

**ITEM 7. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS**

The following analysis of the results of operations and financial condition of PPL Montana is abbreviated as PPL Montana meets the conditions set forth in General Instruction (I)(1)(a) and (b) of Form 10-K. Such analysis should be read in conjunction with the financial statements in Item 8. Terms and abbreviations appearing here are explained in the glossary.

**Results of Operations**

The following discussion explains significant changes in principal items on the Statement of Income comparing 2003 to 2002. The Statement of Income reflects the results of past operations and is not intended as any indication of future operating results. Future operating results will necessarily be affected by various and diverse factors and developments.

**Earnings**

Net income increased by \$21 million in 2003 compared with 2002. The increase was primarily due to higher wholesale prices in the western U.S and an increase in generation.

**Operating Revenues**

Operating revenues increased by \$48 million in 2003 compared with 2002. The increase was primarily due to an increase in wholesale energy prices of \$27 million and an increase in volume sold of \$21 million.

**Operating Expenses**

Operating expenses increased by \$26 million in 2003 compared with 2002. Operating expenses consist mainly of expenses for fuel, energy purchases, transmission tariffs, plant operations and maintenance, lease rental payments, and general and administrative expenses. The increase was primarily due to higher energy purchases of \$11 million, related to the higher power costs in the western U.S. and higher volumes of \$9 million.

Generation increased by 345 million kWh during 2003 compared with 2002. This increase was primarily the result of improved operational performance from the coal-fired generation units.

**New Accounting Standards**

See Note 22 to the Financial Statements for information on new accounting standards adopted in 2003 or pending adoption.

**Risk Management - Energy Marketing & Trading and Other****Market Risk***Background*

Market risk is the potential loss PPL Montana may incur as a result of price changes associated with a particular financial or commodity instrument. PPL Montana is exposed to market risk from commodity price risk for energy and energy-related products associated with the sale of electricity, the purchase of fuel for the generating assets, and energy trading activities.

PPL Montana has a risk management policy approved by PPL's Board of Directors to manage market risk and counterparty credit risk. (Credit risk is discussed below.) The RMC, comprised of senior management and chaired by the Vice President-Risk Management, oversees the risk management function. Key risk control activities designed to monitor compliance with risk policies and detailed programs include, but are not limited to, credit review and approval, validation of transactions and market prices, verification of risk and transaction limits, sensitivity analyses, and daily portfolio reporting, including open positions, mark-to-market valuations, and other risk measurement metrics. In addition, efforts are ongoing to develop systems to improve the timeliness, quality and breadth of market and credit risk information.

The forward-looking information presented below provides estimates of what may occur in the future, assuming certain adverse market conditions, due to reliance on model assumptions. Actual future results may differ materially from those presented. These disclosures are not precise indicators of expected future losses, but only indicators of reasonably possible losses.

*Contract Valuation*

PPL Montana utilizes forward contracts, options and swaps as part of its risk management strategy to minimize unanticipated fluctuations in earnings caused by commodity price volatility. When available, quoted market prices are used to determine the fair value of a commodity or financial instrument. This may include exchange prices, the average mid-point bid/ask spreads obtained from brokers, or an independent valuation by an external source, such as a bank. However, market prices for energy or energy-related contracts may not be readily determinable because of market illiquidity. If no active trading market exists, contracts are valued using internally developed models, which are then reviewed by an independent, internal group. Although PPL Montana believes that its valuation methods are reasonable, changes in the underlying assumptions could result in significantly different values and realization in future periods.

To record derivatives at their fair value, PPL Montana discounts the forward values using LIBOR. Additionally, PPL Montana reduces derivative assets' carrying value to recognize differences in counterparty credit quality and potential illiquidity in the market.

- The credit adjustment takes into account the probability of default, as calculated by an independent service, for each counterparty that has an out-of-the money position with PPL Montana.
- The liquidity adjustment takes into account the fact that it may not be appropriate to value contracts at the midpoint of the bid/ask spread. PPL Montana might have to accept the "bid" price if PPL Montana wanted to close an open sales position or PPL Montana might have to accept the "ask" price if PPL Montana wanted to close an open purchase position.

#### *Accounting and Reporting*

PPL Montana follows the provisions of SFAS 133, "Accounting for Derivative Instruments and Hedging Activities," as amended by SFAS 138, "Accounting for Certain Derivative Instruments and Certain Hedging Activities," and SFAS 149, "Amendment of Statement 133 on Derivative Instrument and Hedging Activities," interpreted by DIG issues (together, "SFAS 133"), EITF 02-3, "Issues Involved in Accounting for Derivative Contracts Held for Trading Purposes and Contracts Involved in Energy Trading and Risk Management Activities," and EITF 03-11, "Reporting Realized Gains and Losses on Derivative Instruments That Are Subject to FASB Statement No. 133 and Not 'Held for Trading Purposes' as Defined in Issue No. 02-3," to account for and report on contracts entered into to manage market risk. SFAS 133 requires that all derivative instruments be recorded at fair value on the balance sheet as an asset or liability (unless they meet SFAS 133's criteria for exclusion) and that changes in the derivative's fair value be recognized currently in earnings unless specific hedge accounting criteria are met.

In April 2003, the FASB issued SFAS 149, which amends and clarifies SFAS 133 to improve financial accounting and reporting for derivative instruments and hedging activities. To ensure that contracts with comparable characteristics are accounted for similarly, SFAS 149 clarifies the circumstances under which a contract with an initial net investment meets the characteristics of a derivative, clarifies when a derivative contains a financing component, amends the definition of an "underlying" and amends certain other existing pronouncements. Additionally, SFAS 149 placed additional limitations on the use of the normal purchase or normal sale exception. SFAS 149 was effective for contracts entered into or modified and for hedging relationships designated after June 30, 2003, except certain provisions relating to forward purchases or sales of when-issued securities or other securities that did not yet exist. PPL Montana adopted SFAS 149 as of July 1, 2003. The adoption of SFAS 149 did not have a significant impact on PPL Montana.

PPL Montana adopted the final provisions of EITF 02-3 during the fourth quarter of 2002. As such, PPL Montana now reflects its net realized and unrealized gains and losses associated with all derivatives that are held for trading purposes in the "Net energy trading margins" line on the Statement of Income. Derivative contracts that met the definition of energy trading activities as defined by EITF 98-10, "Accounting for Energy Trading and Risk Management Activities" are reflected in the financial statements using the accrual method of accounting. Under the accrual method of accounting, unrealized gains and losses are not reflected in the financial statements. Prior periods were reclassified. No cumulative effect adjustment was required upon adoption.

PPL Montana has adopted the final provisions of EITF 03-11 prospectively as of October 1, 2003. As a result of this adoption, non-trading bilateral sales of electricity at major market delivery points are netted with purchases that offset the sales at those same delivery points. A major market delivery point is any delivery point with liquid pricing available. See Note 17 to the Financial Statements for the impact of adopting EITF 03-11.

PPL Montana's short-term derivative contracts are recorded as "Price risk management assets" and "Price risk management liabilities" on the Balance Sheet. Long-term derivative contracts are included in "Noncurrent Assets - Other" and "Noncurrent Liabilities - Other."

#### *Accounting Designation*

Energy contracts that do not qualify as derivatives receive accrual accounting. For energy contracts that meet the definition of a derivative, the circumstances and intent existing at the time that energy transactions are entered into determine their accounting designation. These designations are verified by PPL Montana's risk control group on a daily basis. The following is a summary of the guidelines that have been provided to the traders who are responsible for contract designation for derivative energy contracts due to the adoption of SFAS 149:

- Any wholesale and retail contracts to sell or buy electricity and the related capacity that are expected to be delivered from PPL Montana's generation or that are approved by the RMC to fulfill a strategic element of PPL Montana's overall marketing strategy are considered "normal." These transactions are not recorded in the financial statements and have no earnings impact until delivery.
- Physical electricity-only transactions can receive cash flow hedge treatment if all of the qualifications under SFAS 133 are met. Any unrealized gains or losses on transactions receiving cash flow hedge treatment are recorded in other comprehensive income. These unrealized gains and losses become realized when the contracts settle and are recognized in income when the hedged transactions occur.

- Physical electricity purchases that increase PPL Montana's long position and any energy sale or purchase judged a "market call" are considered speculative, with unrealized gains or losses recorded immediately through earnings.

Financial transactions, which can be settled in cash, cannot be considered "normal" because they do not require physical delivery. These transactions receive cash flow hedge treatment if they lock-in the price PPL Montana will receive or pay for energy expected to be generated or purchased in the spot market. Any unrealized gains or losses on transactions that receive cash flow hedge treatment are recorded in other comprehensive income. These unrealized gains and losses become realized when the contracts settle and are recognized in income when the hedged transactions occur.

- Option contracts that do not meet the requirements of DIG Issue C15, "Scope Exceptions: Interpreting the Normal Purchases and Normal Sales Exception as an Election," do not receive hedge accounting treatment and are marked to market through earnings.

#### Commodity Price Risk

Commodity price risk is one of PPL Montana's most significant risks due to the level of investment that PPL Montana maintains in its generation assets, coupled with the volatility of prices for energy and energy-related products. Several factors influence price levels and volatilities. These factors include, but are not limited to, seasonal changes in demand, weather conditions, available generating assets within regions, transportation availability and reliability within and between regions, market liquidity, and the nature and extent of current and potential federal and state regulations. To hedge the impact of market price fluctuations on PPL Montana's energy-related assets, liabilities and other contractual arrangements, PPL EnergyPlus sells and purchases physical energy at the wholesale level under FERC market-based tariffs throughout the U.S. and enters into financial exchange-traded and over-the-counter contracts. Because of the generating assets PPL Montana owns or controls, the majority of PPL Montana's energy transactions qualify for accrual or hedge accounting.

Within PPL Montana's hedge portfolio, the decision to enter into energy contracts hinges on the expected value of PPL Montana's generation. To address this risk, PPL Montana takes a conservative approach in determining the number of MWhs that are available to be sold forward. In this regard, PPL Montana reduces the maximum potential output that a plant may produce by three factors - planned maintenance, unplanned outages and economic conditions. The potential output of a plant is first reduced by the amount of unavailable generation due to planned maintenance on a particular unit. Another reduction, representing the unplanned outage rate, is the amount of MWhs that historically are not produced by a plant due to such factors as equipment breakage. Finally, the potential output of certain plants (like peaking units) are reduced because their higher cost

of production will not allow them to economically run during all hours.

At times, PPL Montana's non-trading portfolio includes full requirements energy contracts. The obligation to serve these contracts changes minute by minute. PPL Montana analyzes historical on-peak and off-peak usage patterns, as well as spot prices and weather patterns, to determine a monthly level of block electricity that best fits the usage patterns in order to minimize earnings volatility. On a forward basis, PPL Montana reserves a block amount of generation for full requirements energy contracts that is expected to be the best match with their anticipated usage patterns and energy peaks. Anticipated usage patterns and peaks are affected by expected load growth, regional economic drivers and seasonality.

PPL Montana's commodity derivative contracts that qualify for hedge accounting treatment mature at various times through 2010. The following chart sets forth PPL Montana's net fair market value of these contracts as of December 31, 2003:

	<u>Gains</u>
Fair value of contracts outstanding at the beginning of the year	\$ 11
Contracts realized or otherwise settled during the year	1
Fair value of new contracts at inception	
Other changes in fair values	<u>10</u>
Fair value of contracts outstanding at the end of the year	<u>\$ 22</u>

During 2003, PPL Montana realized or otherwise settled net losses of approximately \$1 million related to contracts entered into prior to January 1, 2003. This amount does not reflect intra-quarter contracts that were entered into and settled during the period.

"Other changes in fair values," a gain of approximately \$10 million, represent changes in the market value that occurred during 2003 for contracts that were outstanding at the end of 2003.

The following chart segregates estimated fair values of PPL Montana commodity derivative contracts that qualify for hedge accounting treatment at December 31, 2003 based on whether the fair values are determined by quoted market prices or other more subjective means.

**Fair Value of Contracts at Period-End  
Gains/(Losses)**

Source of Fair Value	Maturity Less Than 1 Year	Maturity 1-3 Years	Maturity 3-5 Years	Maturity in Excess of 5 Years	Total Fair Value
Prices actively quoted					
Prices provided by other external sources	\$ 11	\$ 12	\$ (1)		\$ 22
Prices based on models and other valuation methods					
Fair value of contracts outstanding at the end of the period	<u>\$ 11</u>	<u>\$ 12</u>	<u>\$ (1)</u>		<u>\$ 22</u>

The "Prices provided by other external sources" category includes PPL Montana's forward positions and options in natural gas and power and natural gas basis swaps at points for which over-the-counter (OTC) broker quotes are available. The fair values of electricity positions recorded above use the midpoint of the bid/ask spreads obtained through OTC brokers. On average, OTC quotes for forwards and swaps of natural gas and power extend one and two years into the future.

The "Prices based on models and other valuation methods" category includes the value of transactions for which an internally developed price curve was constructed as a result of the long-dated nature of the transaction or the illiquidity of the market point, or the value of options not quoted by an exchange or OTC broker. Additionally, this category includes "strip" transactions whose prices are obtained from external sources and then modeled to monthly prices as appropriate.

Because of PPL Montana's efforts to hedge the value of the energy from its generation assets, PPL Montana has open contractual positions. If PPL Montana were unable to deliver firm capacity and energy under its agreements, under certain circumstances it would be required to pay damages. These damages would be based on the difference between the market price to acquire replacement capacity or energy and the contract price of the undelivered capacity or energy. Depending on price volatility in the wholesale energy markets, such damages could be significant. Extreme weather conditions, unplanned power plant outages, transmission disruptions, non-performance by counterparties (or their counterparties) with which it has power contracts and other factors could affect PPL Montana's ability to meet its firm capacity or energy obligations, or cause significant increases in the market price of replacement capacity and energy. Although PPL Montana attempts to mitigate these risks, there can be no assurance that it will be able to fully meet its firm obligations, that it will not be required to pay damages for failure to perform, or that it will not experience counterparty non-performance in the future.

As of December 31, 2003, PPL Montana estimated that a 10% adverse movement in market prices across all geographic areas and time periods would have decreased the value of the commodity contracts in its non-trading portfolio by

approximately \$80 million, as compared to a decrease of \$76 million at December 31, 2002. However, the change in the value of the non-trading portfolio would have been substantial offset by an increase in the value of the underlying commodity the electricity generated, because these contracts serve to the market risk inherent in the generation of electricity. Additionally, the value of PPL Montana's unsold generation would be improved. Because PPL Montana's electricity portfolio is generally in a net sales position, the adverse movement in prices is usually an increase in prices.

PPL Montana also executes energy contracts to take advantage of market opportunities. As a result, PPL Montana may at times create a net open position in its portfolio that could result in significant losses if prices do not move in the manner or direction anticipated. The margins from these trading activities are shown in the Statement of Income as "Net energy trading margins."

PPL Montana's trading contracts mature at various times through 2004. PPL Montana's net fair market value of trading contracts as of December 31, 2003 and 2002 was insignificant.

As of December 31, 2003, the net loss on PPL Montana's trading activities expected to be recognized in earnings during the next three months is insignificant.

PPL Montana estimated that a 10% adverse movement in market prices across all geographic areas and time periods would have decreased the value of the commodity contracts in its trading portfolio by an insignificant amount at December 31, 2003 and 2002.

#### Interest Rate Risk

PPL Montana may use borrowings to provide funds for its operations. PPL and PPL Energy Supply may utilize various financial derivative products and risk management techniques on behalf of PPL Montana to adjust the mix of fixed and floating interest rates in PPL Montana's debt portfolio and thereby reduce its exposure to adverse interest rate movements. PPL Montana had no borrowings outstanding as of December 31, 2003.

#### Credit Risk

Credit risk relates to the risk of loss that PPL Montana would incur as a result of non-performance by counterparties of their contractual obligations. PPL Montana maintains credit policies and procedures with respect to counterparties (including requirements that counterparties maintain certain credit ratings criteria) and requires other assurances in the form of credit support or collateral in certain circumstances in order to limit counterparty credit risk. However, PPL Montana has concentrations of suppliers and customers among electric utilities and other energy marketing and trading companies. These concentrations of counterparties may impact PPL Montana's overall exposure to credit risk, either positively or negatively, in that counterparties may be similarly affected by

changes in economic, regulatory or other conditions. As discussed above under "Contract Valuation," PPL Montana records certain non-performance reserves to reflect the probability that a counterparty with contracts that are out of the money (from the counterparty's standpoint) will default in its performance, in which case PPL Montana would have to sell into a lower-priced market or purchase from a higher-priced market. These reserves are reflected in the fair value of assets recorded in "Price risk management assets" on the Balance Sheet. PPL Montana also records reserves to reflect the probability that a counterparty will not make payments for deliveries PPL Montana has made but not yet billed. These reserves are reflected in "Unbilled revenues" on the Balance Sheet. PPL Montana has also established a reserve with respect to certain sales to the California ISO for which PPL Montana has not yet been paid. See Note 14 to the Financial Statements.

## Competition

See Item 1, "Business - Competition," for additional information.

### Application of Critical Accounting Policies

PPL Montana's financial condition and results of operations are impacted by the methods, assumptions and estimates used in the application of critical accounting policies. The following accounting policies are particularly important to the financial condition or results of operations of PPL Montana, and require estimates or other judgments of matters inherently uncertain. Changes in the estimates or other judgments included within these accounting policies could result in a significant change to the information presented in the financial statements. (These accounting policies are also discussed in Note 1 to the Financial Statements.) PPL's senior management has reviewed these critical accounting policies, and the estimates and assumptions regarding them, with its Audit Committee. In addition, PPL's senior management has reviewed the following disclosures regarding the application of these critical accounting policies with the Audit Committee.

#### 1) Price Risk Management

See "Risk Management - Energy Marketing & Trading and Other" above.

#### 2) Pension and Other Postretirement Benefits

PPL Montana follows the guidance of SFAS 87, "Employers' Accounting for Pensions," and SFAS 106, "Employers' Accounting for Postretirement Benefits Other Than Pensions," when accounting for these benefits. Under these accounting standards, assumptions are made regarding the valuation of benefit obligations and performance of plan assets. Delayed recognition of differences between actual results and expected or estimated results is a guiding principle of these standards. This delayed recognition of actual results allows for a smoothed recognition of changes in benefit obligations and plan performance over the working lives of the employees who

benefit under the plans. The primary assumptions are as follows:

- **Discount Rate** - The discount rate is used in calculating the present value of benefits, which are based on projections of benefit payments to be made in the future.
- **Expected Return on Plan Assets** - Management projects the future return on plan assets considering prior performance, but primarily based upon the plans' mix of assets and expectations for the long-term returns on those asset classes. These projected returns reduce the net benefit costs the company will record currently.
- **Rate of Compensation Increase** - Management projects employees' annual pay increases, which are used to project employees' pension benefits at retirement.
- **Health Care Cost Trend Rate** - Management projects the expected increases in the cost of health care.

In selecting discount rates, PPL Montana considers fixed-income security yield rates. At December 31, 2003, PPL Montana decreased the discount rate from 6.75% to 6.25% as a result of decreased fixed-income security returns.

In selecting an expected return on plan assets, PPL Montana considers past performance and economic forecasts for the types of investments held by the plan. At December 31, 2003, PPL Montana's expected return on plan assets remained at 9.0%.

In selecting a rate of compensation increase, PPL Montana considers past experience in light of movements in inflation rates. At December 31, 2002, PPL Montana's rate of compensation increase remained at 4.00%.

In selecting health care cost trend rates, PPL Montana considers tax implications, past performance and forecasts of health care costs. At December 31, 2003, PPL Montana's health care cost trend rates were 11% for 2004, gradually declining to 5.0% for 2010.

A variance in the assumption listed above could have a significant impact on the projected benefit obligations, accrued pension and other postretirement benefit liabilities, reported annual net periodic pension and other postretirement benefit cost and other comprehensive income (OCI).

A 25 basis point reduction in the discount rate would increase the projected benefit obligations and pre-tax OCI charge by \$2 million and would have an insignificant impact on the accrued pension and other postretirement benefit liabilities (excluding additional minimum liability) and reported annual net periodic pension and other postretirement benefit cost. A 100 basis point increase in the health care cost trend rate would increase the projected benefit obligations by \$1 million and would have an insignificant impact on the accrued pension and other postretirement benefit liabilities and the annual net periodic pension and other postretirement benefit cost. A 25 basis point

change in the expected return on plan assets or rate of compensation increase would have an insignificant impact on the projected benefit obligations, accrued pension and other postretirement benefit liabilities, reported annual net periodic pension and other postretirement benefit cost and OCI. While the information above reflects either an increase or decrease in each assumption, the inverse of this change would have a similar impact in the opposite direction. Each sensitivity above reflects an evaluation of the change based solely on a change in that assumption.

At December 31, 2003, PPL Montana had recognized accrued pension and other postretirement benefit liabilities of \$16 million, included in "Noncurrent Liabilities - Other" on the Balance Sheet. PPL Montana's total projected obligation for these benefits was approximately \$66 million, but was offset by \$46 million of assets held in a pension trust.

In 2003, PPL Montana recognized net periodic pension and other postretirement costs charged to operating expenses of \$6 million, excluding amounts credited to construction and other non-expense accounts. This amount is comparable to the expense recognized during 2002.

During 2003, PPL Montana made contributions to its pension plan totaling \$15 million. As a result, PPL Montana was able to decrease its recognized additional minimum pension liability. Recording the reduction in the additional minimum pension liability resulted in a decrease to the pension-related charge to OCI, net of taxes, of \$1 million. This adjustment decreased the pension-related balance in OCI, which is a reduction to Member's Equity, to \$5 million at December 31, 2003. The charges to OCI will reverse in future periods if the fair value of trust assets exceeds the accumulated benefit obligation.

