UNITED STATES SECURITIES AND EXCHANGI SCHEDULE E-5
Washington, D.C. 20549

Form 10-K

(Mark One)

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

For the fiscal year ended December 31, 2000

or

☐ **TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 19**

For the transition period from to

Commission File Number 1-3187

See REA's "Petition for Waiver of "Certain Minimum Filing Requirements," paragraph 4(h)

Reliant Energy, Incorporate

(Exact name of registrant as specified in its charte

Texas	**74-0694415**
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification Number)
1111 Louisiana **Houston, Texas 77002**	**(713) 207-3000**
(Address and zip code of principal executive offices)	(Registrant's telephone number, including area code)

Securities registered pursuant to Section 12(b) of the Act:

Title of each class	Name of each exchange on which registered
Common Stock, without par value, and associated rights to purchase preference stock	New York Stock Exchange Chicago Stock Exchange
HL&P Capital Trust I 8.125% Trust Preferred Securities, Series A	New York Stock Exchange
REI Trust I 7.20% Trust Originated Preferred Securities, Series C	New York Stock Exchange

Securities registered pursuant to Section 12(g) of the Act: Preferred Stock, cumulative, no par — $4 series

Commission File Number 1-13265

Reliant Energy Resources Corp.

(Exact name of registrant as specified in its charter)

Delaware	**76-0511406**
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification Number)
1111 Louisiana **Houston, Texas 77002**	**(713) 207-3000**
(Address and zip code of principal executive offices)	(Registrant's telephone number, including area code)

Securities registered pursuant to Section 12(b) of the Act:

Title of each class	Name of each exchange on which registered
NorAm Financing I 6¼% Convertible Trust Originated Preferred Securities	New York Stock Exchange
6% Convertible Subordinated Debentures due 2012	New York Stock Exchange

Securities registered pursuant to Section 12(g) of the Act: None

Reliant Energy Resources Corp. meets the conditions set forth in General Instruction I(1)(a) and (b) of Form 10-K and is therefore filing this Form 10-K with the reduced disclosure format.

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

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K is not contained herein and will not be contained, to the best of each of the registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K. ☐

The aggregate market value of the voting stock held by non-affiliates of Reliant Energy, Incorporated (Company) was $12,387,338,940 as of March 12, 2001, using the definition of beneficial ownership contained in Rule 13d-3 promulgated pursuant to the Securities Exchange Act of 1934 and excluding shares held by directors and executive officers. As of March 12, 2001, the Company had 296,125,961 shares of Common Stock outstanding, including 8,575,565 ESOP shares not deemed outstanding for financial statement purposes. Excluded from the number of shares of Common Stock outstanding are 4,511,691 shares held by the Company as treasury stock. As of March 12, 2001, all 1,000 outstanding shares of Reliant Energy Resources Corp.'s Common Stock were held by the Company.

Portions of the definitive proxy statement relating to the 2001 Annual Meeting of Shareholders of the Company, which will be filed with the Securities and Exchange Commission within 120 days of December 31, 2000, are incorporated by reference in Item 10, Item 11, Item 12 and Item 13 of Part III of this Form 10-K.

This combined Annual Report on Form 10-K is separately filed by Reliant Energy, Incorporated and Reliant Energy Resources Corp. Information contained herein relating to Reliant Energy Resources Corp. is filed by Reliant Energy, Incorporated and separately by Reliant Energy Resources Corp. on its own behalf. Reliant Energy Resources Corp. makes no representation as to information relating to Reliant Energy, Incorporated (except as it may relate to Reliant Energy Resources Corp.) and its subsidiaries, or any other affiliate or subsidiary of Reliant Energy, Incorporated.

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CAUTIONARY STATEMENT REGARDING FORWARD-LOOKING INFORMATION

From time to time we make statements concerning our expectations, beliefs, plans, objectives, goals, strategies, future events or performance and underlying assumptions and other statements that are not historical facts. These statements are "forward-looking statements" within the meaning of the Private Securities Litigation Reform Act of 1995. Actual results may differ materially from those expressed or implied by these statements. In some cases, you can identify our forward-looking statements by the words "anticipates," "believes," "continue," "could," "estimates," "expects," "intends," "may," "plans," "potential," "predicts," "should," "will" or other similar words.

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

- state, federal and international legislative and regulatory developments, including deregulation, re-regulation and restructuring of the electric utility industry and changes in or application of environmental and other laws and regulations to which we are subject,
- the timing of the implementation of our business separation plan,
- the effects of competition, including the extent and timing of the entry of additional competitors in our markets,
- industrial, commercial and residential growth in our service territories,
- our pursuit of potential business strategies, including acquisitions or dispositions of assets or the development of additional power generation facilities,
- state, federal and other rate regulations in the United States and in foreign countries in which we operate or into which we might expand our operations,
- the timing and extent of changes in commodity prices and interest rates,
- weather variations and other natural phenomena,
- political, legal and economic conditions and developments in the United States and in foreign countries in which we operate or into which we might expand our operations, including the effects of fluctuations in foreign currency exchange rates,
- financial market conditions and the results of our financing efforts,
- the performance of our projects, and
- other factors we discuss in this Form 10-K, including those outlined in "Management's Discussion and Analysis of Financial Condition and Results of Operations — Certain Factors Affecting Our Future Earnings."

We have based our forward-looking statements on management's beliefs and assumptions based on information available at the time the statements are made. We caution you that assumptions, beliefs, expectations, intentions and projections about future events may and often do vary materially from actual results. Therefore, actual results may differ materially from those expressed or implied by our forward-looking statements.

The following sections of this Form 10-K contain forward-looking statements:

- Our Business —
  - Deregulation and Competition
  - Restructuring
- Electric Operations —
  - Electric Operations Assets —

        - Generation
    - Texas Genco —
        - Texas Genco Operations and Market Framework
        - Texas Genco Option
    - Fuel and Purchased Power —
        - Natural Gas Supply
        - Coal and Lignite Supply
        - Nuclear Fuel Supply
        - Purchased Power Supply
- Natural Gas Distribution —
    - Supply and Transportation
- Wholesale Energy —
    - Power Generation Operations —
        - Southwest Region
        - Midcontinent Region
        - Florida
        - Texas
    - Development Activities
    - Domestic Trading, Marketing, Power Origination and Risk Management Operations
- European Energy —
    - European Power Generation Operations —
        - Market Framework
    - European Trading, Marketing and Risk Management Operations
- Other Operations —
    - Unregulated Retail Electric Business
    - eBusiness —
        - Pantellos
        - IntercontinentalExchange
- Regulation —
    - State and Local Regulations —
        - Texas —
            - Electric Operations — The Legislation
            - Electric Operations — Rate Case
    - European Regulation
- Environmental Matters —

- General Environmental Issues
- Air Emissions
- Water Issues
- Mercury Contamination
- Other

- Legal Proceedings
- Management's Discussion and Analysis of Financial Condition and Results of Operations —
  - Results of Operations by Business Segment —
    - European Energy
  - Certain Factors Affecting Our Future Earnings —
    - Business Separation and Restructuring
    - Competitive, Regulatory and Other Factors Affecting Our Electric Operations
    - Competitive, Regulatory and Other Factors Affecting Our Wholesale Energy Operations
    - Competitive, Regulatory and Other Factors Affecting Our European Energy Operations
    - Competitive and Other Factors Affecting RERC Operations
    - Environmental Expenditures
  - Liquidity and Capital Resources —
    - Company Consolidated Capital Requirements
    - Future Sources and Uses of Cash Flows
  - New Accounting Pronouncements
- Quantitative and Qualitative Disclosures About Market Risk.

PART I

ITEM 1. *Business.*

OUR BUSINESS

General

Reliant Energy, Incorporated, a Texas corporation, was incorporated in 1906. In this Form 10-K, we refer to Reliant Energy, Incorporated as "Reliant Energy" and to Reliant Energy and its subsidiaries as "we" or "us," unless the context clearly indicates otherwise. Reliant Energy Resources Corp., a Delaware corporation and wholly owned subsidiary of Reliant Energy, was incorporated in 1996. In this Form 10-K, we refer to Reliant Energy Resources Corp. as "RERC Corp." and to RERC Corp. and its subsidiaries as "RERC," unless the context clearly indicates otherwise. The executive offices of Reliant Energy and RERC Corp. are located at 1111 Louisiana, Houston, TX 77002 (telephone number 713-207-3000).

We are a diversified international energy services and energy delivery company that provides energy and energy services in North America and Western Europe through the following business segments:

- Electric Operations,
- Natural Gas Distribution,
- Pipelines and Gathering,
- Wholesale Energy,
- European Energy, and
- Other Operations.

For information about the revenues, operating income, assets and other financial information relating to our business segments, please read "Management's Discussion and Analysis of Financial Condition and Results of Operations — Results of Operations by Business Segment" in Item 7 of this Form 10-K, Note 18 to our consolidated financial statements, which, together with the notes related to those statements, we refer to in this Form 10-K as our "consolidated financial statements," "Management's Narrative Analysis of the Results of Operations of Reliant Energy Resources Corp. and its Consolidated Subsidiaries" in Item 7 of the RERC Form 10-K and Note 12 to RERC's consolidated financial statements, which, together with the notes related to those statements, we refer to in this Form 10-K as "RERC's consolidated financial statements."

RERC conducts its operations primarily in the natural gas industry. RERC's operations are included in our Natural Gas Distribution and Pipelines and Gathering business segments, and include natural gas gathering, transmission, marketing, storage and distribution services. In addition, prior to December 31, 2000, RERC provided energy trading, marketing, power origination and risk management services in North America and Western Europe through our Wholesale Energy and European Energy business segments. RERC's operations are described below in the consolidated description of our business segments.

Deregulation and Competition

In June 1999, the Texas legislature adopted the Texas Electric Choice Plan (Legislation), which substantially amended the regulatory structure governing electric utilities in Texas in order to allow retail electric competition. Retail pilot projects for up to 5% of each utility's load in all customer classes will begin in June 2001, and retail electric competition for all other customers will begin on January 1, 2002. In preparation for that competition, we expect to make significant changes in our electric utility operations currently conducted through our electric utility division, Reliant Energy HL&P. Under the Legislation:

- beginning on January 1, 2002, retail customers of investor-owned electric utilities in Texas, including Reliant Energy HL&P, will be entitled to purchase their electricity from any of a number of "retail

electric providers," which will have been certified by the Public Utility Commission of Texas (Texas Utility Commission),

- beginning on January 1, 2002, power generators will sell electric energy to wholesale purchasers, including retail electric providers, at unregulated rates, and
- by January 1, 2002, electric utilities in Texas, including Reliant Energy HL&P, will have restructured their businesses in order to separate power generation, transmission and distribution, and retail electric provider activities into separate units.

Reliant Energy filed its initial business separation plan with the Texas Utility Commission in January 2000 and filed amended plans in April 2000 and August 2000. In December 2000, the Texas Utility Commission approved Reliant Energy's amended business separation plan (Business Separation Plan) pursuant to which its generation, transmission and distribution, and retail operations will be separated into three different companies, although a final order has not been issued as of this date.

For additional information regarding the Legislation, retail competition in Texas and its application to our operations and structure, please read "— Restructuring," "Electric Operations," and "Regulation — State and Local Regulations — Texas — Electric Operations — The Legislation" in Item 1 of this Form 10-K, "Management's Discussion and Analysis of Financial Condition and Results of Operations — Certain Factors Affecting Our Future Earnings — Competitive, Regulatory and Other Factors Affecting Our Electric Operations" in Item 7 of this Form 10-K and Note 4 to our consolidated financial statements.

Restructuring

In anticipation of electric deregulation in Texas, and pursuant to the Legislation, we submitted our Business Separation Plan to the Texas Utility Commission. Pursuant to the Business Separation Plan, we will restructure our businesses into two separate publicly traded companies in order to separate our unregulated businesses from our regulated businesses. Under the Business Separation Plan, our wholly owned subsidiary, Reliant Resources, Inc. (Reliant Resources), holds substantially all of our unregulated businesses, including the operations conducted by our:

- Wholesale Energy business segment,
- European Energy business segment,
- communications business,
- eBusiness group,
- new ventures group, and
- retail electric business.

In connection with this separation, on December 31, 2000, Reliant Energy contributed the capital stock of certain of its subsidiaries to Reliant Resources, including Reliant Energy Power Generation, Inc.; Reliant Energy Ventures, Inc.; Reliant Energy Communications, Inc.; Reliant Energy Wholesale Service Company; Reliant Energy Trading Exchange, Inc.; Reliant Energy Broadband, Inc.; Reliant Energy Net Ventures, Inc.; ReliantEnergy.com, Inc.; Guidestreet, Inc.; and Reliant Energy Solutions, LLC. In addition, the assets and operations of Reliant Energy's retail marketing, unregulated retail and customer care operations were transferred to Reliant Resources.

As further described below and as part of the separation, Reliant Energy will undergo a restructuring of its corporate organization to achieve a public utility holding company structure (Restructuring). This holding company, which we refer to in this Form 10-K as the "Regulated Holding Company," will hold essentially all of what are currently our regulated businesses.

We expect Reliant Resources will conduct an initial public offering of no more than 20% of its outstanding common stock (Offering) in 2001. Reliant Resources has filed a registration statement with the

Securities and Exchange Commission (SEC) relating to its shares of common stock to be sold in the Offering that has not yet been declared effective by the SEC. The shares of Reliant Resources common stock may not be sold, nor may offers to buy be accepted, prior to the time the registration statement becomes effective. This Form 10-K does not constitute an offer to sell or the solicitation of an offer to buy shares of Reliant Resources common stock. After the Offering, we will own over 80% of Reliant Resources' outstanding common stock. We anticipate that the Regulated Holding Company will distribute to its shareholders the remaining shares of Reliant Resources common stock it would own after the Offering within 12 months of the completion of the Offering (Distribution). Reliant Energy will agree that $1.9 billion of the indebtedness owed by Reliant Resources to Reliant Energy and subsidiaries as of December 31, 2000, will be converted into equity prior to the closing of the Offering, as a capital contribution that will be recorded as an increase to stockholders' equity of Reliant Resources.

The Offering and the Distribution are subject to further Board of Director approvals, market and other conditions, and government actions, and the Distribution is subject to receipt of a favorable Internal Revenue Service ruling that the Distribution would be tax-free to Reliant Energy or its successor and its shareholders for U.S. federal income tax purposes, as applicable. There can be no assurance that the Offering and the Distribution will be completed as described or within the time periods outlined above.

Prior to the closing of the Offering, Reliant Energy will enter into a number of agreements with Reliant Resources relating to the separation of our unregulated businesses and our regulated businesses. These agreements will provide for, among other things, the transfer of assets and liabilities related to our regulated and unregulated businesses, as well as Reliant Energy's interim and ongoing relationships with Reliant Resources, including the provision by Reliant Energy of various interim services to Reliant Resources.

Additionally, as part of our Business Separation Plan, and pursuant to these separation agreements, we will convey regulated electric generating assets of our Electric Operations business segment to a yet to be formed indirect wholly owned limited partnership of Reliant Energy, which we refer to in this Form 10-K as "Texas Genco." Reliant Energy will grant Reliant Resources an option, exercisable in January 2004, to purchase all of the shares of capital stock of Texas Genco owned by the Regulated Holding Company after Texas Genco conducts a public offering or distribution of no more than 20% of its capital stock (Texas Genco Option). For additional information regarding the Texas Genco Option, please read "Electric Operations — Texas Genco — Texas Genco Option" in Item 1 of this Form 10-K.

Concurrent with the Distribution, and in order to comply with applicable regulatory requirements, under our Business Separation Plan, Reliant Energy will complete the Restructuring and the Regulated Holding Company will be the parent company of our subsidiaries that own and operate our regulated businesses. We expect the Regulated Holding Company will have subsidiaries owning and operating our:

- electric transmission and distribution operations,
- Natural Gas Distribution business segment,
- Texas generating assets (subject to Reliant Resources' option to purchase exercisable in 2004),
- Pipelines and Gathering business segment, and
- interests in energy companies in Latin America and India until disposition of these investments.

In this Form 10-K, references to Reliant Energy in connection with events occurring or the performance of agreements after the Restructuring generally refer to the Regulated Holding Company. For additional information regarding the separation of our unregulated and regulated businesses and related agreements, Reliant Resources, the Offering, the Distribution, Texas Genco, the Restructuring and our relationship with Reliant Resources, please read Note 4(b) to our consolidated financial statements. For additional information regarding our Latin America business segment discontinued operations, please read Note 19 to our consolidated financial statements.

As part of the separation of our unregulated and regulated businesses, on December 31, 2000, RERC Corp. transferred all of the outstanding capital stock of Reliant Energy Services International, Inc. (RESI),

Arkla Finance Corporation (Arkla Finance) and Reliant Energy Europe Trading & Marketing, Inc. (RE Europe Trading), to Reliant Resources. As a result of these stock transfers, RESI, Arkla Finance and RE Europe Trading each became a wholly owned subsidiary of Reliant Resources. Also, on December 31, 2000, a wholly owned subsidiary of Reliant Resources merged with and into Reliant Energy Services, Inc. (Reliant Energy Services), which was at that time a wholly owned subsidiary of RERC Corp., with Reliant Energy Services as the surviving corporation. As a result of this merger, Reliant Energy Services became a wholly owned subsidiary of Reliant Resources. As consideration for the stock transfers and the merger, Reliant Resources paid $94 million to RERC Corp.

Reliant Energy Services, RESI and RE Europe Trading conducted RERC's trading, marketing, power origination and risk management operations. Arkla Finance holds an investment in marketable equity securities.

Discontinued Operations

By the end of 2000, our Latin America business segment had sold its investments in Brazil, Colombia and El Salvador for $790 million in after-tax proceeds. Our remaining Latin America business segment investments include a wholly owned cogeneration facility and an electric distribution company in Argentina and a minority interest in a coke calcining plant in India. We are engaged in negotiations for the sale of these investments and anticipate the transactions to be concluded by December 2001. As of December 1, 2000, we began reporting the results from our Latin America business segment as discontinued operations. For additional information regarding our discontinued operations, please read Note 19 to our consolidated financial statements.

As discussed above, RERC Corp. transferred all of the outstanding stock of RE Europe Trading to Reliant Resources. As a result of the transfer, RERC Corp. is reporting the results of RE Europe Trading as discontinued operations. For additional information regarding RERC's discontinued operations, please read Note 13 to RERC's consolidated financial statements.

ELECTRIC OPERATIONS

Our Electric Operations business segment conducts operations through an unincorporated division of Reliant Energy under the name "Reliant Energy HL&P." We are a member of the Electric Reliability Council of Texas, Inc. (ERCOT) and our electric operations are inter-connected to ERCOT's transmission grid encompassing most of the state of Texas. We generate, purchase for resale, transmit, distribute and sell electricity to approximately 1.7 million customers in a 5,000-square-mile area on the Texas Gulf Coast, including Houston.

Until January 1, 2002, we expect to conduct our electric operations as a traditional integrated electric utility, including generation, transmission and distribution, and retail operations. As required by the Legislation, beginning January 1, 2002, we expect full retail competition will begin in Texas. Prior to that date, we will have restructured our electric operations into a transmission and distribution segment, a generation segment and a retail segment. For additional information regarding the separation of the operations of our Electric Operations business segment, please read "— Texas Genco," and "Regulation — State and Local Regulations — Texas — Electric Operations — The Legislation" in Item 1 of this Form 10-K and Note 4 to our consolidated financial statements. The retail electric function (the sale of electricity as opposed to distribution and transmission services) will be conducted by subsidiaries of Reliant Resources. For additional information regarding these retail operations, please read "Other Operations — Unregulated Retail Electric Business."

