Indirect Participants"). Persons who are not Participants may beneficially own securities held by or on behalf of DTC only through the Participants or the Indirect Participants. The ownership interest and transfer of ownership interest of each actual purchase of each security held by or on behalf of DTC are recorded on the records of the Participants and Indirect Participants.

DTC has also advised NRG that, pursuant to procedures established by it, (i) upon deposit of the Global Notes, DTC will credit the accounts of

Participants designated by the Initial Purchasers with portions of the principal amount of the Global Notes and (ii) ownership of such interests in the Global Notes will be shown on, and the transfer of ownership thereof will be effected only through, records maintained by DTC (with respect to the Participants) or by the Participants and the Indirect Participants (with respect to other owners of beneficial interests in the Global Notes).

Investors in the Global Notes may hold their interests therein directly through DTC if they are Participants in such system, or indirectly through organizations which are Participants in such system. All interests in a Global Note may be subject to the procedures and requirements of DTC. The laws of some states require that certain persons take physical delivery in certificated form of securities that they own. Consequently, the ability to transfer beneficial interests in a Global Note to such persons will be limited to that extent. Because DTC can act only on behalf of Participants, which in turn act on behalf of Indirect Participants and certain banks, the ability of a person having beneficial interests in a Global Note to pledge such interest to persons that do not participate in the DTC system, or otherwise take actions in respect of such interest, may be affected by the lack of a physical certificate evidencing such interests. For certain other restrictions on the transferability of the Notes, see "--Exchange of Book-Entry Notes for Certificated Notes" below.

Except as described below, owners of interests in the Global Notes will not have Notes registered in their name, will not receive physical delivery of Notes in certificated form and will not be considered the registered owners of holders thereof under the Indenture for any purpose.

Payments in respect of the Global Note registered in the name of DTC or its nominee will be payable by the Trustee to DTC in its capacity as the registered holder under the Indenture. Under the terms of

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the Indenture, the Trustee will treat the persons in whose names the Notes, including the Global Notes, are registered as the owners thereof for the purpose of receiving such payments and for any and all purposes whatsoever. Consequently, neither the Trustee nor any agent thereof has or will have any responsibility or liability for (i) any aspect of DTC's records or any Participant's or Indirect Participant's records relating to or payments made on account of beneficial ownership interests in the Global Note or for maintaining, supervising or reviewing any of DTC's records or any Participant's or Indirect Participant's records relating to the beneficial ownership interests in the Global Note or (ii) any other matter relating to the actions and practices of DTC or any of its Participants or Indirect Participants. DTC has advised NRG that its current practice, upon receipt of any payment in respect of securities such as the Notes, is to credit the accounts of the relevant Participants with the payment on the payment date, in amounts proportionate to their respective holdings in principal amount of beneficial interests in the relevant security as shown on the records of DTC unless DTC has reason to believe it will not receive payment on such payment date. Payments by the Participants and the Indirect Participants to the beneficial owners of Notes will be governed by standing instructions and customary practices and will be the responsibility of the Participants or the Indirect Participants and will not be the responsibility of DTC, the Trustee or NRG. Neither NRG nor the Trustee will be liable for any delay by DTC or any of its Participants in identifying the beneficial owners of the Notes, and NRG and the Trustee may conclusively rely on and will be protected in relying on instructions from DTC or its nominee for all purposes.

DTC has advised NRG that it will take any action permitted to be taken by a holder of Notes only at the direction of one or more Participants to whose account with DTC interests in the Global Notes are credited and only in respect of such portion of the Notes as to which such Participant or Participants has or have given such direction. However, if there is an Event of Default under the Declaration, DTC reserves the right to exchange the Global Notes for Notes in certificated form and to distribute such Notes to its Participants.

The information in this section concerning DTC and its book-entry system has been obtained from sources that NRG believes to be reliable, but NRG has not independently determined the accuracy thereof. NRG will not have any responsibility for the performance by DTC or its Participants of their respective obligations under the rules and procedures governing their operations.

#### EXCHANGE OF BOOK-ENTRY NOTES FOR CERTIFICATED NOTES

A Global Note is exchangeable for Notes in registered certificated form if (i) DTC notifies NRG that it is unwilling or unable to continue as clearing agency for the Global Note or has ceased to be a clearing agency registered under the Exchange Act and NRG thereupon fails to appoint a successor clearing agency within 90 days, (ii) NRG in its sole discretion elects to cause the issuance of definitive certificated Notes or (iii) there has occurred and is continuing an Event of Default or any event which after notice or lapse of time or both would be an Event of Default under the Indenture. In addition, beneficial interests in a Global Note may be exchanged for certificated Notes upon request but only upon at least 20 days, prior written notice given to the Trustee by or on behalf of DTC in accordance with customary procedures. In all cases certificated Notes delivered in exchange for any Global Note or beneficial interest therein will be registered in the names, and issued in denominations of \$100,000 and integral multiples of \$1,000 in excess thereof, requested by or on behalf of the clearing agency (in accordance with its customary procedures).

#### THE TRUSTEE

Norwest Bank Minnesota, National Association is the Trustee under the Indenture. NRG and its affiliates also maintain banking and other commercial relationships with the Trustee and its affiliates in the ordinary course of business.

#### GOVERNING LAW

The Indenture and the Notes will be governed by, and construed in accordance with, the laws of the State of New York.

#### REGISTRATION RIGHTS

Holder of New Notes (other than as set forth below) are not entitled to any registration rights with respect to the New Notes. Pursuant to the Registration Rights Agreement, Holders of Old Notes are entitled to certain registration rights. Under the Registration Rights Agreement, NRG has agreed, for the benefit of the Holders of the Old Notes, that it will, at its cost, (i) file a registration statement with the Commission with respect to the Exchange Offer within 60 days after the Closing Date (or if the 60th day is not a business day, the first business day thereafter) and (ii) use its best efforts to cause such registration statement to be declared effective under the Securities Act within 180 days after the Closing Date (or if the 180th day is not a business day, the first business day thereafter). The Registration Statement of which this Prospectus is a part constitutes the Exchange Offer Registration Statement.

In the event that any Holder shall notify NRG that (A) such Holder is not eligible to participate in the Exchange Offer or (B) such Holder may not resell the New Notes acquired by it in the Exchange Offer to the public without delivering a prospectus and the prospectus contained in the Exchange Offer Registration Statement is not appropriate or available for such resales by such Holder or (C) such Holder is a broker-dealer and holds Old Notes that are part of an unsold allotment from the original sale of the Old Notes, NRG will file with the Commission a shelf registration statement (the "Shelf Registration Statement") to cover resales of Transfer Restricted Securities by such Holders who satisfy certain conditions relating to the provision of information in connection with the Shelf Registration Statement. NRG will use



its best efforts to cause the Shelf Registration Statement, if applicable, to be declared effective on or prior to 215 days after the date on which NRG becomes obligated to file the Shelf Registration Statement or receives certain notices from holders of the Old Notes and will use its best efforts to keep the Shelf Registration Statement continuously effective until the earlier of (i) two years after the effective date thereof, (ii) the date on which all Transfer Restricted Securities registered thereunder are disposed of in accordance therewith and (iii) one year after the effective date thereof if such Shelf Registration Statement is filed at the request of an Initial Purchaser. For purposes of the foregoing, "Transfer Restricted Securities" means each Old Note until the earliest to occur of (i) the date on which such Old Note has been exchanged for a New Note in the Exchange Offer, (ii) the date on which such Old Note has been effectively registered under the Securities Act and disposed of in accordance with the Shelf Registration Statement or (iii) the date on which such Old Note is distributed to the public pursuant to Rule 144 under the Securities Act.

A Holder of Old Notes who sells such Old Notes pursuant to the Shelf Registration Statement generally would be required to be named as a selling securityholder in the related prospectus and to deliver a prospectus to purchasers, will be subject to certain of the civil liability provisions under the Securities Act in connection with such sales and will be bound by the provisions of the Registration Rights Agreement that are applicable to such a Holder (including certain indemnification obligations).

The summary herein of certain provisions of the Registration Rights Agreement does not purport to be complete and is subject to, and is qualified in its entirety by reference to, all the provisions of the Registration Rights Agreement, a copy of which is filed as an exhibit to the Registration Statement of which this Prospectus is a part.

#### SPECIAL INTEREST

In the event that either the Exchange Offer is not consummated or a Shelf Registration Statement with respect to any Transfer Restricted Securities is not declared effective on or prior to the 215th day following the date of original issuance of any Transfer Restricted Securities (or if the 215th day is not a business day, the first business day thereafter), interest will accrue (in addition to stated interest on the Securities) from and including the next day following such 215-day period. In each case such additional interest (the "Special Interest") will be payable in cash semiannually in arrears each June 15, and December 15, commencing December 15, 1997, at a rate per annum equal to 0.25% of the principal amount of such Transfer Restricted Securities. The aggregate amount of Special Interest payable pursuant to the above provisions will in no event exceed 0.25% per annum of the principal amount of any Transfer Restricted Securities. Upon the consummation of the Exchange Offer or the effectiveness of a Shelf Registration Statement, after the 215-day period described above, the Special Interest payable on

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such Transfer Restricted Securities from the date of such effectiveness or consummation, as the case may be, will cease to accrue and all accrued and unpaid Special Interest shall be paid to the holders of such Transfer Restricted Securities.

In the event that a Shelf Registration Statement is declared effective pursuant to the preceding paragraph, if the Company fails to keep such Registration Statement continuously effective for the period required by this Agreement, then from such time as the Shelf Registration Statement is no longer effective until the earlier of (i) the date that the Shelf Registration Statement is again deemed effective, (ii) the date that is the second anniversary of the Closing Date or (iii) the date as of which all of the Securities are sold pursuant to the Shelf Registration Statement, Special Interest shall accrue at a rate per annum equal to 0.25% of the principal amount of the Securities and shall be payable in cash semiannually in arrears each June 15 and December 15, commencing December 15, 1997.

The filing and effectiveness of the Registration Statement of which this Prospectus is a part and the consummation of the Exchange Offer will eliminate all rights of the Holders of Old Notes eligible to participate in the Exchange Offer to receive Special Interest that would have been payable if such actions had not occurred.

CERTAIN UNITED STATES FEDERAL INCOME TAX CONSIDERATIONS

The following is a discussion of certain United States Federal income tax considerations associated with the exchange of Old Notes for New Notes and the ownership and disposition of the New Notes by Holders who acquire the New Notes pursuant to the Exchange Offer. This discussion is based upon existing United States Federal income tax law, which is subject to change, possibly retroactively. This discussion does not describe all relevant aspects of United States Federal income taxation that may be important to particular Holders in light of their individual investment circumstances or certain types of Holders subject to special tax rules (e.g., financial institutions, insurance companies, broker-dealers, or tax-exempt organizations) or to persons that hold or will hold the Notes as a position in a "straddle" or as part of a "hedging" or "conversion" transaction, all of whom may be subject to tax rules that differ significantly from those described below. In addition, this discussion does not describe any foreign, state, or local tax considerations. This discussion deals only with Old Notes and New Notes held by initial purchasers of Old Notes as "capital assets" (generally, property held for investment) within the meaning of Section 1221 of the Internal Revenue Code of 1986, as amended (the "Code").

For purposes of this discussion, a "U.S. Holder" is (i) an individual citizen or resident of the United States, (ii) a corporation, partnership or other entity created or organized in or under the laws of the United States or of any political subdivision thereof, (iii) an estate that is subject to United States federal income taxation without regard to the source of its income, or (iv) a trust whose administration is subject to the primary supervision of a United States court and which has one or more United States fiduciaries who have the authority to control all substantial decisions of the trust. For purposes of this discussion, a "Non-U.S. Holder" is any Holder who is not a U.S. Holder.

PROSPECTIVE HOLDERS OF THE NEW NOTES ARE URGED TO CONSULT THEIR TAX ADVISORS CONCERNING THE PARTICULAR TAX CONSEQUENCES OF ACQUIRING, OWNING, AND DISPOSING OF THE NEW NOTES, INCLUDING THE APPLICABILITY AND EFFECT OF ANY STATE, LOCAL AND FOREIGN INCOME AND OTHER TAX LAWS.

EXCHANGE OFFER

The consummation of the Exchange Offer will not be a taxable event for United States Federal income tax purposes. Accordingly, a Holder receiving New Notes pursuant to the terms of the Exchange Offer will have the same adjusted tax basis and holding period in New Notes, for United States Federal income tax purposes, as such Holder had in the Old Notes tendered in exchange

therefor.

#### U.S. HOLDERS

Interest payable on the New Notes will be includible in the income of a Holder in accordance with such Holder's normal method of accounting. Except in the case of an Old Note purchased at a discount to its original issue price, a Holder will recognize capital gain or loss upon the sale or other disposition of a New Note in an amount equal to the difference between the amount realized from such disposition and his tax basis in the New Note. Under recently-enacted legislation, net capital gain (i.e., generally, capital gain in excess of capital loss) recognized by an individual Holder upon the disposition of New Notes that have been held for more than 18 months will generally be subject to tax at a rate not to exceed 20%. Net capital gain recognized by a Holder upon the disposition of New Notes that have been held for more than 12 months but for not more than 18 months will continue to be subject to tax at a rate not to exceed 28% and net capital gain from the disposition of New Notes that have been held for 12 months or less will continue to be subject to tax at ordinary income tax rates. In addition, capital gain recognized by a corporate Holder will continue to be subject to tax at the ordinary income tax rates applicable to corporations.

In the case of a Holder who has purchased a New Note at a discount to its original issue price in excess of a statutorily defined de minimis amount and has not elected to include such discount in income on a current basis, (i) any gain recognized on the disposition of a New Note will be subject to tax as ordinary income, rather than capital gain, to the extent of accrued market discount and (ii) a portion of the interest expense on indebtedness incurred or maintained to purchase or carry such note may not be deducted until the note is disposed of in a taxable transaction.

#### NON-U.S. HOLDERS

Under present United States federal income and estate tax law, assuming certain certification requirements are satisfied (which include identification of the beneficial owner of the instrument), and subject to the discussion of backup withholding below:

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(a) payments of interest on the New Notes to any Non-U.S. Holder generally will not be subject to United States federal income or withholding tax, provided that (1) the Holder does not actually or constructively own 10% or more of the total combined voting power of all classes of stock of NRG entitled to vote, (2) the Holder is not a controlled foreign corporation that is related to NRG through stock ownership, and (3) such interest payments are not effectively connected with the conduct of a United States trade or business of the Holder;

(b) a Holder who is a Non-U.S. Holder generally will not be subject to the United States federal income tax on gain realized on the sale, exchange or other disposition of a New Note, unless (1) such Holder is an individual who is present in the United States for 183 days or more during the taxable year and certain other requirements are met, or (2) the gain is effectively connected with the conduct of a United States trade or business of the Holder; and

(c) if interest on the New Notes is exempt from withholding of United States federal income tax under the rules above, the New Notes will not be included in the estate of a deceased Non-U.S. Holder for United States federal estate tax purposes.

The certification referred to above may be made on an Internal Revenue Service ("IRS") Form W-8 or substantially similar substitute form.

#### BACKUP WITHHOLDING AND INFORMATION REPORTING

A Holder of the New Notes may be subject to information reporting and to

backup withholding at a rate of 31 percent of certain amounts paid to the Holder unless such Holder (a) is a corporation or comes within certain other exempt categories and, when required, provides proof of such exemption or (b) provides a correct taxpayer identification number, certifies as to no loss of exemption from backup withholding and otherwise complies with applicable requirements of the backup withholding rules. Under current regulations, information reporting and backup withholding do not apply to interest payments made at an address outside the United States to a Holder of the New Notes that is not a U.S. Holder if the beneficial owner of the New Notes (a) provides a statement in which such owner certifies, under penalties of perjury, that such owner is not a United States person and provides such owner's name and address or (b) otherwise establishes an exemption; provided that NRG or its paying agent, as the case may be, does not have actual knowledge that the Holder is a U.S. Holder.

Under current regulations, payment of the proceeds from the sale of the New Notes to or through a foreign office of a "broker" (as defined in applicable Treasury regulations) will not be subject to information reporting or backup withholding, except that if the broker is a United States person, a controlled foreign corporation for United States federal income tax purposes or a foreign person 50 percent or more of whose gross income from all sources for the three-year period ending with the close of its taxable year preceding the payment was effectively connected with a United States trade or business, information reporting (but not backup withholding) may apply to such payments unless the broker has in its records documentary evidence that the Holder of the New Notes is not a United States person and certain conditions are met or the Holder of the New Note otherwise establishes an exemption. Payment of the proceeds from a sale of the New Notes to or through the United States office of a broker is subject to information reporting and backup withholding unless the Holder certifies as to its non-U.S. status under penalties of perjury or otherwise establishes an exemption.

Any amounts withheld under the backup withholding rules are not additional tax and may be credited against the U.S. Holder's United States federal income tax liability, provided that the required information is furnished to the IRS.

Recently, the Treasury Department promulgated final regulations regarding the withholding and information reporting rules discussed above. In general, the final regulations do not significantly alter the substantive withholding and information reporting requirements described above but unify current certification procedures and forms and clarify reliance standards. The final regulations will generally be effective for payments made after December 31, 1998, subject to certain transition rules.

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#### RATINGS

Standard & Poor's Ratings Group and Moody's Investors Service, Inc. have given the Old Notes the ratings set forth under "Summary -- Summary Description of the New Notes." NRG expects that the New Notes would be assigned the same ratings as the Old Notes. Such ratings reflect only the views of these organizations, and an explanation of the significance of each such rating may be obtained from Standard & Poor's Corporation, 25 Broadway, New York, New York 10004 and Moody's Investors Service, Inc., 99 Church Street, New York, New York 10007. There is no assurance that such ratings will continue for any given period of time or that they will not be revised downward or withdrawn entirely by such rating agencies or either of them if, in their judgment, circumstances so warrant. A downward change in or withdrawal of such ratings or either of them may have an adverse effect on the market price of the Notes.

## PLAN OF DISTRIBUTION

Each broker-dealer that receives New Notes for its own account pursuant to the Exchange Offer must acknowledge that it will deliver a prospectus in connection with any resale of such New Notes. This Prospectus as it may be amended or supplemented from time to time, may be used by a broker-dealer in connection with the resales of New Notes received in exchange for Old Notes where such Old Notes were acquired as a result of market-making activities or other trading activities. NRG has agreed that, starting on the Expiration Date and ending on the close of business on the 90th day following the Expiration Date, it will make this Prospectus, as amended or supplemented, available to any broker-dealer for use in connection with any such resale. In addition, until , 1997 (90 days from the date of this Prospectus), all dealers effecting transactions in the New Notes may be required to deliver a prospectus.

NRG will not receive any proceeds from any sale of New Notes by broker-dealers or any other persons. New Notes received by broker-dealers for their own account pursuant to the Exchange Offer may be sold from time to time in one or more transactions in the over-the-counter market, in negotiated transactions, through the writing of options on the New Notes or a combination of such methods of resale, at market prices prevailing at the time of resale, at prices related to such prevailing market prices or negotiated prices. Any such resale may be made directly to purchasers or to or through brokers or dealers who may receive compensation in the form of commissions or concessions from any such broker-dealer and/or purchasers of any such New Notes. Any broker-dealer that resells New Notes that were received by it for its own account pursuant to the Exchange Offer and any broker or dealer that participates in a distribution of such New Notes may be deemed to be an "underwriter" within the meaning of the Securities Act and any profit on any such resale of New Notes and any commissions or concessions received by any such persons may be deemed to be underwriting compensation under the Securities Act. The Letter of Transmittal states that by representing that it will deliver and by delivering a prospectus, a broker-dealer will not be deemed to admit that it is an "underwriter" within the meaning of the Securities Act.

For a period of 90 days after the Expiration Date, NRG will promptly send additional copies of this Prospectus and any amendment or supplement to this Prospectus to any broker-dealer that requests such documents in the Letter of Transmittal. NRG has agreed to pay all expenses incident to NRG's performance of, or compliance with, the Registration Rights Agreement and will indemnify the Holders (including any broker-dealers) and certain parties related to the Holders against certain liabilities, including liabilities under the Securities Act.

Certain legal matters with respect to the validity of the New Notes will be passed upon for NRG by Skadden, Arps, Slate, Meagher & Flom LLP and by James J. Bender, Vice President and General Counsel of NRG.

EXPERTS

The consolidated financial statements of NRG as of December 31, 1995 and 1996 and for each of the two years in the period ended December 31, 1996 included in this Prospectus have been so included in reliance on the report of Price Waterhouse LLP, independent accountants, given on the authority of said firm as experts in auditing and accounting.

The financial statements of NRG as of December 31, 1994 included in this Prospectus have been so included in reliance on the report of Deloitte & Touche LLP, independent auditors, given on the authority of said firm as experts in auditing and accounting.

The financial statements of Sunshine State Power BV and Sunshine State Power (No. 2) BV as of December 31, 1996, 1995 and 1994 and for each of the three years in the period ended December 31, 1996 included in this Prospectus have been so included in reliance on the reports of Price Waterhouse Nederland BV, independent accountants, given on the authority of said firm as experts in auditing and accounting.

The balance sheets as of December 31, 1995 and 1994 of San Joaquin Valley Energy Partners I, L.P. (the Partnership), and the statements of income, partners' equity and cash flows for each of the two years in the period ended December 31, 1995, included in this Prospectus, have been included herein in reliance on the report of Coopers & Lybrand L.L.P., independent accountants, which report includes an explanatory paragraph disclosing that the Partnership entered into an agreement during 1995 whereby the Partnership's power purchase contracts were transferred back to Pacific Gas & Electric, given on the authority of that firm as experts in accounting and auditing.

The financial statements of Mittledeutsche Braunkohlengesellschaft mbH as of December 31, 1996, 1995 and 1994 and each of the three years in the period ended December 31, 1996 included in this Prospectus have been so included in reliance on the report of Deloitte & Touche GmbH, independent auditors, given on the authority of said firm as experts in auditing and accounting.

The financial statements of Saale Energie GmbH as of December 31, 1996 and the year ended December 31, 1996 included in this Prospectus have been so included in reliance on the report of Deloitte & Touche GmbH, independent auditors, given on the authority of said firm as experts in auditing and accounting.

The financial statements of Quiet Life Limited as of June 30, 1997 and of Loy Yang Power Limited as of June 30, 1996 and for the two years then ended included in this Prospectus have been so included in reliance on the report of the Auditor-General of Australia.

The reconciliation to U.S. GAAP of the financial statements of Loy Yang Power Limited covering the period from February 1, 1995 to June 30, 1995, the financial year ended June 30, 1996 and the period from July 1, 1996 to May 12, 1997 included in this Prospectus have been so included in reliance on the report of Arthur Andersen, independent auditors, given on the authority of said firm as experts in auditing and accounting.

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REPORT OF INDEPENDENT ACCOUNTANTS

The Board of Directors and Shareholders  
 NRG Energy, Inc.

In our opinion, the accompanying consolidated balance sheets and the related consolidated statements of income, of stockholder's equity, and of cash flows present fairly, in all material respects, the financial position of NRG Energy, Inc. (a wholly-owned subsidiary of Northern States Power Company) and its subsidiaries at December 31, 1996 and 1995, and the results of their operations and their cash flows for the years then ended in conformity with generally accepted accounting principles. These financial statements are the responsibility of NRG's management; our responsibility is to express an opinion on these financial statements based on our audits. We conducted our audits of these statements in accordance with generally accepted auditing standards which 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, assessing the accounting principles used and significant estimates made by management and evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for the opinion expressed above.



NRG ENERGY, INC.  
 CONSOLIDATED BALANCE SHEETS

	DECEMBER 31,	
	1996	1995
	(THOUSANDS OF DOLLARS)	
ASSETS		
Current Assets:		
Cash and cash equivalents.....	\$ 12,438	\$ 7,039
Restricted cash.....	17,688	9,773
Accounts receivable--trade, less allowance for doubtful accounts of \$143 and \$103.....	12,061	9,333
Accounts receivable-affiliates.....	6,708	4,640
Current portion of notes receivable-affiliates.....	3,601	5,267
Current portion of notes receivable.....	5,985	2,791
Inventory.....	2,312	1,811
Prepayments and other current assets.....	4,644	1,744
TOTAL CURRENT ASSETS.....	65,437	42,398
Property, Plant and Equipment, at Original Cost:		
In service.....	176,072	170,253
Under construction.....	24,683	5,914
	200,755	176,167
Less accumulated depreciation.....	(71,106)	(64,248)
Net property, plant and equipment.....	129,649	111,919
Other Assets:		
Investments in projects.....	365,749	221,129
Capitalized project costs.....	9,267	4,185
Notes receivable, less current portion-affiliates.....	58,169	32,389
Notes receivable, less current portion.....	9,309	--
Intangible assets, net of accumulated amortization of \$5,647 and \$4,127.....	40,476	41,996
Debt issuance costs, net of accumulated amortization of \$338 and \$189.....	2,753	573
Total other assets.....	485,723	300,272
TOTAL ASSETS.....	\$680,809	\$454,589

See accompanying notes.

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NRG ENERGY, INC.  
CONSOLIDATED BALANCE SHEETS -- (CONTINUED)

	DECEMBER 31,	
	1996	1995
	(THOUSANDS OF DOLLARS)	
LIABILITIES AND STOCKHOLDER'S EQUITY		
Current liabilities:		
Current portion of long-term debt.....	\$ 4,848	\$ 3,762
Accounts payable-trade.....	4,443	6,208
Note payable-affiliates.....	3,867	1,185
Accrued income taxes.....	1,930	7,366
Accrued property and sales taxes.....	2,159	1,895
Accrued salaries, benefits and related costs.....	6,559	5,178
Accrued interest.....	4,726	824
Other current liabilities.....	4,424	1,578
TOTAL CURRENT LIABILITIES.....	32,956	27,996
Long-term debt, less current portion.....	207,293	86,272
Deferred revenues.....	6,340	7,726
Deferred income taxes.....	8,606	9,166
Deferred investment tax credits.....	1,853	2,069
Deferred compensation.....	1,847	1,596
TOTAL LIABILITIES.....	258,895	134,825
Commitments and Contingencies (Note 13)		
Stockholder's Equity:		
Common stock; \$1 par value; 1,000 shares authorized; 1,000 shares issued and outstanding.....	1	1
Additional paid-in capital.....	351,013	271,013
Retained earnings.....	66,301	46,323
Currency translation adjustments.....	4,599	2,427
TOTAL STOCKHOLDER'S EQUITY.....	421,914	319,764
TOTAL LIABILITIES AND STOCKHOLDER'S EQUITY.....	\$680,809	\$454,589

See accompanying notes.

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NRG ENERGY, INC.  
CONSOLIDATED STATEMENTS OF INCOME

	YEAR ENDED DECEMBER 31,	
	1996	1995
	(THOUSANDS OF DOLLARS)	
Operating revenues:		
Revenues from wholly-owned operations.....	\$ 71,649	\$64,180
Equity in operating earnings of unconsolidated affiliates.....	32,815	23,639
Total operating revenues.....	104,464	87,819
Operating costs and expenses:		
Cost of wholly-owned operations.....	36,562	32,535
Depreciation and amortization.....	8,378	8,283
General, administrative and development expenses .....	39,248	34,647
Total operating costs and expenses.....	84,188	75,465
Operating income.....	20,276	12,354
Other income (expense):		
Equity in gain from project termination settlements ....	--	29,850
Other income, net.....	9,477	4,896
Interest expense.....	(15,430)	(7,089)
Total other income (expense).....	(5,953)	27,657
Income before income taxes.....	14,323	40,011
Income (benefit) taxes.....	(5,655)	8,810
Net Income.....	\$ 19,978	\$31,201

See accompanying notes.

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NRG ENERGY, INC.  
CONSOLIDATED STATEMENTS OF CASH FLOWS

	YEAR ENDED DECEMBER 31,	
	1996	1995
	(THOUSANDS OF DOLLARS)	
CASH FLOWS FROM OPERATING ACTIVITIES		
Net income.....	\$ 19,978	\$ 31,201
Adjustments to reconcile net income to net cash provided (used) by operating activities .....		

Undistributed equity in operating earnings of unconsolidated affiliates.....	(17,827)	(20,074)
Depreciation and amortization.....	8,378	8,283
Deferred income taxes and investment tax credits.....	(776)	(2,608)
Cash provided (used) by changes in certain working capital items		
Accounts receivable.....	(2,728)	1,102
Accounts receivable-affiliates.....	(2,068)	(2,889)
Accrued income taxes.....	(5,436)	9,808
Inventory.....	(501)	(107)
Prepayments and other current assets.....	(2,900)	(571)
Accounts payable-trade.....	(1,765)	1,009
Accounts payable-affiliates.....	2,682	(3,037)
Accrued property and sales taxes.....	264	(396)
Accrued salaried, benefits and related costs.....	1,381	2,427
Accrued interest.....	3,902	553
Other current liabilities.....	2,846	1,094
Cash (used) by changes in other assets and liabilities .....	(1,284)	(1,004)
Equity in gain from project termination settlement.....	--	(29,850)
	-----	-----
NET CASH PROVIDED (USED) BY OPERATING ACTIVITIES.....	4,146	(5,059)
CASH FLOWS FROM INVESTING ACTIVITIES		
Investments in projects.....	(140,590)	(25,776)
Loans to projects.....	(36,617)	(35,411)
Capital expenditures.....	(24,588)	(11,036)
Cash distribution from project termination settlement.....	15,671	14,179
(Increase) decrease in restricted cash.....	(7,915)	4,044
Other, net.....	(4,486)	(3,104)
	-----	-----
NET CASH USED BY INVESTING ACTIVITIES.....	(198,525)	(57,104)
CASH FLOWS FROM FINANCING ACTIVITIES		
Capital contributions from parent.....	80,000	55,000
Proceeds from issuance of long-term debt.....	122,671	--
Principal payments on long-term debt.....	(2,893)	(3,305)
	-----	-----
NET CASH PROVIDED BY FINANCING ACTIVITIES.....	199,778	51,695
	=====	=====
NET INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS.....	5,399	(10,468)
CASH AND CASH EQUIVALENTS AT BEGINNING OF YEAR.....	7,039	17,507
	-----	-----
CASH AND CASH EQUIVALENTS AT END OF YEAR.....	\$ 12,438	\$ 7,039
	=====	=====
SUPPLEMENTAL DISCLOSURES OF CASH FLOW INFORMATION		
Interest paid (net of amount capitalized).....	\$ 11,527	\$ 6,536
Income taxes paid.....	1,164	1,447

See accompanying notes.

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NRG ENERGY, INC.  
CONSOLIDATED STATEMENTS OF STOCKHOLDER'S EQUITY

	COMMON STOCK	ADDITIONAL PAID-IN CAPITAL	RETAINED EARNINGS	CURRENCY TRANSLATION ADJUSTMENTS	TOTAL STOCKHOLDER'S EQUITY
	(THOUSANDS OF DOLLARS)				
Balances at December 31, 1994 ....	\$1	\$216,013	\$15,122	\$ 3,586	\$234,722
Net income.....			31,201		31,201
Capital contributions from parent.....		55,000			55,000
Currency translation adjustments .				(1,159)	(1,159)
	-----	-----	-----	-----	-----
Balances at December 31, 1995 ....	1	271,013	46,323	2,427	319,764
Net income.....			19,978		19,978
Capital contributions from parent.....		80,000			80,000
Currency translation adjustments .				2,172	2,172
	-----	-----	-----	-----	-----
Balances at December 31, 1996 ....	\$1	\$351,013	\$66,301	\$ 4,599	\$421,914
	=====	=====	=====	=====	=====

See accompanying notes.

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NRG ENERGY, INC.  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

1. ORGANIZATION

NRG Energy, Inc., a Delaware corporation, was incorporated on May 29, 1992, as a wholly-owned subsidiary of Northern States Power Company (NSP). Beginning in 1989, NRG was doing business through its predecessor companies, NRG Energy, Inc. and NRG Group, Inc., Minnesota corporations which were merged into NRG subsequent to its incorporation. NRG and its subsidiaries and affiliates develop, build, acquire, own and operate nonregulated energy-related businesses.

2. PRINCIPLES OF CONSOLIDATION

Principles of Consolidation and Basis of Presentation

The consolidated financial statements include the accounts of NRG and its subsidiaries (referred to collectively herein as NRG). All significant intercompany transactions and balances have been eliminated in consolidation. As discussed in Note 5, NRG has investments in partnerships, joint ventures and projects for which the equity method of accounting is applied. Earnings from equity in international investments are recorded net of foreign income taxes.

Cash Equivalents

Cash equivalents include highly liquid investments (primarily commercial paper) with a remaining maturity of three months or less at the time of purchase.

Restricted Cash

Restricted cash consists primarily of cash collateral required in connection with foreign currency hedging activities (see Note 12) and cash collateral for letters of credit issued in relation to project development activities.

Inventory

Inventory is valued at the lower of average cost or market and consists principally of spare parts and raw materials used to generate steam.

Property, Plant and Equipment

Property, plant and equipment are capitalized at original cost. Significant additions or improvements extending asset lives are capitalized, while repairs and maintenance are charged to expense as incurred. Depreciation is computed using the straight-line method over the following estimated useful lives:

Facilities and improvements.....	20-45 years
Machinery and equipment.....	7-30 years
Office furnishings and equipment ....	3-5 years

## Capitalized Interest

Interest incurred on funds borrowed to finance projects expected to require more than three months to complete is capitalized. Capitalization of interest is discontinued when the project is completed and considered operational. Capitalized interest is amortized using the straight line method over the useful life of the related project. Capitalized interest was \$364,000 and \$253,000 in 1996 and 1995, respectively.

## Development Costs and Capitalized Project Costs

These costs include professional services, dedicated employee salaries, permits, and other costs which are incurred incidental to a particular project. Such costs are expensed as incurred until a sales

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NRG ENERGY, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

## 2. PRINCIPLES OF CONSOLIDATION (Continued)

agreement or letter of intent is signed and the project has been approved by NRG's Board of Directors. Additional costs incurred after this point are capitalized. When project operations begin, previously capitalized project costs are reclassified to investment in projects and amortized on a straight-line basis over the lesser of the life of the project's related assets or revenue contract period.

### Debt Issuance Costs

Costs to issue long-term debt have been capitalized and are being amortized over the terms of the related debt.

### Intangibles

Intangibles consist principally of service agreements and the excess of the cost of investment in subsidiaries over the underlying fair value of the net assets acquired and are being amortized using the straight-line method over 20 years. NRG periodically evaluates the recovery of goodwill and other intangibles based on an analysis of estimated undiscounted future cash flows.

Service agreement intangibles relate solely to the 1993 acquisition of the Minneapolis Energy Center. The 20-year amortization period is based on the remaining term of customer energy service agreements.

### Income Taxes

NRG is included in the consolidated tax returns of NSP. NRG calculates its income tax provision on a separate return basis under a tax sharing agreement with NSP as discussed in Note 9. Current federal and state income taxes are payable to or receivable from NSP. NRG records income taxes using the liability method. Income taxes are deferred on all temporary differences between pretax financial and taxable income and between the book and tax bases of assets and liabilities. Deferred taxes are recorded using the tax rates scheduled by law to be in effect when the temporary differences reverse. Investment tax credits are deferred and amortized over the estimated lives of the related property. NRG's policy for income taxes related to international operations is discussed in Note 9.

### Revenue Recognition

Under fixed-price contracts, revenues are recognized as deliveries of products or services are made. Revenues and related costs under cost reimbursable contract provisions are recorded as costs are incurred. Anticipated future losses on contracts are charged against income when identified.

Deferred revenues relate to a 1988 legal settlement with a major thermal customer. Settlement proceeds were deferred when received and are reflected in operating income on a straight-line basis over the life of the related steam contract which expires in 2001.

#### Foreign Currency Translation

The local currencies are generally the functional currency of NRG's foreign operations. Foreign currency denominated assets and liabilities are translated at end-of-period rates of exchange. The resulting currency adjustments are accumulated and reported as a separate component of stockholder's equity. Income, expense and cash flows are translated at weighted-average rates of exchange for the period.

Exchange gains and losses that result from foreign currency transactions (e.g., converting cash distributions made in one currency to another currency) are included in the results of operations as a component of equity in earnings of unconsolidated affiliates. Through December 31, 1996, NRG has not experienced any material translation gains or losses from foreign currency transactions that have occurred since the respective foreign investment dates.

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NRG ENERGY, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

## 2. PRINCIPLES OF CONSOLIDATION (Continued)

### Derivative Financial Instruments

NRG's policy is to hedge foreign currency denominated investments as they are made to preserve their U.S. dollar value, where appropriate hedging vehicles are available. NRG has entered into currency hedging transactions through the use of forward foreign currency exchange agreements. Gains and losses on these agreements offset the effect of foreign currency exchange rate fluctuations on the valuation of the investments underlying the hedges. Hedging gains and losses, net of income tax effects, are reported with other currency translation adjustments as a separate component of stockholder's equity. NRG is not hedging currency translation adjustments related to future operating results. NRG does not speculate in foreign currencies. None of these derivative financial instruments are reflected in NRG's balance sheet.

### Use of Estimates

In recording transactions and balances resulting from business operations, NRG uses estimates based on the best information available. Estimates are used for such items as plant depreciable lives, tax provisions, uncollectible accounts and actuarially determined benefit costs. As better information becomes available (or actual amounts are determinable), the recorded estimates are revised. Consequently, operating results can be affected by revisions to prior accounting estimates.

### Reclassifications

Certain reclassifications have been made to the 1995 financial statements to conform to the 1996 presentation. These reclassifications had no effect on net income or stockholder's equity as previously reported.

## 3. BUSINESS ACQUISITIONS

In March 1996, a joint venture between NRG and Transfield signed an 18-year power purchase agreement and an agreement for the acquisition and refurbishment of the 180 MW Collinsville coal-fired power generation facility in Queensland, Australia. NRG would own a 50% interest and operate the facility in conjunction with Transfield.

In April 1996, NRG, through bankruptcy proceedings, purchased a 41.86% interest in O'Brien Environmental Energy, Inc. that has been renamed as NRG Generating (U.S.) Inc. (NRGG). In addition to an equity interest in NRGG, NRG acquired certain landfill gas projects in the purchase which were transferred to NEO and a cogeneration facility.

On December 19, 1996 NRG and Nordic Power Invest AB purchased 96.6% of Bolivian Power Company Limited. NRG's ownership is 58%, however it is NRG's intent to reduce its holding to 50% or less.

NEO, a wholly-owned subsidiary, owns a 50% interest in Minnesota Methane LLC. In 1996, Minnesota Methane LLC acquired a 12 MW project in West Covina, California and acquired six projects as part of the NRGG acquisition. Of the projects acquired, four were operating facilities and two were projects under development and construction. In 1994, NEO acquired a 50% interest in Northbrook Energy. In 1996, Northbrook Energy acquired seven additional hydroelectric plants.

The total acquisition investments in these projects through December 31, 1996, including capitalized development costs, was approximately \$121.5 million. Earnings from equity interests in these NRG projects acquired in 1996 contributed \$2.7 million to NRG's 1996 earnings.

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NRG ENERGY, INC.  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

4. PROPERTY, PLANT AND EQUIPMENT

The major classes of property, plant and equipment at December 31 were as follows:

	1996	1995
	-----	-----
	(THOUSANDS OF DOLLARS)	
Facilities and equipment, including construction work in progress of \$24,683 and \$5,914.....	\$187,014	\$163,099
Land and improvements.....	10,397	10,397
Office furnishings and equipment.....	3,344	2,671
	-----	-----
Total property, plant and equipment.....	200,755	176,167
Accumulated depreciation.....	(71,106)	(64,248)
	-----	-----
Net property, plant and equipment.....	\$129,649	\$111,919
	=====	=====

5. INVESTMENTS ACCOUNTED FOR BY THE EQUITY METHOD

NRG has investments in various international and domestic energy projects. The equity method of accounting is applied to such investments in affiliates, which include joint ventures and partnerships, because the ownership structure prevents NRG from exercising a controlling influence over operating and financial policies of the projects. Under this method, equity in pretax income or losses of domestic partnerships and in the net income or losses of international projects are reflected as equity in earnings of unconsolidated affiliates.

A summary of NRG's significant equity-method investments which were in operation at December 31, 1996 is as follows:

	GEOGRAPHIC AREA	ECONOMIC INTEREST	PURCHASED OR PLACED IN SERVICE
NAME			
-----			



MIBRAG Mining and Power Generation .....	Germany	33.3%	January 1994
Gladstone Power Station .....	Australia	37.5%	March 1994
Schkopau Power Station.....	Germany	20.6%	January and July 1996
Scudder Latin American Trust for Independent Power Energy Project.....	Latin America	25.0%	June 1993
Collinsville Electric Generation .....	Australia	50.0%	March 1996
COBEE .....	Bolivia	58.0%	December 1996
NRG Generating.....	USA	41.9%	April 1996
Various Independent Power Production Facilities .	USA	45%-50%	July 1991-December 1996
Rosebud Syncoal Partnership.....	USA	50.0%	August 1993

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NRG ENERGY, INC.  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

5. INVESTMENTS ACCOUNTED FOR BY THE EQUITY METHOD (Continued)

Summarized financial information for investments in unconsolidated affiliates accounted for under the equity method as of and for the year ended December 31, is as follows:

	1996	1995
	(THOUSANDS OF DOLLARS)	
Operating revenues.....	\$ 886,947	\$ 776,612
Costs and expenses.....	794,255	615,696
Net income.....	\$ 92,692	\$ 160,916
Current assets.....	\$ 647,213	\$ 757,124
Noncurrent assets.....	3,420,950	2,557,992
Total assets.....	\$4,068,163	\$3,315,116
Current liabilities.....	\$ 365,905	\$ 290,805
Noncurrent liabilities.....	2,732,922	2,236,919
Equity.....	969,336	787,392
Total liabilities and equity.....	\$4,068,163	\$3,315,116
NRG's share of equity.....	\$ 365,749	\$ 221,129
NRG's share of income.....	32,815	23,639

In June 1995, a power sales contract between a California energy project, in which NRG is a 45% investor, and an unaffiliated utility company was terminated. A pretax gain of \$29.9 million was recognized by NRG for its share of the termination settlement.

NRG recorded pretax charges of \$1.5 million in 1996 and \$5.0 million in 1995 to write down the carrying value of certain energy projects.

6. RELATED PARTY TRANSACTIONS.

Operating Agreements

NRG has two agreements with NSP for the purchase of thermal energy. Under the terms of the agreements, NSP charges NRG for certain costs (fuel, labor, plant maintenance, and auxiliary power) incurred by NSP to produce the thermal energy. NRG paid NSP \$6.0 million in 1996 and \$3.7 million in 1995 under these agreements.

NRG has a renewable 10-year agreement with NSP, expiring on December 31, 2001, whereby NSP agrees to purchase refuse-derived fuel for use in certain

of its boilers and NRG agrees to pay NSP a burn incentive. NRG has an agreement expiring in 1997 to sell wood by-product obtained from a thermal customer to NSP for use as fuel. Under these agreements, NRG received \$1.5 million and \$1.9 million from NSP, and paid \$2.2 million and \$2.3 million to NSP in 1996 and 1995, respectively.

Administrative Services and Other Costs

NRG and NSP have entered into an agreement to provide for the reimbursement of actual administrative services provided to each other, an allocation of NSP administrative costs and a working capital fee. Services provided by NSP to NRG are principally cash management, legal, accounting, employee relations and engineering. In addition, NRG employees participate in certain employee benefit plans of NSP as discussed in Note 10. During 1996 and 1995, NRG paid NSP \$7.2 million and \$6.8 million, respectively, as reimbursement under this agreement.

Allocation is on a direct charge, actual cost basis where possible. When this is not possible, an allocation is made based upon employee headcounts, operating revenues and investment in fixed assets. Management believes that "allocated" costs approximate expenses that would be incurred on a stand alone basis.

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NRG ENERGY, INC.  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

6. RELATED PARTY TRANSACTIONS. (Continued)

In 1996, NRG and NSP entered into an agreement for NRG to provide operations and maintenance services for NSP's Elk River resource recovery facility and Becker ash landfill. During 1996, NSP paid NRG \$1.5 million as reimbursement under this agreement.

7. NOTES RECEIVABLE

Notes receivable consist primarily of fixed and variable rate notes secured by equity interests in partnerships and joint ventures. The interest rate on the notes ranged from 7.0% to 12.5% at December 31, 1996 and 1995.

8. LONG-TERM DEBT

Long-term debt consists of the following at December 31:

	1996	1995
	-----	
	(THOUSANDS OF DOLLARS)	
NRG Energy Center, Inc. Senior Secured Notes Series due June 15, 2013, 7.31%.....	\$ 76,986	\$79,326
Note payable to NSP, due December 1, 1995-2006 5.40%-6.75%.....	8,405	8,958
NRG Sunnyside, Inc. note payable, due December 31, 1997, 10.00%.....	1,750	1,750
NRG Energy Senior Notes, due February 1, 2006, 7.625% ..	125,000	--
	-----	
	212,141	90,034
Less current maturities.....	(4,848)	(3,762)
	-----	
Total.....	\$207,293	\$86,272
	=====	

The NRG Energy Center, Inc. notes are secured principally by long-term

assets of the Minneapolis Energy Center (MEC). In accordance with the terms of the note agreements, MEC is required to maintain compliance with certain financial covenants primarily related to incurring debt, disposing of MEC assets, and affiliate transactions. MEC was in compliance with these covenants at December 31, 1996.

The note payable to NSP relates to long-term debt assumed by NRG in connection with the transfer of ownership of an RDF processing plant by NSP to NRG in 1993.

The NRG Sunnyside, Inc. note payable was issued in connection with the purchase of an equity interest in a waste-coal project in 1994.

The NRG Energy Senior Notes were issued in January 1996, are unsecured and require semi-annual interest payments on February 1 and August 1.

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NRG ENERGY, INC.  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

8. LONG-TERM DEBT (Continued)

Annual maturities of long-term debt for the years ending after December 31, 1996 are as follows:

(THOUSANDS OF DOLLARS)	
1997.....	\$ 4,848
1998.....	3,335
1999.....	3,581
2000.....	3,841
2001.....	4,160
Thereafter ..	192,376
	-----
Total.....	\$212,141
	=====

NRG has revolving-credit agreements which allow for Letters of Credit which may not exceed \$63.9 million. There were \$18.4 million and \$0 outstanding letters of credit under the credit agreements at December 31, 1996 and 1995, respectively.

9. INCOME TAXES

NRG and its parent, NSP, have entered into a federal and state income tax sharing agreement relative to the filing of consolidated federal and state income tax returns. The agreement provides, among other things, that (1) if NRG, along with its subsidiaries, is in a taxable income position, NRG will be currently charged with an amount equivalent to its federal and state income tax computed as if the group had actually filed separate federal and state returns, and (2) if NRG, along with its subsidiaries, is in a tax loss position, NRG will be currently reimbursed to the extent its combined losses are utilized in a consolidated return, and (3) If NRG, along with its subsidiaries, generates tax credits, NRG will be currently reimbursed to the extent its tax credits are utilized in a consolidated return.

The provision for income taxes consists of the following:

	1996	1995
	-----	
	(THOUSANDS OF DOLLARS)	
Current		
Federal.....	\$ 633	\$ 9,965
State.....	253	3,268
Foreign.....	616	233
	-----	
	1,502	13,466
Deferred		
Federal.....	(3,655)	(1,592)
State.....	(1,498)	(1,012)
	-----	
	(5,153)	(2,604)
Tax credits recognized.....	(2,004)	(2,052)
	-----	
Total income tax (benefit) expense.....	\$ (5,655)	\$ 8,810
	=====	

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NRG ENERGY, INC.  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

9. INCOME TAXES (Continued)

The components of the net deferred income tax liability at December 31 were:

	1996	1995
	-----	
	(THOUSANDS OF DOLLARS)	
Deferred tax liabilities		
Differences between book and tax bases of property .....	\$16,606	\$16,364
Investments in projects.....	2,988	1,226
Goodwill.....	2,974	444
Other.....	2,646	112
	-----	
Total deferred tax liabilities.....	25,214	18,146
Deferred tax assets		
Deferred revenue.....	3,043	3,099
Development costs.....	5,581	--
Deferred investment tax credits.....	766	856
Deferred compensation, accrued vacation and other reserves.....	1,536	1,412
Steam capacity rights.....	1,043	1,109
Other.....	4,639	2,504
	-----	
Total deferred tax assets.....	16,608	8,980
	-----	
Net deferred tax liability.....	\$ 8,606	\$ 9,166
	=====	

Rate Reconciliation

At December 31, 1996, the effective income tax rate (benefit) of (39.5)% differs from the statutory federal income tax rate of 35% primarily due to the fact that NRG generated a domestic tax loss of \$15 million for the year. For the year ended December 31, 1995, NRG had a domestic tax income of \$9.2 million with the change between 1996 and 1995 primarily attributable to a \$29.9 million gain from the sale of a power agreement at SJVEP.

Income before income taxes includes net foreign equity income of \$28 million and \$32 million in 1996 and 1995, respectively. NRG's management intends to reinvest the earnings of foreign operations indefinitely. Accordingly, U.S. income taxes and foreign withholding taxes have not been provided on the earnings of foreign subsidiary companies. The cumulative amount of undistributed earnings of foreign subsidiaries upon which no U.S. income taxes or foreign withholding taxes have been provided is approximately \$87.3 million at December 31, 1996. The additional U.S. income tax and foreign withholding tax on the unremitted foreign earnings, if repatriated, would be offset in whole or in part by Foreign tax credits. Thus, it is impracticable to estimate the amount of tax that might be payable.