Refer to Note 12 to the Financial Statements for additional information regarding pension and other postretirement benefits.

### 3) Leasing

PPL Montana applies the provisions of SFAS 13, "Accounting for Leases," to all leasing transactions. In addition, PPL Montana applies the provisions of numerous other accounting pronouncements issued by the FASB and the EITF that provide specific guidance and additional requirements related to accounting for various leasing arrangements. In general, there are two types of leases from a lessee's perspective: operating leases - leases accounted for off-balance sheet and capital leases - leases capitalized on the balance sheet.

In accounting for leases, management makes various assumptions, including the discount rate, the fair market value of the leased assets and the estimated useful life, in determining whether a lease should be classified as operating or capital. Changes in these assumptions could result in the difference between whether a lease is determined to be an operating lease or a capital lease, thus significantly impacting the amounts to be recognized in the financial statements.

In addition to uncertainty inherent in management's assumptions, leasing transactions and the related accounting rules become increasingly complex when they involve: sale/leaseback accounting (leasing transactions where the lessee previously owned the leased assets), synthetic leases (leases that qualify for operating lease treatment for book accounting purposes and financing treatment for tax accounting purposes) and lessee involvement in the construction of leased assets.

At December 31, 2003, PPL Montana subsidiaries participated in one significant sale/leaseback transaction. This transaction has been accounted for as an operating lease.

### Sale/Leaseback

In July 2000, PPL Montana sold its interest in the Colstrip generating plant to owner lessors who are leasing the assets back to PPL Montana under four 36-year operating leases. This transaction is accounted for as an operating lease in accordance with current rules related to sale/leaseback arrangements. If for any reason this transaction did not meet the requirements for off-balance sheet operating lease treatment as a sale/leaseback, PPL Montana would have approximately \$315 million of additional assets and liabilities recorded on its balance sheet at December 31, 2003 and would have recorded additional expenses currently estimated at \$9 million, after-tax, in 2003.

See Note 10 to the Financial Statements for additional information related to operating leases.

### 4) Loss Contingencies

PPL Montana periodically records the estimated impacts of various conditions, situations or circumstances involving uncertain outcomes. These events are called "contingencies," and PPL Montana's accounting for such events is prescribed by SFAS 5, "Accounting for Contingencies." SFAS 5 defines a contingency as "an existing condition, situation, or set of circumstances involving uncertainty as to possible gain or loss to an enterprise that will ultimately be resolved when one or more future events occur or fail to occur."

For loss contingencies, the loss must be accrued if (1) information is available that indicates it is "probable" that the loss has been incurred, given the likelihood of the uncertain future events; and (2) the amount of the loss can be reasonably estimated. FASB defines "probable" as cases in which "the future event or events are likely to occur." SFAS 5 does not permit the accrual of contingencies that might result in gains.

The accrual of a loss contingency involves considerable judgment on the part of management. The accounting aspects of loss contingencies include: (1) the initial identification and recording of the loss contingency; (2) the determination of a triggering event for reducing a recorded loss contingency; and (3) the on-going assessment as to whether a recorded loss contingency is reasonable.

## Initial Identification and Recording of the Loss Contingency

PPL Montana uses its internal expertise, and outside experts (such as lawyers, tax specialists and engineers), as necessary, to help estimate the probability that a loss has been incurred and the amount (or range) of the loss. PPL Montana continuously assesses potential loss contingencies for environmental remediation, litigation claims, regulatory penalties and other events.

PPL Montana has identified certain events which could give rise to a loss, but which do not meet the conditions for accrual under SFAS 5. SFAS 5 requires disclosure, but not a recording, of potential losses when it is "reasonably possible" that a loss has been incurred. FASB defines "reasonably possible" as cases in which "the chance of the future event or events occurring is more than remote but less than likely." See Note 14 to the Financial Statements for disclosure of potential loss contingencies, most of which have not met the criteria for accrual under SFAS 5.

## Reducing Recorded Loss Contingencies

When a loss contingency is recorded, PPL Montana identifies the triggering event for subsequently reducing the loss contingency. The triggering events generally occur when the contingency has been resolved and the actual loss is incurred or the risk of loss has diminished or been eliminated. The following are some of the triggering events which provide for the reduction of certain recorded loss contingencies:

- Certain loss contingencies are systematically reduced based on the expiration of contract terms. An example of this is the recorded liability for above-market purchase contracts, as described below.
- Allowances for excess or obsolete inventory are reduced as the inventory items are pulled from the warehouse shelves and sold as scrap or otherwise disposed.
- Allowances for uncollectible accounts are reduced when accounts are written off after prescribed collection procedures have been exhausted.
- Environmental loss contingencies are reduced when PPL Montana makes payments for environmental remediation.

## On-Going Assessment of Recorded Loss Contingencies

PPL Montana reviews its loss contingencies on a regular basis to assure that the recorded potential loss exposures are reasonable. This involves ongoing communication and analyses with internal and external legal counsel, engineers, tax specialists, managers in various operational areas and other parties.

All three aspects of accounting for loss contingencies - the initial identification and recording of a probable loss, the

identification of triggering events to reduce the loss contingency, and the ongoing assessment of the reasonableness of a recorded loss contingency - require significant judgment by PPL Montana's management.

The largest contingency currently on PPL Montana's balance sheet is the loss contingency for the above-market purchase contract being the difference between the out-of-market contract terms and the fair value of the energy. This loss contingency was originally recorded at \$59 million in 1999, when PPL Montana purchased the assets of Montana Power and assumed the contract. Under purchase accounting, PPL Montana recorded the out-of-market cost of the purchase contract. This loss contingency for the out-of-market contract was recorded because it was probable that the loss had been incurred and the loss could be reasonably estimated, using forward pricing information. The out-of-market loss contingency was \$57 million at December 31, 2003.

When the loss contingency related to the contract was recorded in 1999, PPL Montana established the triggering events for when the loss contingency would be reduced. A schedule was established to reduce the liability based on projected purchases over the life of the contract which expires in 2010. The liability is being reduced over the agreement terms as an adjustment to "Energy purchases" on the Statement of Income.

PPL Montana assessed the remaining \$57 million out-of-market liability at December 31, 2003, comparing the energy purchases under the terms of the contract, with the purchases assuming market prices for the energy.

Market prices for the contract were derived by using internal forward energy price curves. The forward energy price curves in this scenario were based on the revenue and sales information for 2004 through 2010, as comprehended in the current business plan of PPL Montana. The assessment also used sensitivities around the forward energy prices, adjusting such prices upwards and downwards by 10%.

The assessment was dependent on forward energy prices and the projected purchase levels of the contract. The forward prices of energy are dependent on many variables, including growth in electricity demand, available generation, and general economic conditions. Changes in these and other factors can have a dramatic impact on future electricity prices. Accordingly, forward energy price sensitivities were used in the assessment. If estimated forward market prices were adjusted upwards by 10% in each of the years from 2004 through 2010, the contract would have an estimated liability of \$48 million. Conversely, if estimated forward market prices were adjusted downwards by 10% during the remaining term of the contract, the contract would have an estimated liability of \$61 million. The recorded contingency of \$57 million falls within the range calculated in the year-end assessment. As noted above, it is very difficult to estimate future electricity prices, which are dependent on many variables and subject to significant volatility. PPL Montana's management believes that the current recorded liability was fairly stated at December 31, 2003.

In connection with the December 2001 bankruptcy filings by Enron Corporation and its affiliates (collectively "Enron"), PPL Montana terminated certain electricity, gas and other trading agreements with Enron. At the time that these trading agreements were terminated, they were at prices more favorable to PPL Montana than current market prices, and PPL Montana established a reserve for uncollectible accounts of \$29 million. In October 2002, PPL Montana filed proofs of claim in Enron's bankruptcy proceedings for \$29 million. These claims were against Enron North America and Enron Power Marketing (the "Enron Subsidiaries"), and against Enron Corporation, which had guaranteed the Enron Subsidiaries' performance (the "Enron Corporation Guarantees").

During 2003, PPL Montana and Enron engaged in discussions regarding the amount of claims that would be allowed against the Enron Subsidiaries. Although no formal agreement on such amounts has been reached, based on informal discussions with Enron's counsel, PPL Montana believes that its claims against the Enron Subsidiaries will eventually be allowed in the bankruptcy at approximately \$25 million. Accordingly, PPL

Montana reduced its receivables from Enron, and the associated reserve for uncollectible accounts, by \$4 million. PPL Montana also determined that it is probable that it will recover approximately \$6 million of these receivables from the Enron Subsidiaries, and may collect additional amounts under the Enron Corporation Guarantees. Therefore, PPL Montana determined that it was appropriate to reduce its reserve by an additional \$6 million. PPL Montana will continue to reassess the reserve for uncollectible accounts associated with its receivables from Enron.

#### **Other Information**

PPL's Audit Committee has approved the independent auditor provide audit and audit-related services and other services permitted by the Sarbanes-Oxley Act of 2002 and SEC rules. The audit and audit-related services include services in connection with statutory and regulatory filings, reviews of offering documents and registration statements, employee benefit plan audits and internal control reviews.

### **ITEM 7A. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK**

**PPL Corporation, PPL Energy Supply, LLC, PPL Electric Utilities Corporation and PPL Montana, LLC**

Reference is made to "Risk Management - Energy Marketing & Trading and Other" in Management's Discussion and Analysis of Financial Condition and Results of Operations.

**PPL Corporation**  
**Management's Report on Responsibility for Financial Statements**

PPL management is responsible for the preparation, integrity and objectivity of the consolidated financial statements and all other information in this annual report. The financial statements were prepared in accordance with accounting principles generally accepted in the United States of America and include amounts based on management's best estimates and judgments where necessary. Management believes that the financial statements are free of material misstatements and present fairly the financial position, results of operations and cash flows of PPL.

**PPL management is responsible** for establishing and maintaining an effective internal control structure and effective disclosure controls and procedures for financial reporting. PPL maintains a system of internal control that is designed to provide reasonable assurance that PPL assets are safeguarded from loss or unauthorized use or disposition and that transactions are executed in accordance with management's authorization and are properly recorded to permit the preparation of financial statements in accordance with generally accepted accounting principles. This system is augmented by a careful selection and training of qualified personnel, specific delegations of authority, a proper division of responsibilities, and utilization of written policies and procedures. An internal audit program monitors the effectiveness of this control system. Management believes that its internal control structure and its disclosure controls and procedures for financial reporting are adequate and effective.

The Audit Committee of the Board of Directors consists entirely of independent directors who are not employees of PPL. The Audit Committee reviews audit plans related to PPL's internal controls, financial reports and related matters and meets regularly with management as well as the independent auditors and internal auditors. The independent auditors and the internal auditors have free access to the Audit Committee, without management present, to discuss internal accounting control, auditing and financial reporting matters.

PricewaterhouseCoopers LLP, the independent certified public accountants, audited PPL's consolidated financial statements and issued their opinion above.

PPL management also recognizes its responsibility for fostering a strong ethical climate so that it conducts its business affairs according to the highest standards of personal and corporate conduct.



William F. Hecht  
*Chairman, President and Chief Executive Officer*



John R. Biggar  
*Executive Vice President and Chief Financial Officer*

**Report of Independent Auditors**

To the Board of Directors and Shareowners of  
PPL Corporation:

In our opinion, the consolidated financial statements listed in the index appearing under Item 8 on page 95 present fairly, in all material respects, the financial position of PPL Corporation and its subsidiaries ("PPL") at December 31, 2003 and 2002, and the results of their operations and their cash flows for each of the three years in the period ended December 31, 2003 in conformity with accounting principles generally accepted in the United States of America. In addition, in our opinion, the financial statement schedule listed in the index appearing under Item 8 presents fairly, in all material respects, the information set forth therein when read in conjunction with the related consolidated financial statements. These financial statements and financial statement schedule are the responsibility of the Company's management; our responsibility is to express an opinion on these financial statements and financial statement schedule based on our audits. We conducted our audits of these statements in accordance with auditing standards generally accepted in the United States of America, which require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

As discussed in Note 17 to the consolidated financial statements, PPL changed its method of accounting for derivative and hedging activities pursuant to Statement of Financial Accounting Standards ("SFAS") No. 133, *Accounting for Derivative Instruments and Hedging Activities*, as amended by SFAS No. 138, *Accounting for Certain Derivative Instruments and Certain Hedging Activities (an amendment of FASB Statement 133)*, in 2001. As discussed in Note 12 to the consolidated financial statements, PPL also changed its method of accounting for the amortization of unrecognized gains or losses in the annual pension expense/income determined under SFAS No. 87, *Employers' Accounting for Pensions*, in 2001. As discussed in Note 18 to the consolidated financial statements, PPL adopted SFAS No. 142, *Goodwill and Other Intangible Assets*, in 2002. As discussed in Note 21 to the consolidated financial statements, PPL adopted SFAS No. 143, *Accounting for Asset Retirement Obligations*, in 2003. As discussed in Note 22 to the consolidated financial statements, PPL adopted SFAS No. 150, *Accounting for Certain Financial Instruments with Characteristics of both Liabilities and Equity*, Emerging Issues Task Force No. 03-11, *Reporting Realized Gains and Losses on Derivative Instruments That Are Subject to FAS 133 and Not "Held for Trading Purposes" as Defined in Issue No. 02-3*, FASB Interpretation ("FIN") No. 45, *Guarantor's Accounting and Disclosure Requirements for Guarantees, Including Indirect Guarantees of Indebtedness of Others*, and FIN No. 46, *Consolidation of Variable Interest Entities – an interpretation of ARB 51*, as amended by FIN 46(R), in 2003. In addition, as discussed in Note 1 to the consolidated financial statements, PPL elected the fair value method of accounting for stock-based compensation as prescribed by SFAS 123, *Accounting for Stock-Based Compensation*, as amended by SFAS No. 148, *Accounting for Stock-Based Compensation Transition and Disclosure, an Amendment of FASB Statement No. 123*, in 2003.



February 2, 2004

**PPL Energy Supply, LLC**  
**Management's Report on Responsibility for Financial Statements**

PPL Energy Supply management is responsible for the preparation, integrity and objectivity of the consolidated financial statements and other information in this annual report. The financial statements were prepared in accordance with accounting principles generally accepted in the United States of America and include amounts based on management's best estimates and judgments where necessary. Management believes that the financial statements are free of material misstatements and present fairly the financial position, results of operations and cash flows of PPL Energy Supply.

PPL Energy Supply management is responsible for establishing and maintaining an effective internal control structure and effective disclosure controls and procedures for financial reporting. PPL Energy Supply maintains a system of internal control that is designed to provide reasonable assurance that PPL Energy Supply assets are safeguarded from loss or unauthorized use or disposition and that transactions are executed in accordance with management's authorization and are properly recorded to permit the preparation of financial statements in accordance with generally accepted accounting principles. This system is augmented by a careful selection and training of qualified personnel, specific delegations of authority, a proper division of responsibilities, and utilization of written policies and procedures. An internal audit program monitors the effectiveness of this control system. Management believes that its internal control structure and its disclosure controls and procedures for financial reporting are adequate and effective.

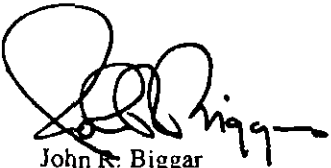
PPL's Audit Committee, which consists entirely of independent directors who are not employees of PPL, reviews audit plans related to PPL Energy Supply's internal controls, financial reports and related matters and meets regularly with management as well as the independent auditors and internal auditors. The independent auditors and the internal auditors have free access to PPL's Audit Committee, without management present, to discuss internal accounting control, auditing and financial reporting matters.

PricewaterhouseCoopers LLP, the independent certified public accountants, audited PPL Energy Supply's consolidated financial statements and issued their opinion above.

PPL Energy Supply management also recognizes its responsibility for fostering a strong ethical climate so that it conducts its business affairs according to the highest standards of personal and corporate conduct.



William F. Hecht  
President



John R. Biggar  
Vice President

**Report of Independent Auditors**

To the Board of Managers and Sole Member of  
PPL Energy Supply, LLC:

In our opinion, the consolidated financial statements listed in the index appearing under Item 8 on page 95 present fairly, in all material respects, the financial position of PPL Energy Supply, LLC and its subsidiaries ("PPL Energy Supply") at December 31, 2003 and 2002, and the results of their operations and their cash flows for each of the three years in the period ended December 31, 2003 in conformity with accounting principles generally accepted in the United States of America. In addition, in our opinion, the financial statement schedule listed in the index appearing under Item 8 presents fairly, in all material respects, the information set forth therein when read in conjunction with the related consolidated financial statements. These financial statements and financial statement schedule are the responsibility of the Company's management; our responsibility is to express an opinion on these financial statements and financial statement schedule based on our audits. We conducted our audits of these statements in accordance with auditing standards generally accepted in the United States of America, which require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

As discussed in Note 17 to the consolidated financial statements, PPL Energy Supply changed its method of accounting for derivative and hedging activities pursuant to Statement of Financial Accounting Standards ("SFAS") No. 133, *Accounting for Derivative Instruments and Hedging Activities*, as amended by SFAS No. 138, *Accounting for Certain Derivative Instruments and Certain Hedging Activities (an amendment of FASB Statement 133)*, in 2001. As discussed in Note 12 to the consolidated financial statements, PPL Energy Supply also changed its method of accounting for the amortization of unrecognized gains or losses in the annual pension expense/income determined under SFAS No. 87, *Employers' Accounting for Pensions*, in 2001. As discussed in Note 18 to the consolidated financial statements, PPL Energy Supply adopted SFAS No. 142, *Goodwill and Other Intangible Assets*, in 2002. As discussed in Note 21 to the consolidated financial statements, PPL Energy Supply adopted SFAS No. 143, *Accounting for Asset Retirement Obligations*, in 2003. As discussed in Note 22 to the consolidated financial statements, PPL Energy Supply adopted SFAS No. 150, *Accounting for Certain Financial Instruments with Characteristics of both Liabilities and Equity*, Emerging Issues Task Force No. 03-11, *Reporting Realized Gains and Losses on Derivative Instruments That Are Subject to FAS 133 and Not "Held for Trading Purposes" as Defined in Issue No. 02-3*, FASB Interpretation ("FIN") No. 45, *Guarantor's Accounting and Disclosure Requirements for Guarantees, Including Indirect Guarantees of Indebtedness of Others*, and FIN No. 46, *Consolidation of Variable Interest Entities -- an interpretation of ARB 51*, as amended by FIN 46(R), in 2003.

  
February 2, 2004

**PPL Electric Utilities Corporation**  
**Management's Report on Responsibility for Financial Statements**

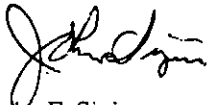
PPL Electric management is responsible for the preparation, integrity and objectivity of the consolidated financial statements and all other information in this annual report. The financial statements were prepared in accordance with accounting principles generally accepted in the United States of America and include amounts based on management's best estimates and judgments where necessary. Management believes that the financial statements are free of material misstatements and present fairly the financial position, results of operations and cash flows of PPL Electric.

PPL Electric management is responsible for establishing and maintaining an effective internal control structure and effective disclosure controls and procedures for financial reporting. PPL Electric maintains a system of internal control that is designed to provide reasonable assurance that PPL Electric assets are safeguarded from loss or unauthorized use or disposition and that transactions are executed in accordance with management's authorization and are properly recorded to permit the preparation of financial statements in accordance with generally accepted accounting principles. This system is augmented by a careful selection and training of qualified personnel, specific delegations of authority, a proper division of responsibilities, and utilization of written policies and procedures. An internal audit program monitors the effectiveness of this control system. Management believes that its internal control structure and its disclosure controls and procedures for financial reporting are adequate and effective.

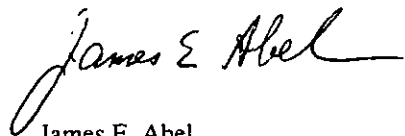
PPL's Audit Committee, which consists entirely of independent directors who are not employees of PPL, reviews audit plans related to PPL Electric's internal controls, financial reports and related matters and meets regularly with management as well as the independent auditors and internal auditors. The independent auditors and the internal auditors have free access to PPL's Audit Committee, without management present, to discuss internal accounting control, auditing and financial reporting matters.

PricewaterhouseCoopers LLP, the independent certified public accountants, audited PPL Electric's consolidated financial statements and issued their opinion above.

PPL Electric management also recognizes its responsibility for fostering a strong ethical climate so that it conducts its business affairs according to the highest standards of personal and corporate conduct.



John F. Sipics  
*President*



James E. Abel  
*Treasurer*

**Report of Independent Auditors**

To the Board of Directors and Shareowner of  
PPL Electric Utilities Corporation:

In our opinion, the consolidated financial statements listed in the index appearing under Item 8 on page 95 present fairly, in all material respects, the financial position of PPL Electric Utilities Corporation and its subsidiaries ("PPL Electric") at December 31, 2003 and 2002, and the results of their operations and their cash flows for each of the three years in the period ended December 31, 2003 in conformity with accounting principles generally accepted in the United States of America. In addition, in our opinion, the financial statement schedule listed in the index appearing under Item 8 presents fairly, in all material respects, the information set forth therein when read in conjunction with the related consolidated financial statements. These financial statements and financial statement schedule are the responsibility of the Company's management; our responsibility is to express an opinion on these financial statements and financial statement schedule based on our audits. We conducted our audits of these statements in accordance with auditing standards generally accepted in the United States of America, which require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

As discussed in Note 12 to the consolidated financial statements, PPL Electric changed its method of accounting for the amortization of unrecognized gains or losses in the annual pension expense/income determined under Statement of Financial Accounting Standards No. 87, *Employers' Accounting for Pensions*, in 2001.