Reliant Energy HL&P's transmission system carries electricity from the power plant to the substation and from one substation to another. These substations serve to connect the power plants, the high voltage transmission lines and the lower voltage distribution lines. Unlike the transmission system, which carries high voltage electricity over great distances, distribution lines carry lower voltage power from the substation to customers. The distribution system consists of primary distribution lines, transformers, secondary distribution

lines and service wires. Rates for our transmission and distribution services will be set by the Texas Utility Commission during a rate hearing that is currently in progress, and we will be allowed to provide services only under authorized tariffs. For additional information regarding those tariffed rates, read "Regulation — State and Local Regulations — Texas — Electric Operations — Rate Case" in Item 1 of this Form 10-K. The transmission and distribution operations will not own the electricity that it transmits and therefore will not be subject to commodity risk. After retail competition begins, our generation operations will be conducted by Texas Genco, which will generate power for sale to wholesale purchasers, including retail electric providers, at unregulated rates. For additional information regarding the operations of Texas Genco, please read "— Texas Genco — Texas Genco Operations and Market Framework" in Item 1 of this Form 10-K and Note 4(b) to our consolidated financial statements.

Electric Operations Assets

All of the power generating facilities and other operating properties of our Electric Operations business segment are located in the state of Texas.

Transmission and Distribution.

Electric Lines — Overhead. As of December 31, 2000, we owned 25,646 pole miles of overhead distribution lines and 3,586 circuit miles of overhead transmission lines, including 480 circuit miles operated at 69,000 volts, 2,061 circuit miles operated at 138,000 volts and 1,045 circuit miles operated at 345,000 volts.

Electric Lines — Underground. As of December 31, 2000, we owned 12,653 circuit miles of underground distribution lines and 14.9 circuit miles of underground transmission lines, including 6.8 circuit miles operated at 69,000 volts and 8.1 circuit miles operated at 138,000 volts.

Substations. As of December 31, 2000, we owned 218 major substation sites (252 substations) having a total installed rated transformer capacity of 58,041 megavolt amperes.

Generation. As of December 31, 2000, Reliant Energy HL&P owned and operated 12 power generating facilities (62 generating units), with a net generating capacity of 14,040 megawatts (MW), including a 30.8% interest in the South Texas Project Electric Generating Station (South Texas Project). The South Texas Project is a nuclear generating plant with two 1,250 MW nuclear generating units. For additional information regarding the South Texas Project, please read Note 6 to our consolidated financial statements.

The following table contains information regarding the system capability at peak demand of our Electric Operations business segment:

Year	Installed Net Capability At Peak (MW)	Firm Purchased Power Contracts (MW)	Total Net Capability (MW)	Maximum Hourly Firm Demand		% Change From Prior Year	Calculated Reserve Margin (%) (4) (5)
				Date	MW(2) (3)		
1996	13,960	445	14,405	July 23	11,694	2.1	23.2
1997	13,960	445	14,405	August 21	12,246	4.7	17.6
1998	14,040	320	14,360	August 3	13,006	6.2	10.4
1999	14,052	320	14,372	August 20	13,053	0.4	10.1
2000	14,040	770(1)	14,810	September 5	14,569	11.6	1.7

(1) Includes 450 MW of firm capacity purchased to meet peak demand.

(2) Excludes loads on interruptible service tariffs, residential direct load control and commercial/industrial load cooperative capability. Including these loads, the maximum hourly demand served was 14,272 MW in 1998, 14,642 MW in 1999 and 15,505 MW in 2000.

(3) Maximum hourly firm demand in 1998, 1999 and 2000 were influenced by hotter than normal weather at the time of the system peak.

(4) At any given time we have the ability to enter, and have entered, into non-firm contracts for purchased power on the spot market within ERCOT, to provide additional total capability. The ERCOT reserve margin for 2000 was over 10%.

(5) Electric Operations expects to lose approximately 5% of peak load in 2001 due to the implementation of the retail pilot programs. Please read "Regulation — State and Local Regulations — Texas — Electric Operations — The Legislation" in Item 1 of this Form 10-K.

Based on present trends, Reliant Energy estimates that the maximum hourly firm demand for electricity in Reliant Energy HL&P's service area will grow at a compound annual rate of approximately 1.5% over the next ten years. Assuming average weather conditions and including the net effects of demand-side management programs, we expect to have an adequate reserve margin in excess of maximum hourly firm demand load requirements in 2001. The reduced reserve margins for 1998, 1999 and 2000 reflect customer growth, the relatively small change in total net capacity and the extremely hot weather conditions at peak in Reliant Energy HL&P's service area during those summers, which increased system peak loads by approximately 400 MW, 500 MW and 1,100 MW, respectively. Sales of electricity by our Electric Operations business segment during the summer months are generally higher, and can be significantly higher, than sales during other months of the year due to the reliance on air conditioning by customers in Houston and in other parts of Reliant Energy HL&P's service territory. However, Texas' approach to deregulation has provided many opportunities for new generation. Generators in ERCOT added 4,295 MW of new capacity in 2000 and are expected to add more than 8,400 megawatts by the summer of 2001. This additional capacity is expected to result in ERCOT reserve margins in excess of 28% for 2001 under normal weather conditions, significantly more than the 15% ERCOT minimum requirement. Therefore, we expect there to be sufficient generating resources available in ERCOT for the summer of 2001. With Reliant Energy HL&P's interconnections with the rest of ERCOT, adequate capacity should be available to serve Reliant Energy HL&P customers. Although these reserve margins would be lower under extreme weather conditions, we still expect there to be adequate capacity to meet peak demand. For additional information regarding our purchases of power to meet demand, please read "— Fuel and Purchased Power — Purchased Power Supply" below. For additional information regarding capacity auctions of wholesale energy after retail electric competition begins, please read "Regulation — State and Local Regulations — Texas — Electric Operations — The Legislation" in Item 1 of this Form 10-K.

Texas Genco

Texas Genco Facilities. In connection with our Business Separation Plan, we plan to transfer all of our regulated electric generating assets to Texas Genco at the time of the Restructuring. All of these assets are located in Texas. The following table describes the electric power generation facilities to be conveyed by Reliant Energy to Texas Genco:

Generation Facilities	Texas Genco Generation Facilities Net Generating Capacity as of December 31, 2000 (in MW)	Dispatch Type(1)	Primary Fuel
W. A. Parish	3,606	Base, Inter, Peak	Gas/Coal
Limestone	1,532	Base	Lignite
South Texas Project(2)	770	Base	Nuclear
San Jacinto	162	Base	Gas
Cedar Bayou	2,260	Inter	Gas/Oil
P. H. Robinson	2,213	Inter	Gas
T. H. Wharton	1,254	Inter, Peak	Gas
S. R. Bertron	844	Inter, Peak	Gas
Greens Bayou	760	Inter, Peak	Gas/Oil
Webster	387	Inter, Peak	Gas
Deepwater	174	Inter, Peak	Gas
H. O. Clarke	78	Peak	Gas
Total	14,040		

(1) The designations "Base," "Inter" and "Peak" indicate whether the facilities described are base-load, intermediate, or peaking facilities, respectively.

(2) We own a 30.8% interest in the South Texas Project electric generating station, a nuclear generating plant consisting of two 1,250 MW generating units.

Power generation facilities can generally be categorized by their variable cost to produce electricity, which determines the order in which they are utilized to meet electricity demand. "Base-load" facilities are those that typically have low variable costs and provide power at all times. Base-load facilities are used to satisfy the base level of demand for power, or "load," that is not dependent upon time of day or weather. "Peaking" facilities have the highest variable cost to generate electricity and typically are used only during periods of highest demand for power. "Intermediate" facilities have cost and usage characteristics in between those of base-load and peaking facilities.

Texas Genco Operations and Market Framework. Any wholesale producer of electricity that can access ERCOT will be allowed to sell in the Texas market. Transmission capacity, which may be limited, must be utilized to affect such sales. In the Texas market, buyers and sellers may negotiate bilateral wholesale capacity, energy and ancillary services contracts. Also, the power generation facilities of companies that were formerly part of integrated utilities must auction the output of 15% of their capacity. For additional information regarding capacity auctions, please read "Regulation — State and Local Regulations — Texas — Electric Operations — The Legislation" in Item 1 of this Form 10-K and Note 4(b) to our consolidated financial statements. Furthermore, buyers and sellers may participate in the spot market. We expect the Texas wholesale electric market to be a very competitive market. For additional information regarding purchased power after 2001, please read "— Fuel and Purchased Power — Purchased Power Supply" below.

In the Texas market, ERCOT has been established as the independent system operator (ISO) to administer and control the open-access transmission system. ISO responsibilities include ensuring that information relating to a customer's choice of retail electric provider is conveyed in a timely manner to anyone needing the information. The ISO also ensures that electricity production and delivery are accurately accounted for among the generation resources and wholesale buyers and sellers in the ERCOT region and serves as agent for suppliers of ancillary services in the ERCOT region.

Power generation assets will continue to be rate-regulated through the end of 2001 under the Legislation. For additional information regarding the impairment of the value of regulatory assets and the recovery of these amounts, please read "Management's Discussion and Analysis of Financial Condition and Results of Operations — Certain Factors Affecting Our Future Earnings — Competitive, Regulatory and Other Factors Affecting Our Electric Operations — Other Regulatory Factors" in Item 7 of this Form 10-K and Note 4(a) to our consolidated financial statements.

Texas Genco Option. Pursuant to the Business Separation Plan, we expect the Regulated Holding Company will cause Texas Genco to either issue and sell in an initial public offering or to distribute to its shareholders no more than 20% of the common stock of Texas Genco by June 30, 2002. Our Business Separation Plan contemplates the grant to Reliant Resources of the Texas Genco Option, exercisable in January 2004. The per share exercise price under the Texas Genco Option will be:

- the average daily closing price on a national exchange for publicly held shares of common stock of Texas Genco for the 30 consecutive trading days with the highest average closing price during the 120 trading days immediately preceding January 10, 2004, plus
- a control premium, up to a maximum of 10%, to the extent a control premium is included in the valuation determination made by the Texas Utility Commission relating to the market value of Texas Genco's common stock equity.

The exercise price formula is based upon the generation asset valuation methodology in the Legislation that we have proposed to use. This market value will be used to determine the amount we will be allowed to recover as stranded costs if the market value of those assets is less than the book value of those assets. For additional information regarding the recovery of stranded costs, please read Notes 4(a) and 14(i) to our consolidated financial statements.

The exercise price is also subject to adjustment based on the difference between the per share dividends paid during the period there is a public ownership interest in Texas Genco and Texas Genco's per share earnings during that period.

If the disposition to the public of common stock of Texas Genco is by means of a primary or secondary public offering, the public offering may be of as little as 17% (rather than 19%) of Texas Genco's outstanding common stock, in which case Reliant Energy will have the right to subsequently reduce its interest to a level not less than 80%.

If Reliant Resources exercises the Texas Genco Option and purchases the shares of Texas Genco common stock, Reliant Resources will also be required to purchase all notes and other receivables from Texas Genco then held by the Regulated Holding Company, at their principal amount plus accrued interest. Similarly, if Texas Genco holds notes or receivables from Reliant Energy, Reliant Resources will assume those obligations in exchange for a payment to Reliant Resources by Reliant Energy of an amount equal to the principal plus accrued interest.

Exercise of the Texas Genco Option by Reliant Resources will be subject to various regulatory approvals, including Hart-Scott-Rodino antitrust clearance and United States Nuclear Regulatory Commission (NRC) license transfer approval. The Texas Genco Option will be exercisable only if the Distribution is completed.

Fuel and Purchased Power

Our Electric Operations business segment relies primarily on natural gas, coal and lignite as fuel for the generation of electricity. For information regarding our fuel contracts, please read Note 14(b) to our consolidated financial statements. Our Electric Operations business segment's 1999 and 2000 historical energy mix is set forth below. These figures represent the generation and purchased power used to meet system load and for off-system sales:

	Historical Energy Mix(%)	
	1999	2000
Natural gas	35	37
Coal and lignite	39	35
Nuclear	8	8
Purchased power	18	20
Total	100	100

Based on our current assumptions regarding the cost and availability of fuel, plant operation schedules, load growth, load management and the impact of environmental regulations, we do not expect the fuel mix used by our Electric Operations business segment to vary materially during 2001 even though we anticipate a higher level of plant maintenance and outages in 2001 associated with the installation of environmental equipment that could affect the fuel mix. However, as a result of the Legislation and the introduction of retail electric competition in 2002, we cannot predict how the fuel mix will be affected after 2001. Please read "Environmental Matters" in Item 1 of this Form 10-K.

Natural Gas Supply. In 2000, our Electric Operations business segment purchased approximately 54% of its natural gas requirements under long-term contracts, which will expire in 2004. The largest supplier under these contracts is Kinder Morgan Texas Pipeline, Inc., a unit of Kinder Morgan, L.P. (supplying 28% of our natural gas requirements). Our Electric Operations business segment purchased the remaining 46% of its natural gas requirements on the spot market. Substantially all of these natural gas contracts contain pricing provisions based on fluctuating spot market prices. Based on current market conditions, we believe we will be able to replace the supplies of natural gas covered under expiring long-term contracts with gas purchased on the spot market or under long-term or short-term contracts. The natural gas consumption and cost information for our Electric Operations business segment in the year 2000 is as follows:

2000 average daily consumption	808 Bbtu(1)
2000 peak daily consumption	1,504 Bbtu
Average cost of natural gas	$ 3.98 per MMBtu(2)

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(1) Billion British thermal units (Bbtu).

(2) Compared to $2.47 per million British thermal unit (MMBtu) in 1999 and $2.18 per MMBtu in 1998.

Through December 31, 2001, the Texas Utility Commission provides for recovery of most fuel and purchased power costs from customers through a fixed fuel factor included in electric rates. For additional information regarding our filings to recover these costs from our customers, please read Note 4(d) to our consolidated financial statements. For additional information regarding fuel factor adjustments once retail electric competition begins, please read "Regulation — State and Local Regulations — Texas — Electric Operations — The Legislation."

Although natural gas supplies have been sufficient in recent years, available supplies are subject to disruption due to weather conditions, transportation constraints and other events. As a result of these factors, supplies of natural gas may become unavailable from time to time or prices may increase rapidly in response to temporary supply constraints or other factors.

Coal and Lignite Supply. Our Electric Operations business segment purchases approximately 80% of the coal for its four coal-fired units under two long-term contracts from mines in Wyoming. The first of these contracts will expire in 2010, and the second will expire in 2011. We obtain the remaining coal required to operate these units under short-term contracts. Burlington Northern Santa Fe Railroad and Union Pacific Railroad Company transported our coal supply during 2000 under long-term rail transportation contracts. A new long-term rail transportation contract with Burlington Northern Santa Fe Railroad went into effect in March 2000.

We obtain the lignite used to fuel the two units of our Limestone Electric Generating station from a surface mine adjacent to the plant. We own the mining equipment, facilities and a portion of the lignite reserves located at this mine. We believe the lignite reserves we currently own under lease and contract will be sufficient to provide substantially all of the lignite requirements of this facility through 2015. During 2000, a test burn of subbituminous coal was performed at the Limestone station in order to determine its viability as a fuel for that station. As a component of our nitrogen oxides (NOx) control strategy for this station, we anticipate utilizing a blend of lignite and Wyoming subbituminous coal beginning in 2002. We expect that we will obtain Wyoming coal through spot and long-term contracts at a delivered price equivalent to that of lignite.

Nuclear Fuel Supply. The South Texas Project satisfies its fuel supply requirements by acquiring uranium concentrates, converting uranium concentrates into uranium hexafluoride, enriching uranium hexafluoride, and fabricating nuclear fuel assemblies.

We have numerous contracts covering a portion of our nuclear fuel needs for uranium, conversion services, enrichment services and fuel fabrication. These contracts have varying expiration dates and most are short to medium term (less than seven years). Management believes that sufficient capacity for nuclear fuel supplies and processing exists to preclude the impairment of normal operations of South Texas Project's nuclear generating units.

Purchased Power Supply. Our Electric Operations business segment purchases power from various qualifying facilities exercising their rights under the Public Utility Regulatory Policies Act of 1978. These purchases are generally at the discretion of the qualifying facility and are made pursuant to a pricing methodology defined in tariffs approved by the Texas Utility Commission. Reliant Energy HL&P purchased a total of 14.8 million megawatt hours (MWh) and 16.4 million MWh from qualified facilities in 1999 and 2000, respectively. Due to the Legislation and the commencement of wholesale competition, we anticipate terminating or renegotiating the contracts requiring us to purchase qualified facility power by the end of December 2001, as regulation culminates for the generation portion of our Electric Operations business segment.

From time to time, as market conditions dictate, we also purchase power under contracts from various wholesale market participants, exempt wholesale generators, power marketers and other utilities. For additional information regarding additional generation supply in ERCOT, please read "— Electric Operations Assets — Generation" above. The increase in supply could result in a lower cost per MWh in the open market, unless demand increases more than anticipated. As a result, we may purchase more power in the future than we have in the past.

Competition

Please read "Management's Discussion and Analysis of Financial Condition and Results of Operations — Certain Factors Affecting Our Future Earnings — Competitive, Regulatory and Other Factors Affecting Our Electric Operations" in Item 7 of this Form 10-K, which section is incorporated herein by reference.

NATURAL GAS DISTRIBUTION

Our Natural Gas Distribution business segment consists of intrastate natural gas sales to, and natural gas transportation for, residential, commercial and industrial customers in Arkansas, Louisiana, Minnesota, Mississippi, Oklahoma and Texas and some non-rate regulated retail gas marketing operations.

We conduct intrastate natural gas sales to, and natural gas transportation for, residential, commercial and industrial customers through three unincorporated divisions of RERC Corp.: Reliant Energy Arkla (Arkla), Reliant Energy Entex (Entex) and Reliant Energy Minnegasco (Minnegasco). These operations are regulated as gas utility operations in the jurisdictions served by these divisions.

- *Arkla.* Arkla provides natural gas distribution services in Arkansas, Louisiana, Oklahoma and Texas. The largest metropolitan areas served by Arkla are Little Rock, Arkansas and Shreveport, Louisiana. In 2000, approximately 68% of Arkla's total throughput was attributable to retail sales of gas and approximately 32% was attributable to transportation services.
- *Entex.* Entex provides natural gas distribution services in over 500 communities in Louisiana, Mississippi and Texas. The largest metropolitan area served by Entex is Houston, Texas. In 2000, approximately 97% of Entex's total throughput was attributable to retail sales of gas and approximately 3% was attributable to transportation services.
- *Minnegasco.* Minnegasco provides natural gas distribution services in over 240 communities in Minnesota. The largest metropolitan area served by Minnegasco is Minneapolis, Minnesota. In 2000, approximately 97% of Minnegasco's total throughput was attributable to retail sales of gas and approximately 3% was attributable to transportation services.

The demand for intrastate natural gas sales to, and natural gas transportation for, residential, commercial and industrial customers is seasonal. In 2000, approximately 73% of our Natural Gas Distribution business segment's revenues occurred in the first and fourth quarters. These patterns reflect the higher demand for natural gas for heating purposes during those periods.

Supply and Transportation

Arkla. In 2000, Arkla purchased approximately 57% of its natural gas supply from Reliant Energy Services, 15% pursuant to third-party contracts, with terms varying from three months to one year, and 28% on the spot market. Arkla's major third-party natural gas suppliers in 2000 included Oneok Gas Marketing Company, Marathon Oil Company and Aquila Energy Marketing Corporation. Arkla transports substantially all of its natural gas supplies under contracts with our pipeline subsidiaries. These transportation contracts were renegotiated during 2000 and have been extended to March 2005.

Entex. In 2000, Entex purchased virtually all of its natural gas supply pursuant to term contracts, with terms varying from one to five years. Entex's major third-party natural gas suppliers in 2000 included Enron North America Corp., Kinder Morgan Texas Pipeline, L.P., Gulf Energy Marketing, Island Fuel Trading and Koch Energy Trading. Entex transports its natural gas supplies on both interstate and intrastate pipelines under long-term contracts with terms varying from one to five years.