10. BENEFITS PLANS AND OTHER POSTRETIREMENT BENEFITS

Pension Benefits

NRG participates in NSP's noncontributory, defined benefit pension plan that covers the majority of all U.S. employees. Benefits are based on a combination of years of service, the employee's highest average pay for 48 consecutive months, and Social Security benefits. Net annual periodic pension cost includes the following components:

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NRG ENERGY, INC.  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

10. BENEFITS PLANS AND OTHER POSTRETIREMENT BENEFITS (Continued)

	1996	1995
	-----	
	(THOUSANDS OF DOLLARS)	
Service cost-benefits earned during the period.....	\$ 1,115	\$ 688
Interest cost on projected benefit obligation .	1,013	525
Actual return on assets.....	(1,983)	(1,542)
Net amortization and deferral.....	1,258	1,147
	-----	
Net periodic pension cost.....	\$ 1,403	\$ 818
	=====	

NRG's funding policy is to contribute to NSP the full actuarial pension cost accrued, less future tax benefits to be realized from such costs. Plan assets consist principally of common stock of public companies, corporate bonds and U.S. government securities. The funded status of the pension plan in which NRG employees participate is as follows at December 31, 1996 and 1995:

NSP Plan -- 1996

	TOTAL	NRG PORTION
	-----	
	(THOUSANDS OF DOLLARS)	
Actuarial present value of benefit obligation .....		
Vested.....	\$ 660,920	\$ 6,464
Nonvested.....	147,278	3,422
	-----	
Accumulated benefit obligation.....	\$ 808,198	\$ 9,886
	=====	
Projected benefit obligation.....	\$ 993,821	\$14,253
Plan assets at fair value.....	1,634,696	12,986

Plan assets (in excess of) less than projected benefit obligation.....	(640,875)	1,267
Unrecognized prior service cost.....	(19,734)	(86)
Unrecognized net actuarial gain (loss).....	651,368	256
Unrecognized net transitional asset.....	539	--
Net pension (prepaid) liability recorded.....	\$ (8,702)	\$ 1,437

NSP Plan -- 1995

	TOTAL	NRG PORTION
	(THOUSANDS OF DOLLARS)	
Actuarial present value of benefit obligation		
Vested.....	\$ 686,403	\$ 3,050
Nonvested.....	155,177	1,520
Accumulated benefit obligation.....	\$ 841,580	\$ 4,570
Projected benefit obligation.....	\$1,039,981	\$ 8,828
Plan assets at fair value.....	1,456,530	6,657
Plan assets (in excess of) less than projected benefit obligation.....	(416,549)	2,171
Unrecognized prior service cost.....	(20,805)	(91)
Unrecognized net actuarial gain (loss).....	452,699	(1,388)
Unrecognized net transitional asset.....	615	--
Net pension liability recorded.....	\$ 15,960	\$ 692

The weighted average discount rate used in determining the actuarial present value of the projected benefit obligation was 7.5% in 1996 and 7% in 1995. The rate of increase in future compensation levels

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NRG ENERGY, INC.  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

10. BENEFITS PLANS AND OTHER POSTRETIREMENT BENEFITS (Continued)

used in determining the actuarial present value of the projected obligation was 5% in 1996 and in 1995. The assumed long-term rate of return on assets used for cost determinations was 9% for 1996 and 8% for 1995. Changes in actuarial assumptions increased 1996 pension costs by \$284,000 and are expected to decrease 1997 costs by \$150,000.

Postretirement Health Care

NRG participates in NSP's contributory health and welfare benefit plan that provides health care and death benefits to the majority of all U.S. employees after their retirement. The plan is intended to provide for sharing of costs of retiree health care between NRG and retirees. For employees retiring after January 1, 1994, a six-year cost-sharing strategy was implemented with retirees paying 15% of the total cost of health care in 1994, increasing to a total of 40% in 1999.

Postretirement health care benefits for NRG are determined and recorded under the provisions of SFAS No. 106, "Employers' Accounting for Postretirement Benefits Other Than Pensions." SFAS No. 106 requires the actuarially determined obligation for postretirement health care and death benefits to be fully accrued by the date employees attain full eligibility for such benefits, which is generally when they reach retirement age. In

conjunction with the adoption of SFAS No. 106 in 1993, NRG elected to amortize on a straight-line basis over 20 years the unrecognized accumulated postretirement benefit obligation (APBO) of \$1.4 million for current and future retirees.

Plan assets as of December 31, 1996, consisted of investments in equity mutual funds and cash equivalents. NRG's funding policy is to contribute to NSP benefits actually paid under the plan. The following table sets forth the funded status of the health care plan in which NRG employees participate at December 31, 1996 and 1995:

NSP Plan -- 1996

	TOTAL	NRG PORTION
	-----	-----
	(THOUSANDS OF DOLLARS)	
APBO		
Retirees.....	\$ 144,180	\$ 323
Fully eligible plan participants .....	23,438	619
Other active plan participants .....	101,065	2,269
	-----	-----
Total APBO.....	268,683	3,211
Plan assets at fair value.....	(15,514)	--
	-----	-----
APBO in excess of plan assets.....	253,169	3,211
Unrecognized net actuarial loss .....	(12,467)	(366)
Unrecognized net transition obligation.....	(172,480)	(1,133)
	-----	-----
Net benefit obligation recorded .....	\$ 68,222	\$ 1,712
	=====	=====

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NRG ENERGY, INC.  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

10. BENEFITS PLANS AND OTHER POSTRETIREMENT BENEFITS (Continued)

NSP Plan -- 1995

	TOTAL	NRG PORTION
	-----	-----
	(THOUSANDS OF DOLLARS)	
APBO		
Retirees.....	\$ 145,800	\$ 67
Fully eligible plan participants .....	24,400	518
Other active plan participants .....	116,800	2,239
	-----	-----
Total APBO.....	287,000	2,824
Plan assets at fair value.....	(11,600)	--
	-----	-----
APBO in excess of plan assets.....	275,400	2,824
Unrecognized net actuarial loss .....	(40,400)	(510)
Unrecognized net transition obligation.....	(183,200)	(1,203)
	-----	-----
Net benefit obligation recorded .....	\$ 51,800	\$ 1,111

=====

The assumed health care cost trend rates used in measuring the APBO at December 31, 1996 and 1995, were 9.8% and 10.4% for those under age 65, and 7.1% and 7.3% for those over age 65, respectively. The assumed cost trends are expected to decrease each year until they reach 5.5% for both age groups in the year 2004, after which they are assumed to remain constant. A 1% increase in the assumed health care cost trend rate for each year would increase the APBO by approximately 14% as of December 31, 1996. Service and interest cost components of the net periodic postretirement cost would increase by approximately 17% with a similar one percent increase in the assumed health care cost trend rate. The assumed discount rate used in determining the APBO was 7.5% for December 31, 1996 and 7% for December 31, 1995, compounded annually. The assumed long-term rate of return on assets used for cost determinations under SFAS No. 106 was 8% for 1996 and 1995. Changes in actuarial assumptions had an immaterial impact on 1996 costs and are not expected to materially impact 1997 costs.

The net annual periodic postretirement benefit cost recorded for 1996 and 1995 consists of the following components:

	1996	1995
	-----	
	(THOUSANDS OF DOLLARS)	
Service cost-benefits earned during the year.....	\$257	\$171
Interest cost on APBO.....	233	171
Amortization of transition obligation .....	70	70
Net amortization and deferral.....	26	--
	-----	
Net periodic postretirement health care cost.....	\$586	\$412
	=====	

NRG Equity Plan

Employees are eligible to participate in the NRG Equity Plan (the Plan), a long term incentive plan. The Plan grants phantom equity units to employees based upon performance and job grade. NRG's equity units are valued based upon NRG's growth and financial performance. The primary financial measures used in determining the equity units' value are revenue growth, return on investment and cash flow from operations. The units are awarded to employees annually at the respective years calculated share price (grant price). The Plan provides employees with a cash payout for the appreciation in equity unit value over the vesting period. The Plan has a seven year vesting schedule with actual payments beginning after the end of the third year and continuing at 20% each year for the subsequent five years. The Plan includes a change of control provision, which allow all shares to vest if the ownership of NRG

10. BENEFITS PLANS AND OTHER POSTRETIREMENT BENEFITS (Continued)

were to change. Phantom equity units outstanding at December 31, 1996 and 1995 were 1,380,990 and 1,164,090, respectively. The cost of the phantom equity units is expensed over the vesting period from the date of issuance (\$452,000 and \$422,000 in 1996 and 1995, respectively).



Deferred Compensation

Certain employees of NRG are eligible to participate in a deferred compensation program. The employee can elect to defer a portion of their compensation until retirement. Earnings on the amounts deferred are equal to the return on the Fixed Income Option of the NSP Retirement Savings Plan. Earnings will be compounded annually and credited monthly. Payouts begin upon retirement with payments made over 180 equal monthly installments (or a minimum of \$500 per month until their account balance is zero.)

11. SALES TO SIGNIFICANT CUSTOMERS

NRG and the Ramsey/Washington Resource Recovery Project have a service agreement for waste disposal which expires in 2006. Approximately 29.1% in 1996 and 32.1% in 1995 of NRG's revenues from wholly-owned operations were recognized under this contract. In addition, sales to one thermal customer amounted to 14.1% and 15.6% of revenues from wholly-owned operations in 1996 and 1995, respectively.

12. FINANCIAL INSTRUMENTS

The estimated December 31 fair values of recorded financial instruments are as follows:

	1996		1995	
	CARRYING AMOUNT	FAIR VALUE	CARRYING AMOUNT	FAIR VALUE
	(THOUSANDS OF DOLLARS)			
Cash and cash equivalents.....	\$ 12,438	\$ 12,438	\$ 7,039	\$ 7,039
Restricted cash.....	17,688	17,688	9,773	9,773
Notes receivable, including current portion.....	77,064	77,064	40,447	40,447
Long-term debt, including current portion ..	212,141	200,875	90,034	91,682

For cash, cash equivalents and restricted cash, the carrying amount approximates fair value because of the short-term maturity of those instruments. The fair value of notes receivable is based on expected future cash flows discounted at market interest rates. The fair value of long term debt is estimated based on the quoted market prices for the same or similar issues.

Derivatives

NRG has entered into seven forward foreign currency exchange contracts with counterparties to hedge exposure to currency fluctuations to the extent permissible by hedge accounting requirements. Pursuant to these contracts, transactions have been executed that are designed to protect the economic value in U.S. dollars of NRG's equity investments and retained earnings, denominated in Australian dollars and German deutsche marks (DM). As of December 31, 1996, NRG had \$132 million of foreign currency denominated assets that were hedged by forward foreign currency exchange contracts with a notional value of \$123 million. In addition, NRG had approximately \$82 million of foreign currency denominated retained earnings from foreign projects that were hedged by forward foreign currency exchange contracts with a notional value of \$59 million. Because the effects of both currency translation adjustments to foreign investments and currency hedge instrument gains and losses are recorded on a

## 12. FINANCIAL INSTRUMENTS (Continued)

net basis in stockholders' equity (not earnings), the impact of significant changes in currency exchange rates on these items would have an immaterial effect on NRG's financial condition and results of operations. In connection with the forward foreign currency exchange contracts, cash collateral of \$16 million was required at December 31, 1996, which is reflected as restricted cash on NRG's balance sheet. The forward foreign currency exchange contracts terminate in 1998 through 2006 and require foreign currency interest payments by either party during each year of the contract. If the contracts had been terminated at December 31, 1996, \$13.3 million would have been payable by NRG for currency exchange rate changes to date. Management believes NRG's exposure to credit risk due to non-performance by the counterparties to its forward exchange contracts is not significant, based on the investment grade rating of the counterparties.

## 13. COMMITMENTS AND CONTINGENCIES

### Operating Lease Commitments

NRG leases certain of its facilities and equipment under operating leases, some of which include escalation clauses, expiring on various dates through 2010. Rental expense under these operating leases was \$741,000 in 1996 and \$796,000 in 1995. Future minimum lease commitments under these leases for the years ending after December 31, 1996 are as follows:

	(THOUSANDS OF DOLLARS)
1997.....	\$ 1,050
1998.....	936
1999.....	956
2000.....	982
2001.....	1,008
Thereafter ..	5,349
	-----
Total.....	\$10,281
	=====

### Capital Commitments -- International

NRG signed a Joint Development Agreement for the acquisition, upgrading, expansion and development of Energy Center Kladno in Kladno, Czech Republic. The acquisition of the existing facility is the first phase of a development project that will include upgrading the existing plant and developing a new power generation facility. NRG has a \$44 million commitment for the additional facilities.

NRG together with its partners, signed a power contract with PT Perusahaan Listrik Negara, the state-owned Indonesian electric company, to build, own and operate a 400 MW coal-fired power station in Cilegon, West Java, Indonesia. NRG has a \$65 million commitment for the facility.

NRG is contractually committed to additional equity investments of \$14 million for Scudder Latin American Power I and \$7 million to Scudder Latin American Power II as of December 31, 1996.

NRG reached agreement to purchase a 50% equity interest in the Enfield Energy Centre, a 350 MW power project located in the North London borough of Enfield, England. NRG has a \$62 million commitment.

NRG and Transfield signed an acquisition agreement for the acquisition and refurbishment of the 180 MW Collinsville coal-fired power generation facility in Queensland, Australia. NRG has a \$9 million commitment.

NRG ENERGY, INC.  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

## 13. COMMITMENTS AND CONTINGENCIES (Continued)

Future capital commitments related to international projects are as follows:

(MILLIONS OF DOLLARS)	
1997 .....	\$ 37
1998 .....	75
1999 .....	52
2000 .....	29
2001 .....	8
-----	
Total .....	\$201
=====	

## Capital Commitments -- Domestic

In 1996 NRG has provided a \$10 million loan commitment to a wholly-owned subsidiary of NRG Generating (U.S.) Inc. (NRGG). The purpose of the loan is to allow NRGG to fund its capital contribution to a cogeneration project currently under construction. NRG anticipates funding the loan in 1997.

Also in 1996, NRG has committed to provide NRGG power generation investment opportunities in the United States over a period of three years. The projects must have an aggregate, over the three year term, equity value of at least \$60 million or a minimum of 150 net megawatts. In addition, NRG has committed to finance these projects to the extent funds are not available to NRGG on comparable terms from other sources.

## Claims and Litigation

In normal course of business, NRG is a party to routine claims and litigation arising from current and prior operations. NRG is actively defending these matters and does not believe the outcome of such matters would materially impact the results of operations or financial position.

## 14. SEGMENT REPORTING

NRG conducts its business within one industry segment--independent power generation. Operations in the United States include wholly-owned operations and investments in various domestic energy projects. International operations include investments in various international energy projects. See Note 5 for significant equity method investments.

1996	U.S.	EUROPE	ASIA PACIFIC	OTHER AMERICAS	CORPORATE/ OTHER	TOTAL
-----						
(IN THOUSANDS)						
-----						
Revenues from wholly-owned operations.....	\$ 71,649					\$ 71,649
Equity in operating earnings (losses) of unconsolidated affiliates.....	1,473	\$ 17,385	\$11,155	\$ 967	\$ 1,835	32,815
-----						
Total operating revenues.....	73,122	17,385	11,155	967	1,835	104,464
Net income.....	28,182	17,385	11,155	967	(37,711) (1)	19,978

Assets reported on a consolidated basis.....	148,666				42,159 (2)	190,825
Equity investments and loans to affiliates.....	130,786	210,587	97,988	50,623		489,984
Total assets.....	279,452	210,587	97,988	50,623	42,159	680,809

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NRG ENERGY, INC.  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

14. SEGMENT REPORTING (Continued)

1995	U.S.	EUROPE	ASIA PACIFIC	OTHER AMERICAS	CORPORATE/ OTHER	TOTAL
(IN THOUSANDS)						
Revenues from wholly-owned operations.....	64,180					64,180
Equity in operating earnings (losses) of unconsolidated affiliates.....	(2,398)	22,143	11,451	29	(7,586)	23,639
Total operating revenues.....	61,782	22,143	11,451	29	(7,586)	87,819
Net income.....	50,813	22,143	11,451	29	(53,235) (1)	31,201
Assets reported on a consolidated basis.....	124,807				21,569 (2)	146,376
Equity investments and loans to affiliates.....	118,220	106,809	78,303	4,881		308,213
Total assets.....	\$243,027	\$106,809	\$78,303	\$4,881	\$ 21,569	\$454,589

(1) Includes all expenses not allocated to either consolidated operations or equity investments. This includes general, administrative and development expenses as well as other income (net), interest expense and taxes.

(2) Includes cash, debt issuance costs and other items not directly related to specific asset groups.

15. SUBSEQUENT EVENT

On February 6, 1997, NRG signed a subscription agreement with Energy Developments Limited (EDL) to acquire up to 20% of common stock, and an additional 15% of preference shares at AUS\$2.20 per share. EDL is an Australian company engaged exclusively in independent power generation from landfill gas, coal seam methane and natural gas (including latest technology combined cycle projects). EDL is the largest generator of power from coal seam methane in the world. The company currently operates over 200 MW of generation across five states and territories of Australia and has commenced the development of new projects in the United Kingdom, Asia and New Zealand. The current equity megawatt ownership held by EDL is approximately 170 MW. EDL is a publicly traded company with its securities listed on the Australian Stock Exchange. On February 11, 1997 NRG made an initial purchase of 7.2% (4.5 million shares) of common stock for AUS\$9.9 million (US\$7.9 million).

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REPORT OF INDEPENDENT AUDITORS  
NRG ENERGY, INC. AND SUBSIDIARIES

To the Board of Directors and Stockholder  
NRG Energy, Inc.  
Minneapolis, Minnesota

We have audited the accompanying consolidated balance sheet of NRG Energy, Inc. (the Company) (a wholly-owned subsidiary of Northern States Power Company) as of December 31, 1994 and the related consolidated statements of income, stockholder's equity, and cash flows for the year ended December 31, 1994. These consolidated financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these consolidated financial statements based on our audit. We did not audit the 1994 financial statements of Sunshine State Power BV and Sunshine State Power (No. 2) BV, the Company's investments in which are accounted for by use of the equity method. These investments represent 19% of total assets as of December 31, 1994 and the equity in earnings represents 32% of equity in earnings of projects for the year ended December 31, 1994. The financial statements of Sunshine State Power BV and Sunshine State Power (No. 2) BV were audited by other auditors whose reports have been furnished to us, and our opinion, insofar as it relates to the amounts included for such entities, is based solely on the reports of such other auditors.

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

In our opinion, based on our audit and the reports of the other auditors, such consolidated financial statements present fairly, in all material respects, the financial position of the Company as of December 31, 1994, and the results of its operations and its cash flows for the year ended December 31, 1994, in conformity with generally accepted accounting principles.

Deloitte & Touche LLP

Minneapolis, Minnesota  
March 24, 1995

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NRG ENERGY, INC.  
CONSOLIDATED BALANCE SHEET

	DECEMBER 31, 1994
	(THOUSANDS OF DOLLARS)
ASSETS	
Current Assets:	
Cash and cash equivalents.....	\$ 17,507
Restricted cash.....	13,817
Accounts receivable--trade, less allowance for doubtful accounts of \$185.....	11,576
Accounts receivable--affiliates.....	610
Income taxes receivable.....	2,442
Current portion of notes receivable.....	3,115
Inventory.....	1,704
Prepayments and other current assets.....	1,173
TOTAL CURRENT ASSETS.....	51,944
Property, Plant and Equipment, at Original Cost:	
In service.....	163,438
Under construction.....	2,289
	165,727
Less accumulated depreciation.....	(58,093)

Net property, plant and equipment.....	107,634
-----	
Other Assets:	
Investments in projects.....	164,863
Capitalized project costs.....	3,030
Notes receivable, less current portion-affiliates.....	3,687
Intangible assets, net of accumulated amortization of \$2,549 .....	44,798
Debt issuance costs, net of accumulated amortization of \$148 .....	614
-----	
Total other assets.....	216,992
-----	
TOTAL ASSETS.....	\$376,570
=====	

See accompanying notes.

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NRG ENERGY, INC.  
CONSOLIDATED BALANCE SHEET -- (CONTINUED)

	DECEMBER 31, 1994
	-----
	(THOUSANDS OF DOLLARS)
LIABILITIES AND STOCKHOLDER'S EQUITY	
Current liabilities:	
Current portion of long-term debt.....	\$ 3,306
Accounts payable--trade.....	5,199
Note payable--affiliates.....	3,037
Accrued property and sales taxes.....	2,291
Accrued salaries, benefits and related costs.....	2,751
Other current liabilities.....	11,021
-----	
TOTAL CURRENT LIABILITIES.....	27,605
-----	
Long-term debt, less current portion.....	90,033
Deferred revenues.....	8,811
Deferred income taxes.....	11,519
Deferred investment tax credits.....	2,324
Deferred compensation.....	1,556
-----	
TOTAL LIABILITIES.....	141,848
-----	
Commitments and Contingencies (Note 13)	
Stockholder's Equity:	
Common stock; \$1 par value; 1,000 shares authorized; 1,000 shares issued and outstanding.....	1
Additional paid-in capital.....	216,013
Retained earnings.....	15,122
Currency translation adjustments.....	3,586
-----	
TOTAL STOCKHOLDER'S EQUITY.....	234,722
-----	
TOTAL LIABILITIES AND STOCKHOLDER'S EQUITY.....	\$376,570
=====	

See accompanying notes.

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NRG ENERGY, INC.  
CONSOLIDATED STATEMENT OF INCOME

YEAR ENDED DECEMBER 31, 1994  
-----  
(THOUSANDS OF DOLLARS)

Operating revenues:	
Revenues from wholly-owned operations.....	\$63,970
Equity in operating earnings of unconsolidated affiliates.....	27,155
	-----
Total operating revenues.....	91,125
	-----
Operating costs and expenses:	
Cost of wholly-owned operations.....	34,861
Depreciation and amortization.....	8,675
General, administrative and development expenses .....	19,993
	-----
Total operating costs and expenses.....	63,529
	-----
Operating income.....	27,596
Other income (expense):	
Equity in gain from project termination settlements ....	9,685
Other income, net.....	1,411
Interest expense.....	(6,682)
	-----
Total other income .....	4,414
	-----
Income before income taxes.....	32,010
	-----
Income taxes.....	2,472
	-----
Net Income.....	\$29,538
	=====

See accompanying notes.

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NRG ENERGY, INC.  
CONSOLIDATED STATEMENT OF CASH FLOWS

	YEAR ENDED DECEMBER 31, 1994
	-----
	(THOUSANDS OF DOLLARS)
CASH FLOWS FROM OPERATING ACTIVITIES	
Net income.....	\$ 29,538
Adjustments to reconcile net income to net cash provided (used) by operating activities .....	
Undistributed equity in operating earnings of unconsolidated affiliates.....	(18,511)
Depreciation and amortization.....	8,675
Deferred income taxes and investment tax credits.....	(523)
Cash (used) provided by changes in certain working capital items:	
Accounts receivable--trade.....	(2,964)
Accounts receivable--affiliates.....	468
Accrued income taxes.....	(1,892)
Inventory.....	(438)
Prepayments and other current assets.....	(205)
Accounts payable--trade.....	(4,459)
Accounts payable--affiliates.....	942
Accrued property and sales taxes.....	(76)
Accrued salaries, benefits and related costs.....	1,246
Other current liabilities.....	1,240
Cash (used) by changes in other assets and liabilities .....	(615)
	-----
NET CASH PROVIDED (USED) BY OPERATING ACTIVITIES.....	12,426
	-----
CASH FLOWS FROM INVESTING ACTIVITIES	
Investments in projects.....	(102,119)
Loans to projects.....	(4,415)
Capital expenditures.....	(5,750)
(Increase) decrease in restricted cash.....	(13,817)
Other, net.....	2,255
	-----
NET CASH USED BY INVESTING ACTIVITIES.....	(123,846)
CASH FLOWS FROM FINANCING ACTIVITIES	
Capital contributions from parent.....	103,885
Dividends and other distributions paid to parent.....	(9)
Proceeds from issuance of long-term debt.....	2,375
Principal payments on long-term debt.....	(2,487)
	-----
NET CASH PROVIDED BY FINANCING ACTIVITIES.....	103,764

NET INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS.....	(7,656)
CASH AND CASH EQUIVALENTS AT BEGINNING OF YEAR.....	25,163
CASH AND CASH EQUIVALENTS AT END OF YEAR.....	\$ 17,507
SUPPLEMENTAL DISCLOSURES OF CASH FLOW INFORMATION	
Interest paid (net of amount capitalized).....	\$ 6,808
Income tax benefits received, net of taxes paid.....	(1,939)

See accompanying notes.

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NRG ENERGY, INC.  
CONSOLIDATED STATEMENT OF STOCKHOLDER'S EQUITY

	COMMON STOCK	ADDITIONAL PAID-IN CAPITAL	RETAINED EARNINGS (DEFICIT)	CURRENCY TRANSLATION ADJUSTMENTS	TOTAL STOCKHOLDER'S EQUITY
(THOUSANDS OF DOLLARS)					
Balances at December 31, 1993 .....	\$1	\$112,128	\$ (14,407)		\$ 97,722
Net income.....			29,538		29,538
Dividends and other distributions to parent.....			(9)		(9)
Capital contributions from parent ...		103,885			103,885
Currency translation adjustments ....				\$3,586	3,586
Balances at December 31, 1994 .....	\$1	\$216,013	\$ 15,122	\$3,586	\$234,722

See accompanying notes.

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NRG ENERGY, INC.  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

1. ORGANIZATION AND BASIS OF PRESENTATION

NRG Energy, Inc. (the Company), a Delaware Corporation, was incorporated on May 29, 1992, as a wholly-owned subsidiary of Northern States Power Company (NSP). Beginning in 1989, the Company was doing business through its predecessor companies. NRG Energy, Inc. and NRG Group, Inc. Minnesota corporations which were merged into the Company subsequent to its incorporation. The Company and its subsidiaries and affiliates develop, build, acquire, own and operate nonregulated energy-related businesses.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Principles of consolidation

The accompanying consolidated financial statements include the accounts of the Company and its subsidiaries (referred to collectively herein as NRG). All significant intercompany transactions have been eliminated. Investments in partnerships, joint ventures and projects representing ownership of more than 20%, but not in excess of 50%, are accounted for on the equity method.

Cash equivalents

Cash equivalents include highly liquid investments (primarily commercial paper) with a remaining maturity of three months or less at the time of purchase.

Restricted cash

Restricted cash consists primarily of cash collateral required in



connection with foreign currency hedging activities (see Note 12) and cash collateral for letters of credit issued in relation to project development activities.

#### Inventory

Inventory is valued at the lower of average cost or market and consists principally of spare parts and raw materials used to generate steam.

#### Property, plant and equipment

Property, plant and equipment are capitalized at original cost. Depreciation is computed using the straight-line method over the following estimated useful lives:

Buildings and improvements.....	20-45 years
Machinery and equipment.....	7-30 years
Office furniture and equipment ....	3-5 years

#### Capitalized interest

Interest incurred on funds borrowed to finance projects expected to require more than three months to complete is capitalized. Capitalization of interest is discontinued when the project is completed and considered operational. Capitalized interest is amortized using the straight-line method over the useful life of the related project. Capitalized interest was \$45,000 in 1994.

#### Development and capitalized project costs

These costs include professional services, dedicated employee salaries, permits, and other costs which are incurred incidental to a particular project. Such costs are expensed as incurred until a sales agreement or letter of intent is signed, after which time they are capitalized. When project operations begin, previously capitalized project costs are amortized on a straight-line basis over the lesser of the life of the project's related assets or revenue contract period.

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NRG ENERGY, INC.  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

## 2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

#### Debt issuance costs

Costs to issue long-term debt have been capitalized and are being amortized over the terms of the related debt.

#### Intangibles

Intangibles consist principally of service agreements and the excess of the cost of investment in subsidiaries over the underlying fair value of the net assets acquired and are being amortized using the straight-line method over 30 years. Intangibles also include patents which are being amortized using the straight-line method over 17 years. The Company periodically evaluates the recovery of goodwill and other intangibles based on an analysis of the estimated undiscounted future cash flows.

#### Income taxes

The Company is included in the consolidated tax returns of NSP. NRG

calculates its income tax provision on a separate return basis under a tax sharing arrangement with NSP. Current federal and state income taxes are payable to or receivable from NSP. NRG records income taxes in accordance with Statement of Financial Accounting Standards (SFAS) No. 109 "Accounting for Income Taxes." Under the liability method required by SFAS No.109, income taxes are deferred on all temporary differences between pretax financial and taxable income and between the book and tax bases of assets and liabilities. Deferred taxes are recorded using the tax rates scheduled by law to be in effect when the temporary differences reverse. Investment tax credits are deferred and amortized over the estimated lives of the related property.

#### Revenue recognition

Under fixed-price contracts, revenues are recognized as deliveries of products or services are made. Revenues and related costs under cost reimbursable contract provisions are recorded as costs are incurred. Anticipated future losses on contracts are charged against income when identified.

Deferred revenues related to a 1988 legal settlement with a major thermal customer. Settlement proceeds were deferred when received and are reflected in operating income on a straight-line basis over the life of the related steam contract which expires in 2001.

#### Foreign currency translation

The local currencies are generally the functional currency of NRG's foreign operations. Foreign currency denominated assets and liabilities are translated at end-of-period rates of exchange. Income, expense and cash flows are translated at weighted-average rates of exchange for the period. The resulting currency translation adjustments are accumulated and reported as a separate component of stockholder's equity.

Exchange gains and losses that result from foreign currency transactions (e.g., converting cash distributions made in one currency to another currency) are included in the results of operations. Through December 31, 1994, NRG has not experienced any material translation gains or losses from foreign currency transactions.

#### Derivative financial instruments

NRG's policy is to hedge financial currency denominated investments as they are made to preserve their U.S. dollar value. NRG has entered into currency hedging transactions through the use of forward

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### NRG ENERGY, INC.

#### NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

#### 2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

foreign currency exchange agreements. Gains and losses on these contracts offset the effect of foreign currency exchange rate fluctuations on the valuation of the investments underlying the hedges. The effect of hedging gains and losses, net of income taxes, is reported with other currency translation adjustments as a separate component of stockholder's equity. The Company is not hedging currency translation adjustments related to operating results. NRG does not speculate in foreign currencies.

#### Accounting change

In 1994, the Company adopted SFAS No. 112, "Employers' Accounting for Postretirement Benefits." SFAS No. 112 requires the accrual of certain employee costs (such as injury compensation or severance) to be paid in future periods. The adoption of this new accounting standard did not have a material effect on NRG's results of operations or financial condition.

### 3. BUSINESS ACQUISITIONS

Through its subsidiaries, NRG purchased equity interests during 1994 in three significant international projects, two in Germany and one in Australia. One of the investments is a 33% interest in Mitteldeutsche Braunkohlengesellschaft mbH (MIBRAG), a German corporation. MIBRAG was formed by the German government to operate mines, electric power plants and other energy-related facilities. The other German investment is a 50% interest in Saale Energie GmbH (Saale), also a German corporation. Saale owns a 400 megawatt share of a 900 megawatt power plant currently under construction near Schkopau, Germany. The Australian investment is a 37.5% interest (held by wholly-owned NRG subsidiaries Sunshine State Power BV and Sunshine State Power (No. 2) BV) in a joint venture that acquired a 1,680 megawatt coal-fired power plant in Gladstone, Queensland, Australia, which is operated by an NRG subsidiary. The total acquisition investments in these three projects through 1994, including capitalized developments costs, was approximately \$100 million. Earnings from equity interests in these NRG international projects acquired in 1994 contributed \$25.6 million to NRG's 1994 earnings.

On December 31, 1994, NRG, through a wholly-owned subsidiary, purchased a 50% partnership interest in Sunnyside Cogeneration Associates, a Utah joint venture (partnership) which owns and operates a 51 megawatt waste coal plant in Utah. The acquisition investment by NRG was \$11.5 million. The waste coal plant is currently being operated by a 50%-owned NRG partnership.

In August 1993, NRG Energy Center, Inc., a wholly-owned subsidiary of NRG, acquired the assets of the Minneapolis Energy Center (MEC), a district heating and cooling system in downtown Minneapolis, Minnesota. The system uses steam and chilled water generating facilities to heat and cool buildings for about 90 heating and 30 cooling customers. The acquisition was reflected in the financial statements under the purchase method of accounting. Accordingly, the assets acquired and liabilities assumed in the acquisition have been recorded at their fair values. The purchase price was \$110 million, \$84 million of which was financed by project debt. The purchase price primarily included facilities, long-term service agreements and goodwill. The results of operations of MEC since August 1993 have been included in the consolidated financial statements.

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NRG ENERGY, INC.  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

### 4. PROPERTY, PLANT AND EQUIPMENT

The major classes of property, plant and equipment at December 31 were as follows:

	1994
	-----
	(THOUSANDS OF DOLLARS)
Facilities and equipment, including construction work in progress of \$2,289	\$153,221
Land and improvements.....	10,397
Office furnishings and equipment.....	2,109
	-----
Total property, plant and equipment .....	165,727
Accumulated depreciation.....	(58,093)
	-----
Net property, plant and equipment.....	\$107,634
	=====

### 5. INVESTMENTS ACCOUNTED FOR BY EQUITY METHOD

A summary of NRG's significant equity-method investments which were in operation at December 31, 1994 is as follows:

NAME	GEOGRAPHIC AREA	ECONOMIC INTEREST	PURCHASED OR PLACED IN SERVICE
Various Independent Power Production Facilities.....	U.S.A.	45%-50%	July 1991-December 1994
Rosebud Syncoal Partnership.....	U.S.A.	50%	August 1993
MIBRAG.....	Europe	33%	January 1994
Gladstone Power Station.....	Australia	37.5%	March 1994
Schkopau Power Station.....	Europe	20.6%	Under Construction
Scudder Latin American Trust for Independent Power Energy Projects .....	Latin America	6.3%-12.5%	April-December 1994

Summarized financial information for investments in projects accounted for under the equity method as of and for the year ended December 31, is as follows:

	1994
	(THOUSANDS OF DOLLARS)
Operating revenues.....	\$ 731,308
Costs and expenses.....	604,428
Net income.....	\$ 126,880
Current assets.....	\$ 452,651
Noncurrent assets.....	1,787,089
Total assets.....	\$2,239,740
Current liabilities.....	\$ 159,840
Noncurrent liabilities.....	1,757,057
Equity.....	322,843
Total liabilities and equity.....	\$2,239,740
NRG's share of equity.....	\$ 164,863
NRG's share of income.....	\$ 27,155

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NRG ENERGY, INC.  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

5. INVESTMENTS ACCOUNTED FOR BY EQUITY METHOD (Continued)

In July 1994, Michigan Cogeneration Partners Limited Partnership (MCP), a partnership between subsidiaries of NRG and Cogentrix, Inc., reached an agreement with Consumers Power Company (Consumers), an electric utility headquartered in Jackson, Michigan, to terminate the power sales contract related to a 65 megawatt cogeneration facility being developed by MCP in Parchment, Michigan. The agreement to terminate the contract required Consumers to make payment to MCP of \$29.8 million. As a result, NRG recorded in Other Income. A net pretax gain from the termination of this contract of \$9.7 million in 1994.

In 1994, the Company recorded a pretax charge of \$5.0 million to write down the carrying value of two energy projects. The charge was determined based on estimated discounted future cash flows, and is recorded in Other Income, Net.

6. RELATED PARTY TRANSACTIONS

Operating Agreements

NRG has two agreements with NSP for the purchase of thermal energy. Under the terms of the agreements, NSP charges NRG for certain incremental costs (fuel, labor, plant maintenance, and auxiliary power) incurred by NSP to produce the thermal energy. NRG paid NSP \$6.6 million in 1994 under these agreements.

NRG has a renewable 10-year agreement with NSP, expiring on December 31, 2001, whereby NSP agrees to purchase refuse-derived fuel for use in certain of its boilers and NRG agrees to pay NSP a burn incentive. NRG has an agreement expiring in 2006 to sell wood by-products obtained from a thermal customer to NSP for use as fuel. Under these agreements, NRG received \$1.7 million from NSP and paid \$2.2 million to NSP in 1994.

Administrative Services and Other Costs

NRG and NSP have entered into an agreement to provide for the reimbursement of actual administrative services provided to each other, an allocation of NSP administrative costs and a working capital fee. Services provided by NSP to NRG are principally cash management, legal, accounting, employee relations and engineering. In addition, NRG employees participate in operating certain employee benefit plans of NSP. During 1994, NRG paid NSP \$6.2 million as reimbursement for the cost of services provided.

Allocation is on a direct charge, actual cost basis where possible. When this is not possible, an allocation is made based upon employee headcounts, operating revenues and investment in fixed assets. Management believes that "allocated" costs approximate expenses that would be incurred on a stand alone basis.

7. NOTES RECEIVABLE

Notes receivable consist primarily of fixed and variable rate notes secured by equity interests in partnerships and joint ventures. The weighted average interest rate on the notes was 11.2% at December 31, 1994.

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NRG ENERGY, INC.  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

8. LONG-TERM DEBT

Long-term debt consists of the following at December 31:

	1994
	----- (THOUSANDS OF DOLLARS)
NRG Energy Center, Inc. Senior Secured Notes Series due June 15, 2013, 7.31% .....	\$81,498
Note payable to NSP, due December 1, 1995-2006, 5.40%-6.75% ....	9,466
NRG Sunnyside Inc. note payable, due December 31, 1997, 10.00% .	2,375
	-----
	93,339
Less current maturities.....	(3,306)
	-----
	\$90,033
	=====

The NRG Energy Center, Inc. notes are secured principally by MEC's long-term assets. In accordance with the terms of the note agreements, the

Company is required to maintain compliance with certain financial covenants primarily related to incurring debt, disposing of Company assets, and affiliate transactions. The Company was in compliance with these covenants at December 31, 1994.

The Note Payable to NSP relates to long-term debt assumed by the Company in connection with the transfer of ownership of an RDF processing plant by NSP to the Company during 1993.

The NRG Sunnyside, Inc. note payable was issued in connection with the purchase of an equity interest in a waste-coal project during 1994.

Annual maturities of long-term debt for the years ending after December 31, 1994 are as follows:

(THOUSANDS OF DOLLARS)	
1995.....	\$ 3,306
1996.....	3,762
1997.....	3,979
1998.....	3,335
1999.....	3,581
Thereafter ..	75,376
	-----
Total.....	\$93,339
	=====

The Company has a revolving-credit agreement which may not exceed \$5.0 million. At December 31, 1994, there were no borrowings under the credit agreement.

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NRG ENERGY, INC.  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

9. INCOME TAXES

The provision for income taxes consists of the following:

1994	
-----	
(THOUSANDS OF DOLLARS)	
Current	
Federal.....	\$ 1,694
State.....	737
Foreign.....	219
	-----
	2,650
Deferred	
Federal.....	1,280
State.....	369
	-----
	1,649
Tax credits recognized ..	(1,827)
	-----
Total income tax expense.....	\$ 2,472
	=====

The components of the net deferred income tax liability at December 31 were:

	1994
	----- (THOUSANDS OF DOLLARS)
Deferred tax liabilities	
Differences between book and tax bases of property .....	\$13,269
Investments in projects.....	6,168
Goodwill.....	256
Other.....	930
	-----
Total deferred tax liabilities.....	20,623
Deferred tax assets	
Deferred revenue.....	3,645
Development costs.....	2,047
Deferred investment tax credits.....	978
Deferred compensation, accrued vacation and other reserves.....	992
Steam capacity rights.....	1,175
Other.....	267
	-----
Total deferred tax assets.....	9,104
	-----
Net deferred tax liability.....	\$11,519
	=====

Actual income tax expense recorded differs from the statutory federal income tax rate of 35% due to state income taxes, varying tax treatment of foreign income and expenses and tax credits recognized.

Income before income taxes includes foreign income of \$25.6 million in 1994. NRG's management intends to reinvest in earnings of foreign operations indefinitely. Accordingly, U.S. income taxes and foreign withholding taxes have not been provided on the earnings of foreign subsidiary companies. The cumulative amount of undistributed pre-tax earnings of foreign subsidiaries upon which no U.S. income taxes or foreign withholding taxes have been provided is approximately \$25.6 million at December 31, 1994. The additional U.S. income tax and foreign withholding tax on the unremitted foreign earnings, if repatriated, would be offset in whole or in part by foreign tax credits. Thus, it is impracticable to estimate the amount of tax that might be payable.

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NRG ENERGY, INC.  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

10. BENEFIT PLANS AND OTHER POSTRETIREMENT BENEFITS

Pension Benefits

NRG participates in NSP's noncontributory, defined benefit pension plan that covers substantially all employees. Benefits are based on a combination of year of service, the employee's highest average pay for 48 consecutive months, and Social Security benefits. Pension costs for NRG are determined and recorded under the provisions of SFAS No. 87, "Employers' Accounting for Pensions." Net annual periodic pension cost includes the following components:

	1994
	-----
	(THOUSANDS OF DOLLARS)
Service cost-benefits earned during the period.....	\$ 654
Interest cost on projected benefit obligation.....	354
Actual return on assets.....	(58)
Net amortization and deferral .....	(262)
	-----
Net periodic pension cost .....	\$ 688
	=====

The funded status of the pension plan in which NRG employees participate is as follows at December 31:

	NSP PLAN-1994	
	-----	-----
	TOTAL NSP	NRG PORTION
	-----	
	(THOUSANDS OF DOLLARS)	
Actuarial present value of benefit obligation		
Vested.....	\$ 571,254	\$ 563
Nonvested.....	120,420	1,016
	-----	-----
Accumulated benefit obligation.....	\$ 691,674	\$1,579
	=====	=====
Projected benefit obligation.....	\$ 836,957	\$4,228
Plan assets at fair value.....	1,165,584	5,170
	-----	-----
Plan asset in excess of projected benefit obligation.....	(328,627)	(942)
Unrecognized prior service costs.....	(21,538)	(96)
Unrecognized net actuarial gain .....	370,289	1,038
Unrecognized net transitional asset .....	691	--
	-----	-----
Net pension liability recorded .....	\$ 20,815	\$ --
	=====	=====

The weighted-average discount rate used in determining the actuarial present value of the projected benefit obligation was 8% in 1994. The rate of increase in future compensation levels used in determining the actuarial present value of the projected obligation was 5% in 1994. The assumed long-term rate of return on assets used for cost determinations under SFAS No. 87 was 8% for 1994. Plan assets consist principally of common stock of public companies and U.S. Government securities.

#### Postretirement Health Care

Effective January 1, 1993, NRG adopted the provisions of SFAS No. 106, "Employers' Accounting for Postretirement Benefits Other Than Pensions." SFAS No. 106 requires the actuarial determined obligation for postretirement health care and death benefits be fully accrued by the date employees attain full eligibility for such benefits, which is generally when they reach retirement age. In conjunction with the adoption of SFAS No. 106, NRG elected to amortize on a straight-line basis over 20 years the unrecognized accumulated postretirement benefit obligation (APBO) of \$1.4 million for current and future



NRG ENERGY, INC.  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

10. BENEFIT PLANS AND OTHER POSTRETIREMENT BENEFITS (Continued)

retirees. This obligation considered 1994 plan design changes not in effect in 1993, including Medicare integration, increased retiree cost sharing, and managed indemnity measures.

The following table sets forth the funded status of the health care plan in which NRG employees participate at December 31:

NSP PLAN-1994		
	TOTAL NSP	NRG PORTION
(THOUSANDS OF DOLLARS)		
APBO		
Retirees.....	\$ 132,200	\$ 34
Fully eligible plan participants.....	21,500	359
Other active plan participants.....	79,400	1,319
	233,100	1,712
Total APBO.....		
Plan assets at fair value.....	8,000	--
	225,100	1,712
APBO in excess of plan assets.....	2,300	265
Unrecognized net actuarial gain.....	2,300	265
Unrecognized net transition obligation.....	(194,000)	(1,273)
	\$ 33,400	\$ 704
Net benefit obligation recorded.....	\$ 33,400	\$ 704

The assumed health care cost trend rates used in measuring the APBO at December 31, 1994 were 11.0% for those under age 65, and 7.5% for those over age 65. The assumed cost trends are expected to decrease each year until they reach 5.5% for both age groups in the year 2004, after which they are assumed to remain constant. A one percent increase in the assumed health care cost trend rate for each year would increase the APBO by approximately 13% as of December 31, 1994. Service and interest cost components of the net periodic postretirement cost would increase by approximately 16% with a similar one percent increase in the assumed health care cost trend rate. The assumed discount rate used in determining the APBO was 8% for December 31, 1994, compounded annually. The assumed long-term rate of return on assets used for cost determinations under SFAS No. 106 was 8% for 1994. The net annual periodic postretirement benefit cost recorded for 1994 consists of the following components:

1994	
(THOUSANDS OF DOLLARS)	
Service cost--benefits earned during the year .	\$140
Interest cost on APBO.....	126
Amortization of transition obligation .....	70
Net amortization and deferral.....	--
	-----

Net periodic postretirement health care costs..... \$336  
=====

11. SALES TO SIGNIFICANT CUSTOMERS

NRG and the Ramsey/Washington Resource Recovery Project have a service agreement for waste disposal which expires in 2006. Approximately 35.5% in 1994 of the Company's operating revenues from wholly-owned operations were recognized under this contract. In addition, sales to one thermal customer amounted to 16.6% of operating revenues from wholly-owned operations in 1994.

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NRG ENERGY, INC.  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

12. FINANCIAL INSTRUMENTS

The estimated December 31 fair values of NRG's recorded financial instruments are as follows:

	1994	
	CARRYING AMOUNT	FAIR VALUE
	(THOUSANDS OF DOLLARS)	
Cash and cash equivalents.....	\$17,507	\$17,507
Restricted cash.....	13,817	13,817
Notes receivable, including current portion.....	6,802	6,802
Long-term debt, including current portion ..	93,339	82,694

For cash, cash equivalents and restricted cash, the carrying amount approximates fair value because of the short-term maturity of those instruments. The fair value of notes receivable is based on expected future cash flows discounted at market interest rates. The fair value of long-term debt is estimated based on the quoted market prices for the same or similar issues.

NRG has entered into three forward foreign currency exchange contracts with a counterparty to hedge exposure to currency fluctuations to the extent permissible by hedge accounting requirements. Pursuant to these contracts, transactions have been executed that are designed to protect the economic value in U.S. dollars of NRG's equity investments, denominated in Australian dollars and German deutsche marks (DM). NRG's forward currency exchange contracts, in the notional amount of \$93 million, hedge approximately \$94 million of foreign currency denominated investments at December 31, 1994. These foreign currency exchange contracts are not reflected in NRG's balance sheet. The contracts do require cash collateral which was \$6.7 million at December 31, 1994 and is included in restricted cash on NRG's balance sheet. The contracts terminate in 2004 and require foreign currency interest payments by either party during each year of the contract. If the contracts had been terminated at December 31, 1994, \$4.3 million would have been payable by NRG for currency exchange rate changes to date. Management believes NRG's exposure to credit risk due to nonperformance by the counterparty to its forward exchange contracts is not significant, based on the investment grade rating of the counterparty.

13. COMMITMENTS AND CONTINGENCIES

Operating Lease Commitments

The Company has noncancelable operating leases for office space. The leases require the company to pay certain annual operating costs, including maintenance, insurance and real estate taxes. Rental expense under these operating leases was \$178 in 1994 (thousands of dollars). Future minimum lease commitments under these leases for the years ended after December 31, 1994 are as follows:

(THOUSANDS OF DOLLARS)	
1995.....	\$221
1996.....	246
1997.....	131
	-----
Total...	\$598
	=====

Financial Guarantees

Certain of the partnerships in which NRG is an equity investor have loan agreements and debt outstanding which contain restrictive covenants. In the event that certain covenants are not met, NRG has guaranteed the contribution of \$3.8 million of additional equity. No contributions of additional equity were necessary during 1994.

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NRG ENERGY, INC.  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

13. COMMITMENTS AND CONTINGENCIES (Continued)

Capital Commitments

NRG is contractually committed to additional equity investments in an existing German energy project. Such commitments are for approximately DM 36 million in 1995 and DM 35 million in 1996. The 1995 and 1996 commitments would be approximately \$23 million each year, based on exchange rates in effect at December 31, 1994.

In addition, NRG is contractually committed to additional equity investments of \$20.6 million in the Scudder Latin American Trust for Independent Power Energy Projects as of December 31, 1994.

14. SEGMENT REPORTING

NRG conducts its business within one industry segment--independent power generation. Operations in the United States include wholly-owned operations and investments in various domestic energy projects. International operations include investments in various international energy projects. See Note 5 for significant equity method investments.

1994	U.S.	EUROPE	ASIA PACIFIC	OTHER AMERICAS	CORPORATE/ OTHER	TOTAL
-----						
(IN THOUSANDS)						
Revenues from wholly-owned operations.....	\$ 63,970					\$ 63,970
Equity in operating earnings (losses) of unconsolidated affiliates.....	(766)	\$19,340	\$ 8,581			27,155

Total operating revenues.....	63,204	19,340	8,581		91,125
Net income.....	19,668	19,340	8,581	\$(18,051) (1)	29,538
Assets reported on a consolidated basis.....	122,087			34,380 (2)	156,467
Equity investments and loans to affiliates.....	116,073	33,389	70,641		220,103
Total assets.....	\$238,160	\$33,389	\$70,641	\$ 34,380	\$376,570

- (1) Includes all expenses not allocated to either consolidated operations or equity investments. This includes general, administrative and development expenses as well as other income (net), interest expense and taxes.
- (2) Includes cash, debt issuance costs and other items not directly related to specific asset groups.