February 2, 2004

**PPL Montana, LLC**  
**Management's Report on Responsibility for Financial Statements**

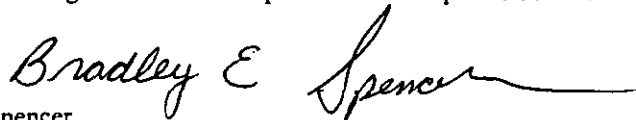
PPL Montana management is responsible for the preparation, integrity and objectivity of the consolidated financial statements and all other information in this annual report. The financial statements were prepared in accordance with accounting principles generally accepted in the United States of America and include amounts based on management's best estimates and judgments where necessary. Management believes that the financial statements are free of material misstatements and present fairly the financial position, results of operations and cash flows of PPL Montana.

PPL Montana management is responsible for establishing and maintaining an effective internal control structure and effective disclosure controls and procedures for financial reporting. PPL Montana maintains a system of internal control that is designed to provide reasonable assurance that PPL Montana assets are safeguarded from loss or unauthorized use or disposition and that transactions are executed in accordance with management's authorization and are properly recorded to permit the preparation of financial statements in accordance with generally accepted accounting principles. This system is augmented by a careful selection and training of qualified personnel, specific delegations of authority, a proper division of responsibilities, and utilization of written policies and procedures. An internal audit program monitors the effectiveness of this control system. Management believes that its internal control structure and its disclosure controls and procedures for financial reporting are adequate and effective.

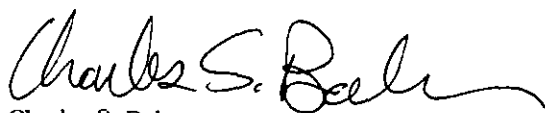
PPL's Audit Committee, which consists entirely of independent directors who are not employees of PPL, reviews audit plans related to PPL Montana's internal controls, financial reports and related matters and meets regularly with management as well as the independent auditors and internal auditors. The independent auditors and the internal auditors have free access to PPL's Audit Committee, without management present, to discuss internal accounting control, auditing and financial reporting matters.

PricewaterhouseCoopers LLP, the independent certified public accountants, audited PPL Montana's consolidated financial statements and issued their opinion above.

PPL Montana management also recognizes its responsibility for fostering a strong ethical climate so that it conducts its business affairs according to the highest standards of personal and corporate conduct.



Bradley E. Spencer  
*Vice President and Chief Operating Officer*



Charles S. Baker  
*Controller*

## Report of Independent Auditors

To the Board of Managers and Member of  
PPL Montana, LLC

In our opinion, the consolidated financial statements listed in the index appearing under Item 8 on page 95 present fairly, in all material respects, the financial position of PPL Montana, LLC and its subsidiaries ("PPL Montana") at December 31, 2003 and 2002, and the results of their operations and their cash flows for each of the three years in the period ended December 31, 2003 in conformity with accounting principles generally accepted in the United States of America. In addition, in our opinion, the financial statement schedule listed in the index appearing under Item 8 presents fairly, in all material respects, the information set forth therein when read in conjunction with the related consolidated financial statements. These financial statements and financial statement schedule are the responsibility of PPL Montana's management; our responsibility is to express an opinion on these financial statements and financial statement schedule based on our audits. We conducted our audits of these statements in accordance with auditing standards generally accepted in the United States of America, which require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

As discussed in Note 17 to the consolidated financial statements, PPL Montana changed its method of accounting for derivative and hedging activities pursuant to Statement of Financial Accounting Standards No. 133, Accounting for Derivative Instruments and Hedging Activities, as amended by Statement of Financial Accounting Standards No. 138, Accounting for Certain Derivative Instruments and Certain Hedging Activities (an amendment of FASB Statement 133) in 2001. As discussed in Note 22 to the consolidated financial statements, PPL Montana adopted Emerging Issues Task Force No. 03-11, Reporting Realized Gains and Losses on Derivative Instruments That Are Subject to FAS 133 and Not "Held for Trading Purposes" as Defined in Issue No. 02-3. As discussed in Note 17, PPL Montana adopted Derivatives Implementations Group Implementation Issue C20, Interpretation of Clearly and Closely Related in Contracts That Qualify for the Normal Purchases and Normal Sales Scope Exception, in 2003.

  
February 2, 2004

## INDEX TO ITEM 8. FINANCIAL STATEMENTS AND SUPPLEMENTARY DATA

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## ITEM 8. FINANCIAL STATEMENTS AND SUPPLEMENTARY DATA

### CONSOLIDATED STATEMENT OF INCOME FOR THE YEARS ENDED DECEMBER 31, PPL Corporation and Subsidiaries

(Millions of Dollars, except per share data)

	2003	2002	2001
<b>Operating Revenues</b>			
Utility.....	\$ 3,710	\$ 3,676	\$ 3,034
Unregulated retail electric and gas.....	152	182	356
Wholesale energy marketing.....	1,214	1,036	1,027
Net energy trading margins.....	12	19	37
Energy related businesses.....	499	568	661
Total.....	<u>5,587</u>	<u>5,481</u>	<u>5,115</u>
<b>Operating Expenses</b>			
Operation			
Fuel.....	617	584	602
Energy purchases.....	1,030	916	911
Other operation and maintenance.....	1,204	1,136	1,059
Amortization of recoverable transition costs.....	260	226	251
Depreciation (Note 1).....	380	367	266
Taxes, other than income (Note 5).....	256	231	155
Energy related businesses.....	491	543	535
Other charges			
Write-down of international energy projects (Note 9).....		113	336
Cancellation of generation projects (Note 9).....			150
Workforce reduction (Note 20).....	9	75	
Write-down of generation assets (Note 9).....		44	
Total.....	<u>4,247</u>	<u>4,235</u>	<u>4,265</u>
<b>Operating Income</b> .....	<u>1,340</u>	<u>1,246</u>	<u>850</u>
Other Income - net (Note 16).....	60	30	
Interest Expense.....	475	561	386
<b>Income from Continuing Operations Before Income Taxes, Minority Interest and Distributions on Preferred Securities</b> .....	<u>925</u>	<u>715</u>	<u>480</u>
Income Taxes (Note 5).....	170	210	261
Minority Interest (Note 1).....	7	78	(2)
Distributions on Preferred Securities (Note 22).....	29	67	52
<b>Income from Continuing Operations</b> .....	<u>719</u>	<u>360</u>	<u>169</u>
Loss from Discontinued Operations (net of income taxes) (Note 9).....	20	2	
<b>Income Before Cumulative Effects of Changes in Accounting Principles</b> .....	<u>699</u>	<u>358</u>	<u>169</u>
Cumulative Effects of Changes in Accounting Principles (net of income taxes) (Notes 12, 18, 21 and 22).....	35	(150)	10
<b>Net Income</b> .....	<u>\$ 734</u>	<u>\$ 208</u>	<u>\$ 179</u>
<b>Earnings Per Share of Common Stock (Note 4)</b>			
<b>Income from Continuing Operations:</b>			
Basic.....	\$ 4.16	\$ 2.36	\$ 1.16
Diluted.....	\$ 4.15	\$ 2.36	\$ 1.15
<b>Net Income:</b>			
Basic.....	\$ 4.25	\$ 1.37	\$ 1.23
Diluted.....	\$ 4.24	\$ 1.36	\$ 1.22
<b>Dividends Declared Per Share of Common Stock</b> .....	\$ 1.54	\$ 1.44	\$ 1.06

The accompanying Notes to Consolidated Financial Statements are an integral part of the financial statements.

# CONSOLIDATED STATEMENT OF CASH FLOWS FOR THE YEARS ENDED DECEMBER 31, PPL Corporation and Subsidiaries

(Millions of Dollars)

	2003	2002	2001
<b>Cash Flows From Operating Activities</b>			
Net income .....	\$ 734	\$ 208	\$ 179
Adjustments to reconcile net income to net cash provided by operating activities			
Loss from discontinued operations .....	20		
Cumulative effects of changes in accounting principles .....	(35)	150	(10)
Depreciation .....	380	289	266
Amortizations - recoverable transition costs and other .....	244	198	224
Charge for cancellation of generation projects .....			150
Payments to cancel generation projects .....		(152)	
Dividends received from unconsolidated affiliates .....	7	14	103
Pension income - net .....	(41)	(42)	(47)
Pension funding .....	(18)		
Write-down of assets .....	13	157	336
Gain on asset sales and insurance settlements .....	(21)		
Distribution requirements - preferred securities .....	29	60	52
Equity in earnings of unconsolidated affiliates .....	11	9	(13)
Equity in earnings of WPD prior to acquiring controlling interest in 2002 .....		(75)	(112)
Deferred income taxes and investment tax credits .....	96	85	(47)
Deferral of storm-related costs .....	(15)		
Workforce reduction - net of cash paid .....	9	67	
Unrealized (gain) loss on derivative hedging activities .....	(38)	24	(16)
Gain on NUG contract termination .....		(25)	
NUG contract termination payment .....		(50)	
Realized gain on nuclear trust fund .....	(19)		
Interest accretion on asset retirement obligation and other .....	22	4	6
Other - net .....	9	7	(2)
Change in current assets and current liabilities			
Accounts receivable .....	11	(48)	35
Accounts payable .....	7	(73)	(101)
Other - net .....	(40)	(6)	(36)
Other operating activities - net			
Other assets .....	37	1	(69)
Other liabilities .....	(62)		11
Net cash provided by operating activities .....	<u>1,340</u>	<u>802</u>	<u>909</u>
<b>Cash Flows From Investing Activities</b>			
Expenditures for property, plant and equipment .....	(771)	(649)	(569)
Investment in generating assets and electric energy projects .....		(261)	(312)
Acquisition of controlling interest in WPD, net of cash acquired .....		(211)	
Proceeds from sale of assets and insurance settlements and other .....	49	20	
Net increase in notes receivable from affiliates .....			210
Other investing activities - net .....	(7)	(28)	(31)
Net cash used in investing activities .....	<u>(729)</u>	<u>(1,129)</u>	<u>(702)</u>
<b>Cash Flows From Financing Activities</b>			
Issuance of long-term debt .....	992		1,529
Retirement of long-term debt .....	(575)	(823)	(616)
Issuance (retirement) of company-obligated mandatorily redeemable preferred securities .....		(250)	575
Issuance of common stock .....	426	587	52
Retirement of preferred stock .....	(31)		(15)
Payment of common dividends and preferred distributions .....	(287)	(261)	(201)
Net increase (decrease) in short-term debt .....	(877)	411	(981)
Other financing activities - net .....	(35)	(27)	(94)
Net cash provided by (used in) financing activities .....	<u>(387)</u>	<u>(363)</u>	<u>249</u>
<b>Effect of Exchange Rates on Cash and Cash Equivalents</b> .....	<u>7</u>	<u>2</u>	<u>(3)</u>
<b>Net Increase (Decrease) in Cash and Cash Equivalents</b> .....	<u>231</u>	<u>(688)</u>	<u>453</u>
Cash and Cash Equivalents at Beginning of Period .....	<u>245</u>	<u>933</u>	<u>480</u>
Cash and Cash Equivalents at End of Period .....	<u>\$ 476</u>	<u>\$ 245</u>	<u>\$ 933</u>
<b>Supplemental Disclosures of Cash Flow Information</b>			
Cash paid during the period for:			
Interest (net of amount capitalized) .....	\$ 456	\$ 412	\$ 373
Income taxes .....	\$ 19	\$ 100	\$ 328

*The accompanying Notes to Consolidated Financial Statements are an integral part of the financial statements.*

**CONSOLIDATED BALANCE SHEET AT DECEMBER 31,  
PPL Corporation and Subsidiaries**

(Millions of Dollars)

	<u>2003</u>	<u>2002</u>
<b>Assets</b>		
<b>Current Assets</b>		
Cash and cash equivalents (Note 1).....	\$ 476	\$ 245
Accounts receivable (less reserve: 2003, \$93; 2002, \$111).....	555	588
Unbilled revenues .....	341	303
Fuel, materials and supplies - at average cost.....	256	242
Prepayments.....	54	122
Deferred income taxes (Note 5).....	105	104
Price risk management assets (Notes 1 and 17).....	90	103
Other .....	162	112
	<u>2,039</u>	<u>1,819</u>
<b>Investments</b>		
Investment in unconsolidated affiliates - at equity (Notes 1 and 3).....	230	234
Investment in unconsolidated affiliates - at cost (Note 1).....	126	107
Nuclear plant decommissioning trust fund (Note 6).....	357	287
Other .....	29	28
	<u>742</u>	<u>656</u>
<b>Property, Plant and Equipment - net (Note 1)</b>		
Electric plant in service		
Transmission and distribution .....	5,456	5,603
Generation .....	3,362	2,679
General .....	431	479
	<u>9,249</u>	<u>8,761</u>
Construction work in progress .....	627	223
Nuclear fuel .....	144	129
	<u>10,020</u>	<u>9,113</u>
Gas and oil plant .....	205	201
Other property.....	221	252
	<u>10,446</u>	<u>9,566</u>
<b>Regulatory and Other Noncurrent Assets (Note 1)</b>		
Recoverable transition costs .....	1,687	1,946
Goodwill (Note 18).....	1,068	474
Other intangibles (Note 18) .....	230	212
Other .....	911	879
	<u>3,896</u>	<u>3,511</u>
	<u>\$ 17,123</u>	<u>\$ 15,552</u>

*The accompanying Notes to Consolidated Financial Statements are an integral part of the financial statements.*

**CONSOLIDATED BALANCE SHEET AT DECEMBER 31,  
PPL Corporation and Subsidiaries**

(Millions of Dollars)

	<u>2003</u>	<u>2002</u>
<b>Liabilities and Equity</b>		
<b>Current Liabilities</b>		
Short-term debt (Note 8).....	\$ 56	\$ 943
Long-term debt.....	395	366
Accounts payable.....	456	452
Above market NUG contracts (Note 14).....	74	75
Taxes.....	182	193
Interest.....	121	101
Dividends.....	70	66
Price risk management liabilities (Notes 1 and 17).....	82	110
Other.....	337	307
	<u>1,773</u>	<u>2,613</u>
<b>Long-term Debt</b> .....	<u>7,464</u>	<u>5,901</u>
<b>Long-term Debt with Affiliate Trusts (Notes 15 and 22)</b> .....	<u>681</u>	
<b>Deferred Credits and Other Noncurrent Liabilities</b>		
Deferred income taxes and investment tax credits (Note 5).....	2,201	2,287
Above market NUG contracts (Note 14).....	278	352
Other (Notes 1, 6, 9, 12 and 21).....	1,362	1,396
	<u>3,841</u>	<u>4,035</u>
<b>Commitments and Contingent Liabilities (Note 14)</b> .....		
<b>Minority Interest (Note 1)</b> .....	<u>54</u>	<u>36</u>
<b>Company-obligated Mandatorily Redeemable Preferred Securities of Subsidiary Trusts Holding Solely Company Debentures (Note 22)</b> .....		<u>661</u>
<b>Preferred Stock</b>		
With sinking fund requirements.....		31
Without sinking fund requirements.....	51	51
	<u>51</u>	<u>82</u>
<b>Shareowners' Common Equity</b>		
Common stock.....	2	2
Capital in excess of par value.....	2,973	2,539
Treasury stock (Note 1).....	(837)	(836)
Earnings reinvested.....	1,478	1,013
Accumulated other comprehensive loss (Notes 1 and 17).....	(297)	(446)
Capital stock expense and other.....	(60)	(48)
	<u>3,259</u>	<u>2,224</u>
	<u>\$ 17,123</u>	<u>\$ 15,552</u>

*The accompanying Notes to Consolidated Financial Statements are an integral part of the financial statements.*

**CONSOLIDATED STATEMENT OF SHAREOWNERS' COMMON EQUITY  
AND COMPREHENSIVE INCOME FOR THE YEARS ENDED DECEMBER 31,  
PPL Corporation and Subsidiaries**

(Millions of Dollars, except per share amounts)

	2003	2002	2001
Common stock at beginning of year .....	\$ 2	\$ 2	\$ 2
Common stock at end of year .....	2	2	2
Capital in excess of par value at beginning of year .....	2,539	1,956	1,895
Common stock issued .....	426	587	54
Other .....	8	(4)	7
Capital in excess of par value at end of year .....	2,973	2,539	1,956
Treasury stock at beginning of year .....	(836)	(836)	(836)
Treasury stock purchased .....	(1)		
Treasury stock at end of year .....	(837)	(836)	(836)
Earnings reinvested at beginning of year .....	1,013	1,023	999
Net income (b) .....	734	208	179
Cash dividends declared on common stock .....	(269)	(218)	(155)
Earnings reinvested at end of year .....	1,478	1,013	1,023
Accumulated other comprehensive loss at beginning of year (c) .....	(446)	(251)	(36)
Foreign currency translation adjustments (b) .....	106	125	(234)
Unrealized gain (loss) on available-for-sale securities (b) .....	24	(3)	(4)
Minimum pension liability adjustments (b) (d) .....	(10)	(301)	
Unrealized gain (loss) on qualifying derivatives (b) .....	29	(16)	23
Accumulated other comprehensive loss at end of year .....	(297)	(446)	(251)
Capital stock expense and other at beginning of year .....	(48)	(37)	(12)
Issuance costs and other charges to issue common stock .....	(9)	(18)	
Issuance costs and other charges to issue PEPS Units .....	(3)		(25)
Other .....		7	
Capital stock expense and other at end of year .....	(60)	(48)	(37)
Total Shareowners' Common Equity .....	<u>\$ 3,259</u>	<u>\$ 2,224</u>	<u>\$ 1,857</u>
Common stock shares at beginning of year (a) .....	165,736	146,580	145,041
Common stock issued through the ESOP, DRIP, ICP, ICPKE, structured equity program and public offering .....	11,652	19,156	1,539
Treasury stock purchased .....	(26)		
Common stock shares at end of year .....	<u>177,362</u>	<u>165,736</u>	<u>146,580</u>
(a) Shares in thousands; \$.01 par value, 390 million shares authorized. Each share entitles the holder to one vote on any question presented to any shareowners' meeting.			
(b) Statement of Comprehensive Income (Loss) (Note 1):			
Net income .....	\$ 734	\$ 208	\$ 179
Other comprehensive income (loss):			
Foreign currency translation adjustments, net of tax (benefit) of \$0, \$(5), \$15 .....	106	125	(234)
Unrealized gain (loss) on available-for-sale securities, net of tax (benefit) of \$14, \$(2), \$(3) .....	24	(3)	(4)
Minimum pension liability adjustments, net of tax (benefit) of \$(4), \$(131) .....	(10)	(301)	
Unrealized gain (loss) on qualifying derivatives, net of tax (benefit) of \$15, \$(10), \$12 .....	29	(16)	23
Total other comprehensive income (loss) .....	149	(195)	(215)
Comprehensive Income (Loss) .....	<u>\$ 883</u>	<u>\$ 13</u>	<u>\$ (36)</u>
(c) See Note 1 for disclosure of balances for each component of Accumulated Other Comprehensive Loss.			
(d) See Note 12 for additional information on the adjustments to the additional minimum pension liability.			

The accompanying Notes to Consolidated Financial Statements are an integral part of the financial statements.

**CONSOLIDATED STATEMENT OF PREFERRED STOCK AT DECEMBER 31,  
PPL Corporation and Subsidiaries (a)**

(Millions of Dollars)

PPL Electric	Outstanding		Shares Outstanding	Shares Authorized
	2003	2002	2003	
<b>Preferred Stock - \$100 par, cumulative</b>				
4-1/2% .....	\$ 25	\$ 25	247,524	629,936
Series Preferred .....	26	57	257,665	10,000,000
	<u>\$ 51</u>	<u>\$ 82</u>		

**Details of Preferred Stock (b)**

With Sinking Fund Requirements (c)	Outstanding		Shares Outstanding	Optional Redemption Price Per Share
	2003	2002	2003	
<b>Series Preferred</b>				
6.125% .....		\$ 17		
6.15% .....		10		
6.33% .....		4		
		<u>\$ 31</u>		
<b>Without Sinking Fund Requirements</b>				
4-1/2% Preferred .....	\$ 25	\$ 25	247,524	\$ 110.00
<b>Series Preferred</b>				
3.35% .....	2	2	20,605	103.50
4.40% .....	12	12	117,676	102.00
4.60% .....	3	3	28,614	103.00
6.75% .....	9	9	90,770	103.38
	<u>\$ 51</u>	<u>\$ 51</u>		

**Decreases in Preferred Stock**

	2003		2002		2001	
	Shares	Amount	Shares	Amount	Shares	Amount
4-1/2% Preferred .....					(134)	
<b>Series Preferred</b>						
5.95% .....					(10,000)	\$ (1)
6.125% .....	(167,500)	\$ (17)			(148,000)	(14)
6.15% .....	(97,500)	(10)				
6.33% .....	(46,000)	(4)				

Decreases in Preferred Stock normally represent: (i) the redemption of stock pursuant to mandatory sinking fund requirements; or (ii) shares redeemed pursuant to optional redemption provisions.

- (a) Each share of PPL Electric's preferred stock entitles the holder to one vote on any question presented to PPL Electric's shareowners' meetings. There were also 10 million shares of PPL's preferred stock and 5 million shares of PPL Electric's preference stock authorized; none were outstanding at December 31, 2003 and 2002.
- (b) The involuntary liquidation price of the preferred stock is \$100 per share. The optional voluntary liquidation price is the optional redemption price per share in effect, except for the 4-1/2% Preferred Stock for which such price is \$100 per share (plus in each case any unpaid dividends).
- (c) See Note 22 for additional information.

