

TXU CORP. AND SUBSIDIARIES
NOTES TO FINANCIAL STATEMENTS

1. BUSINESS RESTRUCTURING AND OTHER ACTIONS

TXU Corp. is a holding company conducting its operations principally through its TXU Energy Holdings and TXU Electric Delivery subsidiaries. TXU Energy Holdings is engaged in electricity generation and retail and wholesale energy sales. TXU Electric Delivery engages in regulated electricity transmission and distribution operations.

TXU Corp. has two reportable segments: TXU Energy Holdings and TXU Electric Delivery. (See Note 19 for further information concerning reportable business segments.)

Mr. C. John Wilder, who was named president and chief executive of TXU Corp. in February 2004, and senior management reviewed TXU Corp.'s operations during 2004 to identify and implement strategic initiatives designed to improve operational and financial performance. Areas reviewed included:

- Noncore business activities;
- Cost effectiveness of generation operations;
- Administrative cost structure, including organizational alignments and headcount;
- Debt portfolio and capital structure; and
- Opportunities to improve retail customer service.

Management believes that its actions in 2004 have resulted in sustainable profitability improvements, principally through streamlining of the organization, optimization of energy supply costs and improved customer retention. In addition, increased focus on income tax, litigation and other contingencies has resulted in significant progress in resolving these matters. These activities have resulted in unusual charges and credits impacting 2004 income from continuing operations, summarized as follows and discussed below in more detail:

	<u>Income Statement</u> <u>Classification</u>	<u>Charge/(Credit) to Earnings</u>	
		<u>Pretax</u>	<u>After-tax</u>
TXU Energy Holdings segment:			
Charges related to leased equipment.....	Other deductions	\$ 180	\$ 117
Software write-off	Other deductions	107	70
Employee severance costs	Other deductions	107	69
Power purchase contract termination	Other deductions	101	66
Spare parts inventory write-down	Other deductions	79	51
Outsourcing transition costs	Other deductions	10	6
Other asset impairments	Other deductions	6	4
Other charges.....	Operating costs/SG&A	8	6
Recognition of deferred gain on plant sales.....	Other income	(58)	(38)
Gain on sale of undeveloped properties	Other income	(19)	(12)
TXU Electric Delivery segment:			
Employee severance costs	Other deductions	20	13
Rate case settlement reserve	Other deductions	21	14
Outsourcing transition costs	Other deductions	4	3
Software write-off and asset impairment	Other deductions	4	2
Other charges.....	Operating costs/SG&A	2	1
Corporate and other:			
Debt extinguishment losses	Other deductions	416	382
Litigation accrual.....	Other deductions	86	56
Executive compensation	SG&A	52	52
Consulting and professional fees.....	SG&A	54	35
Employee severance costs	Other deductions	5	3
Other charges.....	Other deductions	5	3
Recognition of TXU Europe income tax benefit ...	Income taxes	—	(75)
Total		<u>\$ 1,190</u>	<u>\$ 828</u>

In addition, income from discontinued operations totaled \$378 million in 2004, reflecting the recognition of additional tax benefits related to the write-off of the investment in TXU Europe, the dispositions of TXU

Australia and TXU Gas and a charge related to the settlement of potential claims related to TXU Europe. (See Note 4 to Financial Statements.)

Following is a discussion of the major activities associated with the restructuring plan:

Sale of TXU Australia

In July 2004, TXU Corp. completed the sale of TXU Australia to Singapore Power Ltd. for \$1.9 billion in cash and \$1.7 billion in assumed debt, and recorded a gain on sale of \$371 million (\$241 million after-tax). TXU Australia's operations consisted of a portfolio of competitive and regulated energy businesses, principally in Victoria and South Australia, with 2003 revenues of approximately \$1.1 billion. The results of TXU Australia and the gain on sale are reported as discontinued operations as discussed in Note 4 to Financial Statements.

Sale of TXU Fuel

In June 2004, TXU Corp. completed the sale of the assets of TXU Fuel, the former intrastate gas transportation subsidiary of TXU Energy Holdings, to Energy Transfer Partners, L.P. for \$500 million in cash. TXU Fuel had 2003 revenues of approximately \$65 million, the majority of which represented gas transportation fees from TXU Energy Holdings. As part of the transaction, TXU Energy Holdings entered into a transportation agreement, intended to be market-price based, with the new owner to transport gas to TXU Energy Holdings' generation plants. Because of the continuing involvement in the business through the transportation agreement, the pretax gain related to the sale of \$375 million will be recognized over the eight-year life of the transportation agreement, and the business has not been accounted for as a discontinued operation. The pretax gain is net of \$16 million of TXU Energy Holdings goodwill allocated to TXU Fuel.

TXU Gas Transaction

In October 2004, Atmos Energy Corporation and TXU Gas completed a merger by division, which resulted in TXU Corp.'s disposition of the operations of TXU Gas for \$1.9 billion in cash. TXU Gas was largely a regulated business engaged in the purchase, transmission, distribution and retail sale of natural gas with 2003 revenues of approximately \$1.3 billion. The results of TXU Gas, as well as charges related to the sale of \$108 million (\$193 million after-tax), are reported as discontinued operations as discussed in Note 4 to Financial Statements.

In October 2004, TXU Corp. redeemed or legally defeased \$429 million principal amount of TXU Gas debt. In addition, all of the outstanding shares of TXU Gas' preferred stock with a liquidation value of \$75 million were redeemed in November 2004.

Capgemini Outsourcing Agreement

In May 2004, TXU Corp. entered into a services agreement with Capgemini Energy LP (Capgemini), a new company initially providing business process support services to TXU Corp. only, but immediately implementing a plan to offer similar services to other utility companies. Under the ten-year agreement, over 2,500 employees transferred from subsidiaries of TXU Corp. to Capgemini effective July 1, 2004. Outsourced base support services performed by Capgemini for a fixed fee, subject to adjustment for volumes or other factors, include information technology, customer call center, billing, human resources, supply chain and certain accounting activities. TXU Corp. expects that the Capgemini arrangement will result in lower costs and improved service levels.

As part of the agreement, Capgemini was provided a royalty-free right, under an asset license arrangement, to use TXU Corp.'s information technology assets, consisting primarily of capitalized software. A portion of the software was in development and had not yet been placed in service. As a result of outsourcing its information technology activities, TXU Corp. no longer intends to develop the majority of these projects and from TXU Corp.'s perspective the software is abandoned. The agreements with Capgemini do not require that any software in development be completed and placed in service. Consequently, the carrying value of these software projects

was written off, resulting in a charge of \$109 million (\$71 million after-tax). TXU Corp. expects to rely on Capgemini for future enhancements and modifications to the software in use at the time of the transaction.

TXU Corp. obtained a 2.9% limited partnership interest in Capgemini in exchange for the asset license described above. TXU Corp. has the right to sell (the “put option”) its interest and the licensed software to Cap Gemini North America Inc. for \$200 million, plus its share of Capgemini’s undistributed earnings, upon expiration of the services agreement or earlier upon the occurrence of certain unexpected events. Cap Gemini North America Inc. has the right to purchase these interests under the same terms and conditions. The partnership interest has been recorded at an initial value of \$2.9 million and is being accounted for on the cost method.

TXU Corp. has recorded the fair value of the put option, estimated at \$177 million, as a noncurrent asset. Of this amount, \$169 million was recorded as a reduction to the carrying value of the licensed software. This accounting is in accordance with guidance related to sales and licensing of internally developed software described in AICPA Statement of Position 98-1, “Accounting for the Costs of Computer Software Developed or Obtained for Internal Use.” The difference of \$8 million, which represented the fair value of the assumed cash distributions and gains while holding the partnership interest for the period prior to exercise of the put, was recorded as a noncurrent deferred credit. The remaining balance of the software is being amortized over the estimated remaining useful lives.

Also as part of the agreement, TXU Corp. agreed to indemnify Capgemini for severance costs incurred by Capgemini for former TXU Corp. employees terminated within 18 months of their transfer to Capgemini. Accordingly, TXU Corp. recorded a \$40 million (\$26 million after-tax) charge for severance expense in the second quarter of 2004. In addition, TXU Corp. committed to pay up to \$25 million for costs associated with transitioning the outsourced activities to Capgemini. Transition expenses of \$14 million (\$9 million after-tax) were recorded by TXU Corp. during 2004, and the remainder are expected to be expensed as incurred in 2005.

Subject to certain terms and conditions, Cap Gemini North America, Inc. and its parent, Cap Gemini S.A., have guaranteed the performance and payment obligations of Capgemini under the services agreement, as well as the payment of \$200 million in connection with the put option.

In July 2004, TXU Corp. loaned Capgemini \$25 million for working capital purposes pursuant to a promissory note that bears interest at a then market-based annual rate of 4% and matures in July 2019.

Generation Facility Closures and Sales

In December 2004, TXU Corp. committed to immediately cease operating for its own benefit nine leased gas-fired combustion turbines, and recorded a charge of \$157 million (\$102 million after-tax). The charge represents the present value of the future lease payments related to the turbines, net of estimated sublease proceeds. The leases expire in 2017 and 2018. TXU Corp. is currently evaluating opportunities with respect to the turbines, including subleasing the turbines to third parties or decommissioning the turbines. During this evaluation period, the turbines will be available to ERCOT only for system reliability purposes.

In November 2004, TXU Corp. announced plans to deactivate, or mothball, eight gas-fired operating units due to electric industry market conditions in Texas. The units were more than 30 years old and had operated only sparingly during the last two years. The facility closures resulted in employee severance costs of \$7 million (\$5 million after-tax).

In the second quarter of 2004, TXU Corp. initiated a plan to sell the Pedricktown, New Jersey 122 MW power production facility and exit the related power supply and gas transportation agreements. Accordingly, TXU Corp. recorded an impairment charge of \$26 million (\$17 million after-tax) to write down the facility to estimated fair market value. The results of the business and the impairment charge are reported in discontinued operations, as discussed in Note 4 to Financial Statements.

In March 2004, TXU Corp. announced the planned permanent retirement, completed in the second quarter of 2004, of eight gas-fired operating units. TXU Corp. also temporarily closed four other gas-fired units and

placed them under evaluation for retirement. A majority of the 12 units were designated as “peaking units” and operated only during the summer for many years and had operated only sparingly during the last two years. TXU Corp. also closed its Winfield North Monticello lignite mine in Texas, as it was no longer economical to operate when compared to the cost of purchasing coal to fuel the adjacent generation facility. A total charge of \$8 million (\$5 million after-tax) was recorded for employee severance costs and impairments related to the various facility closures.

As a result of the various actions in 2004, TXU Corp. will permanently or temporarily deactivate over 40% of its gas-fired generating capacity in Texas, representing 4,572 MW of capacity.

Other Actions Related to Generation Operations

In December 2004, TXU Corp. executed an agreement to terminate, for a payment of \$172 million, an existing power purchase and tolling agreement that would have expired in 2006. The agreement was entered into in connection with the sale of two generation plants to the counterparty in 2001. As a result of the transaction, TXU Corp. recorded a charge of \$101 million (\$66 million after-tax). The charge represents the payment amount less the remaining out-of-the-money liability related to the agreement originally recorded at its inception. TXU Corp. also recorded a gain of \$58 million (\$38 million after-tax), representing the remaining deferred gains from the sale of the two plants.

In October 2004, TXU Corp. entered into an agreement to terminate the operating lease for certain mining equipment for approximately \$28 million in cash, effective November 1, 2004. The lease termination resulted in a charge of \$21 million (\$14 million after-tax). TXU Corp. entered into a short-term lease with an unrelated third party for the equipment, which is expected to be taken out of service at the expiration of the lease.

As part of a review of its generation asset portfolio in the second quarter of 2004, TXU Corp. completed a review of its spare parts and equipment inventory to determine the appropriate level of such inventory. The review included nuclear, coal and gas-fired generation-related facilities. As a result of this review, TXU Corp. recorded a charge of \$79 million (\$51 million after-tax), to reflect excess inventory on hand and to write down carrying values to scrap values.

Organizational Realignment and Headcount Reductions

During 2004, management completed a comprehensive organizational review, including an analysis of staffing requirements. As a result, TXU Corp. completed a self-nomination severance program and other involuntary severance actions, and recorded severance charges totaling \$77 million (\$49 million after-tax).

Liability and Capital Management

TXU Corp. utilized cash proceeds from the sale of TXU Australia, TXU Gas and TXU Fuel and other assets sales as well as cash provided from operations and lower-cost debt issuances to increase value and reduce risks through an ongoing liability management initiative. Largely under this initiative, in 2004 TXU Corp. repurchased or legally defeased \$3.6 billion of debt securities (including equity-linked debt securities and debt held by subsidiary trusts). In addition, TXU Corp. repurchased \$6.7 billion of common equity and other securities.

The following debt securities were repurchased or legally defeased in 2004:

	Principal Amount Repurchased	Debt Extinguishment Losses (pretax)
<u>TXU Corp.</u>		
Floating Convertible Senior Notes due July 15, 2033	\$ 500	\$ 315
4.446% Fixed Senior Notes Series K (equity-linked) due November 16, 2006	450	23
5.450% Fixed Senior Notes Series L (equity-linked) due November 16, 2007	399	22
5.800% Fixed Senior Notes Series M (equity-linked) due May 16, 2008	256	23
7.250% Long-term debt held by subsidiary trust (Capital I Trust)	237	7
8.700% Long-term debt held by subsidiary trust (Capital II Trust)	155	4
6.375% Fixed Senior Notes Series J due June 15, 2006	117	7
Other, including unamortized debt expenses and retirement fees	—	14
<u>TXU Gas</u>		
Floating Rate long-term debt held by subsidiary trust (Capital I Trust)	154	—
7.125% Fixed Notes due June 15, 2005	150	—
6.564% Fixed Remarketed Reset Notes due January 1, 2008	125	—
<u>TXU Electric Delivery</u>		
7.625% Fixed First Mortgage Bonds due July 1, 2025(a)	215	—
7.375% Fixed First Mortgage Bonds due October 1, 2025(a)	178	—
<u>TXU Energy Holdings</u>		
2.838% Floating Rate Senior Notes due January 17, 2006	400	—
Brazos River Authority Pollution Control Revenue Bonds – 4.950% Fixed Series 2001A due October 1, 2030, remarketing date April 1, 2004(b)	121	
Brazos River Authority Pollution Control Revenue Bonds – portions of Series 2003C, 2002A, 2001C, 2001D, and 1995B	100	1
Total	<u>\$ 3,557</u>	<u>\$ 416</u>

- (c) Repurchased with the proceeds from the securitization (transition) bonds issuance in June 2004.
(d) Purchased upon mandatory tender.

TXU Corp. also repurchased the following securities during 2004:

	Purchase Price	Common Shares Repurchased (in millions)
Common equity - accelerated share repurchase programs (including fees) and open market repurchases	\$ 4,737	84.3
Exchangeable preferred membership interests of TXU Energy Holdings	1,852	—
Preferred stock of TXU Gas	75	—
Total	<u>\$ 6,664</u>	<u>84.3</u>

See Notes 7, 8, 10 and 11 for further detail of debt issuances and retirements, financing arrangements, repurchase of exchangeable preferred membership interests, debt held by unconsolidated subsidiary trusts and capitalization.

Contingencies Update

See Note 18 to Financial Statements for more detailed discussion of contingencies. Following is a description of the progress and status of certain matters related to income taxes, litigation and other potential claims:

Recognition of Income Tax Benefits

On its US federal income tax return for calendar year 2002, TXU Corp. claimed an ordinary loss deduction related to the worthlessness of TXU Corp.'s investment in TXU Europe, the tax benefit of which was estimated to be \$983 million (assuming the deduction is sustained on audit). Due to a number of uncertainties regarding

the proper tax treatment of the worthlessness loss, no portion of the tax benefit related to TXU Corp.'s 2002 write-off of its investment in TXU Europe was recognized in income prior to 2004.

In June 2004, the IRS issued a preliminary notice of proposed adjustment proposing to disallow the 2002 worthlessness deduction and treat the worthlessness as a capital loss (deductible only against capital gains). In addition, in 2004 TXU Corp. revised the estimates of capital losses and ordinary deductions expected from the worthlessness deduction utilization. Accordingly, in 2004 TXU Corp. recorded a tax benefit of \$755 million related to the TXU Europe worthlessness deduction, which reflects expected utilization of the capital loss deduction against capital gains realized in 2004 and prior periods. The benefit recognized also included \$220 million for deductions related to the write-off of the investment in TXU Europe expected to be sustained as ordinary as a result of the preliminary notice.

Benefits arising from the resolution of uncertainty regarding utilization of deductions in the year the TXU Europe investment was written-off or in a prior year have been reported in discontinued operations. Additional such benefits arising from subsequent sales of businesses classified as discontinued operations have also been reported in discontinued operations. Accordingly, of the total \$755 million benefit recognized in 2004, \$680 million was reported in discontinued operations. The remaining \$75 million reported in continuing operations relates to the capital gain arising from the sale of the assets of TXU Fuel, the historical operations of which have been classified as continuing operations. Additional tax benefits may be recognized in the future upon final resolution with the IRS of all matters related to the TXU Europe worthlessness deduction or identification of applicable tax planning strategies.

See Note 18 for discussion of income tax contingencies related to TXU Europe and other matters.

Litigation

During the second quarter of 2004, management assessed the progress and status of matters in litigation, and in anticipation of resolution, an accrual of \$100 million (\$65 million after-tax) was recorded. In January 2005, TXU Corp. reached a comprehensive settlement regarding the consolidated amended securities class action lawsuit initially filed in October 2002. The agreement included a one-time payment to the class members of \$150 million, of which \$66 million in reimbursement from insurance carriers has been agreed upon. As a result, the previously recorded expense accrual was reduced by \$16 million (\$10 million after-tax) in the fourth quarter of 2004. The settlement is contingent upon final court approval.

Potential Claims Related to TXU Europe

In January 2005, TXU Corp. executed a comprehensive agreement resolving potential claims relating to TXU Europe. Results from discontinued operations in 2004 include an accrual of \$220 million (\$143 million after-tax) for an expected payment of that amount under the terms of the agreement. A substantial portion of the payment may be recovered from insurance carriers. The agreement is contingent upon creditor approval and the receipt of formal releases.

Rate Case Settlement

In the fourth quarter of 2004, TXU Electric Delivery recorded a \$21 million (\$14 million after-tax) charge for estimated settlement payments. The settlement, which was finalized February 22, 2005, is the result of a number of municipalities initiating an inquiry regarding distribution rates. The agreement avoids any immediate rate actions, but would require TXU Electric Delivery to file a rate case in 2006, based on a 2005 test year, unless the municipalities and TXU Electric Delivery mutually agree that such a filing is unnecessary. The final settlement amounts are being determined; however, TXU Electric Delivery believes the total will closely approximate the amount accrued.

2. SIGNIFICANT ACCOUNTING POLICIES AND CHANGES IN ACCOUNTING STANDARDS

Basis of Presentation — The consolidated financial statements of TXU Corp. have been prepared in accordance with accounting principles generally accepted in the US and on the same basis as the audited financial statements included in its 2003 Form 8-K, except for changes in estimates of depreciable lives of assets and the early adoption of SFAS 123R as discussed below. In the opinion of management, all other adjustments (consisting of normal recurring accruals) necessary for a fair presentation of the results of operations and financial position have been included therein. The financial statements reflect reclassification of prior period amounts to conform to the current period presentation. All intercompany items and transactions have been eliminated in consolidation. All dollar amounts in the financial statements and tables in the notes are stated in millions of US dollars unless otherwise indicated.

Use of Estimates — The preparation of TXU Corp.'s financial statements requires management to make estimates and assumptions about future events that affect the reporting of assets and liabilities at the balance sheet dates and the reported amounts of revenue and expense, including mark-to-market valuation adjustments. In the event estimates and/or assumptions prove to be different from actual amounts, adjustments are made in subsequent periods to reflect more current information. No material adjustments, other than those disclosed elsewhere herein, were made to previous estimates or assumptions during the current year.

Earnings Per Share — Basic earnings per share available to common shareholders are based on the weighted average number of common shares outstanding during the year. Diluted earnings per share include the effect of all potential issuances of common shares under terms of certain debt and other securities and share compensation arrangements. In 2004, results from continuing operations before extraordinary items and cumulative effect of changes in accounting principles, net of the exchangeable preferred membership buyback premium (\$849 million) and preference stock dividends, represented a loss. Consequently, consideration of potential common share issuances results in antidilution, and basic earnings per share is equal to diluted earnings per share.

The exchangeable preferred membership interests, which were repurchased in April 2004, were convertible to 57 million shares of common stock based on an exercise price of \$13.1242 per share. For 2003, the securities were dilutive resulting in addition of 57 million shares to diluted average shares, and earnings available for common stock were increased by \$53 million for purposes of computing diluted earnings per share. For 2002, these securities were antidilutive.

Financial Instruments and Mark-to-Market Accounting — TXU Corp. enters into financial instruments, including options, swaps, futures, forwards and other contractual commitments primarily to manage commodity prices and interest rate risks. In accordance with SFAS 133, the fair value of each derivative is recognized on the balance sheet and changes in the fair value recognized in earnings. This recognition is referred to as "mark-to-market" accounting. However, if certain criteria are met, TXU Corp. may elect the normal purchase and sale exception or may designate the derivative as a cash flow or fair value hedge. As these elections can reduce the volatility in earnings resulting from fluctuations in fair value, results of operations could be materially affected by such elections. A cash flow hedge mitigates the risk associated with variable future cash flows (e.g., a future sale at market prices), while a fair value hedge mitigates risk associated with fixed future cash flows (e.g., debt with fixed interest rate payments).