Minnegasco. In 2000, Minnegasco purchased approximately 81% of its natural gas supply pursuant to term contracts, with terms varying from one to ten years, with more than 25 different suppliers. Minnegasco purchased the remaining 18% on the daily or spot market. Most of the natural gas volumes under long-term contracts are committed under terms providing for delivery during the winter heating season, November through March. Minnegasco purchased approximately 64% of its natural gas requirements from four suppliers in 2000: Pan-Alberta Gas Ltd., Reliant Energy Services, TransCanada Gas Services Inc. and Duke Energy Trading and Marketing, LLC. Minnegasco transports its natural gas supplies on various interstate pipelines under long-term contracts with terms varying from five to ten years.

For additional information regarding our ability to pass through changes in natural gas prices to our customers, please read "Management's Discussion and Analysis of Financial Condition and Results of

Operations — Certain Factors Affecting Our Future Earnings — Competitive and Other Factors Affecting RERC Operations — Natural Gas Distribution" in Item 7 of this Form 10-K.

Arkla and Minnegasco use various leased or owned natural gas storage facilities to meet peak-day requirements and to manage the daily changes in demand due to changes in weather. Minnegasco also supplements contracted supplies and storage from time to time with stored liquefied natural gas and propane-air plant production.

Minnegasco owns and operates a 7.0 billion cubic feet (Bcf) underground storage facility, having a working capacity of 2.1 Bcf available for use during a normal heating season and a maximum daily withdrawal rate of 50 million cubic feet (MMcf) per day. Minnegasco also owns ten propane-air plants with a total capacity of 191 MMcf per day and on-site storage facilities for 11 million gallons of propane (1.0 Bcf gas equivalent). Minnegasco owns a liquefied natural gas facility with a 12 million-gallon liquefied natural gas storage tank (1.0 Bcf gas equivalent) with a send-out capability of 72 MMcf per day.

Although available natural gas supplies have exceeded demand for several years, currently supply and demand appear to be in balance. Our Natural Gas Distribution business segment has sufficient supplies and pipeline capacity under contract to meet its firm customer requirements. However, from time to time, it is possible for limited service disruptions to occur due to weather conditions, transportation constraints and other events. As a result of these factors, supplies of natural gas may become unavailable from time to time or prices may increase rapidly in response to temporary supply constraints or other factors.

Marketing and Sales

Our Natural Gas Distribution business segment's marketing and sales group provides comprehensive natural gas products and services to industrial and commercial customers in the region from Southern Texas to the panhandle of Florida, as well as in the Midwestern United States. In 2000, approximately 94% of total throughput was attributable to the sale of natural gas and approximately 6% was attributable to transportation services. Typical customer contract terms for natural gas sales range from one day to three years. Our marketing and sales groups' operations may be affected by seasonal weather changes, and the relative price of natural gas. In addition, this segment has performed as a natural gas marketer to residential and small commercial customers in several states where natural gas deregulation has occurred. In 2000, however, we decided to exit these markets in order to re-focus resources and efforts on different markets. Accordingly, we divested our retail customer contracts in non-strategic areas during 2000 and completed the sale of our Georgia retail agreements in March 2001.

Assets

As of December 31, 2000, we owned approximately 60,000 linear miles of gas distribution mains, varying in size from one-half inch to 24 inches in diameter. Generally, in each of the cities, towns and rural areas served by our Natural Gas Distribution business segment, we own the underground gas mains and service lines, metering and regulating equipment located on customers' premises and the district regulating equipment necessary for pressure maintenance. With a few exceptions, the measuring stations at which we receive gas from our suppliers are owned, operated and maintained by others, and our distribution facilities begin at the outlet of the measuring equipment. These facilities, including odorizing equipment, are usually located on the land owned by suppliers.

Competition

Please read "Management's Discussion and Analysis of Financial Condition and Results of Operations — Certain Factors Affecting Our Future Earnings — Competitive and Other Factors Affecting RERC Operations — Natural Gas Distribution" in Item 7 of this Form 10-K, which section is incorporated herein by reference.

PIPELINES AND GATHERING

Our Pipelines and Gathering business segment operates two interstate natural gas pipelines as well as gas gathering and pipeline services. Our pipeline operations are conducted by two wholly owned interstate pipeline subsidiaries of RERC Corp., Reliant Energy Gas Transmission Company (REGT) and Mississippi River Transmission Corporation (MRT). Our gathering and pipeline services operations are conducted by a wholly owned gas gathering subsidiary, Reliant Energy Field Services, Inc. (REFS), and a wholly owned pipeline services subsidiary, Reliant Energy Pipeline Services, Inc. (REPS). In 2000, we stopped reporting the results of operations from our gathering operations, assets and business in our Wholesale Energy business segment and began reporting these results in our former Interstate Pipelines business segment, which was renamed the "Pipelines and Gathering" business segment.

Through REFS, we provide natural gas gathering and related services, including related liquids extraction and other well operating services. As of December 31, 2000, REFS operated approximately 4,000 miles of gathering pipelines, which collect natural gas from more than 200 separate systems located in major producing fields in Arkansas, Louisiana, Oklahoma and Texas. Through REPS we provide pipeline project management and facility operation services to affiliates and third parties.

In 2000, approximately 29% of our Pipelines and Gathering business segment's total operating revenue was attributable to services provided by REGT to Arkla, and approximately 14% of its total operating revenue was attributable to services provided by MRT to Laclede Gas Company (Laclede), an unaffiliated distribution company that provides natural gas utility service to the greater St. Louis metropolitan area in Illinois and Missouri. An additional 15% of our Pipelines and Gathering business segment's operating revenues was attributable to the transportation of gas marketed by Reliant Energy Services. Our Pipelines and Gathering segment provides service to Arkla and Laclede under several long-term firm storage and transportation agreements. At the end of 2000, REGT renewed various contracts for firm transportation and storage services with Arkla. These renewals extended the term of service in Arkla's major areas to 2005. The expiration dates for the service agreements with Laclede range from October 2001 through May 2002. We are currently negotiating the terms and conditions of a renewal of these agreements with Laclede.

The business and operations of our Pipelines and Gathering business segment may be affected by seasonal changes in the demand for natural gas, the relative price of natural gas in the Midcontinent and Gulf Coast natural gas supply regions and, to a lesser extent, general economic conditions.

Assets

We own and operate approximately 8,200 miles of gas transmission lines. We also own and operate six natural gas storage fields with a combined daily deliverability of approximately 1.2 Bcf per day and a combined working gas capacity of approximately 55.8 Bcf. REGT also owns a 10% interest, with Gulf South Pipeline Company, LP, in the Bistineau storage facility with 68.8 Bcf of working gas capacity and 1.1 Bcf per day of deliverability. REGT's storage capacity in the Bistineau facility is 18 Bcf (8 Bcf of working gas) with 100 MMcf per day of deliverability. Most of our storage operations are in north Louisiana and Oklahoma. We also own and operate approximately 4,000 miles of gathering pipelines that collect gas from more than 200 separate systems located in major producing fields in Arkansas, Louisiana, Oklahoma and Texas.

Competition

Please read "Management's Discussion and Analysis of Financial Condition and Results of Operations — Certain Factors Affecting Our Future Earnings — Competitive and Other Factors Affecting RERC Operations — Pipelines and Gathering" in Item 7 of this Form 10-K, which section is incorporated herein by reference.

WHOLESALE ENERGY

Our Wholesale Energy business segment provides electricity and energy services in the competitive segments of the United States electric power industry. We acquire, develop and operate electric power generation facilities that are not subject to traditional cost-based regulation. Therefore, under current statutes and regulations we can sell power at prices determined by the market. We also trade and market power, natural gas and other energy-related commodities and provide related risk management services.

Power Generation Operations

As of December 31, 2000, our Wholesale Energy business segment owned or leased electric power generation facilities with an aggregate net generating capacity of 9,231 MW located in five regions of the United States. We also had 2,766 MW of generating capacity under construction as of that date.

The following table describes our Wholesale Energy business segment's power generation facilities by region as of December 31, 2000:

Regional Summary Of Our U.S. Generation Facilities

Region	Number of Generation Facilities	Total Net Generating Capacity(MW)	Dispatch Type(1)	Primary Fuel
Mid-Atlantic				
Operating	21	4,262	Base, Inter, Peak	Gas/Coal/Oil/Hydro
Southwest				
Operating	6	4,045	Base, Inter, Peak	Gas
Under Construction	1	563	Base, Peak	Gas
Combined	7	4,608		
Midcontinent				
Operating	1	255	Peak	Gas
Under Construction	1	962	Peak	Gas
Combined	2	1,217		
Florida				
Operating	1	619	Inter, Peak	Gas/Oil
Under Construction	1	460	Peak	Gas/Oil
Combined	2	1,079		
Texas(2)				
Operating	1	50	Base, CoGen	Gas
Under Construction	1	781	Base, CoGen	Gas
Combined	2	831		
Total				
Operating	30	9,231		
Under Construction	4	2,766		
Combined	34	11,997		

(1) The designations "Base," "Inter," "Peak" and "CoGen" indicate whether the facilities described are base-load, intermediate, peaking or cogeneration facilities, respectively. "Cogeneration" means the combined production of steam and electricity in a generation facility.

(2) Reliant Resources, which holds our Wholesale Energy operations, has an option exercisable in January 2004 to acquire Reliant Energy's interest in Texas Genco, a partnership that is expected to own 14,040 MW of net generating capacity in Texas. For additional information regarding Texas Genco and this option, please read "— Electric Operations — Texas Genco" in Item 1 of this Form 10-K.

The following sections describe the power generation operations and facilities of our Wholesale Energy business segment by region:

Mid-Atlantic Region. As of December 31, 2000, we owned or leased 21 electric power generation facilities with an aggregate net generating capacity of 4,262 MW located in the Pennsylvania-New Jersey-Maryland market (PJM market). These facilities are owned or leased by subsidiaries of Reliant Energy Mid-Atlantic Power Holdings, LLC (REMA) and include 2,009 MW of base-load, 803 MW of intermediate and 1,450 MW of peaking capacity, and represent approximately 7% of the total generation capacity in the PJM market. We sell the power generated by these facilities to customers located in the PJM market and to buyers in adjacent electricity markets. The PJM market is one of the most mature and liquid electricity markets functioning in the United States. In the PJM market, buyers and sellers "clear" their transactions through an hourly auction process. In addition, buyers and sellers can negotiate their own contracts outside of the auction process. We sell power in this market both through the hourly auction process and under negotiated contracts. We purchased our Mid-Atlantic generation facilities from Sithe Energies, Inc. in May 2000 for an aggregate purchase price of $2.1 billion. For additional information related to the purchase of the Mid-Atlantic generation facilities, please read Note 3(a) to our consolidated financial statements.

Southwest Region. As of December 31, 2000, we owned six electric power generation facilities with an aggregate net generating capacity of 4,045 MW located in the states of California and Nevada. These facilities include 240 MW of base-load, 3,395 MW of intermediate and 410 MW of peaking capacity and represent approximately 5% of the total generation capacity in the Southwest region, which encompasses a region in the southwest part of the United States that includes the states of Arizona and California, and portions of the states of New Mexico and Nevada. This region contains approximately 15% of the U.S. population. We sell the power generated by these facilities to customers located in the Southwest region.

We purchased five plants from Southern California Edison Company (SCE) in three transactions in 1998 for an aggregate purchase price of $292 million. Although we exercise management authority over these five plants, we have contracted with SCE to operate and maintain these plants through March 2003. However, we have elected to terminate these contracts effective April 2001.

We own a 50% interest in a 490 MW gas-fired, base-load/peaking facility located near Las Vegas, Nevada. Sempra Energy owns the other 50% interest in this plant. We invested $77 million to develop this plant, which has been in commercial operation since May 2000.

In addition, we have a 563 MW gas-fired, base-load/peaking generation facility under construction in Casa Grande, Arizona. As of December 31, 2000, the engineering work for this facility had been completed and the construction work was approximately 65% complete. Based on this status, we expect this facility will begin commercial operation in the third quarter of 2001.

California was among the first states to restructure its electricity markets, based on the establishment of a pool-based bidding system for wholesale energy and the transfer of authority over the transmission system to the California Independent System Operator (Cal ISO). Although buyers and sellers in California originally transacted for short-term, day-ahead and day-of power through the California Power Exchange (Cal PX), the Cal PX suspended its day-ahead and day-of markets effective January 31, 2001 and filed for bankruptcy protection on March 9, 2001. Consequently, the majority of power that is not generated by the utilities' own generation is currently sold through bilateral contracts or in the Cal ISO's real-time market. For information about the current market conditions in California, please read "Regulation — State and Local Regulations — California" in Item 1 of this Form 10-K and "Management's Discussion and Analysis of Financial Condition and Results of Operations — Certain Factors Affecting Our Future Earnings — Competitive, Regulatory and Other Factors Affecting Our Wholesale Energy Operations — California" in Item 7 of this Form 10-K, as well as Notes 14(h) and 14(g) to our consolidated financial statements.

In the Southwest region, there is presently no regional transmission organization (RTO) in place to manage the transmission systems or to operate energy markets on a region-wide basis, although two RTO working groups are evaluating the establishment of an organization that would assume control, subject to

Federal Energy Regulatory Commission (FERC) approval, over the transmission systems of the utilities operating in this region.

Midcontinent Region. We own two electric power generation facilities in the Midcontinent region. One gas-fired peaking generation facility is located in Shelby County, Illinois. As of December 31, 2000, six of the eight generating units at this facility were in commercial operation. When all of the generating units at this plant are in commercial operation, it will have an aggregate net generating capacity of 344 MW. We expect the remaining two units to be operational by May 2001. We sell the power generated by this facility on the open market. This facility was placed in commercial operation in June 2000 at an aggregate cost of $182 million. Upon completion, we anticipate the total cost of developing this facility will be approximately $210 million.

We also have an 873 MW gas-fired peaking generation facility under construction in Aurora, Illinois. As of December 31, 2000, the engineering work for this facility was approximately 79% complete and the construction work was approximately 54% complete. Based on this status, we expect this facility will begin commercial operation in the second quarter of 2001.

Our Illinois generating facilities are located in the Midcontinent region near Chicago and primarily sell their output in the Mid-America Interconnected Network reliability council. However, they are capable of serving the entire Midcontinent region. The Midcontinent region encompasses all or a portion of three reliability councils that include the states of Illinois, Wisconsin, Missouri, Indiana, Ohio, Michigan, Virginia, West Virginia, Tennessee, Maryland, Mississippi, Pennsylvania, Alabama, Georgia and Kentucky.

Florida. We own one gas and oil-fired intermediate/peaking generation facility with an aggregate net generating capacity of 619 MW located near Titusville, Florida (Indian River plant). This facility can be operated as either an intermediate or a peaking facility and represents approximately 1.5% of the total generation capacity in the state of Florida. We sell up to 593 MW of the power generated by this facility to the Orlando Utilities Commission (OUC) under a four-year power purchase agreement that was scheduled to terminate in September 2003. OUC has exercised its option to extend the power purchase agreement to September 2007 at a base capacity of 500 MW. Any excess power generated by the plant is sold to other utilities and rural electric cooperatives within the region. We purchased this facility from OUC in October 1999 for a net purchase price of $188 million.

In addition to our Indian River plant, we are beginning construction on a 460 MW gas- and oil-fired peaking generation facility in Osceola County, Florida. As of December 31, 2000, the engineering work for this facility was approximately 56% complete and the construction work was approximately 9% complete. We expect this facility will begin commercial operation in the third quarter of 2001.

In the first quarter of 2001, we entered into tolling arrangements with a third party to purchase the rights to utilize and dispatch electric generating capacity of approximately 1,100 MW. This electricity is expected to be generated by two gas-fired, simple-cycle peaking plants, with fuel oil backup, to be constructed by the tolling partner in Florida, which are anticipated to be completed by the summer of 2002.

The state of Florida (other than a portion of the western panhandle) constitutes a single reliability council and contains approximately 5% of the U.S. population. Florida is in the process of establishing an independent system operator that will further define the rules and requirements around which a competitive wholesale market will develop. Transactions in the Florida market are presently non-standard and highly negotiated for terms and conditions. Until the rules for system operations are established, we expect the Florida market to continue to be illiquid.

Texas. We own a 50% interest in a 100 MW gas-fired base/cogeneration facility in Orange, Texas (Sabine plant). Air Liquide owns the other 50% interest in this plant. The Sabine plant, in which we invested $32 million, has been in commercial operation since December 1999. In addition to the Sabine plant, we currently have a 781 MW gas-fired, combined cycle, cogeneration facility under construction in Channelview, Texas (Channelview plant). As of December 31, 2000, the engineering work for this facility was approximately 75% complete and the construction work of Phase I (which consists of 171 MW) was approximately 30% complete. Based on this status, we expect this facility will begin commercial operation in the third quarter

of 2001. Equistar Chemicals, L.P. has agreed to purchase up to 293 MW of the Channelview plant's capacity under a 17-year contract. Discussions regarding the possible sale of a substantial portion of the balance of the output of the plant on a long-term basis are currently underway.

Development Activities

We intend to continue to grow the generation asset portfolios of our Wholesale Energy business segment by developing additional capacity either through building new facilities or expanding existing facilities in our domestic regional markets. As of December 31, 2000, we had 2,766 MW of projects under construction. We consider a project to be "under construction" once we have acquired the necessary permits to begin construction, broken ground at the project site and contracted to purchase machinery for the project, including the combustion turbines. In addition, we have a significant number of other projects that are in various stages of development. These projects may or may not have received all of the necessary permits and approvals to begin construction. We cannot assure you that these projects will be completed. As of March 1, 2001, we had the right to purchase 47 new combustion turbines from General Electric Company and Siemens Westinghouse Power Corporation scheduled for delivery by the third quarter of 2003, representing approximately 6,324 MW of generating capacity for an aggregate purchase price of approximately $1.3 billion. Some of these combustion turbines will be utilized in both simple cycle and combined cycle configurations. The combined cycle configurations will result in increased capacity due to the additional electricity generated by the associated steam turbines. Consequently as of March 1, 2001, the total maximum plant capacity for these turbine commitments is approximately 7,991 MW.

Domestic Trading, Marketing, Power Origination and Risk Management Operations

In addition to our power generation operations, we trade and market power, natural gas and other energy-related commodities and provide related risk management services to our customers. Our domestic trading, marketing, power origination and risk management operations complement our domestic power generation operations by providing a full range of energy management services. These services include management of the sales and marketing of energy, capacity and ancillary services from these facilities, and also management of the purchase and sale of fuels and emissions allowances needed to operate these facilities. Generally we seek to sell a portion of the capacity of our domestic facilities under fixed-price sale contracts, fixed-capacity payments or contracts to sell generation at a predetermined multiple of either gas or oil prices. This provides us with certainty as to a portion of our margins while allowing us to maintain flexibility with respect to the remainder of our generation output. We evaluate the regional forward power market versus our own fundamental analysis of projected future prices in the region to determine the amount of our capacity we would like to sell and the terms of sale pursuant to longer-term contracts. We also take operational constraints and operating risk into consideration in making these determinations. Generally we seek to hedge a portion of our fuel costs, which are usually linked to a percentage of our power sales. We also market energy-related commodities and offer physical and financial wholesale energy marketing and price risk management products and services to a variety of customers. These customers include natural gas distribution companies, electric utilities, municipalities, cooperatives, power generators, marketers or other retail energy providers, aggregators and large volume industrial customers.

The following table illustrates the growth of our physical power and gas trading volumes since 1998:

Trading Volumes

	For the Year Ended December 31,		
	1998	1999	2000
Total Power (MWh)	65,227,898	112,133,103	201,938,485
Total Gas (MMBtu)(1)	1,163,124,196	1,820,261,473	2,509,206,281

(1) These figures include sales to RERC's natural gas distribution companies.

Electric Power Trading and Marketing. We purchase electric power from other generators and marketers and sell power primarily to electric utilities, municipalities and cooperatives and other marketing companies. Our trading and marketing group is also responsible for the marketing of power produced from the power plants we own. We also provide risk management, physical and financial fuel purchase and power sales and optimization services to our customers.