#### 15. SUBSEQUENT EVENT

NRG, through wholly-owned subsidiaries, owns 45% of the San Joaquin Valley Energy Partnership (SJVEP), which owns four plants located near Fresno, California with a total capacity of 55 megawatts. Through February 1995, the plants operated under long-term Standard Offer 4 (SO4) power sales contracts with Pacific Gas and Electric (PG&E) which expire in 2017. On February 28, 1995, PG&E reached basic agreements with SJVEP to acquire the SO4 contracts. The parties entered into a bridging agreement to cover the period until all regulatory approvals are received for the transaction. The bridging agreement required SJVEP to cease power deliveries to PG&E as of February 28, 1995. The negotiated agreements will result in cost savings for PG&E customers as well as economic benefits for SJVEP. The final impact of this transaction on the financial results of NRG will not be known until the agreements have been approved and all costs associated with the idling of the facilities are known. It is expected that a one-time gain from the transaction will be recorded in the first half of 1995. SJVEP will continue to own and maintain the facilities and will explore all available options.

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NRG ENERGY, INC.  
CONSOLIDATED BALANCE SHEETS  
(UNAUDITED)

	SEPTEMBER 30,	
	1997	1996
	(THOUSANDS OF DOLLARS)	
<b>ASSETS</b>		
<b>Current Assets:</b>		
Cash and cash equivalents .....	\$ 19,294	\$ 54,727
Restricted cash .....	347	23,645
Accounts receivable-trade, less allowance for doubtful accounts .....	14,138	12,587
Accounts receivable-affiliates .....	4,956	5,361
Current portion of notes receivable--affiliates .....	11,587	4,109
Current portion of notes receivable .....	46,571	1,403
Income taxes receivable .....	14,249	1,500
Inventory .....	2,624	2,367
Prepayments and other current assets .....	4,972	1,149
<b>TOTAL CURRENT ASSETS .....</b>	<b>118,738</b>	<b>106,848</b>
<b>Property, plant and equipment, at original cost:</b>		
In service .....	215,576	170,673
Under construction .....	26,191	16,916
	241,767	187,589
Less accumulated depreciation .....	(76,852)	(69,400)

Net property, plant and equipment.....	164,915	118,189
Other Assets:		
Investments in projects .....	635,047	266,504
Capitalized project costs .....	26,129	5,921
Notes receivable, less current portion--affiliates .....	75,439	45,363
Intangible assets, net of accumulated amortization .....	40,098	40,856
Debt issuance costs, net of accumulated amortization .....	6,450	2,780
Total other assets .....	783,163	361,424
TOTAL ASSETS .....	\$1,066,816	\$586,461

See accompanying notes.

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NRG ENERGY, INC.  
CONSOLIDATED BALANCE SHEETS -- (CONTINUED)  
(UNAUDITED)

	SEPTEMBER 30,	
	1997	1996
	(THOUSANDS OF DOLLARS)	
LIABILITIES AND STOCKHOLDER'S EQUITY		
Current Liabilities:		
Current portion of long-term debt .....	\$ 43,311	\$ 3,892
Accounts payable--trade .....	2,841	4,405
Accrued income taxes .....	8,586	--
Accrued property and sales taxes .....	2,961	2,827
Accrued salaries, benefits and related costs .....	8,991	5,880
Accrued interest .....	5,471	2,150
Other current liabilities .....	5,587	990
TOTAL CURRENT LIABILITIES .....	77,748	20,144
Long-term debt, less current portion .....	474,427	209,406
Deferred revenues .....	13,597	6,686
Deferred income taxes .....	16,042	14,650
Deferred investment tax credits .....	1,662	1,917
Deferred compensation .....	2,061	1,646
TOTAL LIABILITIES.....	585,537	254,449
Stockholder's Equity:		
Common stock; \$1 par value; 1,000 shares authorized; 1,000 shares issued and outstanding .....	1	1
Additional paid-in capital .....	431,374	271,013
Retained earnings .....	80,715	57,592
Currency translation adjustments .....	(30,811)	3,406
TOTAL STOCKHOLDER'S EQUITY .....	481,279	332,012
TOTAL LIABILITIES AND STOCKHOLDER'S EQUITY .....	\$1,066,816	\$586,461

See accompanying notes.

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NRG ENERGY, INC.

CONSOLIDATED STATEMENTS OF INCOME  
(UNAUDITED)

	NINE MONTHS ENDED SEPTEMBER 30,	
	1997	1996
(THOUSANDS OF DOLLARS)		
Operating Revenues:		
Revenues from wholly-owned operations .....	\$ 65,081	\$ 52,479
Equity in operating earnings of unconsolidated affiliates .....	17,759	19,375
Total operating revenues .....	82,840	71,854
Operating costs and expenses:		
Cost of operations--wholly-owned operations .....	32,863	26,858
Depreciation and amortization .....	7,096	6,300
General, administrative, and development .....	28,402	26,599
Total operating costs and expenses .....	68,361	59,757
Operating income .....	14,479	12,097
Other income (expense):		
Other income, net .....	8,610	6,117
Interest expense .....	(19,815)	(11,303)
Total other income (expense) .....	(11,205)	(5,186)
Income before income taxes .....	3,274	6,911
Income taxes (benefits) .....	(11,140)	(4,358)
Net Income.....	\$ 14,414	\$ 11,269

See accompanying notes.

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NRG ENERGY, INC.  
CONSOLIDATED STATEMENTS OF CASH FLOWS  
(UNAUDITED)

	NINE MONTHS ENDED SEPTEMBER 30,	
	1997	1996
(THOUSANDS OF DOLLARS)		
CASH FLOWS FROM OPERATING ACTIVITIES		
Net income.....	\$ 14,414	\$ 11,269
Adjustments to reconcile net income to net cash provided (used) by operating activities .....		
Undistributed equity in operating earnings of unconsolidated affiliates.....	(2,662)	(8,408)
Depreciation and amortization .....	7,096	6,300
Deferred income taxes and investment tax credits.....	7,245	5,332
Cash provided (used) by changes in certain working capital items		

Accounts receivable.....	(14,138)	(2,113)
Accounts receivable-affiliates.....	7,105	(1,862)
Accrued income taxes.....	1,777	(11,475)
Inventory.....	(312)	(556)
Prepayments and other current assets.....	(328)	595
Accounts payable-trade.....	(1,602)	(1,803)
Accrued property and sales taxes.....	802	932
Accrued salaried, benefits and related costs.....	2,432	(739)
Accrued interest.....	745	450
Other current liabilities.....	1,163	544
Cash provided (used) by changes in other assets and liabilities	3,711	(868)
	-----	-----
Net cash provided (used) by operating activities .....	27,448	(2,402)
	-----	-----
CASH FLOWS FROM INVESTING ACTIVITIES		
Investments in projects .....	(326,882)	(53,403)
Changes in notes receivable .....	(59,195)	(7,819)
Capital expenditures .....	(41,062)	(11,422)
Cash from sale of project investment .....	6,655	--
Decrease (increase) in restricted cash .....	17,341	(13,872)
Cash distribution from project termination settlement .....	--	15,671
Other, net .....	594	--
	-----	-----
Net cash used by investing activities .....	(402,549)	(70,845)
	-----	-----
CASH FLOWS FROM FINANCING ACTIVITIES		
Capital contributions from parent .....	80,361	--
Proceeds from issuance of long-term debt .....	303,511	122,671
Principal payments on long-term debt .....	(1,915)	(1,736)
	-----	-----
Net cash provided by financing activities .....	381,957	120,935
	-----	-----
Net increase in cash and cash equivalents .....	6,856	47,688
	-----	-----
Cash and cash equivalents at beginning of period .....	12,438	7,039
	-----	-----
CASH AND CASH EQUIVALENTS AT END OF PERIOD .....	\$ 19,294	\$ 54,727
	=====	=====

See accompanying notes.

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NRG ENERGY, INC.  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS  
(UNAUDITED)

1. ORGANIZATION AND BASIS OF PRESENTATION

NRG Energy, Inc. (the Company), a Delaware Corporation, was incorporated on May 29, 1992, as a wholly-owned subsidiary of Northern States Power Company (NSP). Beginning in 1989, the Company was doing business through its predecessor companies, NRG Energy, Inc. and NRG Group, Inc., Minnesota corporations which were merged into the Company subsequent to its incorporation. The Company and its subsidiaries and affiliates develop, build, acquire, own and operate nonregulated energy-related businesses.

In the opinion of management, the unaudited interim consolidated financial information of the Company contains all adjustments, consisting of only those of a recurring nature, necessary to present fairly the Company's financial position and results of operations. All significant inter-company accounts, transactions, and profits have been eliminated. These financial statements are for interim periods and do not include all information normally provided in annual financial statements and notes thereto for the year ended December 31, 1996 and should be read in conjunction with the consolidated financial statements and notes thereto for the year ended December 31, 1996, contained in the Company's 1996 Annual Report. The results of operation for the interim periods are not necessarily indicative of the results that may be expected for the full year.

2. RESTRICTED CASH

Restricted cash consists primarily of cash collateral required in

connection with foreign currency hedging activities and cash collateral for letters of credit issued in relation to project development activities. At September 30, 1997, the required levels of restricted cash were lower than the same period in 1996 due to the change in the market value of the Company's exchange swaps and the posting of an \$8 million letter of credit which replaced the collateral requirement.

### 3. PROPERTY, PLANT AND EQUIPMENT

The major classes of property, plant and equipment at September 30 were as follows:

	1997	1996
	-----	-----
	(THOUSANDS OF DOLLARS)	
Facilities and equipment, including construction work in progress of \$26,191 and \$16,916 .....	\$227,363	\$174,221
Land and improvements .....	10,398	10,398
Office furnishings and equipment .....	4,006	2,970
	-----	-----
Total property, plant and equipment .....	241,767	187,589
Accumulated depreciation .....	(76,852)	(69,400)
	-----	-----
Net property, plant and equipment .....	\$164,915	\$118,189
	=====	=====

The primary contributors to the increased facilities and equipment is due to increased work in process at NEO for the construction of its landfill gas projects (\$32 million), investments in NRG's MEC projects (\$5 million), construction at Millennium (\$10 million) and the purchase of San Diego Power & Cooling (\$6 million).

### 4. BUSINESS ACQUISITIONS

On February 6, 1997, NRG signed a subscription agreement with Energy Development Limited (EDL) to acquire up to 20% of common stock , and an additional 15% of preference shares at AUS\$2.20

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NRG ENERGY, INC.  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)  
(UNAUDITED)

### 4. BUSINESS ACQUISITIONS (Continued)

per share. EDL is an Australian company engaged exclusively in independent power generation from landfill gas, coal seam methane and natural gas (including latest technology combined cycle projects). EDL is the largest generator of power from coal seam methane in the world. The company currently operates over 200 MW of generation across five states and territories in of Australia and has commenced the development of new projects in the United Kingdom, Asia and New Zealand. On February 11, 1997 NRG made an initial purchase of 7.2% (4.5 million shares) of common stock for AUS\$9.9 million (US\$7.9 million). On September 24, 1997, NRG purchased an additional 10,109,670 shares of common stock of EDL for an aggregate purchase price of AUS \$22.2 million (US \$16.1 million on that date), bringing NRG's ownership level to 20% of the outstanding shares.

On December 19, 1996 NRG and Nordic Power Invest AB purchased 96.6% of Bolivian Power Company Limited. On October 30, the Company sold a portion of its investment and reduced its ownership to 48.3%.

In May 1997, the Company acquired a 25.37% interest in Loy Yang A for approximately \$257 million. Loy Yang A is a 2,000 MW brown coal fired thermal power station and adjacent coal mine located in Victoria, Australia which the



State of Victoria sold as part of its privatization program. The power station has four generating units, each with a 500 MW boiler and turbo generator, which commenced commercial operation between July 1984 and December 1988. In addition, the Company through its Loy Yang affiliate manages the common infrastructure facilities that are located on the Loy Yang site, the adjacent Loy Yang B 1,000 MW power station and several other nearby power stations.

On June 25, 1997, the Company purchased San Diego Power & Cooling. The purchase price was \$6.7 million, including a note from the seller for \$2.7 million.

In July 1997, the Company acquired a 50% interest in Cadillac Renewable Energy, a 34 MW steam turbine power plant located in Cadillac, Michigan for \$1.9 million. Electricity from the plant is sold to Consumers Energy under a long-term power purchase agreement.

In September 1997, Millennium Cogen, LLC, an NRG affiliate, entered into a Construction and Term Loan Agreement to finance the construction of a 117 MW cogeneration plant in Morris, Illinois. The Company has entered into a \$22 million equity commitment and a \$1.2 million guaranty of certain obligations of Millennium Operation, Inc., an NRG affiliate that will operate the project. The Company will have a 50% ownership interest that is estimated to be operational by December 1998.

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NRG ENERGY, INC.  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)  
(UNAUDITED)

5. LONG-TERM DEBT

Long-term debt consists of the following at September 30:

	1997	1996
	----- (THOUSANDS OF DOLLARS)	
NRG Energy, Inc. revolving credit facility, due March 17, 2000.....	\$ 38,000	\$ --
NRG Energy Center, Inc. Senior Secured Notes Series due June 15, 2013, 7.31% .....	75,070	77,591
Note payable to NSP, due December 1, 1995-2006		
5.40%-6.75% .....	8,406	8,957
Millennium Cogen, LLC, due May 2004, LIBOR + 1%-1.25% .....	16,901	--
NRG Sunnyside, Inc. note payable, due December 31, 1997		
10.00% .....	1,750	1,750
NRG San Diego, Inc., due June 25, 2003		
8.0% .....	2,611	--
NRG Energy Senior Notes, due February 1, 2006		
7.625% .....	125,000	125,000
NRG Energy Senior Notes, due 2007		
7.5% .....	250,000	--
	-----	-----
	517,738	213,298
Less current maturities .....	(43,311)	(3,892)
	-----	-----
Total .....	\$474,427	\$209,406
	=====	=====

The NRG Energy Center, Inc. notes are secured principally by long-term assets of the Minneapolis Energy Center (MEC). In accordance with the terms of the note agreements, MEC is required to maintain compliance with certain financial covenants primarily related to incurring debt, disposing of MEC assets, and affiliate transactions. MEC was in compliance with these covenants at September 30, 1997.

The note payable to NSP relates to long-term debt assumed by the Company in connection with the transfer of ownership of an RDF processing plant by NSP to the Company in 1993.

The NRG Sunnyside, Inc. note payable was issued in connection with the purchase of an equity interest in a waste-coal project in 1994.

The NRG Energy Senior Notes due 2006, were issued in January 1996, are unsecured and require semi-annual interest payments on February 1 and August 1.

The NRG Energy Center Notes due 2007 were issued in June 1997, are unsecured and require semi-annual interest payments on June 15 and December 15.

The NRG San Diego, Inc. Note was issued in June 1997 in conjunction with the acquisition of San Diego Power and Cooling Company.

The NRG Energy revolving credit facility that was issued in March 1997, is unsecured and will be used for general corporate purposes, including letters of credit and interim funding for NRG project investments.

The Millennium Cogen Notes represent a construction and term loan agreement up to \$96.0 million which is secured by the projects' asset. Payment on principal and interest is not required until the end of the term loan agreement.

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NRG ENERGY, INC.  
 NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)  
 (UNAUDITED)

5. LONG-TERM DEBT (Continued)

Annual maturities of long-term debt for the years ending after September 30, 1997 are as follows:

(THOUSANDS OF DOLLARS)	
1997 remaining	\$ 43,311
1998 .....	3,903
1999 .....	4,149
2000 .....	4,409
2001 .....	4,728
2002 .....	5,023
Thereafter .....	452,215
	-----
Total .....	\$517,738
	=====

6. INCOME TAXES

NRG and its parent, NSP, have entered into a federal and state income tax sharing agreement relative to the filing of consolidated federal and state income tax returns. The agreement provides, among other things, that (1) if NRG, along with its subsidiaries, is in a taxable income position, NRG will be currently charged with an amount equivalent to its federal and state income tax computed as if the group had actually filed separate federal and state returns, and (2) if NRG, along with its subsidiaries, is in a tax loss position, NRG will be currently reimbursed to the extent its combined losses are utilized in a consolidated return, and (3) if NRG, along with its

subsidiaries, generates tax credits, NRG will be currently reimbursed to the extent its tax credits are utilized in a consolidated return.

#### 7. ADDITIONAL PAID IN CAPITAL

NSP provided NRG with additional capital contributions of \$80 million in December 1996 (for use in the Cobee acquisition), \$20 million in February 1997 (for investment in various projects including EDL), and \$60.9 in May 1997 (for the Loy Yang acquisition).

#### 8. SUBSEQUENT EVENTS

On November 4, 1997, the Company acquired 100% of the outstanding shares of Pacific Generation Company for \$151.3 million. Pacific Generation has ownership interest in 11 projects with a total capacity of 737 MW, with operations responsibility for 312 MW and net ownership interests of 166 MW. The acquisition was financed primarily through the use of the Company's revolving credit facility.

On November 21, 1997, the Company with its 50/50 partner Destec, signed an Asset Sale Agreement to acquire the El Segundo plant, a 1020 MW facility, from Southern California Edison for \$87.75 million. The financial closing on the facility is set for the first week of January 1998.

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NRG ENERGY, INC. AND SUBSIDIARIES  
UNAUDITED PRO FORMA CONSOLIDATED STATEMENT OF INCOME (CONTINUED)  
(UNAUDITED)

The unaudited pro forma condensed financial data set forth below give effect to (i) the acquisition by NRG of a 25.37% equity interest in Loy Yang A and the financing thereof and (ii) the offering of the Old Notes (the "Offering"). The pro forma statement of income data for the year ended December 31, 1996 and the nine months ended September 30, 1997 give effect to such transactions as if they had occurred on January 1, 1996. As the Loy Yang acquisition and the Offering were consummated prior to September 30, 1997, no pro forma balance sheet data is provided. The pro forma condensed financial data do not purport to be indicative of the combined financial position or results of operations of future periods or indicative of the results that would have occurred had the transactions referred to above been consummated on the dates indicated. The following data should be read in conjunction with, and are qualified in their entirety by, the Consolidated Financial Statements and "Management's Discussion and Analysis of Financial Condition and Results of Operations" included elsewhere in this Prospectus.

	YEAR ENDED DECEMBER 31, 1996	ADJUSTMENTS (1)	PRO FORMA YEAR ENDED DECEMBER 31, 1996
-----			
(THOUSANDS OF DOLLARS)			
Operating Revenues:			
Revenues from wholly-owned operations .....	\$ 71,649	\$ --	\$ 71,649
Equity in operating earnings (losses) of unconsolidated affiliates .....	32,815	(18,121)	14,694
-----			
Total operating revenues .....	104,464	(18,121)	86,343
-----			
Operating Costs and Expenses:			
Cost of operations--wholly-owned operations	36,562	--	36,562
Depreciation and amortization .....	8,378	--	8,378
General, administrative, and development ...	39,248	--	39,248
-----			
Total operating costs and expenses .....	84,188		84,188
-----			
Operating Income .....	20,276	(18,121)	2,155
-----			

Other Income (Expense):			
Other income, net .....	9,477	26,264 (2)	35,741
Interest expense .....	(15,430)	(18,750) (3)	(34,180)
	-----	-----	-----
Total other income (expense) .....	(5,953)	(18,750)	(24,703)
	-----	-----	-----
Income (loss) before Income Taxes .....	14,323	(10,607)	3,716
	-----	-----	-----
Income Taxes .....	5,655	4,373 (4)	10,028
	-----	-----	-----
Net Income (loss) .....	\$ 19,978	\$ (6,234)	\$ 13,744
	=====	=====	=====

- 
- (1) Adjustments were derived from Loy Yang's audited financial statements for the fiscal years ended June 30, 1996 and June 30, 1997 to conform with NRG's December 31, 1996 year-end.
  - (2) Includes interest income and operating and maintenance fees derived from the Loy Yang project.
  - (3) Represents accrued interest on \$250 million principal amount of the Old Notes for twelve months at a rate of 7.5% per annum.
  - (4) Net tax benefit derived from interest expense on the Old Notes.

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NRG ENERGY, INC. AND SUBSIDIARIES  
UNAUDITED PRO FORMA CONSOLIDATED STATEMENT OF INCOME (CONTINUED)  
(UNAUDITED)

	NINE MONTHS ENDED SEPTEMBER 30, 1997	ADJUSTMENTS (1)	PRO FORMA NINE MONTHS ENDED SEPTEMBER 30, 1997
	-----		
	(THOUSANDS OF DOLLARS)		
-----			
Operating Revenues:			
Revenues from wholly-owned operations .....	\$ 65,081	\$ --	\$ 65,081
Equity in operating earnings of unconsolidated affiliates .....	17,759	(7,945) (2)	9,814
	-----	-----	-----
Total operating revenues .....	82,840	(7,945)	74,895
-----			
Operating Costs and Expenses .....			
Cost of operations--wholly-owned operations .	32,863	--	32,863
Depreciation and amortization .....	7,096	--	7,096
General, administrative, and development ....	28,402	--	28,402
	-----	-----	-----
Total operating costs and expenses .....	68,361	--	68,361
-----			
Operating Income .....	14,479	(7,945)	6,534
-----			
Other Income (Expense).....			
Other income, net .....	8,610	8,525 (3)	17,135
Interest expense .....	(19,815)	(6,883) (4)	(26,698)
	-----	-----	-----
Total other income (expense) .....	(11,205)	1,642	(9,563)
-----			
Income (loss) before Income Taxes .....	3,274	(6,303)	(3,029)
-----			
Income Taxes .....	11,140	1,605 (5)	12,745
-----			
Net Income .....	\$ 14,414	\$ (4,698)	\$ 9,716
	=====	=====	=====

- 
- (1) Adjustments were derived from Loy Yang's audited financial statements for the fiscal year ended June 30, 1997.
  - (2) Represents estimated equity earnings from Loy Yang project until May

12, 1997 based upon historical data (January 1, 1997-May 12, 1997) adjusted for differences due to acquisition accounting primarily depreciation charges, finance charges and adjustments to income tax expense. Equity earnings of Loy Yang A from May 13 until September 30 were \$1,393. This amount is summarized in the Historical column of Equity in earnings of unconsolidated affiliates.

- (3) Includes interest income and operating and maintenance fees derived from the Loy Yang project.
- (4) Represents accrued interest on \$250 million principal amount of the Old Notes until May 12 at a rate of 7.5% per annum. Interest of \$7,140 on the Old Notes from May 13 until September 30 is in the Historical column.
- (5) Net tax benefit derived from expense on the Old Notes.

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TO THE SHAREHOLDERS OF SUNSHINE STATE POWER BV

AUDITORS' REPORT

We have audited the accompanying balance sheet of Sunshine State Power BV as of December 31, 1996, 1995 and 1994, and the related statements of income and of cash flows for each of the years in the three year period ended December 31, 1996. 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 auditing standards generally accepted in the United States of America. 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 give a true and fair view of the financial position of the company as of December 31, 1996, 1995 and 1994 and of the results for the years then ended in accordance with accounting principles generally accepted in the Netherlands and comply with the financial reporting requirements included in Part 9, Book 2 of the Netherlands Civil Code.

PRICE WATERHOUSE NEDERLAND BV  
 March 21, 1997  
 Amsterdam, Netherlands

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SUNSHINE STATE POWER BV  
 BALANCE SHEET AT DECEMBER 31, 1996, 1995 AND 1994  
 (BEFORE APPROPRIATION OF THE RESULT FOR THE YEAR)  
 (AMOUNTS EXPRESSED IN THOUSANDS OF AUSTRALIAN DOLLARS)

	1996	1995	1994
	AUD'000	AUD'000	AUD'000
	-----	-----	-----
<b>ASSETS</b>			
<b>FIXED ASSETS</b>			
Intangible fixed assets .....	8,397	8,868	9,338
Tangible fixed assets .....	165,173	161,355	153,662
	-----	-----	-----
	173,570	170,223	163,000

CURRENT ASSETS			
Stocks.....	3,536	1,851	1,845
Receivables .....	4,877	5,835	4,366
Cash and bank balances .....	11,898	11,460	10,425
	-----	-----	-----
	20,311	19,146	16,636
	-----	-----	-----
TOTAL ASSETS .....	193,881	189,369	179,636
	-----	-----	-----
SHAREHOLDERS' EQUITY AND LIABILITIES			
SHAREHOLDERS' EQUITY			
Issued share capital .....	30	30	30
Retained earnings .....	15,014	7,712	--
Result for the year.....	9,133	7,302	7,712
	-----	-----	-----
	24,177	15,044	7,742
	-----	-----	-----
Provisions .....	14,618	9,309	4,496
Long-term liabilities .....	146,817	156,097	158,814
Current liabilities .....	8,269	8,919	8,584
	-----	-----	-----
TOTAL SHAREHOLDERS' EQUITY AND LIABILITIES .....	193,881	189,369	179,636
	-----	-----	-----

The accompanying notes form an integral part of the annual accounts.

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SUNSHINE STATE POWER BV  
STATEMENT OF INCOME FOR THE YEARS ENDED DECEMBER 31, 1996, 1995 AND 1994  
(AMOUNTS EXPRESSED IN THOUSANDS OF AUSTRALIAN DOLLARS)

	1996	1995	1994
	AUD'000	AUD'000	AUD'000
	-----	-----	-----
Net turnover			
Queensland Transmission & Supply Corporation ..	31,245	33,250	23,725
Boyne Smelters Limited .....	21,548	21,378	13,544
	-----	-----	-----
TOTAL .....	52,793	54,628	37,269
Cost of turnover			
Non-fuel .....	9,179	8,163	6,803
Fuel .....	14,562	14,851	11,345
	-----	-----	-----
TOTAL .....	23,741	23,014	18,148
	-----	-----	-----
GROSS PROFIT ON TURNOVER .....	29,052	31,614	19,121
	-----	-----	-----
Operating expenses .....	1,719	3,000	741
Depreciation and amortization expense .....	6,041	5,539	3,854
	-----	-----	-----
TOTAL EXPENSES .....	7,760	8,539	4,595
	-----	-----	-----
NET PROFIT ON TURNOVER .....	21,292	23,075	14,526
	-----	-----	-----
Interest expense .....	10,233	11,100	6,518
Interest income .....	(770)	(718)	(514)
Foreign exchange (gain)/loss .....	(2,527)	744	(2,989)
Disposal of assets loss .....	86	--	--
	-----	-----	-----
NET FINANCIAL EXPENSE .....	7,022	11,126	3,015

Result from ordinary operations before taxation	14,270	11,949	11,511
Taxation .....	5,137	4,647	3,799
	-----	-----	-----
NET RESULT .....	9,133	7,302	7,712
	-----	-----	-----

The accompanying notes form an integral part of the annual accounts.

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SUNSHINE STATE POWER BV  
STATEMENT OF CASH FLOWS FOR THE YEARS ENDED DECEMBER 31, 1996, 1995 AND 1994  
(AMOUNTS EXPRESSED IN THOUSANDS OF AUSTRALIAN DOLLARS)

	1996 AUD'000	1995 AUD'000	1994 AUD'000
	-----	-----	-----
Cash flows from operating activities			
Net result .....	9,133	7,302	7,712
Adjustments to reconcile net result to net cash provided by operating activities:			
Depreciation and amortization .....	6,041	5,539	3,854
Deferred income taxes .....	5,137	4,647	3,799
Foreign exchange loss/(gain) .....	(2,527)	744	(2,989)
Loss on sale of fixed assets.....	86	--	
Changes in operating assets and liabilities:			
Stocks .....	(1,685)	(6)	484
Receivables .....	958	(1,469)	(4,338)
Provisions .....	172	166	125
Current liabilities .....	(1,088)	(102)	4,546
	-----	-----	-----
NET CASH FLOWS PROVIDED BY OPERATING ACTIVITIES	16,227	16,821	13,193
	-----	-----	-----
Cash flows from investing activities			
Purchases of tangible fixed assets .....	(9,495)	(12,762)	(306)
Proceeds from sale of fixed assets .....	21	--	--
Acquisition of 20% of the Gladstone Power Station.....	--	--	(168,332)
	-----	-----	-----
NET CASH FLOWS USED BY INVESTING ACTIVITIES ....	(9,474)	(12,762)	(168,638)
Cash flows from financing activities			
Proceeds (repayments) of notes payable .....	(1,840)	1,014	172,933
Proceeds from issuance of share capital .....			30
Repayments of long-term debt .....	(4,475)	(4,038)	(7,093)
	-----	-----	-----
NET CASH FLOWS (USED) PROVIDED BY FINANCING ACTIVITIES .....	(6,315)	(3,024)	165,870
	-----	-----	-----
NET INCREASE IN CASH AND BANK BALANCES.....	438	1,035	10,425
	-----	-----	-----
Cash and bank balances			
Beginning of year .....	11,460	10,425	--
	-----	-----	-----
End of year .....	11,898	11,460	10,425
	-----	-----	-----
SUPPLEMENTAL DISCLOSURE OF CASH PAID FOR INTEREST .....	10,382	11,043	5,617
	-----	-----	-----

The accompanying notes form an integral part of the annual accounts.

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SUNSHINE STATE POWER BV  
NOTES TO THE ANNUAL ACCOUNTS  
FOR THE YEARS ENDED DECEMBER 31, 1996, 1995 AND 1994  
(AMOUNTS EXPRESSED IN THOUSANDS OF AUSTRALIAN DOLLARS)

1. GENERAL

## ACTIVITIES

Sunshine State Power BV (the Company) was incorporated on November 11, 1993. The Company's principal operating activity is the ownership of 20% of the Gladstone Power Station Joint Venture. The Gladstone Power Station Joint Venture owns and operates the Gladstone Power Station located in Queensland, Australia which it acquired on March 30, 1994. The Gladstone Power Station Joint Venture is an unincorporated joint venture and therefore not a separate legal entity. Accordingly, the Gladstone Power Station Joint Venture owners act as tenants in common owning their proportionate shares of the unincorporated joint venture's assets, liabilities and results of operations. The accounts have been prepared for the years ended December 31, 1996, 1995 and 1994.

## 2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

### GENERAL

Unless otherwise stated assets and liabilities are carried at nominal value.

### BASIS OF PREPARATION

The Company's financial statements have been prepared in accordance with generally accepted accounting principles in the Netherlands (Netherlands GAAP) which may differ in certain respects from generally accepted accounting principles in the United States (US GAAP). With regard to the Company's balance sheet and statement of income, there are no material differences between Netherlands GAAP and US GAAP. With regard to the Company's statement of cash flows, under US GAAP the foreign exchange loss/(gain) would be classified under the cash flows from financing activities section as US GAAP requires that such items be netted with the related cash flow item.

### FOREIGN CURRENCIES

Assets and liabilities at year-end and transactions during the period denominated in a foreign currency are translated into the Company's local currency (Australian \$) at the exchange rates ruling at year-end and at the time of the transaction, respectively. Exchange adjustments are taken to the statement of income.

### INTANGIBLE FIXED ASSETS

Project Development Expenditures -Project development expenditures represent the Company's share of project development expenditures incurred by the Gladstone Power Station Joint Venture to organize the acquisition of the Gladstone Power Station and operate it subsequent to the acquisition.

Capitalized development expenditures are being amortized over the term of the Gladstone Power Station Power sales agreements (35 years), commencing from the date the investment in the project was consummated. The carrying values of capitalized development expenditures and the amortization periods are reviewed annually and any necessary write down is charged against income. Research expenditures and expenditures on development of existing projects are charged against income in the year in which they are incurred.

Financing Costs -Financing costs represent the Company's share of the costs incurred by the Gladstone Power Station Joint Venture to acquire the long-term debt used to finance the acquisition of the Gladstone Power Station. Capitalized financing costs are being amortized over a ten year period, which represents the timeframe until the Company expects the long-term debt will be refinanced.



FOR THE YEARS ENDED DECEMBER 31, 1996, 1995 AND 1994 -- (CONTINUED)

(AMOUNTS EXPRESSED IN THOUSANDS OF AUSTRALIAN DOLLARS)

TANGIBLE FIXED ASSETS

All tangible fixed assets are stated at cost. The Company has not had any revaluations performed on its tangible fixed assets. Tangible fixed assets, with the exception of land, are depreciated over their estimated useful lives or over the life of the power purchase agreement by the straight line method. Ordinary maintenance and repairs are expensed as incurred; replacements and improvements are capitalized.

The estimated useful lives are:

Site roads and preparation .....	35 years
Generators, systems, stacks, etc. .	35 years
Coal handling plant .....	10 -35 years
Other operating fixed assets .....	3 -10 years

STOCKS

Stocks are carried at the lower of cost (principally by the FIFO method or another method which approximates FIFO) and net realizable value. In valuing stocks, appropriate allowance is made for obsolete or slow-moving items.

TRADE DEBTORS

Trade debtors are stated at nominal value.

PROVISIONS

Employee Provisions -Provisions are made for amounts expected to be paid to the operator of the Gladstone Power Station in respect of its employees for the pro rata entitlements for long service and annual leave. These amounts are accrued at actual pay rates having regard to experience of employee's departure and period of service. The provisions are divided into current (expected to be paid in the ensuing twelve months) and non-current portions.

Deferred Tax -Provisions for deferred taxes have been set up where items entering into the determination of accounting profit for one period are recognized for taxation purposes in another. The principal difference arises in connection with the depreciation of fixed assets. In calculating the provision, current tax rates are applied. During 1995, Australian income tax rates increased from 33% to 36%. In 1995, the prior year deferred tax balance was increased to reflect the increase in tax rates with the adjustment being recorded in taxation in the statement of income.

COMPANY INCOME TAX

Company income tax is based upon the results reported in the statement of income as adjusted for permanent differences. Current Australian tax rates are applied.

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SUNSHINE STATE POWER BV  
NOTES TO THE ANNUAL ACCOUNTS

FOR THE YEARS ENDED DECEMBER 31, 1996, 1995 AND 1994 -- (CONTINUED)

(AMOUNTS EXPRESSED IN THOUSANDS OF AUSTRALIAN DOLLARS)

3. INTANGIBLE FIXED ASSETS

The movements in the intangible fixed assets are summarized as follows:

	PROJECT DEVELOPMENT EXPENDITURES AUD'000	FINANCING COSTS AUD'000	TOTAL AUD'000
COST			
Balance at December 31, 1993 .....	--	--	--
Company's share of fixed assets acquired with the Gladstone Power Station acquisition .....	6,984	2,707	9,691
Balance at December 31, 1994 .....	6,984	2,707	9,691
Additions for the year ended December 31, 1995 .....	--	--	--
Balance at December 31, 1995 .....	6,984	2,707	9,691
Additions for the year ended December 31, 1996 .....	--	--	--
Balance at December 31, 1996 .....	6,984	2,707	9,691
ACCUMULATED AMORTIZATION			
Balance at December 31, 1993 .....	--	--	--
Amortization for the year ended December 31, 1994 .....	(150)	(203)	(353)
Amortization for the year ended December 31, 1995 .....	(199)	(271)	(470)
Amortization for the year ended December 31, 1996 .....	(200)	(271)	(471)
Balance at December 31, 1996 .....	(549)	(745)	(1,294)
Net book value at December 31, 1996 .....	6,435	1,962	8,397

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SUNSHINE STATE POWER BV  
NOTES TO THE ANNUAL ACCOUNTS  
FOR THE YEARS ENDED DECEMBER 31, 1996, 1995 AND 1994 -- (CONTINUED)  
(AMOUNTS EXPRESSED IN THOUSANDS OF AUSTRALIAN DOLLARS)

4. TANGIBLE FIXED ASSETS

The movements in the tangible fixed assets are summarized as follows:

	LAND AUD'000	SITE ROADS AND PREPARATION AUD'000	GENERATORS, SYSTEMS, STACKS AUD'000	COAL HANDING PLANT AUD'000	OTHER OPERATING FIXED ASSETS AUD'000	TOTAL AUD'000
COST						
Balance at November 11, 1993 .....	--	--	--	--	--	--
Company's share of assets acquired with Gladstone Power Station acquisition ..	211	2,443	141,118	6,294	1,613	151,679
Additions .....	--	--	7	--	299	306
Balance at December 31, 1994 .....	211	2,443	141,125	6,294	1,912	151,985
Additions .....	--	146	8,943	2,036	721	11,846
Disposals .....	--	--	(1)	--	(10)	(11)
Balance at December 31, 1995 .....	211	2,589	150,067	8,330	2,623	163,820
Additions .....	5	209	11,988	1,334	111	13,647
Disposals .....	--	--	(88)	--	(19)	(107)
Balance at December 31, 1996 .....	216	2,798	161,967	9,664	2,715	177,360
ACCUMULATED DEPRECIATION						
Balance at November 11, 1993 .....	--	--	--	--	--	--
Charge for the period .....	--	(53)	(2,940)	(331)	(177)	(3,501)
Balance at December 31, 1994 .....	--	(53)	(2,940)	(331)	(177)	(3,501)
Charge for the year .....	--	(72)	(4,304)	(452)	(353)	(5,181)
Balance at December 31, 1995 .....	--	(125)	(7,244)	(783)	(530)	(8,682)
Charge for the year .....	--	(79)	(4,497)	(601)	(393)	(5,570)
Balance at December 31, 1996 .....	--	(204)	(11,741)	(1,384)	(923)	(14,252)
Net book value at December 31, 1996 ...	216	2,594	150,226	8,280	1,792	163,108
Construction in progress at December 31, 1996 (construction in progress at December 31, 1995 and 1994 was \$6,217 and \$5,178, respectively) .						2,065
Net tangible fixed assets at December 31, 1996 .....						165,173

5. STOCKS

	DECEMBER 31, 1996	DECEMBER 31, 1995	DECEMBER 31, 1994
	AUD'000	AUD'000	AUD'000
Coal .....	2,318	656	774
Fuel oils .....	154	202	120
Chemicals .....	12	13	26
Spares and consumables	1,052	980	925
	3,536	1,851	1,845

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SUNSHINE STATE POWER BV  
NOTES TO THE ANNUAL ACCOUNTS

FOR THE YEARS ENDED DECEMBER 31, 1996, 1995 AND 1994 -- (CONTINUED)  
(AMOUNTS EXPRESSED IN THOUSANDS OF AUSTRALIAN DOLLARS)

6. RECEIVABLES

	DECEMBER 31, 1996	DECEMBER 31, 1995	DECEMBER 31, 1994
	AUD'000	AUD'000	AUD'000
Trade debtors	4,605	5,501	4,003
Prepayments ..	272	334	363
	4,877	5,835	4,366

All receivables are due in less than one year.

7. CASH AND BANK BALANCES

All cash and bank balances are held by banks and include investments with maturities of three months or less which are readily convertible to cash. The Company's long-term debt agreement places restrictions on the amount of cash and bank balances which must be maintained. At December 31, 1996, 1995 and 1994, the restricted cash and bank balances totaled \$7,000,000, \$7,500,000 and \$6,300,000, respectively.

8. ISSUED SHARE CAPITAL

The authorized share capital consists of 2 000 shares each having a nominal value of 30 Australian dollars (40 Dutch Guilders), of which 1 000 shares have been issued and fully paid up at December 31, 1996 and 1995. The Company's shares are owned by NRGenerating International BV (990) and Gunwale BV (10). Both NRGenerating International BV and Gunwale BV are wholly owned by NRG Energy, Inc., which is incorporated in the United States of America.

9. RETAINED EARNINGS

	1996	1995
	-----	-----
	AUD'000	AUD'000
Balance at January 1 .....	7,712	--
Appropriation of prior years result	7,302	7,712
	-----	-----
Balance at December 31 .....	15,014	7,712
	-----	-----

10. RESULT FOR THE PERIOD

	AUD'000
Balance at November 11, 1993 .....	--
Net result for the period ended December 31, 1994	7,712
1994 net result appropriated to retained earnings	(7,712)
Net result for the year ended December 31, 1995 ..	7,302
1995 net result appropriated to retained earnings	(7,302)
Net result for the year ended December 31, 1996 ..	9,133
	-----
Balance at December 31, 1996 .....	9,133
	-----

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SUNSHINE STATE POWER BV  
NOTES TO THE ANNUAL ACCOUNTS

FOR THE YEARS ENDED DECEMBER 31, 1996, 1995 AND 1994 -- (CONTINUED)  
(AMOUNTS EXPRESSED IN THOUSANDS OF AUSTRALIAN DOLLARS)

11. PROVISIONS

	EMPLOYEE PROVISIONS	DEFERRED TAX	TOTAL
	-----	-----	-----
	AUD'000	AUD'000	AUD'000
Balance at November 11, 1993 .....	--	--	--
Company's share assumed with the Gladstone Power Station acquisition	572	--	572
Charged/(released) to income .....	125	3,799	3,924
	-----	-----	-----
Balance at December 31, 1994 .....	697	3,799	4,496
Charged/(released) to income .....	166	4,647	4,813
	-----	-----	-----
Balance at December 31, 1995 .....	863	8,446	9,309
Charged/(released) to income .....	172	5,137	5,309
	-----	-----	-----
Balance at December 31, 1996 .....	1,035	13,583	14,618
	-----	-----	-----

Approximately \$ 618 (AUD'000) of the employee provisions are current and expected to be paid during 1997.

12. LONG-TERM LIABILITIES

Secured long-term debt due to third parties

	DECEMBER 31, 1996	DECEMBER 31, 1995	DECEMBER 31, 1994
	----- AUD'000	----- AUD'000	----- AUD'000
Secured -with banks .	108,821	113,733	118,208
	-----	-----	-----

Current installments of bank long-term debt are included under current liabilities. The interest rate for long-term debt is variable based on an average of the bid rates quoted by the banks plus a margin of 1.4% at December 31, 1996.

The bank long-term debt is repayable as follows (in AUD'000):

1997 .....	4,913
1998 .....	5,437
1999 .....	5,975
2000 .....	6,600
2001 .....	7,275
Thereafter .....	83,534
	-----
	113,734
	-----

The bank long-term debt is secured by the Company's ownership interest in the Gladstone Power Station Joint Venture.

Unsecured Subordinated Notes Payable (AUD'000)

On March 25, 1994 the Company received loans from NRGenerating International BV and Gunwale BV, the primary shareholders of the Company, in the amounts of \$ 48,312 and \$488 respectively. The notes payable are subordinated to all other liabilities of the Company, bear no interest and are to be repaid in U.S. dollars. During 1996, the Company repaid \$1,822 and \$18 to NRGenerating International BV and Gunwale BV, respectively. There were no repayments made during 1995. During 1994, the Company repaid \$5,152 and \$53 to NRGenerating International BV and Gunwale BV, respectively.

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SUNSHINE STATE POWER BV  
NOTES TO THE ANNUAL ACCOUNTS  
FOR THE YEARS ENDED DECEMBER 31, 1996, 1995 AND 1994 -- (CONTINUED)  
(AMOUNTS EXPRESSED IN THOUSANDS OF AUSTRALIAN DOLLARS)

Repayments on the notes payable are at the discretion of the Company, unless certain events of termination occur, as defined, and then the entire balance of the notes becomes due. The note balances, as adjusted for current period activity and foreign exchange fluctuations, were \$37,616 and \$380 to NRGenerating International BV and Gunwale BV at December 31, 1996, respectively and \$41,940 and \$424 to NRGenerating International BV and Gunwale BV at December 31, 1995, respectively.

13. CURRENT LIABILITIES

DECEMBER 31, 1996	DECEMBER 31, 1995	DECEMBER 31, 1994
----------------------	----------------------	----------------------

	AUD'000	AUD'000	AUD'000
Current installments of bank long-term debt	4,913	4,475	4,038
Trade creditors/suppliers .....	776	1,579	1,370
Accrued coal/rail costs .....	1,152	1,712	1,984
Accrued interest .....	800	959	901
Other accrued expenses .....	628	194	291
	8,269	8,919	8,584

#### 14. RELATED PARTIES

An affiliate of the Company, Sunshine State Power (No. 2) BV owns 17.5% of the Gladstone Power Station Joint Venture. Sunshine State Power (No. 2) BV is owned by the owners of the Company.

The Gladstone Power Station is operated by NRG Gladstone Operating Services Ply Ltd, which is ultimately a wholly-owned subsidiary of NRG Energy Inc. NRG Gladstone Operating Services Ply Ltd operates the Gladstone Power Station under the terms of the Operation and Maintenance Agreement with the Gladstone Power Station Joint Venture. During the periods ended December 31, 1996, 1995 and 1994, the Company paid NRG Gladstone Operating Services Pty Ltd approximately \$288, \$331 and \$194 (AUD'000) respectively in operators fees under the terms of the Operation and Maintenance Agreement.

#### 15. NUMBER OF EMPLOYEES

The average number of persons employed at the Gladstone Power Station during 1996 was approximately 471. These individuals are primarily employed in the operations and maintenance areas of the station. The Company is responsible for 20% of the related costs for these employees. The Company itself has no employees.

#### 16. REMUNERATION OF DIRECTORS

During the periods ended December 31, 1996, 1995 and 1994, none of the directors received remuneration for their services as directors of the Company.

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#### TO THE SHAREHOLDERS OF SUNSHINE STATE POWER (NO. 2) BV AUDITORS' REPORT

We have audited the accompanying balance sheet of Sunshine State Power (No. 2) BV as of December 31, 1996, 1995 and 1994, and the related statements of income and of cash flows for each of the years in the three year period ended December 31, 1996. 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 auditing standards generally accepted in the United States of America. 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 give a true and fair view of the financial position of the company as of December 31, 1996, 1995 and 1994 and of the results for the years then ended in accordance with accounting principles generally accepted in the Netherlands and comply with the financial reporting requirements included in Part 9, Book 2 of the Netherlands Civil Code.

PRICE WATERHOUSE NEDERLAND BV  
 March 21, 1997  
 Amsterdam, Netherlands

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SUNSHINE STATE POWER (NO. 2) BV  
 BALANCE SHEET AT DECEMBER 31, 1996, 1995 AND 1994  
 (BEFORE APPROPRIATION OF THE RESULT FOR THE YEAR)  
 (AMOUNTS EXPRESSED IN THOUSANDS OF AUSTRALIAN DOLLARS)

	1996 AUD'000	1995 AUD'000	1994 AUD'000
	-----	-----	-----
ASSETS			
FIXED ASSETS			
Intangible fixed assets .....	7,348	7,759	8,171
Tangible fixed assets.....	144,524	141,183	134,452
	-----	-----	-----
	151,872	148,942	142,623
CURRENT ASSETS			
Stocks .....	3,093	1,620	1,614
Receivables .....	4,267	5,106	3,869
Cash and bank balances .....	10,416	9,953	9,055
	-----	-----	-----
	17,776	16,679	14,538
	-----	-----	-----
TOTAL ASSETS .....	169,648	165,621	157,161
SHAREHOLDERS' EQUITY AND LIABILITIES			
SHAREHOLDERS' EQUITY			
Issued share capital .....	30	30	30
Retained earnings .....	13,158	6,748	--
Result for the year .....	7,950	6,410	6,748
	-----	-----	-----
	21,138	13,188	6,778
	-----	-----	-----
Provisions .....	12,779	8,155	3,933
Long-term liabilities .....	128,472	136,515	138,939
Current liabilities .....	7,259	7,763	7,511
	-----	-----	-----
TOTAL SHAREHOLDERS' EQUITY AND LIABILITIES .....	169,648	165,621	157,161
	=====	=====	=====

The accompanying notes form an integral part of the annual accounts.

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SUNSHINE STATE POWER (NO. 2) BV  
 STATEMENT OF INCOME FOR THE YEARS ENDED DECEMBER 31, 1996 AND 1995  
 AND PERIOD ENDED DECEMBER 31, 1994  
 (AMOUNTS EXPRESSED IN THOUSANDS OF AUSTRALIAN DOLLARS)

	1996 AUD'000	1995 AUD'000	1994 AUD'000
	-----	-----	-----

Net turnover

Queensland Electricity Commission .....	27,340	29,094	20,759
Boyne Smelters Limited .....	18,854	18,706	11,851
TOTAL .....	46,194	47,800	32,610
Cost of turnover			
Non-fuel .....	8,031	7,143	5,953
Fuel .....	12,742	12,995	9,926
TOTAL .....	20,773	20,138	15,879
GROSS PROFIT ON TURNOVER .....	25,421	27,662	16,731
Operating expenses .....	1,509	2,632	646
Depreciation and amortization expense .....	5,285	4,846	3,373
TOTAL EXPENSES .....	6,794	7,478	4,019
NET PROFIT ON TURNOVER .....	18,627	20,184	12,712
Interest expense .....	8,954	9,713	5,704
Interest income .....	(668)	(626)	(449)
Foreign exchange (gain)/loss .....	(2,157)	609	(2,614)
Disposal of assets loss .....	76	--	--
NET FINANCIAL EXPENSE .....	6,205	9,696	2,641
Result from ordinary operations before taxation	12,422	10,488	10,071
Taxation .....	4,472	4,078	3,323
NET RESULT .....	7,950	6,410	6,748

The accompanying notes form an integral part of the annual accounts.