In accounting for cash flow hedges, derivative assets and liabilities are recorded on the balance sheet at fair value with an offset in other comprehensive income. Amounts remain in other comprehensive income, provided the underlying transactions remain probable of occurring, and are reclassified into earnings as the underlying transactions occur. Fair value hedges are recorded as derivative assets or liabilities with an offset to the carrying value of the related asset or liability. Any ineffectiveness associated with the hedges is recorded in earnings. TXU Corp. did not recognize any ineffectiveness related to fair value hedges in 2004.

Revenue Recognition — TXU Corp. records revenue from electricity sales and delivery service under the accrual method. Revenues are recognized when power or delivery is provided to customers on the basis of periodic cycle meter readings and include an estimated accrual for the value provided from the meter reading

date to the end of the period. The unbilled revenue is calculated at the end of the period based on estimated daily consumption after the meter read date to the end of the period. For retail electric sales, estimated daily consumption is derived using historical customer profiles adjusted for weather and other measurable factors affecting consumption.

Realized and unrealized gains and losses from transacting in energy-related contracts, principally for the purpose of hedging margins on sales of energy, are reported as a component of revenues.

Accounting for Contingencies — The financial results of TXU Corp. may be affected by judgments and estimates related to loss contingencies. Accruals for loss contingencies are recorded when management determines that it is probable that an asset has been impaired or a liability has been incurred and that such economic loss can be reasonably estimated. Such determinations are subject to interpretations of current facts and circumstances, forecasts of future events and estimates of the financial impacts of such events.

Regulatory Assets and Liabilities — The financial statements of TXU Corp.'s regulated electricity delivery operations reflect regulatory assets and liabilities under cost-based rate regulation in accordance with SFAS 71. The assumptions and judgments used by regulatory authorities continue to have an impact on the recovery of costs, the rate earned on invested capital and the timing and amount of assets to be recovered by rates. (See discussion in Note 17).

See Note 5 for a discussion of the extraordinary gain recorded in 2004 and the extraordinary loss recorded in 2002 related to the adjustments in the carrying value of TXU Corp.'s regulatory asset subject to securitization.

Investments — Deposits in a nuclear decommissioning trust fund are accounted for as trading securities and are therefore carried at fair value in the balance sheet. Investments in unconsolidated business entities over which TXU Corp. has significant influence but does not maintain effective control, generally representing ownership of at least 20% and not more than 50% of common equity, are accounted for under the equity method. Assets related to employee benefit plans are held to satisfy deferred compensation liabilities and are recorded at market value. (See Note 6 – Investments).

Property, Plant and Equipment — Properties are stated at original cost. The cost of property additions includes direct labor and materials and applicable overhead, including payroll-related costs.

Depreciation of TXU Corp.'s property, plant and equipment is calculated on a straight-line basis over the estimated service lives of the properties. Depreciation includes the effect of asset retirement obligations as prescribed by SFAS 143 (see Note 3). As is common in the industry, TXU Corp. records depreciation expense using composite depreciation rates that reflect blended estimates of the lives of major asset components as compared to depreciation expense calculated on an asset-by-asset basis. Consolidated depreciation expense as a percent of average depreciable property approximated 2.3% for 2004, 2.5% for 2003 and 2.7% for 2002.

Effective January 1, 2004, the estimates of depreciable lives of lignite-fired generation facilities were extended an average of nine years to better reflect the useful lives of the assets, and depreciation rates for the Comanche Peak nuclear generating plant were decreased as a result of an increase in the estimated lives of boiler and turbine generator components of the plant by an average of five years. The net impact of these changes was a reduction in depreciation expense of \$44 million (\$29 million after-tax, or \$0.10 per share) in 2004.

Effective April 1, 2003, the estimates of the depreciable lives of the Comanche Peak nuclear generating plant and several gas generation plants were extended to better reflect the useful lives of the assets. At the same time, depreciation rates were increased on lignite and gas generation facilities to reflect investments in emissions control equipment. The net impact of these changes was a reduction in depreciation expense of an additional \$12 million (\$8 million after-tax, or \$0.03 per share) in 2004 and \$37 million (\$24 million after-tax, or \$0.06 per share) in 2003.

Allowance For Funds Used During Construction (AFUDC) and Interest Capitalized — AFUDC is a cost accounting procedure whereby amounts based upon interest charges on borrowed funds and a return on equity capital used to finance construction are added to utility plant and equipment being constructed. As a result of the

1999 Restructuring Legislation, only interest has been capitalized related to generation construction since 1999. AFUDC for the regulated business is capitalized as a component of projects under construction. Interest on qualifying projects for businesses that are not regulated is capitalized in accordance with SFAS 34. The equity portion of capitalized AFUDC is accounted for as other income. See Note 20 for details of amounts.

Impairment of Long-Lived Assets — TXU Corp. evaluates long-lived assets for impairment whenever indications of impairment exist, in accordance with the requirement of SFAS 144. The determination of the existence of indications of impairment involves judgments that are subjective in nature and may require the use of estimates in forecasting future results and cash flows related to an asset or group of assets.

In 2002, TXU Corp. recorded an impairment charge of \$237 million (\$154 million after-tax), reported in other deductions, for the writedown of two generation plant construction projects as a result of weaker wholesale electricity market conditions and reduced planned developmental capital spending. Fair value was determined based on appraisals of property and equipment.

Major Maintenance — Major maintenance outage costs related to nuclear fuel reloads, as well as the costs of other major maintenance programs, are charged to expense as incurred.

Amortization of Nuclear Fuel — The amortization of nuclear fuel in the reactors is calculated on the units-of-production method and is included in cost of energy sold.

Defined Benefit Pension Plans and Other Postretirement Benefit Plans — TXU Corp. offers pension benefits through either a defined benefit pension plan or a cash balance plan and also offers certain health care and life insurance benefits to eligible employees and their eligible dependents upon the retirement of such employees from TXU Corp. Reported costs of providing noncontributory defined pension benefits and other postretirement benefits are dependent upon numerous factors, assumptions and estimates. (See Note 14 for information regarding retirement plans and other postretirement benefits).

Franchise and Revenue-Based Taxes — Franchise and revenue-based taxes such as gross receipt taxes are not a “pass through” item such as sales and excise taxes. Gross receipts taxes are assessed to TXU Corp. by state and local governmental bodies, primarily based on revenues, as a cost of doing business. TXU Corp. records gross receipts tax as an expense. Rates charged to customers by TXU Corp. are intended to recover the taxes, but TXU Corp. is not acting as an agent to collect the taxes from customers.

Income Taxes — TXU Corp. files a consolidated federal income tax return, and federal income taxes are allocated to subsidiaries based on their respective taxable income or loss. Investment tax credits are amortized to income over the estimated lives of the properties. Deferred income taxes are provided for temporary differences between the book and tax basis of assets and liabilities. Certain provisions of SFAS 109 provide that regulated enterprises are permitted to recognize deferred taxes as regulatory tax assets or tax liabilities if it is probable that such amounts will be recovered from, or returned to, customers in future rates.

Cash Equivalents — For purposes of reporting cash and cash equivalents, temporary cash investments purchased with a remaining maturity of three months or less are considered to be cash equivalents.

Changes in Accounting Standards — SFAS 123R was issued in December 2004. SFAS 123R is a revision of SFAS 123 and supersedes APB 25. TXU Corp. grants awards of restricted stock and performance units paid in stock and early adopted SFAS 123R in determining reported expenses for these awards in 2004. See Note 12 for additional discussion.

FIN 46R was issued in December 2003 and was effective January 1, 2004, and replaced FIN 46, which was issued in January 2003. FIN 46R expands and clarifies the guidance originally contained in FIN 46, regarding consolidation of variable interest entities. FIN 46R did not impact results of operations or financial position for 2004.

In October 2002, the EITF, through EITF 02-3, rescinded EITF 98-10, which required mark-to-market accounting for all trading activities. SFAS 143, regarding asset retirement obligations, became effective on

January 1, 2003. As a result of the implementation of these two accounting standards, TXU Corp. recorded a cumulative effect of changes in accounting principles as of January 1, 2003. See Note 3 for additional discussion.

As a result of guidance provided in EITF 02-3, in 2003 TXU Corp. discontinued recognizing origination gains on energy contracts. For 2002, TXU Corp. recognized \$40 million in origination gains on retail sales contracts. Because of the short-term nature of these contracts, a portion of these gains would have been recognized on a settlement basis in 2002.

3. CUMULATIVE EFFECT OF CHANGES IN ACCOUNTING PRINCIPLES

SFAS 123R was issued in December 2004. TXU Corp. early adopted SFAS 123R effective October 1, 2004 and recorded a cumulative effect of change in accounting principle of \$10 million after-tax. See Note 12 for additional discussion.

The following summarizes the effect on results for 2003 for changes in accounting principles effective January 1, 2003:

Charge from rescission of EITF 98-10, net of tax effect of \$34 million	\$ (63)
Credit from adoption of SFAS 143, net of tax effect of \$3 million	<u>5</u>
Total net charge.....	<u>\$ (58)</u>

On October 25, 2002, the EITF, through EITF 02-3, rescinded EITF 98-10, which required mark-to-market accounting for all trading activities. Pursuant to this rescission, only financial instruments that are derivatives under SFAS 133 are subject to mark-to-market accounting. Financial instruments that may not be derivatives under SFAS 133, but were marked-to-market under EITF 98-10, consist primarily of gas transportation and storage agreements, power tolling, full requirements and capacity contracts. This new accounting rule was effective for new contracts entered into after October 25, 2002. Nonderivative contracts entered into prior to October 26, 2002, continued to be accounted for at fair value through December 31, 2002; however, effective January 1, 2003, such contracts were required to be accounted for on a settlement basis. Accordingly, a charge of \$97 million (\$63 million after-tax) was reported as a cumulative effect of a change in accounting principles in the first quarter of 2003. Of the total, \$75 million reduced net commodity contract assets and liabilities and \$22 million reduced inventory that had previously been marked-to-market as a trading position. The cumulative effect adjustment represents the net gains previously recognized for these contracts under mark-to-market accounting.

SFAS 143 became effective on January 1, 2003. SFAS 143 requires entities to record the fair value of a legal liability for an asset retirement obligation in the period of its inception. For TXU Corp., such liabilities primarily relate to nuclear generation plant decommissioning, land reclamation related to lignite mining and removal of lignite plant ash treatment facilities. The liability is recorded at its net present value with a corresponding increase in the carrying value of the related long-lived asset. The liability is accreted each period, representing the time value of money, and the capitalized cost is depreciated over the remaining useful life of the related asset.

As the new accounting rule required retrospective application to the inception of the liability, the effects of the adoption reflect the accretion and depreciation from the liability inception date through December 31, 2002. Further, the effects of adoption take into consideration liabilities of \$215 million (previously reflected in accumulated depreciation) TXU Corp. had previously recorded as depreciation expense and \$26 million (reflected in other noncurrent liabilities) of unrealized net gains associated with the decommissioning trusts.

The following table summarizes the impact as of January 1, 2003 of adopting SFAS 143:

Increase in property, plant and equipment – net	\$ 488
Increase in other noncurrent liabilities and deferred credits	(528)
Increase in accumulated deferred income taxes	(3)
Increase in regulatory assets - net.....	<u>48</u>
Cumulative effect of change in accounting principles	<u>\$ 5</u>

The asset retirement liability at December 31, 2004 was \$631 million, comprised of a \$599 million liability as of December 31, 2003, \$39 million of accretion during the twelve months of 2004, reduced by \$26 million in reclamation payments. The asset retirement obligations were adjusted upward by \$19 million due to revisions in estimated cash flows.

With respect to nuclear decommissioning costs, TXU Corp. believes that the adoption of SFAS 143 results primarily in timing differences in the recognition of asset retirement costs that TXU Corp. is currently recovering through the regulatory process.

On a pro forma basis, assuming SFAS 143 had been adopted at the beginning of the year, earnings for 2002 would have increased by \$6.5 million after-tax, and the liability for asset retirement obligations as of December 31, 2002 would have been \$554 million.

4. DISCONTINUED OPERATIONS

The following summarizes the financial information of the various businesses reported as discontinued operations:

	TXU Gas	TXU Australia	Strategic Retail Services	Pedrick- town	Telecom	Mexico	Europe	Total
2004								
Operating revenues	\$ 911	\$ 835	\$ 17	\$ 32	\$ 54	\$ 4	\$ —	\$ 1,853
Operating costs and expenses	898	666	20	37	49	4	—	1,674
Other deductions (income) — net.....	101	2	10	—	16	—	5	134
Interest income	(9)	(2)	(1)	—	(5)	—	—	(17)
Interest expense and related charges...	37	96	—	—	19	—	—	152
Operating income (loss) before income taxes	(116)	73	(12)	(5)	(25)	—	(5)	(90)
Income tax expense (benefit)	(27)	25	(4)	(2)	(8)	(1)	(2)	(19)
Credits (charges) related to exit (after-tax)	(193)	129	(6)	(17)	1	(2)	(143)	(231)
Recognition of tax benefits	—	—	—	—	—	—	—	680
Income (loss) from discontinued operations	<u>\$ (282)</u>	<u>\$ 177</u>	<u>\$ (14)</u>	<u>\$ (20)</u>	<u>\$ (16)</u>	<u>\$ (1)</u>	<u>\$ (146)</u>	<u>\$ 378</u>
2003								
Operating revenues	\$1,344	\$1,103	\$ 60	\$ 22	\$ 162	\$ 95	\$ —	\$ 2,786
Operating costs and expenses	1,227	819	60	28	146	97	—	2,377
Other deductions (income) — net.....	(1)	(19)	11	—	15	(3)	5	8
Interest income	(2)	(6)	(1)	—	(6)	—	—	(15)
Interest expense and related charges...	40	150	1	—	61	1	—	253
Operating income (loss) before income taxes	80	159	(11)	(6)	(54)	—	(5)	163
Income tax expense (benefit)	26	38	(4)	(2)	(11)	—	(1)	46
Charges related to exit (after-tax)	—	—	(9)	—	(34)	—	—	(43)
Income (loss) from discontinued operations	<u>\$ 54</u>	<u>\$ 121</u>	<u>\$ (16)</u>	<u>\$ (4)</u>	<u>\$ (77)</u>	<u>\$ —</u>	<u>\$ (4)</u>	<u>\$ 74</u>
2002 (a)								
Operating revenues	\$ 980	\$ 860	\$ 47	\$ 18	\$ —	\$ 91	\$ 4,052	\$ 6,048
Operating costs and expenses	886	634	122	21	—	96	3,852	5,611
Other deductions (income) — net.....	29	—	—	—	—	(5)	6	30
Interest income	2	(1)	—	—	—	(1)	(15)	(15)
Interest expense and related charges...	61	128	1	—	—	1	255	446
Operating income (loss) before income taxes	2	99	(76)	(3)	—	—	(46)	(24)
Income tax expense (benefit)	1	21	(27)	(1)	—	(1)	(38)	(45)
Charges related to exit (after-tax)	—	—	—	—	—	(15)	(4,187)	(4,202)
Income (loss) from discontinued operations	<u>\$ 1</u>	<u>\$ 78</u>	<u>\$ (49)</u>	<u>\$ (2)</u>	<u>\$ —</u>	<u>\$ (14)</u>	<u>\$ (4,195)</u>	<u>\$ (4,181)</u>

(a) TXU Europe operations are through September 30, 2002.

The TXU Europe business and the TXU Australia business were previously reported in the International segment and the TXU Australia business was subsequently reported in its own segment. The TXU Gas business was previously reported in the Energy Delivery (now TXU Electric Delivery) segment. The Pedricktown business and the strategic retail services operations were previously reported in the TXU Energy Holdings segment. The telecommunications and Mexico operations were previously reported in corporate and other activities.

Recognition of Tax Benefits – As discussed in Note 1, in connection with an IRS preliminary notice of proposed adjustment issued in June 2004, TXU Corp. has recognized income tax benefits arising from the utilization of the previously unrecognized 2002 worthlessness deduction related to the write-off of the investment in TXU Europe. The \$680 million of tax benefits recognized in discontinued operations relate

primarily to capital gains generated in prior years as well as the capital gains arising from the sales of TXU Communications, TXU Australia, and TXU Gas, which can be offset by the 2002 worthlessness deduction.

TXU Europe – In January 2005, TXU Corp. completed a comprehensive settlement agreement resolving potential claims relating to TXU Europe and its affiliates and major creditor groups. The settlement agreement, under which TXU Corp. denies any liability, consists of a one-time payment to TXU Europe of \$220 million (\$143 million after-tax), which will be distributed to creditors. The settlement agreement is contingent upon creditor approval and the formal delivery to TXU Corp. of releases from existing or potential claims. A majority of creditors have already confirmed their approval. The process is expected to be completed in the second quarter of 2005.

TXU Australia – In July 2004, TXU Corp. completed the sale of TXU Australia to Singapore Power Ltd. for \$1.9 billion in cash and \$1.7 billion in assumed debt, and recorded a gain on sale of \$371 million (\$241 million after-tax). TXU Australia's operations consisted of a portfolio of competitive and regulated businesses, principally in Victoria and South Australia.

Results of TXU Australia for 2004 include an income tax charge of \$112 million to establish a deferred tax liability for the excess of TXU Corp.'s carrying value of the investment in the business over the related tax basis, in accordance with accounting rules, as a result of the decision to sell the business.

TXU Gas – In October 2004, Atmos Energy Corporation and TXU Gas completed a merger by division, which resulted in the disposition of the operations of TXU Gas for \$1.9 billion in cash. TXU Gas was largely a regulated business engaged in the purchase, transmission, distribution and retail sale of natural gas. Charges related to the sale, recorded as a reduction of goodwill, totaled \$108 million (\$193 million after-tax). This amount includes the effect of \$19 million in discontinued depreciation expense in accordance with accounting rules for assets held for sale, as well as \$30 million associated with an income tax matter as discussed in the following paragraph.

In June 2004, the IRS Appeals Office rejected TXU Gas' appeal of proposed adjustments to 1993 income tax returns of ENSERCH Corporation, the acquired predecessor of TXU Gas. Additional reserves deemed required by TXU Gas for this matter totaled \$47 million, and in accordance with acquisition accounting rules, \$17 million was recorded as income tax expense in the second quarter of 2004 and \$30 million was recorded as additional goodwill.

Results of TXU Gas for 2004 reflect an after-tax charge of \$99 million in the second quarter to reserve for disallowed regulatory and other assets pursuant to a May 2004 regulatory ruling in connection with a system-wide distribution rate case.

Pedricktown – In the second quarter of 2004, TXU Energy Holdings initiated a plan to sell the Pedricktown, New Jersey 122 MW power production facility and exit the related power supply and gas transportation agreements. Accordingly, results for the second quarter of 2004 included a \$17 million after-tax charge to write down the facility to estimated fair market value.

Telecommunications — In April 2004, TXU Corp. sold its telecommunications business for \$524 million in cash and \$3 million of assumed debt. The business was formerly a joint venture and was consolidated from March 1, 2003 through the sale date. In 2004, TXU Corp. redeemed \$576 million of debt reported in liabilities of telecommunications holding company at December 31, 2003, and also redeemed \$91 million of its debt held in a trust reported in assets of telecommunications holding company at December 31, 2003.

Strategic Retail Services — In December 2003, TXU Energy Holdings finalized a formal plan to sell its strategic retail services business, which was engaged principally in providing energy management services. Results in 2004 reflect a \$9 million (\$6 million after-tax) charge recorded in the second quarter to settle a contract dispute. Substantially all disposition activities have been completed.

Mexico — In January 2004, TXU Corp. completed the sale of its majority-owned gas distribution operations in Mexico for \$11 million in notes receivable and recorded an after-tax loss of \$2 million.

Balance sheet — The following details the assets and liabilities held for sale as of December 31, 2004:

	December 31, 2004		
	Pedrick- town	Other	Total
Current assets	\$ 2	\$ 7	\$ 9
Property, plant and equipment	15	—	15
Assets held for sale	<u>\$ 17</u>	<u>\$ 7</u>	<u>\$ 24</u>
Current liabilities	\$ 3	\$ —	\$ 3
Noncurrent liabilities	3	—	3
Liabilities held for sale	<u>\$ 6</u>	<u>\$ —</u>	<u>\$ 6</u>

5. EXTRAORDINARY ITEMS

The Settlement Plan addressed the issuance of securitization bonds to recover regulatory asset stranded costs and other qualified costs. A financing order finalized in January 2003 authorized the issuance of securitization bonds by TXU Electric Delivery with a principal amount of \$1.3 billion. An extraordinary gain of \$16 million (net of tax of \$9 million) recorded by TXU Electric Delivery in the second quarter of 2004 represents an increase in the carrying value of the regulatory asset subject to securitization. The second and final tranche of the securitization bonds was issued in June 2004. The increase in the related regulatory asset is due to the effect of higher interest rates than previously estimated on the bonds and therefore increased amounts to be recovered from REPs through revenues as a transition charge to service the principal and interest of the bonds. In the fourth quarter of 2002, TXU Electric Delivery recorded an extraordinary loss of \$134 million (net of income tax benefit of \$72 million) principally to write down the regulatory asset to reflect lower interest rates than originally assumed. The balance of the regulatory asset was \$1.6 billion at December 31, 2004.