*The accompanying Notes to Consolidated Financial Statements are an integral part of the financial statements.*

**CONSOLIDATED STATEMENT OF COMPANY-OBLIGATED  
MANDATORILY REDEEMABLE SECURITIES AT DECEMBER 31,  
PPL Corporation and Subsidiaries**

(Millions of Dollars)

	<u>Outstanding</u>	
	<u>2003(c)</u>	<u>2002</u>
<b>Company-obligated Mandatorily Redeemable Preferred Securities of Subsidiary Trusts Holding Solely Company Debentures</b>		
<b>\$25 per security</b>		
7.75% (a) .....	\$	575
<b>\$1,000 per security</b>		
8.23% (b) .....		<u>86</u>
	<u>\$</u>	<u>661</u>

- (a) In May 2001, PPL and PPL Capital Funding Trust I, a wholly-owned financing subsidiary of PPL, issued \$575 million of 7.75% PEPS Units. Each PEPS Unit consists of (i) a contract to purchase shares of PPL common stock on or prior to May 18, 2004 and (ii) a trust preferred security of PPL Capital Funding Trust I with a maturity date of May 2006 and stated liquidation amount of \$25. Each purchase contract requires PPL to make contract adjustment payments of .46% per year, paid quarterly, on the \$25 stated amount of the PEPS Unit and requires the holders of the contracts to purchase a number of shares of PPL common stock on or prior to May 18, 2004. The number of shares required to be purchased will depend on the average market price of PPL's common stock prior to the purchase date, subject to certain limitations. The holders' obligations to purchase shares under the purchase contracts may be settled with the proceeds of a remarketing of the trust preferred securities, which have been pledged to secure these obligations. The distribution rate on each trust preferred security is 7.29% per year, paid quarterly, until May 18, 2004. The trust's sole source of funds for distributions are from payments of interest on the 7.29% subordinated notes of PPL Capital Funding, due May 18, 2006, issued to the trust. PPL has guaranteed the payment of principal and interest on the subordinated notes issued to the trust by PPL Capital Funding. PPL has also fully and unconditionally guaranteed all of the trust's obligations under the trust preferred securities. See Note 8 for a discussion of dividend restrictions related to PPL's subsidiaries.
- (b) SIUK Capital Trust I issued \$82 million of 8.23% preferred securities maturing in February 2027 and invested the proceeds in 8.23% subordinated debentures maturing in February 2027 issued by SIUK Limited. Thus, the preferred securities are supported by a corresponding amount of subordinated debentures. SIUK Limited owned all of the common securities of SIUK Capital Trust I and guaranteed all of SIUK Capital Trust I's obligations under the preferred securities. In January 2003, SIUK Limited transferred its assets and liabilities, including the common securities of SIUK Capital Trust I and the obligations under the subordinated debentures, to WPD LLP. Therefore, WPD LLP currently guarantees all of SIUK Capital Trust I's obligations under the preferred securities. SIUK Capital Trust I may, at the discretion of WPD LLP, redeem the preferred securities, in whole or in part, at 104.115% of par beginning February 2007 and thereafter at an annually declining premium over par through January 2017, after which time they are redeemable at par. With PPL's acquisition of the controlling interest in WPD in September 2002, these preferred securities were consolidated on the books of PPL at their then fair value of \$86 million. See Note 9 for information on the acquisition of a controlling interest in WPD.
- (c) On July 1, 2003, PPL adopted the provisions of SFAS 150, "Accounting for Certain Financial Instruments with Characteristics of Both Liabilities and Equity." These preferred securities are mandatorily redeemable financial instruments, as they require the issuer to redeem the securities for cash on a specified date. Thus, they should be classified as liabilities, as a component of long-term debt, instead of "mezzanine" equity on the Balance Sheet. However, as of December 31, 2003, no amounts were included in "Long-term Debt" for these securities because PPL Capital Funding Trust I and SIUK Capital Trust I were deconsolidated effective December 31, 2003 in connection with the adoption of FIN 46, "Consolidation of Variable Interest Entities, an Interpretation of ARB No. 51," for certain entities. Instead, the subordinated debt securities that support the trust preferred securities are reflected in "Long-term Debt with Affiliate Trusts" as of December 31, 2003. See Note 22 for additional information on SFAS 150 and FIN 46.

*The accompanying Notes to Consolidated Financial Statements are an integral part of the financial statements.*

# CONSOLIDATED STATEMENT OF LONG-TERM DEBT AT DECEMBER 31, PPL Corporation and Subsidiaries

(Millions of Dollars)

	Outstanding		Maturity (a)
	2003	2002	
<b>Bonds:</b>			
6-1/2% - 7-7/8% First Mortgage Bonds (b) .....	\$ 297 (d)	\$ 382	2003-2024
3.125% - 6.40% First Mortgage Pollution Control Bonds (b) .....	314 (e)	314	2008-2029
4.30% - 6-1/4% Senior Secured Bonds (b) .....	900 (f)	800	2007-2013
6.08% to 7.15% Series 1999-1 Transition Bonds .....	1,423 (g)	1,678	2003-2008
5.875% - 9.25% Unsecured Bonds .....	1,982 (h)	1,583	2004-2028
6.20% - 6.40% Inflation-linked Bonds .....	150 (i)	131	2006-2022
1.54% Pollution Control Revenue Bonds .....	9	9	2027
<b>Notes:</b>			
5.75% - 8.375% Medium-term Notes (c) .....	737 (j)	822	2004-2007
6.40% Senior Unsecured Notes .....	500	500	2011
8.05% - 8.30% Senior Secured Notes .....	437 (k)		2013
2.625% Convertible Senior Notes .....	400 (l)		2023
8.70% - 9.64% Unsecured Promissory Notes .....	12 (m)	12	2010-2022
Term Loan - variable rate (2.56% at December 31, 2003) .....	625 (n)		2008
Trust Securities - variable rate (3.435% at December 31, 2003) .....	31 (n)		2008
Other Long-term Debt .....	27	21	2003-2013
	<u>7,844</u>	<u>6,252</u>	
Fair Value Swaps .....	28	28	
Unamortized discount .....	(13)	(13)	
	<u>7,859</u>	<u>6,267</u>	
Less amount due within one year .....	(395)	(366)	
<b>Total Long-term Debt .....</b>	<b>\$ 7,464</b>	<b>\$ 5,901</b>	
<b>Long-term Debt with Affiliate Trusts:</b>			
7.29% Subordinated Notes .....	\$ 592 (o)		2006
8.23% Subordinated Debentures .....	89 (o)		2027
<b>Total Long-term Debt with Affiliate Trusts .....</b>	<b>\$ 681</b>		

- (a) Aggregate maturities of long-term debt through 2008 are (millions of dollars): 2004, \$395; 2005, \$911; 2006, \$1,454; 2007, \$1,070; and 2008, \$1,280.
- (b) The First Mortgage Bonds and the First Mortgage Pollution Control Bonds were issued under, and are secured by, the lien of the 1945 First Mortgage Bond Indenture. The lien of the 1945 First Mortgage Bond Indenture covers substantially all electric transmission and distribution plant owned by PPL Electric. The Senior Secured Bonds were issued under the 2001 Senior Secured Bond Indenture. The Senior Secured Bonds are secured by (i) an equal principal amount of First Mortgage Bonds issued under the 1945 First Mortgage Bond Indenture and (ii) the lien of the 2001 Senior Secured Bond Indenture, which covers substantially all electric transmission and distribution plant owned by PPL Electric and which is junior to the lien of the 1945 First Mortgage Bond Indenture.
- (c) PPL fully and unconditionally guarantees the medium-term notes of PPL Capital Funding, a wholly-owned financing subsidiary of PPL. See Note 8 for a discussion of dividend restrictions related to PPL's subsidiaries.
- (d) In April 2003, PPL Electric redeemed and retired all of its outstanding First Mortgage Bonds 7-7/8% Series due 2023, at an aggregate par value of \$46 million, and in December 2003, retired \$19 million of its First Mortgage Bonds 6-3/4% Series due 2023.
- (e) In February 2003, PPL Electric issued \$90 million of 3.125% Pollution Control Bonds and also retired \$90 million of its 6.40% Series H Pollution Control Bonds.
- (f) In May 2003, PPL Electric issued \$100 million of 4.30% Senior Secured Bonds.
- (g) In August 1999, PPL Transition Bond Company issued \$2.4 billion of transition bonds to securitize a portion of PPL Electric's stranded costs. The bonds were issued in eight different classes, with expected average lives of 1 to 8.7 years. Bond principal payments of \$255 million were made in 2003.
- (h) In March 2003, WPD issued £200 million of 5.875% bonds due 2027 and in May 2003 WPD issued an additional £50 million of 5.875% bonds due 2027. During the fourth quarter, WPD retired \$53 million of 7.375% bonds due 2028.
- (i) Increase due to an increase in foreign currency exchange rates.
- (j) During 2003, PPL Capital Funding retired the following series of medium-term notes: \$60 million of 6.375% Series due 2003, \$20 million of 6.23% Series due 2003 and \$5 million of 6.40% Series due 2003.
- (k) Represents lease financing consolidated through a variable interest entity. See Note 22 for additional information. Secured by, among other things, the generation facility, which had a carrying value of \$442 million as of December 31, 2003 and was included in "Property, Plant and Equipment - net - Construction work in progress" on the Balance Sheet.
- (l) Issued by PPL Energy Supply in May 2003.
- (m) In September 2003, PPL Gas Utilities made a \$750,000 principal payment on its 9.64% Notes due 2010.
- (n) Represents lease financing consolidated through a variable interest entity. See Note 22 for additional information. Borrowings bear interest at a floating rate, based at PPL's option, upon (i) LIBOR plus an applicable percentage that is subject to change based on the credit ratings of PPL Energy Supply or (ii) the greater of (a) the Wachovia Bank N.A. corporate base rate or (b) the federal funds rate plus 0.50%, plus an applicable percentage that is subject to change based on the credit ratings of PPL Energy Supply. Secured by, among other things, the generation facilities and the land on which the facilities are located. As of December 31, 2003, the aggregate carrying value of the facilities and the land was \$617 million, net of accumulated depreciation of \$26 million, and was included in "Property, Plant and Equipment - net - Electric plant in service" and "Regulatory and Other Noncurrent Assets - Other intangibles" on the Balance Sheet.
- (o) Represents debt with a wholly-owned trust that was deconsolidated effective December 31, 2003 as a result of the adoption of FIN 46, "Consolidation of Variable Interest Entities, an Interpretation of ARB No. 51," for certain entities. See Note 22 for further discussion.

The accompanying Notes to Consolidated Financial Statements are an integral part of the financial statements.

**CONSOLIDATED STATEMENT OF INCOME FOR THE YEARS ENDED DECEMBER 31,  
PPL Energy Supply, LLC and Subsidiaries**

(Millions of Dollars)

	2003	2002	2001
<b>Operating Revenues</b>			
Wholesale energy marketing .....	\$ 1,214	\$ 1,036	\$ 1,027
Wholesale energy marketing to affiliates (Note 15).....	1,451	1,434	1,331
Utility .....	934	980	408
Unregulated retail electric and gas .....	152	182	356
Net energy trading margins .....	12	19	37
Energy related businesses.....	486	555	633
<b>Total .....</b>	<b>4,249</b>	<b>4,206</b>	<b>3,792</b>
<b>Operating Expenses</b>			
<b>Operation</b>			
Fuel .....	537	502	500
Energy purchases .....	818	708	734
Energy purchases from affiliates (Note 15) .....	160	171	194
Other operation and maintenance.....	875	812	746
Depreciation (Note 1).....	266	265	169
Taxes, other than income (Note 5) .....	89	78	38
Energy related businesses.....	469	522	508
<b>Other charges</b>			
Write-down of international energy projects (Note 9).....		113	336
Cancellation of generation projects (Note 9) .....			150
Workforce reduction (Note 20).....		41	
Write-down of generation assets (Note 9).....		44	
<b>Total .....</b>	<b>3,214</b>	<b>3,256</b>	<b>3,375</b>
<b>Operating Income .....</b>	<b>1,035</b>	<b>950</b>	<b>417</b>
Other Income - net (Note 16).....	73	44	73
Interest Expense.....	198	207	21
Interest Expense with Affiliate .....	1	3	26
<b>Income from Continuing Operations Before Income Taxes, Minority Interest and Distributions on Preferred Securities .....</b>	<b>909</b>	<b>784</b>	<b>443</b>
Income Taxes (Note 5) .....	185	266	274
Minority Interest (Note 1).....	7	78	(2)
Distributions on Preferred Securities (Note 22).....	5	9	
<b>Income from Continuing Operations .....</b>	<b>712</b>	<b>431</b>	<b>171</b>
Loss from Discontinued Operations (net of income taxes) (Note 9) .....	20	2	
<b>Income Before Cumulative Effects of Changes in Accounting Principles .....</b>	<b>692</b>	<b>429</b>	<b>171</b>
Cumulative Effects of Changes in Accounting Principles (net of income taxes) (Notes 12, 18, 21 and 22).....	35	(150)	3
<b>Net Income.....</b>	<b>\$ 727</b>	<b>\$ 279</b>	<b>\$ 174</b>

The accompanying Notes to Consolidated Financial Statements are an integral part of the financial statements.

# CONSOLIDATED STATEMENT OF CASH FLOWS FOR THE YEARS ENDED DECEMBER 31, PPL Energy Supply, LLC and Subsidiaries

(Millions of Dollars)

	2003	2002	2001
<b>Cash Flows From Operating Activities</b>			
Net income .....	\$ 727	\$ 279	\$ 174
Adjustments to reconcile net income to net cash provided by operating activities			
Loss from discontinued operations .....	20		
Cumulative effects of changes in accounting principles .....	(35)	150	(3)
Depreciation .....	266	175	169
Amortization - energy commitments and other .....	(38)	(56)	(61)
Charge for cancellation of generation projects .....			150
Payments to cancel generation projects .....		(152)	
Dividends received from unconsolidated affiliates .....	7	14	103
Pension income - net .....	(39)	(20)	(23)
Pension funding .....	(15)		
Write-down of assets .....	13	157	336
Gain on asset sales and insurance settlements .....	(21)		
Equity in earnings of unconsolidated affiliates .....	8	8	(15)
Equity in earnings of WPD prior to acquiring controlling interest in 2002 .....		(75)	(112)
Deferred income taxes and investment tax credits .....	154	158	14
Workforce reduction - net of cash paid .....		37	
Unrealized (gain) loss on derivative hedging activities .....	(16)	3	(16)
Gain on NUG contract termination .....		(25)	
NUG contract termination payment .....		(50)	
Realized gain on nuclear trust fund .....	(19)		
Interest accretion on asset retirement obligation and other .....	22	4	6
Deferred revenue on PLR supply to affiliate .....			90
Other - net .....	16	7	(2)
Change in current assets and current liabilities			
Accounts receivable .....	(50)	109	47
Accounts payable .....	(21)	(32)	(145)
Other - net .....	(42)	(40)	(101)
Other operating activities - net			
Other assets .....	17	(1)	
Other liabilities .....	(44)	1	8
Net cash provided by operating activities .....	<u>910</u>	<u>651</u>	<u>619</u>
<b>Cash Flows From Investing Activities</b>			
Expenditures for property, plant and equipment .....	(506)	(404)	(380)
Investment in generating assets and electric energy projects .....		(261)	(312)
Acquisition of controlling interest in WPD, net of cash acquired .....		(211)	
Proceeds from sale of assets and insurance settlements .....	47	20	
Net (increase) decrease in notes receivable from affiliates .....	653	(260)	986
Other investing activities - net .....	10	(28)	(16)
Net cash provided by (used in) investing activities .....	<u>204</u>	<u>(1,144)</u>	<u>278</u>
<b>Cash Flows From Financing Activities</b>			
Issuance of long-term debt .....	802		729
Retirement of long-term debt .....	(60)	(14)	(9)
Contributions from Member .....	261	160	953
Distributions to Member .....	(1,168)	(710)	(463)
Net increase (decrease) in short-term debt .....	(862)	392	(193)
Net decrease in short-term debt payable to affiliates .....			(1,200)
Other financing activities - net .....	(16)	(3)	(26)
Net cash used in financing activities .....	<u>(1,043)</u>	<u>(175)</u>	<u>(209)</u>
Effect of Exchange Rates on Cash and Cash Equivalents .....	7	2	(3)
Net Increase (Decrease) in Cash and Cash Equivalents .....	78	(666)	685
Cash and Cash Equivalents at Beginning of Period .....	149	815	130
Cash and Cash Equivalents at End of Period .....	<u>\$ 227</u>	<u>\$ 149</u>	<u>\$ 815</u>
<b>Supplemental Disclosures of Cash Flow Information</b>			
Cash paid during the period for:			
Interest (net of amount capitalized) .....	\$ 171	\$ 97	\$ 53
Income taxes .....	\$ 16	\$ 27	\$ 60
<b>Non-cash Contributions from Member</b>			
Intercompany notes and accounts receivable .....			\$ 920

The accompanying Notes to Consolidated Financial Statements are an integral part of the financial statements.

**CONSOLIDATED BALANCE SHEET AT DECEMBER 31,  
PPL Energy Supply, LLC and Subsidiaries**

(Millions of Dollars)

	<u>2003</u>	<u>2002</u>
<b>Assets</b>		
<b>Current Assets</b>		
Cash and cash equivalents (Note 1).....	\$ 227	\$ 149
Accounts receivable (less reserve: 2003, \$68; 2002, \$87).....	320	353
Unbilled revenues .....	215	187
Accounts receivable from affiliates (Note 15).....	71	11
Notes receivable from affiliates (Note 15).....	2	655
Fuel, materials and supplies - at average cost.....	198	200
Price risk management assets (Notes 1 and 17) .....	88	93
Other .....	175	159
	<u>1,296</u>	<u>1,807</u>
<b>Investments</b>		
Investment in unconsolidated affiliates - at equity (Notes 1 and 3).....	212	234
Investment in unconsolidated affiliates - at cost (Note 1).....	126	107
Nuclear plant decommissioning trust fund (Note 6).....	357	287
Other .....	5	10
	<u>700</u>	<u>638</u>
<b>Property, Plant and Equipment - net (Note 1)</b>		
Electric plant in service		
Transmission and distribution .....	3,129	3,390
Generation .....	3,362	2,679
General .....	200	279
	<u>6,691</u>	<u>6,348</u>
Construction work in progress .....	593	176
Nuclear fuel .....	144	129
	<u>7,428</u>	<u>6,653</u>
Electric plant .....	7,428	6,653
Gas and oil plant .....	21	23
Other property.....	163	213
	<u>7,612</u>	<u>6,889</u>
<b>Other Noncurrent Assets</b>		
Goodwill (Note 18).....	1,013	419
Other intangibles (Note 18) .....	96	91
Other .....	533	497
	<u>1,642</u>	<u>1,007</u>
	<u>\$ 11,250</u>	<u>\$ 10,341</u>

*The accompanying Notes to Consolidated Financial Statements are an integral part of the financial statements.*

**CONSOLIDATED BALANCE SHEET AT DECEMBER 31,  
PPL Energy Supply, LLC and Subsidiaries**

(Billions of Dollars)

	<u>2003</u>	<u>2002</u>
<b>Liabilities and Equity</b>		
<b>Current Liabilities</b>		
Short-term debt (Note 8).....	\$ 56	\$ 928
Long-term debt .....	6	6
Accounts payable .....	381	382
Accounts payable to affiliates (Note 15).....	53	76
Above market NUG contracts (Note 14) .....	74	75
Taxes.....	110	114
Interest .....	74	55
Deferred revenue on PLR energy supply to affiliate (Note 15) .....	12	12
Price risk management liabilities (Notes 1 and 17).....	76	96
Other .....	222	216
	<u>1,064</u>	<u>1,960</u>
<b>Long-term Debt</b> .....	<u>4,140</u>	<u>2,225</u>
<b>Long-term Debt with Affiliate Trust (Notes 15 and 22)</b> .....	<u>89</u>	<u></u>
<b>Deferred Credits and Other Noncurrent Liabilities</b>		
Deferred income taxes and investment tax credits (Note 5) .....	1,012	1,022
Above market NUG contracts (Note 14) .....	278	352
Deferred revenue on PLR energy supply to affiliate (Note 15) .....	58	69
Other (Notes 1, 6, 9, 12 and 21).....	1,077	1,084
	<u>2,425</u>	<u>2,527</u>
<b>Commitments and Contingent Liabilities (Note 14)</b> .....	<u></u>	<u></u>
<b>Minority Interest (Note 1)</b> .....	<u>54</u>	<u>36</u>
<b>Company-obligated Mandatorily Redeemable Preferred Securities of Subsidiary Trusts Holding Solely Company Debentures (Note 22)</b> .....	<u></u>	<u>86</u>
<b>Member's Equity</b> .....	<u>3,478</u>	<u>3,507</u>
	<u>\$ 11,250</u>	<u>\$ 10,341</u>

*The accompanying Notes to Consolidated Financial Statements are an integral part of the financial statements.*

**CONSOLIDATED STATEMENT OF MEMBER'S EQUITY AND COMPREHENSIVE INCOME  
FOR THE YEARS ENDED DECEMBER 31,  
PPL Energy Supply, LLC and Subsidiaries**

(Millions of Dollars)

	<u>2003</u>	<u>2002</u>	<u>2001</u>
Member's Equity at beginning of year .....	\$ 3,507	\$ 3,972	\$ 2,577
Comprehensive income:			
Net income .....	727	279	174
Other comprehensive income (loss) (a)			
Foreign currency translation adjustments, net of tax (benefit) of \$0, \$(5), \$15 (b) .....	106	125	(234)
Unrealized gain (loss) on qualifying derivatives, net of tax (benefit) of \$17, \$(15), \$29 .....	33	(23)	46
Minimum pension liability adjustments, net of tax (benefit) of \$(5), \$(128), \$0 (c) .....	(12)	(296)	(1)
Unrealized gain on available-for-sale securities, net of tax of \$12 .....	24		
Total Comprehensive income (loss) .....	<u>878</u>	<u>85</u>	<u>(15)</u>
Member's contributions .....	261	160	1,873
Distributions to Member .....	<u>(1,168)</u>	<u>(710)</u>	<u>(463)</u>
Member's Equity at end of year .....	<u>\$ 3,478</u>	<u>\$ 3,507</u>	<u>\$ 3,972</u>

(a) See Note 1 for disclosure of balances for each component of Accumulated Other Comprehensive Loss.