Power Origination. We have a specific group of employees focused on developing and providing customers with long-term customized products (power origination products). These products are designed and negotiated on a case-by-case basis to meet the specific energy requirements of our customers. Our power origination teams work closely with our trading and marketing group and our power generation group to sell long-term products from our power generation assets. They also work to leverage our market knowledge to capture attractive opportunities available through selling products that combine or repackage energy products purchased from third parties with other third-party products or with products from our power generation assets. Our efforts to sell power origination products from our power generation assets have been focused on longer-term forward sales to municipalities, cooperatives and other companies that serve end users, as well as sales of near-term products that are not widely traded. Our power origination products that combine or repackage third-party products are generally highly structured and therefore require the application of our commercial capabilities (*e.g.*, power trading and asset positions).

Natural Gas Trading and Marketing. We purchase natural gas from a variety of suppliers under daily, monthly, variable-load, base-load and term contracts that include either market-sensitive or fixed pricing provisions. We sell natural gas under sales agreements that have varying terms and conditions, most of which are intended to match seasonal and other changes in demand. We sold an average of 6.9 Bcf per day of natural gas in 2000, an average of 5.0 Bcf per day in 1999 and an average of 3.2 Bcf per day in 1998, some of which was sold to our natural gas distribution companies. We plan to continue to purchase natural gas to supply our power plants.

Our natural gas marketing activities include contracting to buy natural gas from suppliers at various points of receipt, aggregating natural gas supplies and arranging for their transportation, negotiating the sale of natural gas, and matching natural gas receipts and deliveries based on volumes required by customers. We make transportation arrangements with affiliated and non-affiliated interstate and intrastate pipelines through a variety of means, including short-term and long-term firm and interruptible agreements. We also enter into various short-term and long-term firm and interruptible agreements for natural gas storage in order to offer peak delivery services to satisfy winter heating and summer electric generating demands. These services are also intended to provide an additional level of performance security and backup services to our customers.

Other Commodities and Derivatives. We trade and market other energy-related commodities. We use derivative financial instruments to manage and hedge our fixed-price purchase and sale commitments and to provide fixed-price or floating-price commitments as a service to our customers and suppliers. We also use derivative financial instruments to reduce our exposure relative to the volatility of the cash and forward market prices and to protect our investment in storage inventories. For additional information regarding our financial exposure to derivative financial instruments, please read "Management's Discussion and Analysis of Financial Results and Operations — Certain Factors Affecting Our Future Earnings — Competitive, Regulatory and Other Factors Affecting Our Wholesale Energy Operations — Price Volatility" in Item 7 of this Form 10-K and "Quantitative and Qualitative Disclosures About Market Risk" in Item 7A of this Form 10-K.

Risk Management Controls. We control the scope of our trading, marketing, power origination and risk management operations through a comprehensive set of policies and procedures involving senior levels of our management. Our Board of Directors sets the risk limit parameters and the audit committee of the Board has oversight for the ongoing evaluation of the adequacy of the risk control organization and policies. A risk oversight committee, comprised of corporate and business segment officers, oversees all of our activities, which include commodity price, credit, foreign currency, equity and interest rate risk, including our trading, marketing, power origination and risk management operations. The committee also proposes value-at-risk limits to our Board of Directors. Our Board ultimately sets our aggregate value-at-risk limit. We have a corporate risk control organization, headed by a chief risk control officer, which is assigned responsibility for

establishing and enforcing the policies, procedures and limits and evaluating the risks inherent in proposed transactions. Key risk control activities include credit review and approval, credit and performance risk measurement and monitoring, validation of transactions, portfolio valuation, and daily portfolio reporting for our trading and asset activities, including mark-to-market valuation, value-at-risk and other risk measurement metrics. For additional information regarding our risk management accounting policies, please read "Quantitative and Qualitative Disclosures About Market Risk" in Item 7A of this Form 10-K.

Competition

Please read "Management's Discussion and Analysis of Financial Condition and Results of Operations — Certain Factors Affecting Our Future Earnings — Competitive, Regulatory and Other Factors Affecting Our Wholesale Energy Operations" in Item 7 of this Form 10-K, which section is incorporated herein by reference.

EUROPEAN ENERGY

Our European Energy business segment includes the operations of N.V. UNA (UNA) and its subsidiaries and our European trading, marketing and risk management operations. We created this segment in the fourth quarter of 1999 with the acquisition of UNA and the formation of our European trading, marketing and risk management operations. For additional information regarding our acquisition of UNA, please read Note 3(b) to our consolidated financial statements. Our European Energy business segment generates and sells power from its generation facilities in the Netherlands and participates in the emerging wholesale energy trading and marketing industry in Northwest Europe.

European Power Generation Operations

Facilities. As of December 31, 2000, we owned five electric power generation facilities with an aggregate net generating capacity of 3,476 MW located in the Netherlands. These facilities are grouped in three clusters in the Amsterdam, Utrecht and Velsen regions. UNA is the third largest generating company in the Netherlands in terms of both installed capacity and electricity production. In 2000, UNA generated more than 20% of the country's electricity production, excluding electricity generated by cogeneration or other industrial processes. In addition to electricity, UNA's generating stations supply a number of municipalities, including Amsterdam, Nieuwegein, Utrecht and Purmerend, with hot water for district heating purposes in cooperation with two large Dutch distribution companies. In 2000, approximately 47% of UNA's generation output was natural gas-fired, 15% was blast furnace gas-fired, 38% was coal-fired and less than 1% was oil-fired. UNA procures its gas from Gasunie, the monopoly gas supplier in the Netherlands. UNA procures its coal from GKE, a coal trading and supply company owned jointly by UNA and one of the other large Dutch generation companies.

We acquired UNA, then named N.V. Energieproduktiebedrijf UNA, effective in October 1999. UNA was the first Dutch generating company to have its stock sold to investors under a privatization program established under the Dutch Electricity Act. The total net purchase price of the acquisition was $1.9 billion based on the October 7, 1999 exchange rate of 2.06 Dutch Guilders (NLG) per U.S. dollar.

The following table describes the electric power generation facilities we owned in the Netherlands as of December 31, 2000:

Dutch Generation Facilities

Generation Facilities(1)	Location	Net Generating Capacity (MW)	Dispatch Type(2)	Primary Fuel
Hemweg	Amsterdam	1,229	Base, Peak	Coal/Gas
Velsen	Velsen	990	Base, Inter, Peak	Gas/Blast Furnace Gas
Utrecht	Utrecht	939	Base, Inter, Peak	Gas/Oil
Diemen	Amsterdam	249	Base	Gas
Purmerend	Purmerend	69	Inter	Gas
Total		3,476		

(1) We own a 100% interest in each facility listed. All of these facilities are operational.

(2) The designations "Base," "Inter" and "Peak" indicate whether the facilities described are base-load, intermediate or peaking facilities, respectively.

Market Framework. The Netherlands has a peak demand of approximately 14,200 MW. In 1999, UNA and the three other largest Dutch generating companies supplied approximately 52% of the electricity consumed in the Netherlands. Smaller Dutch producers supplied about 30% of consumed electricity and the remainder was imported. The wholesale market opened to competition on January 1, 2001. The retail market has been open to competition for large industrial customers since January 1, 1999. In 2002, the next retail segment, composed primarily of commercial customers, will open to competition. The remaining customers, mainly residential users, are expected to be able to choose their supplier by early 2003. The timing of the opening of these markets is subject to change at the discretion of the Dutch Minister of Economic Affairs.

Customers who can select their electric supplier have the choice of purchasing power through bilateral contracts or on the Amsterdam Power Exchange, which was the first power exchange in Northwest Europe and has been in operation since the spring of 1999. Distribution companies, which serve the captive customers in the Netherlands, are effectively required to purchase a substantial amount of their requirements through bilateral contracts with a term of at least one year.

With the start of full-scale wholesale deregulation in January 2001, the high voltage transmission grid company (TenneT) has taken on the role of independent system operator. In this role, TenneT is responsible for the stability of the transmission grid.

European Trading, Marketing and Risk Management Operations

In October 1999, we established our European trading, marketing and risk management operations in order to participate in the emerging European energy trading and marketing businesses. We are initially focusing on trading opportunities in the Netherlands and Germany and plan to expand into other European markets in the future. Our marketing operations will initially concentrate on selling power to large industrial and commercial customers as well as distribution companies.

Our European trading, marketing and risk management operations utilize a business model, including risk management and control policies, that is similar to that utilized in our operations in the United States, while recognizing relevant differences between these markets. Currently, the primary difference is a much lower level of liquidity in both gas and power markets in Continental Europe than in the United States. This difference is largely the result of market maturity. In the United States, natural gas deregulation preceded power deregulation and began over a decade ago. In Continental Europe, restructuring of the power markets began less than two years ago and restructuring of the gas markets is only just beginning. Given the strides made thus far in Europe and the lessons learned from energy deregulation in the United States, the United

Kingdom and other countries around the world, we expect liquidity to increase steadily in European gas and power markets. We expect to capitalize on these developments by drawing on our U.S. and European experiences to offer the types of products and services that customers will need in the new and developing environment. As of December 31, 2000, our European trading, marketing and risk management operations had committed to sell the full amount of UNA's targeted sales through 2001.

Competition

Please read "Management's Discussion and Analysis of Financial Condition and Results of Operations — Certain Factors Affecting Our Future Earnings — Competitive, Regulatory and Other Factors Affecting Our European Energy Operations" in Item 7 of this Form 10-K, which section is incorporated herein by reference.

OTHER OPERATIONS

Our Other Operations business segment includes:

- the operations of our unregulated retail electric businesses,
- the operations of our communications business (Communications),
- the operations of our eBusiness group,
- the operations of our venture capital division (New Ventures),
- the operations of Reliant Energy Thermal Systems, Inc. (Reliant Energy Thermal Systems),
- various office buildings and other real estate used in our business operations,
- unallocated corporate costs, and
- inter-segment eliminations.

Unregulated Retail Electric Businesses

We intend to become a provider of retail electric services in Texas through Reliant Energy Retail Services, LLC (Services) and Reliant Energy Solutions, LLC (Solutions) when the market opens to retail competition in January 2002. Beginning with full retail electric competition in Texas on January 1, 2002, we will provide electricity and related products and services to residential and small commercial customers through Services, and we will offer customized, integrated electric commodity, energy management and e-commerce services to the large commercial and industrial customers through Solutions. Both Services and Solutions have been certified as retail electric providers by the Texas Utility Commission, and both are wholly owned, indirect subsidiaries of Reliant Resources.

Services will provide retail electric services to all of the approximately 1.5 million residential and small commercial customers served by Reliant Energy HL&P located in its certificated service area who do not take action to select another retail electric provider. Services will be the affiliated retail electric provider in Reliant Energy HL&P's certificated service area (both before and after the Distribution) and will be a non-affiliated retail electric provider in other parts of Texas. For additional information regarding retail electric competition, please read "Regulation — State and Local Regulations — Texas — Electric Operations — The Legislation" in Item 1 of this Form 10-K.

In preparation for retail electric competition in Texas, we are expanding an infrastructure of business systems, procedures and practices to meet the needs of our retail businesses. These include a customer care system module and wholesale/retail energy supply, risk management, e-commerce, scheduling/settlement, customer relationship management and sales force automation systems. As of December 31, 2000, we had spent $50 million on retail infrastructure development. In addition, we plan to spend approximately $48 million by the end of 2001.

Market Framework. For additional information regarding the Legislation, retail competition and its application to our operations and structure, please read "Our Business — Restructuring," "Electric Operations," and "Regulation — State and Local Regulations — Texas — Electric Operations — The Legislation" in Item 1 of this Form 10-K, "Management's Discussion and Analysis of Financial Condition and Results of Operations — Certain Factors Affecting Our Future Earnings — Competitive, Regulatory and Other Factors Affecting Our Electric Operations" in Item 7 of this Form 10-K and Note 4 to our consolidated financial statements, which sections and note are incorporated herein by reference.

Solutions. Solutions provides customized, integrated energy solutions, including commodity, risk management and energy services products, and demand side and eBusiness management services to large commercial and industrial customers. These services include the replacement or upgrade of energy-intensive capital equipment, infrastructure optimization, substation development, maintenance and control, and power quality assurance. Solutions targets institutional, government, manufacturing, industrial and large commercial customers, including multisite retailers and restaurants, petroleum refineries, chemical companies, and internet data centers. These customers typically have a peak electricity demand of greater than one MW for the aggregate of their Texas facilities. As of December 31, 2000, this customer segment in Texas included approximately 7,000 customer accounts or metered service points (approximately 2,000 buying organizations) consuming an aggregate of 100 million MWh of electricity per year.

Since its formation in April 1996, Solutions has completed over 220 projects for large commercial, institutional, governmental and industrial clients. In November 1999, Solutions acquired the Energy Service Division of Southland Industries, Inc. for $37 million. This strategic acquisition strengthened Solutions' engineering and project management expertise and established a comprehensive marketing arrangement with Southland Industries, a leading engineering and construction firm. Solutions has also developed an integrated product offering to serve both the commodity and energy services needs of its customers.

Communications

We formed our Communications business to be a single-source, integrated communications provider, offering web hosting and web design, enhanced data services, and local and long distance voice services to business customers within Texas. In November 1999, we began operation as a competitive local exchange carrier offering resold voice and data services to small and mid-sized business customers in Houston. In April 2000, we acquired Insync Internet Services, a business-to-business Internet services provider based in Houston with an additional presence in Austin and remote facilities in Dallas and San Antonio. Communications now serves as a facilities-based competitive local exchange carrier and Internet services provider with switching capacity, access to a fiber corridor that surrounds the Houston metropolitan area as well as network operations centers and managed data centers in Houston and Austin. As of December 31, 2000, we provided enhanced data services and local and long distance voice services to approximately 2,600 customers in Texas. The voice and data transmission markets in which we operate are highly competitive. We compete with a broad range of competitors, including the regional local exchange incumbent. Our Communications group has been transferred to Reliant Resources.

eBusiness

We formed our eBusiness group in November 1999 to manage, expand and enhance our Internet presence and capabilities. The eBusiness group is charged with facilitating Internet use by our core businesses and, through Reliant Energy Net Ventures, Inc., investing in and managing a portfolio of Internet-related businesses. As of December 31, 2000, our eBusiness group had invested $18 million in the following new Internet-based businesses:

- *Pantellos.* In June 2000, we, along with 20 other leading power, gas and pipeline companies, formed Pantellos, an energy industry e-procurement marketplace. The newly formed company is beginning to deliver a broad suite of integrated e-supply chain solutions to the electric, natural gas distribution, natural gas pipeline and other energy sectors. This marketplace, located at *www.pantellos.com*, became

operational in January 2001. We expect Pantellos' primary competitors will be online vertical marketplaces, such as Enporion.com and UtilityFrontier.com.

- *IntercontinentalExchange.* In July 2000, we, along with five other natural gas and power companies, American Electric Power, Aquila Energy, Duke Energy, El Paso Corporation and Mirant (formerly known as Southern Energy), made an investment in IntercontinentalExchange, a new, web-based system for trading commodities. These six companies accounted for approximately 28% of the natural gas volumes and 32% of the power volumes traded in the U.S. market in 2000. The exchange, *www.intcx.com,* began trading precious metals in August 2000 and began trading crude oil, oil products, natural gas and electricity in October 2000. The potential benefits of this investment include reducing our cost structure and facilitating trading activity by combining the liquidity of many of the large traders. The principal online competitors of IntercontinentalExchange are EnronOnline, HoustonStreet.com and Altra.com in addition to more traditional exchanges, such as NYMEX.

The operations of our eBusiness group are conducted, and our ownership interest in the aforementioned eBusinesses are held, by wholly owned subsidiaries of Reliant Resources.

New Ventures

In August 1998, we formed our New Ventures division to manage our existing new technology investments and to identify and invest in promising new technologies and businesses that relate to our energy services operations. Focus areas for investment include distributed generation, power quality, clean energy, energy industry software and systems, and broadband infrastructure.

We make our investments either directly or indirectly as limited partners in venture capital funds. As of December 31, 2000, we have invested $30 million in five venture capital funds with an energy, utility and communications focus and have made commitments to invest an additional $14 million in these funds. As of December 31, 2000, these funds held investments in 43 companies. Excluding our investment in Grande Communications, Inc. discussed below, New Ventures' direct investment portfolio consists of eight companies with a total of $8 million invested as of December 31, 2000.

In September 2000, we agreed to make a $25 million equity investment in Grande Communications, Inc. Grande Communications is a Texas-based communications company building a deep fiber broadband network that will offer bundled services, including high-speed Internet, all-distance telephone and advanced cable entertainment to homes and businesses. We are also committed, under specified conditions, to invest a similar amount in a future Grande Communications equity financing. Grande Communications has announced its intention to build a broadband network in the Houston area and has secured a cable franchise from the city of Houston. The Houston buildout will be in addition to buildouts in the Central Texas cities of Austin, San Marcos and San Antonio which are already under development.

Our competitors include other large electricity, energy services and communications companies with venture capital operations and venture capital and private equity funds. Both we and our competitors are subject to the fluctuations in the private and public capital markets that may seriously impair our ability to participate in attractive opportunities for future investments and/or liquidate investments by private or public market sale.

Our New Ventures operations are wholly owned by Reliant Resources.

Reliant Energy Thermal Systems

Reliant Energy Thermal Systems provides a comprehensive range of products and services, including energy and facility management, engineering, construction and operation of site-specific heating and cooling plants for projects, such as buildings, universities and hospitals, as well as district cooling systems for cities and large metropolitan areas. Reliant Energy Thermal Systems, in conjunction with Exelon Thermal Systems of Chicago, also operates the Northwind Houston district cooling plant, which serves downtown Houston's

central business district with low-temperature chilled water services. Reliant Energy Thermal Systems is a wholly owned subsidiary of Reliant Energy and will become a subsidiary of the Regulated Holding Company.

REGULATION

We are subject to regulation by various federal, state, local and foreign governmental agencies, including the regulations described below.

Public Utility Holding Company Act

Holding Company Status. Reliant Energy is both a public utility holding company and an electric utility company as defined in the Public Utility Holding Company Act of 1935 (1935 Act); however, it is exempt from regulation as a holding company under Section 3(a)(2) of the 1935 Act. Although RERC Corp. is a gas utility company as defined under the 1935 Act, it is not a holding company within the meaning of the 1935 Act. Reliant Energy and RERC Corp. remain subject to regulation under the 1935 Act with respect to certain acquisitions of voting securities of other domestic public utility companies and utility holding companies.

Section 33(a)(1) of the 1935 Act exempts foreign utility company affiliates of Reliant Energy and RERC Corp. from regulation as "public utility companies," thereby permitting Reliant Energy and RERC Corp. to invest in foreign utility companies without registration under the 1935 Act as a holding company or approval by the SEC. The exemption, however, is subject to the SEC having received certification from each state commission having jurisdiction over the retail rates of any electric or gas utility company affiliated with Reliant Energy or RERC Corp. that such commission has the authority and resources to protect ratepayers subject to its jurisdiction and that it intends to exercise its authority. The Texas Utility Commission and the state regulatory commissions exercising jurisdiction over RERC Corp. (Arkansas, Louisiana, Minnesota, Mississippi, Oklahoma and Texas) have provided a certification to the SEC subject, however, to the right of such commissions to revise or withdraw their certifications as to any future acquisition of a foreign utility company. The Texas Utility Commission and the state regulatory commissions of Arkansas and Minnesota have imposed limitations on the amount of investments by utility companies (including Reliant Energy and RERC Corp.) in foreign utility companies and, in some cases, foreign electric wholesale generating companies. These limitations are based upon a utility company's consolidated net worth, retained earnings, and debt and stockholders' equity, respectively.

Subject to some limited exceptions, Section 33(f)(1) of the 1935 Act also prohibits any public utility company from issuing any security for the purpose of financing the acquisition, ownership or operation of a foreign utility company, or assuming any obligation or liability in respect of any security of a foreign utility company.