6. INVESTMENTS

The following information is a summary of the investment balance as of December 31, 2004 and 2003:

	December 31,	
	2004	2003
Nuclear decommissioning trust	\$ 361	\$ 323
Land	84	89
Assets related to deferred compensation plans	155	150
Note receivable from Capgemini	25	—
Investment in Capgemini	3	—
Various equity method investments	—	2
Common equity investments in subsidiary trusts (see Note 10)	—	30
Other notes receivable	11	3
Miscellaneous other	25	35
Total investments	<u>\$ 664</u>	<u>\$ 632</u>

Nuclear Decommissioning Trust — Deposits in a trust fund for costs to decommission the Comanche Peak nuclear-powered generation plant are carried at fair value. Decommissioning costs are being recovered from TXU Electric Delivery's customers as a transmission and distribution charge over the life of the plant and deposited in the trust fund. Gains and losses on investments in the trust fund are offset by corresponding adjustments to regulatory assets and liabilities. A summary of investments in the fund as of December 31, 2004 and 2003 follows:

	December 31, 2004			
	Cost	Unrealized gain	Unrealized (loss)	Fair market value
Debt securities	\$ 142	\$ 7	\$ (1)	\$ 148
Equity securities	143	82	(12)	213
	<u>\$ 285</u>	<u>\$ 89</u>	<u>\$ (13)</u>	<u>\$ 361</u>

	December 31, 2003			
	Cost	Unrealized gain	Unrealized (loss)	Fair market value
Debt securities	\$ 139	\$ 6	\$ (2)	\$ 143
Equity securities	126	66	(12)	180
	<u>\$ 265</u>	<u>\$ 72</u>	<u>\$ (14)</u>	<u>\$ 323</u>

Debt securities held at December 31, 2004 mature as follows: \$62 million in one to five years, \$52 million in five to ten years and \$34 million after ten years.

Assets Related to Deferred Compensation Plans — The majority of these assets represent cash surrender values of life insurance policies that are purchased to fund liabilities under deferred compensation plans. TXU Corp. pays the premiums and is the beneficiary of these life insurance policies. As of December 31, 2004 and 2003, the face amount of these policies was \$504 million and \$533 million, and the net cash surrender values were \$134 million and \$116 million, respectively. Changes in cash surrender value are netted against premiums paid. Other investment assets held to satisfy deferred compensation liabilities are recorded at market value.

7. SHORT-TERM FINANCING

Short-term Borrowings — At December 31, 2004, TXU Corp. had outstanding short-term borrowings consisting of bank borrowings of \$210 million at a weighted average interest rate of 5.25%. At December 31, 2003, TXU Corp. had no outstanding short-term borrowings.

Credit Facilities — At December 31, 2004, TXU Corp. had access to credit facilities (some of which provide for long-term borrowings) as follows:

Facility	Maturity Date	Authorized Borrowers	At December 31, 2004			
			Facility Limit	Letters of Credit	Cash Borrowings	Availability
364-day Credit Facility	June 2005	TXU Energy Holdings, TXU Electric Delivery	\$ 600	\$ 75	\$ —	\$ 525
Three-Year Revolving Credit Facility	June 2007	TXU Energy Holdings, TXU Electric Delivery	1,400	18	210	1,172
Five-Year Revolving Credit Facility	December 2005	TXU Corp.	425	419	—	6
Five-Year Revolving Credit Facility	June 2009	TXU Energy Holdings, TXU Electric Delivery	500	—	—	500
Five-Year Revolving Credit Facility	December 2009	TXU Energy Holdings	500	—	—	500
Total			\$ 3,425	\$ 512	\$ 210	\$ 2,703

In December 2004, TXU Corp. amended its \$500 million five-year revolving credit facility with LOC 2003 Trust, a special purpose, wholly-owned subsidiary of TXU Corp. (LOC Trust). The amendment reduced the facility limit to \$425 million. LOC Trust, in turn, amended its \$500 million five-year revolving credit facility with the group of lenders, reducing the credit facility to \$425 million and terminating the LOC Trust capitalization requirement. Amounts repaid under the Facility cannot be reborrowed and the amount and maturity of any outstanding letter of credit cannot be increased or extended. The maturity of the Facility was modified from July 15, 2008 to December 31, 2005. These amendments resulted in the return of the \$525

million cash collateral to TXU Corp. that was previously reflected on TXU Corp.'s balance sheet as restricted cash. LOC Trust is included in the consolidated financial statements of TXU Corp. to comply with US GAAP.

In November 2004, TXU Energy Holdings entered into a five-year revolving credit facility that allows for revolving loans and letters of credit. Letters of credit may total up to \$500 million. Revolving loans may total up to \$250 million. The aggregate amount of borrowings outstanding at any one time may not exceed \$500 million. TXU Energy Holdings intends to use this facility for general and corporate purposes, including, in the case of letters of credit, support for pollution control revenue bonds.

In June 2004, US Holdings, TXU Energy Holdings and TXU Electric Delivery replaced \$2.25 billion of credit facilities scheduled to mature in 2005 with \$2.5 billion of credit facilities for TXU Energy Holdings and TXU Electric Delivery maturing in June 2005, 2007 and 2009. These facilities are used for working capital and general corporate purposes and provide back-up for any future issuances of commercial paper by TXU Energy Holdings or TXU Electric Delivery. At December 31, 2004, there was no such commercial paper outstanding.

Sale of Receivables — TXU Corp. has established an accounts receivable securitization program. The activity under this program is accounted for as a sale of accounts receivable in accordance with SFAS 140. Under the program, subsidiaries of TXU Corp. (originators) sell trade accounts receivable to TXU Receivables Company, a consolidated wholly-owned bankruptcy remote direct subsidiary of TXU Corp., which sells undivided interests in the purchased accounts receivable for cash to special purpose entities established by financial institutions (the funding entities). Funding under the program as of December 31, 2004 was \$474 million.

Effective June 30, 2004, the program was extended through June 28, 2005. As part of the extension, the maximum amount available under the program was increased from \$600 million to \$700 million in recognition of seasonal power sales. Additionally, the extension allows for increased availability of funding through a credit ratings-based reduction (based on each originator's credit rating) of customer deposits previously used to reduce the amount of undivided interests that could be sold. Undivided interests will now be reduced by 100% of the customer deposits for a Baa3/BBB- rating; 50% for a Baa2/BBB rating; and zero % for a Baa1/BBB+ and above rating. Effective as of August 31, 2004, TXU Corp. amended the program in order to consummate the TXU Gas transaction. As a result, TXU Receivables Company repurchased from the funding entities the receivables related to TXU Gas, as an originator, and subsequently assigned those receivables back to TXU Gas, terminating TXU Gas' participation in the receivables program.

All new trade receivables under the program generated by the originators are continuously purchased by TXU Receivables Company with the proceeds from collections of receivables previously purchased. Changes in the amount of funding under the program, through changes in the amount of undivided interests sold by TXU Receivables Company, are generally due to seasonal variations in the level of accounts receivable and changes in collection trends. TXU Receivables Company has issued subordinated notes payable to the originators for the difference between the face amount of the uncollected accounts receivable purchased, less a discount, and cash paid to the originators that was funded by the sale of the undivided interests. The balance of the subordinated notes payable was \$337 million at December 31, 2004 and \$511 million at December 31, 2003.

The discount from face amount on the purchase of receivables principally funds program fees paid by TXU Receivables Company to the funding entities, as well as a servicing fee paid by TXU Receivables Company to TXU Business Services, a direct subsidiary of TXU Corp. The program fees (losses on sale), which consist primarily of interest costs on the underlying financing, were approximately \$12 million in both 2004 and 2003 and \$22 million in 2002 and approximated 2.1%, 2.4% and 3.7% in 2004, 2003 and 2002, respectively, of the average funding under the program on an annualized basis; these fees represent the net incremental costs of the program to the originators and are reported in SG&A expenses. The servicing fee, which totaled approximately \$7 million in both 2004 and 2003 and \$9 million in 2002, compensates TXU Business Services for its services as collection agent, including maintaining the detailed accounts receivable collection records.

The December 31, 2004 balance sheet reflects \$811 million face amount of trade accounts receivable of TXU Energy Holdings and TXU Electric Delivery, reduced by \$474 million of undivided interests sold by TXU Receivables Company. Funding under the program related to continuing operations decreased \$73 million in

2004, increased \$100 million in 2003 and decreased \$15 million in 2002. Funding increases or decreases under the program are reflected as operating cash flow activity in the statement of cash flows. The carrying amount of the retained interests in the accounts receivable approximated fair value due to the short-term nature of the collection period.

Activities of TXU Receivables Company for 2004, 2003 and 2002 were as follows:

	<u>Year Ended December 31,</u>		
	<u>2004</u>	<u>2003</u>	<u>2002</u>
Cash collections on accounts receivable	\$ 8,449	\$ 8,538	\$ 6,778
Face amount of new receivables purchased	(8,149)	(8,143)	(7,491)
Discount from face amount of purchased receivables.....	19	19	31
Program fees paid	(12)	(12)	(22)
Servicing fees paid.....	(7)	(7)	(9)
Increase (decrease) in subordinated notes payable.....	<u>(174)</u>	<u>(524)</u>	<u>742</u>
Operating cash flows used by (provided to) TXU Corp. under the program.....	126	(129)	29
Cash flows related to disposed TXU Gas business	<u>(53)</u>	<u>29</u>	<u>(14)</u>
Cash flows used by (provided to) continuing operations	<u>\$ 73</u>	<u>\$ (100)</u>	<u>\$ 15</u>

Upon termination of the program, cash flows to TXU Corp. would be delayed as collections of sold receivables would be used by TXU Receivables Company to repurchase the undivided interests sold instead of purchasing new receivables. The level of cash flows would normalize in approximately 16 to 31 days.

Contingencies Related to Sale of Receivables Program — Although TXU Receivables Company expects to be able to pay its subordinated notes from the collections of purchased receivables, these notes are subordinated to the undivided interests of the financial institutions in those receivables, and collections might not be sufficient to pay the subordinated notes. The program may be terminated if either of the following events occurs:

- 1) all of the originators cease to maintain their required fixed charge coverage ratio and debt to capital (leverage) ratio;
- 2) the delinquency ratio (delinquent for 31 days) for the sold receivables, the default ratio (delinquent for 91 days or deemed uncollectible), the dilution ratio (reductions for discounts, disputes and other allowances) or the days collection outstanding ratio exceed stated thresholds and the financial institutions do not waive such event of termination. The thresholds apply to the entire portfolio of sold receivables, not separately to the receivables of each originator.

The delinquency and dilution ratios exceeded the relevant thresholds during the first four months of 2003, but waivers were granted. These ratios were affected by issues related to the transition to competition. Certain billing and collection delays arose due to implementation of new systems and processes within TXU Corp. and ERCOT for clearing customers' switching and billing data. Also, strengthened credit and collection policies and practices have brought the ratios into consistent compliance with the program requirements.

Under terms of the receivables sale program, all the originators are required to maintain specified fixed charge coverage and leverage ratios (or supply a parent guarantor that meets the ratio requirements). The failure, by an originator or its parent guarantor, if any, to maintain the specified financial ratios would prevent that originator from selling its accounts receivable under the program. If all the originators and the parent guarantor, if any, fail to maintain the specified financial ratios so that there are no eligible originators, the facility would terminate.

8. LONG-TERM DEBT

Long-term Debt — At December 31, 2004 and 2003, the long-term debt of TXU Corp. consisted of the following:

	December 31, 2004	December 31, 2003
<u>TXU Energy Holdings</u>		
Pollution Control Revenue Bonds:		
Brazos River Authority:		
3.000% Fixed Series 1994A due May 1, 2029, remarketing date May 1, 2005(a)	\$ 39	\$ 39
5.400% Fixed Series 1994B due May 1, 2029, remarketing date May 1, 2006(a)	39	39
5.400% Fixed Series 1995A due April 1, 2030, remarketing date May 1, 2006(a)	50	50
5.050% Fixed Series 1995B due June 1, 2030, remarketing date June 19, 2006(a)	114	118
7.700% Fixed Series 1999A due April 1, 2033	111	111
6.750% Fixed Series 1999B due September 1, 2034, remarketing date April 1, 2013(a)	16	16
7.700% Fixed Series 1999C due March 1, 2032	50	50
4.950% Fixed Series 2001A due October 1, 2030, remarketing date April 1, 2004(a)	—	121
4.750% Fixed Series 2001B due May 1, 2029, remarketing date November 1, 2006(a)	19	19
5.750% Fixed Series 2001C due May 1, 2036, remarketing date November 1, 2011(a)	217	274
2.030% Floating Series 2001D due May 1, 2033 (b)	268	271
2.450% Floating Taxable Series 2001I due December 1, 2036(b)	62	63
2.030% Floating Series 2002A due May 1, 2037(b)	45	61
6.750% Fixed Series 2003A due April 1, 2038, remarketing date April 1, 2013(a)	44	44
6.300% Fixed Series 2003B due July 1, 2032	39	39
6.750% Fixed Series 2003C due October 1, 2038	52	72
5.400% Fixed Series 2003D due October 1, 2029, remarketing date October 1, 2014(a)	31	31
Sabine River Authority of Texas:		
6.450% Fixed Series 2000A due June 1, 2021	51	51
5.500% Fixed Series 2001A due May 1, 2022, remarketing date November 1, 2011(a)	91	91
5.750% Fixed Series 2001B due May 1, 2030, remarketing date November 1, 2011(a)	107	107
5.800% Fixed Series 2003A due July 1, 2022	12	12
6.150% Fixed Series 2003B due August 1, 2022	45	45
Trinity River Authority of Texas:		
6.250% Fixed Series 2000A due May 1, 2028	14	14
5.000% Fixed Series 2001A due May 1, 2027, remarketing date November 1, 2006(a)	37	37
Other:		
6.875% TXU Mining Fixed Senior Notes due August 1, 2005	30	30
6.125% Fixed Senior Notes due March 15, 2008(c)	250	250
7.000% Fixed Senior Notes due March 15, 2013	1,000	1,000
2.838% Floating Rate Senior Notes due January 17, 2006(d)	400	—
Capital lease obligations	9	13
Other	—	8
Fair value adjustments related to interest rate swaps	15	11
Unamortized discount	—	(2)
Total TXU Energy Holdings	3,257	3,085
<u>TXU Electric Delivery</u>		
8.250% Fixed First Mortgage Bonds due April 1, 2004	—	100
6.250% Fixed First Mortgage Bonds due October 1, 2004	—	121
6.750% Fixed First Mortgage Bonds due July 1, 2005	92	92
7.625% Fixed First Mortgage Bonds due July 1, 2025	—	215
7.375% Fixed First Mortgage Bonds due October 1, 2025	—	178
6.375% Fixed Senior Secured Notes due May 1, 2012	700	700
7.000% Fixed Senior Secured Notes due May 1, 2032	500	500
6.375% Fixed Senior Secured Notes due January 15, 2015(c)	500	500
7.250% Fixed Senior Secured Notes due January 15, 2033	350	350
5.000% Fixed Debentures due September 1, 2007(c)	200	200
7.000% Fixed Debentures due September 1, 2022	800	800
Unamortized discount	(19)	(30)
Sub-total	3,123	3,726
TXU Electric Delivery Transition Bond Company LLC(e)		
2.260% Fixed Series 2003 Bonds due in semiannual installments through February 15, 2007	80	103
4.030% Fixed Series 2003 Bonds due in semiannual installments through February 15, 2010	122	122
4.950% Fixed Series 2003 Bonds due in semiannual installments through February 15, 2013	130	130

	December 31, 2004	December 31, 2003
5.420% Fixed Series 2003 Bonds due in semiannual installments through August 15, 2015	145	145
3.520% Fixed Series 2004 Bonds due in semiannual installments through November 15, 2009	270	—
4.810% Fixed Series 2004 Bonds due in semiannual installments through November 15, 2012	221	—
5.290% Fixed Series 2004 Bonds due in semiannual installments through May 15, 2016	290	—
Total TXU Electric Delivery Transition Bond Company LLC	<u>1,258</u>	<u>500</u>
Total TXU Electric Delivery	4,381	4,226
US Holdings		
7.170% Fixed Senior Debentures due August 1, 2007	10	10
9.580% Fixed Notes due in semiannual installments through December 4, 2019	68	70
8.254% Fixed Notes due in quarterly installments through December 31, 2021	64	67
2.494% Floating Rate Junior Subordinated Debentures, Series D due January 30, 2037(d)	1	1
8.175% Fixed Junior Subordinated Debentures, Series E due January 30, 2037	<u>8</u>	<u>8</u>
Total US Holdings	151	156
TXU Gas		
6.375% Fixed Notes due February 1, 2004	—	150
7.125% Fixed Notes due June 15, 2005	—	150
6.564% Fixed Remarketed Reset Notes due January 1, 2008, remarketing date July 1, 2005	—	125
Unamortized valuation adjustment	—	<u>1</u>
Total TXU Gas	—	426
TXU Corp.		
6.375% Fixed Senior Notes Series B due October 1, 2004	—	175
6.375% Fixed Senior Notes Series C due January 1, 2008(c)	200	200
4.050% Fixed Senior Notes Series E due August 16, 2004	—	2
6.375% Fixed Senior Notes Series J due June 15, 2006(c)	683	800
4.446% Fixed Senior Notes Series K due November 16, 2006	50	500
5.450% Fixed Senior Notes Series L due November 16, 2007 remarketing date August 16, 2005(f)	101	500
5.800% Fixed Senior Notes Series M due May 16, 2008 remarketing date February 16, 2006(f)	184	440
4.800% Fixed Senior Notes Series O due November 15, 2009(c)	1,000	—
5.550% Fixed Senior Notes Series P due November 15, 2014	1,000	—
6.500% Fixed Senior Notes Series Q due November 15, 2024(c)	750	—
6.550% Fixed Senior Notes Series R due November 15, 2034	750	—
6.000% Fixed Pinnacle Overfund Trust Debt due semiannually through August 15, 2004(g)	—	91
8.820% Building Financing due semiannually through February 11, 2022	120	130
3.570% Floating Convertible Senior Notes due July 15, 2033(d)	25	525
Fair value adjustments related to interest rate swaps	—	32
Unamortized discount	<u>(11)</u>	<u>(2)</u>
Total TXU Corp.	4,852	3,393
Total TXU Corp. consolidated	12,641	11,286
Less amount due currently	<u>(229)</u>	<u>(678)</u>
Total long-term debt	<u>\$ 12,412</u>	<u>\$ 10,608</u>

- (a) These series are in the multiannual mode and are subject to mandatory tender prior to maturity on the mandatory remarketing date. On such date, the interest rate and interest rate period will be reset for the bonds.
- (b) Interest rates in effect at December 31, 2004. These series are in a weekly rate mode and are classified as long-term as they are supported by long-term irrevocable letters of credit.
- (c) Interest rates swapped to floating on an aggregate \$2.3 billion principal amount.
- (d) Interest rates in effect at December 31, 2004.
- (e) These bonds are nonrecourse to TXU Electric Delivery.
- (f) Equity-linked.
- (g) Offset by trust fund in the same amount reported in assets of telecommunications holding company at December 31, 2003.

Debt Issuances and Retirements in 2004

TXU Corp. has utilized cash proceeds from the sale of TXU Australia, TXU Gas, and TXU Fuel and other asset sales as well as cash provided from operations and lower-cost debt issuances to increase value and reduce risks through an ongoing liability management initiative. The following table summarizes the 2004 issuances:

	Principal Amount
<i>Issuances:</i>	
<u>TXU Corp.</u>	
4.800% Fixed Senior Notes Series O due November 15, 2009.....	\$1,000
5.550% Fixed Senior Notes Series P due November 15, 2014.....	1,000
6.500% Fixed Senior Notes Series Q due November 15, 2024.....	750
6.550% Fixed Senior Notes Series R due November 15, 2034.....	750
<u>TXU Energy Holdings</u>	
2.838% Floating Rate Senior Notes due January 17, 2006 (a) (b).....	800
<u>TXU Electric Delivery</u>	
Securitization bonds.....	<u>790</u>
Total.....	<u><u>\$5,090</u></u>

(a) Interest rates in effect at December 31, 2004.

(b) In December 2004, TXU Energy Holdings repurchased \$400 million of its Floating Rate Senior Notes at par. See Note 1.

During 2004, TXU Electric Delivery issued three classes of securitization (transition) bonds with fixed annual interest rates ranging from 3.52% to 5.29% that require semiannual interest and principal installment payments beginning in November 2004 through specified dates in 2009 through 2016. TXU Electric Delivery used the proceeds to retire two series of mortgage bonds with an aggregate principal amount of \$393 million due in 2025 and repurchase shares of common stock from US Holdings for \$375 million. US Holdings used the proceeds it received to repay short-term borrowings. As a result of the retirement of the two series of mortgage bonds, TXU Electric Delivery has the ability to release the liens on its outstanding senior secured notes, making them rank equally with TXU Electric Delivery's other senior unsecured debt. No decision has been made regarding the release of liens.

During the year ended December 31, 2004, in addition to the amounts repurchased or legally defeased discussed in Note 1, TXU Corp. made scheduled principal payments on long-term debt as follows:

	Principal Amount
TXU Corp.	\$ 187
TXU Gas	150
US Holdings	5
TXU Energy Holdings	13
TXU Electric Delivery	<u>253</u>
Total (a).....	<u><u>\$ 608</u></u>

(a) Excludes \$576 million of debt retired in 2004, reported in liabilities of telecommunications holding company at December 31, 2003.