(b) Includes a \$94 million credit for the write-off of the CEMAR cumulative translation adjustment in June 2002. See Note 9 for additional information.

(c) See Note 12 for additional information on the adjustments to the additional minimum pension liability.

*The accompanying Notes to Consolidated Financial Statements are an integral part of the financial statements.*

**CONSOLIDATED STATEMENT OF COMPANY-OBLIGATED  
MANDATORILY REDEEMABLE SECURITIES AT DECEMBER 31,  
PPL Energy Supply, LLC and Subsidiaries**

(Millions of Dollars)

	<u>Outstanding</u>	
	<u>2003(b)</u>	<u>2002</u>
<b>Company-obligated Mandatorily Redeemable Preferred Securities of Subsidiary Trusts Holding Solely Company Debentures - \$1,000 per security</b>		
8.23% (a) .....	\$	86

- (a) SIUK Capital Trust I issued \$82 million of 8.23% preferred securities maturing in February 2027 and invested the proceeds in 8.23% subordinated debentures, maturing in February 2027, issued by SIUK Limited. Thus, the preferred securities are supported by a corresponding amount of subordinated debentures. SIUK Limited owned all of the common securities of SIUK Capital Trust I and guaranteed all of SIUK Capital Trust I's obligations under the preferred securities. In January 2003, SIUK Limited transferred its assets and liabilities, including the common securities of SIUK Capital Trust I and the obligations under the subordinated debentures, to WPD LLP. Therefore, WPD LLP currently guarantees all of SIUK Capital Trust I's obligations under the preferred securities. SIUK Capital Trust I may, at the discretion of WPD LLP, redeem the preferred securities, in whole or in part, at 104.115% of par beginning February 2007 and thereafter at an annually declining premium over par through January 2017, after which time they are redeemable at par. With PPL Energy Supply's acquisition of the controlling interest in WPD in September 2002, these preferred securities were consolidated on the books of PPL Energy Supply at their then fair value of \$86 million. See Note 9 for information on the acquisition of a controlling interest in WPD.
- (b) On July 1, 2003, PPL Energy Supply adopted the provisions of SFAS 150, "Accounting for Certain Financial Instruments with Characteristics of Both Liabilities and Equity." These preferred securities are mandatorily redeemable financial instruments, as they require the issuer to redeem the securities for cash on a specified date. Thus, they should be classified as liabilities, as a component of long-term debt, instead of "mezzanine" equity on the Balance Sheet. However, as of December 31, 2003, no amounts were included in "Long-term Debt" for these securities because SIUK Capital Trust I was deconsolidated effective December 31, 2003 in connection with the adoption of FIN 46, "Consolidation of Variable Interest Entities, an Interpretation of ARB No. 51," for certain entities. Instead, the subordinated debentures that support the trust preferred securities are reflected in "Long-term Debt with Affiliate Trust" as of December 31, 2003. See Note 22 for additional information on SFAS 150 and FIN 46.

*The accompanying Notes to Consolidated Financial Statements are an integral part of the financial statements.*

# CONSOLIDATED STATEMENT OF LONG-TERM DEBT AT DECEMBER 31, PPL Energy Supply, LLC and Subsidiaries

(Millions of Dollars)

	Outstanding		Maturity (a)
	2003	2002	
6.40% Senior Unsecured Notes .....	\$ 500	\$ 500	November 1, 2003
2.625% Convertible Senior Notes (b).....	400		May 15, 2003
5.875% to 9.25% Unsecured Bonds (c).....	1,982	1,583	2004-2008
Variable rate (3.435% at December 31, 2003) Trust Securities (d).....	31		June 2003
Term loan - variable rate (2.56% at December 31, 2003) (d).....	625		June 2003
8.05% Senior Secured Notes (e).....	284		December 2003
8.30% Senior Secured Notes (e).....	153		December 2003
6.20% - 6.40% Bonds - Inflation-linked bonds (f).....	150	131	2006-2008
6% Bolivian Govt. ....	9	10	2004-2008
2.57% - 18% UF-denominated debt with various banks.....	4	6	2004-2008
9% Note payable.....	1	2	2003-2004
Other Long-term Debt .....	15	3	2003-2004
	<u>4,154</u>	<u>2,235</u>	
Unamortized discount.....	(8)	(4)	
	<u>4,146</u>	<u>2,231</u>	
Less amount due within one year.....	(6)	(6)	
Total Long-term Debt .....	<u>\$ 4,140</u>	<u>\$ 2,225</u>	
<b>Long-term Debt with Affiliate Trust:</b>			
8.23% Subordinated Debentures (g) .....	<u>\$ 89</u>		2003-2008

- (a) Aggregate maturities of long-term debt through 2008 are (millions of dollars): 2004, \$6; 2005, \$185; 2006, \$427; 2007, \$183; 2008, \$885. There are no debt securities outstanding that have sinking fund requirements.
- (b) Issued by PPL Energy Supply in May 2003.
- (c) In March 2003, WPD issued £200 million of 5.875% bonds due 2027 and in May 2003 WPD issued an additional £50 million of 5.875% bonds due 2027. During the fourth quarter, WPD retired \$53 million of 7.375% bonds due 2028.
- (d) Represents lease financing consolidated through a variable interest entity. See Note 22 for additional information. Borrowings bear interest at a floating rate based, at PPL's option, upon (i) LIBOR plus an applicable percentage that is subject to change based on the credit ratings of PPL Energy Supply or (ii) the greater of (a) the Wachovia Bank N.A. corporate base rate or (b) the federal funds rate plus 0.50%, plus an applicable percentage that is subject to change based on the credit ratings of PPL Energy Supply. Secured by, among other things, the generation facilities and the land on which the facilities are located. As of December 31, 2003, the aggregate carrying value of the facilities and the land is \$617 million, net of accumulated depreciation of \$26 million, and is included in "Property, Plant and Equipment - net - Electric plant in service" and "Regulatory and Other Noncurrent Assets - Other intangibles" on the Balance Sheet.
- (e) Represents lease financing consolidated through a variable interest entity. See Note 22 for additional information. Secured by, among other things, the generation facility, which has a carrying value of \$442 million as of December 31, 2003 and is included in "Property, Plant and Equipment - net - Construction work in progress" on the Balance Sheet.
- (f) Increase due to an increase in foreign currency exchange rates.
- (g) Represents debt with a wholly-owned trust that was deconsolidated effective December 31, 2003 as a result of the adoption of FIN 46, "Consolidation of Variable Interest Entities, an Interpretation of ARB No. 51," for certain entities. See Note 22 for further discussion.

*The accompanying Notes to Consolidated Financial Statements are an integral part of the financial statements.*

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**CONSOLIDATED STATEMENT OF INCOME FOR THE YEARS ENDED DECEMBER 31,  
PPL Electric Utilities Corporation and Subsidiaries**

(Millions of Dollars)

	2003	2002	2001
<b>Operating Revenues</b>			
Retail electric .....	\$ 2,597	\$ 2,527	\$ 2,437
Retail electric to affiliate .....	8	23	20
Wholesale electric .....	29	28	33
Wholesale electric to affiliate (Note 15) .....	152	160	176
Energy related businesses .....	2	10	28
<b>Total</b> .....	<b>2,788</b>	<b>2,748</b>	<b>2,694</b>
<b>Operating Expenses</b>			
<b>Operation</b>			
Energy purchases .....	211	208	177
Energy purchases from affiliate (Note 15) .....	1,444	1,431	1,325
Other operation and maintenance .....	345	319	288
Amortization of recoverable transition costs .....	260	226	251
Depreciation (Note 1) .....	103	94	91
Taxes, other than income (Note 5) .....	164	153	116
Energy related businesses .....	1	9	27
Workforce reduction (Note 20) .....	9	33	
<b>Total</b> .....	<b>2,537</b>	<b>2,473</b>	<b>2,275</b>
<b>Operating Income</b> .....	<b>251</b>	<b>275</b>	<b>419</b>
Other Income - net (Note 16) .....	6	16	16
Interest Expense .....	211	218	211
<b>Income Before Income Taxes</b> .....	<b>46</b>	<b>73</b>	<b>205</b>
Income Taxes (Note 5) .....	18	18	65
<b>Income Before Cumulative Effect of a Change in Accounting Principle</b> .....	<b>28</b>	<b>55</b>	<b>140</b>
Cumulative Effect of a Change in Accounting Principle (net of income taxes) (Note 12) .....			5
<b>Income Before Distributions on Preferred Securities</b> .....	<b>28</b>	<b>55</b>	<b>145</b>
Distributions on Preferred Securities .....	3	16	26
<b>Income Available to PPL Corporation</b> .....	<b>\$ 25</b>	<b>\$ 39</b>	<b>\$ 119</b>

*The accompanying Notes to Consolidated Financial Statements are an integral part of the financial statements.*

**CONSOLIDATED STATEMENT OF CASH FLOWS FOR THE YEARS ENDED DECEMBER 31,  
PPL Electric Utilities Corporation and Subsidiaries**

(Millions of Dollars)

	<u>2003</u>	<u>2002</u>	<u>2001</u>
<b>Cash Flows From Operating Activities</b>			
Net income.....	\$ 25	\$ 39	\$ 119
Adjustments to reconcile net income to net cash provided by operating activities			
Depreciation.....	103	94	91
Amortizations - recoverable transition costs and other.....	281	245	260
Distribution requirements - preferred securities.....	3	16	26
Deferred income taxes and investment tax credits.....	17	21	31
Workforce reduction - net of cash paid.....	9	31	
Deferral of storm-related costs.....	(15)		
Prepayment on PLR energy supply from affiliate.....			(90)
Pension income.....	(4)	(17)	(24)
Cumulative effect of a change in accounting principle.....			(5)
Change in current assets and current liabilities			
Accounts receivable.....	21	(65)	76
Accounts payable.....	70	(97)	(113)
Other - net.....	3	5	33
Other operating activities - net			
Other assets.....	(4)	11	(22)
Other liabilities.....	19	(9)	10
Net cash provided by operating activities.....	<u>528</u>	<u>274</u>	<u>392</u>
<b>Cash Flows From Investing Activities</b>			
Expenditures for property, plant and equipment.....	(235)	(224)	(138)
Net (increase) decrease in notes receivable from parent and affiliates.....	90	260	(280)
Other investing activities - net.....		5	(14)
Net cash provided by (used in) investing activities.....	<u>(145)</u>	<u>41</u>	<u>(432)</u>
<b>Cash Flows From Financing Activities</b>			
Issuance of long-term debt.....	190		800
Retirement of long-term debt.....	(430)	(285)	(465)
Retirement of company-obligated mandatorily redeemable preferred securities.....		(250)	
Contribution from parent.....	75	240	
Purchase of treasury stock.....			(280)
Retirement of preferred stock.....	(31)		(15)
Payment of preferred distributions.....	(3)	(22)	(26)
Payment of common dividends to PPL Corporation.....	(29)	(63)	(81)
Net increase (decrease) in short-term debt.....	(15)	15	(59)
Other financing activities - net.....	(7)		(22)
Net cash used in financing activities.....	<u>(250)</u>	<u>(365)</u>	<u>(148)</u>
<b>Net Increase (Decrease) in Cash and Cash Equivalents.....</b>	<b>133</b>	<b>(50)</b>	<b>(188)</b>
Cash and Cash Equivalents at Beginning of Period.....	29	79	267
Cash and Cash Equivalents at End of Period.....	<u>\$ 162</u>	<u>\$ 29</u>	<u>\$ 79</u>
<b>Supplemental Disclosures of Cash Flow Information</b>			
Cash paid during the period for:			
Interest (net of amount capitalized).....	\$ 204	\$ 222	\$ 214
Income taxes.....	\$ 17	\$ 32	\$ 63

*The accompanying Notes to Consolidated Financial Statements are an integral part of the financial statements.*

**CONSOLIDATED BALANCE SHEET AT DECEMBER 31,  
PPL Electric Utilities Corporation and Subsidiaries**

(Millions of Dollars)

	<u>2003</u>	<u>2002</u>
<b>Assets</b>		
<b>Current Assets</b>		
Cash and cash equivalents (Note 1) .....	\$ 162	\$ 29
Accounts receivable (less reserve: 2003, \$24; 2002, \$23) .....	212	216
Unbilled revenues .....	123	113
Accounts receivable from affiliates (Note 15) .....	27	44
Notes receivable from affiliates (Note 15) .....	35	90
Income tax receivable .....	5	35
Prepayments .....	12	51
Prepayment on PLR energy supply from affiliate (Note 15) .....	45	12
Deferred income taxes (Note 5) .....	54	43
Other .....	<u>54</u>	<u>36</u>
	<u>675</u>	<u>669</u>
<b>Property, Plant and Equipment - net (Note 1)</b>		
Electric plant in service		
Transmission and distribution .....	2,327	2,214
General .....	<u>226</u>	<u>192</u>
	2,553	2,406
Construction work in progress .....	<u>31</u>	<u>46</u>
Electric plant .....	2,584	2,452
Other property .....	<u>5</u>	<u>4</u>
	<u>2,589</u>	<u>2,456</u>
<b>Regulatory and Other Noncurrent Assets (Note 1)</b>		
Recoverable transition costs .....	1,687	1,946
Intangibles (Note 18) .....	116	118
Prepayment on PLR energy supply from affiliate (Note 15) .....	58	69
Other .....	<u>344</u>	<u>325</u>
	<u>2,205</u>	<u>2,458</u>
	<u>\$ 5,469</u>	<u>\$ 5,583</u>

*The accompanying Notes to Consolidated Financial Statements are an integral part of the financial statements.*

**CONSOLIDATED BALANCE SHEET AT DECEMBER 31,  
PPL Electric Utilities Corporation and Subsidiaries**

(Millions of Dollars)

	<u>2003</u>	<u>2002</u>
<b>Liabilities and Equity</b>		
<b>Current Liabilities</b>		
Short-term debt .....		\$ 15
Long-term debt .....	\$ 289	274
Accounts payable .....	44	42
Accounts payable to affiliates (Note 15).....	92	24
Taxes .....	86	96
Interest .....	32	34
Other .....	<u>83</u>	<u>63</u>
	<u>626</u>	<u>548</u>
<b>Long-term Debt</b> .....	<u>2,648</u>	<u>2,901</u>
<b>Deferred Credits and Other Noncurrent Liabilities</b>		
Deferred income taxes and investment tax credits (Note 5) .....	728	702
Other (Notes 1 and 12).....	<u>194</u>	<u>203</u>
	<u>922</u>	<u>905</u>
<b>Commitments and Contingent Liabilities (Note 14)</b> .....		
<b>Preferred Stock</b>		
With sinking fund requirements (Notes 8 and 22) .....		31
Without sinking fund requirements.....	<u>51</u>	<u>51</u>
	<u>51</u>	<u>82</u>
<b>Shareowner's Common Equity</b>		
Common stock .....	1,476	1,476
Additional paid-in capital.....	361	282
Treasury stock (Note 1) .....	(912)	(912)
Earnings reinvested.....	304	308
Capital stock expense and other .....	<u>(7)</u>	<u>(7)</u>
	<u>1,222</u>	<u>1,147</u>
	<u>\$ 5,469</u>	<u>\$ 5,583</u>

*The accompanying Notes to Consolidated Financial Statements are an integral part of the financial statements.*

**CONSOLIDATED STATEMENT OF SHAREOWNER'S COMMON EQUITY  
FOR THE YEARS ENDED DECEMBER 31,  
PPL Electric Utilities Corporation and Subsidiaries**

*(Millions of Dollars, except share amounts)*

	<u>2003</u>	<u>2002</u>	<u>2001</u>
Common stock at beginning of year .....	\$ 1,476	\$ 1,476	\$ 1,476
Common stock at end of year .....	<u>1,476</u>	<u>1,476</u>	<u>1,476</u>
Additional paid-in capital at beginning of year.....	282	51	55
Capital contribution from PPL.....	75	240	
Other .....	4	(9)	(4)
Additional paid-in capital at end of year.....	<u>361</u>	<u>282</u>	<u>51</u>
Treasury stock at beginning of year.....	(912)	(912)	(632)
Treasury stock purchased.....			(280)
Treasury stock at end of year .....	<u>(912)</u>	<u>(912)</u>	<u>(912)</u>
Earnings reinvested at beginning of year .....	308	332	277
Net income (a).....	25	39	119
Cash dividends declared on common stock .....	(29)	(63)	(64)
Earnings reinvested at end of year .....	<u>304</u>	<u>308</u>	<u>332</u>
Capital stock expense and other at beginning of year.....	(7)	(16)	(16)
Other .....		9	
Capital stock expense and other at end of year .....	<u>(7)</u>	<u>(7)</u>	<u>(16)</u>
Total Shareowner's Common Equity .....	<u>\$ 1,222</u>	<u>\$ 1,147</u>	<u>\$ 931</u>
Common stock shares at beginning of year (b).....	78,030	78,030	102,230
Treasury stock purchased.....			(24,200)
Common stock shares at end of year .....	<u>78,030</u>	<u>78,030</u>	<u>78,030</u>

(a) PPL Electric's net income approximates comprehensive income.

(b) Shares in thousands. No par value. 170 million shares authorized. All common shares of PPL Electric stock are owned by PPL.

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**CONSOLIDATED STATEMENT OF PREFERRED STOCK AT DECEMBER 31,  
PPL Electric Utilities Corporation and Subsidiaries (a)**

(Millions of Dollars)

	Outstanding		Shares	Shares Authorized
	2003	2002	Outstanding	
	2003	2002	2003	
<b>Preferred Stock - \$100 par, cumulative</b>				
4-1/2% .....	\$ 25	\$ 25	247,524	629,936
Series Preferred.....	26	57	257,665	10,000,000
	<u>\$ 51</u>	<u>\$ 82</u>		

**Details of Preferred Stock (b)**

	Outstanding		Shares	Optional Redemption Price Per Share
	2003	2002	Outstanding	
	2003	2002	2003	
<b>With Sinking Fund Requirements (c)</b>				
Series Preferred				
6.125%.....		\$ 17		
6.15%.....		10		
6.33%.....		4		
		<u>\$ 31</u>		
<b>Without Sinking Fund Requirements</b>				
4-1/2% Preferred.....	\$ 25	\$ 25	247,524	\$ 110.00
Series Preferred				
3.35%.....	2	2	20,605	103.50
4.40%.....	12	12	117,676	102.00
4.60%.....	3	3	28,614	103.00
6.75%.....	9	9	90,770	103.38
	<u>\$ 51</u>	<u>\$ 51</u>		

**Decreases in Preferred Stock**

	2003		2002		2001	
	Shares	Amount	Shares	Amount	Shares	Amount
4-1/2% Preferred.....					(134)	
Series Preferred						
5.95%.....					(10,000)	\$ (1)
6.125%.....	(167,500)	\$ (17)			(148,000)	(14)
6.15%.....	(97,500)	(10)				
6.33%.....	(46,000)	(4)				

Decreases in Preferred Stock normally represent: (i) the redemption of stock pursuant to mandatory sinking fund requirements; or (ii) shares redeemed pursuant to optional redemption provisions.

- (a) Each share of PPL Electric's preferred stock entitles the holder to one vote on any question presented to PPL Electric's shareowners' meetings. There were 5 million shares of PPL Electric's preference stock authorized; none were outstanding at December 31, 2003 and 2002.
- (b) The involuntary liquidation price of the preferred stock is \$100 per share. The optional voluntary liquidation price is the optional redemption price per share in effect, except for the 4-1/2% Preferred Stock for which such price is \$100 per share (plus in each case any unpaid dividends).
- (c) See Note 22 for additional information.