In connection with the Restructuring, the Regulated Holding Company will register as a public utility holding company under the 1935 Act. Such registration will subject the Registered Holding Company to extensive reporting and accounting requirements mandated by the 1935 Act, including the filing of an annual report with the SEC and the requirement that recordkeeping is done in accordance with SEC regulations related to registered holding companies. The Registered Holding Company will generally be required to obtain SEC approval prior to the issuance, acquisition and disposition of securities and assets by it and its subsidiaries and must obtain SEC approval for certain utility mergers and acquisitions. The entry by the Registered Holding Company and its subsidiaries into businesses other than electric and/or gas utility businesses and businesses incidental thereto is also regulated and limited under the 1935 Act.

Proposals to Repeal the 1935 Act. In recent years, several bills have been introduced in Congress that would repeal the 1935 Act. Repeal or significant modification to the 1935 Act could have a significant impact on us and the electric utility industry. At this time, however, we are not able to predict the outcome of any bills to repeal the 1935 Act or the outlook for additional legislation in 2001.

Federal Energy Regulatory Commission

Natural Gas. The transportation and sale for resale of natural gas in interstate commerce is subject to regulation by the FERC under the Natural Gas Act and the Natural Gas Policy Act of 1978, as amended. The FERC has jurisdiction over, among other things, the construction of pipeline and related facilities used in the transportation and storage of natural gas in interstate commerce, including the extension, expansion or abandonment of these facilities. The rates charged by interstate pipelines for interstate transportation and storage services are also regulated by the FERC.

REGT and MRT periodically file applications with the FERC for changes in their rates and charges designed to allow them to recover their costs of providing service to customers (to the extent allowed by prevailing market conditions), including a reasonable rate of return. These rates are normally allowed to become effective after a suspension period, and in some cases are subject to refund under applicable law, until such time as the FERC issues an order on the allowable level of rates. REGT is currently operating under rates approved by the FERC that took effect in February 1995, and MRT is currently providing services pursuant to a negotiated rate settlement approved by the FERC in October 1997; however, MRT expects to file to change its rates on or before April 1, 2001.

On February 9, 2000, the FERC issued Order No. 637, which introduces several measures to increase competition for interstate pipeline transportation services. Order No. 637 authorizes interstate pipelines to propose term-differentiated and peak/off-peak rates, and requires pipelines, including MRT and REGT, to make tariff filings to expand pipeline service options for customers. Both MRT and REGT made compliance filings in 2000; however, neither pipeline's Order No. 637 tariff filing has been acted upon by the FERC. On November 24, 2000, the FERC issued an order authorizing MRT to recover four Bcf of undercollected fuel over a three-year period. Several customers have sought rehearing of the FERC's order. Rehearings have not yet been addressed by the FERC and MRT began recovering the undercollected fuel on February 1, 2001.

Electricity. Under the Federal Power Act, the FERC has exclusive jurisdiction over wholesale sales of electricity and the transmission of electricity in interstate commerce by "public utilities." Public utilities that are subject to the FERC's jurisdiction must file rates with the FERC applicable to their wholesale sales or transmission of electricity. Most of our generation subsidiaries sell power at wholesale and are public utilities under the Federal Power Act. The FERC has authorized these subsidiaries to sell electricity and related services at wholesale, at market-based rates. In its orders authorizing market-based rates, the FERC also has granted these subsidiaries waivers of many of the accounting, record keeping and reporting requirements that are imposed on public utilities with cost-based rate schedules.

The FERC's orders accepting the market-based rate schedules filed by our subsidiaries or their predecessors, as is customary with these orders, reserved the right to revoke or limit our market-based rate authority if the FERC subsequently determines that any of our affiliates possess excessive market power. If the FERC were to revoke or limit our market-based rate authority, we would have to file, and obtain the FERC's acceptance of, cost-based rate schedules for all or some of our sales. In addition, the loss of market-based rate authority could subject us to the accounting, record keeping and reporting requirements that the FERC imposes on public utilities with cost-based rate schedules. Sales from our Electric Operations business segment are not subject to FERC jurisdiction because ERCOT is not connected to a national grid.

The FERC issued Order No. 2000 in December 1999. Order No. 2000, which applies to all FERC jurisdictional transmission companies (Transco), describes the FERC's intention to oversee the establishment of large regional transportation organizations (RTOs) and sets forth the minimum characteristics and functions of RTOs. Among the basic minimum characteristics are that the RTOs must be independent and must be of sufficient scope and geographical configuration. Order No. 2000 also encourages RTOs to work with each other to minimize or eliminate "seams" issues between RTOs in order that inter-regional transactions will flow more freely. The FERC's goal is to encourage the growth of a robust competitive wholesale market for electricity. Although Transcos are not required to join RTOs, they are encouraged to do so. Under Order No. 2000, RTOs are to be operational by December 15, 2001. However, there can be no assurance that this timeline or the FERC's goals will be achieved. At least 14 separate organizations, covering the substantial majority of all FERC jurisdictional Transcos, are in various stages of organization and have

made at least preliminary filings with the FERC. For additional information regarding the impact of this FERC order on future earnings, please read "Management's Discussion and Analysis of Financial Condition and Results of Operations — Certain Factors Affecting Our Future Earnings — Competitive, Regulatory and Other Factors Affecting Our Wholesale Energy Operations — Regulation" in Item 7 of this Form 10-K.

Trading and Marketing. Our Wholesale Energy business segment's trading and marketing operations are subject to the FERC's jurisdiction under both the Natural Gas Act and the Federal Power Act. As a gas marketer, we make sales of natural gas in interstate commerce at wholesale pursuant to a blanket certificate issued by the FERC, but the FERC does not otherwise regulate the rates, terms or conditions of these gas sales. We are also a "public utility" under the Federal Power Act, and our wholesale sales of electricity in interstate commerce are subject to a FERC-filed rate schedule that authorizes us to make sales at negotiated, market-based rates.

In authorizing market-based rates for various of our subsidiaries, the FERC has imposed some restrictions on these entities' transactions with our Electric Operations business segment, including a prohibition on the receipt of goods or services on a preferential basis. The FERC also has imposed restrictions on natural gas transactions between our Pipelines and Gathering business segment and our Wholesale Energy business segment's trading and marketing operations to preclude any preferential treatment. Similar restrictions apply to transactions between our Electric Operations business segment and our Wholesale Energy business segment's trading and marketing operations under Texas utility regulatory laws.

State and Local Regulations

Texas.

Electric Operations — The Legislation. Reliant Energy HL&P's electric utility operations are currently subject to traditional cost-of-service regulation at rates regulated by the Texas Utility Commission. However, in June 1999, the Texas legislature adopted the Legislation which substantially amended the regulatory structure governing electric utilities in Texas in order to allow retail competition. Retail pilot projects for up to 5% of each utility's load in all customer classes will begin in June 2001, and retail electric competition for all other customers will begin on January 1, 2002. While the Legislation calls for the commencement of retail competition beginning on January 1, 2002, the Texas Utility Commission may delay the date on which the retail electric market is opened to competition in any power region in Texas if it determines that the region is unable to offer fair competition and reliable service to all retail customer classes on that date.

The Legislation also requires electric utilities in Texas to restructure their businesses in order to separate power generation, transmission and distribution, and retail activities into three different units, whether commonly or separately owned. Generally, the "retail electric providers" that have been certified by the Texas Utility Commission will procure or buy electricity from the wholesale generators at unregulated rates, sell electricity at retail to their customers and pay the transmission and distribution utility a regulated tariffed rate for delivering the electricity to their customers. For additional information regarding these tariffed rates, please read "— Electric Operations — Rate Case" below. Retail electric providers will not be permitted to own or operate generation assets and their prices will not be subject to traditional cost-of-service rate regulation. Retail electric providers that are affiliates of, or successors in interest to, electric utilities may compete substantially statewide for these sales, but prices they may charge to residential and small commercial customers within the affiliated electric utility's certificated service territory are subject to limitations, known as the "price to beat," at the outset of retail competition as described below.

Two of Reliant Resources' indirect wholly owned subsidiaries, Services and Solutions, have been certified by the Texas Utility Commission as retail electric providers. Under our Business Separation Plan, these subsidiaries are the successors to the retail functions formerly performed by Reliant Energy HL&P. As "affiliated retail electric providers" of Reliant Energy HL&P, these subsidiaries will become the retail electric provider on January 1, 2002 for all customers of Reliant Energy HL&P who do not take action to select another retail electric provider. As of December 31, 2000, Reliant Energy HL&P had approximately 1.5 million residential and small commercial customers. Pursuant to Texas Utility Commission regulation, effective January 1, 2002, the retail rates charged to former Reliant Energy HL&P residential and small

commercial customers who have not elected service from another retail electric provider will be fixed at the price to beat, which will be a price equal to 6% less than Reliant Energy HL&P's average rates, on a bundled basis, in effect on January 1, 1999, adjusted to take into account a new fuel factor as of December 31, 2001. The retail subsidiary serving residential and small commercial customers has the right to request the Texas Utility Commission to adjust the fuel factor included in the price to beat not more than twice a year if it demonstrates that the existing fuel factor does not adequately reflect significant changes in the market price of natural gas and purchased energy used to serve retail customers. It may not sell electricity at a price other than the price to beat to residential or small commercial customer classes in Reliant Energy HL&P's former service territory until January 1, 2005, unless before that date the Texas Utility Commission determines that 40% or more of the amount of electric power that was consumed in 2000 by the relevant class of customers within the affiliated transmission and distribution utility's traditional certificated service territory is committed to be served by other retail electric providers. In addition, as long as an affiliated retail electric provider continues to provide retail service, the Legislation requires it to make the price to beat available to residential and small commercial customers in the certificated service area of the related affiliated utility through January 1, 2007.

The price to beat applies only to electric services provided to residential and small commercial customers. Electric services provided to large commercial and industrial customers, whether by the affiliated retail electric provider or a nonaffiliated retail electric provider, may be provided at any negotiated price. For additional information regarding Solutions, please read "Other Operations — Unregulated Retail Electric Businesses — Reliant Energy Solutions."

The Legislation also requires the affiliated retail electric provider to reconcile and credit to the affiliated transmission and distribution utility in early 2004 any positive difference between the price to beat, reduced by a specified delivery charge, and the prevailing market price of electricity, unless the Texas Utility Commission determines that, on or prior to January 1, 2004, 40% or more of the amount of electric power that was consumed in 2000 by residential or small commercial customers, as applicable, within the affiliated transmission and distribution utility's certificated service territory is committed to be served by other retail electric providers. If the 40% test is not met and a payment by the retail electric provider is required, the amount of the credit will not exceed, but could be up to, $150 per customer multiplied by the number of residential or small commercial customers, as the case may be, served by the affiliated transmission and distribution utility that are buying electricity from the affiliated retail electric provider at the price to beat on January 1, 2004, less the number of new retail electric customers that the affiliated retail electric provider serves in areas of Texas outside of the affiliated utility's certificated service area. Any such amounts credited to the transmission and distribution utility will be netted against stranded costs in the 2004 true-up proceeding.

In order to facilitate a competitive market, each power generation company that is unbundled from an integrated electric utility in Texas will be required to sell at auction 15% of the output of its installed generating capacity. The first auction will be held prior to September 1, 2001 for power to be delivered after January 1, 2002. This obligation continues until January 1, 2007, unless before that date the Texas Utility Commission determines that at least 40% of the electric power consumed in 2000 by residential or small commercial customers, as applicable, within the affiliated transmission and distribution utility's certificated service territory as of January 1, 2002 is committed to be served by other retail electric providers. An affiliated retail electric provider may not purchase capacity sold by its affiliated power generation company in the mandated capacity auctions.

The Legislation requires the Texas Utility Commission to determine procedures and criteria for designating retail electric providers to serve as providers of last resort in areas of the state in which retail competition is in effect. A provider of last resort is required to offer a standard retail electric service package for each class of customers designated by the Texas Utility Commission at a fixed rate approved by the Texas Utility Commission, and is required to provide the service package to any requesting retail customer in the territory for which it is the provider of last resort. The Texas Utility Commission is required to designate the initial providers of last resort by June 1, 2001. In the event that no retail electric provider applies to be the provider of last resort in a given area of the state, the Texas Utility Commission may require a retail electric provider to become the provider of last resort as a condition to receiving or maintaining its retail electric provider certificate. In the event that a retail electric provider fails to serve any or all of its customers, the

provider of last resort is required to offer that customer the standard retail service package for that customer class with no interruption of service to the customer. Pursuant to the Legislation, the transmission and distribution utility is not required to serve as the provider of last resort.

For additional information regarding the Legislation, retail competition and the application of the Legislation to our operations and structure, please read "Our Business — Restructuring" and "Electric Operations" in Item 1 of this Form 10-K, and "Management's Discussion and Analysis of Financial Condition and Results of Operations — Certain Factors Affecting Our Future Earnings — Competitive, Regulatory and Other Factors Affecting Our Electric Operations — Competition and Deregulation" in Item 7 of this Form 10-K as well as Note 4 to our consolidated financial statements, which are incorporated herein by reference.

Electric Operations — Rate Case. On March 31, 2000, Reliant Energy HL&P filed its "Wires Case" with the Texas Utility Commission as required by the Legislation. This filing represents the "unbundling" or separating of costs related to providing transmission and distribution service. The Wires Case will set the regulated rates of delivering electricity when electric competition begins, including pilot programs. The regulated wires rate, or non-bypassable delivery charge, will include the transmission and distribution rate, a system benefit fund fee, a nuclear decommissioning fund charge, a municipal franchise fee, a transition charge associated with any securitization of regulatory assets or a portion of stranded costs and a competition transition charge, if any. Hearings were conducted in phases and all have been concluded as of January 2001. Reliant Energy HL&P is currently awaiting a "Proposal for Decision" on the final phase of the case, which is expected in late March 2001. The Texas Utility Commission is expected to render an interim order in late April 2001 establishing the rates to be charged for the pilot project beginning in June 2001, with the final wires rates anticipated to be established in August 2001.

Electric Operations — Fuel Filings. For additional information regarding Reliant Energy HL&P's fuel filings for the recovery of under-recovered fuel costs, including the recent filing on March 15, 2001, please read Note 4(d) to our consolidated financial statements.

Electric Operations — Other. Currently, Reliant Energy HL&P conducts its electric utility operations under a certificate of convenience and necessity granted by the Texas Utility Commission. The certificate of convenience and necessity covers the present service area and facilities of our Electric Operations business segment. In addition, Reliant Energy HL&P holds non-exclusive franchises from the incorporated municipalities in the service territory of our Electric Operations business segment. These franchises give Reliant Energy HL&P the right to operate its transmission and distribution system within the streets and public ways of these municipalities for the purpose of delivering electric service to the municipality, its residents and businesses. None of these franchises expires before 2007.

California.

California began the deregulation of its electricity market in 1996, fashioning a wholesale market structure administered by two independent non-profit corporations: the Cal ISO, responsible for operational control of the transmission system and the purchase or sale of electricity in "real-time" to balance actual supply and demand, and the Cal PX, responsible for conducting auctions for the purchase or sale of electricity on a day-ahead or day-of basis. As part of the California deregulation, California's public utilities sold essentially all of their gas-fired plants to third-party generators. The utilities were required to sell their remaining generation into the Cal PX markets and purchase all of their power requirements from the Cal PX markets at market-based rates approved by the FERC. California's regulatory system initially prohibited the utilities from entering into forward contracts to cover the bulk of their customers' requirements. Retail electricity rates were frozen at levels in effect on June 10, 1996, with a 10% rate reduction for residential and smaller commercial customers. As a result of rising wholesale power costs in 2000 driven by a combination of factors, including higher natural gas prices and emission allowance costs, reduction in available hydroelectric generation resources, increased demand, decreases in net imports, structural market flaws, including over-reliance on the spot market, and limitations on supply as a result of maintenance and other outages, the utilities have been unable to recover their purchased power costs through the retail rates they are allowed to

charge and have accumulated huge debts to wholesale power suppliers, including us, as a result. The California Legislature is currently considering legislation under which a state entity would be formed to purchase and operate a substantial share of the transmission lines in California in an effort to avoid potential bankruptcy filings by the utilities, and is also considering other actions to re-regulate power suppliers operating in the state. For additional information regarding the situation in California, please read "Wholesale Energy — Power Generation Operations — Southwest Region," "Management's Discussion and Analysis of Financial Condition and Results of Operations — Results of Operations by Business Segment — Wholesale Energy" and "— Certain Factors Affecting Our Future Earnings — Competitive, Regulatory and Other Factors Affecting Our Wholesale Energy Operations — California" in Item 7 of this Form 10-K, and Notes 14(g) and 14(h) to our consolidated financial statements.

Other States.

Natural Gas Distribution. In almost all communities in which our Natural Gas Distribution business segment provides service, RERC operates under franchises, certificates or licenses obtained from state and local authorities. The terms of the franchises, with various expiration dates, typically range from 10 to 30 years. None of our Natural Gas Distribution segment's material franchises expire before 2005. In most cases, franchises to provide natural gas utility services are not exclusive.

Substantially all of our Natural Gas Distribution segment's retail sales are subject to traditional cost-of-service regulation at rates regulated by the relevant state public service commissions and, in Texas, by the Texas Railroad Commission and municipalities we serve. None of our Natural Gas Distribution segment's local distribution companies are currently a party to any material pending rate proceeding. For additional information regarding our ability to recover increased costs of natural gas from our customers, please read "Management's Discussion and Analysis of Financial Condition and Operations — Certain Factors Affecting our Future Earnings — Competitive and Other Factors Affecting RERC Operations — Natural Gas Distribution" in Item 7 of this Form 10-K.

Wholesale Energy. All of our Wholesale Energy business segment's existing generation facilities sell power only at wholesale. None of the states in which these facilities are located regulate sales from these facilities under traditional utility cost-of-service regulation. In the PJM market and in California, the independent system operators have imposed price caps that limit the maximum sales prices for wholesale power. In addition, in some states, including California, proposals have been made to re-regulate the provision of wholesale power under traditional cost-of-service regulation. In New Jersey, existing law provides that the relevant regulatory agency may re-impose cost-of-service regulation if the agency concludes that competition is not sufficient. In addition, most states regulate the siting or construction of generation facilities.

Nuclear Regulatory Commission

Under the 1954 Atomic Energy Act and the 1974 Energy Reorganization Act, the NRC regulates nuclear plants and has the authority to impose fines or shut down nuclear plants for non-compliance with its requirements.

Under the 1980 Federal Low-Level Radioactive Waste Policy Act and related Texas legislation, the Texas Low-Level Radioactive Waste Disposal Authority is authorized to build and operate a low-level waste disposal facility in Texas. Currently, the South Texas Project disposes of its low-level nuclear waste under a short-term agreement at the Barnwell facility in South Carolina. In the event the Barnwell facility stops accepting waste before a Texas disposal site is opened, the South Texas Project would store its waste in an interim storage facility located at the nuclear plant. The plant currently has storage capacity for at least five years of low-level nuclear waste generated by the project.

For information regarding the NRC's regulation of nuclear decommissioning trust funds, please read Note 14(l) to our consolidated financial statements.

European Regulation

In 1998, the Netherlands established a privatization program under the Dutch Electricity Act. Under this legislation, the Dutch electricity market opened to limited wholesale and retail competition on January 1, 1999, and industrial customers who are end users were able to select their electric suppliers. Beginning January 1, 2001, the wholesale market was completely opened to competition. The next customer segment, composed primarily of commercial customers, will be liberalized in 2002. The remaining customers, mainly residential, are expected to be able to choose their electric supplier by 2003. The timing of these market openings is subject to change, however, at the discretion of the Dutch Minister of Economic Affairs. For additional information regarding the recent stranded costs legislation in the Netherlands, please read "Management's Discussion and Analysis of Financial Condition and Results of Operations — Certain Factors Affecting Our Future Earnings — Competitive, Regulatory and Other Factors Affecting Our European Energy Operations — Other" in Item 1 of the Form 10-K and Note 14(i) to our consolidated financial statements.