Fair Value Hedges — TXU Corp. uses fair value hedging strategies to manage its exposure to fixed interest rates on long-term debt. At December 31, 2004, \$2.3 billion of fixed rate debt had been effectively converted to variable rates through interest rate swap transactions, expiring through 2024. These swaps qualified for and have been designated as fair value hedges using the short-cut method of hedge accounting provided by SFAS 133. As such, TXU Corp. assumes that changes in the value of the derivative are exactly offset by changes in the value of the debt; therefore, there is no hedge ineffectiveness recognized.

In 2004, fixed-to-variable swaps related to \$1.7 billion of debt were settled for a gain of \$30 million, which will be amortized to offset interest expense over the remaining life of the related debt.

Leases — In February 2002, TXU Corp. sold its interest in its headquarters building in Dallas, Texas for \$145 million. Simultaneously with the sale of the property, TXU Corp. entered into a twenty-year lease obligation for the property. At the end of the initial twenty-year term of the lease, TXU Corp. has the right, but not the obligation, to renew the lease for three ten-year renewal terms under which rents will be based on then-existing market conditions. The sale was accounted for as a financing and the obligation is reported in long-term debt.

Convertible Senior Notes — At December 31, 2004, TXU Corp. had \$25 million principal amount outstanding of its Floating Rate Convertible Senior Notes due 2033. TXU Corp. originally issued \$525 million of the convertible senior notes in July 2003. During 2004, \$500 million principal amount of the notes were repurchased for \$803 million, resulting in debt extinguishment losses of \$315 million (\$309 million after-tax), which includes \$12 million in unamortized debt expenses, reported in other deductions.

The notes bear regular interest at an annual floating rate equal to 3-month LIBOR, determined quarterly, plus 150 basis points, and are payable in arrears quarterly commencing October 15, 2003. The notes will bear additional contingent interest during periods after July 15, 2008 if the average trading price of the notes for a specified period exceeds 120% of the principal amount of the notes. The conversion rate is subject to adjustments in certain circumstances, and was adjusted in January 2005 as a result of the increase in the dividend payment on January 3, 2005, which reflected the increased annual dividend rate of \$2.25 per share. The notes conversion rate, as adjusted, is 29.1256 shares of TXU Corp. common stock per \$1,000 principal amount of notes, which equates to 742,004 shares at \$34.3341 per share. Should the holders elect to convert the notes, TXU Corp. has the option to settle the conversion in cash, common stock or a combination of both. TXU Corp. intends to settle any future conversion of the remaining \$25 million principal amount of outstanding notes in common stock. The notes are included in diluted earnings per share when the effect of conversion is dilutive.

Equity-Linked Debt Securities — At December 31, 2004, TXU Corp. had outstanding equity-linked debt securities consisting of the following:

Security	Stock Purchase Contract						
	Senior Notes		Contract Adjustment Payment Rate (1)	Price per Share		Number of Shares	
	Principal Amount	Interest Rate (1)		Minimum	Maximum	Minimum	Maximum
Issued 2001:							
Series L due 2007	101	5.450%(2)	3.300%(3)	\$45.64	\$55.68	1,817,414	2,217,326
Issued 2002:							
Series M due 2008	<u>184</u>	5.800%(4)	2.325%(5)	\$51.15	\$62.91	<u>2,926,116</u>	<u>3,599,192</u>
Total	<u>\$ 285</u>					<u>4,743,530</u>	<u>5,816,518</u>

- (1) Rates are annual, payments are quarterly.
- (2) Payable until August 16, 2005, after which the annual interest rate is expected to be reset in a remarketing.
- (3) Applied to the par value of \$25 and payable from November 16, 2004 until November 16, 2005.
- (4) Expected to be remarketed between November 16, 2005 and February 16, 2006, at which time the rate may change.
- (5) Payable until the stock purchase contract settlement date of May 16, 2006.

As a result of its ongoing liability management initiative (see Note 1), TXU Corp. repurchased the following equity-linked debt securities for \$1.116 billion in cash:

	Principal Amount	Debt Extinguishment Losses (Pre-tax)	Credit to Additional Paid- in-Capital (b)
4.446% Fixed Senior Notes Series K due November 16, 2006 (a).....	\$ 450	\$ 23	\$ 38
5.450% Fixed Senior Notes Series L due November 16, 2007.....	399	22	38
5.800% Fixed Senior Notes Series M due May 16, 2008	<u>256</u>	<u>23</u>	<u>20</u>
Total	<u>\$ 1,105</u>	<u>\$ 68</u>	<u>\$ 96</u>

(a) Includes \$238 million repurchased by TXU Corp. in connection with the remarketing of such notes in August 2004.

(b) Includes out-of-the-money value (to holders) of the equity purchase contracts of \$59 million and reversals of previously established contract adjustment payment liabilities of \$37 million.

With the settlement in November 2004 of the stock purchase contracts associated with the Series K, TXU Corp. issued 1,817,371 shares of common stock. The contracts were settled with \$101 million in proceeds from the August 2004 remarketing of the debt.

In August 2002, TXU Corp. issued 8,365,133 shares with the settlement of the stock purchase contracts associated with the Series E securities. The contracts were settled with \$101 million in cash.

Equity-linked debt securities consist of (i) senior notes and (ii) a stock purchase contract that obligates the holder to purchase TXU Corp. common stock on a future settlement date. The number of shares issuable upon settlement of stock purchase contracts represents the stated value of the notes divided by an average of the market price of TXU Corp. common stock immediately preceding the settlement date. The calculation of shares issuable is subject to a minimum price, which is typically the market price of common stock at the time of initial issuance of the equity-linked debt securities, and a maximum price, which includes a premium over the minimum price that was negotiated in connection with the pricing of the offering.

To the extent the market price of TXU Corp. common stock is below the minimum price on the applicable settlement date, holders of equity-linked debt securities would be required to purchase TXU Corp. common stock at a price higher than the market price at that time. To the extent the market price is above the maximum price on the applicable settlement date, holders of equity-linked securities would be allowed to purchase TXU Corp. common stock at a price lower than the market price at that time. The market price of TXU Corp.'s common stock is currently above the maximum price for each series of equity-linked debt securities currently outstanding.

In addition to interest, holders receive contract adjustment payments through the contract settlement dates, which are generally two years prior to maturity of the debt securities. On the contract settlement date, the holder must purchase the common stock at the calculated price, and may elect to participate in a remarketing of the senior notes to fund such purchase, or settle the purchase contract in cash and continue to hold the senior notes. If the remarketing of the senior notes is not successful, the holders have the right to put the notes to TXU Corp. for the calculated number of shares of common stock.

TXU Corp. has the right to defer the contract adjustment payments on these equity-linked debt securities, but any such election would subject TXU Corp. to restriction on the payment of dividends on and redemption of outstanding shares of its common stock. TXU Corp. currently has no plan to defer these contract adjustment payments.

At the time of issuance of the securities, TXU Corp. recorded a liability for the present value of the contract adjustment payments with an offsetting reduction to common stock equity. The total maximum number of shares of TXU Corp. common stock issuable in connection with the stock purchase contracts have been reserved.

Debt Issuances and Retirements in 2003:

In 2003, TXU Corp. and its consolidated subsidiaries (excluding TXU Australia, which is classified as discontinued operations) issued \$2.8 billion of long-term debt including \$1.3 billion of fixed rate senior notes, \$568 million of pollution control revenue bonds, \$525 million of convertible senior notes, and \$500 million of securitization (transition) bonds. TXU Corp. and its consolidated subsidiaries (excluding TXU Australia) retired \$2.2 billion of long-term debt during 2003, including \$770 million of senior notes, \$663 million of first mortgage bonds, \$638 million of pollution control revenue bonds, and \$116 million of other long-term debt.

Maturities — Sinking fund and maturity requirements for long-term debt instruments at December 31, 2004, were as follows:

Year	
2005.....	\$ 229
2006.....	1,242
2007.....	425
2008.....	749
2009.....	1,117
Thereafter.....	8,885
Unamortized premium and discount and fair value adjustments.....	(15)
Capital lease obligations.....	9
Total.....	<u>\$ 12,641</u>

9. PREFERRED SECURITIES OF SUBSIDIARIES

	December 31,	
	2004	2003
Exchangeable preferred membership interests of TXU Energy Holdings, net of \$104 unamortized discount.....	\$ —	\$ 646
Preferred stock of TXU Gas.....	—	75
Preferred stock of US Holdings.....	<u>38</u>	<u>38</u>
Total.....	<u>\$ 38</u>	<u>\$ 759</u>

Exchangeable Preferred Membership Interests of TXU Energy Holdings — In April 2004, TXU Corp. repurchased TXU Energy Holdings' exchangeable preferred membership interests with a liquidation amount of \$750 million for \$1.85 billion (including transaction costs). The excess of the purchase price over the carrying value of the securities, net of \$384 million in income tax benefits recorded as a deferred tax asset, was recorded as a charge to additional paid-in capital in the amount of \$849 million. The carrying value of the securities was \$617 million, which is the liquidation amount of \$750 million net of \$102 million in unamortized discount and \$31 million in unamortized debt issuance costs, both recorded at the time of issuance of the securities in November 2002. The charge to additional paid-in capital is accounted for in a manner similar to TXU Corp.'s preference share dividends, resulting in a reduction in net income available to common shareholders.

Preferred Stock of TXU Gas — All of TXU Gas' preferred stock was redeemed in November 2004 in connection with the TXU Gas transaction. See Note 1 for further discussion.

Preferred Stock of US Holdings — At December 31, 2004 and 2003, US Holdings had 379,231 shares of cumulative, preferred stock without par value outstanding with a total stated value of \$38 million. Dividend rates range from \$4.00 to \$5.08 per share. The preferred stock can be redeemed at prices ranging from \$101.79 per share to \$112.00 per share.

The holders of preferred stock of US Holdings have no voting rights except for changes to the articles of incorporation that would change the rights or preferences of such stock, authorize additional shares of stock or create an equal or superior class of stock. They have the right to vote for the election of directors only if certain dividend arrearages exist.

10. LONG-TERM DEBT HELD BY SUBSIDIARY TRUSTS

Statutory business trusts were established as wholly-owned financing subsidiaries of TXU Corp. and TXU Gas. The assets of the trusts consisted solely of Junior Subordinated Debentures issued by TXU Corp. or TXU Gas, and the trusts issued preferred interests, as presented below:

	Preferred Interests		Trust Assets (Long-Term Debt of TXU Corp. or TXU Gas)	
	December 31, 2004	December 31, 2003	December 31, 2004	December 31, 2003
<u>TXU Corp.</u>				
Capital I Trust (9.2 million units of 7.25% Series due 2029)	\$ —	\$ 223	\$ —	\$ 237
Capital II Trust (6.0 million units of 8.70% Series due 2034)	—	145	—	155
Total.....	—	368	—	392
<u>TXU Gas</u>				
Capital I Trust (150 thousand units of Floating Rate Series due 2028).....	—	147	—	154
Total.....	\$ —	\$ 515	\$ —	\$ 546

TXU Corp. and TXU Gas, as the parent companies, owned the subsidiary trusts' common interests, which are reported in investments in the balance sheet, and each had effectively issued a full and unconditional guarantee of its trusts' preferred interests.

During 2004, TXU Corp. redeemed the 7.25% and 8.70% Series debt securities at par. The trusts used the proceeds to redeem the preferred interests held by investors and the common interests held by TXU Corp.

In October 2004, TXU Gas legally defeased all of the \$154 million principal amount TXU Gas Floating Rate Series debt securities at par, which resulted in the defeasance of the preferred and common interests. See Note 1 regarding the TXU Gas transaction.

11. SHAREHOLDERS' EQUITY

Common Stock Equity — Under Texas law, TXU Corp. may only declare dividends out of its surplus, which is statutorily defined as a company's net assets (i.e. total assets minus total debts) less its stated capital. The write-off in 2002 of TXU Corp.'s investment in TXU Europe in 2002 resulted in negative surplus. In February 2003, TXU Corp. received shareholder approval as permitted under Texas law to reclassify approximately \$8 billion of its stated capital to surplus.

In October 2004, the Board of Directors adopted a revised dividend and cash distribution policy. The new policy sets the dividend on TXU Corp.'s common stock at an annual rate of \$2.25 per share. The Board of Directors declared a regular quarterly dividend of 56.25 cents per share, payable on January 3, 2005 to shareholders of record as of December 3, 2004.

In April 2004, TXU Corp. repurchased TXU Energy Holdings' exchangeable preferred membership interests, as described in Note 9, which resulted in a charge of \$849 million to additional paid-in capital. Additional paid-in capital at December 31, 2003 and 2002 included \$111 million related to the discount at issuance of the securities. The securities were originally issued as exchangeable subordinated notes and were exchanged for preferred membership interests by TXU Energy Holdings in July 2003.

In November 2004, TXU Corp. repurchased 52.5 million shares of its outstanding common stock through an accelerated share repurchase agreement at an initial price of \$64.57 per share for a total of \$3.4 billion. Under the agreement, the broker-dealer counterparty immediately borrows shares that are sold to and canceled by TXU Corp. The counterparty subsequently purchases an equal amount of shares in the open market. TXU Corp.'s purchase price is subject to a future contingent adjustment based on the actual costs of the shares purchased by the counterparty. See Note 18 for further discussion of the contingent purchase price adjustment.

In June 2004, TXU Corp. repurchased and canceled 20 million shares of its outstanding common stock through an accelerated share repurchase agreement at an initial price of \$39.86 per share. In the third quarter of 2004, the broker-dealer that executed the repurchase transaction completed the process of purchasing an equal amount of shares in the open market, and TXU Corp. paid a purchase price adjustment of \$7 million based upon the actual cost of the shares repurchased by such broker-dealer. Including this adjustment, the total purchase price was \$804 million.

During 2004, TXU Corp. repurchased in the open market and canceled 11.8 million shares of its common equity securities for \$489 million. Additional share purchases included 500,000 shares that were deposited in a trust and 1.0 million shares that were distributed to Mr. Wilder, both under terms of his employment agreement. These purchases totaled \$52 million.

Under Texas law, a corporation shall, upon the repurchase and cancellation of its outstanding shares, reduce its stated capital by an amount equal to the amount in stated capital represented by those shares so repurchased and canceled. As such, TXU Corp. reduced its common stock equity balance by an amount equal to \$161 million with the residual amount related to these share repurchases being applied as a reduction to the additional paid-in capital balance in the same amount. The stated amount per share established in February 2005 for future share issuances is \$0.01.

The Thrift Plan is an employee savings plan under which TXU Corp. matches employees' contributions of their earnings with common shares. Also see Note 14 for additional discussion. At December 31, 2004, the Thrift Plan had an obligation of \$229 million outstanding in the form of a note that TXU Corp. had purchased from a third-party lender in 1990 and recorded as a reduction to common equity. The note had been issued in connection with purchases of TXU Corp. common stock on the open market by the Thrift Plan trustee to satisfy future matching requirements. At December 31, 2004, the Thrift Plan trustee held 3,590,204 shares of TXU Corp. common stock. These shares (LESOP shares) are held by the trustee under the leveraged employee stock ownership provision of the Thrift Plan until allocated to Thrift Plan participants when required to meet TXU Corp.'s matching obligations. The Thrift Plan uses dividends on the LESOP shares held and contributions from TXU Corp., if required, to repay interest and principal on the note. TXU Corp. contributed \$26 million in 2004 and \$25 million in 2003, recorded as a charge to earnings, to service the note. Allocations of LESOP shares to participants' accounts increased common stock equity by \$3 million in 2004, \$4 million in 2003 and \$8 million in 2002.

TXU Corp. has a Direct Stock Purchase and Dividend Reinvestment Plan (DRIP) for investors. Issuances of new shares to satisfy purchases by DRIP participants (including reinvestment of dividends) increased common stock by \$4 million in 2004, \$10 million in 2003 and \$40 million in 2002. Since April 2004, share purchases by DRIP participants have been satisfied by purchases in the open market.

At December 31, 2004, authorized but unissued common shares of TXU Corp. were registered with the SEC for new issuance pursuant to the following:

DRIP Plan	2,460,878
Thrift Plan	6,960,428
Long-Term Incentive Compensation Plan	5,166,725
Equity-linked debt securities	6,553,511
Other	<u>717,272</u>
Total	<u>21,858,814</u>

Preference Stock — TXU Corp. has 3,000 shares of Series B preference stock outstanding. The preference stock has a dividend rate of 7.24% until June 15, 2005. The dividend rate for subsequent periods will be

determined according to periodic auctions. The Series B preference stock has a liquidation preference of \$100,000 per share. TXU Corp. may not redeem the shares before June 15, 2005. TXU Corp. is authorized to issue up to 50 million shares of preference stock in one or more series.

Shareholders Rights Plan — In February 1999, the Board of Directors adopted a shareholder rights plan pursuant to which shareholders were granted rights to purchase one one-hundredth of a share of Series A Preference Stock (Rights) for each share of TXU Corp.'s common stock held.

In the event that any person acquires more than 15% of TXU Corp.'s outstanding common stock in a transaction not approved by the Board of Directors, the Rights become exercisable, entitling each holder (other than the acquiring person or group) to purchase that number of shares of securities or other property of TXU Corp. having a market value equal to two times the exercise price of the Rights. If TXU Corp. were acquired in a merger or other business combination, each Right would entitle its holder to purchase a number of the acquiring company's common shares having a market value of two times the exercise price of the Right. In either case, TXU Corp.'s Board of Directors may choose to redeem the Rights before they become exercisable. TXU Corp.'s Board declared a dividend of one Right for each outstanding share of common stock. Rights were distributed to shareholders of record on March 1, 1999.

Dividend Restrictions — Terms of TXU Corp.'s Series B preference stock restrict TXU Corp.'s payment of common stock dividends while any preference share payment default exists.

TXU Corp. is required to make contract adjustment payments to the holders of equity-linked debt securities. TXU Corp. has the right to defer the contract adjustment payments, but any such election would subject TXU Corp. to restrictions on the payment of dividends on and redemption of outstanding shares of common stock. TXU Corp. has no plans to defer these contract adjustment payments.

As a holding company, TXU Corp. depends, in part, on the dividends it receives from its subsidiaries. US Holdings' outstanding preferred stock limits its ability to pay dividends on its common stock unless immediately after such dividend, US Holdings' earned surplus is greater than one and one-half times the full annual dividend on the preferred stock. The mortgage of TXU Electric Delivery restricts TXU Electric Delivery's payment of dividends to the amount of its retained earnings.

At December 31, 2004, there were no restrictions on the payment or redemption of common stock dividends by TXU Corp. under the above agreements.

The table below reflects the changes in TXU Corp. common stock outstanding for each of the years ending December 31, 2004, 2003 and 2002:

	<u>2004</u>	<u>2003</u>	<u>2002</u>
Balance at beginning of year	323,883,092	321,974,000	265,140,087
Issuances in public offerings.....	—	—	46,800,000
Issuances under equity-linked debt securities	1,817,371	—	8,365,133
Issuances under Direct Stock Purchase and Dividend			
Reinvestment Plan	110,014	508,379	1,069,264
Issuances under Long-Term Incentive Compensation Plan (a)	593,514	1,920,600	971,600
Repurchases	(84,257,444)	—	—
Forfeitures and cancellations under Long-Term Incentive			
Compensation Plan (b).....	<u>(2,293,667)</u>	<u>(519,887)</u>	<u>(372,084)</u>
Balance at end of year	<u>239,852,880</u>	<u>323,883,092</u>	<u>321,974,000</u>

- (a) Includes distributions of restricted stock as well as additional shares issued as a result of exceeding share price performance targets.
(b) Reflects forfeitures and cancellations of restricted stock awards granted plus additional shares resulting from reinvestment of dividends on restricted stock..

12. STOCK-BASED COMPENSATION PLANS

The Long-Term Incentive Compensation Plan (LTIP) is a stock-based compensation plan providing discretionary awards (LTIP awards) of restricted stock and performance units payable in common stock for qualified management employees. The maximum number of shares of common stock for which LTIP awards may be granted under the plan is 10,000,000, of which 6,394,151 shares remain authorized and available (including 1,227,426 forfeited shares). During 2004, 2003, and 2002, the Board of Directors granted LTIP awards that were issued subject to share price performance and vesting requirements over two and three year periods. The number of common shares to be ultimately distributed varies from 0% to 200% of the initial number of LTIP awards, based on TXU Corp.'s total return to shareholders over the applicable period compared to the total returns provided by the companies comprising the Standard & Poor's 500 Electric Utilities Index. TXU Corp. has established restrictions that limit employees' opportunities to liquidate vested stock awards. For both restricted stock and performance unit awards, dividends over the vesting period are converted to equivalent shares of TXU Corp. common stock to be distributed upon vesting.

Effective with the 1997 merger of ENSERCH Corporation (subsequently TXU Gas) and TXU Corp., outstanding options for ENSERCH Corporation common stock were exchanged for options for 532,913 shares of TXU Corp.'s common stock (TXU Gas Stock Option Plan). The weighted average exercise price for outstanding options at the beginning and end of 2004 was \$24.55 and \$22.50, respectively, and the weighted average exercise price for forfeited/expired options was \$28.83. No further options have been, or will be, granted under this plan.