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SUNSHINE STATE POWER (NO. 2) BV

STATEMENT OF CASH FLOWS FOR THE YEARS ENDED DECEMBER 31, 1996 AND 1995  
AND PERIOD ENDED DECEMBER 31, 1994  
(AMOUNTS EXPRESSED IN THOUSANDS OF AUSTRALIAN DOLLARS)

	1996 AUD'000	1995 AUD'000	1994 AUD'000
Cash flows from operating activities			
Net result .....	7,950	6,410	6,748
Adjustments to reconcile net result to net cash provided by operating activities:			
Depreciation and amortization .....	5,285	4,846	3,373
Deferred income taxes .....	4,472	4,078	3,323
Foreign exchange loss/(gain) .....	(2,157)	609	(2,614)
Loss on sale of fixed assets.....	76	--	--
Changes in operating assets and liabilities:			
Stocks .....	(1,473)	(6)	423
Receivables .....	839	(1,237)	(3,845)
Provisions .....	152	144	110
Current liabilities .....	(886)	(131)	3,978
NET CASH FLOWS PROVIDED BY OPERATING ACTIVITIES .....	14,258	14,713	11,496
Cash flows from investing activities:			
Purchases of tangible fixed assets .....	(8,308)	(11,165)	(268)
Proceeds from sale of fixed assets .....	17	--	--
Acquisition of 20% of the Gladstone Power Station .....	--	--	(147,288)
NET CASH FLOWS USED BY INVESTING ACTIVITIES.....	(8,291)	(11,165)	(147,556)
Cash flows from financing activities:			
Proceeds (repayments) of notes payable .....	(1,588)	883	151,316



Proceeds from issuance of share capital .....			30
Repayments of long-term debt .....	(3,916)	(3,533)	(6,231)
NET CASH FLOWS (USED) BY FINANCING ACTIVITIES .....	(5,504)	(2,650)	145,115
NET INCREASE IN CASH AND BANK BALANCES .....	463	898	9,055
Cash and bank balances			
Beginning of year .....	9,953	9,055	--
End of year .....	10,416	9,953	9,055
SUPPLEMENTAL DISCLOSURE OF CASH PAID FOR INTEREST .....	9,084	9,667	4,916

The accompanying notes form an integral part of the annual accounts.

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SUNSHINE STATE POWER (NO. 2) BV

NOTES TO THE ANNUAL ACCOUNTS FOR THE YEARS ENDED DECEMBER 31, 1996  
AND 1995 AND PERIOD ENDED DECEMBER 31, 1994  
(AMOUNTS EXPRESSED IN THOUSANDS OF AUSTRALIAN DOLLARS)

1. GENERAL

ACTIVITIES

Sunshine State Power (No. 2) BV (the Company) was incorporated on February 24, 1994. The Company's principal operating activity is the ownership of 17.5% of the Gladstone Power Station Joint Venture. The Gladstone Power Station Joint Venture owns and operates the Gladstone Power Station located in Queensland, Australia, which it acquired on March 30, 1994. The Gladstone Power Station Joint Venture is an unincorporated joint venture and therefore not a separate legal entity. Accordingly, the Gladstone Power Station Joint Venture owners act as tenants in common owning their proportionate shares of the unincorporated joint venture's assets, liabilities and results of operations. The accounts have been prepared for the years ended December 31, 1996 and 1995 and period ended December 31, 1994.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

GENERAL

Unless otherwise stated assets and liabilities are carried at nominal value.

BASIS OF PREPARATION

The Company's financial statements have been prepared in accordance with generally accepted accounting principles in the Netherlands (Netherlands GAAP) which may differ in certain respects from generally accepted accounting principles in the United States (US GAAP). With regard to the Company's balance sheet and statement of income, there are no material differences between Netherlands GAAP and US GAAP. With regard to the Company's statement of cash flows, under US GAAP the foreign exchange loss/(gain) would be classified under the cash flows from financing activities section as US GAAP requires that such items be netted with the related cash flow item.

FOREIGN CURRENCIES

Assets and liabilities at year-end and transactions during the period denominated in a foreign currency are translated into the Company's local currency (Australian \$) at the exchange rates ruling at year-end and at the time of the transaction, respectively. Exchange adjustments are taken to the statement of income.

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Project development expenditures -Project development expenditures represent the Company's share of project development expenditures incurred by the Gladstone Power Station Joint Venture to organize the acquisition of the Gladstone Power Station and operate it subsequent to the acquisition.

Capitalized development expenditures are being amortized over the term of the Gladstone Power Station Power sales agreements (35 years), commencing from the date the investment in the project was consummated. The carrying values of capitalized development expenditures and the amortization periods are reviewed annually and any necessary write down is charged against income. Research expenditures and expenditures on development of existing projects are charged against income in the year in which they are incurred.

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SUNSHINE STATE POWER (NO. 2) BV

NOTES TO THE ANNUAL ACCOUNTS FOR THE YEARS ENDED DECEMBER 31, 1996  
AND 1995 AND PERIOD ENDED DECEMBER 31, 1994 -- (CONTINUED)

Financing costs -Financing costs represent the Company's share of the costs incurred by the Gladstone Power Station Joint Venture to acquire the long-term debt used to finance the acquisition of the Gladstone Power Station. Capitalized financing costs are being amortized over a ten year period, which represents the timeframe until the Company expects the long-term debt will be refinanced.

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All tangible fixed assets are stated at cost. The Company has not had any revaluations performed on its tangible fixed assets. Tangible fixed assets, with the exception of land, are depreciated over their estimated useful lives by the straight line method. Ordinary maintenance and repairs are expensed as incurred; replacements and improvements are capitalized.

The estimated useful lives are:

Site roads and preparation .....	35 years
Generators, systems, stacks, etc. ....	35 years
Coal handling plant .....	10 -35 years
Other operating fixed assets .....	3 -10 years

STOCKS

Stocks are carried at the lower of cost (principally by the FIFO method or another method which approximates FIFO) and net realizable value. In valuing stocks, appropriate allowance is made for obsolete or slow-moving items.

TRADE DEBTORS

Trade debtors are stated at nominal value.

PROVISIONS

Employee provisions -Provisions are made for amounts expected to be paid to the operator of the Gladstone Power Station in respect of its employees for the pro rata entitlements for long service and annual leave. These amounts are accrued at actual pay rates having regard to experience of employee's departure and period of service. The provisions are divided into current (expected to be paid in the ensuing twelve months) and non-current portions.

Deferred tax -Provisions for deferred taxes have been set up where items entering into the determination of accounting profit for one period are recognized for taxation purposes in another. The principal difference arises in connection with the depreciation of fixed assets. In calculating the provision, current tax rates are applied. During 1995 Australian income tax rates increased from 33% to 36%. In 1995 the prior year deferred tax balance was increased to reflect the increase in tax rates with the adjustment being recorded in taxation in the statement of income.

COMPANY INCOME TAX

Company income tax is based upon the results reported in the statement of income as adjusted for permanent differences. Current Australian tax rates are applied.

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SUNSHINE STATE POWER (NO. 2) BV  
 NOTES TO THE ANNUAL ACCOUNTS FOR THE YEARS ENDED DECEMBER 31, 1996  
 AND 1995 AND PERIOD ENDED DECEMBER 31, 1994 -- (CONTINUED)

3. INTANGIBLE FIXED ASSETS

The movements in the intangible fixed assets are summarized as follows:

	PROJECT DEVELOPMENT EXPENDITURES	FINANCING COSTS	TOTAL
	AUD'000	AUD'000	AUD'000
<b>COST</b>			
Balance at February 24, 1994 .....	--	--	--
Company's share of fixed assets acquired with Gladstone Power Station acquisition .....	6,111	2,369	8,480
Balance at December 31, 1994 .....	6,111	2,369	8,480
Additions for the year ended December 31, 1995 ...	--	--	--
Balance at December 31, 1995 .....	6,111	2,369	8,480
Additions for the year ended December 31, 1996 ...	--	--	--
Balance at December 31, 1996 .....	6,111	2,369	8,480
<b>ACCUMULATED AMORTIZATION</b>			
Balance at February 24, 1994.....	--	--	--
Amortization for the period ended December 31, 1994 .....	(131)	(178)	(309)
Amortization for the year ended December 31, 1995	(175)	(237)	(412)
Amortization for the year ended December 31, 1996	(174)	(237)	(411)
Balance at December 31, 1996 .....	(480)	(652)	(1,132)
Net book value at December 31, 1996 .....	5,631	1,717	7,348

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SUNSHINE STATE POWER (NO. 2) BV  
 NOTES TO THE ANNUAL ACCOUNTS FOR THE YEARS ENDED DECEMBER 31, 1996  
 AND 1995 AND PERIOD ENDED DECEMBER 31, 1994 -- (CONTINUED)

4. TANGIBLE FIXED ASSETS

The movements in the tangible fixed assets are summarized as follows:

OTHER

	LAND	SITE ROADS AND PREPARATION	GENERATORS, SYSTEMS, STACKS	COAL HANDLING PLANT	OPERATING FIXED ASSETS	TOTAL
	AUD'000	AUD'000	AUD'000	AUD'000	AUD'000	AUD'000
COST						
Balance at February 24, 1994 .....	--	--	--	--	--	--
Company's share of assets acquired with Gladstone Power Station acquisition .....	184	2,138	123,476	5,508	1,411	132,717
Other additions .....	--	--	6	--	262	268
Balance at December 31, 1994 .....	184	2,138	123,482	5,508	1,673	132,985
Additions .....	--	128	7,827	1,781	631	10,367
Disposals .....	--	--	(1)	--	(9)	(10)
Balance at December 31, 1995 .....	184	2,266	131,308	7,289	2,295	143,342
Additions .....	5	182	10,489	1,168	97	11,941
Disposals .....	--	--	(77)	--	(16)	(93)
Balance at December 31, 1996 .....	189	2,448	141,720	8,457	2,376	155,190
ACCUMULATED DEPRECIATION						
Balance at February 24, 1994 .....	--	--	--	--	--	--
Charge for the period .....	--	(46)	(2,571)	(292)	(155)	(3,064)
Balance at December 31, 1994 .....	--	(46)	(2,571)	(292)	(155)	(3,064)
Charge for the year .....	--	(63)	(3,767)	(396)	(309)	(4,535)
Balance at December 31, 1995 .....	--	(109)	(6,338)	(688)	(464)	(7,599)
Charge for the year .....	--	(69)	(3,935)	(526)	(344)	(4,874)
Balance at December 31, 1996 .....	--	(178)	(10,273)	(1,214)	(808)	(12,473)
Net book value at December 31, 1996 .....	189	2,270	131,447	7,243	1,568	142,717
Construction in progress at December 31, 1996 (construction in progress at December 31, 1995 and 1994 was \$5,440 and \$4,531, respectively) .....	--	--	--	--	--	1,807
Net tangible fixed assets at December 31, 1996 .....	--	--	--	--	--	144,524

## 5. STOCKS

	DECEMBER 31, 1996	DECEMBER 31, 1995	DECEMBER 31, 1994
	AUD'000	AUD'000	AUD'000
Coal .....	2,028	574	678
Fuel oils .....	135	177	105
Chemicals .....	10	11	23
Spares and consumables .....	920	858	808
	3,093	1,620	1,614

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## SUNSHINE STATE POWER (NO. 2) BV

NOTES TO THE ANNUAL ACCOUNTS FOR THE YEARS ENDED DECEMBER 31, 1996  
AND 1995 AND PERIOD ENDED DECEMBER 31, 1994 -- (CONTINUED)

## 6. RECEIVABLES

	DECEMBER 31, 1996	DECEMBER 31, 1995	DECEMBER 31, 1994
	AUD'000	AUD'000	AUD'000
Trade debtors .....	4,030	4,814	3,503
Prepayments ..	237	292	366

4,267	5,106	3,869
-----	-----	-----

All receivables are due in less than one year.

7. CASH AND BANK BALANCES

All cash and bank balances are held by banks and include investments with maturities of three months or less which are readily convertible to cash. The Company's long-term debt agreement places restrictions on the amount of cash and bank balances which must be maintained. At December 31, 1996, 1995 and 1994, the restricted cash and bank balances totaled \$6,100,000, \$6,500,000 and \$5,500,000, respectively.

8. ISSUED SHARE CAPITAL

The authorized share capital consists of 2,000 shares each having a nominal value of 75 Australian dollars (100 Dutch Guilders), of which 400 shares have been issued and fully paid up at December 31, 1996 and 1995. The Company's shares are owned by NRGenerating International BV (396) and Gunwale BV (4). Both NRGenerating International BV and Gunwale BV are wholly owned by NRG Energy, Inc., which is incorporated in the United States of America.

9. RETAINED EARNINGS

	1996	1995
	-----	-----
	AUD'000	AUD'000
Balance at January 1 .....	6,748	--
Appropriation of prior years result	6,410	6,748
	-----	-----
Balance at December 31 .....	13,158	6,748
	-----	-----

10. RESULT FOR THE PERIOD

	AUD'000
	-----
Balance at February 24, 1994 .....	--
Net result for the period ended December 31, 1994	6,748
1994 net result appropriated to retained earnings	(6,748)
Net result for the year ended December 31, 1995 ..	6,410
1995 net result appropriated to retained earnings	(6,410)
Net result for the year ended December 31, 1996 ..	7,950
	-----
Balance at December 31, 1996 .....	7,950
	-----

11. PROVISIONS

	EMPLOYEE PROVISIONS	DEFERRED TAX	TOTAL
	AUD'000	AUD'000	AUD'000
Balance at February 24, 1994 .....	--	--	--
Company's share assumed with the Gladstone Power Station acquisition .....	500	--	500
Charged/(released) to income .....	110	3,323	3,433
Balance at December 31, 1994 .....	610	3,323	3,933
Charged/(released) to income .....	144	4,078	4,222
Balance at December 31, 1995 .....	754	7,401	8,155
Charged/(released) to income .....	152	4,472	4,624
Balance at December 31, 1996 .....	906	11,873	12,779

Approximately \$541 (AUD'000) of the employee provisions are current and expected to be paid during 1997.

## 12. LONG-TERM LIABILITIES

Secured long-term debt due to third parties

	DECEMBER 31, 1996	DECEMBER 31, 1995	DECEMBER 31, 1994
	AUD'000	AUD'000	AUD'000
Secured--with banks .	95,218	99,516	103,432

Current installments of bank long-term debt are included under current liabilities. The interest rate for long-term debt is variable based on an average of the bid rates quoted by the banks plus a margin of 1.4% at December 31, 1996.

The bank long-term debt is repayable as follows (in AUD'000):

1997 .....	4,298
1998 .....	4,758
1999 .....	5,228
2000 .....	5,775
2001 .....	6,366
Thereafter .....	73,091
	-----
	99,516
	-----

The bank long-term debt is secured by the Company's ownership interest in the Gladstone Power Station Joint Venture.

Unsecured subordinated note payable (AUD'000)

On March 25, 1994 the Company received loans from NRGenerating International BV and Gunwale BV, the primary shareholders of the Company, in the amount of \$42,273 and \$427, respectively. The notes payable are subordinated to all other liabilities of the Company, bear no interest and

are to be repaid in US dollars. During 1996, the Company repaid \$1,572 and \$16 to NRGenerating International BV and Gunwale BV, respectively. There were no repayments made during 1995. During 1994, the

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SUNSHINE STATE POWER (NO. 2) BV

NOTES TO THE ANNUAL ACCOUNTS FOR THE YEARS ENDED DECEMBER 31, 1996  
AND 1995 AND PERIOD ENDED DECEMBER 31, 1994 -- (CONTINUED)

Company repaid \$4,533 and \$46 to NRGenerating International BV and Gunwale BV, respectively. Repayments on the notes payable are at the discretion of the Company, unless certain events of termination occur, as defined, and then the entire balance of the notes becomes due. The note balances, as adjusted for current period activity and foreign exchange fluctuations, were \$32,922 and \$332 to NRGenerating International BV and Gunwale BV at December 31, 1996 respectively and \$36,629 and \$370 to NRGenerating International BV and Gunwale BV at December 31, 1995, respectively.

13. CURRENT LIABILITIES

	DECEMBER 31, 1996	DECEMBER 31, 1995	DECEMBER 31, 1994
	AUD'000	AUD'000	AUD'000
Current installments of bank long-term debt	4,298	3,916	3,533
Trade creditors/suppliers .....	696	1,345	1,199
Accrued coal/rail costs .....	1,008	1,498	1,736
Accrued interest .....	700	834	788
Other accrued expenses .....	557	170	255
	7,259	7,763	7,511

14. RELATED PARTIES

An affiliate of the Company, Sunshine State Power BV owns 20% of the Gladstone Power Station Joint Venture. Sunshine State Power BV is owned by the owners of the Company.

The Gladstone Power Station is operated by NRG Gladstone Operating Services Pty Ltd, which is ultimately a wholly-owned subsidiary of NRG Energy Inc. NRG Gladstone Operating Services Pty Ltd operates the Gladstone Power Station under the terms of the Operation and Maintenance Agreement with the Gladstone Power Station Joint Venture. During the periods ended December 31, 1996, 1995 and 1994, the Company paid NRG Gladstone Operating Services Pty Ltd approximately \$252, \$289 and \$170 (A\$S'000) respectively in operators fees under the terms of the Operation and Maintenance Agreement.

15. NUMBER OF EMPLOYEES

The average number of persons employed at the Gladstone Power Station during 1996 was approximately 471. These individuals are primarily employed in the operations and maintenance areas of the station. The Company is responsible for 17.5% of the related costs for these employees. The Company itself has no employees.

16. REMUNERATION OF DIRECTORS

During the periods ended December 31, 1996, 1995 and 1994, none of the directors received remuneration for their services as directors of the Company.

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SAN JOAQUIN VALLEY ENERGY PARTNERS I, L.P.  
(A CALIFORNIA LIMITED PARTNERSHIP)

BALANCE SHEET  
DECEMBER 31, 1996  
(UNAUDITED)

ASSETS	1996
	-----
<b>CURRENT ASSETS:</b>	
Cash and cash equivalents .....	\$2,270,941
Accounts receivable .....	125,319
Fuel inventory .....	48,069
Receivable from affiliates .....	26,299
Prepaid/Other .....	82,257
	-----
Total current assets .....	2,552,885
Property, plant, and equipment, net .....	4,964,030
	-----
Total Assets .....	\$7,516,915
	=====
<b>LIABILITIES AND PARTNERS' EQUITY</b>	
<b>CURRENT LIABILITIES:</b>	
Accounts payable .....	\$ 56,983
Accrued liabilities .....	1,629,878
	-----
Total current liabilities .....	1,686,861
Commitments and Contingencies (see Note 4)	
Partners' equity .....	5,830,054
	-----
Total liabilities and Partners' equity ...	\$7,516,915
	=====

The accompanying notes are an integral part of the financial statements.

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SAN JOAQUIN VALLEY ENERGY PARTNERS I, L.P.  
(A CALIFORNIA LIMITED PARTNERSHIP)

STATEMENT OF INCOME

FOR THE YEAR ENDED DECEMBER 31, 1996  
(UNAUDITED)

REVENUE:	1996
	-----
Electricity sales.....	\$ --
<b>Costs and expenses:</b>	
Operating .....	855,601
General and administrative .....	532,943
	-----
Total costs and expenses .	1,388,544
	-----
Operating loss .....	(1,388,544)
Interest Income .....	294,168
Other Income (Note 6) .....	5,309,304
	-----
Total Other Income .....	5,603,472
	-----



Net Income ..... \$ 4,214,928  
=====

The accompanying notes are an integral part of the financial statements.

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SAN JOAQUIN VALLEY ENERGY PARTNERS I, L.P.  
(A CALIFORNIA LIMITED PARTNERSHIP)

STATEMENT OF PARTNERS' EQUITY  
FOR THE YEAR ENDED DECEMBER 31, 1996  
(UNAUDITED)

Partners' equity, December 31, 1995 .....	\$ 52,135,092
Net income for the year ended December 31, 1996 .....	4,214,928
Partnership distributions for the year ended December 31, 1996 .....	(50,519,966)
	-----
Partners' equity, December 31, 1996 .....	\$ 5,830,054
	=====

The accompanying notes are an integral part of the financial statements.

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SAN JOAQUIN VALLEY ENERGY PARTNERS I, L.P.  
(A CALIFORNIA LIMITED PARTNERSHIP)

STATEMENT OF CASH FLOWS  
FOR THE YEAR ENDED DECEMBER 31, 1996  
(UNAUDITED)

1996

Cash flows from operating activities:	
Net income.....	\$ 4,214,928
Adjustments to reconcile net income to net cash: provided by operating activities:	
Change in assets and liabilities:	
Increase in accounts receivable .....	(63,001)
Decrease in receivable from PG&E .....	52,050,216
Decrease in inventory .....	75,960
Decrease in prepaid/other assets .....	50,628
Decrease in due from affiliates .....	2,337
Decrease in accounts payable/book overdraft .	(8,610)
Decrease in accrued liabilities .....	(6,689,178)
-----	
Net cash provided by operating activities ..	\$ 49,633,280
-----	
Cash flows from investing activities:	
Sale and maturities of short-term investments ..	3,756,078
-----	
Net cash provided by investing activities ..	3,756,078
-----	
Cash flows from financing activities:	
Principal payments on long-term debt .....	(598,451)
Partnership distributions .....	(50,519,966)
-----	
Net cash used in financing activities .....	(51,118,417)
-----	
Net increase in cash and cash equivalents .....	2,270,941
Cash and cash equivalents at beginning of year ..	--
-----	
Cash and cash equivalents at end of year .....	\$ 2,270,941
=====	

The accompanying notes are an integral part of the financial statements.

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SAN JOAQUIN VALLEY ENERGY PARTNERS I, L.P.  
(A CALIFORNIA LIMITED PARTNERSHIP)  
NOTES TO FINANCIAL STATEMENTS  
(UNAUDITED)

1. ORGANIZATION AND OPERATION:

San Joaquin Valley Energy Partners I, L.P. (Partnership), a California limited partnership was formed on July 31, 1992, to purchase and operate three biomass power plant facilities in Madera and Merced Counties, California.

The Partnership sold electricity to Pacific Gas & Electric (PG&E) until February 28, 1995, when the plants ceased operations in anticipation of the transfer of the Partnership's power purchase agreements (PPA's) back to PG&E.

The General Partners are San Joaquin Valley Energy I, Inc., a California corporation (SJVEI), and Power Partners II, a California general partnership. The Limited Partners are NRG Jackson Valley II, Inc., a California

corporation (NRG II); Donovan D. Bohn, an individual; and Volkar/Coombs Partners, a California general partnership (VCP). The Partnership agreement stipulates that the term of the Partnership shall continue for a period ending the earlier of December 31, 2030, or the date on which the Partnership is dissolved by law or by mutual agreement of the Partners.

SJVE I and NRG II are wholly owned subsidiaries of NRG Energy, Inc., a Delaware corporation.

The Partners of Power Partners II are Power Joint Ventures II, Inc. and P&W Ventures II, Inc., both California corporations. VH Energy, L.L.C., an Illinois limited company, and Roland S. Coombs, an individual, are the Partners of VCP. Patrick J. Volkar is the sole shareholder of Power Joint Ventures II, Inc., and Roland S. Coombs is the sole shareholder of P&W Ventures II, Inc., Patrick J. Volkar and Sandra A. Hunt are the members of VH Energy, L.L.C.

## 2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES:

### Basis of Presentation

The Partnership financial statements as of and for the year ended December 31, 1996 are unaudited. In the opinion of management, the unaudited financial statements of the Partnership contain all adjustments, consisting only of normal recurring accruals, necessary to present fairly the Partnership's financial position and results of operations.

### Cash and Cash Equivalents

For purposes of the statement of cash flows, cash and cash equivalents include cash and all investment instruments purchased with a maturity of three months or less.

The Partnership invests its cash in time deposits and money market accounts most of which are not federally insured. The Partnership has not experienced any losses on these deposits. The carrying amounts of cash and cash equivalents approximates fair value because of the short maturity of these instruments.

### Accounts Receivable

Management believes that there are no uncollectible accounts receivable; therefore, there is no allowance for doubtful accounts at December 31, 1996.

### Fuel Inventory

Fuel inventory consists of unburned fuel char, urban wood waste, wood chips, nut hulls and other biomass, and is stated at the lower of averaged cost or market.

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SAN JOAQUIN VALLEY ENERGY PARTNERS I, L.P.  
(A CALIFORNIA LIMITED PARTNERSHIP)  
NOTES TO FINANCIAL STATEMENTS--CONTINUED  
(UNAUDITED)

## 2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES: (Continued)

### Property, Plant and Equipment

Property, plant and equipment is stated at cost, reduced to fair value in 1995. Since then depreciation has been suspended and no sales or purchases of fixed assets have taken place.

### Environmental Restoration Costs/Contingencies

The Partnership has reduced its estimate of environmental restoration

costs of its plant sites to \$105,060 during the past year based on a current review of engineering studies performed and the monitoring of plant activity. (see Note 6.)

#### Income Taxes

The net income or loss of the Partnership for income tax purposes, along with any associated tax credits, is included in the tax returns of the individual partners. Accordingly, no provision has been made for federal or state income taxes in the accompanying financial statements.

The allocation of taxable income, gains, losses and credits to the partners is specified in the Partnership agreement.

#### Estimates

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

### 3. PROPERTY, PLANT AND EQUIPMENT:

Property, plant and equipment consist of the following at December 31:

	1996
	-----
Power plants .....	\$4,700,000
Land .....	264,030
	-----
	4,964,030
Less accumulated depreciation	--
	-----
	\$4,964,030
	=====

In accordance with SFAS 121, as a result of the PPA transfer, property, plant and equipment was written to its estimated fair value at December 31, 1995. The recorded amounts for property, plant and equipment at December 31, 1996 are still considered to be fair value.

### 4. COMMITMENTS AND CONTINGENCIES

The Partnership has entered into contractual agreements to purchase specified quantities of biomass fuels from various vendors, and the partnership has agreed to assume a fuel purchase commitment of San Joaquin Valley Energy Partners IV, L.P. (SJVEP IV). The purchase price of the fuels is a specified amount above the market cost per bone dry ton. The periods covered by the contracts range from one to eight years with the longest expiring in the year 1999.

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SAN JOAQUIN VALLEY ENERGY PARTNERS I, L.P.  
(A CALIFORNIA LIMITED PARTNERSHIP)  
NOTES TO FINANCIAL STATEMENTS--CONTINUED  
(UNAUDITED)

### 4. COMMITMENTS AND CONTINGENCIES (Continued)

Since agreeing to transfer its PPA's back to PG&E, the Partnership has

sought to terminate all of its fuel purchase commitments. Management believes the Partnership will not incur any additional loss on termination in excess of amounts already accrued.

The Partnership is party to one minor claim with a former vendor. The Partnership's liability for such matter is uncertain, however, management believes that the final resolution of this matter will not have a material adverse effect on the Partnership's financial position or results of operations.

5. TRANSACTIONS WITH AFFILIATES:

At December 31, 1996, the receivable from affiliates related through common ownership consists of:

	1996
	-----
Due from affiliates relating to the purchase of Biomass fuel and charges for administration, insurance, and workers' compensation costs, consisting of:	
BioConversion Partners, L.P. ....	\$14,828
San Joaquin Valley Energy partners IV, L.P. (SJVEP IV) .....	11,471

6. OTHER INCOME

During 1996, based upon updated analysis, the Partnership has re-assessed its estimated exposure for environmental restoration costs and has concluded that no remediation will be required. It has, therefore, reduced its accrual for such charges from \$4,850,000 at December 31, 1995 to \$105,060 at December 31, 1996. The remaining amount of other income was due primarily to the settlements of accrued liabilities at favorable terms.

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REPORT OF INDEPENDENT ACCOUNTANTS

To the Management Committee of  
San Joaquin Valley Energy Partners I, L.P.

We have audited the accompanying balance sheets of San Joaquin Valley Energy Partners I, L.P., a California limited partnership (the Partnership) as of December 31, 1995 and 1994, and the related statements of income, partners' equity and cash flows for the years then ended. These financial statements are the responsibility of the Partnership'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 audits 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 San Joaquin Valley Energy Partners I, L.P. at December 31, 1995 and 1994, and the results of its operations and its cash flows for the years then ended, in conformity with

generally accepted accounting principles.

As discussed in Note 6 to the financial statements, during 1995, the Partnership entered into an agreement whereby the Partnership's power purchase contracts were transferred back to Pacific Gas & Electric.

/s/ Coopers & Lybrand L.L.P.

Sacramento, California  
February 29, 1996

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SAN JOAQUIN VALLEY ENERGY PARTNERS I, L.P.  
(A CALIFORNIA LIMITED PARTNERSHIP)

BALANCE SHEETS  
DECEMBER 31, 1995 AND 1994

	1995	1994
	-----	-----
ASSETS		
Current assets:		
Short-term investments .....	\$ 3,756,078	\$ --
Restricted cash.....	--	13,710,534
Receivable from PG&E.....	52,050,216	--
Accounts receivable.....	62,318	3,657,340
Fuel inventory.....	124,029	1,660,162
Receivable from affiliates.....	28,636	217,748
Other.....	132,885	225,075
	-----	-----
Total current assets.....	56,154,162	19,470,859
Property, plant, and equipment, net.....	4,964,030	29,519,412
Organization and debt issue costs, net of accumulated amortization of \$828,565 at December 31, 1994 .....	--	1,753,268
Notes receivable from partners and affiliates .....	--	1,600,000
	-----	-----
	\$61,118,192	\$52,343,539
	=====	=====
LIABILITIES AND PARTNERS' EQUITY		
Current liabilities:		
Book overdraft.....	\$ 21,473	\$ --
Accounts payable.....	44,120	1,130,659
Accrued liabilities.....	8,319,056	1,608,285
Long-term debt, current portion.....	184,163	5,455,695
	-----	-----
Total current liabilities.....	8,568,812	8,194,639
Long-term debt, net of current portion.....	414,288	24,077,127
	-----	-----
Total liabilities.....	8,983,100	32,271,766
Commitments (Note 7)		
Partners' equity.....	52,135,092	20,071,773
	-----	-----
	\$61,118,192	\$52,343,539
	=====	=====

The accompanying notes are an integral part of the financial statements.

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SAN JOAQUIN VALLEY ENERGY PARTNERS I, L.P.

(A CALIFORNIA LIMITED PARTNERSHIP)

STATEMENTS OF INCOME  
FOR THE YEARS ENDED DECEMBER 31, 1995 AND 1994

	1995	1994
Revenue:		
Electricity sales.....	\$ 6,107,863	\$38,957,267
Costs and expenses:		
Operating.....	3,814,238	18,879,930
Depreciation and amortization.....	450,997	2,599,187
General and administrative.....	198,431	1,134,205
Total costs and expenses.....	4,463,666	22,613,322
Operating income.....	1,644,197	16,343,945
Other income (expense):		
Interest and bank agency fees.....	(525,598)	(2,702,966)
Interest income.....	541,537	388,481
Other.....	141,900	3,810
Income before extraordinary item.....	1,802,036	14,033,270
Extraordinary item (Note 6):		
Net gain on transfer of power purchase contracts.....	58,468,139	--
Net income.....	\$60,270,175	\$14,033,270

The accompanying notes are an integral part of the financial statements.

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SAN JOAQUIN VALLEY ENERGY PARTNERS I, L.P.  
(A CALIFORNIA LIMITED PARTNERSHIP)

STATEMENTS OF PARTNERS' EQUITY  
FOR THE YEARS ENDED DECEMBER 31, 1995 AND 1994

Partners' equity, December 31, 1993.....	\$ 11,484,304
Net income for the year ended December 31, 1994.....	14,033,270
Partnership distributions for the year ended December 31, 1994.....	(5,445,801)
Partners' equity, December 31, 1994.....	20,071,773
Net income for the year ended December 31, 1995.....	60,270,175
Partnership distributions for the year ended December 31, 1995.....	(28,206,856)
Partners' equity, December 31, 1995.....	\$ 52,135,092

The accompanying notes are an integral part of the financial statements.

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SAN JOAQUIN VALLEY ENERGY PARTNERS I, L.P.

(A CALIFORNIA LIMITED PARTNERSHIP)

STATEMENTS OF CASH FLOWS  
FOR THE YEARS ENDED DECEMBER 31, 1995 AND 1994

	1995	1994
Cash flows from operating activities:		
Net income .....	\$ 60,270,175	\$ 14,033,270
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization .....	450,997	2,599,187
Impairment of assets .....	26,861,778	--
Change in assets and liabilities:		
Decrease (increase) in accounts receivable ...	3,595,022	(800,190)
Increase in receivable from PG&E .....	(52,050,216)	--
Decrease in inventory .....	826,682	164,807
Decrease (increase) in other assets .....	92,190	(1,373)
Decrease (increase) in due from affiliates ...	189,112	(16,642)
Decrease in accounts payable .....	(1,086,539)	(1,163,127)
Increase in accrued liabilities .....	6,416,097	7,968
Net cash provided by operating activities .....	45,565,298	14,823,900
Cash flows from investing activities:		
Purchases of property, plant and equipment .....	--	(2,065,289)
Purchase of short-term investments .....	(3,756,078)	--
Net cash used in investing activities .....	(3,756,078)	(2,065,289)
Cash Flows from financing activities:		
Increase in book overdraft .....	21,473	--
Decrease (increase) in restricted cash .....	13,710,534	(1,861,694)
Principal payments on long-term debt .....	(28,934,371)	(5,451,116)
Proceeds from note receivable .....	1,600,000	--
Partnership distributions .....	(28,206,856)	(5,445,801)
Net cash used in financing activities .....	(41,809,220)	(12,758,611)
Net change in cash and cash equivalents .....	--	--
Cash at beginning of period .....	--	--
Cash and cash equivalents at December 31 .....	\$	\$
Supplemental disclosures of cash flow information:		
Cash paid during period for:		
Interest .....	\$ 1,633,204	\$ 2,566,348

The accompanying notes are an integral part of the financial statements.

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SAN JOAQUIN VALLEY ENERGY PARTNERS I, L.P.  
(A CALIFORNIA LIMITED PARTNERSHIP)

NOTES TO FINANCIAL STATEMENTS

1. ORGANIZATION AND OPERATION:

San Joaquin Valley Energy Partners I, L.P. (Partnership), a California limited partnership, was formed on July 31, 1992, to purchase and operate three biomass power plant facilities in Madera and Merced Counties, California.



The Partnership sold electricity to Pacific Gas & Electric (PG&E) until February 28, 1995, when the plants ceased operations in anticipation of the transfer of the Partnership's power purchase agreements (PPA's) back to PG&E.

The General Partners are San Joaquin Valley Energy I, Inc., a California corporation (SJVE I), and Power Partners II, a California general partnership. The Limited Partners are NRG Jackson Valley II, Inc., a California corporation (NRG II); Donovan D. Bohn, an individual; and Volkar/Coombs Partners, a California general partnership (VCP). The Partnership agreement stipulates that the term of the Partnership shall continue for a period ending the earlier of December 31, 2030, or the date on which the Partnership is dissolved by law or by mutual agreement of the Partners.

SJVE I and NRG II are wholly owned subsidiaries of NRG Energy, Inc., a Delaware corporation.

The Partners of Power Partners II are Power Joint Ventures II, Inc., and P&W Ventures II, Inc., both California corporations. VH Energy, L.L.C., an Illinois limited liability company, and Roland S. Coombs, an individual, are the Partners of VCP. Patrick J. Volkar is the sole shareholder of Power Joint Ventures II, Inc., and Roland S. Coombs is the sole shareholder of P&W Ventures II, Inc. Patrick J. Volkar and Sandra A. Hunt are the members of VH Energy, L.L.C.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES:

Cash and Cash Equivalents

For purposes of the statement of cash flows, cash and cash equivalents include cash and all investment instruments purchased with a maturity of three months or less.

Cash and Restricted Cash

At December 31, 1994, cash balances totalling \$13,710,534 were restricted as to use under the terms of various agreements. There were no such restrictions at December 31, 1995. The restrictions related to the following:

	1994
Receipt account .....	\$ 8,076,401
Operating account .....	572,543
Debt service account .....	4,650,938
Maintenance reserve account	410,652
	-----
	\$13,710,534
	=====

The Partnership invests its cash and restricted cash in time deposits, money market accounts, and short term investment mutual funds, most of which are not federally insured. The Partnership has not experienced any losses on these deposits.

Accounts Receivable

Management believes that there are no uncollectible accounts receivable; therefore, there is no allowance for doubtful accounts at December 31, 1995.

(A CALIFORNIA LIMITED PARTNERSHIP)

NOTES TO FINANCIAL STATEMENTS -- CONTINUED

Fuel Inventory

Fuel inventory consists of unburned fuel char, urban wood waste, wood chips, nut hulls and other biomass, and is stated at the lower of average cost or market.

At December 31, 1995, the Partnership has entered into commitments to sell the entire balance of its inventory recorded as of year end.

Property, Plant and Equipment

Property, plant and equipment is stated at cost, reduced to fair value in 1995. Major additions are capitalized, and repairs and maintenance costs are expensed as incurred. Depreciation of the biomass power plants was calculated on a straight-line basis over the terms of the respective power purchase agreements (PPA's). Depreciation on the other assets was calculated on a straight-line basis over their estimated useful lives, ranging from three to eight years. Depreciation has been suspended effective February 28, 1995. Gains or losses from disposals are reflected in current earnings.

Organization and Debt Issue Costs

Organization and debt issue costs were stated at cost, and were being amortized until 1995 when deemed to be fully impaired and unrealizable, and consequently were written off in connection with the transfer of PPA's back to PG&E.

Impairment of Long-Lived Assets

The Partnership has adopted Statement of Financial Accounting Standards No. 121, Accounting for the Impairment of Long-lived Assets and for Long-lived Assets to Be Disposed Of (SFAS 121), as of December 31, 1995. Under SFAS 121, the Partnership's assets have been impaired as a result of the transfer of power purchase contracts back to PG&E. Accordingly, an impairment loss of \$26,861,778, to reduce the carrying value of the assets to their fair value, has been included in the net gain on transfer of PPA. Fair value has been estimated by management using salvage and sales values for similar plants and related components. The amount the Partnership might ultimately realize could differ materially in the near term from the amount assumed in estimating fair value.

Environmental Restoration Costs

The Partnership has estimated the cost of environmental restoration of its plant sites. Estimated costs relate to evaporation ponds and other plant site restoration. Total accrued environmental restoration costs total \$4,850,000 at December 31, 1995. The amount the Partnership might ultimately incur could differ materially in the near term from the amount accrued.

Income Taxes

The net income or loss of the Partnership for income tax purposes, along with any associated tax credits, is included in the tax returns of the individual partners. Accordingly, no provision has been made for federal or state income taxes in the accompanying financial statements.

The allocation of taxable income, gains, losses and credits to the partners is specified in the Partnership agreement.

Estimates

The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and

disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

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SAN JOAQUIN VALLEY ENERGY PARTNERS I, L.P.  
(A CALIFORNIA LIMITED PARTNERSHIP)

NOTES TO FINANCIAL STATEMENTS -- CONTINUED

3. NOTES RECEIVABLE FROM PARTNERS AND AFFILIATES:

Notes receivable at December 31 consist of:

	1995	1994
	-----	-----
Notes receivable from partners and affiliates, floating rate interest (weighted average interest rate 6.88% at December 31, 1994) .....	\$ --	\$1,600,000
	=====	=====

4. PROPERTY, PLANT AND EQUIPMENT:

Property, plant and equipment consist of the following at December 31:

	1995	1994
	-----	-----
Power plants .....	\$4,700,000	\$32,898,035
Land .....	264,030	264,030
Equipment and other .....	--	932,274
	-----	-----
	4,964,030	34,094,339
Less accumulated depreciation	--	(4,574,927)
	-----	-----
	\$4,964,030	\$29,519,412
	=====	=====

In accordance with SFAS 121, as a result of the PPA transfer, property, plant and equipment has been written down to its estimated fair value at December 31, 1995.

5. LONG-TERM DEBT:

Long-term debt consists of the following at December 31:

	1995	1994
	-----	-----
Note payable to a financial institution, floating-rate interest (weighted average interest rate 6.88% at December 31, 1994) .....	\$ --	\$28,746,665
Payable to an unaffiliated partnership, without interest, payable in annual installments of \$142,850 through August 1, 1999; uncollateralized .....	592,138	695,709
Equipment contracts .....	6,313	90,448
	-----	-----
	598,451	29,532,822
Less current portion .....	(184,163)	(5,455,695)

-----	-----
\$ 414,288	\$24,077,127
=====	=====

The Partnership entered into interest rate swap agreements with a notional amount of \$28,746,665 at December 31, 1994, to reduce the impact of changes in interest rates on its floating-rate notes payable. These agreements, which effectively capped interest rates, involve the exchange of floating-rate for fixed interest payment obligations and resulted in a weighted average fixed interest rate of 5.87% at December 31, 1994, on the Partnership's floating-rate debt.

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SAN JOAQUIN VALLEY ENERGY PARTNERS I, L.P.  
(A CALIFORNIA LIMITED PARTNERSHIP)

NOTES TO FINANCIAL STATEMENTS -- CONTINUED

The aggregate maturities for the long-term debt are as follows:

DECEMBER 31,	
-----	
1996.....	\$184,163
1997.....	142,850
1998.....	142,850
1999.....	128,588
	-----
	\$598,451
	=====

6. POWER PURCHASE CONTRACTS:

The Partnership had agreements (PPA's) to sell Pacific Gas & Electric (PG&E) all electricity produced by the plants through the years 2019-2020. The Partnership also received capacity payments throughout the terms of the PPA's when it operated the plants above specified production levels. The PPA's provided for guaranteed rates ending in years 1998-2000, after which the rates were to be based on PG&E's avoided cost as defined by the PPA's.

During 1994 the Partnership entered into a curtailment agreement with PG&E to limit the output of the power plants during certain off-peak hours. The Partnership received curtailment payments of \$1,968,491 and \$8,091,462 during 1995 and 1994 respectively.

During 1995, the Partnership entered into negotiations regarding an agreement whereby PG&E would compensate the Partnership to transfer back to PG&E its existing PPA's. Effective February 28, 1995, the Partnership entered into a bridging agreement with PG&E whereby the Partnership shutdown its power plants and received payments while a final agreement was being negotiated to transfer the PPA's back to PG&E. Such bridging payments were then deducted from the total compensation received for the transfer of the PPA's.

The final PPA transfer agreement was finalized on July 10, 1995, and provided for the transfer of all of the Partnership's rights under the existing PPA's in exchange for total compensation of \$99,212,716, \$47,162,500 of which was received at closing and through bridging payments, and \$52,050,216 of which was received on March 1, 1996.

A net gain on transfer of PPA's of \$58,468,139 has been recognized in 1995, and consists of:

Total consideration from PG&E .....	\$99,212,716
Less:	
Impairment of assets .....	26,861,778
Operating and maintenance costs during bridging period .....	1,170,291
Loan, agency and prepayment fees .....	1,960,894
Estimated environmental restoration costs .....	4,850,000
Severance, fuel contract settlement and other costs .	5,901,614
	-----
Net gain on transfer of PPA's .....	\$58,468,139
	=====

7. COMMITMENTS:

The Partnership has entered into contractual agreements to purchase specified quantities of biomass fuels from various vendors, and the Partnership has agreed to assume a fuel purchase commitment of San Joaquin Valley Energy Partners IV, L.P. (SJVEP IV). The purchase price of the fuels is a specified amount above the market cost per bone dry ton. The periods covered by the contracts range from one to eight years with the longest expiring in the year 1999. Under these contracts, the Partnership purchased fuel totaling \$--in 1995 and \$8,217,550 in 1994.

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SAN JOAQUIN VALLEY ENERGY PARTNERS I, L.P.  
(A CALIFORNIA LIMITED PARTNERSHIP)

NOTES TO FINANCIAL STATEMENTS -- CONTINUED

Since agreeing to transfer its PPA's back to PG&E, the Partnership has sought to terminate all of its fuel purchase commitments. Management believes the Partnership will not incur any additional loss on termination.

8. EMPLOYEE BENEFIT PLAN:

The Partnership established a 401(k) retirement savings plan (Plan) effective January 1, 1994, that covered all employees. The Partnership contributed approximately \$74,000 during 1994 to the Plan. During 1995, the Plan was terminated at no cost to the Partnership.

9. TRANSACTIONS WITH AFFILIATES:

At December 31, 1995 and 1994, the receivable from affiliates related through common ownership consists of:

	1995	1994
	-----	-----
Due from affiliates relating to the purchase of Biomass fuel and charges for administration, insurance, and workers' compensation costs, consisting of:		
BioConversion Partners, L.P. ....	\$ 2,648	\$ 7,963
San Joaquin Valley Energy Partners IV, L.P. (SJVEP IV) .....	25,988	37,715
Due from the owners of SJVEP IV relating to interest on notes receivable .....	\$ --	\$282,221
Due from BioConversion Partners, L.P. relating to the purchase of unburned fuel .....	--	110,152

The Partnership has an agreement with BioConversion Partners, L.P., (BioConversion) to purchase unburned fuel (Char). The sales price of the char is based on the BTU heat value of the char applied to the average cost per

BTU paid by BioConversion for its biomass fuel. The total amount of char purchased by the Partnership was \$123,417 and \$871,951 in 1995 and 1994, respectively.

The Partnership has an agreement with BioConversion to purchase or sell excess biomass fuel at cost. The total amount of biomass fuel sold to BioConversion was \$-0-and \$182,601 in 1995 and 1994, respectively. The Partnership purchased excess biomass fuel of \$-0-and \$138,102 during 1995 and 1994, respectively.

The Partnership has service agreements to provide general and administrative services to BioConversion and SJVEP IV. The total amount of management fees earned in 1995 and 1994 was \$42,474 and \$34,147 respectively. The Partnership also purchases insurance for BioConversion and SJVEP IV which is then charged back to each of the entities based upon the fair value of their plant assets. The total amount of insurance expense charged to BioConversion was \$32,152 and \$48,421 and to SJVEP IV was \$75,021 and \$112,984 in 1995 and 1994, respectively.

The Partnership incurred approximately \$26,000 and \$43,000 in 1995 and 1994, respectively, for administration and management services provided by Jackson Valley Energy Partners, L.P. (JVEP), a partnership affiliated through common ownership.

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SAN JOAQUIN VALLEY ENERGY PARTNERS I, L.P.  
(A CALIFORNIA LIMITED PARTNERSHIP)

NOTES TO FINANCIAL STATEMENTS -- CONTINUED

The Partnership paid approximately \$37,000 in 1994 to a partner for consulting services, of which approximately \$31,000 was paid on behalf of JVEP. During 1995, the Partnership received payment in full from JVEP for these services.

#### 10. FAIR VALUE OF FINANCIAL INSTRUMENTS:

The carrying amounts of cash and cash equivalents, short term investments, receivable from PG&E and book overdraft approximates fair value because of the short term maturity of these instruments. The carrying amount of long-term debt is not materially different than its estimated fair value based on the fair value of debt with similar terms.

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REPORT OF DELOITTE & TOUCHE GMBH, INDEPENDENT AUDITORS

To the Shareholders  
MIBRAG mbH  
Theissen, Germany

We have audited the accompanying consolidated balance sheets of Mitteldeutsche Braunkohlengesellschaft mbH and its subsidiaries (MIBRAG or

Group) as of December 31, 1996, 1995 and 1994, and the related consolidated statements of income, shareholders' equity, and cash flows for each of the years in the three-year period ended December 31, 1996. These financial statements are the responsibility of the Group'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 in Germany and the United States of America. 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 consolidated financial statements referred to above present fairly, in all material respects, the consolidated financial position of MIBRAG mbH and subsidiaries as of December 31, 1996, 1995, and 1994, and the consolidated results of their operations and cash flows for each of the years in the three-year period ended December 31, 1996, in conformity with accounting principles generally accepted in Germany.

Generally accepted accounting principles in Germany vary in certain significant respects from generally accepted accounting principles in the United States. Application of generally accepted accounting principles in the United States would have affected the results of operations for each of the years in the three-year period ended December 31, 1996 and stockholders' equity as of December 31, 1996 and 1995 to the extent summarized in Note C to the consolidated financial statements.