*The accompanying Notes to Consolidated Financial Statements are an integral part of the financial statements.*

**CONSOLIDATED STATEMENT OF LONG-TERM DEBT AT DECEMBER 31,  
PPL Electric Utilities Corporation and Subsidiaries**

(Millions of Dollars)

	Outstanding		Maturity (a)
	2003	2002	
<b>First Mortgage Bonds (b)</b>			
6-7/8%.....		\$ 19	February 1, 2003
6-7/8%.....	\$ 25	25	March 1, 2004
6-1/2%.....	110	110	April 1, 2005
6.55%.....	146	146	March 1, 2006
7-3/8%.....	10	10	2014-2018
6-3/4% to 7-7/8%.....	(c)	66	2019-2023
7.30%.....	6	6	2024-2029
<b>First Mortgage Pollution Control Bonds (b)</b>			
3.125% Series.....	90 (d)		November 1, 2008
6.40% Series H.....	(d)	90	November 1, 2021
5.50% Series I.....	53	53	February 15, 2027
6.40% Series J.....	116	116	September 1, 2029
6.15% Series K.....	55	55	August 1, 2029
<b>Senior Secured Bonds (b)</b>			
5-7/8%.....	300	300	August 15, 2007
6-1/4%.....	500	500	August 15, 2009
4.30%.....	100 (e)		June 1, 2013
	<u>1,511</u>	<u>1,496</u>	
<b>Series 1999-1 Transition Bonds</b>			
6.08% to 7.15%.....	1,423 (f)	1,678	2003-2008
Pollution Control Revenue Bonds - 1.54%.....	9	9	June 1, 2021
	<u>2,943</u>	<u>3,183</u>	
Unamortized discount.....	(6)	(8)	
	<u>2,937</u>	<u>3,175</u>	
Less amount due within one year.....	(289)	(274)	
Total Long-term Debt.....	<u>\$ 2,648</u>	<u>\$ 2,901</u>	

- (a) Aggregate maturities of long-term debt through 2008 are (millions of dollars): 2004, \$289; 2005, \$376; 2006, \$434; 2007, \$600; and 2008, \$395. There are no bonds outstanding that have sinking fund requirements.
- (b) The First Mortgage Bonds and the First Mortgage Pollution Control Bonds were issued under, and are secured by, the lien of the 1945 First Mortgage Bond Indenture. The lien of the 1945 First Mortgage Bond Indenture covers substantially all electric transmission and distribution plant owned by PPL Electric. The Senior Secured Bonds were issued under the 2001 Senior Secured Bond Indenture. The Senior Secured Bonds are secured by (i) an equal principal amount of First Mortgage Bonds issued under the 1945 First Mortgage Bond Indenture and (ii) the lien of the 2001 Senior Secured Bond Indenture, which covers substantially all electric transmission and distribution plant owned by PPL Electric and which is junior to the lien of the 1945 First Mortgage Bond Indenture.
- (c) In April 2003, PPL Electric redeemed and retired all of its outstanding First Mortgage Bonds, 7-7/8% Series due 2023, at an aggregate par value of \$46 million and in December 2003, retired \$19 million of its First Mortgage Bonds 6-3/4% Series due 2023.
- (d) In February 2003, PPL Electric issued \$90 million of 3.125% Series Pollution Control Bonds and also retired \$90 million of its 6.40% Series H Pollution Control Bonds.
- (e) In May 2003, PPL Electric issued \$100 million of 4.30% Senior Secured Bonds.
- (f) In August 1999, PPL Transition Bond Company issued \$2.4 billion of transition bonds to securitize a portion of PPL Electric's stranded costs. The bonds were issued in eight different classes, with expected average lives of 1 to 8.7 years. Bond principal payments of \$255 million were made in 2003.

The accompanying Notes to Consolidated Financial Statements are an integral part of the financial statements.

**CONSOLIDATED STATEMENT OF INCOME FOR THE YEARS ENDED DECEMBER 31,  
PPL Montana, LLC and Subsidiaries**

(Millions of Dollars)

	<u>2003</u>	<u>2002</u>	<u>2001</u>
<b>Operating Revenues</b>			
Wholesale energy marketing .....	\$ 287	\$ 237	\$ 335
Wholesale energy marketing to affiliate (Note 15).....	64	68	80
Net energy trading margins.....		(1)	6
Other .....	<u>3</u>	<u>2</u>	<u>3</u>
Total.....	<u>354</u>	<u>306</u>	<u>424</u>
<b>Operating Expenses</b>			
Operation			
Fuel.....	36	32	30
Energy purchases.....	73	53	82
Other operation and maintenance .....	97	98	101
Transmission.....	11	7	8
Depreciation (Note 1).....	11	11	10
Taxes, other than income (Note 5).....	<u>16</u>	<u>17</u>	<u>16</u>
Total.....	<u>244</u>	<u>218</u>	<u>247</u>
<b>Operating Income</b> .....	<b>110</b>	<b>88</b>	<b>177</b>
Other Income - net.....	9		3
Interest Expense.....	<u>5</u>	<u>6</u>	<u>9</u>
<b>Income Before Income Taxes</b> .....	<b>114</b>	<b>82</b>	<b>171</b>
Income Taxes (Note 5) .....	<u>45</u>	<u>35</u>	<u>68</u>
<b>Income Before Cumulative Effect of a Change in Accounting Principle</b> .....	<b>69</b>	<b>47</b>	<b>103</b>
Cumulative Effect of a Change in Accounting Principle (net of income taxes) (Note 14).....	<u>(1)</u>		
<b>Net Income</b> .....	<u><u>\$ 68</u></u>	<u><u>\$ 47</u></u>	<u><u>\$ 103</u></u>

*The accompanying Notes to Consolidated Financial Statements are an integral part of the financial statements.*

**CONSOLIDATED STATEMENT OF CASH FLOWS FOR THE YEARS ENDED DECEMBER 31,  
PPL Montana, LLC and Subsidiaries**

(Millions of Dollars)

	<u>2003</u>	<u>2002</u>	<u>2001</u>
<b>Cash Flows From Operating Activities</b>			
Net income.....	\$ 68	\$ 47	\$ 103
Adjustments to reconcile net income to net cash provided by operating activities			
Cumulative effect of a change in accounting principle .....	1		
Allowance for doubtful accounts.....	(10)		28
Depreciation .....	11	11	10
Amortization - wholesale energy commitments .....	(6)	(17)	(20)
Deferred income taxes.....	21	17	7
Changes in current assets and liabilities			
Accounts receivable .....	6	(5)	38
Accounts receivable/payable to Member.....	(4)	(14)	(27)
Accounts receivable/payable to affiliate.....	3	6	(22)
Accounts payable and accrued expenses .....	2	(2)	(17)
Other - net.....	(8)	(6)	(10)
Other operating activities			
Prepaid operating lease for generating assets.....	(25)	(27)	(15)
Pension funding.....	(12)	9	12
Other - net.....	7	(5)	2
Net cash provided by operating activities.....	<u>54</u>	<u>14</u>	<u>89</u>
<b>Cash Flows From Investing Activities</b>			
Proceeds from sale of property, plant and equipment.....			5
Expenditures for property, plant and equipment.....	(21)	(19)	(26)
Net cash used in investing activities.....	<u>(21)</u>	<u>(19)</u>	<u>(21)</u>
<b>Cash Flows From Financing Activities</b>			
Net borrowings (repayments) on revolving line of credit with affiliate.....	(26)	(18)	44
Distribution to Member .....	(5)		(167)
Net cash used in financing activities .....	<u>(31)</u>	<u>(18)</u>	<u>(123)</u>
<b>Net Increase (Decrease) in Cash and Cash Equivalents .....</b>	<b>2</b>	<b>(23)</b>	<b>(55)</b>
Cash and Cash Equivalents at Beginning of Period.....	<u>1</u>	<u>24</u>	<u>79</u>
Cash and Cash Equivalents at End of Period.....	<u>\$ 3</u>	<u>\$ 1</u>	<u>\$ 24</u>
<b>Supplemental Disclosures of Cash Flow Information</b>			
Cash paid during the period for:			
Interest .....	\$ 1	\$ 1	\$ 2
Income taxes .....	\$ 30	\$ 32	\$ 88

*The accompanying Notes to Consolidated Financial Statements are an integral part of the financial statements.*

**CONSOLIDATED BALANCE SHEET AT DECEMBER 31,  
PPL Montana, LLC and Subsidiaries**

(Millions of Dollars)

	<u>2003</u>	<u>2002</u>
<b>Assets</b>		
<b>Current Assets</b>		
Cash and cash equivalents (Note 1).....	\$ 3	\$ 1
Accounts receivable (less reserve: 2003, \$36; 2002, \$46) .....	5	3
Unbilled revenues.....	23	23
Accounts receivable from joint owners.....	9	8
Accounts receivable from Member .....	6	2
Fuel, materials and supplies - at average cost.....	7	6
Price risk management assets (Notes 1 and 17).....	14	12
Deferred income taxes (Note 5) .....	10	17
Prepayments and other .....	6	4
	<u>83</u>	<u>76</u>
<b>Noncurrent Assets</b>		
Property, plant and equipment - net (Note 1) .....	443	433
Prepaid operating lease for generating assets (Note 10).....	80	55
Intangibles (Note 18).....	43	39
Deferred income taxes (Note 5) .....		12
Other.....	27	28
	<u>593</u>	<u>567</u>
	<u>\$ 676</u>	<u>\$ 643</u>
<b>Liabilities and Equity</b>		
<b>Current Liabilities</b>		
Accounts payable .....	\$ 34	\$ 31
Accounts payable to affiliates .....	4	1
Revolving line of credit with affiliate (Notes 8 and 15).....		26
Accrued expenses.....	16	17
Price risk management liabilities (Notes 1 and 17).....	7	12
Wholesale energy commitments (Note 14) .....	3	2
	<u>64</u>	<u>89</u>
<b>Noncurrent Liabilities</b>		
Employee benefit obligations.....	16	27
Wholesale energy commitments (Note 14).....	54	62
Deferred income taxes (Note 5) .....	6	
Other (Note 12) .....	31	31
	<u>107</u>	<u>120</u>
<b>Commitments and Contingent Liabilities (Note 14) .....</b>		
<b>Member's Equity .....</b>	<u>505</u>	<u>434</u>
	<u>\$ 676</u>	<u>\$ 643</u>

The accompanying Notes to Consolidated Financial Statements are an integral part of the financial statements.

**CONSOLIDATED STATEMENT OF MEMBER'S EQUITY AND COMPREHENSIVE INCOME  
FOR THE YEARS ENDED DECEMBER 31,  
PPL Montana, LLC and Subsidiaries**

*(Millions of Dollars)*

	<u>2003</u>	<u>2002</u>	<u>2001</u>
Member's Equity at beginning of year .....	\$ 434	\$ 421	\$ 453
Comprehensive income:			
Net income (a) .....	68	47	103
Other comprehensive income (loss): (a)			
Unrealized gain (loss) on qualifying derivatives, net of tax (benefit) of \$4, (19), \$21 .....	7	(29)	33
Minimum pension liability adjustment .....	<u>1</u>	<u>(5)</u>	<u>(1)</u>
Total comprehensive income	76	13	135
Distribution to Member .....	<u>(5)</u>	<u>          </u>	<u>(167)</u>
Member's Equity at end of year .....	<u>\$ 505</u>	<u>\$ 434</u>	<u>\$ 421</u>

(a) See Note 1 for disclosure of balances for each component of Accumulated Other Comprehensive Income.

*The accompanying Notes to Consolidated Financial Statements are an integral part of the financial statements.*

## COMBINED NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Terms and abbreviations appearing in Combined Notes to Consolidated Financial Statements are explained in the glossary. Dollars are in millions, except per share data, unless otherwise noted.

### **1. Summary of Significant Accounting Policies**

#### **Business and Consolidation**

*(PPL, PPL Energy Supply and PPL Electric)*

PPL is an energy and utility holding company that, through its subsidiaries, is primarily engaged in the generation and marketing of electricity in the northeastern and western U.S. and in the delivery of electricity in Pennsylvania, the U.K. and Latin America. Based in Allentown, Pennsylvania, PPL's principal subsidiaries are PPL Energy Funding, PPL Electric, PPL Gas Utilities, PPL Services and PPL Capital Funding.

*(PPL and PPL Energy Supply)*

PPL Energy Funding is the parent of PPL Energy Supply, which serves as the holding company for PPL's principal unregulated subsidiaries. PPL Energy Supply is the parent of PPL Generation, PPL EnergyPlus and PPL Global.

PPL Generation owns and operates a portfolio of domestic power generating assets. These power plants are located in Pennsylvania, Montana, Arizona, Illinois, Connecticut, New York and Maine and use well-diversified fuel sources including coal, nuclear, natural gas, oil and hydro. PPL EnergyPlus markets or brokers electricity produced by PPL Generation, along with purchased power, natural gas and oil in competitive wholesale and deregulated retail markets, primarily in the northeastern and western portions of the U.S. PPL Global acquires and develops domestic generation projects that are, in turn, operated by PPL Generation as part of its portfolio of generation assets. PPL Global also acquires and holds international energy projects that are primarily focused on the distribution of electricity.

*(PPL and PPL Electric)*

PPL Electric is the principal regulated subsidiary of PPL. PPL Electric's principal businesses are the transmission and distribution of electricity to serve retail customers in its franchised territory in eastern and central Pennsylvania, and the supply of electricity to retail customers in that territory as a PLR.

*(PPL, PPL Energy Supply and PPL Montana)*

PPL Montana commenced operations in 1999, after the purchase of substantially all of the generation assets and certain contracts of the utility division of Montana Power. PPL Montana operates steam generation and hydroelectric facilities throughout Montana. PPL Montana has been designated as an

EWG under the Federal Power Act and sells wholesale power throughout the western U.S. PPL Montana Holdings, LLC is the sole Member of PPL Montana and is an indirect, wholly-owned subsidiary of PPL.

*(PPL, PPL Energy Supply, PPL Electric and PPL Montana)*

The consolidated financial statements of PPL, PPL Energy Supply, PPL Electric and PPL Montana include each company's own accounts as well as the accounts of all entities in which the company has a controlling financial interest. Investments in entities in which the company has the ability to exercise significant influence but does not have a controlling financial interest are accounted for under the equity method. All other investments are carried at cost. All significant intercompany transactions have been eliminated. Any minority interests in operating results, and equity ownership, are reflected in the consolidated financial statements.

*(PPL and PPL Energy Supply)*

It is the policy of PPL and PPL Energy Supply to consolidate foreign subsidiaries and record equity in earnings of other foreign entities on a lag, based on the availability of financial data on a U.S. GAAP basis:

- Earnings from foreign equity method investments are recorded on a three-month lag.
- PPL and PPL Energy Supply consolidate the results of foreign entities in which they have a controlling financial interest (WPD, Emel, EC, the Bolivian subsidiaries and other investments) on a one-month lag.

Effective August 21, 2002, PPL Energy Supply deconsolidated CEMAR and began accounting for it using the cost method. See Note 9 for further discussion.

Effective December 31, 2003, PPL's and PPL Energy Supply's consolidated financial statements include the accounts of the lessors under the operating leases for the Sundance, University Park and Lower Mt. Bethel generation facilities. These entities are not included in the consolidated financial statements for periods ending prior to December 31, 2003. See "FIN 46 and FIN 46(R)" in Note 22 for further discussion.

Effective December 31, 2003, PPL deconsolidated PPL Capital Funding Trust I, a wholly-owned trust, and PPL Energy Supply deconsolidated SIUK Capital Trust I, also a wholly-owned trust. Both entities are included in PPL's consolidated financial statements for periods ending prior to December 31, 2003. SIUK Capital Trust I is included in PPL Energy Supply's consolidated financial statements for periods ending prior to December 31, 2003. See "FIN 46 and FIN 46(R)" in Note 22 for further discussion.

The consolidated financial statements of PPL and PPL Energy Supply include their share of undivided interests in jointly-owned facilities, as well as their share of the related operating costs of those facilities. See Note 13 for additional information.

**Use of Estimates** (PPL, PPL Energy Supply, PPL Electric and PPL Montana)

The preparation of financial statements in conformity with U.S. GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities, the disclosure of contingent liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

PPL records loss accruals in accordance with SFAS 5, "Accounting for Contingencies."

**Accounting Records** (PPL and PPL Electric)

The system of accounts for PPL Electric and PPL Gas Utilities are maintained in accordance with the Uniform System of Accounts prescribed by the FERC and adopted by the PUC.

**Cash Equivalents** (PPL, PPL Energy Supply, PPL Electric and PPL Montana)

All highly liquid debt instruments purchased with original maturities of three months or less are considered to be cash equivalents.

**Property, Plant and Equipment**

(PPL, PPL Energy Supply, PPL Electric and PPL Montana)

PP&E is recorded at original cost, unless impaired. If impaired, the asset is written down to fair value at that time, which becomes the asset's new cost basis. Original cost includes material, labor, contractor costs, construction overheads and financing costs, where applicable. The cost of repairs and minor replacements are charged to expense as incurred. PPL records costs associated with planned major maintenance projects in the period in which the costs are incurred. No costs are accrued in advance of the period in which the work is performed.

When a component of PP&E is retired that was depreciated under the composite or group method, the original cost is charged to accumulated depreciation. When all or a significant portion of an operating unit is retired or sold that was depreciated under the composite or group method, the property and the related accumulated depreciation account is reduced and any gain or loss is included in income, unless otherwise required by regulators. Depreciation is computed over the estimated useful lives of property using various methods including the straight-line, composite and group methods. PPL and its subsidiaries periodically review and adjust the depreciable lives of their fixed assets.

AFUDC is capitalized as part of the construction costs for regulated projects. Interest is capitalized as part of construction costs for non-regulated projects.

Following are the classes of PP&E, with the associated accumulated depreciation, at December 31:

	2003			
	PPL	PPL Energy Supply	PPL Electric	PPL Montana
Electric plant				
Generation	\$ 8,191	\$ 8,191		\$ 403
Transmission and distribution	7,324	3,568	\$ 3,756	
General	728	365	353	54
Construction work in progress	627	593	31	20
Nuclear fuel	308	308		
Gas and oil	321	63		
Other property	276	214	5	
	17,775	13,302	4,145	477
Less: Accumulated depreciation and amortization	7,329	5,690	1,556	34
	<u>\$ 10,446</u>	<u>\$ 7,612</u>	<u>\$ 2,589</u>	<u>\$ 443</u>

	2002			
	PPL	PPL Energy Supply	PPL Electric	PPL Montana
Electric plant				
Generation	\$ 7,407	\$ 7,407		\$
Transmission and distribution	7,279	3,695	\$ 3,584	
General	749	414	324	41
Construction work in progress	223	176	46	14
Nuclear fuel	312	312		
Gas and oil	321	64		
Other property	301	262	5	
	16,592	12,330	3,959	458
Less: Accumulated depreciation and amortization	7,026	5,441	1,503	25
	<u>\$ 9,566</u>	<u>\$ 6,889</u>	<u>\$ 2,456</u>	<u>\$ 433</u>

Following are the weighted-average rates of depreciation at December 31:

	2003			
	PPL	PPL Energy Supply	PPL Electric	PPL Montana
Generation	2.01%	2.01%		2.14%
Transmission and distribution	3.16%	4.10%	2.31%	
General	3.75%	3.96%	3.64%	4.39%

## Debt Securities

(PPL, PPL Energy Supply and PPL Electric)

Debt securities that have been classified as held-to-maturity have been so classified due to the intent to hold such securities to maturity and the ability to do so. All other debt securities have been classified as available-for-sale or trading.

## Regulation

(PPL, PPL Energy Supply and PPL Electric)

PPL Electric, PPL Gas Utilities, and a Latin American affiliate account for regulated operations in accordance with the provisions of SFAS 71, "Accounting for the Effects of Certain Types of Regulation," which requires rate-regulated entities to reflect the effects of regulatory decisions in their financial statements.

The following regulatory assets were included in the "Regulatory and Other Noncurrent Assets" section of the Balance Sheet at December 31:

	PPL		PPL Electric	
	2003	2002	2003	2002
Recoverable transition costs	\$ 1,687	\$ 1,946	\$ 1,687	\$ 1,946
Taxes recoverable through future rates	250	260	242	235
Other	24	13	20	8
	<u>\$ 1,961</u>	<u>\$ 2,219</u>	<u>\$ 1,949</u>	<u>\$ 2,189</u>

Based on the PUC Final Order, PPL Electric began amortizing its competitive transition (or stranded) costs, \$2.97 billion, over an 11-year transition period effective January 1, 1999. In August 1999, competitive transition costs of \$2.4 billion were converted to intangible transition costs when they were securitized by the issuance of transition bonds. The intangible transition costs are being amortized over the life of the transition bonds, through December 2008, in accordance with an amortization schedule filed with the PUC. The assets of PPL Transition Bond Company, including the intangible transition property, are not available to creditors of PPL or PPL Electric. The transition bonds are obligations of PPL Transition Bond Company and are non-recourse to PPL and PPL Electric. The remaining competitive transition costs are also being amortized based on an amortization schedule previously filed with the PUC, adjusted for those competitive transition costs that were converted to intangible transition costs. As a result of the conversion of a significant portion of the competitive transition costs into intangible transition costs, amortization of substantially all of the remaining competitive transition costs will occur in 2009.

Included in "Other" above, are approximately \$15 million of storm restoration costs associated with the September 2003 Hurricane Isabel. These costs have been deferred in accordance with the PUC declaratory order of January 16, 2004. The

2002

	PPL	PPL Energy Supply	PPL Electric	PPL Montana
Generation	1.88%	1.88%		2.16%
Transmission and distribution	2.99%	3.70%	2.30%	
General	2.72%	2.99%	2.54%	4.75%

The annual provisions for depreciation have been computed principally in accordance with the following ranges, in years, of assets lives:

	PPL	PPL Energy Supply	PPL Electric	PPL Montana
Generation	5-65	5-65		30-50
Transmission and distribution	15-80	30-40	15-80	
General	3-80	3-60	10-80	5-55

(PPL and PPL Energy Supply)

As of July 1, 2003, PPL Energy Supply changed the depreciable lives of its gas-fired peaking plants from 30 to 40 years based upon engineering estimates. This change decreased depreciation by \$1 million in 2003 and is expected to decrease depreciation by \$8 million in 2004 and thereafter, which includes the impact for certain gas-fired peaking plants consolidated in accordance with FIN 46. See Note 22 for further discussion of FIN 46.

(PPL Electric)

When a component of regulated PP&E is retired, the original cost plus the cost of retirement, less salvage, is charged to accumulated depreciation.