The following table presents information about these stock-based compensation plans:

	<u>LTIP Awards</u>	<u>TXU Gas Stock Option Plan</u>
Balance — December 31, 2001	1,169,358	79,450
Granted.....	1,002,650	—
Forfeited/expired.....	(277,950)	(52,105)
Vested/Exercised	<u>(361,067)</u>	<u>(1,139)</u>
Balance — December 31, 2002.....	<u>1,532,991</u>	<u>26,206</u>
Granted.....	1,900,600	—
Forfeited/expired.....	(515,591)	(2,532)
Vested	<u>(37,167)</u>	<u>—</u>
Balance — December 31, 2003.....	<u>2,880,833</u>	<u>23,674</u>
Granted.....	1,970,265	—
Forfeited/expired.....	(1,710,150)	(4,305)
Vested/Exercised	<u>(3,667)</u>	<u>(16,733)</u>
Balance — December 31, 2004.....	<u>3,137,281</u>	<u>2,636</u>
To vest/exercisable in — 2005	874,566	1,243
To vest/exercisable in — 2006	867,500	1,393
To vest/exercisable in — 2007	1,395,215	—
Weighted average fair-value — 2004		
Outstanding — Beginning of year.....	\$ 9.65	
Granted.....	\$ 6.98	
Forfeited	\$ 8.65	
Vested	\$ —	
Outstanding — End of year	\$ 37.51	

Weighted average fair value of awards		
granted in:		
2002.....	\$	17.93
2003.....	\$	5.46
2004.....	\$	6.98

Historically, TXU Corp. has accounted for stock-based compensation plans using the intrinsic value method under APB 25. Compensation expense over the vesting period was remeasured each reporting period based on the market price of the stock and the assumed number of shares distributable given the share price performance to date. Reported compensation expense related to LTIP awards totaled \$25 million in 2003 and \$1 million in 2002.

For the 2004 reporting period, TXU Corp. early adopted SFAS 123R, which eliminates the alternative of applying the intrinsic value measurement provisions of APB 25 to stock compensation awards and requires the measurement of the cost of such awards over the vesting period based on the grant-date fair value of the award. TXU Corp. adopted SFAS 123R using the modified retrospective method, which allows for application to only prior interim periods in the year of initial adoption and resulted in the recognition of a \$15 million (\$10 million after-tax) cumulative change in accounting principle. For a portion of the 2004 period, the performance unit awards were payable in cash, but the awards were modified in December of 2004 and will be payable in stock.

TXU Corp. determined the fair value of its LTIP awards utilizing a valuation model that takes into account three principal factors: the probability weighted expected number of shares to be distributed upon vesting, the risk of uncertainty during the vesting period, and the restrictions limiting liquidation of vested stock awards. Based on the fair values determined under this model, reported expense in 2004 related to LTIP awards totaled \$56 million (\$36 million after-tax, or \$0.19 per share). As of December 31, 2004, unrecognized expense related to nonvested LTIP awards totaled \$48 million, which is expected to be recognized over a weighted average period of two years.

Had compensation expense for LTIP awards and previously existing awards under the TXU Gas Stock Option Plan been determined based upon the fair value methodology prescribed under SFAS 123, TXU Corp.'s net income would not have been materially different for the years ended December 31, 2003 and 2002.

13. INCOME TAXES

The components of TXU Corp.'s provisions for income taxes for continuing operations are as follows:

	Year Ended December 31,		
	2004	2003	2002
Current:			
US Federal.....	\$ 25	\$279	\$ 67
State.....	26	11	7
Non-US.....	<u>2</u>	<u>1</u>	<u>2</u>
Total.....	<u>53</u>	<u>291</u>	<u>76</u>
Deferred:			
US Federal.....	31	(16)	26
State.....	(19)	(1)	1
Non-US.....	<u>—</u>	<u>—</u>	<u>—</u>
Total.....	<u>12</u>	<u>(17)</u>	<u>27</u>
Investment tax credits.....	<u>(23)</u>	<u>(22)</u>	<u>(26)</u>
Total.....	<u>\$ 42</u>	<u>\$252</u>	<u>\$ 77</u>

Reconciliation of income taxes computed at the US federal statutory rate to provision for income taxes:

	Year Ended December 31,		
	2004	2003	2002
Income from continuing operations before income taxes, extraordinary loss and cumulative effect of changes in accounting principles:			
Domestic.....	\$ 123	\$ 821	\$ 184
Non-US.....	<u>—</u>	<u>(3)</u>	<u>(2)</u>
Total.....	<u>123</u>	<u>818</u>	<u>182</u>
Income taxes (benefit) at the US federal statutory rate of 35%.....	43	286	64
Loss on extinguishment of debt.....	107	—	—
Depletion allowance.....	(25)	(25)	(25)
Release of TXU Europe reserves.....	(75)	—	—
Amortization of investment tax credits.....	(23)	(22)	(26)
Investment tax credits – deferred tax.....	6	6	7
Amortization (under regulatory accounting) of statutory rate changes.....	(8)	(8)	(8)
Compensation expense.....	18	—	—
State income taxes, net of federal tax benefit.....	5	6	5
Nondeductible losses.....	—	—	53
Other.....	<u>(6)</u>	<u>9</u>	<u>7</u>
Income tax expense.....	<u>\$ 42</u>	<u>\$ 252</u>	<u>\$ 77</u>
Effective tax rate.....	34.1%	30.8%	42.3%

TXU Corp. had net tax benefits from dividend deductions related to LESOP Shares (see Note 11) of \$0.5 million, \$0.5 million and \$2.7 million in 2004, 2003 and 2002 which were credited directly to retained earnings.

Deferred income taxes provided for temporary differences based on tax laws in effect at December 31, 2004 and 2003, balance sheet dates are as follows:

	December 31,					
	2004			2003		
	Total	Current	Noncurrent	Total	Current	Noncurrent
Deferred Tax Assets						
Litigation liabilities	\$ 30	\$ 30	\$ —	\$ —	\$ —	\$ —
TXU Europe settlement	60	60	—	—	—	—
Unamortized investment tax credits	154	—	154	164	—	164
Impairment of assets	70	—	70	183	—	183
Alternative minimum tax	638	—	638	613	—	613
Retail clawback liability	33	—	33	61	—	61
Employee benefit liabilities	297	—	297	259	—	259
Net operating loss (NOL) carryforwards	684	—	684	1,537	15	1,522
NOL valuation allowance	(167)	—	(167)	(1,283)	—	(1,283)
Nuclear asset retirement obligation	151	—	151	150	—	150
State income taxes	11	—	11	7	—	7
Other	427	137	290	272	94	178
Total	<u>2,388</u>	<u>227</u>	<u>2,161</u>	<u>1,963</u>	<u>109</u>	<u>1,854</u>
Deferred Tax Liabilities						
Depreciation differences and capitalized construction costs	3,512	—	3,512	4,129	—	4,129
Deductions related to TXU Europe	592	—	592	409	—	409
Regulatory assets	595	—	595	616	—	616
State income taxes	46	—	46	42	—	42
Other	140	3	137	272	15	257
Total	<u>4,885</u>	<u>3</u>	<u>4,882</u>	<u>5,468</u>	<u>15</u>	<u>5,453</u>
Net Deferred Tax (Asset) Liability	<u>\$ 2,497</u>	<u>\$ (224)</u>	<u>\$ 2,721</u>	<u>\$ 3,505</u>	<u>\$ (94)</u>	<u>\$ 3,599</u>

	December 31,					
	2004			2003		
	Net Current Asset	Net Current Liability	Net Noncurrent Liability	Net Current Asset	Net Current Liability	Net Noncurrent Liability
Summary of Deferred Income Taxes						
US Federal	\$ 224	\$ —	\$ 2,686	\$ 94	\$ —	\$ 3,564
State	—	—	35	—	—	35
Total	<u>\$ 224</u>	<u>\$ —</u>	<u>\$ 2,721</u>	<u>\$ 94</u>	<u>\$ —</u>	<u>\$ 3,599</u>

At December 31, 2004, TXU Corp. had \$638 million of alternative minimum tax credit carryforwards (AMT) available to offset future tax payments. The AMT credit carryforwards have no expiration date. At December 31, 2004, TXU Corp. had net operating loss (NOL) carryforwards for federal income tax purposes of \$1.955 billion that expire as follows: \$1.896 billion in 2022, \$50 million in 2023 and \$9 million in 2024. The NOL carryforwards can be used to offset future taxable income. TXU Corp. fully expects to utilize all of its NOL carryforwards prior to their expiration date. TXU Corp. utilized \$716 million of NOL carryforwards in 2004. The NOL valuation allowance which was established in 2002 for the deduction related to the worthlessness of TXU Corp.'s investment in TXU Europe was adjusted downward in 2004 to \$167 million as a result of the filing of the 2003 tax return and receipt of an IRS notice of proposed adjustment.

The tax effects of the components included in accumulated other comprehensive income for the year ended December 31, 2004, was a net benefit of \$8 million.

TXU Corp.'s income tax returns are subject to examination by applicable tax authorities. The Internal Revenue Service is currently examining the tax years ended 1993 through 2002. In management's opinion, an adequate provision has been made for any future taxes that may be owed as a result of any examination.

See Note 18 under "Income Tax Contingencies" for discussion of the TXU Europe tax benefit recognized and the status of IRS audits.

14. RETIREMENT PLANS AND OTHER POSTRETIREMENT BENEFITS

TXU Corp. is the plan sponsor of, and a participating employer in, the TXU Retirement Plan, which provides benefits to most employees based on years of service and average earnings. The TXU Retirement Plan (Retirement Plan), is a defined benefit pension plan intended to qualify under Section 401(a) of the Internal Revenue Code of 1986, as amended (Code) and is subject to the provisions of the Employee Retirement Income Security Act of 1974, as amended (ERISA). Employees are eligible to participate in the Retirement Plan upon their completion of one year of service and the attainment of age 21. All benefits are funded by the participating employers. The Retirement Plan provides benefits to participants under one of two formulas: (i) a cash balance formula under which participants earn monthly contribution credits based on their compensation and a combination of their age and years of service, plus monthly interest credits, or (ii) a traditional defined benefit formula based on years of service and the average earnings of the three years of highest earnings. The cash balance interest component of the cash balance plan is variable and is determined using the yield on 30-year Treasury bonds.

All eligible employees hired after January 1, 2001 participate under the cash balance formula. Certain employees who, prior to January 1, 2002, participated under the traditional defined benefit formula, continue their participation under that formula. Under the cash balance formula, future increases in earnings will not apply to prior service costs. It is TXU Corp.'s policy to fund the plans on a current basis to the extent deductible under existing federal tax regulations. Such contributions, when made, are intended to provide not only for benefits attributed to service to date, but also those expected to be earned in the future.

TXU Corp. also has supplemental retirement plans for management employees, the information for which is included in the data below.

In addition, eligible employees of TXU Corp. may participate in a qualified savings plan, the Thrift Plan. This plan is a participant-directed defined contribution profit sharing plan intended to qualify under Section 401(a) of the Code, and is subject to the provisions of ERISA. The Thrift Plan includes an employee stock ownership component. Under the terms of the Thrift Plan, as amended effective in 2002, employees who do not earn more than the IRS threshold compensation limit used to determine highly compensated employees may contribute, through pre-tax salary deferrals and/or after-tax payroll deductions, the maximum amount of their regular salary or wages permitted under law. Employees who earn more than such threshold may contribute from 1% to 16% of their regular salary or wages. Employer matching contributions are also made in an amount equal to 100% of the first 6% of employee contributions for employees who are covered under the cash balance formula of the Retirement Plan, and 75% of the first 6% of employee contributions for employees who are covered under the traditional defined benefit formula of the Retirement Plan. Employer matching contributions

are invested in TXU Corp. common stock. TXU Corp.'s contributions to the Thrift Plan, including cash and TXU Corp. common stock, aggregated \$25 million for 2004, \$29 million for 2003 and \$30 million for 2002.

Minimum Pension Liability — The minimum pension liability represents the excess of the accumulated benefit obligation over the plans' assets and the liability already recorded under SFAS 87. This additional liability is recorded as an adjustment to shareholders' equity, as a component of accumulated comprehensive income. Based on the actuarial information at year-end 2004 and 2003, minimum pension liability gains were \$24 million and \$54 million, respectively, net of tax. The recording of the liability did not affect TXU Corp.'s financial covenants in any of its credit agreements.

Changes in Assumed Discount Rate — During 2004, the discount rate assumption for the pension and other postretirement benefit plans was revised as a result of remeasurements required by the Capgemini and TXU Gas transactions and changing interest rates. For the first half of 2004, the discount rate was 6.25%. The rate used for the third quarter was 6.5%, and the rate used in the fourth quarter was 6.0%. In selecting the assumed discount rate, TXU Corp. considered fixed income security yields for a AA rated portfolio of bonds as reported by Moody's.

	Year Ended December 31,		
	2004	2003	2002
<i>Assumptions used to determine net periodic benefit cost:</i>			
Discount rate	6.00% - 6.50%	6.25%	6.75%
Expected return on pension plan assets	8.50%	8.50%	8.50%
Rate of compensation increase	3.57%	3.95%	3.95%
<i>Assumptions used to determine benefit obligations at December 31:</i>			
Discount rate	6.00%	6.25%	6.75%
Rate of compensation increase	3.57%	3.95%	3.95%

Defined Benefit Plans —Information regarding defined benefit pension plans, based on December 31 measurement dates, follows:

	Year Ended December 31,		
	2004	2003	2002
<i>Components of Net Pension Costs:</i>			
Service cost	\$ 46	\$ 48	\$ 42
Interest cost	130	126	124
Expected return on assets	(142)	(142)	(157)
Amortization of unrecognized net transition asset	—	(1)	(1)
Amortization of unrecognized prior service cost	4	5	5
Amortization of net (gain) loss	13	7	(7)
Recognized settlement loss	—	2	—
Recognized curtailment loss	7	—	—
Net periodic pension cost	<u>\$ 58</u>	<u>\$ 45</u>	<u>\$ 6</u>
<i>Change in Pension Obligation:</i>			
Projected benefit obligation at beginning of year	\$2,173	\$1,935	
Service cost	46	48	
Interest cost	130	126	
Actuarial (gain) loss	(30)	157	
Benefits paid	(108)	(93)	
Curtailments	7	—	
Projected benefit obligation at end of year	<u>\$2,218</u>	<u>\$2,173</u>	
Accumulated benefit obligation at end of year	<u>\$2,079</u>	<u>\$1,943</u>	
<i>Change in Plan Assets:</i>			
Fair value of assets at beginning of year	\$1,819	\$1,529	
Actual return on assets	231	341	
Employer contributions	51	37	
Benefits paid	(106)	(88)	
Fair value of assets at end of year	<u>\$1,995</u>	<u>\$1,819</u>	
<i>Funded Status:</i>			
Projected pension benefit obligation	\$(2,218)	\$(2,173)	
Fair value of assets	1,995	1,819	
Unrecognized net transition asset	—	(1)	
Unrecognized prior service cost	15	29	
Unrecognized net loss	158	280	
Accrued pension cost	<u>\$ (50)</u>	<u>\$ (46)</u>	
<i>Amounts Recognized in the Balance Sheet Consist of:</i>			
Prepaid benefit cost	\$ 8	\$ —	
Accrued benefit liability	(92)	(124)	
Intangible asset	12	29	
Accumulated other comprehensive loss	14	32	
Accumulated deferred income taxes	8	17	
Net amount recognized	<u>\$ (50)</u>	<u>\$ (46)</u>	

At December 31, 2004, those pension plans that had a projected benefit obligation (PBO) that exceeded the fair value of plan assets had a total PBO of \$2.201 billion and total plan assets of \$1.971 billion. At December 31, 2003, the PBO for all pension plans exceeded the fair value of plan assets.

At December 31, 2004, those pension plans that had an accumulated benefit obligation (ABO) that exceeded the fair value of plan assets had a total ABO of \$2.062 billion and total plan assets of \$1.971 billion. At December 31, 2003, those pension plans that had an ABO that exceeded the fair value of plan assets had a total ABO of \$881 million and total plan assets of \$717 million.

Asset Allocations - The weighted-average asset allocations of pension plans at December 31, 2004 and 2003, by asset category are as follows:

Asset Type	Allocation of Plan Assets		Target Allocation Ranges	Expected Long-term Returns
	2004	2003		
US equity.....	52.1%	52.3%	40%-75%	9.5%
International equity	14.5%	13.1%	5%-20%	10.0%
Fixed income.....	29.1%	31.2%	15%-50%	6.8%
Real estate	4.3%	3.4%	0%-10%	8.0%
	<u>100.0%</u>	<u>100.0%</u>		<u>8.75%</u>

Expected Long-term Rate of Return on Assets Assumption — TXU Corp. considered both historical returns and future expectations for returns of various asset classes in its determination of the expected long-term rate of return assumption. A key expectation is that current interest rates will move towards an equilibrium interest rate that produces a 6% yield on intermediate government bonds. Expected returns for other asset classes are based on incremental returns over such expected government bond yield. The expected return for each asset class is then weighted based on the target asset allocation to develop the expected long-term rate of return assumption for the portfolio.

Investment Strategy — The investment objective is to provide a competitive return on the assets in each plan, while at the same time preserving the value of those assets. The strategy is to invest a third of the assets in fixed income and two thirds in equity, while maintaining sufficient cash to pay benefits and expenses.

The fixed income assets are diversified by sector and security, are intermediate in duration, and maintain an average quality rating of at least “A” (as determined by a major ratings agency such as Moody’s). The allocation to fixed income assets also includes an allocation to core, income producing real estate through private, unlevered real estate investment trusts. The equity assets are diversified by size, style and location with a conservative bias toward value securities.

Contributions in 2005 — Estimated funding in 2005 is \$22 million for the pension plan and \$53 million for the other postretirement benefits plan.

Postretirement Benefits Other Than Pensions — In addition to the Retirement Plan and the Thrift Plan, TXU Corp. offers health care and life insurance benefits to eligible employees and their eligible dependents upon the retirement of such employees. For employees retiring on or after January 1, 2002, the retiree contributions required for such coverage vary based on a formula depending on the retiree’s age and years of service.

	Year Ended December 31,		
	2004	2003	2002
<i>Assumptions used to determine net periodic benefit cost:</i>			
Discount rate	6.00% - 6.50%	6.25%	6.75%
Expected return on plan assets.....	8.01%	8.01%	8.26%
<i>Components of Net Periodic Postretirement Benefit Costs:</i>			
Service cost	\$15	\$18	\$12
Interest cost	60	63	63
Expected return on assets.....	(18)	(15)	(16)
Amortization of unrecognized net transition obligation.....	2	4	8
Amortization of unrecognized prior service cost/(credit)	(2)	1	6
Amortization of net loss.....	25	29	11
Recognized curtailment gain	(2)	—	—
Net postretirement benefit cost.....	<u>\$80</u>	<u>\$100</u>	<u>\$84</u>

	December 31,	
	2004	2003
<i>Assumptions used to determine benefit obligations at December 31:</i>		
Discount rate	6.00% - 6.50%	6.25%
<i>Change in Postretirement Benefit Obligation:</i>		
Benefit obligation at beginning of year	\$1,002	\$1,156
Service cost	15	18
Interest cost	60	63
Participant contributions.....	11	11
Plan amendments	—	(270)
Actuarial loss	31	88
Benefits paid	(70)	(64)
Curtailments.....	(62)	—
Benefit obligation at end of year	<u>\$ 987</u>	<u>\$1,002</u>

<i>Change in Plan Assets:</i>		
Fair value of assets at beginning of year	\$206	\$174
Actual return on assets.....	27	29
Employer contributions.....	52	54
Participant contributions.....	9	9
Benefits paid	(65)	(60)
Fair value of assets at end of year.....	<u>\$229</u>	<u>\$206</u>

<i>Funded Status:</i>		
Benefit obligation.....	\$ (987)	\$(1,002)
Fair value of assets.....	229	206
Unrecognized net transition obligation.....	11	17
Unrecognized prior service credit.....	(16)	(166)
Unrecognized net loss	342	549
Accrued postretirement benefit cost.....	<u>\$ (421)</u>	<u>\$ (396)</u>

The expected increase in costs of future benefits covered by the postretirement benefit plan is projected using a health care cost trend rate for pre-65 liabilities of 10% for 2005, decreasing by 1% each year until the ultimate rate of 5% is reached in 2010. For post-65 liabilities, the rate is 11% for 2005, decreasing by 1% each year until the ultimate rate of 5% is reached in 2011. A one percentage point increase in the assumed health care cost trend rate in each future year would increase the accumulated other postretirement benefit obligation at December 31, 2004, by approximately \$117 million and other postretirement benefits cost for 2004 by approximately \$11 million. A one percentage point decrease in the assumed health care cost trend rate would decrease the accumulated other postretirement benefit obligation at December 31, 2004, by approximately \$97 million and other postretirement benefits cost for 2004 by approximately \$10 million.

TXU Corp.'s other postretirement benefit plan weighted average asset allocations at December 31, 2004 and 2003, by asset category are as follows:

Asset Type	Allocation of Plan Assets	
	2004	2003
US equity.....	58.0%	57.9%
International equity.....	6.6%	5.5%
Fixed income.....	33.5%	35.2%
Real estate.....	1.9%	1.4%
	<u>100.0%</u>	<u>100.0%</u>

Plan Type	Expected Long-term Returns
401(h) accounts	8.75%
Life Insurance VEBA	8.75%
Union VEBA	8.75%
Non-Union VEBA	5.75%
Insurance Continuation Reserve	6.25%
	<u>8.66%</u>

Investment strategy and the basis used to determine the expected long-term return on assets for postretirement benefit plans is similar to that discussed above for the pension plans.