Halle, Germany  
October 24, 1997

DELOITTE & TOUCHE GmbH  
Wirtschaftsprüfungsgesellschaft

(Roder)

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MITTELDEUTSCHE BRAUNKOHLENGESSELLSCHAFT MBH

CONSOLIDATED STATEMENTS OF INCOME  
(IN THOUSANDS DM)

	YEAR ENDED DECEMBER 31,		
	1996	1995	1994
Sales revenue .....	621,439	650,705	813,085
Changes in inventories .....	(3,719)	(9,462)	(115)
Capitalized own services.....	4,249	6,143	2,450
Other operating income.....	84,904	76,900	38,025
Total revenue.....	706,873	724,286	853,445
Cost of materials.....	138,468	133,670	244,491
Personnel expenses.....	249,437	251,509	259,012
Depreciation on intangible and tangible fixed assets.....	201,362	317,457	165,392
Other operating expenses.....	264,998	229,235	231,820
Total operating expenses.....	854,265	931,871	900,715
Operating income .....	(147,392)	(207,585)	(47,270)

Income from associated company and from companies in which participations are held .....	5,224	1,252	2,096
Income from long-term investments.....	7,035	--	--
Interest income (net).....	3,906	15,607	10,028
Net income from ordinary activities.....	(131,227)	(190,726)	(35,146)
Property tax .....	825	1,612	1,043
Net income .....	(132,052)	(192,338)	(36,189)
Profit/loss carried forward .....	32	--	--
Withdrawal from capital reserve.....	137,020	197,338	41,189
Balance sheet profit/loss .....	5,000	5,000	5,000

See accompanying Notes to Consolidated Financial Statements

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MITTELDEUTSCHE BRAUNKOHLENGESSELLSCHAFT MBH

CONSOLIDATED BALANCE SHEETS  
(IN THOUSANDS DM)

		AT DECEMBER 31,		
NOTE		1996	1995	1994
ASSETS				
NON-CURRENT ASSETS				
Intangible assets				
1. Concessions, trade marks, patents and licenses.....	B,E	18,368	12,498	2,388
2. Payments on account .....	B,E	--	--	979
		18,368	12,498	3,367
Tangible assets				
1. Land and landrights .....	B,E	63,482	56,006	48,819
2. Buildings .....	B,E	116,051	107,047	101,354
3. Strip mines .....	B,E	47,955	47,441	48,412
4. Technical equipment and machinery .....	B,E	367,327	357,082	398,325
5. Factory and office equipment .....	B,E	59,566	49,495	77,649
6. Payments on account and assets under construction .....		40,132	101,726	166,778
		694,513	717,797	841,337
Financial assets				
1. Participations (including associated company)	B,F	28,973	19,482	7,050
2. Loans granted to participation .....	B,G	16,867	17,600	2,121
3. Long-term investments .....	B,H	20,260	--	--
4. Other loans .....	B,I	94,500	82,208	--
		160,600	119,290	9,171
TOTAL NON-CURRENT ASSETS .....		873,481	849,585	853,875
Overburden.....	B,J	304,911	306,399	319,932
CURRENT ASSETS				
Inventories				
1. Raw materials and supplies .....	B	8,359	6,941	6,633
2. Unfinished services .....	B	170	--	--
3. Finished and trade goods.....	B	1,837	2,239	168
		10,366	9,180	6,801
Receivables and other assets				
1. Trade receivables .....	B,K	74,397	54,660	63,838
2. Receivables from enterprises in which participations are held .....	B	5,513	11,493	473
3. Other assets .....	B	62,731	84,390	60,406
		142,641	150,543	124,717
Investments				
Other investments.....	B,L	210,289	--	--
Checks, cash-in-hand, bank balances.....	B	183,690	405,885	287,792
TOTAL CURRENT ASSETS .....		546,986	566,608	419,310
Prepaid expenses.....	B	6,528	6,760	5,681
TOTAL ASSETS .....		1,731,906	1,730,352	1,598,798



See accompanying Notes to Consolidated Financial Statements

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	NOTE	AT DECEMBER 31,		
		1996	1995	1994
SHAREHOLDERS' EQUITY AND LIABILITIES				
SHAREHOLDERS' EQUITY				
Subscribed capital .....		60,000	60,000	60,000
Capital reserve .....		730,208	778,170	831,547
Balance sheet profit DM 5,000,000 each year				
thereof distributed DM 5,000,000 each year .....		--	--	--
Minority interest .....		(19,007)	28,726	(2)
TOTAL SHAREHOLDERS' EQUITY .....		771,201	866,896	891,545
Special item for investment subsidies and incentives .....	B	45,013	40,492	28,104
Provisions				
1. Accruals for pensions and similar obligations	M	3,621	4,742	3,057
2. Taxation accruals .....	N	2,600	3,578	2,982
3. Environmental ("Altfasten") and mining provisions .....	B,O	392,058	384,120	366,037
4. Other accruals .....	P	39,148	45,597	42,649
		437,425	438,037	414,925
Liabilities				
1. Liabilities to banks.....	B,Q,R	325,307	223,033	141,459
2. Downpayments received .....	B,R	140	--	--
3. Trade payables .....	B,R	75,737	93,464	61,029
4. Payables to participations .....	B,R	8,615	3,421	1,871
5. Other payables .....	B,R	68,467	65,006	59,865
		478,266	384,924	264,224
Deferred income .....		1	3	--
TOTAL SHAREHOLDERS' EQUITY AND LIABILITIES .....		1,731,906	1,730,352	1,598,798

See accompanying Notes to Consolidated Financial Statements

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MITTELDEUTSCHE BRAUNKOHLENGESSELLSCHAFT MBH

CONSOLIDATED STATEMENTS OF CASH FLOWS  
(IN THOUSANDS DM)

	YEAR ENDED		
	1996	1995	1994
Cash flows from operating activities:			
Net loss for the year .....	(132,052)	(192,338)	(36,189)
Adjustments to reconcile net loss to net cash provided by operating activities:			
Depreciation on intangible and tangible assets .....	201,362	317,457	165,392
Planned release of the special line item for investment subsidies and incentives .....	(8,979)	(8,181)	(12,997)
Loss on disposal of fixed assets .....	1,997	13,701	21,095
Change in assets and liabilities:			
Short-term overburden .....	1,512	577	71
Inventories .....	(1,186)	(2,379)	1,758
Short-term receivables and other assets .....	7,901	(47,440)	(76,236)
Increase in accruals .....	(612)	23,112	68,597
Short-term liabilities .....	(15,599)	38,167	124,994
Short-term prepaid expenses .....	(76)	(333)	(354)
Deferred income .....	(2)	3	--
CASH PROVIDED BY OPERATING ACTIVITIES .....	54,266	142,346	256,131
Cash flows from investing activities:			
Capital expenditures .....	(239,704)	(362,534)	(178,608)

Additions to the special item for investment subsidies and incentives .....	13,499	20,569	
Proceeds from disposal of fixed assets .....	12,451	35,666	1,225
Decrease in long-term overburden .....	1,976	10,956	--
Increase in long-term investments (securities) .....	(210,289)	--	--
CASH USED FOR INVESTING ACTIVITIES .....	(422,067)	(295,343)	(177,383)
Cash flows from financing activities:			
Change in equity:			
Dividends paid .....	(5,000)	(5,000)	(5,000)
Investors capital contribution .....	43,674	180,189	--
Withdrawal by MI KG investors .....	(18,257)	--	--
Capital contribution due to settlement agreement with BvS .....	15,941	--	
Capital infusion .....			50,000
Increase in long-term liabilities .....	108,940	75,033	--
Decrease in long-term receivables .....	308	20,868	114,044
CASH PROVIDED BY FINANCING ACTIVITIES .....	145,606	271,090	159,044
NET DECREASE (PRIOR YEARS: INCREASE) IN CASH .....	(222,195)	118,093	237,792
CASH AT BEGINNING OF YEAR .....	405,885	287,792	50,000
CASH AT YEAR-END .....	183,690	405,885	287,792

See accompanying Notes to Consolidated Financial Statements

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MITTELDEUTSCHE BRAUNKOHLENGESSELLSCHAFT MBH

CONSOLIDATED STATEMENTS OF CHANGES IN SHAREHOLDERS' EQUITY  
(IN THOUSANDS DM)

	SUBSCRIBED CAPITAL	CAPITAL RESERVE	MINORITY INTEREST	TOTAL
BALANCE AS OF JANUARY 1, 1994.....	60,000	827,706	0	887,706
Dividends paid .....		(5,000)		(5,000)
MIBRAG's share in the 1994 loss .....		(36,187)		(36,187)
Change in minority interest.....			(2)	(2)
Contribution by shareholders.....		54,010		54,010
Land valuations according to section 36 of DMBilG.....		(8,982)		(8,982)
BALANCE AS OF DECEMBER 31, 1994 .....	60,000	831,547	(2)	891,545
BALANCE AS OF JANUARY 1, 1995.....	60,000	831,547	(2)	891,545
Dividends paid .....		(5,000)		(5,000)
MIBRAG mbH's share in the net loss 1995 .....		(48,377)		(48,377)
Change in minority interest.....			28,728	28,728
BALANCE AS OF DECEMBER 31, 1995 .....	60,000	778,170	28,726	866,896
BALANCE AS OF JANUARY 1, 1996 .....	60,000	778,170	28,726	866,896
Dividends paid .....		(5,000)		(5,000)
MIBRAG mbH's share in the net loss 1996 .....		(58,904)		(58,904)
Change in minority interest .....			(47,733)	(47,733)
Capital contribution--settlement agreement .....		15,942		15,942
BALANCE AS OF DECEMBER 31, 1996 .....	60,000	730,208	(19,007)	771,201

See accompanying Notes to Consolidated Financial Statements

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MITTELDEUTSCHE BRAUNKOHLENGESSELLSCHAFT MBH

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS  
(IN THOUSANDS OF DM)

## NOTE A ORIGINATION AND NATURE OF BUSINESS

ORIGINATION: Mitteldeutsche Braunkohlengesellschaft mbH ("MIBRAG" or "MIBRAG mbH") was created from split-up of MIBRAG AG, previously owned by the Treuhandanstalt (the German government privatization agency), into three separate entities. Effective January 1, 1994 a consortium comprised of NRG Energy, Inc., Morrison Knudsen Corporation, and PowerGen plc. jointly acquired 99 % of the active mining, power generation and related assets and liabilities from the Treuhandanstalt through its Dutch holding company (MIBRAG B.V.). The remaining 1% was transferred on December 18, 1996 from the German government privatization agency to Lambique Beheer B.V., Amsterdam, a subsidiary of NRG Energy, Inc., Morrison Knudsen B.V., Amsterdam, and PowerGen Netherlands B.V., Amsterdam in equal portions (1/3 %) for each partner.

NATURE OF BUSINESS: The operations of MIBRAG mbH include two open-cast brown coal mines in Profen and Schleenhain, a lease on a third mine in Zwenkau, and rights to future mining reserves. The operations also include over 200 MW of power generation and two coal briquetting plants. A significant portion of the sales of MIBRAG is made pursuant to long-term coal and energy supply contracts.

## NOTE B SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The consolidated financial statements of Mitteldeutsche Braunkohlengesellschaft mbH and subsidiaries have been prepared in accordance with the German Commercial Code, which represents accounting principles generally accepted in Germany ("German GAAP"). German GAAP varies in certain significant respects from accounting principles generally accepted in the United States of America ("US GAAP"). Application of US GAAP would have affected the results of operations for each of the years in the three-year period ended December 31, 1996 and stockholders' equity as of December 31, 1996, 1995 and 1994 to the extent summarized in note C to the consolidated financial statements. All amounts herein are shown in thousands of Deutsche Mark ("DM") unless otherwise noted.

PRINCIPLES OF CONSOLIDATION: All material companies in which MIBRAG has legal or effective control are fully consolidated. In 1996, MIBRAG consolidated 5 (1995: 4, 1994: 4) domestic subsidiaries, including one company, GALA, for the first time. For the years ended December 31, 1996, 1995 and 1994 all subsidiaries were consolidated.

One significant investment, MUEG, in which MIBRAG has an ownership interest of 50% is accounted for in accordance with the equity method. This investment is referred to as an associated company in these financial statements.

All other investments in which MIBRAG has an ownership in the range of 20% to 50% are either not considered to be significant for the presentation of the consolidated financial statements of MIBRAG or MIBRAG has no significant influence in these companies. These companies are included at cost and referred to as participations in these financial statements.

All significant intercompany accounts and transactions have been eliminated in consolidation.

USE OF ESTIMATES: The preparation of financial statements in conformity with generally accepted accounting principles necessarily requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the balance sheet dates and the reported amounts of revenues and expenses during the reported periods. Actual results could differ from those estimates.

TOTAL COST METHOD: The income statement has been presented according to the total cost (or type of expenditure) format as commonly used in Germany. According to this format, production and all other expenses incurred during the period are classified by type of expenses.

## MITTELDEUTSCHE BRAUNKOHLENGESSELLSCHAFT MBH

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)  
(IN THOUSANDS OF DM)

## NOTE B SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

REVENUE RECOGNITION: Revenue is recognized when title passes or services are rendered, net of discounts, customer bonuses and rebates granted.

INTANGIBLE ASSETS: Intangible assets are valued at acquisition cost and are amortized over their respective useful lives (5 to 15 years).

PROPERTY, PLANT, AND EQUIPMENT: Property, plant, and equipment acquired is recorded on the basis of acquisition or manufacturing cost, including capitalized mine development costs and subsequently reduced by scheduled depreciation charges over the assets' useful lives as follows: buildings -- 3 to 25 years, technical facilities and machinery -- 4 to 33 years; and facilities, factory and office equipment -- 5 to 10 years. Maintenance and repair costs are expensed as incurred. Depreciation is computed principally by the straight-line method over the expected useful lives of the assets. The amortization of mine development costs is provided on the basis of tonnage mined in relation to total estimated recoverable tonnage. Depreciation on additions during the first or the second half of the year are estimated using full-year or half-year rates, respectively. Low value items are expensed in the year of acquisition. Opportunities for special tax deductible depreciation are utilized for both book and tax purposes.

INVESTMENTS: The long-term loans and investments are recorded at cost.

OVERBURDEN: Overburden represents the costs of removing the surface above a coal field subsequent to the initial opening of the field to the extent that the removal exceeds what is needed for the current years coal extraction. These are costs incurred in advance in respect of future coal production. The overburden of the individual mines on the balance sheet dates were consolidated and valued on an average cost basis.

INVENTORY: Inventories are carried at the lower of average cost or market. Obsolescence provisions are made to the extent that inventory risks are determinable.

RECEIVABLES AND OTHER ASSETS: All receivables are valued at cost, taking into account all known risks. A lump-sum allowance for doubtful accounts is deducted from the receivables in recognition of the general risk inherent in the receivables.

CASH AND CASH EQUIVALENTS: Cash and cash equivalents include cash, checks, current accounts and time deposits.

INVESTMENT GRANTS: To support the acquisition of certain tangible assets, investment allowances and subsidies were granted by the federal government and the German states of Saxony and Saxony-Anhalt. The application, conditions and payments of investment grants are ruled by German law and several regulations and statements. Investment allowances and subsidies received and formally claimed are credited to the special item account. The special item is amortized into income over the normal operating useful lives of the underlying assets to which the allowances and subsidies relate.

ENVIRONMENTAL AND MINING PROVISIONS: Accruals for environmental and mining-related matters are recorded when it is probable that a liability has been incurred and the amount of the liability can be reasonably estimated, based on current law and existing technologies. These accruals are adjusted periodically as assessment and remediation efforts progress or as additional technical or legal information becomes available.

LIABILITIES: Liabilities are shown at their repayment amounts.

PER SHARE AMOUNTS: Per share amounts are not disclosed in the financial statements. MIBRAG is a nonpublic enterprise.

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MITTELDEUTSCHE BRAUNKOHLENGESELLSCHAFT MBH

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)  
(IN THOUSANDS OF DM)

NOTE C SIGNIFICANT DIFFERENCES BETWEEN GERMAN AND UNITED STATES GENERALLY  
ACCEPTED ACCOUNTING PRINCIPLES

The MIBRAG consolidated financial statements comply with German GAAP, which differs in certain significant respects from US GAAP. The significant differences that affect the consolidated net income and stockholders' equity of MIBRAG are set out below.

I. APPLICATION OF THE PURCHASE METHOD OF ACCOUNTING

As of December 31, 1993 the predecessor of MIBRAG -- MIBRAG AG was split into three legal entities:

MIBRAG mbH  
MBV GmbH and  
Romonta GmbH.

The assets and liabilities of the predecessor company were allocated to the three newly founded companies according to a split-up plan, which is required under the applicable German split-up law. Under German GAAP the assets and liabilities of MIBRAG AG were transferred at book value to the financial statements of the three successor companies. The transaction resulted in an shareholders' equity of DM 887.7 million in MIBRAG's opening balance sheet as of January 1, 1994 according to German GAAP.

The acquisition of 99% of the shares in MIBRAG mbH on January 1, 1994 by MIBRAG B.V. was accounted for using the purchase method of accounting and the purchase price adjustments to the historical cost basis have been pushed down to the US GAAP financial statements of MIBRAG mbH. According to the purchase agreement the purchase price for 99% of the shares consists of two components - a fixed and a variable portion. The variable portion depends on future coal mined and briquettes sold, while the fixed portion was calculated as follows:

	MILLION DM
Fixed purchase price.....	290.0
less: assumption of a loan obligation .....	(139.2)
less: investment commitment by MIBRAG B.V.	(110.8)
Net fixed acquisition costs .....	40.0

The estimated fair value of all individual assets acquired and liabilities assumed at the date of the acquisition amounted to DM 1,570.3 million (assets) and DM 773 million (liabilities), respectively. The remaining difference of DM 757.3 million was proportionally allocated to reduce the value assigned to noncurrent assets, excluding long-term investments, assuming fixed acquisition costs of DM 40 million.

The variable portions of the acquisition cost were not considered in the above calculation because the amounts were contingent upon future events, which were not considered to be reasonably estimable.

## II. SUBSEQUENT ADJUSTMENT OF THE US GAAP OPENING BALANCE

As referred to above, the MIBRAG purchase agreement states that MIBRAG B.V. will pay a total of DM 40 million to the successor of the Treuhandanstalt (THA), the Bundesanstalt für vereinigungsbedingte Sonderaufgaben (BvS) at a future date. This amount is to be reduced by the amount of certain incremental transportation costs incurred by MIBRAG for lignite transportation to one of its major customers. For US GAAP purposes, this liability is reflected as a liability of MIBRAG mbH and results in a reduction of MIBRAG equity and an increase in liabilities by DM 40 million.

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MITTELDEUTSCHE BRAUNKOHLENGESELLSCHAFT MBH

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)  
(IN THOUSANDS OF DM)

NOTE C SIGNIFICANT DIFFERENCES BETWEEN GERMAN AND UNITED STATES GENERALLY  
ACCEPTED ACCOUNTING PRINCIPLES (Continued)

### III. NOTES TO SIGNIFICANT US GAAP ADJUSTMENTS

#### 1. Fixed assets other than financial investments

These adjustments are caused by different book values of fixed assets in German and US GAAP financial statements. There are four primary reasons for differences in book values:

- o In the US opening balance sheet as of January 1, 1994, according to purchase accounting, fixed asset balances, other than financial assets, were adjusted to their fair market values. Related unamortized investment subsidies were also included in these adjustments as of January 1, 1994.
- o As of January 1, 1994, the assets were reduced by the allocation of the difference between the net acquisition costs for the MIBRAG shares and the net fair market value of MIBRAG's assets and liabilities.
- o Special accelerated depreciation for tax purposes is recorded in the German financial statements.
- o The depreciation period of long term assets are based upon lives acceptable for German tax purposes, which differ from the useful lives for US accounting purposes.

Upon disposal, the above differences also resulted in differing gains or losses on disposition.

#### Financial investment in MUEG

For German GAAP purposes, MIBRAG accounted for the investment in MUEG as of January 1, 1994 using the cost method. Under US GAAP the book value was increased to account for the equity earnings that were not distributed to MIBRAG as of that date.

#### 2. Relocation accruals

At January 1, 1994, MIBRAG had made a commitment to relocate the villages of Grossgrimma, Heuersdorf, Schwerzau and Breunsdorf at a total estimated cost of DM 273 million. Such amounts were provided for at January 1, 1994. Deferred costs, which are amortized in accordance with quantities of coal extracted, were recorded at the same amount.

The German GAAP balance as of January 1, 1994 included provisions for DM 56 million of this total. In accordance with German accounting principles such reserves and accruals for the relocation of villages can not be accrued

earlier than 2 years prior to the relocation, and some of the relocation costs are to be expensed as incurred.

### 3. Investment in power plants

In 1995 and 1996, third party investors paid in DM 216 million into a MIBRAG subsidiary, MIBRAG Industriekraftwerke GmbH & Co. KG ("MI"). MI runs three lignite-fired power plants. The investment is structured such that the third party investors obtain the accelerated depreciation opportunities for tax purposes while retaining a put option to sell their investments back to MIBRAG at predetermined prices. The third party investments are considered additions to equity for German GAAP, while these arrangements are accounted for as a financing in accordance with US GAAP.

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MITTELDEUTSCHE BRAUNKOHLERGESELLSCHAFT MBH

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)  
(IN THOUSANDS OF DM)

NOTE C SIGNIFICANT DIFFERENCES BETWEEN GERMAN AND UNITED STATES GENERALLY  
ACCEPTED ACCOUNTING PRINCIPLES (Continued)

### 4. Schkopau transportation credits

The liability to BvS as described in item II above is reduced by the amount of excess incremental transportation costs, incurred by MIBRAG for certain lignite shipments. The transportation cost credits are not reflected in MIBRAG's German financial statements, but reduce the liability to BvS in the US GAAP balance sheet.

### 5. Interest capitalization

Interest is expensed in the German financial statements, however interest expense related to qualified assets is capitalized in the US GAAP financial statements.

### 6. Accrued liabilities

Certain mining and other accruals, which were provided for at January 1, 1994 in accordance with US GAAP purchase accounting, were recorded in the German financial statements in 1994.

### 7. Receivables/payables at non-market interest rates

Certain accounts receivables or loans payable are recorded in the German GAAP financial statements at their nominal values. Because these carry non-market interest rates, such receivables and payables were adjusted to their market values

### 8. Overburden

Overburden in the German financial statements includes capitalized depreciation based upon the historical costs. Because of the purchase accounting adjustments, a different amount of depreciation is capitalized in overburden in the US GAAP financial statements. In addition, purchase accounting adjustments as of January 1, 1994 included the write-down of overburden on a mine to be closed.

### 9. Other

Certain costs and income in the German financial statements are capitalized or deferred for US GAAP purposes, respectively.

### 10. Unrealized security gains

Unrealized security gains on available-for-sale securities are not

accounted for under German GAAP, but are recorded in a separate component of equity for US GAAP purposes.

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MITTELDEUTSCHE BRAUNKOHLENGESSELLSCHAFT MBH

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)  
(IN THOUSANDS OF DM)

NOTE C SIGNIFICANT DIFFERENCES BETWEEN GERMAN AND UNITED STATES GENERALLY  
ACCEPTED ACCOUNTING PRINCIPLES (Continued)

RECONCILIATION TO U.S. GAAP

The following is a summary of the significant adjustments to net income for the years 1994, 1995 and 1996 and to stockholders' equity at December 31, 1994, 1995 and 1996, which will be required if U.S. GAAP had been applied instead of German GAAP.

	NOTE	YEAR ENDED DECEMBER 31,		
		1996	1995	1994
Net income as reported in the consolidated income statement under German GAAP.....		(132,052)	(192,338)	(36,189)
Adjustments required to conform with U.S. GAAP:				
Fixed assets.....	(1)	143,280	301,385	152,735
Relocation of villages.....	(2)	46,803	21,258	15,897
Investments in power plants.....	(3)	7,208	0	0
Schkopau transportation credits.....	(4)	12,367	0	0
Interest capitalization.....	(5)	4,549	(52)	1,542
Accrued liabilities.....	(6)	0	0	21,546
Receivables/payables at non-market interest rates.....	(7)	(8,728)	(9,628)	(1,173)
Overburden.....	(8)	(15,201)	(1,253)	(25,534)
Other.....	(9)	(2,012)	(29,417)	(749)
NET INCOME IN ACCORDANCE WITH U.S. GAAP.....		56,214	89,955	128,075

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MITTELDEUTSCHE BRAUNKOHLENGESSELLSCHAFT MBH

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)  
(IN THOUSANDS OF DM)

NOTE C SIGNIFICANT DIFFERENCES BETWEEN GERMAN AND UNITED STATES GENERALLY  
ACCEPTED ACCOUNTING PRINCIPLES (Continued)

MITTELDEUTSCHE BRAUNKOHLENGESSELLSCHAFT MBH

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS  
(IN THOUSANDS OF DM)

	NOTE	AT DECEMBER 31,			
		1996	1995	1994	1/1/1994
Shareholders' equity as in the consolidated balance sheet under German GAAP .....		771,201	866,896	891,545	887,706
Less minority interest .....		1	1	0	0
Adjusted shareholders' equity under German GAAP .....		771,202	866,897	891,545	887,706
Adjustments required to conform with U.S.					



GAAP:					
Long-term asset valuation .....	(1)	34,939	(108,341)	(409,726)	(562,461)
Relocation of villages .....	(2)	(40,333)	(87,136)	(108,394)	(124,291)
Investment in power plants .....	(3)	(190,896)	(172,689)	--	--
Payable to THA/BvS .....	(4)	(27,633)	(40,000)	(40,000)	--
Interest capitalization .....	(5)	6,039	1,490	1,542	--
Accrued liabilities .....	(6)	(30,153)	(30,153)	(30,153)	(51,699)
Receivables/payables at non-market interest rate .....	(7)	12,498	21,226	30,854	32,027
Overburden .....	(8)	(211,991)	(196,790)	(195,537)	(170,003)
Other .....	(9)	(3,457)	(1,445)	27,972	28,721
Change for the year in net unrealized securities gains (net of income tax effects) .....	(10)	5,853	--	--	--
-----					
SHAREHOLDERS' EQUITY IN ACCORDANCE WITH U.S. GAAP .....		326,068	253,059	168,103	40,000
=====					

#### NOTE D CONCENTRATION OF CREDIT RISK AND LONG-TERM COAL SALES AGREEMENTS

MIBRAG mbH markets its coal principally to electric utilities in Germany. As of December 31, 1996, 1995 and 1994 accounts receivable from electric utilities totaled DM 74,397, DM 54,660 and DM 63,838, respectively. Credit is extended based on an evaluation of the customer's financial condition, and collateral is not generally required. Credit losses are provided for in the financial statements and consistently have been minimal.

MIBRAG mbH is committed under several long-term contracts to supply raw brown coal and whirl fine coal to the Schkopau power station and the Lippendorf power station. Under the terms of the Schkopau Agreement closed with VEBA Kraftwerke Ruhr AG (VKR), Gelsenkirchen, MIBRAG mbH delivers annually up to 5.8 million tons of coal commencing 1995. The agreement will be in effect until 2010 with an option for VKR to extend the agreement for another 10 years. The price to be paid by the Schkopau power station is a fixed price adjusted by an annual escalation rate.

The Lippendorf Agreements provide for deliveries of up to 10 million tons per year from 1999 through 2040 with an option for the MIBRAG customers to extend for an additional 3 year period. These

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#### MITTELDEUTSCHE BRAUNKOHELENGESELLSCHAFT MBH

#### NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED) (IN THOUSANDS OF DM)

#### NOTE D CONCENTRATION OF CREDIT RISK AND LONG-TERM COAL SALES AGREEMENTS (Continued)

Agreements were closed with Vereinigte Energiewerke AG (VEAG), Berlin, and Bayernwerk AG, Munich, and replace the agreements on deliveries to the old power station at Lippendorf. The price to be paid by the Lippendorf power station is a base-price with escalation and adjustment based on quality of the coal delivered. The new Lippendorf power station is still under construction.

A substantial portion of the Company's remaining coal reserves is dedicated to the production of coal for such agreements.

Sales to the two largest customers comprise, as a percentage of total sale, 58%, 55% and 65% in 1996, 1995 and 1994, respectively. Sales to the five largest customers comprise, as a percentage of total sale, 86%, 74% and 75% in 1996, 1995 and 1994, respectively.

#### NOTE E PROPERTY, PLANT AND EQUIPMENT (INTANGIBLE AND TANGIBLE ASSETS)

The group depreciation charges are as follows: DM 201,362 (1996), DM 317,457 (1995), and DM 165,392 (1994), including normal depreciation, unplanned depreciation and special tax depreciation in terms of section 4 of

the German tax law, "Fordergebietsgesetz". According to that law certain tangible assets can be depreciated up to 50 % of the historical costs in the first five years of acquisition in addition to the normal depreciation.

Composition:

1996				
	NORMAL DEPRECIATION	SPECIAL TAX DEPRECIATION	UNPLANNED DEPRECIATION	TOTAL
a) Intangible assets				
Concessions, trade marks, patents and licenses .....	2,085	--	--	2,085
b) Tangible assets				
Buildings .....	14,810	13,090	1,701	29,601
Strip-mines .....	985	--	--	985
Technical equipment and machinery.....	63,576	76,765	3,289	143,630
Factory and office equipment .	16,627	8,143	291	25,061
	-----	-----	-----	-----
	98,083	97,998	5,281	201,362
	=====	=====	=====	=====

The unplanned depreciation (DM 5,281) refers to the closed briquette plant Deuben (DM 4,281), to the former residence Holzberg (DM 556) and to the repair shop Naunhof (DM 179), which has been replaced by the repair shop Profen in 1996. Other assets from different locations were unplanned depreciated to the lower market value as of December 31, 1996 (DM 265).

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MITTELDEUTSCHE BRAUNKOHLERGESELLSCHAFT MBH

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)  
(IN THOUSANDS OF DM)

NOTE E PROPERTY, PLANT AND EQUIPMENT (INTANGIBLE AND TANGIBLE ASSETS)  
(Continued)

1995				
FIXED ASSETS	NORMAL DEPRECIATION	SPECIAL TAX DEPRECIATION	UNPLANNED DEPRECIATION	TOTAL
a) Intangible assets				
Concessions, trade marks, patents and licenses .....	1,065	--	--	1,065
b) Tangible assets				
Buildings .....	10,704	32,661	1,620	44,985
Strip-mines .....	971	--	--	971
Technical equipment and machinery.....	62,008	142,962	12,603	217,573
Factory and office equipment ..	21,424	31,099	340	52,863
	-----	-----	-----	-----
	96,172	206,722	14,563	317,457
	=====	=====	=====	=====

The unplanned depreciation (DM 14,563) refers to machinery and equipment (DM 8,416), which was shut down at the Schleenhain mine, to the heating pipe of the Hydrogenation plant Zeitz (DM 5,161), and to other equipment retired (DM 986).

1994

FIXED ASSETS	NORMAL DEPRECIATION	SPECIAL DEPRECIATION	TOTAL
a) Intangible assets			
Concessions, trade marks, patents and licenses .....	615	--	615
b) Tangible assets			
Buildings .....	10,298	6,114	16,412
Strip-mines .....	1,107	--	1,107
Technical equipment and machinery .....	70,679	48,517	119,196
Factory and office equipment .....	17,483	10,579	28,062
	-----	-----	-----
	100,182	65,210	165,392
	=====	=====	=====

NOTE F INVESTMENTS IN OTHER GROUP COMPANIES

MIBRAG mbH holds 20 % or more of the voting rights in 8 companies.

One of these companies -- MUEG Mitteldeutsche Umwelt-und Entsorgungs GmbH, Braunsbedra, (MUEG for short) -has been accounted for using the equity method based on its audited annual financial statements as of December 31, 1995, 1994, and 1993. The audited financial statement as of December 31, 1996 are not available yet. MUEG was founded in 1990 and coordinates the waste disposal activities in the Central German brown coal area. The equity value as of December 31, 1996 is as follows:

	DM
Cost and contributions .....	12,186
+ Net profit share 1994-1996 .....	3,472
. / . Distributed profits share 1994-1996 .....	3,472
	-----
= Carrying amount "at equity" as of 12/31/1996 ..	12,186
	=====

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MITTELDEUTSCHE BRAUNKOHLENGESSELLSCHAFT MBH

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)  
(IN THOUSANDS OF DM)

NOTE F INVESTMENTS IN OTHER GROUP COMPANIES (Continued)

The other 7 companies have been accounted for at their historical acquisition costs, because either MIBRAG mbH is unable to exercise significant influence over the investees operating and financial policies or the impact on the consolidated financial statements is not material.

NOTE G LOAN TO FERNWAERME HOHENMOELSEN GMBH

In accordance with the purchase contract dated December 14, 1995, MIBRAG sold the district heating network assets to the Fernwarme Hohenmolsen GmbH, effective as of 1 January 1995, at a net sales price of DM 19 million. After deducting a down payment of DM 1.4 million in 1995, the balance will be repaid in equal installments over a period of 25 years and an interest rate of 5 per cent fixed until 1999. After 1999 the interest rate will be adjusted to the changed market rate at that time.

The fair market value of the loan was as follows:

DEC. 31, 1996      DEC. 31, 1995

DM	DM
16,867	17,600

NOTE H LONG-TERM INVESTMENTS

Near year-end of 1996 marketable debt securities with a face value of DM 20 million were acquired. These securities are carried at their costs. The acquisition cost approximates the fair value for this category of securities based on quoted market prices as of December 31, 1996. The securities will not be sold before 1998. Gains due to the accrual of interest of TDM 245 in 1996 are included in interest income. The maturity date will be in the period within one year through five years.

NOTE I OTHER LOANS

The other loans refer to loans granted to the new investors of a subsidiary of MIBRAG mbH. In accordance with the first additional clause of the loan contract dated April 3, 1995 between KfW (Kreditanstalt für Wiederaufbau) and MIBRAG mbH, KfW grant MIBRAG mbH a loan of DM 82,208 to December 30, 2005 at a fixed interest rate of 6.67%. As per agreement the loan was received on December 29, 1995.

The loans to the new investors of the subsidiary of MIBRAG mbH were granted at the same conditions as those applicable to the loan between MIBRAG mbH and KfW.

NOTE J OVERBURDEN

The reconciliation of the overburden costs is as follows:

	DEC. 31, 1996		(IN MILLIONS) DEC. 31, 1995		DEC. 31, 1994	
	TONNAGE METRIC TONS	VALUE DM	TONNAGE METRIC TONS	VALUE DM	TONNAGE METRIC TONS	VALUE DM
Profen .....	12.7	113.6	12.8	129.2	14.2	143.5
Schleenhain ..	15.2	140.7	15.2	140.7	17.0	155.0
Zwenkau .....	5.8	50.6	4.6	38.5	4.4	21.4
	-----	-----	-----	-----	-----	-----
	33.7	304.9	32.6	308.4	35.6	319.9
	=====	=====	=====	=====	=====	=====

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MITTELDEUTSCHE BRAUNKOHLERGESELLSCHAFT MBH

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)  
(IN THOUSANDS OF DM)

NOTE J OVERBURDEN (Continued)

The basis for the determination of the overburden is the total quantity of partially exposed raw brown coal. The herein included volume of completely exposed coal can be mined without further removal with the equipment in place. This part of the immediately extractable overburden balances can be analyzed as follows:

	DEC. 31, 1996		(IN MILLIOINS) DEC. 31, 1995		DEC. 31, 1994	
	TONNAGE METRIC TONS	VALUE DM	TONNAGE METRIC TONS	VALUE DM	TONNAGE METRIC TONS	VALUE DM
Profen .....	2.5	23.0	2.0	20.1	2.4	24.0
Schleenhain .	temporary shut down between 1995 and 1999				0.6	5.8
Zwenkau .....	0.3	2.0	0.2	1.5	0.2	0.9
	2.8	25.0	2.2	21.6	3.2	30.7

#### NOTE K TRADE RECEIVABLES

Trade receivables were disclosed in the balance sheet, net of allowances, as follows:

#### ALLOWANCES (IN DM)

Dec. 31, 1996	Dec. 31, 1995	Dec. 31, 1994
954	514	894

#### NOTE L SHORT-TERM INVESTMENTS

In 1996 marketable debt securities were acquired at costs of DM 210.3 million. These securities were set up to reinvest the additional liquidity resulting from the entry of new investors of a subsidiary of MIBRAG mbH. Realized gains of DM 5.9 million were disclosed in interest income. The maturity dates of the securities vary from one year to five years.

#### NOTE M ACCRUALS FOR PENSIONS AND SIMILAR OBLIGATIONS

The provision was mainly raised for briquette benefit claims of active employees on the basis of the collective agreement of November 9, 1993 in respect to allowances in kind. Employees entitled must be employees of the company at the date of retirement. The entitlement elapses with early ending of the working relationship or on receipt of social plan benefits.

The calculation based on an actuarial valuation of January 10, 1997. The valuation took into account the entitlement to the redemption value of DM 185.00 per metric ton of briquettes as specified in the collective agreement and the employees entitled to benefits as of June 30, 1996.

#### NOTE N TAXATION ACCRUALS

MIBRAG did not accrue for income tax under German GAAP, because of net operating losses in 1994 through 1996. Deferred tax assets and liabilities have not been recorded, because there are no significant differences between the German GAAP financial statement and tax bases of the assets and liabilities.

For US GAAP accounting purposes mainly due to the application of purchase accounting and different useful lives for depreciable fixed assets, the financial values differ significantly from the tax basis.

Significant components of MIBRAG's deferred tax liabilities and assets at December 31, 1996, that result from carryforwards and temporary differences between the US GAAP financial statement basis and tax basis of assets and liabilities are summarized as follows:

	1996
	-----
Deferred tax liability	
long term assets .....	32.1
investment subsidies .....	3.4
unrealized holding gains .....	7.5
	-----
Total deferred liability .....	43.0
	-----
Deferred tax assets	
overburden .....	118.8
accruals and liabilities .....	98.0
Net operating loss carryforwards	126.1
Total deferred tax assets .....	342.9
	-----
Net deferred tax asset .....	299.9
	-----
Valuation allowance .....	299.9
	=====
Deferred tax asset/liability ....	0.0
	=====

Because all differences in the opening balances between German and US GAAP are either deductible or taxable for German tax purposes these differences, which result in a net deductible difference, would be considered to be temporary in accordance with US GAAP. Because, however, as of the acquisition date, it was considered more likely than not that the whole deferred tax asset would not be realizable due to ongoing operating losses in the foreseeable future, a valuation allowance for the entire net deferred tax asset was recorded.

For the years 1994 to 1996 it is considered that the probability remains more likely than not that there will be sufficient future taxable income to realize the deferred tax asset.

Therefore a valuation allowance of 100% on the net deferred tax asset is still considered to be necessary as of December 31, 1996.

The German corporation income tax rate on undistributed income is 45%. This differs from the company's effective tax rate of 0%, because the company has no taxable income and in the recording of a deferred tax benefit for net loss carry forwards is prohibited under German GAAP.

Since 1991 land taxation payments have been made in advance based on 0.2 % of the DM-opening balance sheet values until the land tax values have been determined. As the total strip mining and surrounding land have been valued at 0.00 DM/sqm land tax has only been paid where specific assessments have been made. New assessments have been made for the outstanding payments from 1991 until 1996 taking into account the special tax authorities regulation "Einheitsbewertung des Grubengelandes bei Braunkohlenbergbau" (dated January 11, 1995), decrees of the new Federal States to the same topic (dated May 21, 1993) and the current tax authorities advises.

At December 31, 1996 the Company had DM 225 million net operating loss carryforwards, which do not expire and may be applied against future taxable income.

## MITTELDEUTSCHE BRAUNKOHLENGESSELLSCHAFT MBH

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)  
(IN THOUSANDS OF DM)

## NOTE O ENVIRONMENTAL AND MINING PROVISIONS

The following is a summary of environmental and mining provisions (in DM):

	BALANCE AS OF DEC. 31, 1996	BALANCE AS OF DEC. 31, 1995	BALANCE AS OF DEC. 31, 1994
1) End-lake provision .....	287,262	268,357	257,569
2) Provision for environmental pollution .....	9,975	10,000	10,000
3) Landscaping .....	19,420	28,009	23,833
4) Planting .....	12,776	16,097	9,601
5) Relocation of villages .....	62,623	61,657	65,034
	-----	-----	-----
	392,056	384,120	366,037
	=====	=====	=====

In 1996 reclassifications were made relating to landscaping (DM 10,488) and planting (DM 763) that have to be made in connection to end-lake restoration, so that the provision raised in prior years and in the current year were allocated to the end-lake provision section.

## 1) END-LAKE PROVISION

The duty of reclaiming mining fields, to make the area reusable in the public's interest, follows from the duty specified in section 2 of the Bundesberggesetz (BBergG) -- Federal Mining Law. In terms thereof a mine closure plan must be prepared (section 53 BBergG) for termination of above earth mining. In this plan, the actions must be described to protect third parties from dangers caused by the mining operation and to ensure the reusefulness of the earth surface (section 51 BBergG).

The duty of reclaiming of the mining fields applies to MIBRAG in respect of the Profen and Schleenhain mines. MIBRAG is exempted from this duty in respect of the Zwenkau mine in terms of section 4 (3) of the operating lease agreement of 17 December 1993 with MBV, the state-owned company responsible for reclamation of closed mines in the east German region.

The mining field reclamation of the Profen and Schleenhain mines after the ceasing of production is planned for 2029-2046 and 2041-2073 respectively. A legally binding closure plan laying down the principles for action plans in accordance with the BBergG is normally approved two years in advance to the commencement of production by the relevant mining department. The liability to reclaim the area exists from the start of mining activities. The calculation of the total costs for reclaiming mining fields are estimated on the bases of current prices.

The total restructuring costs consist mainly of costs for reconstruction bank reinforcement, dewatering and watering.

## MITTELDEUTSCHE BRAUNKOHLENGESSELLSCHAFT MBH

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)  
(IN THOUSANDS OF DM)

## NOTE O ENVIRONMENTAL AND MINING PROVISIONS (Continued)

The calculation for the respective three years were as follows:

DECEMBER 31, 1996

	TOTAL RESTORATION COSTS DM	TOTAL FIELD VOLUME T	EXTRACTION AS OF DEC. 31, 1996 T	BALANCE AS OF DEC. 31, 1996 DM
Profen .....	246,748	472,100	172,447	90,131
Schleenhain .....	488,239	810,613	327,293	197,131
	734,987	1,282,713	499,740	287,262

DECEMBER 31, 1995

	TOTAL RESTORATION COSTS DM	TOTAL FIELD VOLUME T	EXTRACTION AS OF DEC. 31, 1995 T	BALANCE AS OF DEC. 31, 1995 DM
Profen .....	222,411	472,100	162,492	76,552
Schleenhain .....	475,047	810,613	327,293	191,805
	697,458	1,282,713	489,785	268,357

DECEMBER 31, 1994

	TOTAL RESTORATION COSTS DM	TOTAL FIELD VOLUME T	EXTRACTION AS OF DEC. 31, 1994 T	BALANCE AS OF DEC. 31, 1994 DM
Profen .....	219,938	472,100	153,404	71,467
Schleenhain .....	463,817	810,613	325,250	186,102
	683,755	1,282,713	478,654	257,569

2) PROVISION FOR ENVIRONMENTAL POLLUTION ("ATTLASTEN")

This provision for the clean-up/safeguarding of "Altlasten" is determined in respect of disposals sites and old locations of MIBRAG mbH in refinement and mining production areas, on which waste deposits can be found.

The duty for clean-up results from the waste disposal laws of Saxony and Saxony-Anhalt, in terms of which the subsequent use of the mine area must be without problems. The obligation to avoid danger results from the general applicable law of Germany and the individual states. A danger from a policing point of view occurs when a danger is presented to the surrounding area. The company has listed areas susceptible of contamination in a land register.

An accrual of DM 10 million which is the ceiling for such costs in accordance with the purchase and sales agreement with the Treuhandanstalt, was recorded.

3) LANDSCAPING

In this provision are included costs for reclaiming disposal areas and leveling of the area outside the embankments. These costs include costs for continuous landscaping as well as closing down landscaping.



NOTE O ENVIRONMENTAL AND MINING PROVISIONS (Continued)

The duty results from the "Bundesberggesetz", that states that land must be made reusable during production and after production has ended (sections 55, 2, 4 BBergG).

The provision for landscaping has been recalculated as of December 31, 1996, 1995, 1994, based on the special strategic plans, recultivation plan 1994/95 of Profen and Schleenhain, the strategic plan of the Zwenkau mine, internal budget documentation as well as costing documentation.

The strategic plans categorize the disposal areas according to future usage plans, e.g. agricultural or foresting uses and special uses (roads, flood areas, recreation etc.). The cost estimation has been prepared by the recultivation department based on use, technology, period of recultivation, material-, personnel- and technical expenses utilizing generally used market prices.

The provision was as follows (in DM):

	DEC. 31, 1996	DEC. 31, 1995	DEC. 31, 1994
	-----	-----	-----
Profen .....	6,886	11,203	8,782
Schleenhain ..	8,645	13,485	13,922
Zweckau .....	3,889	3,321	1,129
	-----	-----	-----
	19,420	28,009	23,833
	=====	=====	=====

4) PLANTING

In this account provision is made for costs in connection with temporary planting as well as the revegetation of the mining pits after closure.

The duty for planting results from the environmental protection clauses contained in the general and mine closure strategic plans. Legal basis are the "Bundesberggesetz" (sections 55 and 66) and the "Bundesimmissionsschutzgesetz" (Federal Emission Law). The "Bundesberggesetz" determines that preventative measures must also be taken at the time of mining and the "Bundesimmissionsschutzgesetz" determines that mines must be operated in such a way that harmful environmental effects must be prevented, that can be prevented with available technology.

The quantification results from the surveyed areas, that have been used for disposal and that have not been finally planted and the border embankments that have not been planted. Open cast areas have to be planted at the difference between actual and technically required areas. Via temporary planting, dust pollution and earth erosion are reduced.

The account's composition at the balance sheet dates was as follows (in DM):

	DEC. 31, 1996	DEC. 31, 1995	DEC. 31, 1994
	-----	-----	-----
Profen .....	4,335	5,663	4,629
Schleenhain ..	8,441	10,434	4,972
	-----	-----	-----
	12,776	16,097	9,601

5) RELOCATION OF VILLAGES

The provision for relocation of villages is in respect of relocation costs for the municipalities of Schwerzau, Grossgrimma, Breunsdorf and Heuersdorf, which is necessary for the expansion of the Profen and Schleenhain mines.

The obligation is based on the agreements that have been reached with the relevant municipalities. In addition the company has expressed through its appearance in the public that the relocations will take place at a specified date, which has created a factual obligation to fulfill.

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MITTELDEUTSCHE BRAUNKOHLENGESSELLSCHAFT MBH

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)  
(IN THOUSANDS OF DM)

NOTE O ENVIRONMENTAL AND MINING PROVISIONS (Continued)

The calculation of the provision is based on a method that has been accepted by the taxation authorities in western Germany for the Rhine brown coal area. This method takes into account the relocation planning costs infrastructural projects, projected development costs, cemetery relocation, demolition and landmark preservation. The provision is built up in equal annual amounts, commencing in the two years before the relocation takes place and ending in the middle of the relocation year.

For the almost completed town relocations in Schwerzau and Breunsdorf provisions have been raised for liabilities that will become payable from 1997 through 2000 (namely for landmark protection and for demolition costs).

Composition (in DM):

	DEC. 31, 1996	DEC. 31, 1995	DEC. 31, 1994
Schwerzau ....	1,407	1,892	2,350
Grossgrimma ..	35,248	38,361	37,439
Breunsdorf ..	2,400	1,785	9,500
Heuersdorf ..	23,568	19,619	15,745
	-----	-----	-----
	62,623	61,657	65,034
	=====	=====	=====

NOTE P OTHER ACCRUALS

Accrued liabilities are as follows (in DM):

	DEC. 31, 1996	DEC. 31, 1995	DEC. 31, 1994
1) Severance payments .....	20,875	18,400	19,600
2) Personnel expenses			
-Employment anniversaries .....	2,712	3,143	2,114
-Vacation .....	377	548	738
-Equalization amount in terms of the Act on Handicapped Persons.....	217	266	343
	-----	-----	-----
	3,306	3,957	3,195

3) Remaining accruals .....	14,967	23,240	20,054
	=====	=====	=====
	39,148	45,597	42,849
	=====	=====	=====

#### 1) SEVERANCE PAYMENTS

The calculation of the provision was based on an average wage rate and an average employment service period of 25 years. The employees are entitled to one time severance payment if the company initiates termination or in the case of retrenchments. The severance payments are limited to DM 36 per person.

For the period from January 1, 1996 to January 1, 2001 the planned personnel reductions according to the latest estimates will come up to 671 employees. The amount is reduced by employees which the Treuhandanstalt/BvS has assumed responsibility for.

#### 2) PERSONNEL EXPENSES

MIBRAG mbH grants awards in recognition of long services in the company, based on the collective bargaining agreement of January 1, 1992 and the company agreement of October 1, 1995. The

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### MITTELDEUTSCHE BRAUNKOHLENGESELLSCHAFT MBH

#### NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED) (IN THOUSANDS OF DM)

##### NOTE P OTHER ACCRUALS (Continued)

employees are entitled to financial awards, which increase in proportion to their employment periods. The valuations of the benefits were based on the actuarial valuations of January 10, 1997, January 18, 1996 and February 15, 1995, taking into account commercial principles. Since a reduction in the personnel force is anticipated, the obligation has only been accrued for if the person has been employed by MIBRAG mbH for at least 10 years.

The liability for vacation arises from the vacation days outstanding at balance sheet dates, which have been determined for each employee.

#### 3) REMAINING PROVISIONS

Composition (in DM):

	DEC. 31, 1996	DEC. 31, 1995	DEC. 31, 1994
	-----	-----	-----
Contingencies:			
- Consulting fees .....	781	5,300	--
- Outstanding invoices .....	5,651	4,293	1,220
- Water usage fees .....	1,710	1,564	925
- Briquette sales returns .....	510	1,323	450
- Inventory fees .....	149	345	570
- Others .....	760	18	5,144
	-----	-----	-----
	9,561	12,843	8,309
	-----	-----	-----
Scrapping of fixed assets			
Breitenfeld/Profen.....	1,120	6,471	6,471
Asbestos clean up .....	654	856	1,483
Auditing, consulting and year-end accounting fees.....	790	555	1,500
Others .....	2,842	2,515	2,291
	-----	-----	-----
	5,406	10,397	11,745
	-----	-----	-----

14,967	23,240	20,054
--------	--------	--------

NOTE Q LONG-TERM DEBT

Long-term debt consists of the following (in DM):

	DEC. 31, 1996	DEC. 31, 1995	DEC. 31, 1994
KfW-loans .....	323,730	221,438	139,230
Norddeutsche Landesbank (Nord LB)	1,577	1,595	2,229
	325,307	223,033	141,459

Liabilities to KfW-loans refer to three loans from the Kreditanstalt fur Wiederaufbau, Frankfurt/Main:

- The first loan was granted by contract, dated December 9, 1992, for the construction of a raw brown coal powered industrial power station with a circulating "Wirbelschicht" power source in Wahlitz of DM 139,230. The interest rate has been fixed at 7% p.a. until December 9, 2002, 5% thereof is borne by the Federal Department of Environmental Affairs, for the first 5 years. The redemption period is 20 years. The repayments in 40 equal amounts commence from June 30, 1998.

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MITTELDEUTSCHE BRAUNKOHLENGESSELLSCHAFT MBH

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)  
(IN THOUSANDS OF DM)

NOTE Q LONG-TERM DEBT (Continued)

- On April 3, 1995 MIBRAG mbH as well as a subsidiary closed loan agreements with Kreditanstalt fur Wiederaufbau (KfW).
- MIBRAG entered into the loan agreement to partially finance the limited partner capital contribution of the new investors in one subsidiary. The determination of the final loan amount (DM 103,000) was documented by the amendments, dated December 21, 1995 and January 15, 1996. The redemption period is 13 years. In 1996 the loan was fully called up by MIBRAG mbH, DM 8,500 were redeemed in December 1996, so that the balance as of December 31, 1996 amounted to DM 94,500. The interest rates after the first redemption of DM 8,500 are as follows:

AMOUNT DM	INTEREST RATE %	FIXED UNTIL YEAR
75,424	6.67	2005
10,838	6.82	2005
3,335	6.76	2005
4,903	6.26	2005
94,500		

The interest rate after 2005 will be adjusted to the market rate at that

time.