Prior to 2001, UNA, the other large Dutch generating companies and the Dutch distribution companies operated under various agreements that regulated, among other things, the rates UNA could charge for its generation output. Pursuant to these agreements, UNA and other generators sold their generating output to a national production pool operated by a company owned by the generators and, in return, received a standardized remuneration. The remuneration included fuel cost, capital cost and operation and maintenance expenses. UNA also operated under the protocol, which is an agreement under which the Dutch generators agreed to provide capacity, energy and various other services to distributors for a total payment of NLG 3.4 billion ($1.45 billion based on the December 31, 2000 exchange rate of 2.34 NLG per U.S. Dollar) over the period 1997 through 2000 plus compensation of actual fuel costs. Effective January 1, 2001, these agreements expired.

ENVIRONMENTAL MATTERS

General Environmental Issues

We are subject to a number of federal, state and local requirements relating to the protection of the environment and the safety and health of personnel and the public.

These requirements relate to a broad range of our activities, including:

- the discharge of pollutants into the air, water and soil,
- the identification, generation, storage, handling, transportation, disposal, record keeping, labeling and reporting of, and emergency response in connection with, hazardous and toxic materials and wastes, including asbestos, associated with our operations,
- noise emissions from our facilities, and
- safety and health standards, practices and procedures that apply to the workplace and to operation of our facilities.

In order to comply with these requirements, we may need to spend substantial amounts and devote other resources from time to time to:

- construct or acquire new equipment,
- acquire permits and/or marketable allowances or other emission credits for facility operations,
- modify or replace existing and proposed equipment, and
- clean up or decommission waste disposal areas, fuel storage and management facilities, and other locations and facilities, including coal mine refuse piles and generation facilities.

We anticipate investing up to $711 million in capital and other special project expenditures between 2001 and 2005 for environmental compliance. If we do not comply with environmental requirements that apply to our operations, regulatory agencies could seek to impose on us civil, administrative and/or criminal liabilities as well as seek to curtail our operations. Under some statutes, private parties could also seek to impose civil fines or liabilities for property damage, personal injury and possibly other costs. For additional information regarding environmental expenditures, please read "Management's Discussion and Analysis of Financial Condition and Results of Operations — Certain Factors Affecting Our Earnings — Environmental Expenditures" in Item 7 of this Form 10-K and Note 14(g) to our consolidated financial statements.

Air Emissions

As part of the 1990 amendments to the Federal Clean Air Act, requirements and schedules for compliance were developed for attainment of health-based standards. As part of this process, standards for the emission of NOx, a product of the combustion process associated with power generation and natural gas compression, are being developed or have been finalized. The standards require reduction of emissions from our power generating units in California, Texas and the Mid-Atlantic Region and some of our natural gas compression facilities. We believe the reductions will require substantial expenditures in the years 2001 through 2004, with possible additional expenditures after that for our facilities in Texas. The post-2004 requirements in Texas are currently being litigated, and the outcome of the litigation cannot be predicted at this time. Our facilities in the Netherlands are in compliance with applicable Dutch NOx emission regulations. Discussions are currently ongoing between the Dutch government and the electric utility sector as to the acceptable level of emissions. While no outcome can be predicted, we currently believe that a market-based NOx emissions trading system will be implemented in the 2002 time frame, and that ultimately some level of emission reductions will be required from our generating facilities.

The Environmental Protection Agency (EPA) has announced its determination to regulate hazardous air pollutants (HAPs) from coal-fired and oil-fired steam electric generating units under Section 112 of the Clean Air Act. The EPA plans to develop maximum achievable control technology (MACT) standards for these types of units. The rulemaking for coal- and oil-fired steam electric generating units must be completed by December 2004. Compliance with the rules will be required within three years thereafter. The MACT standards that will be applicable to the units cannot be predicted at this time so the impact on our facilities is uncertain. In addition, a request for reconsideration of the EPA's decision to impose MACT standards has been filed with the EPA. We cannot predict the outcome of the request.

In 1998, the United States became a signatory to the United Nations Framework Convention on Climate Change (the Kyoto Protocol). The Kyoto Protocol calls for developed nations to reduce their emissions of greenhouse gases. Carbon dioxide, which is a major byproduct of the combustion of fossil fuel, is considered to be a greenhouse gas. The Kyoto Protocol, however, will not become enforceable law in the United States unless and until the U.S. Senate ratifies it. If the Senate ultimately ratifies the Kyoto Protocol, any resulting limitations on power plant carbon dioxide emissions could have a material adverse impact on all fossil fuel fired facilities, including those belonging to us. The European Union, of which the Netherlands is a member, has adopted the Kyoto Protocol as the goal for greenhouse gas emission targets. UNA, through innovative use of "green fuels" and efficiency improvements, expects to meet its portion of the target reductions.

The EPA is conducting a nationwide investigation regarding the historical compliance of coal-fueled electric generating stations with various permitting requirements of the Clean Air Act. Specifically, the EPA and the U.S. Department of Justice have initiated formal enforcement actions and litigation against several other utility companies that operate these stations, alleging that these companies modified their facilities without proper pre-construction permit authority. Since June 1998, six of our coal-fired facilities in the Mid-Atlantic region have received requests for information related to work activities conducted at those sites. The EPA has not filed an enforcement action or initiated litigation in connection with these Mid-Atlantic facilities at this time. Nevertheless, any litigation, if pursued successfully by the EPA, could accelerate the timing of emission reductions currently contemplated for the facilities and result in the imposition of penalties.

In February 2001, the U.S. Supreme Court upheld a previously adopted EPA ambient air quality standard for fine particulate matter. While attaining this new standard may ultimately require expenditures for air quality control system upgrades for our facilities, regulations addressing affected sources and required controls are not expected until after 2005. Consequently, it is not possible to determine the impact on our operations at this time. For additional information regarding clear-air expenditures, please read "Management's Discussion and Analysis of Financial Condition and Results of Operations — Certain Factors Affecting Our Future Earnings — Environmental Expenditures — Clean Air Act Expenditures" in Item 7 of this Form 10-K.

Water Issues

In July 2000, the EPA issued final rules for the implementation of the Total Maximum Daily Load program of the Clean Water Act (TMDL). The goal of the TMDL rules is to establish, over the next 15 years, the maximum amounts of various pollutants that can be discharged into waterways while keeping those waterways in compliance with water quality standards. The establishment of TMDL values may eventually result in more stringent discharge limits in each facility's discharge permit. Such limits may require our facilities to install additional water treatment, modify operational practices or implement other wastewater control measures. Subsequent to the issuance of the final rule, the U.S. Congress acted to prohibit implementation of the rule until at least the fourth quarter of 2001.

The EPA proposed rules that would impose uniform technology requirements on new cooling water intake structures. These rules are expected to be finalized, and rules for existing structures proposed, during the summer of 2001. It is not known at this time what requirements the final rules for existing intake structures might impose, whether any of our facilities might require modification as a result or what the magnitude of our obligations would be.

A number of efforts are under way within the EPA to evaluate water quality criteria for parameters associated with fossil fuel combustion. These parameters include arsenic, mercury and selenium. Significant changes in these criteria could impact station discharge limits and could require our facilities to install additional water treatment equipment. The impact on us as a result of these initiatives is unknown at this time. For additional information regarding environmental expenditures associated with this, please read "Management's Discussion and Analysis of Financial Condition and Results of Operations — Certain Factors Affecting Our Future Earnings — Environmental Expenditures — Water, Mercury and Other Expenditures" in Item 7 of this Form 10-K.

Mercury Contamination

Like similar companies, our pipeline and natural gas distribution operations have in the past employed elemental mercury in measuring and regulating equipment meters used on our pipelines. It is possible that small amounts of mercury may have been spilled in the course of normal maintenance and replacement operations and that these spills may have contaminated the immediate area around the meters with elemental mercury. This type of contamination has been found by us in the past, and we have conducted remediation at sites found to be contaminated. Although we are not aware of additional specific sites, it is possible that other contaminated sites may exist and that remediation costs may be incurred for these sites. Although the total amount of these costs cannot be known at this time, based on our experience and that of others in the natural gas industry to date and on the current regulations regarding remediation of these sites, we believe that the cost of any remediation of these sites will not be material to our financial position, results of operations or cash flows. For additional information regarding environmental expenditures associated with mercury contamination, please read "Management's Discussion and Analysis of Financial Condition and Results of Operations — Certain Factors Affecting Our Future Earnings — Environmental Expenditures — Water, Mercury and Other Expenditures" in Item 7 of this Form 10-K.

Other

We have been named, along with numerous others, as a defendant in several lawsuits filed by a large number of individuals who claim injury due to exposure to asbestos while working at sites along the Texas Gulf Coast. Most of these claimants have been workers who participated in construction of various industrial facilities, including power plants, and some of the claimants have worked at locations owned by us. We anticipate that additional claims like those received may be asserted in the future, and we intend to continue our practice of vigorously contesting claims that we do not consider to have merit. Although their ultimate outcome cannot be predicted at this time, we do not believe, based on our experience to date, that these matters, either individually or in the aggregate, will have a material adverse effect on our financial position, results of operations or cash flows.

EMPLOYEES

As of December 31, 2000, we had 15,633 full-time employees. The following table sets forth the number of our employees by business segment as of December 31, 2000:

Segment	Number
Electric Operations	6,667
Natural Gas Distribution	4,791
Pipelines and Gathering	608
Wholesale Energy	1,776
European Energy	926
Other Operations	865
Total	15,633

The number of employees of Reliant Energy and its subsidiaries who are represented by unions or other collective bargaining groups include (i) Electric Operations, 2,797; (ii) Natural Gas Distribution, 1,544; (iii) Wholesale Energy, 769; and (iv) European Energy, 846.

EXECUTIVE OFFICERS OF RELIANT ENERGY

(As of March 12, 2001)

Name	Age	Officer Since	Present Position
R. Steve Letbetter(1)	52	1978	Chairman, President, Chief Executive Officer and Director
Robert W. Harvey(1)	45	1999	Vice Chairman
David M. McClanahan	51	1986	Vice Chairman, and President and Chief Operating Officer, Reliant Energy Delivery Group
Stephen W. Naeve(1)	53	1988	Vice Chairman and Chief Financial Officer
Joe Bob Perkins(1)	40	1996	President and Chief Operating Officer, Reliant Energy Wholesale Group
Hugh Rice Kelly(1)	58	1984	Executive Vice President, General Counsel and Corporate Secretary
Mary P. Ricciardello(1)	45	1993	Senior Vice President and Chief Accounting Officer

(1) Effective as of the Distribution, these individuals will resign their positions with Reliant Energy, except that Mr. Letbetter will continue to serve as non-executive Chairman of the Reliant Energy Board of Directors.

Mr. Letbetter has served as Chairman of Reliant Energy since January 2000 and as President and Chief Executive Officer of Reliant Energy since June 1999. He has been a director of Reliant Energy since 1995. He has served in various executive officer capacities with Reliant Energy since 1978.

Mr. Harvey has served as Vice Chairman of Reliant Energy since June 1999. Prior to joining Reliant Energy, he served as a director in the Houston office of McKinsey & Company, Inc.

Mr. McClanahan has served as Vice Chairman of Reliant Energy since October 2000 and as President and Chief Operating Officer of the Reliant Energy Delivery Group since 1999. Previously, he served as President and Chief Operating Officer of the Reliant Energy HL&P division from 1997 to 1999. He has served in various executive officer capacities with Reliant Energy since 1986, including Group Vice President — Finance and Regulatory Relations of Reliant Energy HL&P from 1993 to 1996.

Mr. Naeve has served as Vice Chairman of Reliant Energy since June 1999 and as Chief Financial Officer of Reliant Energy since 1997. Between 1997 and 1999, he served as Executive Vice President and Chief Financial Officer of Reliant Energy. He has served in various executive officer capacities with Reliant Energy since 1988, including Vice President — Strategic Planning and Administration between 1993 and 1996.

Mr. Perkins has served as President and Chief Operating Officer, Reliant Energy Wholesale Group, and as President and Chief Operating Officer, Reliant Energy Power Generation, Inc. since 1998. In 1998, Mr. Perkins served as President and Chief Operating Officer of Reliant Energy Power Generation Group. Between 1996 and 1998, Mr. Perkins served as Vice President — Corporate Planning and Development. Prior to joining Reliant Energy, he served as Vice President of Business Development and Corporate Secretary of Coral Energy Resources, L.P. and Vice President and General Manager of Coral Power, L.L.C. Between 1994 and 1995, he was Director of Business Development for Tejas Gas Corporation.

Mr. Kelly has served as Executive Vice President, General Counsel and Corporate Secretary of Reliant Energy since 1997. Between 1984 and 1997, he served as Senior Vice President, General Counsel and Corporate Secretary of Reliant Energy.

Ms. Ricciardello has served as Chief Accounting Officer of Reliant Energy since June 2000 and as Senior Vice President since June 1999. Between 1999 and 2000, she served as Senior Vice President and Comptroller of Reliant Energy. She also served as Vice President and Comptroller of Reliant Energy from 1996 to 1999. She has served in various executive officer capacities with Reliant Energy since 1993.

Executive Officers of the Regulated Holding Company and Reliant Resources

We currently expect that at the time of the Distribution, the executive officers of the Regulated Holding Company will include the following:

David M. McClanahan — President and Chief Executive Officer
Scott E. Rozzell — Executive Vice President and General Counsel
Stephen C. Schaeffer — Executive Vice President
James S. Brian — Senior Vice President and Chief Accounting Officer

Other executive officer positions of the Regulated Holding Company have not been finalized at this time.

We currently expect that at the time of the Offering, the executive officers of Reliant Resources will include the following:

R. Steve Letbetter — Chairman, President and Chief Executive Officer
Robert W. Harvey — Executive Vice President and Group President, Emerging Businesses
Stephen W. Naeve — Executive Vice President and Chief Financial Officer
Joe Bob Perkins — Executive Vice President and Group President, Wholesale Businesses
Hugh Rice Kelly — Senior Vice President, General Counsel and Corporate Secretary
Mary P. Ricciardello — Senior Vice President and Chief Accounting Officer

ITEM 2. *Properties.*

Character of Ownership

We and RERC own our principal properties in fee, except for three plants previously owned, and currently leased, by REMA that were sold and leased back under long-term leveraged leases, and except for the land on which two plants of our Wholesale Energy business segment (one in Nevada and one in Texas) are located. Also, most electric lines and gas mains are located, pursuant to easements and other rights, on public roads or on land owned by others.

Substantially all of the real estate, electric distribution system properties, buildings and franchises owned directly by Reliant Energy (excluding real estate and other properties of subsidiaries of Reliant Energy) are subject to a lien created under a Mortgage and Deed of Trust dated as of November 1, 1944 (as supplemented, Mortgage) between Reliant Energy and South Texas Commercial National Bank of Houston (The Chase Manhattan Bank, as Successor Trustee). The lien of the Mortgage excludes cash, stock in subsidiaries and certain other assets. Additionally, the properties owned by REMA, as well as the two previously mentioned plants in Nevada and Texas in our Wholesale Energy business segment, are subject to liens of creditors of the respective subsidiaries.

Electric Operations

For information regarding the properties of our Electric Operations business segment, please read "Electric Operations — Electric Operations Assets" in Item 1 of this Form 10-K, which information is incorporated herein by reference.

Natural Gas Distribution

For information regarding the properties of our Natural Gas Distribution business segment, please read "Natural Gas Distribution — Assets" in Item 1 of this Form 10-K, which information is incorporated herein by reference.

Pipelines and Gathering

For information regarding the properties of our Pipelines and Gathering business segment, please read "Pipelines and Gathering — Assets" in Item 1 of this Form 10-K, which information is incorporated herein by reference.

Wholesale Energy

For information regarding the properties of our Wholesale Energy business segment, please read "Wholesale Energy — Power Generation Operations" in Item 1 of this Form 10-K, which information is incorporated herein by reference.

European Energy

For information regarding the properties of our European Energy business segment, please read "European Energy — European Power Generation Operations" in Item 1 of this Form 10-K, which information is incorporated herein by reference.

Other Operations

For information regarding the properties of our Other Operations business segment, please read "Other Operations" in Item 1 of this Form 10-K, which information is incorporated herein by reference.

ITEM 3. *Legal Proceedings.*

(a) Reliant Energy.

For a description of certain legal and regulatory proceedings affecting Reliant Energy, see Notes 4, 14(g), 14(h) and 14(i) to our consolidated financial statements, which notes are incorporated herein by reference.

(b) RERC Corp.

For a description of certain legal and regulatory proceedings affecting RERC, see Notes 9(c) and 9(d) to RERC's consolidated financial statements, which notes are incorporated herein by reference.

ITEM 4. ***Submission of Matters to a Vote of Security Holders.***

No matters were submitted to a vote of Reliant Energy's security holders during the fourth quarter of the fiscal year ended December 31, 2000.

PART II

ITEM 5. ***Market for Reliant Energy's and RERC Corp.'s Common Equity and Related Stockholder Matters.***

As of March 12, 2001, Reliant Energy's common stock was held of record by approximately 75,089 shareholders. Reliant Energy's common stock is listed on the New York and Chicago Stock Exchanges and is traded under the symbol "REI." All of the 1,000 outstanding shares of RERC Corp.'s common stock are held by Reliant Energy.

The following table sets forth the high and low sales prices of Reliant Energy's common stock on the New York Stock Exchange composite tape during the periods indicated, as reported by *Bloomberg*, and the dividends declared for these periods. Dividend payout was $1.50 per share in both 1999 and 2000. The dividend declared during the fourth quarter of 2000 was paid in March 2001.

	Market Price		Dividend Declared
	High	Low	Per Share
1999			
First Quarter			$0.375
January 6	$32.25		
March 31		$26.06	
Second Quarter			$0.375
April 14		$25.50	
May 25	$31.69		
Third Quarter			$0.375
September 3	$28.63		
September 28		$26.31	
Fourth Quarter			$0.375
October 4	$28.44		
December 31		$22.88	
2000			
First Quarter			$0.375
March 7		$19.88	
March 16	$24.38		
Second Quarter			$0.375
April 7		$22.56	
June 23	$29.81		
Third Quarter			$0.375
July 3		$29.81	
September 29	$46.50		
Fourth Quarter			$0.375
October 2	$48.19		
December 6		$38.06	

The closing market price of Reliant Energy's common stock on December 31, 2000 was $43.31 per share.

Future dividends will be subject to determination based upon our results of operations and financial condition, our future business prospects, any applicable contractual restrictions and other factors that our Board of Directors considers relevant.

ITEM 6. *Selected Financial Data.*

The following table presents selected financial data with respect to our consolidated financial condition and results of consolidated operations and should be read in conjunction with our consolidated financial statements and the related notes in Item 8 of this Form 10-K. In December 2000, our Board of Directors approved a plan to dispose of our Latin America business segment through the sale of its assets. Accordingly, we are reporting the results of our Latin America business segment as discontinued operations for all periods presented. The selected financial data includes the financial statement effect of REMA since the May 2000 acquisition, UNA since the October 1999 acquisition and RERC since the August 1997 acquisition. These acquisitions were accounted for under the purchase method. Please read Note 3 to our consolidated financial statements for additional information regarding the REMA and UNA acquisitions and Note 19 to our consolidated financial statements for additional information regarding the discontinued operations.