Future Benefit Payments— Estimated future benefit payments to beneficiaries are as follows:

	<u>2005</u>	<u>2006</u>	<u>2007</u>	<u>2008</u>	<u>2009</u>	<u>2010-14</u>
Pension benefits.....	\$100	\$102	\$106	\$111	\$115	\$675
Other postretirement benefits.....	\$60	\$62	\$65	\$67	\$70	\$401

Medicare Act—The Medicare Prescription and Drug, Improvement and Modernization Act of 2003 (the Medicare Act) was enacted in December 2003. TXU Corp. is accounting for the effects of the Medicare Act in accordance with FASB Staff Position 106-2. For 2004, the effect of the adoption of the Medicare Act was a reduction of approximately \$28 million in TXU Corp.'s other postretirement benefit costs. TXU Corp. elected to immediately reflect the financial impact of the recently enacted Medicare reform legislation in the accounting for other postretirement benefit costs, resulting in a \$1.9 million reduction in expense in 2003 and a reduction in the accumulated postretirement benefit obligation of \$142 million in accordance with FSP 106-1, subsequently superseded by FSP 106-2.

15. FAIR VALUE OF FINANCIAL INSTRUMENTS

The carrying amounts and related estimated fair values of TXU Corp.'s significant financial instruments were as follows:

	December 31, 2004		December 31, 2003	
	Carrying Amount	Fair Value	Carrying Amount	Fair Value
On balance sheet assets (liabilities):				
Long-term debt (including current maturities) (a) (b)	\$ (12,632)	\$ (13,330)	\$ (11,273)	\$ (11,571)
Long-term debt held by subsidiary trusts.....	\$ —	\$ —	\$ (546)	\$ (554)
LESOP note receivable (see Note 11)	\$ 229	\$ 286	\$ 235	\$ 280
Financial guarantees.....	\$ —	\$ —	\$ (2)	\$ (1)
Exchangeable preferred membership interests (c)	\$ —	\$ —	\$ (646)	\$ (1,580)

Off balance sheet assets (liabilities):

Financial guarantees.....	\$ —	\$ (7)	\$ —	\$ (9)
Accelerated share repurchase agreement (See Note 18).....	\$ —	\$ 13	\$ —	\$ —

(a) Excludes capital leases.

(b) Includes stock purchase contracts related to equity-linked debt.

(c) Reported in 2003 as preferred securities of subsidiaries.

In accordance with SFAS 133, financial instruments that are derivatives are recorded on the balance sheet at fair value.

The fair values of on balance sheet instruments are estimated at the lesser of either the call price or the market value as determined by quoted market prices, where available, or, where not available, at the present value of future cash flows discounted at rates consistent with comparable maturities with similar credit risk.

The fair value of each financial guarantee is based on the difference between the credit spread of the entity responsible for the underlying obligation and a financial counterparty applied, on a net present value basis, to the notional amount of the guarantee.

The carrying amounts for financial assets classified as current assets and the carrying amounts for financial liabilities classified as current liabilities approximate fair value due to the short maturity of such instruments. The fair values of other financial instruments, including the Capgemini put option, for which carrying amounts and fair values have not been presented are not materially different than their related carrying amounts.

16. DERIVATIVE FINANCIAL INSTRUMENTS

For derivative instruments designated as cash flow hedges, TXU Corp. recognized a net unrealized ineffectiveness loss of \$21 million (\$14 million after-tax) in 2004, a net gain of \$6 million (\$4 million after-tax) in 2003 and a net loss of \$41 million (\$27 million after-tax) in 2002. The ineffectiveness gains and losses related to commodity hedges and were reported as a component of revenues.

The net effect of unrealized mark-to-market ineffectiveness accounting, which includes the above amounts as well as the effect of reversing unrealized gains and losses recorded in previous periods to offset realized gains and losses in the current period, totaled \$19 million in net losses in 2004, \$36 million in net gains in 2003 and \$41 million in net losses in 2002.

The maximum length of time TXU Corp. hedges its exposure to the variability of future cash flows for forecasted energy-related transactions is approximately four years.

In 2002, TXU Corp. entered into certain cash flow hedges related to future forecasted interest payments. These hedges were terminated later in 2002, and \$133 million (\$86 million after-tax) was recorded as a charge to other comprehensive income. These losses are being amortized to earnings over a period of up to thirty years, as the forecasted transactions remain probable of occurring.

Cash flow hedge amounts reported in accumulated other comprehensive income will be recognized in earnings as the related forecasted transactions are settled or are deemed to be no longer probable of occurring. No amounts were reclassified into earnings in 2004, 2003 or 2002 as a result of the discontinuance of cash flow hedges because of the probability a hedged forecasted transaction would not occur.

As of December 31, 2004, TXU Corp. expects that \$118 million (\$77 million after-tax) in accumulated other comprehensive loss will be recognized in earnings over the next twelve months. This amount represents the projected value of the hedges over the next twelve months relative to what would be recorded if the hedge transactions had not been entered into. The amount expected to be reclassified is not a forecasted loss incremental to normal operations, but rather it demonstrates the extent to which volatility in earnings (which would otherwise exist) is mitigated through the use of cash flow hedges. The following table summarizes balances currently recognized in accumulated other comprehensive loss:

	Accumulated Other Comprehensive Loss at December 31, 2004		
	Commodity- related	Interest- related	Total
Dedesignated hedges (amounts fixed)	\$ 90	\$ 78	\$ 168
Hedges subject to market price fluctuations	<u>4</u>	<u>—</u>	<u>4</u>
Total	<u>\$ 94</u>	<u>\$ 78</u>	<u>\$ 172</u>

17. TEXAS ELECTRIC INDUSTRY RESTRUCTURING

Restructuring Legislation

As a result of the 1999 Restructuring Legislation, on January 1, 2002, TXU Corp. disaggregated (unbundled) its Texas electric utility business into a power generation company, a retail electric provider and an electricity transmission and distribution (delivery) utility. Unbundled electricity delivery utilities within ERCOT, such as TXU Electric Delivery, remain regulated by the Public Utility Commission of Texas (the Commission).

Effective January 1, 2002, REPs affiliated with electricity delivery utilities were required to charge price-to-beat rates, established by the Commission, to residential and small business customers located in their historical service territories. TXU Energy Holdings, whose REP is affiliated with an electricity delivery utility, was required to charge the price-to-beat rate, adjusted for fuel factor changes, to such classes of customers until the earlier of January 1, 2005 or the date on which 40% of the electricity consumed by customers in that class is supplied by competing REPs. Currently, TXU Energy Holdings may offer rates different from the price-to-beat rate to customers in that class, but it must also continue to make the price-to-beat rate available for residential and small business customers until January 1, 2007. In December 2003, the Commission found that TXU Energy Holdings had met the 40% requirement to be allowed to offer alternatives to the price-to-beat rate for small business customers in its historical service territory.

Under amended Commission rules, effective in April 2003, affiliated REPs of utilities are allowed to petition the Commission twice a year for a change in the fuel factor component of their price-to-beat rates if the average price of natural gas futures increases or decreases more than 5% (10% if the petition is filed after November 15 of any year) from the level used to set the existing price-to-beat fuel factor rate. TXU Energy Holdings implemented two price-to-beat increases in both 2003 and 2004.

Also, effective January 1, 2002, power generation companies affiliated with electricity delivery utilities may charge unregulated prices in connection with ERCOT wholesale power transactions. Estimated costs

associated with TXU Energy Holdings' nuclear power plant decommissioning obligations continue to be recovered by TXU Electric Delivery as an electricity distribution fee surcharge over the life of the plant.

Regulatory Settlement Plan

On December 31, 2001, US Holdings filed a Settlement Plan with the Commission. It resolved all major pending issues related to US Holdings' transition to competition pursuant to the 1999 Restructuring Legislation. The Settlement Plan does not remove regulatory oversight of TXU Electric Delivery's business nor does it eliminate TXU Energy Holdings' price-to-beat rates and related fuel adjustments. The Settlement Plan became final and non-appealable in January 2003.

The major elements of the Settlement Plan are:

Excess Mitigation Credit — Over the two-year period ended December 31, 2003, TXU Electric Delivery implemented a stranded cost excess mitigation credit in the amount of \$389 million (originally estimated to be \$350 million), plus \$26 million in interest, applied as a reduction to distribution fees charged to all REPs, including TXU Energy Holdings. The credit was funded through payments on a note receivable from TXU Energy Holdings.

Regulatory Asset Securitization — US Holdings received a financing order authorizing the issuance of securitization (transition) bonds in the aggregate principal amount of up to \$1.3 billion to recover regulatory asset stranded costs and other qualified costs. Accordingly, TXU Electric Delivery Transition Bond Company LLC, a bankruptcy remote financing subsidiary of TXU Electric Delivery, issued an initial \$500 million of securitization bonds in 2003 and the remaining \$790 million in the first half of 2004. The principal and interest on the bonds are recoverable through revenues as a transition charge to all REPs, including TXU Energy Holdings. There is no remaining issuance authorization under the financing order.

Retail Clawback Credit — The Settlement Plan provides that a retail clawback credit will be implemented unless 40% of the electricity consumed by residential and small business customers in a REP's historical service territory is supplied by competing REPs after the first two years of competition. This threshold was reached for small business customers, as discussed above, but not for residential customers. The amount of the credit is equal to the number of residential customers retained by TXU Energy Holdings in the historical service territory as of January 1, 2004, less the number of new customers TXU Energy Holdings had added outside of the historical service territory as of January 1, 2004, multiplied by \$90. The credit, which is being funded by TXU Energy Holdings, is being applied to delivery fees charged by TXU Electric Delivery to REPs, including TXU Energy Holdings, over a two-year period beginning January 1, 2004. In 2002, TXU Energy Holdings recorded a charge to cost of energy sold of \$185 million (\$120 million after-tax) to accrue an estimated retail clawback liability. In 2003, TXU Energy Holdings reduced the liability to \$173 million, with an offsetting credit to earnings of \$12 million (\$8 million after-tax) to reflect the calculation of the estimated liability applicable only to residential customers in accordance with the Settlement Plan. In 2004, TXU Energy Holdings further reduced the estimated liability by \$12 million (\$8 million after-tax) to reflect revised estimates of customer counts, with an offsetting credit to earnings. As of December 31, 2004, the balance of the retail clawback liability accrual was \$82 million. As the amount of the credit is based on numbers of customers over the related two-year period, the liability is subject to further adjustments.

Stranded Costs and Fuel Cost Recovery — TXU Energy Holdings' stranded costs, not including regulatory assets, are fixed at zero. US Holdings will not seek to recover its unrecovered fuel costs which existed at December 31, 2001. Also, it will not conduct a final fuel cost reconciliation, which would have covered the period from July 1998 until the beginning of competition in January 2002.

18. COMMITMENTS AND OTHER CONTINGENCIES

Clean Air Act — The federal Clean Air Act, as amended (Clean Air Act) includes provisions which, among other things, place limits on SO₂ and NO_x emissions produced by electricity generation plants. TXU Energy Holdings' capital requirements have not been significantly affected by the requirements of the Clean Air Act. In addition, all permits required for the air pollution control provisions of the 1999 Restructuring

Legislation have been applied for and TXU Energy Holdings has initiated a construction program to install control equipment to achieve the required reductions.

Power Purchase Contracts — Certain contracts to purchase electricity provide for capacity payments to ensure availability and provide for adjustments based on the actual power taken under the contracts. Capacity payments under these contracts totaled \$230 million in both 2004 and 2003 and \$296 million in 2002.

Expected future capacity payments under existing agreements are estimated as follows:

2005.....	\$ 108
2006.....	56
2007.....	18
2008.....	—
2009.....	—
Thereafter.....	—
Total capacity payments	<u>\$ 182</u>

At December 31, 2004, TXU Corp. had commitments for pipeline transportation and storage reservation fees as follows:

2005.....	\$ 74
2006.....	45
2007.....	44
2008.....	41
2009.....	43
Thereafter.....	<u>107</u>
Total pipeline transportation and storage reservation fees	<u>\$ 354</u>

On the basis of TXU Corp.'s current expectations of demand from its electricity customers as compared with its capacity and take-or-pay payments, management does not consider it likely that any material payments will become due for electricity not taken beyond capacity payments.

Coal Contracts — TXU Corp. has commitments under coal purchase agreements and coal transportation agreements as follows:

2005.....	\$ 96
2006.....	109
2007.....	95
2008.....	98
2009.....	102
Thereafter.....	—
Total.....	<u>\$ 500</u>

Leases — TXU Corp. has entered into operating leases covering various facilities and properties including generation plant facilities, combustion turbines, transportation equipment, mining equipment, data processing equipment and office space. Certain of these leases contain renewal and purchase options and residual value guarantees. Lease costs charged to operating expense totaled \$190 million, \$215 million and \$222 million in 2004, 2003 and 2002, respectively.

As of December 31, 2004, future minimum lease payments under both capital leases and operating leases (with initial or remaining noncancelable lease terms in excess of one year) were as follows:

<u>Year</u>	<u>Capital Leases</u>	<u>Operating Leases</u>
2005.....	\$ 2	\$ 78
2006.....	2	82
2007.....	2	84
2008.....	2	80
2009.....	1	77
Thereafter.....	<u>2</u>	<u>427</u>
Total future minimum lease payments.....	11	<u>\$ 828</u>
Less amounts representing interest.....	<u>2</u>	
Present value of future minimum lease payments.....	9	
Less current portion.....	<u>1</u>	
Long-term capital lease obligation.....	<u>\$ 8</u>	

Accelerated Share Repurchase — In November 2004, TXU Corp. entered into an agreement with a broker-dealer counterparty under which TXU Corp. repurchased 52.5 million shares of its outstanding common stock at an initial price of \$64.57 per share for a total of \$3.4 billion. Under the agreement, the counterparty immediately borrows shares that are sold to and canceled by TXU Corp. and in turn purchases shares in the open market over a subsequent time period; the agreement is subject to a future contingent purchase price adjustment based on the actual costs of the shares purchased by the counterparty. The price adjustment can be settled, at TXU Corp.'s option, in cash or in shares of its common stock. As of March 8, 2005, the counterparty had repurchased 55% of the shares under the agreement at an average price per share of \$68.07. Assuming the counterparty repurchased the remaining shares at a price per share equal to \$78.41, which was the closing price of TXU Corp.'s common stock on March 8, 2005, then TXU Corp. would be required to pay up to approximately \$464 million (including related settlement fees and expenses) in cash and/or issue up to approximately 5.9 million shares of TXU Corp. common stock to the counterparty in settlement of the transaction. The settlement amount can increase or decrease depending upon the actual price paid for the shares repurchased by the counterparty under the program. The settlement is expected to occur between the second and fourth quarter of 2005, depending upon the timing and pace of the counterparty's purchases.

Guarantees — TXU Corp. has entered into contracts that contain guarantees to outside parties that could require performance or payment under certain conditions. These guarantees have been grouped based on similar characteristics and are described in detail below.

Project development guarantees — In 1990, US Holdings repurchased an electric co-op's minority ownership interest in the Comanche Peak nuclear generation plant and assumed the co-op's indebtedness to the US government for the facilities. US Holdings is making principal and interest payments to the co-op in an amount sufficient for the co-op to make payments on its indebtedness. US Holdings guaranteed the co-op's payments, and in the event that the co-op fails to make its payments on the indebtedness, the US government would assume the co-op's rights under the agreement, and such payments would then be owed directly by US Holdings. At December 31, 2004, the balance of the indebtedness was \$131 million with maturities of principal and interest extending to December 2021. The indebtedness is secured by a lien on the purchased facilities.

Residual value guarantees in operating leases — TXU Corp. is the lessee under various operating leases that obligate it to guarantee the residual values of the leased facilities. Accounting rules require the recording of a liability for all guarantees entered into subsequent to December 31, 2002. At December 31, 2004, the aggregate maximum amount of residual values guaranteed was approximately \$204 million with an estimated residual recovery of approximately \$135 million. The substantial majority of the maximum guarantee amount relates to leases entered into prior to December 31, 2002. The average life of the lease portfolio is approximately seven years.

Letters of credit — TXU Energy Holdings has entered into various agreements that require letters of credit for financial assurance purposes. Approximately \$383 million of letters of credit were outstanding at December 31, 2004 to support existing floating rate pollution control revenue bond debt of approximately \$375 million. The letters of credit are available to fund the payment of such debt obligations. These letters of credit have expiration dates in 2008.

TXU Energy Holdings has outstanding letters of credit in the amount of \$9 million for miscellaneous credit support requirements. Although the average life of the letters of credit is approximately one year, the obligation to provide guarantees is ongoing.

TXU Energy Holdings has outstanding letters of credit in the amount of \$99 million to support hedging and risk management margin requirements in the normal course of business. As of December 31, 2004, approximately 27% of the obligations supported by these letters of credit mature within one year, and substantially all of the remainder mature in the next three years.

Surety bonds — TXU Corp. has outstanding surety bonds of approximately \$30 million to support performance under various subsidiary contracts and legal obligations in the normal course of business. The term of the surety bond obligations is approximately one year.

Other — US Holdings has entered into contracts with public agencies to purchase cooling water for use in the generation of electric energy and has agreed, in effect, to guarantee the principal, \$6 million at December 31, 2004, and interest on bonds issued by the agencies to finance the reservoirs from which the water is supplied. The bonds mature in 2011 and have an interest rate of 5.50%. US Holdings is required to make periodic payments equal to such principal and interest, including amounts assumed by a third party and reimbursed to US Holdings. In addition, US Holdings is obligated to pay certain variable costs of operating and maintaining the reservoirs. US Holdings has assigned to a municipality all its contract rights and obligations in connection with \$1 million remaining principal amount of bonds at December 31, 2004, issued for similar purposes, which had previously been guaranteed by US Holdings. US Holdings is, however, contingently liable in the event of default by the municipality.

In connection with the TXU Gas transaction, on October 1, 2004, TXU Corp. agreed, for a period of three years, to indemnify Atmos Energy Corporation for certain qualified environmental claims that may arise in relation to the assets acquired by Atmos Energy Corporation. TXU Corp. is not required to indemnify Atmos Energy Corporation until the aggregate of all such qualified claims exceeds \$10 million, and TXU Corp. is only required to indemnify Atmos Energy Corporation for 50% of qualified claims between \$10 million and \$20 million. The maximum amount that TXU Corp. would be required to pay Atmos Energy Corporation pursuant to this environmental indemnity is \$192.5 million. In addition, TXU Corp. agreed to indemnify Atmos Energy Corporation for up to \$500 million for any liability related to assets retained by TXU Corp., including certain inactive gas plant sites not acquired by Atmos Energy Corporation, and up to \$1.4 billion for contingent liabilities associated with pre-closing tax and employee related matters. In each case, TXU Corp.'s indemnification is limited to 10 years. The maximum aggregate amount that TXU Corp. may be required to pay is \$1.925 billion. The estimated fair value of the indemnification recorded upon completion of the TXU Gas transaction was \$2.5 million.

In 1992, a discontinued engineering and construction business of TXU Gas completed construction of a plant, the performance of which is warranted by TXU Gas through 2008. The maximum contingent liability under the guarantee is approximately \$112 million. No claims have been asserted under the guarantee and none are anticipated. TXU Corp. retains this contingent liability under the terms of the TXU Gas transaction agreement.

Income Tax Contingencies — TXU Corp. and certain of its subsidiaries are currently under audit by the IRS with respect to tax returns for various tax periods subsequent to 1992 and prior to 2003, and are subject to audit by other taxing authorities and by the IRS for subsequent tax periods. The amount and timing of any tax assessments resulting from these audits are uncertain, and could have a material effect on the company's liquidity and results of operations. Certain audit matters as to which management believes there is a reasonable possibility of a material future tax assessment are discussed below. Other than as discussed below under "*TXU Europe*" and "*TXU Gas 1993 Audit*", there have been no material adjustments to tax reserves.

TXU Corp. 1994-1996 Audit — The IRS audit of TXU Corp.'s 1994 -1996 federal tax return has been completed, and all material issues have been agreed upon.

TXU Corp. 1997-2002 Audit — The IRS is currently examining TXU Corp.'s federal income tax returns for 1997-2002. In addition to proposed adjustments with respect to the worthlessness of TXU Corp.'s investment in TXU Europe (discussed separately below), the IRS has issued notices of proposed adjustment with respect to several other items. The IRS will likely issue additional proposed adjustments during the spring of 2005, and is expected to complete its examination by the third quarter of 2005. TXU Corp. expects to protest a number of adjustments, and expects that the protested issues will not be resolved until after 2005. Management believes that reserves recorded for potential adjustments to TXU Corp.'s 1997-2002 tax returns are adequate to provide for the expected outcome of the IRS's proposed adjustments.

TXU Europe — On its US federal income tax return for calendar year 2002, TXU Corp. claimed an ordinary loss deduction related to the worthlessness of TXU Corp.'s investment in TXU Europe, the tax benefit of which is estimated to be \$983 million (assuming the deduction is sustained on audit). Due to a number of uncertainties regarding the proper tax treatment of the worthlessness loss, no portion of the tax benefit related to TXU Corp.'s 2002 write-off of its investment in TXU Europe was recognized in income prior to the second quarter of 2004.