- - The second loan contract closed on April 3, 1995 between KfW and a subsidiary was granted for partially financing of the modernization and reshaping of both industrial power plants in Deuben and Mumsdorf, especially for the construction of the flue gas desulfurization plants. DM 70,000 have been called up as of January 12, 1996, additional DM 20,000 as of December 30, 1996. The total loan amount is DM 134,000. The redemption period is 13 years with the following interest rates:

AMOUNT DM	INTEREST RATE %	FIXED UNTIL DATE
70,000	6.8	January 12, 2006
20,000	3-month or 6-month FIBOR	December 30, 2010
90,000		

The interest rate after January 12, 2006 will be adjusted to the market rate at that time.

Interest paid for the three loans in 1996, 1995, and 1994 was DM 14.1 million, DM 2.8 million, and DM 1.4 million, respectively.

The loans from the Norddeutsche LB granted for construction purposes in Draschwitz relate to the relocation of Schwerzau. A 1% annual redemption has been agreed on. The loan is interest free until 2010. After that the interest rate amounts to 8% p.a.

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MITTELDEUTSCHE BRAUNKOHLERGESELLSCHAFT MBH

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)  
(IN THOUSANDS OF DM)

NOTE R MATURITY PERIODS OF LIABILITIES

The maturity periods of liabilities are as follows (in thousands DM):

	LIABILITIES TO BANKS *	TRADE PAYABLES	PAYABLES TO PARTICIPATIONS	OTHER PAYABLES	DOWNPAYMENTS RECEIVED	TOTAL
Balance as of Dec. 31, 1994.....	141,459	61,029	1,871	59,865	--	264,224
thereof: maturity period .						
--up to 1 year ..	2,229	60,928	1,871	59,557	--	124,585
--1-5 years .....	--	101	--	160	--	261
--more than 5 years .....	139,230	--	--	148	--	139,378
Balance as of Dec. 31, 1995.....	223,033	93,464	3,421	65,006	--	384,924
thereof: maturity period						
--up to 1 year ..	8,500	93,212	3,421	64,866	--	169,999
--1-5 years .....	--	252	--	--	--	252
--more than 5 years .....	214,533	--	--	140	--	214,673
Balance as of Dec. 31, 1996.....	325,307	75,737	8,615	68,467	140	478,266
thereof: maturity period .						
--up to 1 year ..	14,118	73,628	8,615	58,152	140	154,653
--1-5 years .....	82,910	2,109	--	2,420	--	87,439

--more than 5  
years ..... 228,279                    --                    --                    7,895                    --                    236,174

-----  
\*        Liabilities to banks are fully secured by mortgages

NOTE S COMMITMENTS AND CONTINGENCIES

(IN DM)	AT DECEMBER 31,		
	1996	1995	1994
Guarantees for indebtedness of others.....	86,430	108,405	35,350
Other contractual obligations .....	163,200	127,000	239,000

The other contractual obligations refer to long term investment projects in the mines Profen and Schleenhain and in the three power stations.

MIBRAG leases office equipment and railway-carriages, expiring at various dates. Rental and lease expenses amounted to DM 2,390, DM 2,853 and DM 2,355 in the years ended December 31, 1994, 1995 and 1996, respectively. The future minimum lease payments under operating leases are as follows: 1997: DM 2,361; 1998: DM 232; 1999: DM 97; and no obligations thereafter. Future rental expenses for railway-carriages are bound for one year with an option to extend in the following year. These expenses approximately amount to DM 2 million p.a

NOTE T RELATED PARTY TRANSACTIONS

Between MIBRAG and two subsidiaries of the common parent companies NRG Energy Inc., Morrison-Knudsen Corp. and PowerGen plc. agreements for consulting and management services were closed in respect of the mining operations and the refinement facilities.

These contracts determine certain consultancy services to be provided by the two subsidiaries Morrison-Knudsen Deutschland GmbH (MKD) and Saale Energie Service GmbH (SES) to MIBRAG or its subsidiaries.

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MITTELDEUTSCHE BRAUNKOHLENGESELLSCHAFT MBH

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)  
(IN THOUSANDS OF DM)

NOTE T RELATED PARTY TRANSACTIONS (Continued)

MIBRAG is obliged to determine and pay the cost-related remuneration for these services.

Payments for consultancy services in 1994 were restricted to an amount of DM 10 million, set by the THA in the purchase agreement. In 1995 and 1996 the payments were unrestricted.

Expenditures for MIBRAG were as follows (in thousands DM):

1996	1995	1994
-----	-----	-----

MKD ...	18,396	17,655	7,500
SES ...	7,894	8,599	2,500
	-----	-----	-----
	26,290	26,254	10,000
	=====	=====	=====

NOTE U SETTLEMENT AGREEMENT

MIBRAG B.V., MIBRAG mbH and BvS, as the former shareholder of the MIBRAG AG, entered into a settlement agreement on January 23, 1997, which has been negotiated since January 1, 1994. As a result of the settlement agreement BvS paid to MIBRAG mbH DM 15.941 million for the undercapitalization of one of the power plants, which was included in the split-up to MIBRAG on December 31, 1993. The undercapitalization claim was raised by MIBRAG B.V. as the purchaser of the shares in MIBRAG mbH, because a loan for power plant financing was called up early in 1993, not in accordance with the loan contract.

Under German GAAP the settlement of the claim by MIBRAG B.V. to BvS was accounted for as capital contribution from MIBRAG B.V. to MIBRAG mbH, which resulted in an increase in the additional paid-in capital by DM 15.941 million.

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[LETTERHEAD OF DELOITTE & TOUCHE]

REPORT OF DELOITTE & TOUCHE GMBH, INDEPENDENT AUDITORS

To the Shareholders  
 Saale Energie GmbH  
 Schkopau, Germany

We have audited the accompanying balance sheet of Saale Energie GmbH (SEG) as of December 31, 1996, and the related statements of operations and of cash flows for the year then ended. These financial statements are the responsibility of SEG's management. Our responsibility is to express an opinion on these financial statements based on our audit.

We conducted our audit in accordance with generally accepted auditing standards in Germany and the United States of America. 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 audit provides 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 Saale Energie GmbH as of December 31, 1996, and the results of its operations for the year then ended, in conformity with accounting principles generally accepted in Germany.

Generally accepted accounting principles in Germany vary in certain significant respects from generally accepted accounting principles in the United States of America. Application of generally accepted accounting principles in the United States of America would have affected the results of operations for the year ended December 31, 1996 and shareholders' equity as of December 31, 1996 to the extent summarized in Note C to the financial statements.

Halle, Germany  
 October 31, 1997

DELOITTE & TOUCHE GmbH  
 Wirtschaftsprüfungsgesellschaft

(Roder)

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SAALE ENERGIE GMBH

STATEMENT OF OPERATIONS  
(IN THOUSANDS DM)

	YEAR ENDED DECEMBER 31, 1996
Sales revenue .....	161,309
Other operating income.....	3
Total revenue .....	161,312
Cost of materials and service purchased .....	170,897
Depreciation of intangible and tangible fixed assets .	1
Other operating expenses .....	1,060
Total operating expenses .....	171,958
Results from operations.....	(10,646 )
Income from companies in which participations are held.....	6,581
Interest expense (net) .....	(3,845)
Results from ordinary activities .....	(7,910)
Income tax .....	(40)
Net loss .....	(7,870)

See accompanying Notes to Financial Statements

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SAALE ENERGIE GMBH

BALANCE SHEET  
(IN THOUSANDS DM)

	NOTE	AT DECEMBER 31, 1996
ASSETS		
Contributions outstanding.....		713
NON-CURRENT ASSETS		
FIXED ASSETS		
Tangible assets		
Factory and office equipment .....	B	2
FINANCIAL ASSETS		



1.Subsidiaries.....	B, E	49
2.Participations .....	B, E	200,677
3.Loans granted to participations ..	B, F	82,200
		-----
TOTAL NON-CURRENT ASSETS .....		282,928
CURRENT ASSETS		
INVENTORIES		
Raw materials and supplies.....	B	325
RECEIVABLES AND OTHER ASSETS		
1.Trade receivables .....	B, D, G	24,764
2.Other assets.....	B, G	14,549
CHEQUES, CASH-IN-HAND, BANK		
BALANCES .....	B	28,748
		-----
TOTAL CURRENT ASSETS .....		68,386
		-----
TOTAL ASSETS .....		352,027
		=====
SHAREHOLDERS' EQUITY AND LIABILITIES		
Shareholders' Equity.....	H	
Subscribed capital.....		1,000
Capital reserve.....		48,041
Net loss for the year.....		(7,870)
Profit/loss carried forward .....		(3,513)
		-----
TOTAL SHAREHOLDERS' EQUITY .....		37,658
PROVISIONS		
1.Taxation accruals .....		--
PROVISIONS		
Other accruals.....	B	40
LIABILITIES		
1.Trade payables.....	B, I	8,836
2.Payables to shareholders.....	B, I	92,084
3.Payables to subsidiaries.....	B, I	4,375
4.Payables to participations .....	B, I	174,885
5.Other payables.....	B, I	34,149
		-----
TOTAL SHAREHOLDERS' EQUITY AND		
LIABILITIES .....		352,027
		=====

See accompanying Notes to Financial Statements

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SAALE ENERGIE GMBH

STATEMENT OF CASH FLOWS  
(IN THOUSANDS DM)

YEAR ENDED  
DECEMBER 31, 1996  
-----

Cash flows from operating activities:	
Net loss for the year.....	(7,870)
Adjustments to reconcile net loss to net cash provided by operating activities:	
Depreciation on tangible assets and current asset write-offs.....	4
Change in assets and liabilities:	
Inventories.....	384
Short-term trade receivables .....	(24,647)
Other assets.....	(14,415)

Decrease in accruals.....	(1,535)
Short-term trade payables.....	8,218
Interest payable.....	3,583
Other liabilities.....	114,597
	-----
CASH PROVIDED BY OPERATING ACTIVITIES .....	78,319
	-----
Cash flows from investing activities:	
Increase in participations.....	(82,658)
	-----
CASH USED FOR INVESTING ACTIVITIES .....	(82,658)
	-----
Cash flows from financing activities:	
Increase in capital reserve.....	1,600
Increase in other payables.....	25,468
Increase in payables to shareholders.....	4,132
	-----
CASH PROVIDED BY FINANCING ACTIVITIES.....	31,200
	-----
NET INCREASE IN CASH .....	26,861
CASH AT BEGINNING OF YEAR .....	1,887
	-----
CASH AT END OF YEAR .....	28,748
	=====

See accompanying Notes to Consolidated Financial Statements

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SAALE ENERGIE GMBH

NOTES TO FINANCIAL STATEMENTS  
(IN THOUSANDS DM)

NOTE A ORIGINATION AND NATURE OF BUSINESS

ORIGINATION According to the Articles of Association, Saale Energie GmbH ("SEG") was established on November 11, 1993. The company's shares are held at 50% by NRGenerating International B.V., Amsterdam and at 50% by PowerGen Holdings B.V., Rotterdam.

NATURE OF BUSINESS: The operations of SEG include all activities relating to the direct and indirect acquisition, ownership, administration and operation of power generating facilities located in Schkopau, including the purchase of fuel and the sale of energy produced in the facilities. The business of the company further constitutes all activities relating to the supply of management, maintenance and consulting services in respect of power stations and related plants. The company is authorized to take all other actions and engage in all other businesses which appear to be necessary and useful in order to carry into effect the purpose of the company. In particular it is authorized to hold, acquire and create subsidiaries, branches, companies and interest in other enterprises.

NOTE B SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The financial statements of SEG have been prepared in accordance with the German Commercial Code, which represents accounting principles generally accepted in Germany ("German GAAP"). German GAAP vary in certain significant respects from accounting principles generally accepted in the United States of America ("US GAAP"). Application of US GAAP would have affected the result of operations for the year ended December 31, 1996 to the extent summarized in Note C to the financial statements. All amounts herein are shown in thousands of Deutsche Mark ("DM") unless otherwise stated.

SEG was not required to prepare consolidated financial statements for 1996. SEG owns a 98% share of its subsidiary Saale Energie Service GmbH. The company is included at cost in SEG's financial statements. Furthermore, SEG

holds a 41.1% share in the Kraftwerk Schkopau GbR and a 44.4% share in the Kraftwerk Schkopau Betriebsgesellschaft mbH. These companies are included at cost and referred to as participations in these financial statements.

USE OF ESTIMATES: The preparation of financial statement in conformity with generally accepted accounting principles necessarily requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the balance sheet date and the reported amounts of revenues and expenses during the reported period. Actual results could differ from those estimates.

TOTAL COST METHOD: The income statement has been presented according to the total cost (or type of expenditure) format as commonly used in Germany. According to this format, production and all other expenses incurred during the period are classified by type of expenses.

REVENUE RECOGNITION: Revenue is recognized when title passes or services are rendered, net of discounts, customer bonuses and rebates granted.

FIXED ASSETS: Fixed tangible assets are recorded on the basis of acquisition or manufacturing cost and subsequently reduced by scheduled depreciation charges over the assets' useful lives.

FINANCIAL ASSETS: Inventories are accounted for at historical purchase cost.

RECEIVABLES AND OTHER ASSETS: All receivables are recorded at nominal value. No provision for doubtful accounts has been recorded.

BANK BALANCES: Bank balances include current accounts.

ACCRUALS AND LIABILITIES: Accruals have been recorded for known obligations at the balance sheet date at the amounts of the estimated liability. Liabilities are valued at the amounts outstanding.

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SAALE ENERGIE GMBH

NOTES TO FINANCIAL STATEMENTS -- (CONTINUED)

NOTE C SIGNIFICANT DIFFERENCES BETWEEN GERMAN AND UNITED STATES GENERALLY ACCEPTED ACCOUNTING PRINCIPLES

SEG's financial statements comply with German GAAP, which differs in certain significant respects from US GAAP. The differences that would have a significant effect on net income and shareholders' equity are set out below.

1. CONSOLIDATION

SEG was not required to prepare consolidated financial statements for 1996. If US GAAP had been applied, SEG would be required to prepare consolidated financial statements including the financial statements of Saale Energie Service GmbH (SES), its 98% owned subsidiary.

US GAAP financial statements would therefore include the 1996 operating results of SES, net of minority interest, and would exclude the dividend income received by SEG.

2. ACCOUNTING FOR LONG TERM SERVICE AND SUPPLY AGREEMENTS

For German GAAP purposes the amounts billed to SEG resulting from the use and benefit agreement between SEG and Kraftwek Schkopau GbR were recorded as expenses of the period. Parallel, the amounts attributable to the long-term electricity supply contract were recorded as revenue in the period they were received. See Note D.

In accordance with US GAAP, these agreements would be considered as

leasing agreements. The use and benefit agreement would be considered as a capital lease and the long-term sales agreement as it relates to capacity availability is treated as a direct financing lease arrangement. The revenues and expenses recorded based upon current billings would be replaced by the amortization of unearned direct finance lease income and interest expense on lease obligations in accordance with US GAAP.

The net present value of the minimum lease payments to be made by VEAG under the terms of the agreement amounts to DM875.272, whereas the net present value of the lease obligation liable to GbR over the minimum period of 25 years is DM728.240 at December 31, 1996.

### 3. OUTSTANDING CONTRIBUTIONS BY SHAREHOLDERS'

As of December 31, 1996 contributions from shareholders were outstanding at DM713, which were not deducted from German shareholders' equity. US GAAP shareholders' equity has to be reduced by the outstanding contributions.

### 4. DEFERRED TAXES

Under German GAAP, SEG did not accrue for income tax, because of net operating losses in 1996. Deferred tax assets and liabilities have not been recorded, because under German GAAP they are only recognized to the extent that deferred tax liabilities exceed deferred tax assets. Deferred tax assets are not recorded for operating loss carryforwards.

For US GAAP accounting purposes, mainly due to the application of lease accounting, the financial values differ significantly from the tax basis.

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SAALE ENERGIE GMBH

### NOTES TO FINANCIAL STATEMENTS -- (CONTINUED)

Significant components of SEG's deferred tax liabilities and assets at December 31, 1996, that result from carryforwards and temporary differences between the US GAAP financial statement basis and tax basis of assets and liabilities are summarized as follows:

	1996
	-----
Deferred tax liability	
lease accounting .....	17.6
investment in GbR .....	50.2
	-----
Total deferred liability .....	67.8
	-----
Deferred tax assets operating loss carryforwards	54.7
	-----
Net deferred tax liability .....	13.1
	=====

Because all differences in the opening balances between German and US GAAP are taxable for German tax purposes these differences, which result in a net taxable difference, would be considered to be temporary in accordance with US GAAP.

### RECONCILIATION TO US GAAP

The following is a summary of the significant adjustments to net income for the year 1996 which will be required if US GAAP had been applied instead of German GAAP.

	NOTE	YEAR ENDED DECEMBER 31, 1996
		-----
Net loss as reported in the income statement under German GAAP .....		(7,870)
Adjustments required to conform with US GAAP:		
Consolidation of SES .....	(1)	(40)
Lease adjustment .....	(2)	31,536
Deferred taxes .....	(4)	(14,101)
		-----
Net income in accordance with US GAAP .....		9,525
		=====

The following is a summary of the significant adjustments to shareholders' equity as of December 31, 1996 which will be required if US GAAP had been applied instead of German GAAP.

	NOTE	YEAR ENDED DECEMBER 31, 1996
		-----
Shareholders' equity as reported in the balance sheet under German GAAP .....		37,658
Adjustments required to conform with US GAAP:		
Consolidation of SES .....	(1)	3,277
Lease adjustment .....	(2)	31,536
Outstanding contributions .....	(3)	(713)
Deferred taxes .....	(4)	(13,087)
		-----
Shareholders' equity in accordance with US GAAP .....		58,671
		=====

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SAALE ENERGIE GMBH

NOTES TO FINANCIAL STATEMENTS -- (CONTINUED)

NOTE D LONG-TERM SALES AND SERVICE AGREEMENTS

According to a long-term electricity supply contract between SEG and Vereinigte Energie AG (VEAG), SEG supplies its total available electricity capacity to VEAG. The contract was closed for a 25 years period starting at the date of commissioning of the power plant. In terms of the contract VEAG is obliged to pay on a monthly basis a price that covers (1) the availability of electrical supply capacity and (2) the operating cost incurred to produce the electricity. Under the terms of this agreement VEAG has agreed to make payments of DM2,142.7 million over the period of the agreement (25 years). In 1996 SEG's sales revenues of DM161,309 solely relate to sales made to VEAG.

SEG has a use and benefit agreement with Kraftwerk Schkopau GbR (GbR), under which GbR grants SEG a notional share of 400 MW (power share) in the total net capacity of the power station for its sole use. The SEG power share encompasses all equipment and installations of the power station. In return SEG has obliged to pay all costs of GbR related to the SEG-power share as stipulated in the agreement plus profit mark-up plus value added tax. In 1996 the SEG has recorded expenses of DM95,797 related to this agreement.

In order to manage and operate its share in the power plan SEG closed a contract with Kraftwerk Schkopau Betriebsgesellschaft mbH (KSB) on December 10, 1993. In terms of this contract, SEG commissions KSB with the conversion of coal using its power share of 400 MW of the Schkopau power plant, and KSB accepts responsibility for all costs of operating and maintaining the power plant. In terms of the contract SEG is obliged to pay for KSB's services.

NOTE E INVESTMENTS IN SUBSIDIARIES AND PARTICIPATIONS

SEG holds a 98% share in Saale Energie Service GmbH (SES). The investment is accounted for at its historical acquisition cost of DM49. The business of the company comprises of all activities relating to the supply of management, maintenance and consulting services in respect of power stations and related plants, especially for the lignite power stations of the Mitteldeutsche Braunkohlengesellschaft mbH (MIBRAG) and its subsidiaries.

A 41.1% participation in the Kraftwerk Schkopau GbR (GbR), which is the owner of the Schkopau power plant, is held by SEG, and is recorded at cost.

SEG's 44.4% share in the Kraftwerk Schkopau Betriebsgesellschaft mbH (KSB) has been recorded at the historical acquisition cost of DM22. SEG has assigned its share in KSB to C & L Deutschland Revision AG in security for VEBA Vereinigte Kraftwerke Ruhr AG (VKR).

NOTE F LOAN TO KRAFTWERK SCHKOPAU GBR

In terms of the loan agreement between the participants of the GbR, SEG has granted a loan of DM98 million to GbR, of which DM16,440 was drawn during 1996. The balance outstanding at December 31, 1996 was DM82,200. The loan is unsecured and bears interest at a fixed rate of 7% p.a. The loan has been granted for an indefinite period and the repayment terms are not fixed.

NOTE G RECEIVABLES AND OTHER ASSETS

The trade receivables of DM25, as reported on December 31, 1996, relate solely to power supplies to VEAG. The other assets are mainly receivables from tax authorities.

NOTE H CHANGE IN SHAREHOLDERS' EQUITY

The Shareholders' equity of SEG changed in 1996 solely by the net loss of 1996 (DM7,870) from DM45,528 to DM37,658.

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SAALE ENERGIE GMBH

NOTES TO FINANCIAL STATEMENTS -- (CONTINUED)

NOTE I LIABILITIES

The maturity periods of the liabilities are as follows (in DM):

	MATURITY PERIOD OF LESS THAN 1 YEAR	MATURITY PERIOD BETWEEN 1 AND 5 YEARS	TOTAL BALANCE AS OF DEC. 31, 1996
1) Trade payables .....	8,836	--	8,836
2) Payables to shareholding companies .....	6,387	85,697	92,084
3) Payables to subsidiaries .....	--	4,375	4,375
4) Payables to companies in which participants are held .....	174,884	--	174,884
5) Other liabilities .....	--	34,150	34,150
	190,107	124,222	314,329
	=====	=====	=====

2) PowerGen plc., London and NRGenerating B.V., Amsterdam granted a loan to SEG for the partial funding of its financial requirements at a total amount of DM148,054. The loans are not collateralized and bear interest at a fixed rate of 7.5% p.a. The loans are granted for an indefinite period and no fixed repayment terms have been set.

The loans from shareholding companies comprise as follows (in DM:)

	DEC. 31, 1996
	-----
NRGENERATING B.V.	
Loan .....	42,860
Interest .....	3,169
Miscellaneous credits	59
	-----
	46,088
	-----
POWERGEN PLC.	
Loan .....	42,819
Interest .....	3,167
Miscellaneous credits	10
	-----
	45,996
	=====
	92,084
	=====

3) In terms of the loan agreements dated February 7, 1996 and September 25, 1996 SES granted to SEG loans amounting DM6,500 and DM1,000 respectively. DM3,368 was repaid during 1996. The unsecured loans bear interest at a variable rate equal to the German Central Bank's discount rate plus 2% p.a. Included in the balance as of December 31, 1996 are interest payable of DM243. The loans can be called up at any time.

4) The liability as of December 31, 1996 comprises as follows (in DM):

a) Kraftwerk Schkopau GbR (GbR) .....	168,912
b) Kraftwerk Schkopau Betriebsgesellschaft mbH (KSB) .	5,973
	-----
	174,885
	=====

a) The payables to GbR comprise of two components. DM110,109 refer to the fees due for 1996 in terms of the use and benefit agreement dated December 10, 1993 and represent SEG's share in the power plant's expenses. DM58,803 result from SEG's obligation to reimburse its share

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SAALE ENERGIE GMBH

NOTES TO FINANCIAL STATEMENTS -- (CONTINUED)

in the shortfall achieved in the 1995 financial statement of the GbR as well as the shortfall achieved in 1996 up to the commissioning date of the power plant (March 31).

b) The liability mainly arises from the regulations of the coal

conversion contract, closed on December 10, 1993 between SEG and KSB. In terms of this contract SEG commissions KSB with the conversion of coal using its power share of 400 MW of the Schkopau power plant, and KSB accepts responsibility for all costs of operating and maintaining the power plant. In terms of the contract SEG is obliged to pay for KSB's services.

5) VEBA Vereinigte Kraftwerke Ruhr AG (VKR), the other participant of the GbR, granted a loan up to DM50 million to SEG for purposes of funding the interest due during the construction period of the power plant. DM8,682 and DM25,468 has been drawn by SEG during 1995 and 1996 respectively. A variable interest rate of 3 month LIBOR plus 1.5% p.a. was agreed upon.

NOTE J OTHER FINANCIAL COMMITMENTS

In order to provide the GbR with own funds, the two participants of the GbR closed on December 10, 1993 a financing agreement. In terms of this agreement SEG is obliged to contribute DM82 million to the GbR, which is already fulfilled. SEG is also required to grant a loan of DM98 million in total to the GbR, of which DM82 million have been called up as of December 31, 1996. The remaining DM16 million can be called up any time.

For financial commitments relating to the leased assets and lease commitments see note C.

NOTE K RELATED PARTY TRANSACTIONS

SEG has a long-term coal supply agreement with MIBRAG, a company in which SEG's parent companies each have one-third ownership. Under the terms of this agreement MIBRAG delivers raw brown coal to the power station in Schkopau until 2010 at market prices paid by SEG. The annual volume of coal to be delivered by MIBRAG was not fixed in the agreement.

Additionally, SES, a subsidiary of SEG, and MIBRAG entered into a consulting and management agreement. This agreement determines certain consultancy services provided by SES. MIBRAG is obliged to pay the cost-related remuneration for these services. In 1996 MIBRAG paid DM7,894 to SES.

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SAALE ENERGIE GMBH

STATEMENT OF OPERATIONS (UNAUDITED)  
(IN THOUSANDS DM)

	YEAR ENDED DECEMBER 31, 1995	YEAR ENDED DECEMBER 31, 1994
	-----	-----
Sales revenue.....	101	--
Other operating income.....		
	-----	-----
Total revenue.....	101	--
Cost of materials.....	1,223	--
Depreciation of intangible and tangible fixed assets ..	--	--
Other operating expenses.....	241	311
	-----	-----
Total operating expenses.....	1,464	311
Results from operations.....	(1,363)	(311)
	-----	-----
Income from companies in which participations are held.....	--	--
Interest expense (net).....	(2,375)	578
	-----	-----
Results from ordinary activities.....	(3,738)	267
Income tax.....	--	40
	-----	-----



Net loss..... (3,738) 227  
=====

See accompanying Notes to Financial Statements

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SAALE ENERGIE GMBH

BALANCE SHEET (UNAUDITED)  
(IN THOUSANDS DM)

	NOTE	AT DECEMBER 31, 1995	AT DECEMBER 31, 1994
		-----	-----
<b>ASSETS</b>			
Contributions outstanding.....		713	713
<b>NON-CURRENT ASSETS</b>			
Fixed assets			
Tangible assets			
Factory and office equipment.....	B	3	4
Financial assets			
1. Subsidiaries.....	B,D	49	49
2. Participations.....	B,D	136,867	44,682
3. Loans granted to participations .....	B,E	65,760	24,660
		-----	-----
TOTAL NON-CURRENT ASSETS.....		202,679	69,395
<b>CURRENT ASSETS</b>			
Inventories			
Raw materials and supplies.....	B	712	0
Receivables and other assets			
1. Trade receivables.....	B,C,F	117	0
2. Other assets.....	B,F	134	28
Cheques, cash-in-hand, bank balances ....	B	1,887	1,246
		-----	-----
TOTAL CURRENT ASSETS.....		2,850	1,274
		-----	-----
TOTAL ASSETS.....		206,242	71,382
		=====	=====
<b>SHAREHOLDERS' EQUITY AND LIABILITIES</b>			
<b>SHAREHOLDERS' EQUITY</b>			
Subscribed capital.....		1,000	1,000
Capital reserve.....		48,040	31,125
Net profit/loss for the year.....		(3,738)	(2)
Profit/Loss carried forward.....		225	227
		-----	-----
TOTAL SHAREHOLDERS' EQUITY.....		45,527	32,350
Provisions			
Tax accruals.....		40	40
Other accruals.....	B	1,535	151
Liabilities			
1. Trade payables.....	B,G	618	38
2. Payables to shareholders.....	B,G	87,125	28,348
3. Payables to participations.....	B,G	56,212	0
4. Other payables.....	B,G	15,185	10,455
		-----	-----
TOTAL SHAREHOLDERS' EQUITY AND LIABILITIES.....		206,242	71,382
		=====	=====

See accompanying Notes to Financial Statements

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SAALE ENERGIE GMBH

CONSOLIDATED STATEMENTS OF CASH FLOWS (UNAUDITED)  
(IN THOUSANDS DM)

	YEAR ENDED DECEMBER 31, 1995	YEAR ENDED DECEMBER 31, 1994
Cash flows from operating activities:		
Net loss (1994: profit) for the year.....	(3,738)	227
Adjustments to reconcile net loss to net cash provided by operating activities:		
Depreciation on intangible and tangible assets.....	4	
Change in assets and liabilities:		
Inventories.....	(712)	0
Short-term receivables and other assets.....	(223)	(28)
Increase in accruals.....	1,384	191
Short-term payables.....	578	38
Other liabilities.....	1,048	456
CASH PROVIDED BY OPERATING ACTIVITIES.....	(1,659)	884
Cash flows from investing activities:		
Increase in financial investments.....	(77,074)	(69,346)
CASH USED FOR INVESTING ACTIVITIES.....	(77,074)	(69,346)
Cash flows from financing activities:		
Additional paid-in capital.....	16,915	31,126
Increase in long-term liabilities.....	62,459	38,346
CASH PROVIDED BY FINANCING ACTIVITIES.....	79,374	69,472
NET INCREASE IN CASH.....	641	1,010
CASH AT BEGINNING OF YEAR.....	1,246	236
CASH AT YEAR-END.....	1,887	1,246

See accompanying notes to Consolidated Financial Statements

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SAALE ENERGIE GMBH

NOTES TO FINANCIAL STATEMENTS (UNAUDITED)  
(IN THOUSANDS DM)

NOTE A ORIGINATION AND NATURE OF BUSINESS

ORIGINATION: According to the Articles of Association, Saale Energie GmbH ("SEG") was established on November 11, 1993. The company's shares are held at 50% by NRegenerating International B.V., Amsterdam and at 50% by PowerGen Holdings B.V., Rotterdam.

NATURE OF BUSINESS: The operations of SEG include all activities relating to the direct and indirect acquisition, ownership, administration and operation of power generating facilities located in Schkopau, including the purchase of fuel and the sale of energy produced in the facilities. The business of the company further constitutes all activities relating to the supply of management, maintenance and consulting services in respect of power stations and related plants. The company is authorized to take all other actions and engage in all other businesses which appear to be necessary and useful in order to carry into effect the purpose of the company. In particular it is authorized to hold, acquire and create subsidiaries, branches, companies and interest in other enterprises.

NOTE B SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The financial statements of SEG have been prepared in accordance with the German Commercial Code, which represents accounting principles generally accepted in Germany ("German GAAP"). German GAAP vary in certain significant respects from accounting principles generally accepted in the United States of America ("US GAAP").

SEG was not required to prepare consolidated financial statements for 1994

and 1995. SEG owns a 98% share of its subsidiary Saale Energie Service GmbH. The company is included at cost in SEG's financial statements. Furthermore, SEG holds a 41.1% share in the Kraftwerk Schkopau GbR and a 44.4% share in the Kraftwerk Schkopau Betriebsgesellschaft mbH. These companies are included at cost and referred to as participations in these financial statements.

**USE OF ESTIMATES:** The preparation of financial statement in conformity with generally accepted accounting principles necessarily requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the balance sheet date and the reported amounts of revenues and expenses during the reported period. Actual results could differ from those estimates.

**TOTAL COST METHOD:** The income statement has been presented according to the total cost (or type of expenditure) format as commonly used in Germany. According to this format, production and all other expenses incurred during the period are classified by type of expenses.

**REVENUE RECOGNITION:** Revenue is recognized when title passes or services are rendered, net of discounts, customer bonuses and rabates granted.

**FIXED ASSETS:** Fixed tangible assets are recorded on the basis of acquisition or manufacturing cost and subsequently reduced by scheduled depreciation charges over the assets' useful lives.

**FINANCIAL ASSETS:** The long-term loans and investments are recorded at cost.

**INVENTORIES:** Inventories are accounted for at historical purchase cost.

**RECEIVABLES AND OTHER ASSETS:** All receivables are recorded at nominal value. No provision for doubtful accounts has been recorded.

**BANK BALANCES:** Bank balances include current accounts.

**ACCRUALS AND LIABILITIES:** Accruals have been recorded for known obligations at the balance sheet date at the amounts of the estimated liability. Liabilities are valued at the amounts outstanding.

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SAALE ENERGIE GMBH

NOTES TO FINANCIAL STATEMENTS (UNAUDITED) -- (CONTINUED)

NOTE C LONG-TERM SALES AND SERVICE AGREEMENTS

According to a long-term electricity supply contract between SEG and Vereinigte Energie AG (VEAG), dated December 7, 1993, SEG supplies its total available electricity capacity to VEAG. The contract was closed for a 25 years period starting at the date of commissioning of the power plant. In terms of the contract VEAG is obliged to pay on a monthly basis a price that covers (1) the availability of electrical supply capacity and (2) the operating cost incurred to produce the electricity. SEG began to supply such available capacity in late 1995.

SEG has a use and benefit agreement with Kraftwerk Schkopau GbR (GbR), under which GbR grants SEG a notional share of 400 MW (power share) in the total net capacity of the power station for its sole use. The SEG power share encompasses all equipment and installations of the power station.

In order to manage and operate its share in the power plant SEG closed a contract with Kraftwerk Schkopau Betriebsgesellschaft mbH (KSB) on December 10, 1993. In terms of this contract, SEG commissions KSB with the conversion of coal using its power share of 400 MW of the Schkopau power plant, and KSB accepts responsibility for all costs of operating and maintaining the power plant. In terms of the contract SEG is obliged to pay for KSB's services.

NOTE D INVESTMENTS IN SUBSIDIARIES AND PARTICIPATIONS

SEG holds a 98% share in Saale Energie Service GmbH (SES). The investment is accounted for at its historical acquisition cost of DM 49. The business of the company comprises of all activities relating to the supply of management, maintenance and consulting services in respect of power stations and related plants, especially for the lignite power stations of the Mitteldeutsche Braunkohlengesellschaft mbH (MIBRAG) and its subsidiaries.

A 41.1% participation in the Kraftwerk Schkopau GbR (GbR), which is the owner of the Schkopau power plant, is held by SEG, and is recorded at cost.

SEG's 44.4% share in the Kraftwerk Schkopau Betriebsgesellschaft mbH (KSB) has been recorded at the historical acquisition cost of DM 22. SEG has assigned its share in KSB to C & L Deutschland Revision AG in security for VEBA Vereinigte Kraftwerke Ruhr AG (VKR).

NOTE E LOAN TO KRAFTWERK SCHKOPAU GBR

In terms of the loan agreement between the participants of the GbR, SEG has granted a loan of DM 98 million to GbR, of which DM 41,100 was drawn during 1995 (1994: DM 24,660). The balance outstanding at December 31, 1995 was DM 65,760 (1994: DM 24,660). The loan is unsecured and bears interest at a fixed rate of 7% p.a. The loan has been granted for an indefinite period and the repayment terms are not fixed.

NOTE F RECEIVABLES AND OTHER ASSETS

The trade receivables of DM 117, as reported on December 31, 1995 (1994: DM 0) relate solely to power supplies to VEAG. The other assets are mainly receivables from tax authorities.

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SAALE ENERGIE GMBH

NOTES TO FINANCIAL STATEMENTS (UNAUDITED) -- (CONTINUED)

NOTE G LIABILITIES

The maturity periods of the liabilities are as follows (in DM):

DECEMBER 31, 1995	MATURITY PERIOD OF LESS THAN 1 YEAR	MATURITY PERIOD MORE THAN 1 YEAR	TOTAL BALANCE AS OF DEC. 31, 1995
1) Trade payables .....	617	--	617
2) Payables to shareholding companies.....	--	87,126	87,126
3) Payables to companies in which participations are held.....	27,800	28,412	56,212
4) Other liabilities .....	6,504	8,681	15,185
	34,921	124,219	159,140

DECEMBER 31, 1994	MATURITY PERIOD OF LESS THAN 1 YEAR	MATURITY PERIOD MORE THAN 1 YEAR	TOTAL BALANCE AS OF DEC. 31, 1994
1) Trade payables .....	38	--	38
2) Payables to shareholding companies	28,348	--	28,348
4) Other liabilities .....	5,455	5,000	10,455

33,841	5,000	38,841
--------	-------	--------

2) PowerGen plc., London and NRGenerating B.V., Amsterdam granted a loan to SEG for the partial funding of its financial requirements at an total amount of DM 148,054. The loans are not collateralized and bear interest at a fixed rate of 7.5% p.a. The loans are granted for an indefinite period and no fixed repayment terms have been set.

The loans from shareholding companies comprise as follows (in DM):

	DEC. 31, 1995	DEC. 31, 1994
NRGenerating B.V.	43,603	14,209
PowerGen plc. ....	43,522	14,138
	87,125	28,347

3) The liability as of December 31,1995 of DM 58,803 result from SEG's obligation to reimburse its share in the shortfall achieved in the 1995 financial statement of the GbR.

4) The balance is mainly comprised of a loan granted to SEG by VEBA Vereinigte Kraftwerke Ruhr AG and the outstanding portion of the purchase price to VKR for the shares in Kraftwerk Schkopau GbR.

VEBA Vereinigte Kraftwerke Ruhr AG (VKR), the other participant of the GbR, granted a loan up to DM 50 million to SEG for purposes of funding the interest due during the construction period of the power plant. DM 8,682 has been drawn by SEG during 1995. A variable interest rate of 3 month LIBOR plus 1.5% p.a. was agreed upon.

The purchase price for 41.1% in the shares of GbR was in total DM 20,000. The outstanding balance as of December 31, 1995 was DM 5,000, as of December 31,1994 DM 10,000.

NOTE H OTHER FINANCIAL COMMITMENTS

In order to provide the GbR with own funds, the two participants of the GbR closed on December 10, 1993 a financing agreement. In terms of this agreement SEG is obliged to contribute DM 82 million to the GbR, which is already fulfilled. SEG is also required to grant a loan of DM 98 million in total to the GbR, of which DM 66 million have been called up as of December 31, 1995 (1994: DM 25 million). The remaining amount can be called up any time.

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QUIET LIFE LIMITED  
ACN 065 381 240  
(formerly Loy Yang Power Ltd, name changed 13 May 1997)

PROFIT AND LOSS STATEMENT  
FOR THE YEAR ENDED 30 JUNE 1997

NOTES	30 JUNE 1997 \$	30 JUNE 1996 \$
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OPERATING REVENUE .....	2	459,899,793	574,009,434
Operating Profit before Income Tax .....	3	52,179,438	185,233,791
Income Tax Attributable to Operating Profit ...	5	21,659,694	67,547,498
OPERATING PROFIT AFTER INCOME TAX .....		30,519,744	117,686,293
Extraordinary Item--Profit on sale of business .	4	1,335,852,636	0
Income Tax Attributable to Extraordinary Item ..	5	383,195,543	0
PROFIT ON EXTRAORDINARY ITEM AFTER INCOME TAX .	--	952,657,093	0
OPERATING PROFIT AND EXTRAORDINARY PROFIT AFTER INCOME TAX .....		983,176,837	117,686,293
Retained Earnings at Beginning of Period .....	14	50,618,229	50,618,229
Dividends Paid or Payable.....		1,033,795,086	117,686,293
RETAINED EARNINGS AT END OF PERIOD.....	14	0	50,618,229

This Profit and Loss Statement should be read in conjunction with the Notes  
To And Forming Part of the Financial Statements

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QUIET LIFE LIMITED  
ACN 065 381 240  
(formerly Loy Yang Power Ltd, name changed 13 May 1997)

BALANCE SHEET

AS AT 30 JUNE 1997

	NOTES	30 JUNE 1997 \$	30 JUNE 1996 \$
CURRENT ASSETS			
Cash.....	15.1	15	657,800
Receivables.....	6	0	73,048,889
Inventories.....	7	0	3,559,857
Other assets .....	8	0	1,714,627
TOTAL CURRENT ASSETS		15	78,981,173
NON-CURRENT ASSETS			
Receivables.....	6	0	1,574,810
Inventories.....	7	0	13,176,115
Other assets .....	8	0	5,662,559
Investments.....	9	0	100
Property, plant and equipment.....	10	0	3,159,101,974
TOTAL NON-CURRENT ASSETS .....		0	3,179,515,558
TOTAL ASSETS .....		15	3,258,496,731
CURRENT LIABILITIES			
Creditors and borrowings .....	11	0	2,039,618,476
Provisions.....	12	0	9,110,358
TOTAL CURRENT LIABILITIES .....		0	2,048,728,834
NON-CURRENT LIABILITIES .....			
Creditors and borrowings .....	11	0	1,057,832,534
Provisions.....	12	0	101,317,119

TOTAL NON-CURRENT LIABILITIES		0	1,159,149,653
		-----	-----
TOTAL LIABILITIES .....		0	3,207,878,487
		-----	-----
NET ASSETS .....		15	50,618,244
		-----	-----
EQUITY			
Share capital.....	13	15	15
Retained earnings .....	14	0	50,818,229
		-----	-----
TOTAL EQUITY .....		15	50,618,244
		-----	-----

This Balance Sheet should be read in conjunction with the Notes To  
And Forming Part of the Financial Statements

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QUIET LIFE LIMITED  
ACN 065 381 240  
(formerly Loy Yang Power Ltd, name changed 13 May 1997)

STATEMENT OF CASH FLOWS

FOR THE YEAR ENDED 30 JUNE 1997

	NOTES	30 JUNE 1997 \$	30 JUNE 1996 \$
		-----	-----
CASH FLOWS FROM OPERATING ACTIVITIES			
Receipts from customers.....		447,989,416	661,857,250
Payments to suppliers and employees.....		(132,408,127)	(252,601,057)
Income tax paid.....		(484,975,104)	0
		-----	-----
NET CASH FLOW (USED IN) PROVIDED BY OPERATING ACTIVITIES .....	15.2	(179,393,815)	409,256,193
		-----	-----
CASH FLOWS (USED IN) FROM INVESTING ACTIVITIES			
Proceeds from sale of the business.....	15.3	4,484,928,944	0
Cash balance transferred on sale of business ....		(22,412,523)	0
Payments to acquire property, plant and equipment.....		(14,813,737)	(8,356,243)
Proceeds from sale of property, plant and equipment .....		0	34,091
Proceeds from sale of investments.....		0	223,296
Dividends received.....		0	127,400
		-----	-----
NET CASH FLOW (USED IN) FROM INVESTING ACTIVITIES.....		4,447,702,684	(7,971,456)
		-----	-----
CASH FLOWS FROM FINANCING ACTIVITIES			
Interest and other items of a similar nature received.....		3,063,264	1,907,373
Interest and other costs of finance paid .....		(109,537,439)	(115,063,116)
Hedging receipts associated with borrowings .....		12,007,845	20,764,959
Hedging payments associated with borrowings .....		(19,553,416)	(30,861,150)
Buyback of swaps.....		(79,619,663)	(7,906,790)
Proceeds from borrowings.....		1,222,785,627	86,056,400
Repayment of borrowings.....		(1,129,666,657)	(36,221,000)
Repayment of shareholder loan.....		(1,917,491,710)	0
Buyback of borrowings.....		(1,157,854,106)	(264,281,672)
Dividends paid.....		(1,095,481,066)	(56,000,000)
		-----	-----
NET CASH FLOW USED IN FINANCING ACTIVITIES .....		(4,268,346,521)	(401,604,996)
		-----	-----
NET INCREASE/(DECREASE) IN CASH HELD.....		(37,652)	(320,259)
		-----	-----
CASH AT BEGINNING OF PERIOD.....		37,667	357,926
		-----	-----

CASH AT END OF PERIOD.....	15.1	15	37,667
		-----	-----

This Statement of Cashflows should be read in conjunction with the Notes To  
And Forming Part of the Financial Statements

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QUIET LIFE LIMITED  
ACN 065 381 240  
(FORMERLY LOY YANG POWER LTD, NAME CHANGED 13 MAY 1997)

NOTES TO AND FORMING PART OF THE FINANCIAL STATEMENTS

1 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

1.1 BASIS OF ACCOUNTING

The financial report is a general purpose financial report which has been prepared in accordance with the requirements of the Corporations Law and applicable Accounting Standards. Other mandatory professional reporting requirements (Urgent Issues Group Censensus Views) have also been complied with.

The report is prepared in accordance with the historical cost convention, except for certain assets which, as noted, are at valuation. The accounting policies are consistent with those of the previous year.

1.2 SIGNIFICANT CHANGE IN AFFAIRS

CHANGE OF COMPANY NAME

The company (A.C.N. 065 381 240) changed its name from Loy Yang Power Ltd. to Quiet Life Limited on 13 May 1997.

SALE OF BUSINESS

On 12 May 1997 the company ceased trading and sold all of its cash, receivables, inventories, property, plant and equipment, and contract liabilities and certain creditors (refer note 15.3). All employees were allocated to the new owner with existing employment conditions. The proceeds from the sale were used to extinguish all of the company's debt finance, pay income tax liabilities and to pay a dividend to shareholders equal to the value of retained earnings.

1.3 PRIOR PERIOD COMPARISONS

Comparative information is reclassified where appropriate, to enhance comparability.

1.4 PROPERTY, PLANT AND EQUIPMENT

COST AND VALUATION

Property, plant and equipment were carried at cost.

DEPRECIATION AND AMORTISATION

Depreciation or amortisation was provided for all fixed assets other than freehold land. The majority of assets were depreciated using the straight line method to write off the cost of assets over their expected service lives. The expenditure associated with mine development costs was amortised on a units of production basis. Depreciation or amortisation for all assets commenced on the first day of the month closest to the in-service date.

Changes in depreciation rates and/or depreciable amounts were dealt with on a prospective basis.



## 1.5 RECOVERABLE AMOUNTS

Non-current assets values did not exceed their recoverable amount. Where carrying values exceeded their recoverable amount, assets were revalued downwards to the lower value. The expected net cash flows included in determining the recoverable amounts of non-current assets were discounted to their present value using a market determined risk adjusted discount rate.

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QUIET LIFE LIMITED  
ACN 065 381 240  
(FORMERLY LOY YANG POWER LTD, NAME CHANGED 13 MAY 1997)

NOTES TO AND FORMING PART OF THE FINANCIAL STATEMENTS (CONTINUED)

## 1.6 INVENTORIES

Costs were assigned to inventories using the average cost method. Inventories were valued at lower of cost and net realisable value. An estimate of items which are likely to be utilised in the next twelve months was classified as current.

## 1.7 ACCOUNTING FOR INCOME TAX

The company was until 12 May 1997 subject to the Victorian State Government Tax Equivalent System (VTES) pursuant to Section 88 of the State Owned Enterprises Act 1992. On the 12 May 1997 the company settled its final VTES liability of \$494,975,104. The Department of Treasury and Finance advised on 12 May 1997 that as "the sale transaction involves the transfer of ownership of Loy Yang Power's assets the company will effectively become a "shell" after the transaction. Accordingly, and consistent with this Department's policy on the non-applicability of a Victorian Tax Equivalent System to non-trading shell entities. Loy Yang Power will cease to be subject to a VTES effective from the 12 May 1997 and this Department considers this to be the final transaction under VTES".

The company has adopted the liability method of tax-effect accounting whereby income tax is regarded as an expense and is matched with the accounting profit after allowing for permanent differences.

To the extent that timing differences occur between the time items are recognised in the accounts and when items are taken into account in determining taxable income, the net related taxation benefit or liability is disclosed as a future income tax benefit or a provision for deferred income tax. These account balances are calculated with reference to the rates of income tax which are expected to apply when those timing differences reverse.

Future income tax benefits are not brought to account unless realisation of the asset is assured beyond reasonable doubt. The future income tax benefit arising from tax losses is only carried forward as an asset when the benefit is virtually certain of being realised.

## 1.8 DOUBTFUL DEBTS

The value of estimated doubtful debts was reviewed annually on an individual debtor basis, and appropriate provision made where necessary.

## 1.9 NEGOTIABLE SECURITIES

Where interest was paid in advance on negotiable securities the interest was recognised as an asset and progressively charged to the Profit and Loss Statement over the applicable interest period. Interest payable in arrears was progressively charged to the Profit and Loss Statement over the applicable interest period and recognised as a liability.

Discounts and premiums on face value on the issue of negotiable securities were recognised as variations of the liability to which they relate. The

variations were amortised over the term of the issue, using the effective yield method.

Changes in the capital value of the outstanding liability on index linked securities were recognised as variations in the book value of the liability and charged to the Profit and Loss Statement.

Any gains or losses arising from the buyback of negotiable securities issued by the company were charged to the Profit and Loss Statement as incurred or earned.

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QUIET LIFE LIMITED  
ACN 065 381 240  
(FORMERLY LOY YANG POWER LTD, NAME CHANGED 13 MAY 1997)

NOTES TO AND FORMING PART OF THE FINANCIAL STATEMENTS (CONTINUED)

1.10 DERIVATIVES

The company was exposed to changes in interest rates and commodity prices from its activities. It was the company's policy to use derivative financial instruments to hedge these risks. The company did not enter, hold or issue derivative financial instruments for trading or speculative purposes.

Derivative financial instruments included forward rate agreements, futures, options, interest rate swaps and their Treasury Corporation of Victoria equivalents.