### Property, Plant and Equipment and Intangible Asset Impairments (PPL, PPL Energy Supply, PPL Electric and PPL Montana)

Long-lived assets and identifiable intangibles held and used by PPL and its subsidiaries are reviewed for impairment when events or circumstances indicate carrying amounts may not be recoverable. An impairment loss is recognized if the carrying amount of PP&E and identifiable intangibles is not recoverable from undiscounted future cash flow. The impairment charge is measured by the difference between the carrying amount of the asset and its fair value. Goodwill is reviewed for impairment annually or more frequently when events or circumstances indicate that the carrying value may be greater than the implied fair value. If the carrying value of the reporting unit exceeds its fair value, the implied fair value of goodwill must be calculated. If the implied fair value goodwill is less than its carrying value, the difference represents the amount of impairment. See Notes 9 and 18 for a discussion of asset impairment charges recorded.

ratemaking treatment of these losses will be addressed in the 2004 rate proceeding. PPL and PPL Electric believe there is a reasonable basis for recovery of all regulatory assets.

### **Accounting for Derivatives and Other Contracts Held for Trading Purposes** (PPL, PPL Energy Supply and PPL Montana)

PPL Energy Supply and PPL Montana enter into energy and energy-related contracts. PPL and PPL Energy Supply enter into interest rate derivative contracts to hedge their exposure to changes in the fair value of their debt instruments and to hedge their exposure to variability in expected cash flows associated with existing debt instruments or forecasted transactions. PPL and PPL Energy Supply also enter into foreign currency derivative contracts to hedge foreign currency exposures, including firm commitments, recognized assets or liabilities, forecasted transactions or net investments.

Contracts that meet the definition of a derivative are accounted for under SFAS 133, "Accounting for Derivative Instruments and Hedging Activities," as amended and interpreted. Certain energy contracts have been excluded from the requirements of SFAS 133 because they meet the definition of a "normal purchase or normal sale" under DIG Issue C15, "Scope Exceptions: Normal Purchases and Normal Sales Exception for Certain Option-Type Contracts and Forward Contracts in Electricity." These contracts are reflected in the financial statements using the accrual method of accounting.

Additionally, PPL, PPL Energy Supply and PPL Montana adopted SFAS No. 149, "Amendment of Statement 133 on Derivative Instruments and Hedging Activities," as of July 1, 2003. The requirements of SFAS 149, which required prospective application, placed additional limitations on the use of the normal purchase or normal sale exception. Therefore, the accounting for certain types of transactions has been changed on a prospective basis to conform with SFAS 149.

Under SFAS 133, all derivatives are recognized on the balance sheet at their fair value. On the date the derivative contract is executed, PPL designates the derivative as a hedge of the fair value of a recognized asset or liability or of an unrecognized firm commitment ("fair value" hedge), a hedge of a forecasted transaction or of the variability of cash flows to be received or paid related to a recognized asset or liability ("cash flow" hedge), a foreign currency fair value or cash flow hedge ("foreign currency" hedge), a hedge of a net investment in a foreign operation or a trading derivative. Changes in the fair value of a derivative that is highly effective as, and is designated and qualifies as, a fair value hedge, along with the loss or gain on the hedged asset or liability that is attributable to the hedged risk, are recorded in current-period earnings. Changes in the fair value of a derivative that is highly effective as, and is designated as and qualifies as, a cash flow hedge are recorded in other comprehensive income, until earnings are affected by the variability of cash flows being hedged. Changes in the fair value of derivatives that are designated as and qualify as foreign currency hedges are recorded in either current-period earnings

or other comprehensive income, depending on whether the hedge transaction is a fair value hedge or a cash flow hedge. If a derivative is used as a hedge of a net investment in a foreign operation, its changes in fair value, to the extent effective as a hedge, are recorded within other comprehensive income. Changes in the fair value of derivatives that are not designated as hedging instruments are reported in current-period earnings.

Unrealized gains and losses from changes in market prices of energy contracts accounted for as fair value hedges are reflected in "Energy purchases" on the Statement of Income, as are changes in the underlying positions. Gains and losses from changes in market prices of energy contracts accounted for as cash flow hedges, when recognized on the Statement of Income are reflected in "Wholesale energy marketing" revenues or "Energy purchases," consistent with the hedged item. Gains and losses from changes in the market price of interest rate and foreign currency derivative contracts, when recognized on the Statement of Income, are accounted for in "Interest Expense."

Gains or losses on interest rate derivative contracts that settled prior to the adoption of SFAS 133 were deferred and are being recognized over the life of the debt. Market gains and losses on foreign currency derivative contracts that settled prior to the adoption of SFAS 133 were recognized in accordance with SFAS 52, "Foreign Currency Translation," and are included in "Foreign currency translation adjustments," a component of accumulated other comprehensive income (loss).

In the fourth quarter of 2002, PPL Energy Supply and PPL Montana adopted the accounting requirements under EITF "Issues Involved in Accounting for Derivative Contracts Held for Trading Purposes and Contracts Involved in Energy Trading and Risk Management Activities." As such, PPL reflects its net realized and unrealized gains and losses associated with all derivatives that are held for trading purposes in the "Net energy trading margins" line on the Statement of Income. Non-derivative contracts that met the definition of energy trading activities as defined by EITF 98-10, "Accounting for Energy Trading and Risk Management Activities" are reflected in the financial statements using the accrual method of accounting. Prior periods were restated.

PPL Energy Supply and PPL Montana have adopted the final provisions of EITF 03-11, "Reporting Realized Gains and Losses on Derivative Instruments That Are Subject to FASB Statement No. 133 and Not 'Held for Trading Purposes' as Defined in Issue No. 02-3," prospectively as of October 1, 2003. As a result of the adoption, non-trading bilateral sales of electricity at major market delivery points are netted with purchases that offset the sales at those same delivery points. A major market delivery point is any delivery point with liquid pricing available. The impact of adopting EITF 03-11 was a reduction in both "Wholesale energy marketing" revenues and "Energy purchases" of \$105 million in PPL's and PPL Energy Supply's Statement of Income and by \$18 million in PPL Montana's Statement of Income.

See Note 17 for additional information on SFAS 133, its amendments and related accounting guidance.

## Revenue Recognition

*(PPL, PPL Energy Supply, PPL Electric and PPL Montana)*

Operating revenues, except for energy related businesses, are recorded based on energy deliveries through the end of the calendar month. Unbilled retail revenues result because customers' meters are read and bills are rendered throughout the month, rather than all being read at the end of the month. Unbilled revenues for a month are calculated by multiplying an estimate of unbilled kWh by the estimated average cents per kWh. Unbilled wholesale energy revenues are recorded at month end to reflect estimated amounts until actual dollars and MWhs are confirmed and invoiced. At that time unbilled revenue is reversed and actual revenue is recorded.

"Energy related businesses" revenue includes revenues from the mechanical contracting and engineering subsidiaries and PPL Global's proportionate share of affiliate earnings under the equity or cost method of accounting, as described in the "Business and Consolidation" section of Note 1. The mechanical contracting and engineering subsidiaries record profits from construction contracts on the percentage-of-completion method of accounting. Income from time and material contracts is recognized currently as the work is performed.

## Utility Revenue

*(PPL and PPL Energy Supply)*

The Statement of Income "Utility" line item contains revenues from domestic and international rate-regulated delivery operations, including WPD.

WPD revenues are stated net of value-added tax.

*(PPL Electric)*

Since most of PPL Electric's operations are regulated, it is not meaningful to use a "Utility" caption. Therefore, the revenues of PPL Electric are presented according to specific types of revenue.

## Income Taxes

*(PPL, PPL Energy Supply, PPL Electric and PPL Montana)*

The income tax provision for PPL and its subsidiaries is calculated in accordance with SFAS 109, "Accounting for Income Taxes." PPL and its domestic subsidiaries file a consolidated U.S. federal income tax return.

*(PPL Energy Supply, PPL Electric and PPL Montana)*

The provision for PPL Energy Supply, PPL Electric and PPL Montana is calculated in accordance with an intercompany tax sharing policy which provides that the taxable income be calculated as if PPL Energy Supply, PPL Electric and PPL Montana and its domestic subsidiaries filed a separate consolidated return.

*(PPL and PPL Electric)*

The provision for PPL Electric's deferred income taxes for regulated assets is based upon the ratemaking principles reflected in rates established by the PUC and the FERC. The difference in the provision for deferred income taxes for regulated assets and the amount that otherwise would be recorded under U.S. GAAP is deferred and included in taxes recoverable through future rates in "Regulatory and Other Noncurrent Assets - Other" on the Balance Sheet. See Note 5 for additional information.

PPL Electric deferred investment tax credits when they were utilized and is amortizing the deferrals over the average lives of the related assets.

*(PPL Montana)*

PPL Montana is a limited liability company and has elected to be classified as an association taxable as a corporation for federal and state income tax purposes. The current tax benefit or provision recognized for each period is reported in "Accounts receivable from Member" or "Accounts payable to affiliates" on the Balance Sheet, as applicable.

## Leases

*(PPL, PPL Energy Supply, PPL Electric and PPL Montana)*

PPL and its subsidiaries apply the provisions of SFAS 13, "Accounting for Leases," as amended and interpreted, to all leasing transactions. See Note 10 for a discussion of accounting for leases under which PPL, PPL Energy Supply, PPL Electric and PPL Montana are lessees.

*(PPL and PPL Energy Supply)*

In 2002, PPL began commercial operation of its 79.9 MW oil-powered station in Shoreham, New York. The Long Island Power Authority has contracted to purchase all of the plant's capacity and ancillary services as part of a 15-year power purchase agreement with PPL EnergyPlus. The capacity payments in the power purchase agreement result in the plant being classified as a direct financing lease, under which PPL EnergyPlus is the lessor. As of December 31, 2003 and 2002, PPL and PPL Energy Supply had a receivable balance of \$277 million and \$260 million (included in "Current Assets - Other" and "Regulatory and Other Noncurrent Assets - Other" for PPL and "Current Assets - Other" and "Other Noncurrent Assets - Other" for PPL Energy Supply) and an unearned revenue

balance of \$167 million and \$152 million (included in "Deferred Credits and Other Noncurrent Liabilities - Other"). Rental income received through this direct financing lease during 2003 and 2002 was \$15 million and \$5 million. Total future minimum lease payments expected to be received are estimated at \$16 million for each of the years from 2004 through 2008.

## Stock-Based Compensation

*(PPL, PPL Energy Supply, PPL Electric and PPL Montana)*

PPL grants stock options, restricted stock, restricted stock units and stock units to employees and directors under several stock-based compensation plans. SFAS 123, "Accounting for Stock-Based Compensation," encourages entities to record compensation expense for stock-based compensation plans at fair value but provides the option of measuring compensation expense using the intrinsic value method prescribed by APB Opinion No. 25, "Accounting for Stock Issued to Employees." The fair value method under SFAS 123 is the preferable method of accounting for stock-based compensation, as it provides a consistent basis of accounting for all stock-based awards, thereby facilitating a better measure of compensation cost and improved financial reporting.

Prior to 2003, PPL accounted for stock-based compensation in accordance with APB Opinion No. 25, as permitted by SFAS 123. Effective January 1, 2003, PPL and its subsidiaries adopted the fair value method of accounting for stock-based compensation, as prescribed by SFAS 123, using the prospective method of transition permitted by SFAS 148, "Accounting for Stock-Based Compensation - Transition and Disclosure, an Amendment of FASB Statement No. 123." See Note 22 for further discussion of SFAS 148. The prospective method of transition requires PPL and its subsidiaries to use the fair value method under SFAS 123 for all stock-based compensation awards granted, modified or settled on or after January 1, 2003. Thus, all awards granted prior to January 1, 2003 continue to be accounted for under the intrinsic value method of APB Opinion No. 25, to the extent such awards are not modified or settled. Stock-based compensation is included in "Other operation and maintenance" expense on PPL's Statement of Income.

Use of the fair value method prescribed by SFAS 123 requires PPL and its subsidiaries to recognize compensation expense for stock options issued. Fair value for the stock options is determined using the Black-Scholes options pricing model.

PPL and its subsidiaries were not required to recognize compensation expense for stock options issued under the intrinsic value method of APB Opinion No. 25, since PPL grants stock options with an exercise price that is not less than the fair market value of PPL's common stock on the date of grant. For stock options granted under the fair value method of SFAS 123, stock option expense for PPL was approximately \$3 million for 2003. As currently structured, awards of restricted stock, restricted stock units and stock units result in the same amount of compensation expense under the fair value method of

SFAS 123 as they would under the intrinsic value method of APB Opinion No. 25.

The following table illustrates the pro forma effect on net income and EPS as if the fair value method had been used to account for all outstanding stock-based compensation awards for the years shown:

<i>(PPL)</i>	<u>2003</u>	<u>2002</u>	<u>2001</u>
<b>Income</b>			
Net Income - as reported	\$ 734	\$ 208	\$ 1
Add: Stock-based employee compensation expense included in reported net income, net of tax	5	3	
Deduct: Total stock-based compensation expense determined under the fair value based method for all awards, net of tax	<u>9</u>	<u>8</u>	
Pro forma net income	<u>\$ 730</u>	<u>\$ 203</u>	<u>\$ 1</u>
<b>EPS</b>			
Basic - as reported	\$ 4.25	\$ 1.37	\$ 1.
Basic - pro forma	\$ 4.23	\$ 1.34	\$ 1.
Diluted - as reported	\$ 4.24	\$ 1.36	\$ 1.
Diluted - pro forma	\$ 4.22	\$ 1.33	\$ 1.

*(PPL Energy Supply)*

	<u>2003</u>	<u>2002</u>	<u>2001</u>
<b>Income</b>			
Net Income - as reported	\$ 727	\$ 279	\$ 1
Add: Stock-based employee compensation expense included in reported net income, net of tax	3	2	
Deduct: Total stock-based compensation expense determined under the fair value based method for all awards, net of tax	<u>6</u>	<u>5</u>	
Pro forma net income	<u>\$ 724</u>	<u>\$ 276</u>	<u>\$ 1</u>

Stock-based compensation expense includes an allocation of PPL Services' expense.

*(PPL Electric and PPL Montana)*

Stock-based compensation expense, including awards granted to employees and an allocation of costs of awards granted to employees of PPL Services, was insignificant under both the intrinsic value and fair value methods for each of 2003, 2002 and 2001.

## Pension and Other Postretirement Benefits *(PPL, PPL Energy Supply, PPL Electric and PPL Montana)*

See Note 12 for a discussion of accounting for pension and other postretirement benefits.

## Comprehensive Income

*(PPL and PPL Energy Supply)*

Comprehensive income consists of net income and other comprehensive income, defined as changes in common equity from transactions not related to shareowners. Other comprehensive income consists of foreign currency translation adjustments recorded by PPL Global, unrealized gains or losses on available-for-sale securities and qualifying derivatives, and the excess of additional pension liability over unamortized prior service costs, net of taxes. Comprehensive income is reflected on the PPL Statement of Shareowners' Common Equity and Comprehensive Income, and "Accumulated other comprehensive loss" is presented on the PPL Balance Sheet. Comprehensive income is reflected on the PPL Energy Supply Statement of Member's Equity and Comprehensive Income, and accumulated other comprehensive loss is included in Member's Equity on the PPL Energy Supply Balance Sheet.

The accumulated other comprehensive loss of PPL consisted of the following at December 31:

	<u>2003</u>	<u>2002</u>
Foreign currency translation adjustments	\$ (37)	\$ (143)
Unrealized gains (losses) on available-for-sale securities	20	(4)
Minimum pension liability	(316)	(306)
Unrealized gains on qualifying derivatives	<u>36</u>	<u>7</u>
	<u>\$ (297)</u>	<u>\$ (446)</u>

The accumulated other comprehensive loss of PPL Energy Supply consisted of the following at December 31:

	<u>2003</u>	<u>2002</u>
Foreign currency translation adjustments	\$ (37)	\$ (143)
Unrealized gains (losses) on available-for-sale securities	22	(2)
Minimum pension liability	(309)	(297)
Unrealized gains on qualifying derivatives	<u>56</u>	<u>23</u>
	<u>\$ (268)</u>	<u>\$ (419)</u>

*(PPL Montana)*

Comprehensive income consists of net income and other comprehensive income, defined as changes in Member's equity from transactions other than with the Member. Other comprehensive income consists of unrealized gains or losses on qualifying derivatives and the excess of additional pension liability over unamortized prior service costs, net of taxes. Comprehensive income is reflected on the Statement of Member's Equity and Comprehensive Income. The accumulated other comprehensive income (loss) of PPL Montana at December 31, 2003 and 2002 was \$6 million and \$(2) million. The 2003 balance consisted of the following: minimum pension liability adjustment of \$(5) million and unrealized gains on qualifying derivatives of \$11 million.

## Treasury Stock *(PPL and PPL Electric)*

Treasury shares are reflected on the balance sheet as an offset to common equity under the cost method of accounting. Management has no definitive plans for the future use of these shares. Treasury shares are not considered outstanding in calculating EPS.

## Foreign Currency Translation and Transactions *(PPL and PPL Energy Supply)*

Assets and liabilities of international operations, where the local currency is the functional currency, are translated at year-end exchange rates, and related revenues and expenses are translated at average exchange rates prevailing during the year. Adjustments resulting from translation are recorded in accumulated other comprehensive loss.

Gains or losses relating to foreign currency transactions are recognized currently in income. The aggregate transaction gain (loss) was \$(1) million, \$(9) million and \$8 million in 2003, 2002 and 2001.

## Independent System Operator *(PPL, PPL Energy Supply and PPL Electric)*

Certain PPL subsidiaries participate in PJM in several roles. Certain PPL subsidiaries also participate in the New England Power Pool (NEPOOL) and the New York ISO (NYISO) in a less significant way than in PJM. In PJM, PPL EnergyPlus is a marketer, a load-serving entity to its customers who selected it as a supplier under the Customer Choice Act and a seller for PPL's Pennsylvania generation subsidiaries. PPL Electric is a transmission owner and provider of last resort in PJM. In NEPOOL, PPL EnergyPlus is a marketer and a seller for PPL's New England generating assets. In the NYISO, PPL EnergyPlus acts as a marketer. PPL Electric does not participate in NEPOOL or NYISO.

A function of interchange accounting is to match participants' MWh entitlements (generation plus scheduled bilateral purchases) against their MWh obligations (load plus scheduled bilateral sales) during every hour of every day. If the net result during any given hour is an entitlement, the participant is credited with a spot market sale to the ISO at the respective market price for that hour; if the net result is an obligation, the participant is charged with a spot market purchase from the ISO at the respective market price for that hour. ISO purchases and sales are not allocated to individual customers.

PPL records the hourly net sales and purchases in its financial statements as sales to and purchases from the respective ISOs, in accordance with the FERC and industry accounting.

## Reclassifications *(PPL, PPL Energy Supply, PPL Electric and PPL Montana)*

Certain amounts in the 2002 and 2001 financial statements have been reclassified to conform to the current presentation.

**Other (PPL, PPL Energy Supply, PPL Electric and PPL Montana)**

See Note 18 for a discussion of the accounting for goodwill and other intangible assets, Note 21 for a discussion of the accounting for asset retirement obligations, and Note 22 for a discussion of other new accounting standards.

**2. Segment and Related Information**

*(PPL and PPL Energy Supply)*

PPL's reportable segments are Supply, Delivery and International. The Supply segment primarily consists of the domestic energy marketing, domestic generation and domestic development operations of PPL Energy Supply. The Delivery segment includes the regulated electric and gas delivery operations of PPL Electric and PPL Gas Utilities. The International segment includes PPL Global's responsibility for the acquisition and holding of international energy projects. The majority of PPL Global's international investments are located in the U.K., Chile, El Salvador and Bolivia.

PPL Energy Supply's reportable segments are Supply and International. The International segment at the PPL Energy Supply level is consistent with the International segment at the PPL level. The Supply segment information reported at the PPL Energy Supply level will not agree with the Supply segment information reported at the PPL level. Additional Supply segment functions, including telecommunications, exist at PPL that are outside of PPL Energy Supply. Furthermore, certain income items, including PLR revenue and certain interest income, exist at the PPL Energy Supply level, but are eliminated in consolidation at the PPL level. Finally, certain expense items are fully allocated to the segments at the PPL level only.

Segments include direct charges, as well as an allocation of indirect corporate costs, for services provided by PPL Services. These service costs include functions such as financial, legal, human resources and information services.