As discussed in Note 1, \$755 million of the tax benefit was recognized during 2004. The tax benefits recognized by TXU Corp. during 2004 were based on the capital loss and ordinary deductions allowed by the IRS in a notice of proposed adjustment originally issued in June 2004 (and subsequently amended in September 2004), adjusted to exclude the effects of elements of the IRS notice that TXU Corp. believes are without merit and unlikely to be sustained. While the notice of proposed adjustment is not binding on the IRS and therefore it is uncertain what positions the IRS might ultimately assert or what, if any, tax liability might result, TXU Corp. believes that the possibility of the IRS adopting a more adverse position is remote.

If TXU Corp.'s ordinary loss deduction claimed on the 2002 tax return is not sustained, TXU Corp. would be required to repay approximately \$452 million in tax refunds previously received (including interest through December 31, 2004) based on the assumptions used to determine the tax benefits recognized during 2004, and before taking into account other potential IRS adjustments to TXU's 1997-2002 tax returns. In addition, TXU Corp. would owe additional tax of \$108 million related to 2004. These amounts are reported as other noncurrent liabilities in the December 31, 2004 balance sheet. No material earnings charge is expected with respect to any such repayment. TXU Corp. is unable to predict the timing of any such repayment, but currently expects that it would not be made prior to 2006.

TXU Corp. believes that its original tax reporting of the worthlessness of its investment in TXU Europe as an ordinary deduction was proper and intends to protest the IRS's proposed adjustments. If TXU Corp.'s position is sustained, approximately \$217 million would be recognized in earnings.

TXU Corp. 2003-2005 Audit — TXU Corp. expects that the IRS will commence an examination of its 2003 through 2005 tax returns during 2006. Consistent with its experience in prior audits, TXU Corp. expects that the IRS will propose adjustments to the tax returns and that TXU Corp. will incur some liability to resolve those proposed adjustments with the IRS. The nature and amount of any such proposed adjustments is uncertain and will likely not be known for several years. TXU Corp. has recorded reserves related to potential audit adjustments to its 2003 – 2004 tax returns, representing the estimated tax expense to be incurred as a result of such audit adjustments.

TXU Gas 1993 Audit — In April 2003, the IRS proposed to TXU Gas certain adjustments to the U.S. federal income tax returns of ENSERCH Corporation (the acquired predecessor of TXU Gas) for the 1993 calendar year. TXU Gas appealed the proposed adjustments to the IRS Appeals Office and in June 2004, the IRS Appeals Office rejected the substance of TXU Gas' appeal of the IRS proposed adjustments, refused to consider a settlement of the disputed issues, and returned the case to the Examination Division to address loss carryback claims from subsequent years. Based on the unsuccessful settlement negotiations, additional tax reserves of \$47 million were recorded during the second quarter of 2004 to account for the excess of the tax, penalty and interest

asserted by the IRS over the amount of tax reserves previously recorded (see Note 4). During the fourth quarter of 2004, TXU Gas paid all tax, interest and penalty due for the 1993 tax year, and reduced its tax reserves and deferred tax assets, all in accordance with the IRS proposed adjustments. TXU Gas expects to file a claim for refund protesting certain of the IRS adjustments.

The results of TXU Gas are presented as discontinued operations as discussed in Note 4. Under the definitive transaction agreement, the buyer of the TXU Gas operations will not assume liabilities, among others, related to ENSERCH tax returns contested by the IRS.

TXU Gas 1994-1997 Audit — The IRS is currently examining the ENSERCH Corporation 1994-1997 federal income tax returns. To date, the IRS has proposed only minor adjustments. However, the IRS is expected to issue a statutory notice of deficiency on or before March 13, 2005, and TXU Gas expects that the notice of deficiency will challenge certain tax effects of the December 1994 incorporation of Enserch Exploration Partners, L.P. (the “1994 Transaction”). TXU Gas estimates that the IRS will propose adjustments which, if sustained in full, would result in a charge to income from discontinued operations, before applicable tax reserves, of \$181 million (including interest through December 31, 2004). Management believes that the reported tax treatment of the 1994 Transaction was proper, and intends to challenge any IRS proposed adjustments. Management believes that reserves recorded for potential adjustments to ENSERCH’s 1994-1997 tax returns are adequate to provide for the expected outcome of the anticipated IRS proposed adjustments.

Labor Contracts — Approximately 1,750 TXU Energy Holdings employees and 175 TXU Electric Delivery employees are represented by labor unions and covered by collective bargaining agreements with varying expiration dates. These agreements generally cover two to three year periods; however, as is normal practice in the industry, wages and benefits are established annually. Negotiations are currently underway with respect to the collective bargaining agreement covering employees at the Comanche Peak plant and discussions are expected to begin in the fall of 2005 regarding the agreements with employees in TXU Energy Holdings’ other power production and mining operations. The TXU Electric Delivery bargaining agreement will expire in 2007 and wages and benefits will be negotiated in the fall of 2005. Management does not anticipate that any changes in collective bargaining agreements will have a material affect on TXU Corp.’s financial position, results of operations or cash flows; however, TXU Corp. is unable to predict the ultimate outcome of these labor negotiations.

Nuclear Insurance — With regard to liability coverage, the Price-Anderson Act (Act) provides financial protection for the public in the event of a significant nuclear power plant incident. The Act sets the statutory limit of public liability for a single nuclear incident at \$10.8 billion currently and requires nuclear power plant operators to provide financial protection for this amount. The Act is being considered by the United States Congress for modification and extension. The terms of a modification, if any, are not presently known and therefore TXU Corp. is unable, at this time, to determine any impact it may have on nuclear liability coverage. As required, TXU Corp. provides this financial protection for a nuclear incident at Comanche Peak resulting in public bodily injury and property damage through a combination of private insurance and industry-wide retrospective payment plans. As the first layer of financial protection, TXU Corp. has \$300 million of liability insurance from American Nuclear Insurers (ANI), which provides such insurance on behalf of a major stock insurance company pool, Nuclear Energy Liability Insurance Association. The second layer of financial protection is provided under an industry-wide retrospective payment program called Secondary Financial Protection (SFP).

Under the SFP, each operating licensed reactor in the US is subject to an assessment of up to \$100.6 million, subject to increases for inflation every five years, in the event of a nuclear incident at any nuclear plant in the US. Assessments are limited to \$10 million per operating licensed reactor per year per incident. All assessments under the SFP are subject to a 3% insurance premium tax, which is not included in the above amounts.

With respect to nuclear decontamination and property damage insurance, NRC regulations require that nuclear plant license-holders maintain not less than \$1.1 billion of such insurance and require the proceeds thereof to be used to place a plant in a safe and stable condition, to decontaminate it pursuant to a plan submitted to and approved by the NRC before the proceeds can be used for plant repair or restoration or to provide for

premature decommissioning. TXU Corp. maintains nuclear decontamination and property damage insurance for Comanche Peak in the amount of \$3.4 billion, above which TXU Corp. is self-insured. The primary layer of coverage of \$500 million is provided by Nuclear Electric Insurance Limited (NEIL), a nuclear electric utility industry mutual insurance company. The remaining coverage includes premature decommissioning coverage provided by NEIL in the amount of \$2.25 billion and \$661 million from other insurance markets and foreign nuclear insurance pools. TXU Corp. is subject to a maximum annual assessment from NEIL of \$31.5 million.

TXU Corp. maintains Accidental Outage Insurance through NEIL to cover the additional costs of obtaining replacement power from another source if one or both of the units at Comanche Peak are out of service for more than twelve weeks as a result of covered direct physical damage. The coverage provides for weekly payments of \$3.5 million for the first fifty-two weeks and \$2.8 million for the next 110 weeks for each outage, respectively, after the initial twelve-week period. The total maximum coverage is \$490 million per unit. The coverage amounts applicable to each unit will be reduced to 80% if both units are out of service at the same time as a result of the same accident. Under this coverage, TXU Corp. is subject to a maximum annual assessment of \$8.8 million.

There have been some revisions made to the nuclear property and nuclear liability insurance policies regarding the maximum recoveries available for multiple terrorism occurrences. Under the NEIL policies, if there were multiple terrorism losses occurring within a one-year time frame, NEIL would make available one industry aggregate limit of \$3.24 billion plus any amounts it recovers from other sources up to the limits for each claimant. If terrorism losses occurred beyond the one-year period, a new set of limits and resources would apply. Under the ANI liability policy, the liability arising out of terrorist acts will be subject to one industry aggregate limit of \$300 million that could be reinstated at ANI's option depending on prevailing risk circumstances and the balance in the Industry Credit Rating Plan reserve fund. Under the US Terrorism Risk Insurance Act of 2002, the US government provides reinsurance with respect to acts of terrorism in the US for losses caused by an individual or individuals acting on behalf of foreign parties. In such circumstances, the NEIL and ANI terrorism aggregates would not apply.

Nuclear Decommissioning — Through December 31, 2001, decommissioning costs were recovered from consumers based upon a 1992 site-specific study through rates placed in effect under TXU Corp.'s January 1993 rate increase request. Effective January 1, 2002, decommissioning costs are recovered through a tariff charged to REPs by TXU Electric Delivery based upon a 1997 site-specific study, adjusted for trust fund assets, as a component of delivery fees effective under TXU Corp.'s 2001 Unbundled Cost of Service filing. Amounts recovered through regulated rates are deposited in external trust funds (see Note 6 under *Investments*). An updated decommissioning study is in the process of being completed. It is anticipated that no material change in the decommissioning funding will be required.

See Note 3 for a discussion of the impact of SFAS 143 on accounting for nuclear decommissioning costs.

Legal Proceedings — On February 18, 2005, a lawsuit was filed by Utility Choice, L.P. and Cirro Group, Inc. in the United States District Court for the Southern District of Texas, Houston Division, against TXU Corp. and certain of its subsidiaries, as well as various other wholesale market participants doing business in ERCOT, claiming generally that defendants engaged in a variety of anticompetitive conduct, including market manipulation in violation of antitrust and other laws. TXU Corp. believes that claims against it and its subsidiary companies are without merit, and TXU Corp. and its subsidiaries intend to vigorously defend the lawsuit. TXU Corp. is, however, unable to estimate any possible loss or predict the outcome of this action.

Between October 19 and December 30, 2004, ten lawsuits were filed by purported customers in various California superior courts against TXU Corp., TXU Energy Trading Co. and TXU Energy Services and other marketers, traders, transporters and sellers of natural gas. Plaintiffs allege that beginning at least by the summer of 2000, defendants manipulated and fixed at artificially high levels natural gas prices in California in violation of the Cartwright Act and other California state laws. These lawsuits have been coordinated in the San Diego Superior Court with numerous other natural gas actions as "In re Natural Gas Anti-Trust Cases I, II, III, IV and V." TXU Corp. believes the claims against TXU Corp. and its subsidiaries are without merit, and intends to vigorously defend the lawsuits. TXU Corp. is, however, unable to estimate any possible loss or predict the outcome of these actions.

On July 7, 2003, a lawsuit was filed by Texas Commercial Energy (TCE) in the United States District Court for the Southern District of Texas, Corpus Christi Division, against TXU Energy Holdings and certain of its subsidiaries, as well as various other wholesale market participants doing business in ERCOT, claiming generally that defendants engaged in market manipulation, in violation of antitrust and other laws, primarily during the period of extreme weather conditions in late February 2003. An amended complaint was filed in February 2004 that joined additional, unaffiliated defendants. Three retail electric providers filed motions for leave to intervene in the action alleging claims substantially identical to TCE's. In addition, approximately 25 purported former customers of TCE filed a motion to intervene in the action alleging claims substantially identical to TCE's, both on their own behalf and on behalf of a putative class of all former customers of TCE. An order granting TXU Energy Holdings' Motion to Dismiss based on the filed rate doctrine was entered on June 24, 2004. TCE has appealed the dismissal; however, TXU Corp. believes the dismissal of the antitrust claims was proper and that it has not committed any violation of the antitrust laws. The appeal remains pending before the Fifth Circuit Court of Appeals. Further, the Commission's investigation of the market conditions in late February 2003 has not resulted in any finding adverse to TXU Corp. Accordingly, TXU Corp. believes that TCE's and the intervenors' claims are without merit, and intends to vigorously defend the lawsuit on appeal. TXU Corp. is, however, unable to estimate any possible loss or predict the outcome of this action.

On April 28, 2003, a lawsuit was filed by a former employee of TXU Portfolio Management in the United States District Court for the Northern District of Texas, Dallas Division, against TXU Corp., TXU Energy Holdings and TXU Portfolio Management. The case is set for trial on June 6, 2005 and discovery in the case is substantially complete. In the case, the plaintiff asserts claims under Section 806 of Sarbanes-Oxley arising from the termination of plaintiff's employment and claims for breach of contract relating to payment of certain bonuses. Plaintiff seeks back pay, payment of bonuses and alternatively, reinstatement or future compensation, including bonuses. TXU Corp. believes the plaintiff's claims are without merit. The plaintiff was terminated as the result of a reduction in force, not as a reaction to any concerns the plaintiff had expressed, and plaintiff was not in a position to evaluate TXU Corp.'s financial statements or assess the adequacy of TXU Corp.'s financial disclosures. Thus, TXU Corp. does not believe that there is any merit to the plaintiff's claims under Sarbanes-Oxley. TXU Corp. disputes the plaintiff's claims and intends to vigorously defend the litigation. TXU Corp. is, however, unable to estimate any possible loss or predict the outcome of this action.

On March 10, 2003, a lawsuit was filed by Kimberly P. Killebrew in the United States District Court for the Eastern District of Texas, Lufkin Division, against TXU Corp. and TXU Portfolio Management, asserting generally that defendants engaged in manipulation of the wholesale electric market, in violation of antitrust and other laws. This case was transferred to the Beaumont Division of the Eastern District of Texas and on March 24, 2004 was transferred to the Northern District of Texas, Dallas Division. This action is brought by an individual, alleging to be a retail consumer of electricity, on behalf of herself and as a proposed representative of a putative class of retail purchasers of electricity that are similarly situated. Defendants have filed a motion to dismiss the lawsuit which is pending before the court; however, as a result of the dismissal of the antitrust claims in the litigation described above brought by TCE, the parties have agreed to stay this litigation until the appeal in the TCE case has been decided. TXU Corp. believes that the plaintiff lacks standing to assert any antitrust claims and that defendants have not violated antitrust laws or other laws as claimed by plaintiff. Therefore, TXU Corp. believes that plaintiff's claims are without merit and plans to vigorously defend the lawsuit. TXU Corp. is however, unable to estimate any possible loss or predict the outcome of this action.

In November 2002 and February and March 2003, three lawsuits were filed in the United States District Court for the Northern District of Texas asserting claims under ERISA on behalf of a putative class of participants in and beneficiaries of various employee benefit plans of TXU Corp. These ERISA lawsuits have been consolidated, and a consolidated complaint was filed in February 2004 against TXU Corp., the directors of TXU Corp., Erle Nye, Peter B. Tinkam, Kirk R. Oliver, Biggs C. Porter, Diane J. Kubin, Barbara B. Curry and Richard Wistrand. On February 10, 2004, the plaintiffs filed their motion for and memorandum in support of class certification. After class certification discovery was completed, the Court denied Plaintiffs' initial class certification motion without prejudice and granted plaintiffs' leave to amend their complaint. Plaintiff's second class certification motion remains pending and TXU Corp. and the individual defendants oppose class certification. The plaintiffs seek to represent a class of participants in such employee benefit plans during period between April 26, 2001 and October 11, 2002. TXU Corp. believes the claims are without merit and intends to vigorously defend the lawsuit. TXU Corp. is, however, unable to estimate any possible loss or predict the outcome of this action.

On October 23, 2002, a derivative lawsuit was filed by a purported shareholder on behalf of TXU Corp. in the 116th Judicial District Court of Dallas County, Texas, against TXU Corp., Erle Nye, Michael J. McNally, David W. Biegler, J.S. Farrington, William M. Griffin, Kerney Laday, Jack E. Little, Margaret M. Maxey, J.E. Oesterreicher, Charles R. Perry and Herbert H. Richardson. The plaintiff alleges breach of fiduciary duty, abuse of control, mismanagement, waste of corporate assets, and breach of duties of loyalty and good faith. The named individual defendants are current or former officers and/or directors of TXU Corp. No amount of damages has been specified. The plaintiffs in such suit have failed to make a demand upon the directors as is required by law, and the case is currently stayed. The plaintiff has filed a motion seeking to lift the stay which is set for hearing on March 25, 2005. The defendants have filed pleadings seeking to have the case dismissed if the stay is lifted due to plaintiffs failure to make the required presuit demand.

In October, November, and December 2002 and January 2003, a number of lawsuits were filed in, removed to or transferred to the United States District Court for the Northern District of Texas against TXU Corp. and certain of its officers. These lawsuits have been consolidated and lead plaintiffs have been appointed by the Court. The complaint alleged violations of the provisions of Sections 10(b) and 20(a) of the Securities and Exchange Act of 1934, as amended, and Rule 10b-5 promulgated thereunder, and Section 11 and 12 of the Securities Act of 1933, as amended, relating to alleged materially false and misleading statements, including statements in prospectuses related to the offering by TXU Corp. of its equity-linked debt securities and common stock in May and June 2002. On July 21, 2003, the lead plaintiffs filed an amended consolidated complaint against Erle Nye, Michael J. McNally, V.J. Horgan, and Brian N. Dickie and directors Derek C. Bonham, J.S. Farrington, William M. Griffin, Kerney Laday, Jack E. Little, Margaret M. Maxey, J.E. Oesterreicher, Herbert H. Richardson and Charles R. Perry, as defendants. On January 20, 2005, TXU Corp. executed a memorandum of understanding pursuant to which TXU Corp. would (i) make a one-time payment of \$150 million, of which \$66 million has been pledged by insurance carriers, resulting in a net disbursement of \$84 million (\$55 million after-tax), (ii) make certain corporate governance changes, including heightened independence standards for directors, (iii) deny any liability in connection with the lawsuits, (iv) and be released from any claims or liabilities thereafter. TXU Corp. may receive additional amounts from insurance carriers, which would reduce the financial impact of the settlement to TXU Corp. TXU Corp. expects to execute a final agreement containing the terms of the settlement, which will be subject to various conditions, including court approval and notice to members of the plaintiff class. The payment is expected to be made in the second quarter of 2005 and sourced from insurance proceeds and working capital, including cash on hand, and credit facility capacity.

Other Contingencies — In October 2003, the former directors and officers of TXU Europe Limited and subsidiaries that are now in administration (collectively TXU Europe), who include current and former officers of TXU Corp. and subsidiary companies, received notices from certain creditors and the administrators of TXU Europe of various claims or potential claims related to losses incurred by creditors, including claims for alleged omissions from a securities offering document and alleged breaches by directors of their English law duties as directors of these companies in failing to minimize the potential losses to the creditors of TXU Europe. On January 27, 2005, TXU Corp. executed a comprehensive agreement resolving potential claims against TXU Corp. relating to TXU Europe. Pursuant to the agreement, TXU Corp. will make a \$220 million one-time payment (\$143 million after-tax), a substantial portion of which may be recovered from insurance carriers, denies any liability, and is released from any such claims. The agreement is contingent upon creditor approval and receipt by TXU Corp. of formal releases. The payment is expected to be made in the second quarter of 2005 and sourced from working capital, credit facility capacity and insurance proceeds should agreements be reached with carriers.

General — In addition to the above, TXU Corp. is involved in various other legal and administrative proceedings in the normal course of business the ultimate resolution of which, in the opinion of management, should not have a material effect upon its financial position, results of operations or cash flows.

19. SEGMENT INFORMATION

TXU Corp.'s operations are aligned into two reportable segments: TXU Energy Holdings and TXU Electric Delivery. The segments are managed separately because they are strategic business units that offer different products or services and involve different risks.

TXU Energy Holdings – consists of operations, principally in the competitive Texas market, involving power production (electricity generation), and retail and wholesale energy sales. The chief executive officer manages these operations as an integrated business, principally because of natural gas price and other risks associated with balancing owned generation supply with sales demand.

TXU Electric Delivery – consists of regulated operations involving the transmission and distribution of electricity in Texas.

Corporate and Other – remaining non-segment operations consisting primarily of discontinued operations, general corporate expenses, equity earnings or losses of unconsolidated affiliates and interest on debt at the TXU Corp. level.

The accounting policies of the segments are the same as those described in the summary of significant accounting policies. TXU Corp. evaluates performance based on income from continuing operations before extraordinary items and cumulative effect of changes in accounting principles. TXU Corp. accounts for intersegment sales and transfers as if the sales or transfers were to third parties, that is, at current market prices.

No customer provided more than 10% of consolidated revenues.