Gains and losses arising from the early termination of general hedges were amortised over the period of the hedge. The exception to this was bond futures where gains and losses were amortised over the average term to maturity of existing fixed.

Gains and losses arising from the early termination of specific hedges were amortised over the shorter of the period of the borrowing being hedged or the period of the hedge.

1.11 EMPLOYEE ENTITLEMENTS

WAGES, SALARIES AND LEAVE

Provision was made for employee entitlement benefits accumulated as a result of employees rendering services up to the sale date. These benefits included wages and salaries, annual leave and associated oncosts.

Liabilities arising in respect of wages and salaries, annual leave and any other employee entitlements expected to be settled within twelve months of the sale date were measured at their nominal amounts. All other employee entitlement liabilities were measured at the present value of their estimated future cash outflows to be made in respect of services provided by employees up to the sale date. In determining the present value of future cash outflows, the interest rates attaching to Federal Government Guaranteed Securities which had terms to maturity approximating the terms of the related liability were used.

Employee entitlement expenses and revenues arising in respect of the following categories:

- o Wages and salaries, non-monetary benefits, annual leave, long service leave, sick leave and other leave entitlements; and
- o other types of employee entitlements,

were charged to the Profit and Loss Statement on a net basis in their respective categories.

SUPERANNUATION

The company contributed towards the Victorian Electricity Industry (VEI) Superannuation Fund on behalf of its employees. These contributions were charged to the Profit and Loss Statement as the liability was recognised (refer note 17.2).

1.12 PROVISION FOR SITE RESTORATION--POWER STATION AND MINE

Recognition of a liability for the cost of restoring the power station and mine sites to an acceptable environmental standard at the end of their useful lives was provided for up until the sale date (refer note 12). This liability included costs of reclamation, plant closure and dismantling, and waste site closure.

The liability was recognised on a gradual basis and was calculated by discounting the estimated future site restoration costs to their net present value. Annual increments to the liability for each site were charged to the Profit and Loss Statement over the estimated remaining life of each site.

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QUIET LIFE LIMITED  
 ACN 065 381 240  
 (FORMERLY LOY YANG POWER LTD, NAME CHANGED 13 MAY 1997)

NOTES TO AND FORMING PART OF THE FINANCIAL STATEMENTS (CONTINUED)

Expected future payments for site restoration were discounted using interest rates attaching, as at the reporting date, to Federal Government Guaranteed Securities with terms to maturity that match, as closely as possible, the estimated future cash outflows.

Cost estimates were based on the assumption that current legal requirements and/or technologies could not change significantly over the life of the power station and mine sites.

Changes in estimates were dealt with on a prospective basis.

The company's obligations for site restoration were transferred to the purchaser of the company's business.

1.13 CASH

For the purpose of the Statement of Cash Flows, cash includes cash on hand and in banks, investments in money market instruments and short-term deposits and securities, net of outstanding overdrafts.

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QUIET LIFE LIMITED  
 ACN 065 381 240  
 (formerly Loy Yang Power Ltd, name changed 13 May 1997)

	30 JUNE 1997	30 JUNE 1996
	\$	\$
	-----	-----
2 OPERATING REVENUE COMPRISES		
Sales revenue .....	441,012,062	557,499,891
Interest revenue (refer note 24.5 for related party component) .....	3,057,422	1,845,183
Proceeds from the sale of non-current assets.....	825,741	587,326
Dividend revenue.....	0	127,400
Other revenue.....	15,004,568	13,949,634
	-----	-----
	459,899,793	574,009,434
	=====	=====

3 OPERATING PROFIT BEFORE INCOME TAX		
The operating profit before income tax is arrived at after charging/(crediting) the following items:		
DEPRECIATION, AMORTISATION AND DIMINUTION		
Plant and equipment.....	82,841,704	96,218,635
Development of mine (amortisation) .....	1,032,676	1,057,471
Leased plant and equipment (amortisation).....	7,488,422	8,678,171
Buildings.....	304,364	320,654
TOTAL DEPRECIATION, AMORTISATION AND DIMINUTION .....	91,667,166	106,274,931
AMOUNTS SET ASIDE TO PROVISIONS		
Employee entitlements .....	4,926,554	4,492,052
Site restoration--power station.....	596,917	486,338
Site restoration--mine.....	225,033	246,940
TOTAL AMOUNT SET ASIDE TO PROVISIONS .....	5,747,504	5,225,330
FINANCE CHARGES (REFER NOTE 24.5) .....	181,865,292	126,710,973
GOVERNMENT MINING ROYALTIES INCURRED .....	8,552,827	9,241,836
ENERGY CONSUMPTION LEVY .....	14,419	29,731
SUPERANNUATION CONTRIBUTIONS .....	2,320,442	2,697,272
RENTAL OPERATING LEASES .....	247,000	419,000
LOSS (PROFIT) ON SALE OF NON-CURRENT ASSETS .....	947,326	(50,803)
RESEARCH AND DEVELOPMENT EXPENDITURE .....	523,566	518,760
4 PROFIT ON EXTRAORDINARY ITEM		
Profit on sale of business (refer note 15.3).....	1,335,852,636	0
Applicable income tax .....	383,195,543	0
	952,657,093	0

Disclosure of the net assets and liabilities sold can be found in note 15.3.

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QUIET LIFE LIMITED  
ACN 065 381 240  
(formerly Loy Yang Power Ltd, name changed 13 May 1997)

	30 JUNE 1997	30 JUNE 1996
	\$	\$
5 INCOME TAX		
5.1 INCOME TAX EXPENSE		
The prima facie tax on operating profit differs from the income tax provided in the accounts as follows:		
Prima facie income tax expense on operating profit .....	18,784,598	66,684,165
Increase in income tax expense due to permanent differences		
Depreciation on buildings.....	0	448,098
Tax on provisions not carried forward.....	395,157	620,720
Provisions for restoration--non-deductible.....	125,468	175,082
Non-deductible expenditure.....	2,499,703	0
Entertainment and other non-deductible items .....	79,411	30,561
Under/(over) provision last year .....	211,418	0
Decrease in income tax expense due to permanent differences ...		
Tax exempt income.....	0	(292,629)
Research and development concession .....	(58,833)	(93,377)
General investment allowance .....	0	(25,122)
Depreciation on buildings.....	(377,218)	0
TOTAL INCOME TAX EXPENSE ATTRIBUTABLE TO OPERATING PROFIT .....	21,658,694	67,547,498
Prima facie income tax expense on extraordinary item .....	480,906,949	0
Decrease in income tax expense due to permanent differences ...		
Non-assessable income on sale of business .....	(97,711,406)	0
TOTAL INCOME TAX EXPENSE ATTRIBUTABLE TO EXTRAORDINARY ITEM.....	383,196,543	0
Total income tax expense is made up of:		
Increase/(decrease) in provision for deferred income tax ....	(136,405,995)	85,298,790
Income tax paid.....	494,975,104	0
(Increase)/decrease future income tax benefit.....	46,286,128	(17,751,292)

404,855,237      67,547,498  
 =====

5.2 ANALYSIS OF TAX BALANCES CARRIED FORWARD

CURRENT

Future income tax benefit, balance at end of year .....	0	1,019,366
Less: provision for deferred income tax, balance at end of year.....	0	451,107
	-----	-----
NET FUTURE INCOME TAX BENEFIT (REFER NOTE 8).....	0	568,259
	=====	=====

NON-CURRENT

Provision for deferred income tax, balance at end of year .....	0	135,954,868
Less: future income tax benefit, balance at end of year .....	0	45,266,762
	-----	-----
NET PROVISION FOR DEFERRED INCOME TAX (REFER NOTE 12) .....	0	90,688,126
	=====	=====

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QUIET LIFE LIMITED  
 ACN 065 381 240

(formerly Loy Yang Power Ltd, name changed 13 May 1997)

	30 JUNE 1997	30 JUNE 1996
	\$	\$
	-----	-----
<b>6 RECEIVABLES</b>		
CURRENT		
Trade debtors (refer note 24.6 for related party component).....	0	69,683,560
Other debtors (refer note 24.6 for related party component).....	0	3,365,329
	-----	-----
	0	73,048,889
	=====	=====
NON-CURRENT		
Trade debtors (refer note 24.6 for related party component).....	0	1,574,810
	=====	=====
<b>7 INVENTORIES</b>		
CURRENT		
General purpose and maintenance stocks at cost.....	0	3,559,857
Less: inventory diminution.....	0	0
	-----	-----
	0	3,559,857
	=====	=====
NON-CURRENT		
General purpose and maintenance stocks at cost.....	0	13,664,090
Less: inventory diminution.....	0	487,975
	-----	-----
	0	13,175,115
	=====	=====
<b>8 OTHER ASSETS</b>		
CURRENT		
Prepayments.....	0	1,146,368
Future income tax benefit (refer note 5.2).....	0	568,259
	-----	-----
	0	1,714,627
	=====	=====
NON-CURRENT		
Unamortised interest rate swap termination losses .....	0	4,827,954
Unamortised futures termination losses.....	0	834,605
	-----	-----
	0	5,662,559
	=====	=====
<b>9 INVESTMENTS</b>		
9.1 NON-CURRENT INVESTMENTS AT COST COMPRISE:		
Unlisted shares in associated companies.....	0	100
	-----	-----

	0	100
	=====	=====
9.2 NON-CURRENT INVESTMENTS IN UNLISTED ASSOCIATED COMPANIES		
PowerWorks Pty. Ltd.		
PowerWorks Pty. Ltd.'s principal activity is to promote the electricity industry to the public		
Ownership interest.....	0%	33%
Investment carrying amount.....	0	100

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QUIET LIFE LIMITED  
ACN 065 381 240  
(formerly Loy Yang Power Ltd, name changed 13 May 1997)

	30 JUNE 1997	30 JUNE 1996
	\$	\$
	-----	-----
The above investment comprised an interest in the ordinary share capital of the associate.		
The balance date of the associate is 30 June, and the associate is incorporated in Australia.		
There were no material post-balance day events or dissimilar accounting policies.		
10 PROPERTY, PLANT AND EQUIPMENT		
Land at cost.....	0	1,588,736
	-----	-----
	0	1,588,736
Buildings at cost.....	0	8,237,289
Less: accumulated depreciation.....	0	457,278
	-----	-----
	0	7,780,011
Plant and equipment at cost.....	0	2,986,003,023
Less: accumulated depreciation.....	0	136,300,056
	-----	-----
	0	2,849,702,967
Plant and equipment under lease at cost*.....	0	274,987,931
Less: accumulated amortisation.....	0	12,314,861
	-----	-----
	0	262,673,070
Mine development at cost.....	0	38,841,697
Less: accumulated amortisation.....	0	1,484,507
	-----	-----
	0	37,357,190
TOTAL PROPERTY, PLANT AND EQUIPMENT AT COST.....	0	3,309,658,676
TOTAL ACCUMULATED DEPRECIATION/AMORTISATION.....	0	150,556,702
	-----	-----
TOTAL WRITTEN DOWN AMOUNT.....	0	3,159,101,974
	=====	=====

\* At 30 June 1996 and until [the] 12 May 1997 the company recorded as an asset plant and equipment which was under lease to either the State Electricity Commission of Victoria or Generation Victoria. The plant was operated in accordance with licences approved by the lessor pending a formal novation of the arrangement. The company's interest in the leased plant was transferred to the purchasers of the business on 12 May 1997.

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QUIET LIFE LIMITED

ACN 065 381 240  
(formerly Loy Yang Power Ltd, name changed 13 May 1997)

	30 JUNE 1997	30 JUNE 1996
	\$	\$
	-----	-----
<b>11 CREDITORS AND BORROWINGS</b>		
<b>CURRENT</b>		
Trade creditors (refer note 24.6 for related party component) ....	0	35,137,803
Bank overdraft (refer note 15.1).....	0	620,133
Shareholder loan (interest free).....	0	1,917,491,710
Interest accrued (refer note 24.6 for related party component) ...	0	23,764,619
Dividend payable (refer note 24.6 for related party component) ...	0	61,686,000
Other loans (refer note 19).....	0	48,889
Other liabilities (refer note 24.6 for related party component and note 17.1 for Accrued Salaries and Wages).....	0	869,322
	-----	-----
	0	2,039,618,478
	=====	=====
<b>NON-CURRENT</b>		
Loans (refer note 19).....	0	1,057,832,534
	-----	-----
	0	1,057,832,534
	=====	=====
<b>12 PROVISIONS</b>		
<b>CURRENT</b>		
Employee entitlements (refer note 17).....	0	7,475,772
Site restoration--mine.....	0	140,000
Redundancies (refer note 17).....	0	1,494,586
	-----	-----
	0	9,110,358
	=====	=====
<b>NON-CURRENT</b>		
Employee entitlements (refer note 17).....	0	5,926,654
Site restoration--power station.....	0	3,734,339
Site restoration--mine.....	0	968,000
Deferred income tax (refer note 5.2).....	0	90,688,128
	-----	-----
	0	101,317,119
	=====	=====
<b>13 SHARE CAPITAL</b>		
<b>AUTHORISED CAPITAL:</b>		
500,000,000 Ordinary Shares of \$1.00 each.....	500,000,000	500,000,000
<b>ISSUED AND PAID UP CAPITAL:</b>		
15 ordinary shares of \$1.00 each, fully paid.....	15	15
<b>14 RETAINED EARNINGS</b>		
Balance at beginning of year.....	50,618,229	50,617,937
Transfer from profit and loss.....	983,176,837	117,688,293
	-----	-----
Total available for appropriation.....	1,033,795,066	168,304,229
Interim dividend paid.....	0	56,000,000
Final dividend paid (1998 Payable).....	1,033,795,066	61,686,000
	-----	-----
BALANCE AT END OF YEAR .....	0	50,618,229
	=====	=====

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QUIET LIFE LIMITED  
ACN 065 381 240  
(formerly Loy Yang Power Ltd, name changed 13 May 1997)

15 STATEMENT OF CASH FLOWS

	30 JUNE 1997	30 JUNE 1996
	\$	\$
	-----	-----

15.1 RECONCILIATION OF CASH

Cash at the end of the financial year as shown in the Statement of Cash Flows is reconciled to the related items in the Balance Sheet as follows:

CASH		
Cash on hand.....	15	7,800
Short term deposits and securities .....	0	650,000
		-----
	15	657,800
OVERDRAFT		
Bank overdraft .....	0	(620,133)
		-----
	0	(620,133)
		-----
	15	37,667
		=====

15.2 RECONCILIATION OF NET CASH FLOWS FROM OPERATING ACTIVITIES WITH OPERATING PROFIT AFTER INCOME TAX

Operating profit after income tax .....	30,619,744	117,686,293
		-----
NON-CASH REVENUES AND EXPENSES, AND REVENUES AND EXPENSES ASSOCIATED WITH FINANCING OR INVESTING ACTIVITIES:		
Depreciation and amortisation expense .....	91,667,166	106,274,931
Income tax expense on operating profit .....	0	67,547,498
Income tax expense on extraordinary item .....	(383,195,543)	0
Interest revenue received .....	(3,057,422)	(1,845,183)
Finance charges .....	181,865,292	126,710,973
Dividend revenue received .....	0	(127,400)
Loss/(profit) on sold and scrapped non-current assets .....	947,326	(50,803)
		-----
	(111,773,181)	298,510,016
ADJUST FOR MOVEMENTS IN ASSETS AND LIABILITIES		
Decrease in operating expenditure accruals .....	(16,467,837)	(30,126,579)
Decrease in deferred income tax .....	(90,688,126)	0
Increase/(decrease) in provisions .....	1,581,423	(4,693,920)
Increase/(decrease) in trust funds and deposits .....	40,956	(711,010)
Decrease in future income tax benefit .....	568,259	0
Decrease in accounts receivable/accrued revenue .....	14,356,026	28,954,710
Increase in prepayments .....	(7,637,788)	(136,169)
Decrease/(increase) in inventory .....	106,709	(227,148)
		-----
	(98,140,378)	(6,940,116)
		-----
NET CASH (USED IN) PROVIDED BY OPERATING ACTIVITIES ..	(179,393,815)	409,256,193
		-----

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QUIET LIFE LIMITED  
ACN 065 381 240

(formerly Loy Yang Power Ltd, name changed 13 May 1997)

15.3 SALE OF BUSINESS

On 12 May 1997, the Company sold all of its business operations. Details of the sale are as follows:

	30 JUNE 1997	30 JUNE 1996
	\$	\$
	-----	-----
PROCEEDS FROM SALE OF THE BUSINESS		
Cash .....	4,484,928,944	0
		-----
	4,484,928,944	0
		-----
BOOK VALUE OF NET ASSETS SOLD		
Cash .....	22,412,523	0
Receivables .....	60,261,829	0



Inventories .....	16,586,135	0
Other assets .....	8,215,997	0
Property, plant and equipment .....	3,083,386,814	0
Creditors and borrowings .....	(21,034,475)	0
Provisions .....	(20,752,516)	0
	-----	-----
	3,149,076,308	0
	-----	-----
PROFIT ON SALE OF BUSINESS (REFER NOTE 4) .....	1,335,852,636	0
	-----	-----

16 EXPENDITURE COMMITMENTS

16.1 CAPITAL EXPENDITURE COMMITMENTS

Outstanding contract commitments for capital expenditure contracted for at balance date but not provided for comprises the following:

Payable not later than one year .....	0	946,000
	-----	-----
	0	946,000
	-----	-----

16.2 NON-CAPITAL EXPENDITURE COMMITMENTS

Outstanding contract commitments for non-capital expenditure contracted for at balance date but provided for comprises the following:

Payable not later than one year .....	0	6,524,000
Payable greater than one and less than two years .	0	1,566,000
	-----	-----
	0	8,090,000
	-----	-----

16.3 LEASE EXPENDITURE COMMITMENTS

Outstanding operating lease (non-cancellable) commitments at balance date but not provided for comprises the following:

Payable not later than one year .....	0	138,000
Payable greater than one and less than two years .	0	145,000
Payable greater than two and less than five years	0	169,000
	-----	-----
	0	452,000
	-----	-----

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16.4 ASSET SALE OBLIGATIONS

The buyers of the company's business were given certain warranties and indemnities that may result in part of the sale price being refunded. The company has been indemnified against these obligations by the State Electricity Commission of Victoria for the purpose of ensuring that it did not pay, and is not perceived to pay, a dividend out of its capital. The indemnity shall in no way limit the company's rights against the Buyers pursuant to the Asset Sale Agreement.

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	30 JUNE 1997	30 JUNE 1996
	\$	\$
	-----	-----
17 EMPLOYEE ENTITLEMENTS		
17.1 AGGREGATE EMPLOYEE ENTITLEMENT		
Current		
Accrued Wages & Salaries (refer note 11) .....	0	185,083
Provision Employee Entitlements (refer note 12) .....	0	7,475,772
Provision Redundancies (refer note 12) .....	0	1,494,586
Non current		
Provision Employee Entitlements (refer note 12) .....	0	5,926,654
	-----	-----
	0	15,082,085
	-----	-----
Accrued Wages and salaries .....	0	185,083
Recreation leave .....	0	6,662,680
Long service leave .....	0	6,739,746
Redundancies .....	0	1,494,586
	-----	-----
	0	15,082,095
	-----	-----

The amounts for long service leave were measured at their present values. The following assumptions were adopted in measuring the present values of the entitlements which were not expected to be paid or settled within 12 months of balance date.

Long Service Leave:

Weighted average rates of increase in annual employee entitlements to settlement of the liabilities .....	0	2.9%
Weighted average discount rates .....	0	8.7%
Weighted average terms to settlement of the liabilities .....	0	11 Years

17.2 SUPERANNUATION FUND

All permanent and directly hired casual employees of the company were entitled to benefits on termination from the Victorian Electricity Industry Superannuation Fund. All casual and permanent employees engaged after 3 October 1994 were members of an accumulation fund. Division D or other external accumulation funds. All other permanent employees were members of Division B or C of the Fund which provided defined benefits in the form of pensions (Division B) or lump sums (Division C).

Both defined benefit schemes are closed to new members. The company contributed to the Fund at the rate of 9.75%.

The effective date of the most recent detailed valuation of the Fund was 30 June 1996. The review was undertaken by William M. Mercer Pty. Ltd. Based on that assessment, the situation for the company as at 30 June 1996 was:

Present value of employees accrued benefits .....	0	54,100,000#
---	---	-------------

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	30 JUNE 1997	30 JUNE 1996
	\$	\$
	-----	-----
Net market value of assets held by the fund to meet future benefit		

payments .....	0	54,600,000#
Excess/(deficit) of present value of employees' benefits over assets held to meet future benefit payments .....	0	500,000#
Vested benefits .....	0	49,300,000#

The present value of employees' accrued benefits is equal to the past membership liability calculated in accordance with Australian Accounting Standard AAS25 "Financial Reporting by Superannuation Plans".

(Vested benefits are those benefits which would have been paid on voluntary termination from the Fund.)

The Company's obligation in respect of superannuation were transferred on 12 May 1997 to the purchasers of the business.

Employer contributions to the fund .....	1,910,364	2,697,272
Additional contributions to the fund to compensate for differences between the resignation and retrenchment benefit, in relation to voluntary retrenchments. ....	244,964	1,228,000

#Note: Asset and benefit figures were unaudited at the time of signing the 1995/96 report. The last full audit was conducted at 30 June 1995.

18 TREASURY

18.1 DERIVATIVES

The company's derivative products were dealt through Treasury Corporation of Victoria (TCV). The only derivative products outstanding as at 30 June 1996 were Interest Rate Swaps. There were no derivatives outstanding at 30 June 1997.

INTEREST RATE SWAPS

Under these swaps, the company agreed with the counterparty to exchange, at specified intervals, the difference between the fixed-rate and floating-rate interest amounts calculated by reference to an agreed notional amount. The notional principal amounts were not exchanged by the parties.

The maturity profile of these swaps in notional principal terms is:

Later than two years and not later than five years .....	0	25,000,000
Later than five years .....	0	195,000,000
	0	220,000,000

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	30 JUNE 1997	30 JUNE 1996
	\$	\$

The following table indicates the type of swaps held by the company and their weighted average interest rates.

Pay-fixed swaps--notional principal amount .....	0	220,000,000
Average pay rate--specific cost .....	0	12.6%
Average receive rate .....	0	7.6%

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	30 JUNE 1997	30 JUNE 1996
	\$	\$
	-----	-----
19 LOANS (REFER NOTE 24.6)		
19.1 LOAN COMPONENTS		
CURRENT LOANS (EXCLUDING SHAREHOLDER LOAN)		
Premium/(discount) on loans.....	0	0
Fixed interest loans.....	0	48,889
Fixed interest bonds.....	0	0
	-----	-----
	0	48,889
NON-CURRENT LOANS		
Premium/(discount) on loans.....	0	38,899,024
Floating rate notes.....	0	249,745,325
Fixed interest bonds.....	0	626,695,000
Capital indexed bonds.....	0	142,428,804
Fixed interest loans.....	0	64,381
	-----	-----
	0	1,057,832,534
	-----	-----
	0	1,057,881,423
	=====	=====
Liabilities in years of maturity, at face value are:		
Not later than one year.....	0	48,889
Later than one year and not later than two years .....	0	353,784,325
Later than two years and not later than five years .....	0	327,721,000
Later than five years.....	0	337,429,000
	-----	-----
	0	1,018,983,214
Plus unamortised adjustments to face value (refer note		
19.2).....	0	38,899,024
	-----	-----
	0	1,057,882,238
	-----	-----
19.2 ADJUSTMENTS TO FACE VALUE OF LOANS		
Current (discount)/premium.....	0	0
Non-Current (discount)/premium.....	0	38,899,024
	-----	-----
	0	38,899,024
	-----	-----
-----		
20 AUDITORS' REMUNERATION		
Amounts received, or due and receivable, by the		
Auditor-General for auditing the financial statements;		
Total amount payable for annual audit fee.....	51,000	52,000

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	30 JUNE 1997	30 JUNE 1996
	\$	\$
	-----	-----
21 DIRECTORS' REMUNERATION		

Amounts paid, or due and payable to the directors of the company .. 137,203 161,500

The number of directors of the company whose annual remuneration (including superannuation contributions, falls within the following bands:

\$ BAND LEVELS	DIRECTORS	DIRECTORS
\$0 - \$10,000.....	3	0
\$20,000 - \$29,999.....	3	3
\$30,000 - \$59,999.....	1	1

During the year period ended 9 May 1997 the company paid premiums for the indemnification and insurance of all directors and officers to the full extent permitted by Corporations Law.

22 EXECUTIVES' REMUNERATION

The number of executives whose remuneration falls within the following bands is set out below:

\$ BAND LEVELS	EXECUTIVES	EXECUTIVES
\$100,000 - \$109,999.....	1	0
\$110,000 - \$119,999.....	0	2
\$120,000 - \$129,999.....	0	1
\$130,000 - \$139,999.....	1	3
\$140,000 - \$149,999.....	1	0
\$150,000 - \$159,999.....	1	0
\$160,000 - \$169,999.....	1	0
\$170,000 - \$179,999.....	0	0
\$190,000 - \$199,999.....	2	0
\$210,000 - \$219,999.....	0	1
\$280,000 - \$289,999.....	1	0

Total remuneration paid, or due and payable by the company or related entities by executive officers of the company whose remuneration exceeds \$100,000..... 1,386,261 974,040

23 SEGMENTS

The company operated entirely in Australia in the production and sale of electricity and coal.

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30 JUNE 1997      30 JUNE 1996  
\$                    \$

24 RELATED PARTY DISCLOSURES

24.1 DIRECTORS OF QUIET LIFE LTD.

COMMENCEMENT      RESIGNATION

DIRECTORS OF QUIET LIFE LTD. DURING THE FINANCIAL YEAR WERE:

Mr. C. Little.....	30 January 1995	13 June 1997
Mr. D. Swan.....	30 January 1995	9 May 1997
Mr. J. C. Richards ....	30 January 1995	9 May 1997
Mr. J. S. Grigg.....	1 May 1995	9 May 1997
Mr. G. Brooke.....	9 May 1997	--
Mr. G. J. Greaves.....	9 May 1997	--
Mr. H. De Jong.....	13 June 1997	--

All directors are non executive.

#### 24.2 TRANSACTIONS WITH DIRECTOR-RELATED ENTITIES

There were no transactions with director-related entities other than transactions on normal commercial terms with the SECV and Department of Treasury and Finance (refer Note 24.4 for related party transactions).

#### 24.3 RESPONSIBLE PERSON AND RELATED PARTIES

The company is a wholly owned subsidiary of the State Electricity Commission of Victoria; an entity which is 100% controlled by the Victorian Government. Statutory Corporations and any other corporate entities owned by the Victorian State government are related parties.

#### 24.4 RELATED PARTY TRANSACTION CATEGORIES

The following types of related party transactions were transacted during the year, on normal commercial terms:

Electricity transmission costs  
Electricity pool costs  
Council rates  
Dividends  
Auditing services  
Brown Coal Royalties  
Technical services  
Payroll tax  
Briquette purchases  
Electricity sales revenue  
Coal sales revenue  
Water purchases and waste water disposals

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Land Tax  
Land leases  
Provision of loan facilities  
Gas purchases  
Superannuation payments  
Victorian equivalent income tax  
Vehicle registration charges  
In addition there was an interest free loan from the shareholder (Note 11).

#### 24.5 OPERATING PROFIT AND LOSS TRANSACTIONS WITH RELATED PARTIES

Interest revenue.....	3,057,422	1,163,621
Interest expense.....	181,865,292	126,710,973
Dividend Revenue.....	--	127,400

#### 24.6 RECEIVABLES AND PAYABLES AT BALANCE DATE AGGREGATE RELATED PARTY RECEIVABLES AT BALANCE

DATE

Current.....	0	57,507,840
Non-current ..	0	1,566,127
	-----	-----
	0	59,073,967
	=====	=====

AGGREGATE RELATED PARTY PAYABLES AT BALANCE DATE

Current.....	0	1,994,184,280
Non-current.....	0	1,058,296,080
	-----	-----
	0	3,052,480,360
	=====	=====

25.0 INTERESTS HELD

There were no interests held in any related party other than those disclosed as investments in Note 9 (1996 only).

25.1 ANNUAL FINANCIAL STATEMENT CONSOLIDATION ELIMINATION ENTRIES

During the 1996/97 financial year, transactions were undertaken with other State Government controlled entities, giving rise to the need for elimination entries in relation to resultant account balances.

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The aggregate eliminations included within the consolidation worksheets required to be prepared for input to the State's Annual Financial Statements are as follows:

	INTER	INTRA
	-----	-----
Assets.....	0	0
Liabilities.....	0	0
Revenues.....	77,830,616	0
Expenses.....	589,378,744	0
Dividends Paid.....	1,095,481,066	0
	-----	-----

The preparation of prior period comparative information has not been practicable or relevant for this financial year.

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AUDITOR-GENERAL'S REPORT

AUDIT SCOPE

The accompanying financial statements of Quiet Life Limited (formerly Loy Yang Power Limited) for the year ended 30 June 1997, comprising a profit and loss statement, balance sheet, statement of cash flows and notes to the financial statements, have been audited. The company's directors are responsible for the preparation and presentation of the financial statements and the information they contain. An independent audit of these financial statements has been carried out in order to express an opinion on them to the members of the company as required by the Corporations Law and Audit Act 1994.

The audit has been conducted in accordance with Australian Auditing Standards to provide reasonable assurance as to whether the financial statements are free of material misstatement. The audit procedures included an examination, on a test basis, of evidence supporting the amounts and other disclosures in the financial statements, and the evaluation of accounting policies and significant accounting estimates. These procedures have been undertaken to form an opinion as to whether, in all material respects, the financial statements are presented fairly in accordance with the basis on which the accounts have been prepared, namely applicable Accounting Standards, other mandatory professional reporting requirements and comply with the Corporations Law, so as to present a view which is consistent with my understanding of the company's financial position and the results of its operations and its cash flows.

The audit opinion expressed on the financial statements has been formed on the above basis.

AUDIT OPINION

In my opinion, the financial statements of Quiet Life Limited (formerly Loy Yang Power Limited) are properly drawn up:

- (a) so as to give a true and fair view of:
  - (i) the company's state of affairs as at 30 June 1997 and of its profit and cash flows for the financial year ended on that date; and
  - (ii) the other matters required by Divisions 4, 4A and 4B of Part 3.6 of the Corporations Law to be dealt with in the financial statements;
- (b) in accordance with the Corporations Law; and
- (c) in accordance with applicable Accounting Standards and other mandatory professional reporting requirements.

/s/ C.A. BARAGWANATH

-----  
C.A. BARAGWANATH  
Auditor-General

MELBOURNE  
29/8/1997

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LOY YANG POWER ANNUAL REPORT 1995/96

PROFIT AND LOSS STATEMENT FOR THE YEAR ENDED 30 JUNE 1996

NOTES	30 JUNE 1996 \$'000	30 JUNE 1995 \$'000
-----	-----	-----



OPERATING REVENUE.....	2	574,009	244,275
Operating Profit before Income Tax.....	3	185,233	79,579
Income Tax Attributable to Operating Profit.....	4	67,547	29,861
OPERATING PROFIT AFTER INCOME TAX.....		117,686	50,618
Retained Profits at beginning of year .....	13	50,618	0
Dividends Paid or Payable.....		117,686	0
Retained Profits at End of Year.....		50,618	50,618

This Profit and Loss Statement should be read in conjunction with the Notes to and forming part of the Financial Statements.

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FINANCIAL STATEMENTS 1995/96

BALANCE SHEET AS AT 30 JUNE 1996

	NOTES	30 JUNE 1996 \$'000	30 JUNE 1995 \$'000
CURRENT ASSETS			
Cash.....	14.1	658	1,015
Receivables.....	5	73,048	100,577
Inventories.....	6	3,560	4,043
Other assets.....	7	1,715	4,155
TOTAL CURRENT ASSETS.....		78,981	109,790
NON-CURRENT ASSETS			
Receivables.....	5	1,575	3,132
Inventories.....	6	13,176	20,101
Other assets.....	7	5,663	0
Investments.....	8	0	128
Property, plant and equipment.....	9	3,159,102	3,245,997
TOTAL NON-CURRENT ASSETS .....		3,179,516	3,269,358
TOTAL ASSETS.....		3,258,497	3,379,148
CURRENT LIABILITIES			
Creditors and borrowings .....	10	2,039,619	2,113,681
Provisions.....	11	9,110	15,060
TOTAL CURRENT LIABILITIES .....		2,048,729	2,128,741
NON-CURRENT LIABILITIES			
Creditors and borrowings .....	10	1,057,833	1,164,699
Provisions.....	11	101,317	35,090
TOTAL NON-CURRENT LIABILITIES.....		1,159,150	1,199,789
TOTAL LIABILITIES.....		3,207,879	3,328,530
NET ASSETS.....		50,618	50,618

## EQUITY

Share capital.....	12	0	0
Retained earnings.....	13	50,618	50,618
		-----	-----
TOTAL EQUITY.....		50,618	50,618
		-----	-----

This Balance Sheet should be read in conjunction with the Notes to and forming part of the Financial Statements.

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## LOY YANG POWER ANNUAL REPORT 1995/96

## STATEMENT OF CASH FLOWS FOR THE YEAR ENDED 30 JUNE 1996

	NOTES	30 JUNE 1996 \$'000	30 JUNE 1995 \$'000
		-----	-----
CASH FLOWS FROM OPERATING ACTIVITIES			
Receipts from customers.....		661,857	262,004
Payments to suppliers and employees.....		(252,601)	(98,270)
		-----	-----
NET CASH FLOW FROM OPERATING ACTIVITIES .....	14.2	409,256	163,734
		-----	-----
CASH FLOWS FROM INVESTING ACTIVITIES			
Payments to acquire property, plant and equipment ....		(8,356)	(5,447)
Proceeds from sale of property, plant and equipment ..		34	117
Proceeds from sale of investments.....		223	0
Dividends received.....		127	0
Net cash allocated.....		0	(629)
		-----	-----
NET CASH FLOW USED IN INVESTING ACTIVITIES.....		(7,972)	(5,959)
		-----	-----
CASH FLOWS FROM FINANCING ACTIVITIES			
Interest and other items of a similar nature received.....		1,907	832
Interest and other costs of finance paid.....		(115,063)	(70,817)
Hedging receipts associated with borrowings .....		20,765	10,980
Hedging payments associated with borrowings .....		(30,861)	(15,490)
Buyback of swaps.....		(7,905)	0
Proceeds from borrowings.....		86,056	49,706
Repayment of borrowings.....		(36,221)	(47,170)
Buyback of borrowings.....		(264,282)	(85,458)
Dividends paid.....		(56,000)	0
		-----	-----
NET CASH FLOW USED IN FINANCING ACTIVITIES.....		(401,604)	(157,417)
		-----	-----
NET INCREASE/(DECREASE) IN CASH HELD.....		(320)	358
		-----	-----
CASH AT BEGINNING OF YEAR.....		358	0
		-----	-----
CASH AT END OF YEAR.....	14.1	38	358
		-----	-----

This Statement of Cash Flows should be read in conjunction with the Notes to and forming part of the Financial Statements.

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## FINANCIAL STATEMENTS 1995/96

## NOTES TO AND FORMING PART OF THE FINANCIAL STATEMENTS

## 1 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

## 1.1 BASIS OF ACCOUNTING

The financial report is a general purpose financial report which has been prepared in accordance with the requirements of the Corporations Law which include disclosures required by Schedule S and applicable Accounting Standards. Other mandatory professional reporting requirements (Urgent Issues Group Consensus Views) have also been complied with.

The report is prepared in accordance with the historical cost convention, except for certain assets which, as noted, are at valuation. The accounting policies are consistent with those of the previous year.

## 1.2 PRIOR PERIOD COMPARISONS

Loy Yang Power Ltd. was incorporated for the twelve months ended 30 June 1995, however the company did not commence trading in its principal activities until 1 February 1995 when substantially all the assets and liabilities of the business were vested in the company pursuant to an Allocation Statement made under the Electricity Industry (Further Amendment) Act 1994.

As a result, comparative profit and loss and cash flow figures reflect five months trading from 1 February 1995 to 30 June 1995.

Comparative information is reclassified where appropriate, to enhance comparability.

## 1.3 PROPERTY, PLANT AND EQUIPMENT

### COST AND VALUATION

Property, plant and equipment are carried at cost.

### DEPRECIATION AND AMORTISATION

Depreciation or amortisation is provided for all fixed assets other than freehold land. The majority of assets are depreciated using the straight line method to write off the cost of assets over their expected service lives. The expenditure associated with mine development costs is amortised on a units of production basis. Depreciation or amortisation for all assets commences on the first day of the month closest to the in-service date.

Changes in depreciation rates and/or depreciable amounts are dealt with on a prospective basis.

## 1.4 RECOVERABLE AMOUNTS

Non-current assets values do not exceed their recoverable amount. Where carrying values exceed their recoverable amount, assets are revalued downwards to the lower value. The expected net cash flows included in determining the recoverable amounts of non-current assets have been discounted to their present value using a market determined risk adjusted discount rate.

## 1.5 INVENTORIES

Costs are assigned to inventories using the average cost method. Inventories are valued at lower of cost and net realisable value. As estimate of items which are likely to be utilised in the next twelve months is classified as current.

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LOY YANG POWER ANNUAL REPORT 1995/96

NOTES TO AND FORMING PART OF THE FINANCIAL STATEMENTS (CONTINUED)

1 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

1.6 ACCOUNTING FOR INCOME TAX

Loy Yang Power Ltd. is subject to the Victorian State Government Tax Equivalent System pursuant to Section 88 of the State Owned Enterprises Act 1992.

Loy Yang Power Ltd. has adopted the liability method of tax-effect accounting whereby income tax is regarded as an expense and is managed with the accounting profit after allowing for permanent differences.

To the extent that timing differences occur between the time items are recognised in the accounts and when these are taken into account in determining taxable income, the net related taxation benefit or liability is disclosed as a future income tax benefit or a provision for deferred income tax. These account balances are calculated with reference to the rates of income tax which are expected to apply when those timing differences reverse.

Future income tax benefits are not brought to account unless realisation of the asset is assured beyond reasonable doubt. The future income tax benefit arising from tax losses is only carried forward as an asset when the benefit is virtually certain of being realised.

#### 1.7 DOUBTFUL DEBTS

The value of estimated doubtful debts is reviewed annually on an individual debtor basis, and appropriate provision is made where necessary.

#### 1.8 NEGOTIABLE SECURITIES

Where interest is paid in advance on negotiable securities the interest is recognised as an asset and progressively charged to the Profit and Loss Statement over the applicable interest period. Interest payable in arrears is progressively charged to the Profit and Loss Statement over the applicable interest period and recognised as a liability.

Discounts and premiums on face value on the issue of negotiable securities are recognised as variations of the liability to which they relate. The variations are amortised over the term of the issue, using the effective yield method.

Changes in the capital value of the outstanding liability on index linked securities are recognised as variations in the book value of the liability and are charged to the Profit and Loss Statement.

Any gains or losses arising from the buyback of negotiable securities issued by Loy Yang Power Ltd. are charged to the Profit and Loss Statement as incurred or earned.

#### 1.9 DERIVATIVES

Loy Yang Power Ltd. is exposed to changes in interest rates and commodity prices from its activities. It is Loy Yang Power Ltd.'s policy to use derivative financial instruments to hedge these risks. Loy Yang Power Ltd. does not enter, hold or issue derivative financial instruments for trading or speculative purposes.

Derivative financial instruments include forward rate agreements, futures, options, interest rate swaps and their Treasury Corporation of Victoria equivalents.

Gains and losses arising from the early termination of general hedges are amortised over the period of the hedge. The exception to this is bond futures where gains and losses are amortised over the average term to maturity of existing fixed debt.

Gains and losses arising from the early termination of specific hedges are amortised over the shorter of the period of the borrowing being hedged or the period of the hedge.

## FINANCIAL STATEMENTS 1995/96

## NOTES TO AND FORMING PART OF THE FINANCIAL STATEMENTS (CONTINUED)

## 1 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

## 1.10 EMPLOYEE ENTITLEMENTS

## WAGES, SALARIES AND LEAVE

Provision is made for employee entitlement benefits accumulated as a result of employees rendering services up to the reporting date. These benefits include wages and salaries, annual leave and associated oncosts.

Liabilities arising in respect of wages and salaries, annual leave and any other employee entitlements expected to be settled within twelve months of the reporting date are measured at their nominal amounts. All other employee entitlement liabilities are measured at the present value of their estimated future cash outflows to be made in respect of services provided by employees up to the reporting date. In determining the present value of future cash outflows, the interest rates attaching to Federal Government Guaranteed Securities which have terms to maturity approximating the terms of the related liability are used.

Employee entitlement expenses are revenues arising in respect of the following categories:

- o wages and salaries, non-monetary benefits, annual leave, long service leave, sick leave and other leave entitlements; and
- o other types of employee entitlements;

are charged to the Profit and Loss Statement on a net basis in their respective categories.

## SUPERANNUATION

Loy Yang Power Ltd. contributes towards the Victorian Electricity Industry (VEI) Superannuation Fund on behalf of its employees. These contributions are charged to the Profit and Loss Statement as the liability arises (refer note 17.2).

## 1.11 PROVISION FOR SITE RESTORATION: POWER STATION AND MINE

Recognition of a liability for the cost of restoring the power station and mine sites to an acceptable environmental standard at the end of their useful lives has been provided for in these accounts (refer notes 11 and 16). This liability includes costs of reclamation, plant closure and dismantling, and waste site closure.

The liability is recognised on a gradual basis and is calculated by discounting the estimated future site restoration costs to their net present value. Annual increments to the liability for each site are charged to the Profit and Loss Statement over the estimated remaining life of each site.

Expected future payments for site restoration are discounted using interest rates attaching, as at the reporting date, to Federal Government Guaranteed Securities with terms to maturity that match, as closely as possible, the estimated future cash outflows.

Cost estimates are based on the assumption that current legal requirements and/or technologies will not change significantly over the life of the power station and mine sites.

Changes in estimates are dealt with on a prospective basis.

1.12 CASH

For the purpose of the Statement of Cash Flows, cash includes cash on hand and in banks, investments in money market instruments and short-term deposits and securities, net of outstanding overdrafts.

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LOY YANG POWER ANNUAL REPORT 1995/96

NOTES TO AND FORMING PART OF THE FINANCIAL STATEMENTS (CONTINUED)

	30 JUNE 1996 \$'000	30 JUNE 1995 \$'000
	-----	-----
2 OPERATING REVENUE COMPRISES		
Sales revenue.....	557,500	238,468
Interest revenue (refer note 25.5) .....	1,845	637
Proceeds from the sale of non-current assets.....	587	117
Dividend revenue.....	127	0
Other revenue.....	13,950	5,053
	-----	-----
	574,009	244,275
	=====	=====

3 OPERATING PROFIT

The operating profit before income tax is arrived at after charging/(crediting) the following items:

DEPRECIATION, AMORTISATION AND DIMINUTION

Plant and equipment.....	96,219	40,255
Development of mine (amortisation).....	1,058	427
Leased plant and equipment (amortisation).....	8,678	3,637
Buildings.....	320	137
Diminution in value of inventories.....	0	727
	-----	-----
TOTAL DEPRECIATION, AMORTISATION AND DIMINUTION .....	106,275	45,183
	=====	=====

AMOUNTS SET ASIDE TO PROVISIONS

Bad and doubtful debts.....	0	0
Employee entitlements.....	4,492	1,170
Site restoration--power station.....	486	430
Site restoration--mine .....	247	356
	-----	-----
TOTAL AMOUNT SET ASIDE TO PROVISIONS .....	5,225	1,956
	=====	=====

INTEREST EXPENSE (REFER NOTE 25.5).....	126,711	59,145
GOVERNMENT MINING ROYALTIES INCURRED.....	9,242	3,654
ENERGY CONSUMPTION LEVY.....	30	7
SUPERANNUATION CONTRIBUTIONS.....	2,697	1,194
RENTAL OPERATING LEASES.....	419	233
PROFIT/(LOSS) ON SALE OF NON-CURRENT ASSETS.....	51	(16)
RESEARCH AND DEVELOPMENT EXPENDITURE.....	519	0

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FINANCIAL STATEMENTS 1995/96

NOTES TO AND FORMING PART OF THE FINANCIAL STATEMENTS (CONTINUED)

	30 JUNE 1996 \$'000	30 JUNE 1995 \$'000
	-----	-----

4 INCOME TAX

4.1 INCOME TAX EXPENSE

The prima facie tax on operating profit differs from the income tax provided in the accounts as follows:

Prima facie income tax expense calculated at 36% (1995: 33%) on the operating profit.....	66,684	26,261
Increase in income tax expense due to permanent differences		
Depreciation on buildings.....	448	281
Tax on provisions not carried forward.....	621	280
Provisions for restoration--non-deductible .....	175	142
Entertainment and other non-deductible items .....	31	444
Decrease in income tax expense due to permanent differences		
Tax exempt income.....	(293)	0
Research and development concession.....	(94)	0
General investment allowance.....	(25)	0
Depreciation on buildings.....	0	(328)
Add: Restatement of deferred tax balances due to change in income tax rate.....	0	1,881
	-----	-----
TOTAL INCOME TAX EXPENSE ATTRIBUTABLE TO OPERATING PROFIT .....	67,547	28,961
	=====	=====
Total income tax expense is made up of:		
Deferred income tax provision.....	85,298	51,107
Less: future income tax benefit.....	17,751	22,146
	-----	-----
	67,547	28,961
	=====	=====

4.2 ANALYSIS OF TAX BALANCES CARRIED FORWARD

CURRENT		
Future income tax benefit, balance at end of year.....	1,019	3,505
Less: provision for deferred income tax, balance at end of year .....	450	360
	-----	-----
NET FUTURE INCOME TAX BENEFIT (REFER NOTE 7).....	569	3,145
	=====	=====
NON-CURRENT		
Provision for deferred income tax, balance at end of year .....	135,955	50,747
Less: future income tax benefit, balance at end of year.....	45,267	25,030
	-----	-----
NET PROVISION FOR DEFERRED INCOME TAX (REFER NOTE 11) .....	90,688	25,717
	=====	=====

The future income tax benefit will only be obtained if:

- a) future assessable income is derived of a nature and of an amount sufficient to enable the benefit to be realised;
- b) the conditions for deductibility imposed by tax legislation continue to be complied with; and
- (c) no changes in tax legislation adversely affect Loy Yang Power Ltd. in realising the benefit.

5 RECEIVABLES

CURRENT		
Trade debtors (refer note 25.6).....	69,684	97,843
Other debtors (refer note 25.6).....	3,364	2,734
	-----	-----
	73,048	100,577
	=====	=====
NON-CURRENT		
Trade debtors (refer note 25.6).....	1,575	3,132
Other debtors (refer note 25.6).....	0	0
	-----	-----
	1,575	3,132
	=====	=====

NOTES TO AND FORMING PART OF THE FINANCIAL STATEMENTS (CONTINUED)

	30 JUNE, 1996	30 JUNE, 1995
	\$'000	\$'000
	-----	-----
6 INVENTORIES		
CURRENT		
General purpose and maintenance stocks at cost.....	3,560	4,043
Less: inventory diminution.....	0	0
	-----	-----
	3,560	4,043
	=====	=====
NON-CURRENT		
General purpose and maintenance stocks at cost.....	13,664	20,828

Less: inventory diminution.....	488	727
	-----	-----
	13,176	20,101
	-----	-----

A review undertaken during the year identified 57.6 million of items that should correctly be identified as depreciable spares. This amount has been transferred to property, plant and equipment.

7 OTHER ASSETS		
Current		
Prepayments.....	1,146	1,010
Future income tax benefit (refer note 4.2).....	569	3,145
	-----	-----
	1,715	4,155
	-----	-----
NON-CURRENT		
Unamortized interest rate swap termination losses.....	4,828	0
Unamortized futures termination losses.....	835	0
	-----	-----
	5,663	0
	-----	-----

8 INVESTMENTS		
8.1 NON-CURRENT INVESTMENTS AT COST COMPRISE:		
Unlisted shares.....	0	128
Unlisted shares in associated companies.....	0	0
	-----	-----
	0	128
	-----	-----
8.2 NON-CURRENT INVESTMENTS IN UNLISTED ASSOCIATED COMPANIES		
PowerWorks Pty. Ltd. ....		
PowerWorks Pty. Ltd's principal activity is to promote the electricity industry to the public		
Ownership interest.....	33.3%	33.3%
Investment carrying amount.....	0.1	0.1

The above investment is held by Loy Yang Power Ltd. and is comprised of interest in the ordinary share capital of the associate.

The balance date of the associate is 30 June, and the associate is incorporated in Australia.

There are no material post-balance day events or dissimilar accounting policies.