	Year Ended December 31,				
	1996	1997(1)	1998(2)	1999(3)	2000(4)
	(In millions, except per share amounts)				
Revenues	$ 4,033	$ 6,786	$11,230	$15,223	$29,339
Income (loss) from continuing operations before extraordinary items and preferred dividends	$ 408	$ 390	$ (278)	$ 1,674	$ 771
(Loss) income from discontinued operations, net of tax	(3)	31	137	(9)	(172)
Loss on disposal of discontinued operations, net of tax	—	—	—	—	(159)
Extraordinary items, net of tax	—	—	—	(183)	7
Net income (loss) attributable to common stockholders	$ 405	$ 421	$ (141)	$ 1,482	$ 447
Basic earnings (loss) per common share:					
Continuing operations before extraordinary items	$ 1.67	$ 1.54	$ (0.98)	$ 5.87	$ 2.71
(Loss) income from discontinued operations, net of tax	(0.01)	0.12	0.48	(0.03)	(0.61)
Loss on disposal of discontinued operations, net of tax	—	—	—	—	(0.56)
Extraordinary items, net of tax	—	—	—	(0.64)	0.03
Basic earnings (loss) per common share	$ 1.66	$ 1.66	$ (0.50)	$ 5.20	$ 1.57
Diluted earnings (loss) per common share:					
Continuing operations before extraordinary items	$ 1.67	$ 1.54	$ (0.98)	$ 5.85	$ 2.68
(Loss) income from discontinued operations, net of tax	(0.01)	0.12	0.48	(0.03)	(0.60)
Loss on disposal of discontinued operations, net of tax	—	—	—	—	(0.55)
Extraordinary items, net of tax	—	—	—	(0.64)	0.03
Diluted earnings (loss) per common share	$ 1.66	$ 1.66	$ (0.50)	$ 5.18	$ 1.56
Cash dividends declared per common share	$ 1.50	$ 1.50	$ 1.50	$ 1.50	$ 1.50
Dividend payout ratio from continuing operations	90%	97%	—	26%	55%
Return on average common equity	10.2%	9.7%	(3.1)%	30.8%	8.3%
Ratio of earnings from continuing operations to fixed charges	2.82	2.42	—	5.43	2.35

	Year Ended December 31,				
	1996	1997(1)	1998(2)	1999(3)	2000(4)
	(In millions, except per share amounts)				
At year-end:					
Book value per common share	$ 16.41	$ 17.28	$ 15.16	$ 18.70	$ 19.10
Market price per common share	$ 22.63	$ 26.75	$ 32.06	$ 22.88	$ 43.31
Market price as a percent of book value	138%	155%	211%	122%	227%
Total assets	$12,277	$18,268	$18,967	$26,456	$32,077
Long-term debt obligations, including current maturities	$ 3,280	$ 5,307	$ 7,049	$ 9,223	$ 6,619
Trust preferred securities	—	$ 362	$ 342	$ 705	$ 705
Cumulative preferred stock	$ 135	$ 10	$ 10	$ 10	$ 10
Capitalization:					
Common stock equity	53%	46%	37%	35%	43%
Cumulative preferred stock	2%	—	—	—	—
Trust preferred securities	—	3%	3%	5%	5%
Long-term debt, including current maturities	45%	51%	60%	60%	52%
Business acquisitions	$ —	$ 1,423	$ 292	$ 1,060	$ 2,103
Capital expenditures	324	328	712	1,166	1,842

(1) 1997 income includes a non-cash, unrealized accounting loss on our indexed debt securities of $79 million (after-tax), or $0.31 loss per basic and diluted share. For additional information on the indexed debt securities, please read Note 8 to our consolidated financial statements.

(2) 1998 income includes a non-cash, unrealized accounting loss on our indexed debt securities of $764 million (after-tax), or $2.69 loss per basic and diluted share. For additional information on the indexed debt securities, please read Note 8 to our consolidated financial statements. Fixed charges exceeded earnings by $367 million in 1998.

(3) 1999 income includes an aggregate non-cash, unrealized accounting gain on our indexed debt securities and our Time Warner (now AOL Time Warner) investment, of $1.2 billion (after-tax), or $4.09 earnings per basic share and $4.08 earnings per diluted share. For additional information on the indexed debt securities and AOL Time Warner investment, please read Note 8 to our consolidated financial statements. The extraordinary item in 1999 is a loss related to an accounting impairment of some generation related regulatory assets of our Electric Operations business segment. For additional information, please read Note 4 to our consolidated financial statements.

(4) 2000 income includes an aggregate non-cash accounting loss on our indexed debt securities and our AOL Time Warner investment of $67 million (after-tax), or $0.23 earnings per basic and diluted share. The extraordinary item in 2000 is a gain related to the early extinguishment of $272 million of long-term debt. For additional information on the indexed debt securities and AOL Time Warner investment, please read Note 8 to our consolidated financial statements.

ITEM 7. ***Management's Discussion and Analysis of Financial Condition and Results of Operations.***

The following discussion and analysis should be read in combination with our consolidated financial statements included in Item 8 of this Form 10-K.

RELIANT ENERGY, INCORPORATED

We are a diversified international energy services and energy delivery company that provides energy and energy services in North America and Western Europe. We operate one of the United States' largest electric utilities in terms of kilowatt-hour (KWh) sales, and our three natural gas distribution divisions together form one of the United States' largest natural gas distribution operations in terms of customers served. We invest in the acquisition, development and operation of international and domestic non-rate regulated power generation facilities. We own two interstate natural gas pipelines that provide gas transportation, supply, gathering and storage services, and we also engage in wholesale energy marketing and trading.

In this section we discuss our results of operations on a consolidated basis and individually for each of our business segments. We also discuss our liquidity and capital resources. Our financial reporting segments include Electric Operations, Natural Gas Distribution, Pipelines and Gathering, Wholesale Energy, European Energy and Other Operations. For segment reporting information, please read Notes 1 and 18 to our consolidated financial statements. For additional information regarding these segments, please read "Business" in Item 1 of this Form 10-K.

Effective December 1, 2000 (measurement date), our Board of Directors approved a plan to dispose of our Latin America business segment and sale of its assets. Accordingly, we are reporting the results of our Latin America business segment as discontinued operations for all periods presented in our consolidated financial statements in accordance with Accounting Principles Board Opinion No. 30. For information regarding the disposal of our Latin America business segment, please read "Our Business — Discontinued Operations" in Item 1 of this Form 10-K and Note 19 to our consolidated financial statements.

In 2000, we submitted our business separation plan to the Texas Utility Commission. We later amended the plan to contemplate the restructuring of our businesses into two separate publicly traded companies in order to separate our unregulated businesses from our regulated businesses. In December 2000, the Business Separation Plan was approved by the Texas Utility Commission, although as of March 19, 2001 a final order has not been issued. For additional information regarding the Business Separation Plan, please read "Our Business — Restructuring" in Item 1 of this Form 10-K and Note 4(b) to our consolidated financial statements.

On July 27, 2000, we announced our intention to form a company, Reliant Resources, to own and operate a substantial portion of our unregulated operations and to offer no more than 20% of the common stock of this company in an initial public offering. Reliant Energy incorporated Reliant Resources as a wholly owned subsidiary in August 2000. Effective as of December 31, 2000, Reliant Energy transferred substantially all of its unregulated operations to Reliant Resources. We currently expect Reliant Resources will conduct an initial public offering in 2001.

On May 12, 2000, one of our subsidiaries purchased entities owning electric power generating assets and development sites located in Pennsylvania, New Jersey and Maryland having an aggregate net generating capacity of approximately 4,262 MW. With the exception of development entities that were sold to another Reliant Energy subsidiary in July 2000, the assets of the entities acquired are held by REMA. The purchase price for the May 2000 transaction was $2.1 billion. We accounted for the acquisition as a purchase, and accordingly, our results of operations include the results of operations for REMA only for the period after the acquisition date. For additional information about this acquisition, including our accounting treatment of the acquisition, please read Note 3(a) to our consolidated financial statements.

Effective October 1999, we acquired UNA, a Dutch electric generation company, for a total purchase price of $1.9 billion based on the October 7, 1999 exchange rate of 2.06 NLG per U.S. dollar. We accounted

for this acquisition as a purchase. For additional information about this acquisition, including our accounting treatment of the acquisition, please read Note 3(b) to our consolidated financial statements.

All dollar amounts in the tables that follow are in millions, except for per share and operational data.

Consolidated Results of Operations

	Year Ended December 31,		
	1998	1999	2000
Revenues	$11,230	$ 15,223	$ 29,339
Operating Expenses	(9,950)	(13,965)	(27,460)
Operating Income	1,280	1,258	1,879
(Loss) Income of Equity Investments	(1)	(1)	43
Other Income, net	68	60	83
Gain (Loss) on AOL Time Warner Investment	—	2,452	(205)
(Loss) Gain on Indexed Debt Securities	(1,176)	(629)	102
Interest Expense and Other Charges	(532)	(550)	(754)
(Loss) Income from Continuing Operations Before Income Taxes and Extraordinary Items	(361)	2,590	1,148
Income Tax Benefit (Expense)	83	(916)	(377)
Income (Loss) from Discontinued Operations, net of tax of ($52), $17 and $46	137	(9)	(172)
Loss on Disposal of Discontinued Operations, net of tax of $13	—	—	(159)
Extraordinary (Loss) Gain, net of tax of $99 and $0	—	(183)	7
Net (Loss) Income Attributable to Common Stockholders	$ (141)	$ 1,482	$ 447
Basic (Loss) Earnings Per Share	$ (0.50)	$ 5.20	$ 1.57
Diluted (Loss) Earnings Per Share	$ (0.50)	$ 5.18	$ 1.56

2000 Compared to 1999.

Net Earnings. We reported consolidated earnings of $447 million ($1.57 per basic share) for 2000 compared to $1.482 billion ($5.20 per basic share) for 1999. The reported income for 2000 included the following extraordinary and unusual items:

- an aggregate after-tax, non-cash accounting loss of $67 million on our indexed debt securities and our related AOL Time Warner investment,
- an extraordinary gain of $7 million related to the early extinguishment of $272 million of long-term debt,
- an after-tax loss of $172 million from discontinued operations of our Latin America business segment, and
- an after-tax loss of $159 million on the disposal of discontinued operations of our Latin America business segment.

The 1999 results included the following extraordinary and unusual items:

- an aggregate after-tax, non-cash accounting gain of $1.166 billion on our indexed debt securities and our AOL Time Warner investment,
- an after-tax extraordinary loss of $183 million relating to an accounting impairment of some generation related regulatory assets of Electric Operations, and
- an after-tax loss of $9 million from discontinued operations of our Latin America business segment.

In 1997, in order to monetize a portion of the cash value of our investment in Time Warner Inc. (TW) convertible preferred stock (TW Preferred), we issued 22.9 million of unsecured 7% Automatic Common Exchange Securities (ACES) having an original principal amount of $1.052 billion and maturing July 1, 2000. The market value of ACES was indexed to the market value of TW Common Stock (TW Common). On July 6, 1999, we converted our investment in TW Preferred into 45.8 million shares of TW Common. Prior to the conversion, our investment in the TW Preferred was accounted for under the cost method at a value of $990 million. Effective on the conversion date, the shares of TW Common were classified as trading securities under Statement of Financial Accounting Standards (SFAS) No. 115, "Accounting for Certain Investments in Debt and Equity Securities" (SFAS No. 115), and an unrealized gain was recorded in the amount of $2.4 billion ($1.5 billion after-tax) to reflect the cumulative appreciation in the fair value of our investment in Time Warner securities. On the July 1, 2000 maturity date, we tendered 37.9 million shares of TW Common to fully settle our obligations in connection with our ACES obligation. On September 21, 1999, we issued approximately 17.2 million of 2.0% Zero-Premium Exchangeable Subordinated Notes due 2029 (ZENS) having an original principal amount of $1.0 billion. At maturity the holders of the ZENS will receive in cash the higher of the original principal amount of the ZENS (subject to adjustment) or an amount based on the then-current market value of TW Common, or other securities distributed with respect to TW Common. We used $537 million of the net proceeds from the offering of the ZENS to purchase 9.2 million additional shares of TW Common, which are classified as trading securities under SFAS No. 115. Prior to the purchase of additional shares of TW Common on September 21, 1999, we owned approximately 8 million shares of TW Common that were in excess of the 37.9 million shares needed to economically hedge our ACES obligation. Prior to January 1, 2001, an increase above $58.25 (subject to some adjustments) in the market value per share of TW Common resulted in an increase in our liability for the ZENS. However, as the market value per share of TW Common declined below $58.25 (subject to some adjustments), the liability for the ZENS did not decline below the original principal amount. Our investment in TW (now AOL Time Warner) securities has been held to facilitate our ability to meet our obligations under the ACES and ZENS.

The following table sets forth summarized financial information regarding our investment in TW securities and our ACES and ZENS obligations (in millions):

	TW Investment	ACES	ZENS
Balance at December 31, 1997	$ 990	$ 1,174	
Loss on indexed debt securities	—	1,176	
Balance at December 31, 1998	990	2,350	
Issuance of indexed debt securities	—	—	$1,000
Purchase of TW Common	537	—	—
Loss on indexed debt securities	—	388	241
Gain on TW Common	2,452	—	—
Balance at December 31, 1999	3,979	2,738	1,241
Loss (Gain) on indexed debt securities	—	139	(241)
Loss on TW Common	(205)	—	—
Settlement of ACES	(2,877)	(2,877)	—
Balance at December 31, 2000	$ 897	$ —	$1,000

For additional information regarding our investment in AOL Time Warner, our indexed debt securities and the effect of adoption of SFAS No. 133, "Accounting for Derivative Instruments and Hedging Activities," as amended, on January 1, 2001 on our ZENS obligation, please read Note 8 to our consolidated financial statements.

In 1999 in connection with the implementation of the Legislation, we evaluated the recovery of our generation related regulatory assets and liabilities. We determined that a pre-tax accounting loss of $282 million existed because we believed only the economic value of our generation related regulatory assets (as defined by the Legislation) would be recovered. Therefore, we recorded a $183 million after-tax

extraordinary loss in the fourth quarter of 1999. If events were to occur that made the recovery of some of the remaining generation related regulatory assets no longer probable, we would write off the remaining balance of such assets as a non-cash charge against earnings. For information regarding the $183 million extraordinary loss, please read "— Certain Factors Affecting Our Future Earnings — Competitive, Regulatory and Other Factors Affecting Our Electric Operations — Other Regulatory Factors" and Note 4(a) to our consolidated financial statements.

In the fourth quarter of 2000, prior to the measurement date, our Latin America business segment sold its investments in El Salvador and a portion of its investments in Colombia for an aggregate $303 million in after-tax proceeds. The measurement date is the date we began reporting our Latin America business segment as discontinued operations. We recorded a $127 million after-tax loss in connection with the sale of these investments which was included in our after-tax loss from discontinued operations of $172 million (net of an income tax benefit of $46 million) in 2000. Subsequent to the measurement date, we sold our investments in Brazil and our remaining investments in Colombia for an aggregate $487 million in after-tax proceeds. We recorded a $114 million after-tax loss in connection with the sale of these investments which was included in our after-tax loss on disposal of discontinued operations of $159 million (net of income taxes of $13 million) in 2000. Our Latin America business segment's remaining investments include a wholly owned cogeneration facility and a distribution company, both located in Argentina, and a minority interest in a coke calcining plant in India. We anticipate that the sale of the remainder of these assets will be completed by December 2001. The total provision for the disposal of discontinued operations of $159 million includes a $5 million reserve for anticipated operating losses through the completion of the sales, which includes $4 million of operating losses from the measurement date through December 31, 2000.

Our consolidated net income, after adjusting for extraordinary and unusual items (as described above) in both years, was $838 million ($2.94 per basic share) for 2000 compared to $508 million ($1.78 per basic share) for 1999. The $330 million increase was primarily due to increased earnings from our Wholesale Energy and Electric Operations segments and additional earnings from our European Energy segment, which was established in the fourth quarter of 1999. The increase was partially offset by lower earnings in 2000 compared to 1999 from our Natural Gas Distribution segment and increased losses from our Other Operations segment.

Operating Income. For an explanation of changes in our operating income, please read the discussion below of operating income (loss) by segment.

Income (Loss) of Equity Investments. Our Wholesale Energy segment reported income from equity investments in 2000 of $43 million compared to equity losses of $1 million in 1999. The equity income in 2000 primarily resulted from an investment in an electric generation plant in Boulder City, Nevada. The plant became operational in May 2000.

Other Income, net. Other income, net was $60 million and $83 million in 1999 and 2000, respectively. The increase in other income in 2000 of $23 million compared to 1999 was primarily due to the following items:

- an increase in interest income of $57 million primarily related to income tax refunds received in 2000 and margin deposits on energy trading activities,
- a pre-tax gain of $18 million in 2000 on the sale of our interest in one of our development stage electric generation projects,
- partially offset by an impairment loss of $27 million on marketable equity securities classified as "available-for-sale" in 2000, distributions of $9 million from venture capital investments in marketable securities classified as "trading" in 1999 and a decline of $19 million in dividend income from our AOL Time Warner investment. For additional information, please read Note 8 to our consolidated financial statements.

During 2000, we incurred a pre-tax impairment loss of $27 million on marketable equity securities classified as "available-for-sale" by Other Operations. Management's determination to recognize this impairment resulted from a combination of events occurring in 2000 related to this investment. Such events

affecting the investment included changes occurring in the investment's senior management, announcement of significant restructuring charges and related downsizing for the entity, reduced earnings estimates for this entity by brokerage analysts and the bankruptcy of a competitor of the entity in the first quarter of 2000. These events coupled with the stock market value of our investment in these securities continuing to be below our cost basis, caused management to believe the decline in fair value to be other than temporary. For additional discussion of this investment, please read Note 2(l) to our consolidated financial statements.

Interest Expense and Other Charges. In 1999 and 2000, interest expense and other charges were $550 million and $754 million, respectively. Increased interest expense and other charges in 2000 compared to 1999 were primarily due to increased levels of short-term borrowings. These increases were associated in part with borrowings to fund the purchase obligation for the acquisition of UNA in the fourth quarter of 1999 and the first quarter of 2000, the acquisition of the REMA entities in the second quarter of 2000, other acquisitions, capital expenditures and increased margin deposits on energy trading activities.

Income Tax Expense. The effective tax rate for 1999 and 2000 was 35.4% and 32.8%, respectively. After adjusting for the unrealized accounting gains and losses on our investment in AOL Time Warner and indexed debt securities, the adjusted effective tax rate for 1999 and 2000 was 33.9% and 33.0%, respectively. The decrease in the effective tax rate in 2000 compared to 1999 was primarily due to a Dutch tax holiday. In 2000 and prior years, under Dutch corporate income tax laws, the earnings of UNA were subject to a zero percent Dutch corporate income tax rate as a result of the Dutch tax holiday related to the Dutch electric industry. In 2002, all of European Energy's earnings in the Netherlands will be subject to the standard Dutch corporate income tax rate, which currently is 35%.

1999 Compared to 1998.

Net Earnings. We reported consolidated earnings in 1999 of $1.482 billion ($5.20 per basic share) compared to a consolidated net loss of $141 million ($0.50 per share) for 1998. The 1999 results included the extraordinary and unusual items discussed above under "— 2000 Compared to 1999 — Net Earnings." The reported loss for 1998 included a $764 million (after-tax) non-cash, unrealized accounting loss on indexed debt securities (as discussed above) and after-tax income from discontinued operations of $137 million.

Our consolidated net income, after adjusting for extraordinary and unusual items (as discussed above) in both years, was $508 million ($1.78 per share) for 1999 compared to $486 million ($1.71 per share) for 1998. The $22 million increase was primarily due to earnings of our European Energy segment, which acquired UNA in the fourth quarter of 1999, and lower losses from our Other Operations segment. These improvements were partially offset by lower earnings in 1999 for our Natural Gas Distribution, Pipelines and Gathering, and Wholesale Energy segments.

Operating Income. For an explanation of changes in our operating income, please read the discussion below of operating income (loss) by business segment.

(Loss) Income of Equity Investments. Our Wholesale Energy segment reported a loss from equity investments of $1 million in both 1998 and 1999.

Other Income, net. Other income, net was $68 million and $60 million in 1998 and 1999, respectively. The decrease in other income in 1999 of $8 million compared to 1998 was primarily due to a decline in dividend income from our AOL Time Warner investment of $15 million from 1998 (please read Note 8 to our consolidated financial statements), partially offset by distributions of $9 million from a venture capital investment of marketable securities classified as "trading" in 1999, as discussed above.