	TXU Energy Holdings	Electric Delivery	Corp. and Other	Eliminations	Consolidated
Operating Revenues					
2004	8,495	2,226	31	(1,444)	9,308
2003	7,986	2,087	16	(1,489)	8,600
2002	7,678	1,994	17	(1,595)	8,094
Regulated Revenues – Included in Operating Revenues					
2004	—	2,226	—	(1,420)	806
2003	—	2,087	—	(1,488)	599
2002	—	1,994	—	(1,582)	412
Affiliated Revenues – Included in Operating Revenues					
2004	3	1,420	21	(1,444)	—
2003	(4)	1,488	5	(1,489)	—
2002	13	1,582	—	(1,595)	—
Depreciation and Amortization					
2004	350	389	21	—	760
2003	407	297	20	—	724
2002	450	264	19	—	733
Equity in Earnings (Losses) of Unconsolidated Subsidiaries					
2004	(5)	(2)	1	7	1
2003	(1)	—	(16)	—	(17)
2002	(2)	—	(105)	—	(107)
Interest Income					
2004	31	56	77	(136)	28
2003	8	52	38	(62)	36
2002	10	49	72	(98)	33
Interest Expense and Other Charges					
2004	353	280	198	(136)	695
2003	323	300	223	(62)	784
2002	215	265	311	(98)	693
Income Tax Expense (Benefit)					
2004	162	116	(236)	—	42
2003	231	126	(105)	—	252
2002	117	117	(157)	—	77
Income from Continuing Operations					
Before Extraordinary Items and Cumulative Effect of Changes in Accounting Principles					
2004	408	255	(582)	—	81
2003	497	258	(189)	—	566
2002	322	245	(462)	—	105
Investment in Equity Investees					
2004	—	—	1	—	1
2003	1	—	1	—	2
2002	3	—	(391)	—	(388)
Total Assets					
2004	14,515	9,493	726	(1,493)	23,241
2003	14,148	9,316	9,508	(1,688)	31,284
2002	15,789	9,015	9,004	(2,424)	31,384

	<u>TXU Energy Holdings</u>	<u>Electric Delivery</u>	<u>Corp. and Other</u>	<u>Eliminations</u>	<u>Consolidated</u>
Capital Expenditures					
2004	281	600	31	—	912
2003	163	543	15	—	721
2002	285	513	15	—	813

*Assets by segment exclude investments in affiliates.

20. SUPPLEMENTARY FINANCIAL INFORMATION

Regulated Versus Unregulated Operations —

	<u>Year Ended December 31,</u>		
	<u>2004</u>	<u>2003</u>	<u>2002</u>
Operating revenues			
Regulated.....	\$ 2,226	\$ 2,087	\$ 1,994
Unregulated.....	8,526	8,002	7,695
Intercompany sales eliminations – regulated.....	(1,420)	(1,488)	(1,582)
Intercompany sales eliminations – unregulated.....	(24)	(1)	(13)
Total operating revenues.....	<u>9,308</u>	<u>8,600</u>	<u>8,094</u>
Costs and operating expenses			
Cost of energy sold and delivery fees – unregulated*.....	3,847	3,640	3,199
Operating costs – regulated.....	730	709	676
Operating costs – unregulated.....	699	680	678
Depreciation and amortization – regulated.....	389	297	264
Depreciation and amortization – unregulated.....	371	427	469
Selling, general and administrative expenses – regulated.....	219	207	213
Selling, general and administrative expenses – unregulated.....	872	700	833
Franchise and revenue-based taxes – regulated.....	248	250	272
Franchise and revenue-based taxes – unregulated.....	119	140	156
Other income.....	(148)	(58)	(41)
Other deductions.....	1,172	42	533
Interest income.....	(28)	(36)	(33)
Interest expense and other charges.....	<u>695</u>	<u>784</u>	<u>693</u>
Total costs and expenses.....	<u>9,185</u>	<u>7,782</u>	<u>7,912</u>
Income from continuing operations before income taxes, extraordinary (gain)/ loss and cumulative effect of changes in accounting principles.....	<u>\$ 123</u>	<u>\$ 818</u>	<u>\$ 182</u>

*Includes unregulated cost of fuel consumed of \$971 million in 2004, \$1,465 million in 2003 and \$1,325 in 2002, respectively. The balance represents energy purchased for resale and delivery fees.

The operations of the TXU Energy Holdings segment are included above as unregulated, as the Texas market is now open to competition. However, retail pricing to residential customers in the historical service territory continues to be subject to certain price controls as discussed in Note 17.

Other Income and Deductions —

	Year Ended December 31,		
	2004	2003	2002
Other income			
Net gain on sale of properties and businesses	\$ 135	\$ 45	\$ 32
Equity portion of allowance for funds used during construction	4	4	3
Other	9	9	6
Total other income	<u>\$ 148</u>	<u>\$ 58</u>	<u>\$ 41</u>
Other deductions			
Loss on sale of properties	\$ 1	\$ —	\$ 2
Asset writedown and lease termination charges	376	—	237
Equity (income) losses of unconsolidated subsidiaries (a)	(1)	17	107
Loss related to telecommunications partnership	—	—	150
Debt extinguishment losses (b)	416	4	27
Litigation charge	84	—	—
Employee severance charges	132	—	—
Termination of power purchase contract	101	—	—
Rate case settlement	21	—	—
Outsourcing transition costs	14	—	—
Transaction-related fees	5	—	—
Expenses related to cancelled construction projects	6	6	7
Premium on redemption of preferred stock	—	3	—
Other	17	12	3
	<u>\$ 1,172</u>	<u>\$ 42</u>	<u>\$ 533</u>

- (a) Of the 2002 amount of \$107 million, \$104 million represents equity in losses of the telecommunications joint venture, which includes \$37 million in impairments of long-lived assets and goodwill.
- (b) Of the 2004 amount of \$416 million, \$8 million represents cost associated with the settlement of equity-linked securities litigation.

Severance Liability Related to Restructuring Activities—

	TXU			
	Energy Holdings	Electric Delivery	Corp. & Other	Total
Liability for severance costs as of January 1, 2004	\$ 2	\$ —	\$ —	\$ 2
Additions to liability	81	14	39	134
Payments charged against liability	(37)	(2)	(33)	(72)
Other adjustments to the liability	(4)	—	(5)	(9)
Liability for severance costs as of December 31, 2004	<u>\$ 42</u>	<u>\$ 12</u>	<u>\$ 1</u>	<u>\$ 55</u>

The above table excludes severance capitalized as a regulatory asset or included in discontinued operations.

Interest Expense and Related Charges —

	Year Ended December 31,		
	2004	2003	2002
Interest (a)	\$ 637	\$ 694	\$ 637
Distributions on exchangeable preferred membership interests of			
TXU Energy Holdings (a)	22	34	—
Interest on long-term debt held by subsidiary trust	19	31	30
Preferred stock dividends of subsidiaries	2	6	9
Amortization of debt discounts, premiums and issuance cost	27	31	29
Capitalized interest including debt portion of allowance for borrowed funds used during construction	(12)	(12)	(12)
Total interest expense and related charges	<u>\$ 695</u>	<u>\$ 784</u>	<u>\$ 693</u>

- (a) Included in interest for the period ended December 31, 2003 is \$34 million related to the exchangeable subordinated notes that were exchanged for preferred membership interests in July 2003. Distributions on preferred membership interests in the 2004 period includes amounts through April 2004, when these securities were purchased by TXU Corp.

Regulatory Assets and Liabilities —

	December 31,	
	2004	2003
Regulatory Assets		
Generation-related regulatory assets securitized by transition bonds	\$ 1,607	\$ 1,654
Securities reacquisition costs	125	121
Recoverable deferred income taxes — net	109	96
Other regulatory assets	<u>153</u>	<u>95</u>
Total regulatory assets	<u>1,994</u>	<u>1,966</u>
Regulatory Liabilities		
Investment tax credit and protected excess deferred taxes	79	88
Over-collection of securitization (transition) bond revenues	23	6
Other regulatory liabilities	<u>1</u>	<u>—</u>
Total regulatory liabilities	<u>103</u>	<u>94</u>
Net regulatory assets	<u>\$ 1,891</u>	<u>\$ 1,872</u>

Included in net regulatory assets are assets of \$121 million at both December 31, 2004 and 2003 that are earning a return. The regulatory assets, other than those subject to securitization, have a remaining recovery period of 15 to 46 years.

Included in other regulatory assets as of December 31, 2004 was \$30 million related to nuclear decommissioning liabilities.

Restricted Cash —

	Balance Sheet Classification	
	At December 31, 2004	
	Current Assets	Investment
Customer collections related to securitization bonds used only to service debt and pay expenses	\$ 43	\$ —
Payment of fees associated with securitization bonds	—	10
Reserve for shortfalls of transition charges	—	3
Collateral for letters of credit	—	19
Demolition and relocation work to be performed by TXU Corp. related to the sale of land	<u>6</u>	<u>15</u>
Total	<u>\$ 49</u>	<u>\$ 47</u>

Accounts Receivable — At December 31, 2004 and December 31, 2003, accounts receivable of \$1.3 billion and \$1.0 billion are stated net of allowance for uncollectible accounts of \$16 million and \$54 million, respectively. During 2004, bad debt expense was \$90 million, account write-offs were \$121 million and other activity decreased the allowance for uncollectible accounts by \$7 million. During 2003, bad debt expense was \$119 million, account write-offs were \$126 million and other activity increased the allowance for uncollectible accounts by \$13 million. Allowances related to receivables sold are reported in current liabilities and totaled \$47 million and \$42 million at December 31, 2004 and 2003, respectively.

Accounts receivable included \$422 million and \$411 million of unbilled revenues at December 31, 2004 and 2003, respectively.

Commodity Contracts — At December 31, 2004 and 2003, current and noncurrent commodity contract assets totaling \$861 million and \$657 million, respectively, are stated net of applicable credit (collection) and performance reserves totaling \$15 million and \$18 million, respectively. Performance reserves are provided for direct, incremental costs to settle the contracts.

Inventories by Major Category —

	December 31,	
	2004	2003
Materials and supplies.....	\$ 169	\$ 258
Fuel stock	79	78
Gas stored underground	<u>72</u>	<u>83</u>
Total inventories	<u>\$ 320</u>	<u>\$ 419</u>

Inventories are carried at average costs and reflect a \$22 million reduction as a result of the rescission of EITF 98-10 as discussed in Note 3.

Property, Plant and Equipment —

	December 31	
	2004	2003
TXU Energy Holdings:		
Generation	\$15,590	\$15,861
Nuclear fuel (net of accumulated amortization of \$998 and \$934).....	118	131
Other assets	492	739
TXU Electric Delivery:		
Transmission	2,544	2,349
Distribution	6,945	6,676
Other assets	371	480
Corporate and Other.....	<u>406</u>	<u>202</u>
Total	26,466	26,438
Less accumulated depreciation	<u>10,228</u>	<u>10,025</u>
Net of accumulated depreciation	16,238	16,413
Construction work in progress	<u>438</u>	<u>390</u>
Net property, plant and equipment	<u>\$16,676</u>	<u>\$16,803</u>

Assets related to capitalized leases included above totaled \$8 million at December 31, 2004 and \$9 million at December 31, 2003, net of accumulated depreciation.

As of December 31, 2004, substantially all of TXU Electric Delivery's electric utility property, plant and equipment (with a net book value of \$6.6 billion) is pledged as collateral on TXU Electric Delivery's first mortgage bonds and senior secured notes.

Intangible Assets — SFAS 142 became effective for TXU Corp. on January 1, 2002. SFAS 142 requires, among other things, the allocation of goodwill to reporting units based upon the current fair value of the reporting units, and the discontinuance of goodwill amortization. SFAS 142 also requires the following additional disclosures regarding intangible assets (other than goodwill) that are amortized or not amortized:

	As of December 31, 2004			As of December 31, 2003		
	Gross			Gross		
	Carrying Amount	Accumulated Amortization	Net	Carrying Amount	Accumulated Amortization	Net
Intangible assets subject to amortization						
included in property, plant and equipment:						
Capitalized software	\$ 364	\$ 294	\$ 70	\$ 512	\$ 248	264
Land easements	173	61	112	176	66	110
Mineral rights and other	<u>31</u>	<u>23</u>	<u>8</u>	<u>31</u>	<u>21</u>	<u>10</u>
Total	<u>\$ 568</u>	<u>\$ 378</u>	<u>\$ 190</u>	<u>\$ 719</u>	<u>\$ 335</u>	<u>\$ 384</u>

Aggregate amortization expense for intangible assets for the years ended December 31, 2004, 2003 and 2002 totaled \$46 million, \$69 million and \$68 million, respectively. At December 31, 2004, the weighted average useful lives of capitalized software, land easements, and mineral rights and other assets were 5 years, 69 years and 40 years, respectively. Estimated amounts of amortization expense for the next five years are as follows:

<u>Year</u>	
2005	\$19
2006	18
2007	15
2008	13
2009	6

Changes in the carrying amount of goodwill (net of accumulated amortization) for the year ended December 31, 2004, are as follows:

	TXU Energy Holdings	TXU Electric Delivery	Total
Balance at December 31, 2003	\$ 533	\$ 25	\$ 558
Disposal of TXU Fuel	<u>(16)</u>	<u>—</u>	<u>(16)</u>
Balance at December 31, 2004	<u>\$ 517</u>	<u>\$ 25</u>	<u>\$ 542</u>

TXU Corp. evaluates goodwill for impairment at least annually (as of October 1) in accordance with SFAS 142. The impairment tests performed are based on discounted cash flow analyses. No goodwill impairment has been recognized for consolidated reporting units reflected in results from continuing operations.

Supplemental Cash Flow Information —

	Year Ended December 31,		
	2004	2003	2002
Cash payments (receipts) related to continuing operations:			
Interest (net of amounts capitalized).....	\$ 695	\$ 720	\$ 635
Income taxes.....	\$ 29	\$ (579)	\$ 3
Cash payments (receipts) related to discontinued operations:			
Interest (net of amounts capitalized).....	\$ 106	\$ 164	\$ 178
Income taxes.....	\$ 47	\$ (18)	\$ (20)
Noncash investing and financing activities:			
Equity-linked securities surrendered to meet obligations under related common stock purchase contracts.....			
	\$ —	\$ —	\$ 238
Discount related to exchangeable preferred membership interests recorded to paid-in-capital.....			
	\$ —	\$ —	\$ 111

The consolidation of Pinnacle was a noncash activity.

See Note 3 for the effects of adopting SFAS 143, which were noncash in nature.

Quarterly Information (unaudited) — The results of operations by quarter are summarized below.

In the opinion of TXU Corp., all other adjustments (consisting of normal recurring accruals) necessary for a fair statement of such amounts have been made. Quarterly results are not necessarily indicative of a full year's operations because of seasonal and other factors.

	Quarter Ended			
	March 31	June 30	Sept. 30	Dec. 31
2004:				
Operating revenues.....	\$ 2,132	\$ 2,303	\$ 2,743	\$ 2,130
Income (loss) from continuing operations before extraordinary gain and cumulative effect of change in accounting principle	\$ 128	\$ (91)	\$ 383	\$ (342)
Exchangeable preferred membership interest buyback premium	\$ —	\$ 849	\$ —	\$ —
Preference stock dividends.....	<u>\$ 5</u>	<u>\$ 5</u>	<u>\$ 5</u>	<u>\$ 6</u>
Net income (loss) available to common stock from continuing operations.....	\$ 123	\$ (945)	\$ 378	\$ (348)
Income (loss) from discontinued operations, net of tax effect	\$ 50	\$ 330	\$ 287	\$ (288)
Extraordinary gain, net of tax effect	\$ —	\$ 16	\$ —	\$ —
Cumulative effect of change in accounting principle, net of tax effect.....	<u>\$ —</u>	<u>\$ —</u>	<u>\$ —</u>	<u>\$ 10</u>
Net income (loss) available for common stock	<u>\$ 173</u>	<u>\$ (599)</u>	<u>\$ 665</u>	<u>\$ (626)</u>
Basic per share of common stock:				
Income (loss) from continuing operations before extraordinary gain and cumulative effect of change in accounting principle	\$.40	\$ (.28)	\$ 1.31	\$ (1.27)
Exchangeable preferred membership interest buyback premium	\$ —	\$ (2.66)	\$ —	\$ —
Preference stock dividends	<u>\$ (.02)</u>	<u>\$ (0.02)</u>	<u>\$ (.02)</u>	<u>\$ (.02)</u>
Net income (loss) available to common stock from continuing operations.....	\$.38	\$ (2.96)	\$ 1.29	\$ (1.29)
Income (loss) from discontinued operations, net of tax effect	\$.16	\$ 1.03	\$.98	\$ (1.07)
Extraordinary gain, net of tax effect	\$ —	\$.05	\$ —	\$ —
Cumulative effect of change in accounting principle, net of tax effect.....	<u>\$ —</u>	<u>\$ —</u>	<u>\$ —</u>	<u>\$.04</u>
Net income (loss) available for common stock	<u>\$.54</u>	<u>\$ (1.88)</u>	<u>\$ 2.27</u>	<u>\$ (2.32)</u>
Diluted per share of common stock:				
Income (loss) from continuing operations before extraordinary gain and cumulative effect of change in accounting principle	\$.37	\$ (.28)	\$.39	\$ (1.27)
Exchangeable preferred membership interest buyback premium	\$ —	\$ (2.66)	\$ —	\$ —
Preference stock dividends	<u>\$ (.01)</u>	<u>\$ (.02)</u>	<u>\$ (.02)</u>	<u>\$ (.02)</u>
Net income (loss) available to common stock from continuing operations.....	\$.36	\$ (2.96)	\$.37	\$ (1.29)
Income (loss) from discontinued operations, net of tax effect	\$.13	\$ 1.03	\$.97	\$ (1.07)
Extraordinary gain, net of tax effect	\$ —	\$.05	\$ —	\$ —
Cumulative effect of change in accounting principle, net of tax effect.....	<u>\$ —</u>	<u>\$ —</u>	<u>\$ —</u>	<u>\$.04</u>
Net income (loss) available for common stock	<u>\$.49</u>	<u>\$ (1.88)</u>	<u>\$ 1.34</u>	<u>\$ (2.32)</u>

Included in fourth quarter 2004 income from continuing operations were losses on retirement of debt of \$352 million (\$334 million after-tax), lease termination costs of \$180 million (\$117 million after-tax) and charges related to the termination of a power purchase contract of \$43 million (\$28 million after-tax). Included in fourth quarter 2004 income from discontinued operations was a settlement charge of \$220 million (\$143 million after-tax) related to potential TXU Europe claims. (See Note 4.)

	Quarter Ended			
	March 31	June 30	Sept. 30	Dec. 31
2003:				
Operating revenues.....	\$ 1,922	\$ 2,157	\$ 2,615	\$ 1,907
Income from continuing operations before cumulative effect of changes in accounting principles.....	\$ 34	\$ 160	\$ 333	\$ 39
Preference stock dividends.....	<u>\$ 5</u>	<u>\$ 6</u>	<u>\$ 5</u>	<u>\$ 6</u>
Net income (loss) available to common stock from continuing operations.....	\$ 29	\$ 154	\$ 328	\$ 33
Income (loss) from discontinued operations, net of tax effect.....	\$ 69	\$ (49)	\$ 64	\$ (10)
Cumulative effect of changes in accounting principles, net of tax effect.....	<u>\$ (58)</u>	<u>\$ —</u>	<u>\$ —</u>	<u>\$ —</u>
Net income available for common stock.....	<u>\$ 40</u>	<u>\$ 105</u>	<u>\$ 392</u>	<u>\$ 23</u>
Basic per share of common stock:				
Income from continuing operations before cumulative effect of changes in accounting principles.....	\$.11	\$.50	\$ 1.04	\$.12
Preference stock dividends.....	<u>\$ (.02)</u>	<u>\$ (.02)</u>	<u>\$ (.02)</u>	<u>\$ (.02)</u>
Net income (loss) available to common stock from continuing operations.....	\$.09	\$.48	\$ 1.02	\$.10
Income (loss) from discontinued operations, net of tax effect.....	\$.22	\$ (.15)	\$.20	\$ (.03)
Cumulative effect of changes in accounting principles, net of tax benefit.....	<u>\$ (.18)</u>	<u>\$ —</u>	<u>\$ —</u>	<u>\$ —</u>
Net income available for common stock.....	<u>\$.13</u>	<u>\$.33</u>	<u>\$ 1.22</u>	<u>\$.07</u>
Diluted per share of common stock:				
Income from continuing operations before cumulative effect of changes in accounting principles.....	\$.11	\$.45	\$.91	\$.12
Preference stock dividends.....	<u>\$ (.01)</u>	<u>\$ (.01)</u>	<u>\$ (.01)</u>	<u>\$ (.01)</u>
Net income (loss) available to common stock from continuing operations.....	\$.10	\$.44	\$.90	\$.11
Income (loss) from discontinued operations, net of tax effect.....	\$.18	\$ (.13)	\$.17	\$ (.04)
Cumulative effect of changes in accounting principles, net of tax benefit.....	<u>\$ (.15)</u>	<u>\$ —</u>	<u>\$ —</u>	<u>\$ —</u>
Net income available for common stock.....	<u>\$.13</u>	<u>\$.31</u>	<u>\$ 1.07</u>	<u>\$.07</u>

Included in fourth quarter 2003 income from discontinued operations were a goodwill impairment charge of \$17 million (\$11 million after-tax) to reflect the fair value of TXU Communications as determined by a sales agreement entered into in January 2004 and a charge of \$13 million (\$9 million after-tax) to impair long-lived assets and accrue liabilities under operating leases from which there will be no future benefit as a result of the decision to exit the business. (See Note 4.)

Reconciliation of Previously Reported Quarterly Information — The following table presents the changes to previously reported quarterly amounts to reflect discontinued operations and the adoption of SFAS 123R.

	Quarter Ended			
	March 31	June 30	Sept. 30	Dec. 31
Increase (Decrease) from Previously Reported				
2004:				
Revenues.....	\$ —	\$ 7	\$ —	\$ —
Income (loss) from continuing operations before extraordinary gain and cumulative effect of change in accounting principle.....	\$ (4)	\$ 1	\$ 3	\$ —
Income (loss) from discontinued operations, net of tax effect.....	\$ —	\$ —	\$ —	\$ —
Net income (loss).....	\$ (4)	\$ 1	\$ 3	\$ —
Net income (loss) available for common stock.....	\$ (4)	\$ 1	\$ 3	\$ —