During the period, unlisted shares held at cost were sold for \$223,296

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FINANCIAL STATEMENTS 1995/96

NOTES TO AND FORMING PART OF THE FINANCIAL STATEMENTS (CONTINUED)

	30 JUNE 1996 \$'000	30 JUNE 1995 \$'000
	-----	-----
9 PROPERTY, PLANT AND EQUIPMENT AT COST		
Land at cost.....	1,589	1,589
	-----	-----
Buildings at cost	1,589	1,589
Less: accumulated depreciation.....	8,237	8,237
	457	137
	-----	-----
Plant and equipment at cost.....	7,780	8,100
Less: accumulated depreciation.....	2,986,003	2,966,792
	136,300	40,250
	-----	-----
Plant and equipment under lease at cost (refer note 15.3) .....	2,849,703	2,926,542
Less: accumulated amortisation.....	274,988	274,988
	12,315	3,637
	-----	-----
Mine development at cost.....	262,673	271,351
Less: accumulated amortisation.....	38,842	38,842
	1,485	427
	-----	-----
Total Fixed Assets at Cost.....	37,357	38,415
Total Accumulated Depreciation/Amortisation.....	3,309,659	3,290,448
	150,557	44,451
	-----	-----



Total Written Down Amount.....	3,159,102	3,245,997
-----		
10 CREDITORS AND BORROWINGS		
CURRENT		
Trade creditors (refer note 25.6).....	35,138	61,047
Bank overdraft (refer note 14.1).....	620	657
Shareholder loan*.....	1,917,492	1,917,492
Interest accrued (refer note 25.6).....	23,765	30,819
Dividend payable (refer note 25.6).....	61,686	0
Other loans (refer note 20).....	49	102,091
Other liabilities (refer note 25.6).....	869	1,580
	-----	-----
	2,039,619	2,113,681
	-----	-----
NON-CURRENT		
Loans (refer note 20).....	1,057,833	1,164,699
	-----	-----
	1,057,833	1,164,699
	-----	-----

There are no guarantees or securities over assets with respect to borrowings.

\*In accordance with the Electricity Industry (Further Amendment) Act 1994 section 153F and the Electricity Industry (Amendment) Act 1995 section 153W, the shareholder loan is an amount owing to the State Electricity Commission of Victoria and, whilst the loan holds a legal obligation, it holds no interest payable and no term is specified for repayment. Loy Yang Power Ltd., however, will be making repayments against the shareholder loan in 1996/97.

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LOY YANG POWER ANNUAL REPORT 1995/96

NOTES TO AND FORMING PART OF THE FINANCIAL STATEMENTS (CONTINUED)

	30 JUNE 1996 \$'000	30 JUNE 1995 \$'000
	-----	-----
11 PROVISIONS		
CURRENT		
Employee entitlements (refer note 17).....	7,476	7,587
Uninsured losses.....	0	75
Site restoration--mine (refer note 16).....	140	60
Redundancies.....	1,494	7,338
	-----	-----
	9,110	15,060
	-----	-----
NON-CURRENT		
Employee entitlements (refer note 17).....	5,927	5,219
Site restoration--power station (refer note 16) .	3,734	3,248
Site restoration--mine (refer note 16).....	968	906
Deferred income tax (refer note 4.2).....	90,688	25,717
	-----	-----
	101,317	35,090
	-----	-----
-----		
12 SHARE CAPITAL		
AUTHORISED CAPITAL		
500,000,000 Ordinary Shares of \$1.00 each .....	500,000	500,000
ISSUED AND PAID UP CAPITAL		
15 ordinary shares of \$1.00 each, fully paid ....	0	0
(Balance not shown due to rounding)		
	-----	-----

13 RETAINED EARNINGS

Balance at Beginning of Year.....	50,618	0
Transfer from profit and loss.....	117,686	50,618
	-----	-----
Total available for appropriation.....	168,304	50,618
Interim dividend paid.....	56,000	0
Final dividend payable.....	61,686	0
	-----	-----
BALANCE AT END OF YEAR.....	50,618	50,618
	-----	-----

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FINANCIAL STATEMENTS 1995/96

NOTES TO AND FORMING PART OF THE FINANCIAL STATEMENTS (CONTINUED)

	30 JUNE 1996 \$'000	30 JUNE 1995 \$'000
	-----	-----
14 STATEMENT OF CASH FLOWS		
14.1 RECONCILIATION OF CASH		
Cash at the end of the financial year as shown in the Statement of Cash Flows is reconciled to the related items in the Balance Sheet as follows:		
CASH		
Cash on hand.....	8	8
Short term deposits and securities.....	650	1,007
	-----	-----
	658	1,015
OVERDRAFT		
Bank overdraft.....	(620)	(657)
	-----	-----
	(620)	(657)
	-----	-----
	38	358
	-----	-----
Loy Yang Power Ltd. has a bank overdraft facility of \$5 million (1995: \$10 million) arranged with the National Australia Bank. \$4.4 million of the facility is available at 30 June 1996.		
14.2 RECONCILIATION OF NET CASH FLOWS FROM OPERATING ACTIVITIES		
Operating profit after income tax.....	117,686	50,618
	-----	-----
Non-cash revenues and expenses, and revenues and expenses associated with financing or investing activities:		
Depreciation and amortisation expense.....	106,275	44,456
Income tax expense.....	67,547	28,961
Interest revenue received.....	(1,845)	(912)
Finance charges.....	126,711	59,145
Dividend revenue received.....	(127)	0
Loss/(profit) on sold and scrapped non-current assets.....	(51)	16
	-----	-----
	298,510	131,666
ADJUST FOR MOVEMENTS IN ASSETS AND LIABILITIES		
Increase/(decrease) in operating expenditure accruals.....	(30,126)	29,572
Increase/(decrease) in provisions.....	(4,694)	(8,343)
Increase/(decrease) in trust funds and deposits.....	(711)	1,308
Decrease/(increase) in accounts receivable/accrued revenue .....	28,954	(41,753)
Decrease/(increase) in prepayments.....	(136)	1,474
Decrease/(increase) in inventory.....	(227)	(808)
	-----	-----
	(6,940)	(18,550)
	-----	-----
NET CASH PROVIDED BY OPERATING ACTIVITIES.....	409,256	163,734
	-----	-----

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NOTES TO AND FORMING PART OF THE FINANCIAL STATEMENTS (CONTINUED)

	30 JUNE 1996 \$'000	30 JUNE 1995 \$'000
	-----	-----
15 EXPENDITURE COMMITMENTS		
15.1 CAPITAL EXPENDITURE COMMITMENTS		
Outstanding contract commitments for capital expenditure contracted for at balance date but not provided for comprises the following:		
Payable not later than one year.....	946	596
	-----	-----
	946	596
	-----	-----
15.2 NON-CAPITAL EXPENDITURE COMMITMENTS		
Outstanding contract commitments for non-capital expenditure contracted for at balance date but not provided for comprises the following:		
Payable not later than one year.....	6,524	3,938
Payable greater than one and less than two years.....	1,566	0
	-----	-----
	8,090	3,938
	-----	-----
15.3 LEASE EXPENDITURE COMMITMENTS		
Outstanding operating lease (non-cancellable) commitments at balance date but not provided for comprises the following:		
Payable not later than one year.....	138	0
Payable greater than one and less than two years.....	145	0
Payable greater than two and less than five years.....	169	0
	-----	-----
	452	0
	-----	-----

Loy Yang Power Ltd. holds \$263 million of plant disclosed as leased assets in note 9. The leases for these assets have not yet been novated to Loy Yang Power Ltd., and they remain with the current lessees being either the State Electricity Commission of Victoria or Generation Victoria. As a consequence Loy Yang Power Ltd. has no lease liability in respect to these leases. Loy Yang Power Ltd. and the State Electricity Commission of Victoria are progressing issues to achieve their formal novation to Loy Yang Power Ltd. The lessors have given their conditional consent for Loy Yang Power Ltd. to use the assets until such time as the leases are formally novated.

Included in the above is a lease relating to an individual asset valued at \$67.7 million (written down value) which has an expiry date of 31 December 1999 unless not renewed by the lessor with effect from 30 June 1996. The renewal option is yet to be exercised. The lessor's consent for Loy Yang Power Ltd. to use the asset continues.

-----

16 SITE RESTORATION COSTS--POWER STATION AND MINE

Provision for site restoration of the power station and mine sites of \$4.8 million has been provided for in the accounts as at 30 June 1996. The total net present value of estimated future cash outflows for site restoration is \$26 million.

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FINANCIAL STATEMENTS 1995/96

NOTES TO AND FORMING PART OF THE FINANCIAL STATEMENTS (CONTINUED)

30 JUNE 1996 \$'000	30 JUNE 1995 \$'000
-----	-----

17 EMPLOYEE ENTITLEMENTS

17.1 AGGREGATE EMPLOYEE ENTITLEMENT

Wages and salaries.....	185	219
Recreation leave.....	6,663	6,176
Long service leave.....	6,740	6,630
Redundancies.....	1,494	7,338
	-----	-----
	15,082	20,363
	-----	-----

The amounts for long service leave are measured at their present values. The following assumptions were adopted in measuring the present values of the entitlements which are not expected to be paid or settled within 12 months of balance date.

LONG SERVICE LEAVE

Weighted average rates of increase in annual employee entitlements to settlement of the liabilities .....	2.9%	4.0%
Weighted average discount rates .....	8.7%	8.8%
Weighted average terms to settlement of the liabilities .....	11 years	11 years

17.2 SUPERANNUATION FUND

All permanent and directly hired casual employees of Loy Yang Power Ltd. are entitled to benefits on termination from the Victorian Electricity Industry Superannuation Fund. All casual and permanent employees engaged after 3 October 1994 are members of an accumulation fund, Division D or other external accumulation funds. All other permanent employees are members of Division B or C of the Fund which provide defined benefits in the form of pensions (Division B) or lump sums (Division C). Both defined benefit schemes are closed to new members. During July 1995 the company contributed to the Fund at the rate of 10% for the defined benefit schemes, and thereafter at a rate of 9.75%. Contributions in excess of those required by the Superannuation Guarantee Charge Act 1992 (6%) are not legally enforceable.

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LOY YANG POWER ANNUAL REPORT 1995/96

NOTES TO AND FORMING PART OF THE FINANCIAL STATEMENTS (CONTINUED)

	30 JUNE 1996 \$'000	30 JUNE 1995 \$'000
	-----	-----
17 EMPLOYEE ENTITLEMENTS (CONTINUED)		
17.2 SUPERANNUATION FUND (CONTINUED)		
The effective date of the most recent detailed valuation of the Fund was 30 June 1996. The review was undertaken by William M. Mercer Pty Ltd. Based on that assessment, the situation for the company as at 30 June 1996 was:		
Present value of employees accrued benefits.....	54,100*	45,800
Net market value of assets held by the fund to meet future benefit payments.....	54,600*	47,500
Excess/(deficit) of present value of employees' benefits over assets held to meet future benefit payments.....	500*	1,700
Vested benefits.....	49,300*	45,700

The present value of employees' accrued benefits is equal to the past membership liability calculated in accordance with Australian Accounting Standard AAS25 "Financial Reporting by Superannuation Plans". (Vested benefits are those benefits which would have been paid on voluntary termination from the Fund.)

Employer contributions to the fund.....	2,697	1,194
Additional contributions to the fund to compensate for differences between the resignation and retrenchment benefit, in relation to voluntary retrenchments.....	1,228	1,140

\*Note: Asset and benefit figures are unaudited at the time of signing this report. The last full audit was conducted at 30 June 1995.

18 CONTINGENT EVENTS

18.1 Loy Yang Power Ltd. was allocated its assets and liabilities from Generation Victoria through an allocation statement in accordance with the Electricity Industry (Further Amendment) Act 1994. Under section

153B of this Act, the allocation statement may be amended at any time at the direction of the Victorian Government Treasurer and relevant Minister.

18.2 Upon the disaggregation of the State Electricity Commission of Victoria (SECV) on 3 January 1994, Generation Victoria entered into a contract with the SECV to meet the SECV's obligations under its contracts for the supply of coal and infrastructure services to the Loy Yang B Joint Venture in consideration of receipt of all SECV's revenues under those contracts. Upon the disaggregation of Generation Victoria on 31 January 1995, Generation Victoria's rights and obligations were allocated to Loy Yang Power Ltd.

Under the contract Loy Yang Power Ltd. is directly liable to the SECV to use its "best endeavours", backed by an indemnity in favour of the SECV for performance of these obligations, subject only to force majeure relief. A failure by Loy Yang Power Ltd. to use its "best endeavours" may result in liabilities being imposed on Loy Yang Power Ltd. At the time of preparation of this report, Loy Yang Power Ltd. is not aware of any breaches of performance obligations on its part.

The SECV remains the contracting party under the contracts with the Loy Yang B Joint Venture.

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FINANCIAL STATEMENTS 1995/96

NOTES TO AND FORMING PART OF THE FINANCIAL STATEMENTS (CONTINUED)

	30 JUNE 1996	30 JUNE 1995
	\$'000	\$'000
	-----	-----

19 TREASURY

19.1 LOY YANG POWER LTD. DERIVATIVES

Loy Yang Power Ltd.'s derivative products are dealt through Treasury Corporation of Victoria (TCV). The only derivative products outstanding as at 30 June 1996 were Interest Rate Swaps.

INTEREST RATE SWAPS

Under these swaps, Loy Yang Power Ltd. agrees with the counterpart to exchange, at specified intervals, the difference between the fixed-rate and floating-rate interest amounts calculated by reference to an agreed notional amount. The notional principal amounts are not exchanged by the parties.

The maturity profile of these swaps in notional principal terms is:

Later than two years and not later than five years.....	25,000	33,744
Later than five years.....	195,000	245,000
	-----	-----
	220,000	278,744
	-----	-----

The following table indicates the type of swaps held by Loy Yang Power Ltd. and their weighted average interest rates.

Pay-fixed swaps: notional principal amount.....	220,000	278,744
Average pay rate: Loy Yang Power Ltd. specific cost.....	12.6%	12.5%
Average receive rate.....	7.6%	7.7%

Loy Yang Power Ltd.'s credit exposures on these swaps is nil as the counterpart in each case is TCV.

VIC INTEREST RATE FORWARDS & VIC HOTSTOCK FORWARDS

The maturity profile in notional principal amount terms, of these Interest Rate and Hotstock Forwards is:

Not Later than one year.....	0	90,000
	-----	-----
	0	90,000
	-----	-----

Both Vic Interest Rate Forwards and Vic Hotstock Forwards were created

by TCV for use by their Participating Authorities following the State Treasurer's instructions that TCV Participating Authorities were to no longer deal in derivative products directly with the financial markets from 1 July 1995.

Vic Interest Rate Forwards are similar to Bill Futures except that there are no initial and variation margins to be paid by either counterpart. Vic Hotstock Forwards are similar to Bond Futures except the maturity dates are specific to TCV's physical hotstocks.

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LOY YANG POWER ANNUAL REPORT 1995/96

NOTES TO AND FORMING PART OF THE FINANCIAL STATEMENTS (CONTINUED)

	30 JUNE 1996 \$'000	30 JUNE 1995 \$'000
20 LOANS (refer note 25.6)		
20.1 LOAN COMPONENTS		
CURRENT LOANS		
Premium/(discount) on loans.....	0	1,782
Fixed interest loans.....	49	88
Fixed interest bonds.....	0	100,221
	49	102,091
NON-CURRENT LOANS		
Premium/(discount) on loans .....	38,899	39,055
Floating rate notes .....	249,745	334,746
Fixed interest bonds .....	626,695	654,895
Capital indexed bonds .....	142,429	135,890
Fixed interest loans .....	65	113
	1,057,833	1,164,699
	1,057,882	1,266,790
Liabilities in years of maturity, at face value are:		
Not later than one year.....	49	100,309
Later than one year and not later than two years .....	353,784	21,249
Later than two years and not later than five years .....	327,721	813,505
Later than five years.....	337,429	290,890
	1,018,983	1,225,953
Plus unamortised adjustments to face value (refer note 20.2).....	38,899	40,837
	1,057,882	1,266,790
20.2 ADJUSTMENTS TO FACE VALUE OF LOANS		
Current (discount)/premium.....	0	1,782
Non-Current (discount)/premium.....	38,899	39,055
	38,899	40,837

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FINANCIAL STATEMENTS 1995/96

NOTES TO AND FORMING PART OF THE FINANCIAL STATEMENTS (CONTINUED)

30 JUNE 1996 \$'000	30 JUNE 1995 \$'000
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20 LOANS (CONTINUED)

20.3 SECURITY--LOANS

All loan funding for Loy Yang Power Ltd. is arranged via Treasury Corporation of Victoria (TCV). Legal inability to the end investor for Loy Yang Power Ltd. loans rests with TCV.

These loans are guaranteed by the State Government of Victoria. In return Loy Yang Power Ltd. pays a financial accommodation levy to the State Government which increases the cost of debt to reflect market rates, based on an assessment of credit risk. For debt novated to TCV, back-to-back loans have been established between Loy Yang Power Ltd. and TCV. Pursuant to Section 36D of the Treasury Corporation of Victoria (Debt Centralisation) Act 1993, Loy Yang Power Ltd. will reimburse TCV for all settlement amounts relating to these loans.

21 AUDITORS' REMUNERATION

Amounts received, or due and receivable, by the Auditor-General for auditing the financial statements:

Total amount payable for annual audit fee .....	52	62
---	----	----

22 DIRECTORS' REMUNERATION

Amounts received, or due and receivable, by the directors of

Loy Yang Power Ltd. ....	162	56
--------------------------	-----	----

The number of directors of Loy Yang Power Ltd. whose annual remuneration (including superannuation contributions) falls within the following bands:

\$ Band levels	Directors	Directors
\$30,000 - \$39,999 .....	3	3
\$60,000 - \$69,999 .....	1	1

During the year Loy Yang Power Ltd. paid premiums for the indemnification and insurance of all directors and officers of Loy Yang Power Ltd. to the full extent permitted by Corporations Law.

The directors have applied ASC Class Order 95/741 in the disclosure of directors' remuneration.

23 EXECUTIVES' REMUNERATION

The number of executives of Loy Yang Power Ltd. whose remuneration falls within the following bands is set out below:

\$ BAND LEVELS	EXECUTIVES	EXECUTIVES
\$100,000 - \$109,999 .....	0	1
\$110,000 - \$119,999 .....	2	4
\$120,000 - \$129,999 .....	1	0
\$130,000 - \$139,999 .....	3	1
\$200,000 - \$209,999 .....	0	1
\$210,000 - \$219,999 .....	1	0

Total remuneration received, or due and receivable, from Loy Yang Power Ltd. or related entities by executive officers of Loy Yang Power Ltd. whose remuneration exceeds \$100,000: .....

974	890
-----	-----

1994/95 amounts represent annual equivalents.

1995/96 amounts represent 12 months actual.

LOY YANG POWER ANNUAL REPORT 1995/96

NOTES TO AND FORMING PART OF THE FINANCIAL STATEMENTS (CONTINUED)

24 SEGMENTS

Loy Yang Power Ltd. operated entirely in Australia in the production and sale of electricity and coal.

25 RELATED PARTY DISCLOSURES

25.1 DIRECTORS OF LOY YANG POWER LTD.

Directors of Loy Yang Power Ltd. during the financial year were:

Mr. C. Little

Mr. D. Swan  
 Mr. J. C. Richards  
 Mr. J. S. Grigg

All directors are non executive.

25.2 TRANSACTIONS WITH DIRECTOR-RELATED ENTITIES

There were no transactions with director-related entities.

25.3 WHOLLY OWNED GROUP

The wholly owned group comprises the ultimate holding entity of Loy Yang Power Ltd., the Victorian State Government, and therefore all Victorian State Government Departments, Statutory Corporations and any other corporate entities owned by the Victorian State Government are related parties.

25.4 RELATED PARTY TRANSACTION CATEGORIES

The following types of related party transactions were transacted during the year, on normal commercial terms:

- Electricity purchases
- Electricity transmission costs
- Electricity pool costs
- Council rates
- Auditing services
- Brown Coal Royalties
- Technical services
- Payroll tax
- Briquette purchases
- Electricity sales revenue
- Coal sales revenue
- Water purchases and waste water disposals
- Loans from shareholder
- Land leases
- Provision of loan facilities
- Gas purchases
- Superannuation payments

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FINANCIAL STATEMENTS 1995/96

NOTES TO AND FORMING PART OF THE FINANCIAL STATEMENTS (CONTINUED)

	30 JUNE 1996	30 JUNE 1995
	\$'000	\$'000
	-----	-----
25 RELATED PARTY DISCLOSURES (continued)		
25.5 OPERATING PROFIT AND LOSS TRANSACTIONS WITH RELATED PARTIES		
Interest revenue.....	1,164	371
Dividend revenue.....	127	0
Interest expense .....	126,711	58,707
25.6 RECEIVABLE AND PAYABLES AT BALANCE DATE		
AGGREGATE RELATED PARTY RECEIVABLES AT BALANCE DATE		
Current .....	57,508	99,469
Non-current.....	1,566	3,132
	-----	-----
	59,074	102,601
AGGREGATE RELATED PARTY PAYABLES AT BALANCE DATE		
Current .....	1,994,185	2,097,008
Non-current.....	1,058,296	1,164,997
	-----	-----



## 25.7 INTERESTS HELD

There are no interests held in any related party other than those disclosed as investments in note 8.

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## LOY YANG POWER ANNUAL REPORT 1995/96

## AUDITOR-GENERAL'S REPORT

## AUDIT SCOPE

The accompanying financial statements of Loy Yang Power Limited for the year ended 30 June 1996, comprising a profit and loss statement, balance sheet, statement of cash flows and notes to the financial statements, have been audited. The company's directors are responsible for the preparation and presentation of the financial statements and the information they contain. An independent audit of these financial statements has been carried out in order to express an opinion on them to the manager of the company, as required by the Corporations Law and Audit Act of 1996.

The audit has been conducted in accordance with Australian Auditing Standards to provide reasonable assurance as to whether the financial statements are free of material misstatement. The audit procedures included an examination, on a test basis, of evidence supporting the amounts and other disclosures in the financial statements, and the evaluation of accounting policies and significant accounting estimates. These procedures have been undertaken to form an opinion as to whether, in all material respects, the financial statements are presented fairly in accordance with the basis on which the accounts have been prepared, namely applicable Accounting Standards, other mandatory professional reporting requirements and comply with the Corporations Law, so as to present a view which is consistent with my understanding of the company's financial position and the results of its operations and its cash flows.

The audit opinion expressed in the financial statements has been formed on the above basis.

## AUDIT OPINION

In my opinion, the financial statements of Loy Yang Power Limited are properly drawn up:

- a) so as to give a true and fair view of:
  - i) the company's state of affairs as at 30 June 1996 and of its profit and cash flows for the financial year ended on that date; and
  - ii) the other matters required by Divisions 1, 4A and 4B of Part 3.6 of the Corporations Law to be dealt with in the financial statements,
- b) in accordance with the Corporations Law, and
- c) in accordance with applicable Accounting Standards and other mandatory professional reporting requirements.

/s/ C.A. Baragwanath  
C.A. Baragwanath  
Auditor-General

Melbourne, 29 August 1996

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[VICTORIAN AUDITOR-GENERAL LETTERHEAD]

AUDITOR-GENERAL'S REPORT

AUDIT SCOPE

The accompanying financial statements of Loy Yang Power Limited for the financial year ended 30 June 1995, comprising a profit and loss statement, balance sheet, statement of cash flows and notes to the financial statements, have been audited. The company's directors are responsible for the preparation and presentation of the financial statements and the information they contain. An independent audit of these financial statements has been carried out in order to express an opinion on them to the members of the company as required by the Corporations Law and the Audit Act 1994.

The audit has been conducted in accordance with Australian Auditing Standards to provide reasonable assurance as to whether the financial statements are free of material misstatement. The audit procedures included an examination, on a test basis, of evidence supporting the amounts and other disclosures in the financial statements, and the evaluation of accounting policies and significant accounting estimates. These procedures have been undertaken to form an opinion as to whether, in all material respects, the financial statements are presented fairly in accordance with applicable Accounting Standards and other mandatory professional reporting requirements and comply with the Financial Management Act 1994 and the Corporations Law, so as to present a view which is consistent with my understanding of the company's financial position and the results of its operations and its cash flows.

The audit opinion expressed on the financial statements has been formed on the above basis.

AUDIT OPINION

In my opinion, the financial statements of the Loy Yang Power Limited are properly drawn up:

- (a) so as to give a true and fair view of:
  - (i) the company's state of affairs as at 30 June 1995 and of its profit and cash flows for the financial year ended on that date, and
  - (ii) the other matters required by Divisions 4, 4A and 4B of Part 3.6 of the Corporations Law to be dealt with in the financial statements.
- (b) in accordance with the Financial Management Act 1994 and the Corporations Law; and
- (c) in accordance with applicable Accounting Standards and other mandatory professional reporting requirements.

/s/ K. G. Hamilton  
-----  
K. G. HAMILTON  
Acting  
Auditor-General

MELBOURNE  
6/9/1995

End of Audited Financial Statements

NRG Energy Inc  
1221 Nicollet Mall  
Suite 700  
Minneapolis MN 55403-2445  
UNITED STATES OF AMERICA

Dear Sirs/Mesdames

LOY YANG POWER -- REPORT ON US GAAP RECONCILIATION AND PRIOR YEAR AUDIT  
WORKPAPERS

At your request, we have performed the agreed-upon procedures set out below with respect to Loy Yang Power Limited for the period 1 February 1995 to 30 June 1995, the financial year ended 30 June 1996, and the period from 1 July 1996 to 12 May 1997. These financial periods were covered by financial statements for the financial years ended 30 June 1995 and 30 June 1996 of Loy Yang Power Limited, and for the financial year ended 30 June 1997 for Quite Life Limited (formerly Loy Yang Power Limited). Each of these financial statements was subject to audit by the Victorian Auditor-General's Office.

The procedures performed were as follows:

- o We audited the reconciliations of both the operating profit after tax for each of the financial periods listed above and shareholders equity as at 30 June 1995, 30 June 1996 and 12 May 1997, from Australian generally accepted accounting principles ("GAAP") to United States ("US") GAAP.
- o We reviewed the workpapers of the Victorian Auditor-General's Office for the purpose of determining whether the audit procedures performed in support of the audit opinions on the financial statements as described above were in accordance with US generally accepted auditing standards ("GAAS").

The following statements are made as a result of the performance of these agreed-upon procedures.

#### AUDIT OF US GAAP RECONCILIATION

We have audited the reconciliation of operating profit after tax of Loy Yang Power Limited for the period from 1 February 1995 to 30 June 1995, the financial year ended 30 June 1996, and the period from 1 July 1996 to 12 May 1997, and of shareholders equity as at 30 June 1995, 30 June 1996 and 12 May 1997, from Australian GAAP to US GAAP, as set out in Schedule 1.

Our audit has been conducted in accordance with Australian Auditing Standards, which are substantially similar in all material respects to US GAAS, to provide reasonable assurance of whether the US GAAP reconciliations are free of material misstatement. Our procedures included the examination of the audited financial statements for each of the financial period listed above of Loy Yang Power Limited in order to identify the application of accounting policies which would be inconsistent with US GAAP, and the examination of the US GAAP reconciliation including examination, on a test basis, of evidence supporting the amounts of the reconciling items. These procedures have been undertaken to form an opinion whether, in all material respects, the US GAAP reconciliations are presented fairly, and represent an amount of operating profit after tax and shareholders equity in accordance with US GAAP. The audit opinion expressed in this report has been formed on the above basis.

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In our opinion, the US GAAP reconciliations of Loy Yang Power Limited are properly drawn up to give a true and fair view of:

- o Operating profit after tax for the period from 1 February 1995 to 30 June 1995, the financial year ended 30 June 1996, and the period from 1 July

1996 to 12 May 1997 under US GAAP; and

- o Shareholders equity as at 30 June 1995, 30 June 1996 and 12 May 1997 under US GAAP.

REVIEW OF WORKPAPERS OF THE VICTORIAN AUDITOR-GENERAL'S OFFICE

We have reviewed the workpapers of the Victorian Auditor-General's Office in support of the audit opinions expressed by the Auditor-General on the financial statements for the financial years ended 30 June 1995 and 30 June 1996 for Loy Yang Power Limited, and for the financial year ended 30 June 1997 for Quite Life Limited (formerly Loy Yang Power Limited).

Our review has been conducted in accordance with Australian Auditing Standards which are substantially similar in all material respects to US GAAS, in order to state whether, on the basis of the procedures described, anything has come to our attention that would indicate that the audits performed by the Auditor-General were not performed in accordance with US GAAS. Our procedures involved the examination of the workpapers of the Auditor-General for each of the financial statements listed above, and an assessment of whether the procedures documented therein would constitute an audit in accordance with US GAAS. As our review does not constitute an audit made in accordance with Australian auditing standards, we do not express an opinion on whether the audit has been performed in accordance with US GAAS.

Based on our review however, nothing has come to our attention that causes us to believe that the audits performed by the Auditor-General on the financial statements for the financial years ended 30 June 1995 and 30 June 1996 for Loy Yang Power Limited, and for the financial year ended 30 June 1997 for Quite Life Limited (formerly Loy Yang Power Limited), have not been performed in accordance with US GAAS.

This report has been prepared to assist you with your reporting obligations to the Securities Exchange Commission, and is not to be used for any other purpose.

If you have any queries in relation to the above, please do not hesitate to contact either Mr Michael Perry (613) 9286 8734 or Mr Scott Ward (613) 9286 8194.

Yours faithfully

/s/ Arthur Andersen

Enc

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SCHEDULE 1

LOY YANG POWER LIMITED

US GAAP RECONCILIATION

	A\$'000 PERIOD TO 12 MAY 1997	A\$'000 YEAR TO 30 JUNE 1996	A\$'000 PERIOD TO 30 JUNE 1995
Operating profit and extraordinary items under Australian GAAP .....	983,177	117,686	50,618

Less: Extraordinary gain on sale of business net of tax.....	7	(952,657)		
Add: Loss on buy-back of debt securities .....	7	82,576		
<hr/>				
Operating profit before sale of business under Australian GAAP.....		113,096	117,686	50,618
Add/(less): US GAAP adjustments				
Provision for redundancies .....	1	(650)	(3,740)	(5,053)
Pension plan .....	2	1,472	(768)	(320)
Tax rate change .....	3		(1,881)	1,881
Revaluation of property, plant & equipment .....	4	4,435	5,142	2,151
Reclassification of spares .....	5		(1,830)	
Shareholder loan .....	6	(81,022)	(76,311)	(32,838)
<hr/>				
Operating profit before sale of business under US GAAP		57,331	38,298	16,439
<hr/>				

		A\$'000 AT 12 MAY 1997	A\$'000 AT 30 JUNE 1996	A\$'000 AT 30 JUNE 1995
<hr/>				
Shareholders equity under Australian GAAP .....		0	50,618	50,618
Less: Extraordinary gain on sale of business net of tax.....	7	(952,657)		
Add: Dividend paid on sale of business .....	7	1,033,795		
Add: Loss on buy-back of debt securities .....	7	82,576		
<hr/>				
Shareholders equity before sale of business under Australian GAAP .....		163,714	50,618	50,618
Add/(less): US GAAP adjustments				
Provision for redundancies .....	1	(9,443)	(8,793)	(5,053)
Pension plan .....	2	1,792	320	1,088
Dividend payable .....	8	(61,686)	61,686	
Tax rate change .....	3			1,881
Revaluation of property, plant & equipment .....	4	11,728	7,293	2,151
Reclassification of spares .....	5	(1,830)	(1,830)	
Shareholder loan .....	6		61,022	137,334
<hr/>				
Shareholders equity before sale of business under US GAAP .....		104,275	170,316	188,019
<hr/>				

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LOY YANG POWER LIMITED

US GAAP RECONCILIATION -- FOOTNOTES

1. PROVISION FOR REDUNDANCIES

A provision for labour redundancies was recognised on the commercialisation of the company on 1 February 1995. In accordance with Australian GAAP, a provision for redundancies can be recognised where positions have been identified as being surplus to requirements, provided the circumstances are such that a constructive liability exists. Under US GAAP, a provision for redundancies can only be recognised in certain restricted circumstances. In particular, a provision redundancies involving voluntary severance offers is restricted to employees who have accepted those offers. Where the conditions for recognition of a redundancy provision do not exist, redundancy benefits paid are expensed as incurred.

2. CONTRIBUTIONS TO PENSION PLANS

Under Australian GAAP, contributions made to pension plans are expensed when due. Under US GAAP, the net periodic pension cost is charged against the profit and loss account in accordance with US Statement of Financial Accounting Standards No. 87.

3. RESTATEMENT OF DEFERRED TAX BALANCES FOR TAX RATE CHANGE

The company's deferred tax balances were restated at 30 June 1995 following the increase in the Australian company tax rate from 33% to 36%

announced by the Australian Treasurer in Parliament on 19 May 1995. This increase was applicable to the company from 1 July 1995. Under Australian GAAP, such an announcement is normally acceptable as adequate evidence that the change will occur. Under US GAAP, a change of tax rate is not recognised until it has been enacted.

#### 4. UPWARD REVALUATIONS OF PROPERTY, PLANT AND EQUIPMENT

Upward revaluations of property, plant and equipment to an amount above historical cost are permitted under Australian GAAP, which result in an increase in depreciation expense charged against the profit and loss account. Since US GAAP does not permit property, plant and equipment to be valued at an amount above historical cost, the company's depreciation expense has been restated to reflect historical cost depreciation.

#### 5. CHANGE IN ACCOUNTING POLICY

Under Australian GAAP, a change in accounting policy which resulted in non-depreciable inventory being classified as depreciable property, plant and equipment was brought to account through prospective adjustment to depreciation charged to the profit and loss account. Under US GAAP, a charge to the profit and loss account made in the period of reclassification, representing a retrospective adjustment for depreciation charges incurred to date.

#### 6. SHAREHOLDER LOAN

Under Australian GAAP, non-interest bearing debt is recognised as the amount of principal due for repayment, and no interest expense is charged to the profit and loss account. Under US GAAP, a notional interest cost is recognised through adjusting the carrying value of the debt to the present value of future obligations for principal repayments.

#### 7. REVERSAL OF RESULT FROM SALE OF BUSINESS

The result from the sale of the business, including the final dividend to the State Electricity Commission of Victoria, and the loss incurred on the buy back of debt securities has been reversed in determining the results of operations and shareholder equity under Australian GAAP.

#### 8. DIVIDEND PAYABLE

Under Australian GAAP, dividends are recognised in the period to which they relate and provision for dividends payable is made where a constructive liability exists for the payment of such dividends at year end. Under US GAAP, a dividends are recognised in the period in which they are declared and become legally payable.

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#### 9. OTHER US GAAP MATTERS

##### Amortisation of deferred mine development costs

The expenditure associated with mine development costs is carried forward to the extent that it is expected to be recouped. Deferred costs are amortised on a units of production basis over proven coal reserves. This accounting treatment is consistent with both Australian and US GAAP.

##### Liability for leased assets

On its commercialisation on 1 February 1995, the company recorded as an asset plant and equipment under lease to the State Electricity Commission of Victoria (SECV) and Generation Victoria (GenVic) with a fair value of A\$274.988 million. The plant and equipment was operated in accordance with licenses approved by the lessor with the consent of the SECV and GenVic pending formal novation of the lease agreement.

Liability for payments to the SECV and GenVic in relation to the leased assets was recognised as a component of the non-interest bearing shareholder loan (refer item 6 above). The amount of this liability was equal to the fair value of the leased assets on commercialisation of the company. For the purpose of the US GAAP reconciliation, the profit and loss charges associated with the financing of the leased assets are included within the notional interest cost on the shareholder loan.

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NO DEALER, SALESMAN OR OTHER PERSON HAS BEEN AUTHORIZED TO GIVE ANY INFORMATION OR TO MAKE ANY REPRESENTATIONS OTHER THAN THOSE CONTAINED IN THIS PROSPECTUS IN CONNECTION WITH THIS OFFERING, AND, IF GIVEN OR MADE, SUCH INFORMATION OR REPRESENTATIONS MUST NOT BE RELIED UPON AS HAVING BEEN AUTHORIZED BY NRG. THE INFORMATION CONTAINED HEREIN IS AS OF THE DATE HEREOF AND SUBJECT TO CHANGE, COMPLETION OR AMENDMENT WITHOUT NOTICE. DELIVERY OF THIS PROSPECTUS AT ANY TIME SHALL NOT CREATE ANY IMPLICATION THAT THERE HAS BEEN NO CHANGE IN THE INFORMATION SET FORTH HEREIN OR IN THE AFFAIRS OF NRG SINCE THE DATE HEREOF OR THAT THE INFORMATION SET FORTH HEREIN IS CORRECT AS OF ANY TIME SUBSEQUENT TO ITS DATE. THIS PROSPECTUS DOES NOT CONSTITUTE AN OFFER TO SELL OR A SOLICITATION OF AN OFFER TO BUY ANY SECURITY OTHER THAN THE NOTES OFFERED HEREBY, NOR DOES IT CONSTITUTE AN OFFER TO SELL OR A SOLICITATION OF AN OFFER TO BUY ANY OF THE NOTES OFFERED HEREBY IN ANY JURISDICTION IN WHICH IT IS UNLAWFUL TO MAKE SUCH AN OFFER OR SOLICITATION TO SUCH PERSON.

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UNTIL MARCH 18, 1998, ALL DEALERS EFFECTING TRANSACTIONS IN THE NEW NOTES, WHETHER OR NOT PARTICIPATING IN THE EXCHANGE OFFER, MAY BE REQUIRED TO DELIVER A PROSPECTUS.

\$250,000,000

NRG ENERGY INC.

7 1/2% SENIOR NOTES  
DUE 2007

[NRG LOGO]

PROSPECTUS

DATED DECEMBER 17, 1997

PART II

INFORMATION NOT REQUIRED IN THE PROSPECTUS

ITEM 13. OTHER EXPENSES OF ISSUANCE AND DISTRIBUTION.

The following is an estimate of all expenses in connection with the issuance and distribution of the securities being registered hereby:

SEC Registration Fee....	\$ 75,758
Accountants' fees and expenses.....	100,000
Attorney's fees and expenses.....	150,000
Printing expenses.....	100,000
Miscellaneous.....	19,242
	-----
Total.....	\$445,000
	=====

ITEM 14. INDEMNIFICATION OF DIRECTORS AND OFFICERS.

As authorized by Section 145 of the General Corporation Law of the State of Delaware, each director and officer of NRG may be indemnified by NRG against expenses (including attorney's fees, judgments, fines and amounts paid in settlement) actually and reasonably incurred in connection with the defense or settlement of any threatened, pending or completed legal proceedings in which he is involved by reason of the fact that he is or was a director or officer of NRG if he acted in good faith and in a manner that he reasonably believed to be in or not opposed to the best interests of NRG and, with respect to any criminal action or proceeding, if he had no reasonable cause to believe that his conduct was unlawful. However, if the legal proceeding is by or in the right of NRG, the director or officer may not be indemnified in respect of any claim, issue or matter as to which he shall have been adjudged to be liable for negligence or misconduct in the performance of his duty to NRG unless a court determines otherwise.

In addition, Article VI of NRG's By-Laws provides that NRG shall indemnify and hold harmless, to the fullest extent permitted by applicable law, any



person who was or is made or is threatened to be made a party or is otherwise involved in any action, suit or proceeding, whether civil, criminal, administrative or investigative (a "Proceeding") by reason of the fact that he or she, or a person for whom he or she is the legal representative, is or was a director, officer, employee or agent of NRG or is or was serving at the request of NRG as a director, officer, employee or agent of another company or of a partnership, joint venture, trust, enterprise or non-profit entity, including service with respect to employee benefit plans, against all liability and loss suffered and expenses reasonably incurred by such person. NRG shall be required to indemnify a person in connection with a Proceeding initiated by such person only if the Proceeding was authorized by the Board of Directors of NRG.

ITEM 15. RECENT SALES OF UNREGISTERED SECURITIES.

On June 12, 1997, NRG sold \$250,000,000 aggregate principal amount of its 7-1/2% Senior Notes Due 2007 (the "Old Notes") to Salomon Brothers Inc, ABN AMRO Chicago Corporation and Chase Securities Inc. (the "Initial Purchasers") for \$250,000,000 less the aggregate discount to Initial Purchasers of \$1,625,000. Such transaction was exempt from the registration requirements of the Securities Act of 1933, in reliance on Section 4(2) of the Securities Act on the basis that such transactions did not involve a public offering. In accordance with the agreement pursuant to which the Initial Purchasers purchased the Old Notes, such Initial Purchasers agreed to offer and sell the Old Notes only to "qualified institutional buyers" (as defined in Rule 144A under the Securities Act) and pursuant to offers and sales that occur outside the United States within the meaning of Regulation S under the Securities Act.

On January 29, 1996, NRG sold \$125,000,000 aggregate principal amount of its 7.625% Senior Notes Due 2006 (the "1996 Notes") to Bear, Stearns & Co. Inc. and Merrill Lynch & Co. (the "1996 Note Initial Purchasers") for \$125,000,000 less the aggregate discount to 1996 Note Initial Purchasers of

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\$812,500. Such transaction was exempt from the registration requirements of the Securities Act of 1933, in reliance on Section 4(2) of the Securities Act on the basis that such transactions did not involve a public offering. In accordance with the agreement pursuant to which the 1996 Note Initial Purchasers purchased the 1996 Notes, such 1996 Note Initial Purchasers agreed to offer and sell the 1996 Notes only to "qualified institutional buyers" (as defined in Rule 144A under the Securities Act), a limited number of institutional "accredited investors" (as defined in Rule 501(a)(1), (2), (3) or (7) under the Securities Act) and pursuant to offers and sales that occur outside the United States within the meaning of Regulation S under the Securities Act.

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ITEM 16. EXHIBITS AND FINANCIAL STATEMENT SCHEDULES.

EXHIBIT

3.1	Certificate of Incorporation of NRG.*
3.2	By-Laws of NRG.*
4.1	Indenture, dated as of June 1, 1997, between NRG and Norwest Bank Minnesota, National Association.*
4.2	Form of Exchange Notes.*
4.3	Registration Rights Agreement, dated as of June 12, 1997, by and among NRG, Salomon Brothers Inc, ABN AMRO Chicago Corporation and Chase Securities Inc.*
5.1	Opinion and consent of Skadden, Arps, Slate, Meagher & Flom LLP as to legality of the Exchange Notes to be issued by NRG.*
5.2	Opinion of James J. Bender, Vice President and General Counsel of NRG.*
10.1	Employment Contract, dated as of June 28, 1995, between NRG and David H. Peterson.*
10.2	Indenture, dated as of January 31, 1996, between NRG and Norwest Bank Minnesota, National Association, as Trustee.*
10.3	Revolving Credit Agreement, dated as of March 17, 1997, among NRG, the banks party thereto and ABN AMRO Bank, N.V. as Agent.*
10.4	Note Agreement, dated August 20, 1993, among NRG Energy Center, Inc. and each of the purchasers named therein.*
10.5	Master Shelf and Revolving Credit Agreement, dated August 20, 1993 among NRG Energy Center, Inc., The Prudential Insurance Company of America and each Prudential Affiliate which becomes party thereto.*
10.6	Energy Agreement, dated February 12, 1988 between NRG (formerly known as Norencor Corporation) and Waldorf Corporation (the "Energy Agreement").*
10.7	First Amendment to the Energy Agreement, dated August 27, 1993.*
10.8	Second Amendment to the Energy Agreement, dated January 31, 1996.*
10.9	Third Amendment to the Energy Agreement, dated August 25, 1997.*
10.10	Construction, Acquisition and Term Loan Agreement, dated September 2, 1997 by and among NEO Landfill Gas, Inc., as Borrower, the lenders named on the signature pages, Credit Lyonnais New York Branch, as Construction/Acquisition Agent and Lyon Credit Corporation, as Term Agent.*
10.11	Guaranty, dated September 12, 1997 by NRG in favor of Credit Lyonnais New York Branch as agent for the Construction/Acquisition Lenders.*
10.12	Construction, Acquisition and Term Loan Agreement, dated September 2, 1997 by and among Minnesota Methane LLC, as Borrower, the lenders named on the signature pages, Credit Lyonnais New York Branch, as Construction/Acquisition Agent and Lyon Credit Corporation, as Term Agent.*
10.13	Guaranty, dated September 12, 1997 by NRG in favor of Credit Lyonnais New York Branch as agent for the Construction/Acquisition Lenders.*
10.14	Non Operating Interest Acquisition Agreement, dated as of September 12, 1997, by and among NRG and NEO Corporation.*
12.1	Computation of ratio of earnings to fixed charges.*
21	Subsidiaries of NRG.*
23.1	Consent of Price Waterhouse LLP.*
23.2	Consent of Deloitte & Touche LLP.*
23.3	Consent of Price Waterhouse Nederland BV.*
23.4	Consent of Coopers & Lybrand L.L.P.*
23.5	Consent of Deloitte & Touche GmbH (MIBRAG).*
23.6	Consent of Deloitte & Touche GmbH (SEG).*
23.7	Consent of the Australian Auditor General.*
23.8	Consent of Arthur Andersen LLP.*
23.9	Consent of Skadden, Arps, Slate, Meagher & Flom LLP (included in Exhibit 5.1).*
23.10	Consent of James J. Bender (included in Exhibit 5.2).*
24	Power of Attorney of certain officers and directors of NRG.*
25	Form T-1 Statement of Eligibility of Norwest Bank Minnesota, National Association to act as trustee under the Indenture.*
27	Financial Data Schedule.*
99.1	Form of Letter of Transmittal.*
99.2	Form of Notice of Guaranteed Delivery.*

\* Previously filed.

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ITEM 17. UNDERTAKINGS.

(a) The undersigned registrant hereby undertakes that:

(1) For purposes of determining any liability under the Securities Act of 1933, the information omitted from the form of prospectus filed as part of this registration statement in reliance upon Rule 430A and contained in a form of prospectus filed by the registrant pursuant to Rule 424(b)(1) or (4) or 497(h) under the Securities Act shall be deemed to be part of this registration statement as of the time it was declared effective.

(2) For the purpose of determining any liability under the Securities Act of 1933, each post-effective amendment that contains a form of prospectus shall be deemed to be a new registration statement relating to the securities offered herein, and the offering of such securities at that time shall be deemed to be the initial bona fide offering thereof.

(b) Insofar as indemnification for liabilities arising under the Securities Act of 1933 may be permitted to directors, officers and controlling persons of the Registrant pursuant to the foregoing provisions, or otherwise, the Registrant has been advised that in the opinion of the Securities and Exchange Commission such indemnification is against public policy as expressed in the Act and is, therefore, unenforceable. In the event

that a claim for indemnification against such liabilities (other than the payment by the Registrant of expenses incurred or paid by a director, officer or controlling person of the Registrant in the successful defense of any action, suit or proceeding) is asserted by such director, officer or controlling person in connection with the securities being registered, the Registrant will, unless in the opinion of its counsel the matter has been settled by the controlling precedent, submit to a court of appropriate jurisdiction the question whether such indemnification by it is against public policy as expressed in the Act and will be governed by the final adjudication of such issue.

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SIGNATURES

Pursuant to the requirements of the Securities Act of 1933, NRG Energy, Inc. certifies that it has reasonable grounds to believe that it meets all of the requirements for filing on Form S-1 and has duly caused this amendment to the registration statement to be signed on its behalf by the undersigned, thereunto duly authorized, in the City of Minneapolis, in the State of Minnesota, on the 12th day of December, 1997.

NRG Energy, Inc.  
 By: /s/ Leonard A. Bluhm  
 -----  
 Leonard A. Bluhm  
 Executive Vice President and  
 Chief Financial Officer

Pursuant to the requirements of the Securities Act of 1933, this Registration Statement has been signed by the following persons in the capacities indicated on the dates indicated:

Signature	Title	Date
----- * ----- David H. Peterson	Chairman of the Board, President and Chief Executive Officer	December 12, 1997
/s/ Leonard A. Bluhm ----- Leonard A. Bluhm	Executive Vice President and Chief Financial Officer	December 12, 1997
----- * ----- Gary R. Johnson	Director	December 12, 1997
----- * ----- Cynthia L. Leshner	Director	December 12, 1997
----- * ----- Edward J. McIntyre	Director	December 12, 1997
----- * ----- John A. Noer	Director	December 12, 1997
*By: /s/ Leonard A. Bluhm ----- Attorney-in-fact		

## EXHIBIT INDEX

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10.10	Construction, Acquisition and Term Loan Agreement, dated September 2, 1997 by and among NEO Landfill Gas, Inc., as Borrower, the lenders named on the signature pages, Credit Lyonnais New York Branch, as Construction/Acquisition Agent and Lyon Credit Corporation, as Term Agent.*	
10.11	Guaranty, dated September 12, 1997 by NRG in favor of Credit Lyonnais New York Branch as agent for the Construction/Acquisition Lenders.*	
10.12	Construction, Acquisition and Term Loan Agreement, dated September 2, 1997 by and among Minnesota Methane LLC, as Borrower, the lenders named on the signature pages, Credit Lyonnais New York Branch, as Construction/Acquisition Agent and Lyon Credit Corporation, as Term Agent.*	
10.13	Guaranty, dated September 12, 1997 by NRG in favor of Credit Lyonnais New York Branch as agent for the Construction/Acquisition Lenders.*	
10.14	Non Operating Interest Acquisition Agreement, dated as of September 12, 1997, by and among NRG and NEO Corporation.*	
12.1	Computation of ratio of earnings to fixed charges.*	
21	Subsidiaries of NRG.*	
23.1	Consent of Price Waterhouse LLP.*	
23.2	Consent of Deloitte & Touche LLP.*	
23.3	Consent of Price Waterhouse Nederland BV.*	
23.4	Consent of Coopers & Lybrand L.L.P.*	
23.5	Consent of Deloitte & Touche GmbH (MIBRAG).*	
23.6	Consent of Deloitte & Touche GmbH (SEG).*	
23.7	Consent of The Australian Auditor General.*	
23.8	Consent of Arthur Andersen LLP.*	
23.9	Consent of Skadden, Arps, Slate, Meagher & Flom LLP (included in Exhibit 5.1).*	
23.10	Consent of James J. Bender (included in Exhibit 5.2).*	
24	Power of Attorney of certain officers and directors of NRG.*	
25	Form T-1 Statement of Eligibility of Norwest Bank Minnesota, National Association to act as trustee under the Indenture.*	
27	Financial Data Schedule.*	
99.1	Form of Letter of Transmittal.*	
99.2	Form of Notice of Guaranteed Delivery.*	

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\* Previously filed.