Interest Expense and Other Charges. In 1998 and 1999, interest expense and other charges were $532 million and $550 million, respectively. Increased interest expense and other charges in 1999 compared to 1998 were primarily due to higher levels of short-term borrowings, long-term debt and trust preferred securities. These increases were associated in part with the acquisition of UNA in the fourth quarter of 1999, our additional investment in AOL Time Warner in 1999, other acquisitions of businesses and capital expenditures. The increase in 1999 was partially offset by a decrease in the average interest rate on our long-term debt.

Income Tax Expense. The effective tax rate for 1998 and 1999 was 22.9% and 35.4%, respectively. After adjusting for the unrealized accounting gains and losses on our investment in AOL Time Warner and indexed debt securities, the adjusted effective tax rate for 1998 and 1999 was 40.4% and 33.9%, respectively. The decrease in effective tax rate in 1999 compared to 1998 was primarily due to the discontinuance of SFAS No. 71, "Accounting for the Effects of Certain Types of Regulation" (SFAS No. 71), for the generation operations of our Electric Operations segment. For information regarding the discontinuance of SFAS No. 71 to the generation operations of our Electric Operations segment, see Note 4(a) to our consolidated financial statements.

RESULTS OF OPERATIONS BY BUSINESS SEGMENT

The following table presents operating income (loss) for each of our business segments for 1998, 1999 and 2000 (in millions). Some amounts from the previous years have been reclassified to conform to the 2000 presentation of the financial statements. These reclassifications do not affect consolidated earnings.

Operating Income (Loss) by Business Segment

	Year Ended December 31,		
	1998	1999	2000
		(in millions)	
Electric Operations	$1,002	$ 981	$1,230
Natural Gas Distribution	167	158	113
Pipelines and Gathering	146	131	137
Wholesale Energy	42	27	482
European Energy	—	32	89
Other Operations	(77)	(71)	(172)
Total Consolidated	$1,280	$1,258	$1,879

Electric Operations

Our Electric Operations segment conducts operations through an unincorporated division of Reliant Energy under the name "Reliant Energy HL&P." This segment generates, purchases, transmits and distributes electricity to approximately 1.7 million customers in a 5,000 square mile area on the Texas Gulf Coast, including Houston.

In 1999, the Texas legislature adopted the Legislation, which substantially amended the regulatory structure governing electric utilities in Texas in order to allow retail competition beginning on January 1, 2002. Prior to adoption of the Legislation, our Electric Operations segment's earnings were capped at an agreed overall rate of return formula on a calendar year basis as part of the transition to competition plan (Transition Plan) approved by the Texas Utility Commission effective January 1, 1998. As a result of the Transition Plan, any earnings prior to the Legislation above the maximum allowed return cap on invested capital were offset by additional depreciation of our Electric Operations segment's electric generation assets. For more information regarding the Legislation, please read "Business — Regulation — State and Local Regulations — Texas — Electric Operations — The Legislation" in Item 1 of this Form 10-K and Note 4(a) to our consolidated financial statements. For more information regarding the Transition Plan, please read Notes 2(g) and 4(c) to our consolidated financial statements.

For a discussion of the factors that may affect the future results of operations of our Electric Operations segment, please read "— Certain Factors Affecting Our Future Earnings — Competitive, Regulatory and Other Factors Affecting Our Electric Operations."

The following table provides summary data regarding the results of operations of our Electric Operations segment for 1998, 1999 and 2000 (in millions, except electric sales data):

	Year Ended December 31,		
	1998	1999	2000
Operating Revenues:			
Base revenues(1)	$ 2,969	$ 2,968	$ 3,141
Reconcilable fuel revenues(2)	1,381	1,515	2,353
Total operating revenues	4,350	4,483	5,494
Operating Expenses:			
Fuel and purchased power	1,455	1,569	2,412
Operation and maintenance	890	916	963
Depreciation and amortization	663	667	507
Other operating expenses	340	350	382
Total operating expenses	3,348	3,502	4,264
Operating Income	$ 1,002	$ 981	$ 1,230
Electric Sales (gigawatt-hours (GWh)):			
Residential	21,216	21,144	22,727
Commercial	16,388	16,616	17,594
Industrial — Firm	26,542	26,020	27,707
Industrial — Interruptible	5,115	5,460	5,542
Other	3,472	2,867	1,724
Total	72,733	72,107	75,294

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(1) Includes miscellaneous revenues, non-reconcilable fuel revenues and purchased power-related revenues.

(2) Includes revenues collected through a fixed fuel factor and surcharges net of adjustments for over/under recovery of fuel.

2000 Compared to 1999. Our Electric Operations segment operating income for 2000 increased $249 million compared to 1999. The increase was primarily due to decreased depreciation and amortization expense, strong customer growth and warmer weather, partially offset by increased operation and maintenance expenses and other taxes.

Base revenues increased $173 million in 2000 due to continued customer growth and demand growth from the effects of weather as compared to 1999. Growth in usage per customer and number of customers contributed $132 million of the increase in base revenues in 2000.

Our 55% increase in reconcilable fuel revenue in 2000 resulted primarily from increased fuel costs as discussed below. The Texas Utility Commission provides for recovery of some fuel and purchased power costs through a fixed fuel factor included in electric rates. Revenues collected through this factor are adjusted monthly to equal expenses; therefore, these revenues and expenses have no effect on earnings unless fuel costs are determined not to be recoverable. The adjusted over/under recovery of fuel costs is recorded on our consolidated balance sheets as other liabilities or regulatory assets, respectively. For information regarding the effect of the Legislation on fuel recovery beginning in 2002, please read "Business — Regulation — State and Local Regulations — Texas — Electric Operations — The Legislation" in Item 1 of this Form 10-K and Note 4 to our consolidated financial statements for information regarding Reliant Energy HL&P fuel filings.

Fuel and purchased power expenses in 2000 increased by $843 million, or 54%, over 1999 expenses. The increase is primarily the result of higher reconcilable costs for natural gas ($2.47 and $3.98 per MMBtu in 1999 and 2000, respectively), higher costs for purchased power ($26.46 and $44.26 per MWh in 1999 and

2000, respectively) and higher sales due to customer growth and increased demand, which led to increased production.

Operation, maintenance and other operating expenses increased $79 million in 2000 compared to 1999 primarily due to the following items:

- a $25 million increase due to transmission expenses resulting from the wholesale rates established by ERCOT,
- a $22 million increase in state franchise taxes and municipal franchise fees due to increased earnings and cash receipts,
- a $24 million assessment for the 1999 and 2000 System Benefit Fund, which was established by the Legislation to insure that public schools were not impacted by the loss of taxes related to the lower property values of generation assets, substantially offset by a decrease in property taxes of $21 million, and
- a $22 million increase in other operation and maintenance expense.

Depreciation and amortization expense decreased $160 million primarily due to our discontinuance of recording additional depreciation and redirected depreciation pursuant to the Transition Plan, the extension of electric generation assets' depreciable lives, fully amortizing some investments in lignite reserves associated with a cancelled generation station and ceasing amortization of regulatory assets pursuant to the Legislation. For additional information regarding items that affect depreciation and amortization expense of Electric Operations pursuant to the Legislation and the Transition Plan, please read Notes 2(g) and 4(a) to our consolidated financial statements.

1999 Compared to 1998. Electric Operations' operating income for the year ended December 31, 1999 was $981 million compared to $1,002 million for the same period in 1998. The $21 million decrease was primarily due to the effects of milder weather and additional base rate credits provided under the Transition Plan, partially offset by continued strong customer growth.

Electric Operations' base revenues were $2,968 million for 1999, a decrease of $1 million from 1998. The effects of milder weather in 1999 compared to 1998 and additional base rate credits in 1999 were offset by continued strong customer growth and increased usage per customer.

Electric Operations' fuel and purchased power expenses in 1999 increased by $114 million, or 8%, over 1998 expenses. The increase is a result of higher costs for natural gas ($2.18 and $2.47 per MMbtu in 1998 and 1999, respectively) and higher costs for lignite ($1.19 and $1.42 per MMbtu in 1998 and 1999, respectively). The 1998 fuel costs include a $12 million charge to non-reconcilable fuel due to some fuel costs being determined not to be recoverable.

Operation, maintenance and other operating expenses increased $36 million in 1999 compared to 1998, including $38 million due to transmission tariffs within ERCOT. A portion of these transmission expenses was offset by an increase of $28 million in transmission tariff revenue. State franchise taxes increased $13 million in 1999 compared to 1998.

Natural Gas Distribution

Natural Gas Distribution's operations consist of intrastate natural gas sales to, and natural gas transportation for, residential, commercial and industrial customers in Arkansas, Louisiana, Minnesota, Mississippi, Oklahoma and Texas and some non-rate regulated retail marketing of natural gas.

For a discussion of the factors that may affect future results of operations of our Natural Gas Distribution segment, please read "— Certain Factors Affecting Our Future Earnings — Competitive and Other Factors Affecting RERC Operations — Natural Gas Distribution."

The following table provides summary data regarding the results of operations of Natural Gas Distribution for 1998, 1999 and 2000 (in millions, except throughput data):

	Year Ended December 31,		
	1998	1999	2000
Operating Revenues	$2,426	$2,788	$4,412
Operating Expenses:			
Natural gas	1,655	1,936	3,503
Operation and maintenance	378	470	553
Depreciation and amortization	131	137	145
Other operating expenses	95	87	98
Total operating expenses	2,259	2,630	4,299
Operating Income	$ 167	$ 158	$ 113
Throughput Data (in billion cubic feet (Bcf)):			
Residential and commercial sales	286	286	318
Industrial sales	56	53	55
Transportation	44	47	50
Retail	347	400	431
Total Throughput	733	786	854

2000 Compared to 1999. Our Natural Gas Distribution segment operating income decreased $45 million in 2000 from 1999. Increases in revenues and natural gas expenses were due primarily to the increase in the price of natural gas. In addition, operating revenues increased $6 million related to gains from the effect of a financial hedge of our Natural Gas Distribution segment's earnings against unseasonably warm weather during peak heating months. Slightly increased operating margins (revenues less fuel costs) in 2000 were offset by higher operating expenses and higher depreciation expense in 2000. Operation and maintenance expenses increased in 2000 primarily due to the following items:

- costs incurred in connection with some non-rate regulated retail natural gas business activities outside our established market areas, which have been discontinued,
- additional provisions against receivable balances resulting from the implementation of a new billing system for Arkla and
- increased employee benefit costs relating to an updated actuarial valuation of employee benefit plans.

Generally, our utility operations of the Natural Gas Distribution segment are allowed to flow through the costs of natural gas to our customers through purchased gas adjustment provisions in rates pursuant to regulations of the states in which they operate. Differences between actual gas costs and the amount collected from customers are deferred on the balance sheet so that there is no impact on operating income.

1999 Compared to 1998. Our Natural Gas Distribution segment operating income decreased $9 million in 1999 compared to 1998 primarily due to increased operating expenses, partially offset by slightly improved operating margins in 1999. Operating expenses increased primarily due to increased employee benefit costs and costs associated with the implementation of an enterprise-wide information system.

Pipelines and Gathering

Our Pipelines and Gathering segment operates two interstate natural gas pipelines, as well as provides gathering and pipeline services.

For a discussion of the factors that may affect future results of operations of our Pipelines and Gathering segment, please read "— Certain Factors Affecting Our Future Earnings — Competitive and Other Factors Affecting RERC Operations — Pipelines and Gathering."

The following table provides summary data regarding the results of operations of our Pipelines and Gathering segment for 1998, 1999 and 2000 (in millions, except throughput data):

	Year Ended December 31,		
	1998	1999	2000
Operating Revenues	$ 346	$ 331	$ 384
Operating Expenses:			
Natural gas	52	41	76
Operation and maintenance	85	91	100
Depreciation and amortization	48	53	56
Other operating expenses	15	15	15
Total operating expenses	200	200	247
Operating Income	$ 146	$ 131	$ 137
Throughput Data (Bcf):			
Natural gas sales	16	15	14
Transportation	825	836	845
Gathering	237	270	288
Elimination(1)	(15)	(14)	(12)
Total Throughput	1,063	1,107	1,135

(1) Elimination of volumes both transported and sold.

2000 Compared to 1999. Our Pipelines and Gathering segment's operating income for 2000 increased $6 million, primarily due to increased gas gathering and processing revenues. Natural gas expense increased $35 million in 2000, primarily due to the increased cost of natural gas per unit. Operation and maintenance expense increased $9 million in 2000, primarily due to the implementation of various projects throughout the year.

1999 Compared to 1998. Our Pipelines and Gathering segment's operating income for 1999 decreased $15 million, primarily due to the settlement of a dispute related to some gas purchase contracts that resulted in the recognition of $6 million of revenues in 1998, a reduction in depreciation and amortization in 1998 of $5 million related to a rate case settlement and an increase in operating expenses in 1999, primarily due to employee benefit expenses.

Operating revenue decreased by $15 million in 1999, primarily due to the settlement of outstanding gas purchase contract litigation in 1998 as discussed above. Natural gas expense decreased $11 million in 1999, primarily due to expiration of gas supply contracts. Operation and maintenance expense increased $6 million in 1999, primarily due to increases in employee benefit expenses. Depreciation and amortization expense increased $5 million in 1999 due to a rate settlement recorded in 1998 as discussed above. The rate settlement, effective January 1998, provided for a $5 million reduction in depreciation rates retroactive to July 1996.

During 1998 and 1999, our Pipelines and Gathering segment's largest unaffiliated customer was a natural gas utility that serves the greater St. Louis metropolitan area in Illinois and Missouri. Revenues from this customer were generated pursuant to several long-term firm storage and transportation agreements that begin to expire at various dates beginning October 2001 through May 2002. We are currently negotiating the terms and conditions of a renewal of these agreements with the unaffiliated customer.

During 2000, we obtained regulatory approval and REGT renewed various contracts for firm transportation and storage with Arkla. These renewals extended the term of service to 2005 in Arkla's market areas.

Wholesale Energy

Our Wholesale Energy segment includes our non-rate regulated power generation operations in the United States and our wholesale energy trading, marketing, power origination and risk management operations in North America.

As of December 31, 2000, our Wholesale Energy segment owned or leased electric power generation facilities with an aggregate net generating capacity of 9,231 MW in the United States. Our Wholesale Energy segment acquired its first power generation facilities in April 1998, and has increased its aggregate net generating capacity since then through a combination of acquisitions, contractual agreements and the development of new generating projects. As of December 31, 2000, we had 2,766 MW of additional net generating capacity under construction. For additional information regarding the acquisition of our Mid-Atlantic generating assets completed in May 2000, including the accounting treatment of this acquisition, please read Note 3(a) to our consolidated financial statements.

For a discussion of the factors that may affect the future results of operations of our Wholesale Energy segment, please read "— Certain Factors Affecting Our Future Earnings — Competitive, Regulatory and Other Factors Affecting Our Wholesale Energy Operations."

The following table provides summary data regarding the results of operations of our Wholesale Energy segment for 1998, 1999 and 2000 (in millions, except operations data).

	Year Ended December 31,		
	1998	1999	2000
Operating Revenues	$4,416	$7,912	$19,234
Operating Expenses:			
Fuel and cost of gas sold	2,421	3,975	10,402
Purchased power	1,829	3,729	7,825
Operation and maintenance	106	154	403
Depreciation and amortization	14	21	109
Other operating expenses	4	6	13
Total Operating Expenses	4,374	7,885	18,752
Operating Income	$ 42	$ 27	$ 482
Operations Data:			
Net Generating Capacity (MW)	3,800	4,469	9,231
Electricity Wholesale Power Sales (MMWh)	65	112	202
Natural Gas Sales (Bcf)	1,163	1,820	2,509

2000 Compared to 1999. Our Wholesale Energy segment's operating income increased $455 million for 2000 compared to 1999. The increase was primarily due to increased energy sales volumes, higher prices for energy and ancillary services, and improved operating results from trading and marketing activities, as well as expansion of our Wholesale Energy segment's generation operations into regions other than the Western United States, including the Mid-Atlantic United States (Pennsylvania, New Jersey and Maryland), Florida and Texas.

Our Wholesale Energy segment's operating revenues increased $11.3 billion (143%) for 2000 compared to 1999. The increase was primarily due to an increase in prices and volumes for both gas and power sales in 2000 as compared to 1999. Our fuel and cost of gas sold and purchased power costs increased $6.4 billion and $4.1 billion, respectively, in 2000 compared to 1999. The increase in fuel and cost of gas sold was primarily due to an increase in gas volumes purchased and to increases in plant output and in the price of gas. The increase in purchased power cost was primarily due to a higher average cost of power and higher power volumes purchased. Operation and maintenance expenses increased $249 million in 2000 compared to 1999. This increase was primarily due to costs associated with the maintenance of facilities acquired or placed into commercial operation during the period, lease expense associated with the Mid-Atlantic generating facilities sale/leaseback transactions, higher run rates at existing facilities, increased costs associated with developing

new power generation projects and higher staffing levels to support increased sales and expanded trading and marketing efforts. Depreciation and amortization expense for 2000 increased $88 million as compared to 1999, primarily as a result of our acquisition of the Mid-Atlantic generating facilities and other generating facilities in 2000.

Our Wholesale Energy segment's operations in California have been affected by the crisis conditions of California's wholesale market, most significantly the financial distress of two of California's public utilities and the subsequent downgrading of those utilities' credit ratings and defaults on payments for wholesale power purchased in the fourth quarter of 2000. The California Legislature has passed emergency legislation appropriating funds to be used by the CDWR for the purchase of wholesale electricity, but these funds have been used to pay only for some of the electricity currently needed by the utilities' customers. We have not been paid for much of the power we sold in November and December 2000 through the Cal PX and to the Cal ISO. In the fourth quarter of 2000, we recorded a pre-tax provision of $39 million against receivable balances related to energy sales in the California market. For additional information regarding the uncertainties in the California wholesale energy market, please read "Wholesale Energy — Power Generation Operations — Southwest Region," "Regulation — State and Local Regulations — California" in Item 1 of this Form 10-K, "— Certain Factors Affecting Our Future Earnings — Competitive, Regulatory and Other Factors Affecting Our Wholesale Energy Operations — California" as well as Notes 14(g) and 14(h) to our consolidated financial statements.

1999 Compared to 1998. Our Wholesale Energy segment reported operating income of $27 million in 1999 compared to $42 million in 1998. The $15 million decrease was due primarily to a decline in market prices for electricity in the California market caused by milder than normal weather and increased hydroelectric generation sold by competitors into the California market. This decline more than offset significant increases in operating income of our trading and marketing operations in 1999. The increases in trading and marketing operating income resulted primarily from increases in volumes of gas, power and heating oil trading and slightly higher margins (revenue less cost of power sold) on power trading.

Operating revenues were $7.9 billion in 1999, a 79% increase from 1998 revenues of $4.4 billion. The increase in revenues was primarily due to increased trading volumes for power, gas and heating oil. Higher sales prices for both power and gas also contributed to increased revenues.

Fuel and cost of gas sold and purchased power costs increased $1.6 billion and $1.9 billion, respectively, in 1999 compared to 1998. These increases were primarily due to the corresponding increase in trading sales volumes. An increase in power and gas prices also contributed to the increase in costs. Operation and maintenance expenses in 1999 increased $48 million compared to 1998. The increase was primarily due to costs associated with the maintenance of the assets in California, which we acquired in April and July 1998. Depreciation and amortization in 1999 increased $7 million from 1998 due primarily to a full year of depreciation and amortization for our California operations as well as additional assets placed into operation during 1999.

European Energy

Our European Energy segment includes the operations of UNA and its subsidiaries and our European trading, marketing and risk management operations. We created this segment in the fourth quarter of 1999 with the acquisition of UNA and the formation of our European trading, marketing and risk management operations. Our European Energy segment generates and sells power from its generation facilities in the Netherlands and participates in the emerging wholesale energy trading and marketing industry in Northwest Europe.

Effective October 7, 1999, we acquired UNA, for a net purchase price of $1.9 billion. From October 1, 1999, our operating results include the results of operations of UNA. The impact of UNA's results of operations from October 1 through October 7, 1999 was immaterial to our consolidated results of operations. For additional information regarding the acquisition of UNA, please read Note 3(b) to our consolidated financial statements.