Financial data for the segments are as follows:

	PPL			PPL Energy Supply		
	2003	2002	2001	2003	2002	2001
<b>Income Statement Data</b>						
<b>Revenues from external customers</b>						
Supply	\$ 1,795	\$ 1,697	\$ 1,668	\$ 3,235	\$ 3,128	\$ 3,235
Delivery	2,778	2,706	2,867			
International (a)	<u>1,014</u>	<u>1,078</u>	<u>580</u>	<u>1,014</u>	<u>1,078</u>	<u>580</u>
	5,587	5,481	5,115	4,249	4,206	3,715
<b>Intersegment revenues</b>						
Supply	1,451	1,434	1,331			
Delivery	160	183	196			
<b>Equity in earnings of unconsolidated affiliates</b>						
Supply	(14)	(12)	12	(11)	(11)	11
International (a)	<u>3</u>	<u>3</u>	<u>113</u>	<u>3</u>	<u>3</u>	<u>113</u>
	(11)	(9)	125	(8)	(8)	124
<b>Depreciation</b>						
Supply	120	129	126	116	127	126
Delivery	110	100	96			
International (a)	<u>150</u>	<u>138</u>	<u>44</u>	<u>150</u>	<u>138</u>	<u>44</u>
	380	367	266	266	265	166
<b>Amortizations - recoverable transition costs and other</b>						
Supply	(27)	(38)	(35)	(38)	(56)	(35)
Delivery	<u>271</u>	<u>236</u>	<u>259</u>			
	244	198	224	(38)	(56)	199
<b>Interest income</b>						
Supply	(2)	(5)	3	17	26	17
Delivery	7	20	10			
International (a)	<u>7</u>	<u>13</u>	<u>2</u>	<u>7</u>	<u>13</u>	<u>2</u>
	12	28	15	24	39	19
<b>Interest expense</b>						
Supply	43	108	58	(19)	(29)	(4)
Delivery	214	214	233			
International (a)	<u>218</u>	<u>239</u>	<u>95</u>	<u>218</u>	<u>239</u>	<u>95</u>
	475	561	386	199	210	405
<b>Income taxes</b>						
Supply	177	119	153	215	199	233
Delivery	23	24	71			
International (a)	<u>(30)</u>	<u>67</u>	<u>37</u>	<u>(30)</u>	<u>67</u>	<u>37</u>
	170	210	261	185	266	270
<b>Net Income</b>						
Supply (b)	502	356	368	531	475	488
Delivery	36	48	126			
International (c)	<u>196</u>	<u>(196)</u>	<u>(315)</u>	<u>196</u>	<u>(196)</u>	<u>(315)</u>
	\$ 734	\$ 208	\$ 179	\$ 727	\$ 279	\$ 173

	PPL			PPL Energy Supply		
	2003	2002	2001	2003	2002	2001
<b>Cash Flow Data</b>						
Expenditures for property, plant and equipment						
Supply	\$ 274	\$ 299	\$ 290	\$ 260	\$ 291	\$ 254
Delivery	251	237	153			
International	246	113	126	246	113	126
	771	649	569	506	404	380

<b>Investment in generating assets and electric energy projects</b>						
Supply		261	176		261	176
International (d)		211	136		211	136
	\$	\$ 472	\$ 312	\$	\$ 472	\$ 312

#### Balance Sheet Data

	PPL		PPL Energy Supply	
	2003	2002	2003	2002
<b>Net investment in unconsolidated affiliates - at equity</b>				
Supply	\$ 207	\$ 198	\$ 189	\$ 198
International	23	36	23	36
	230	234	212	234
<b>Total assets</b>				
Supply	6,491	4,910	6,308	5,566
Delivery	5,690	5,867		
International	4,942	4,775	4,942	4,775
	\$ 17,123	\$ 15,552	\$ 11,250	\$ 10,341

#### Geographic Data

	PPL			PPL Energy Supply		
	2003	2002	2001	2003	2002	2001
<b>Revenues from external customers</b>						
Domestic	\$ 4,573	\$ 4,403	\$ 4,535	\$ 3,235	\$ 3,128	\$ 3,212
Foreign (a)	1,014	1,078	580	1,014	1,078	580
	\$ 5,587	\$ 5,481	\$ 5,115	\$ 4,249	\$ 4,206	\$ 3,792

#### Property, plant and equipment - net

	PPL		PPL Energy Supply	
	2003	2002	2003	2002
Domestic	\$ 7,072	\$ 5,795	\$ 4,238	\$ 3,118
Foreign	3,374	3,771	3,374	3,771
	\$ 10,446	\$ 9,566	\$ 7,612	\$ 6,889

- (a) 2002 contains the consolidated results of WPD. See Note 9 for additional information on the acquisition of a controlling interest in WPD.
- (b) 2003 includes two cumulative-effect changes in accounting principle recorded in January and December 2003. See Notes 21 and 22 for additional information.
- (c) 2002 includes the cumulative-effect change in accounting principle recorded in March 2002. See Note 18 for additional information. The International segment also includes the write-downs of the CEMAR investment recorded in March and June 2002 described in Note 9.
- (d) The 2002 amount represents the acquisition of the controlling interest in WPD.

### 3. Investment in Unconsolidated Affiliates - at Equity

(PPL and PPL Energy Supply)

In the third quarter of 2002, PPL Global acquired a controlling interest in WPD. As a result, PPL Global fully consolidated the financial results of WPD at September 30, 2002. See Note 9 for additional information.

Investment in unconsolidated affiliates accounted for under the equity method were as follows as of December 31 (equity ownership percentages as of December 31, 2003):

	2003	2002
Aguaytia Energy, LLC - 11.4%	\$ 11	\$ 14
Bangor Pacific Hydro Associates - 50.0%	15	14
Hidro Iberica, B.V. - 50.0%	9	8
Latin American Energy & Electricity Fund I, LP - 16.6%	3	3
Safe Harbor Water Power Corporation - 33.3%	15	17
SIUK Capital Trust I - 100%	3	
Southwest Power Partners, LLC - 50.0%	156	167
Teesside Power Limited - 15.4%		
Other PPL Global investments (a)		11
Total PPL Energy Supply	\$ 212	\$ 234
PPL Capital Funding Trust I - 100%	18	
Total PPL	\$ 230	\$ 234

- (a) In 2003, PPL Global sold its investment in Wind Resources Limited, and fully consolidated its investment in TransEmel upon acquisition of the remaining interest. See Note 9 for additional information on TransEmel.

Summarized below is information from the financial statements of unconsolidated affiliates accounted for under the equity method, underlying the amounts included in the consolidated financial statements:

	PPL			PPL Energy Supply		
	2003	2002	2001(a)	2003	2002	2001(a)
<b>Income Statement Data</b>						
Revenues	\$ 126	\$ 118	\$ 111	\$ 126	\$ 118	\$ 111
Operating Income	17	13	42	17	13	42
Net Income (Loss)	(5)	(9)	52	(6)	(9)	52
<b>Balance Sheet Data</b>						
	PPL		PPL Energy Supply			
	As of December 31,		As of December 31,			
	2003	2002	2003	2002		
Current Assets	\$ 131	\$ 139	\$ 126	\$ 139		
Noncurrent Assets	1,414	807	821	807		
Current Liabilities	47	31	42	31		
Noncurrent Liabilities	924	298	349	298		

#### Balance Sheet Data

Current Assets	\$ 131	\$ 139	\$ 126	\$ 139
Noncurrent Assets	1,414	807	821	807
Current Liabilities	47	31	42	31
Noncurrent Liabilities	924	298	349	298

- (a) For purpose of comparability, the summarized information of WPD is excluded from 2001.

#### 4. Earnings Per Share

(PPL)

Basic EPS is calculated by dividing "Net Income" on the Statement of Income by the weighted-average number of common shares outstanding during the period. Diluted EPS is calculated similarly for PPL, except that weighted average shares outstanding are increased for additional shares that would be outstanding if potentially dilutive securities were converted to common stock. Potentially dilutive securities consist of:

- stock options, restricted stock and restricted stock units granted under the incentive compensation plans,
- stock units representing common stock granted under the directors compensation programs,
- common stock purchase contracts that are a component of the PEPS units, and
- convertible senior notes.

The basic and diluted EPS calculations, and the reconciliation of the shares (in thousands) used in the calculations, are shown below:

	2003	2002	2001
<b>Income (Numerator)</b>			
Income from continuing operations	\$ 719	\$ 360	\$ 169
Loss from discontinued operations	(20)	(2)	
Cumulative effect of a change in accounting principle (net of tax)	35	(150)	10
Net Income	\$ 734	\$ 208	\$ 179
<b>Shares (Denominator)</b>			
Shares for Basic EPS	172,795	152,492	145,974
Add: Incremental shares			
Stock options and other share-based awards	597	317	640
Shares for Diluted EPS	173,392	152,809	146,614
<b>Basic EPS</b>			
Income from continuing operations	\$ 4.16	\$ 2.36	\$ 1.16
Loss from discontinued operations	(0.11)	(0.01)	
Cumulative effect of a change in accounting principle (net of tax)	0.20	(0.98)	0.07
Net Income	\$ 4.25	\$ 1.37	\$ 1.23
<b>Diluted EPS</b>			
Income from continuing operations	\$ 4.15	\$ 2.36	\$ 1.15
Loss from discontinued operations	(0.11)	(0.01)	
Cumulative effect of a change in accounting principle (net of tax)	0.20	(0.99)	0.07
Net Income	\$ 4.24	\$ 1.36	\$ 1.22

In May 2001, PPL and PPL Capital Funding Trust I issued 23 million PEPS Units that contain a purchase contract component for PPL's common stock. The purchase contracts will only be dilutive if the average price of PPL's common stock exceeds a threshold appreciation price, which is adjusted for cash

distributions on PPL common stock. The appreciation price was initially set at \$65.03 and has subsequently been adjusted to \$63.94 as of December 31, 2003 based on dividends paid on PPL's common stock since issuance. Since the average price has not exceeded the threshold appreciation price, the purchase contracts were excluded from the diluted EPS calculations.

In January 2004, PPL completed an exchange offer resulting in the exchange of approximately 4 million PEPS Units for PEPS Units, Series B. The primary difference in the units relates to the debt component. The purchase contract components of both units, which are potentially dilutive, are identical. The threshold appreciation price for the purchase contract component of the PEPS Units, Series B was set at the last adjusted threshold appreciation price of \$63.94 for the PEPS Units and will be adjusted in the same manner as that of the PEPS Units. See Note 8 for a more detailed discussion of the exchange offer.

In May 2003, PPL Energy Supply issued \$400 million of 2.625% Convertible Senior Notes due 2023. The notes are guaranteed by PPL and can be converted into shares of PPL common stock, at an initial conversion rate of 20.1106 shares per \$1,000 principal amount of notes, subject to adjustment if:

- during any fiscal quarter starting after June 30, 2003, the market price of PPL's common stock trades at or above \$59.67 per share over a certain period during the preceding fiscal quarter;
- PPL calls the debt for redemption;
- the holder exercises its right to put the debt on any five-year anniversary of the offering;
- the long-term credit rating assigned to the notes by Moody's and Standard & Poor's falls below Ba2 and BB or the notes are not rated; or
- certain specified corporate transactions occur, e.g., change in control and certain distributions to the holders of PPL common stock.

As none of these events has occurred, the Convertible Senior Notes were excluded from the diluted EPS calculations.

The following number of stock options to purchase PPL common shares were excluded in the periods' computations of diluted EPS, because the exercise price of the options was greater than the average market price of the common shares. Therefore, the effect would have been antidilutive.

(Thousands of Shares)	2003	2002	2001
Antidilutive stock options	1,683	1,294	896

#### 5. Income and Other Taxes

For 2003, 2002 and 2001, the statutory U.S. corporate federal income tax rate was 35%. The statutory corporate net income tax rates for Pennsylvania and Montana were 9.99% and 6.75%

(PPL)

The tax effects of significant temporary differences comprising PPL's net deferred income tax liability were as follows:

	2003	2002
<b>Deferred Tax Assets</b>		
Deferred investment tax credits	\$ 48	\$ 54
NUG contracts & buybacks	168	203
Accrued pension costs	81	89
Foreign loss carryforwards	278	232
Foreign - pensions	144	125
Foreign - other	18	3
Write-down of generation assets		18
Impairment write-down		91
Contribution in aid of construction	63	56
Other	222	223
Valuation allowance	<u>(288)</u>	<u>(327)</u>
	<u>734</u>	<u>767</u>
<b>Deferred Tax Liabilities</b>		
Plant - net	1,061	976
Restructuring - CTC	613	700
Taxes recoverable through future rates	106	104
Reacquired debt costs	11	11
Foreign - plant	617	792
Foreign - pensions	227	167
Foreign - other	6	38
Other domestic	73	31
	<u>2,714</u>	<u>2,819</u>
<b>Net deferred tax liability</b>	<u>\$ 1,980</u>	<u>\$ 2,052</u>

Details of the components of income tax expense, a reconciliation of federal income taxes derived from statutory tax rates applied to income from continuing operations for accounting purposes, and details of taxes other than income are as follows:

	2003	2002	2001
<b>Income Tax Expense</b>			
Current-Federal	\$ 26	\$ 41	\$ 270
Current-State	13	(9)	36
Current-Foreign	<u>35</u>	<u>52</u>	<u>8</u>
	<u>74</u>	<u>84</u>	<u>314</u>
Deferred-Federal	39	70	(86)
Deferred-State	24	27	4
Deferred-Foreign	<u>48</u>	<u>44</u>	<u>44</u>
	<u>111</u>	<u>141</u>	<u>(38)</u>
Investment tax credit, net-federal	<u>(15)</u>	<u>(15)</u>	<u>(15)</u>
<b>Total</b>	<u>\$ 170</u>	<u>\$ 210</u>	<u>\$ 261</u>
Total income tax expense-Federal	\$ 50	\$ 96	\$ 169
Total income tax expense-State	37	18	40
Total income tax expense-Foreign	<u>83</u>	<u>96</u>	<u>52</u>
<b>Total</b>	<u>\$ 170</u>	<u>\$ 210</u>	<u>\$ 261</u>

**Reconciliation of Income Tax Expense**

	2003	2002	2001
Indicated federal income tax on pre-tax income before cumulative effect of a change in accounting principle at statutory tax rate - 35%	\$ 324	\$ 250	\$ 168
Increase/(decrease) due to:			
State income taxes	25	11	25
Amortization of investment tax credit	(10)	(11)	(11)
International energy projects - charges (benefits)	(83)	14	144
Difference related to income recognition of foreign affiliates (net of foreign income taxes)	(7)	18	(9)
Federal income tax credits	(52)	(50)	(40)
Contribution of property	(9)		
Other	<u>(18)</u>	<u>(22)</u>	<u>(16)</u>
	<u>(154)</u>	<u>(40)</u>	<u>93</u>
<b>Total income tax expense</b>	<u>\$ 170</u>	<u>\$ 210</u>	<u>\$ 261</u>
<b>Effective income tax rate</b>	18.4%	29.4%	54.4%
<b>Taxes, Other than Income</b>			
State gross receipts	\$ 155	\$ 154	\$ 112
State utility realty	3	3	4
State capital stock	27	7	20
Property - foreign	44	42	
Domestic property and other	<u>27</u>	<u>25</u>	<u>19</u>
	<u>\$ 256</u>	<u>\$ 231</u>	<u>\$ 155</u>

PPL Global had foreign net operating loss carryforwards of approximately \$13 million and \$28 million at December 31, 2003 and 2002. PPL Global also had foreign capital loss carryforwards of \$920 million at December 31, 2003 and \$760 million at December 31, 2002. All of these losses have an unlimited carryforward period. However, it is more likely than not that these losses will not be utilized and as such, a full valuation allowance has been provided.

PPL Global does not pay or record U.S. income taxes on the undistributed earnings of its foreign subsidiaries where management has determined that the earnings are permanently reinvested. The cumulative undistributed earnings are included in "Earnings reinvested" on the Balance Sheet. The amounts considered permanently reinvested at December 31, 2003 and 2002 were \$530 million and \$295 million. If the earnings were remitted as dividends, PPL Global may be subject to additional U.S. taxes, net of allowable foreign tax credits. It is not practical to estimate the amount of additional taxes that might be payable on these foreign earnings.

*(PPL Energy Supply)*

The tax effects of significant temporary differences comprising PPL Energy Supply's net deferred income tax liability were as follows:

	2003	2002
<b>Deferred Tax Assets</b>		
Deferred investment tax credits	\$ 37	\$ 42
NUG contracts & buybacks	168	203
Accrued pension costs	26	34
Foreign loss carryforwards	278	232
Foreign – pensions	144	125
Foreign - other	18	3
Write-down of generation assets		18
Impairment write-down		91
Other domestic	120	120
Valuation allowance	(288)	(327)
	<u>503</u>	<u>541</u>
<b>Deferred Tax Liabilities</b>		
Plant - net	469	396
Foreign investments	9	10
Foreign - plant	617	792
Foreign - pensions	227	167
Foreign - other	6	38
Other domestic	54	25
	<u>1,382</u>	<u>1,428</u>
<b>Net deferred tax liability</b>	<u>\$ 879</u>	<u>\$ 887</u>

Details of the components of income tax expense, a reconciliation of federal income taxes derived from statutory tax rates applied to income from continuing operations for accounting purposes, and details of taxes other than income are as follows:

	2003	2002	2001
<b>Income Tax Expense</b>			
Current-Federal	\$ (15)	\$ 22	\$ 210
Current-State	11	(6)	44
Current-Foreign	35	52	8
	<u>31</u>	<u>68</u>	<u>262</u>
Deferred-Federal	94	134	(22)
Deferred-State	24	32	2
Deferred-Foreign	48	44	44
	<u>166</u>	<u>210</u>	<u>24</u>
Investment tax credit, net-federal	(12)	(12)	(12)
<b>Total</b>	<u>\$ 185</u>	<u>\$ 266</u>	<u>\$ 274</u>
Total income tax expense-Federal	\$ 67	\$ 144	\$ 176
Total income tax expense-State	35	26	46
Total income tax expense-Foreign	83	96	52
<b>Total</b>	<u>\$ 185</u>	<u>\$ 266</u>	<u>\$ 274</u>

#### Reconciliation of Income Tax Expense

	2003	2002	2001
Indicated federal income tax on pre-tax income before cumulative effect of a change in accounting principle at statutory tax rate - 35%	\$ 318	\$ 274	\$ 274
Increase/(decrease) due to:			
State income taxes	27	17	17
Amortization of investment tax credit	(8)	(8)	(8)
International energy projects - charges (benefits)	(83)	14	14
Difference related to income recognition of foreign affiliates (net of foreign income taxes)	(7)	18	18
Federal income tax credits	(52)	(50)	(50)
Other	(10)	1	1
	<u>(133)</u>	<u>(8)</u>	<u>(8)</u>
<b>Total income tax expense</b>	<u>\$ 185</u>	<u>\$ 266</u>	<u>\$ 274</u>
<b>Effective income tax rate</b>	20.4%	33.9%	33.9%
<b>Taxes, Other than Income</b>			
State gross receipts	\$ 3	\$ 4	\$ 4
State capital stock	14	9	9
Property - foreign	44	42	42
Domestic property and other	28	23	23
	<u>\$ 89</u>	<u>\$ 78</u>	<u>\$ 78</u>

PPL Global had foreign net operating loss carryforwards of approximately \$13 million and \$28 million at December 31, 2003 and 2002. PPL Global also had foreign capital loss carryforwards of \$920 million at December 31, 2003 and \$760 million at December 31, 2002. All of these losses have an unlimited carryforward period. However, it is more likely than not that these losses will not be utilized and as such, a full valuation allowance has been provided.

PPL Global does not pay or record U.S. income taxes on the undistributed earnings of its foreign subsidiaries where management has determined that the earnings are permanently reinvested. The cumulative undistributed earnings are included in "Earnings reinvested" on the Balance Sheet. The amounts considered permanently reinvested at December 31, 2003 and 2002 were \$530 million and \$295 million. If the earnings were remitted as dividends, PPL Global may be subject to additional U.S. taxes, net of allowable foreign tax credits. It is not practical to estimate the amount of additional taxes that might be payable on these foreign earnings.

*(PPL Electric)*

The tax effects of significant temporary differences comprising PPL Electric's net deferred income tax liability were as follows:

	2003	2002
<b>Deferred Tax Assets</b>		
Deferred investment tax credits	\$ 9	\$ 11
Accrued pension costs	34	33
Contribution in aid of construction	62	55
Other	<u>64</u>	<u>61</u>
	<u>169</u>	<u>160</u>

<b>Deferred Tax Liabilities</b>		
Electric utility plant - net	558	529
Restructuring - CTC	143	145
Taxes recoverable through future rates	100	99
Reacquired debt costs	11	10
Other	<u>18</u>	<u>11</u>
	<u>830</u>	<u>794</u>
<b>Net deferred tax liability</b>	<u>\$ 661</u>	<u>\$ 634</u>

Details of the components of income tax expense, a reconciliation of federal income taxes derived from statutory tax rates applied to income from continuing operations for accounting purposes, and details of taxes other than income are as follows:

	2003	2002	2001
<b>Income Tax Expense</b>			
Current-Federal	\$ (2)	\$ (8)	\$ 31
Current-State	<u>3</u>	<u>5</u>	<u>6</u>
	<u>1</u>	<u>(3)</u>	<u>37</u>
Deferred-Federal	22	27	27
Deferred-State	<u>(2)</u>	<u>(3)</u>	<u>4</u>
	<u>20</u>	<u>24</u>	<u>31</u>
Investment tax credit, net-federal	<u>(3)</u>	<u>(3)</u>	<u>(3)</u>
Total	<u>\$ 18</u>	<u>\$ 18</u>	<u>\$ 65</u>
Total income tax expense-Federal	\$ 17	\$ 16	\$ 55
Total income tax expense-State	<u>1</u>	<u>2</u>	<u>10</u>
Total	<u>\$ 18</u>	<u>\$ 18</u>	<u>\$ 65</u>

**Reconciliation of Income Tax Expense**

Indicated federal income tax on pre-tax income before cumulative effect of a change in accounting principle at statutory tax rate - 35%	\$ 16	\$ 26	\$ 72
Increase/(decrease) due to:			
State income taxes	1	1	4
Flow through of depreciation differences not previously normalized	1		
Amortization of investment tax credit	(2)	(3)	(3)
Other	<u>2</u>	<u>(6)</u>	<u>(8)</u>
	<u>2</u>	<u>(8)</u>	<u>(7)</u>
<b>Total income tax expense</b>	<u>\$ 18</u>	<u>\$ 18</u>	<u>\$ 65</u>
<b>Effective income tax rate</b>	39.1%	24.7%	31.7%

	2003	2002	2001
<b>Taxes, Other than Income</b>			
State gross receipts	\$ 152	\$ 151	\$ 105
State utility realty	3	3	4
State capital stock	10	(2)	8
Property and other	<u>(1)</u>	<u>1</u>	<u>(1)</u>
	<u>\$ 164</u>	<u>\$ 153</u>	<u>\$ 116</u>

(PPL Montana)

The tax effects of significant temporary differences comprising PPL Montana's net deferred income tax asset were as follows:

	2003	2002
<b>Deferred Tax Assets</b>		
Wholesale energy commitments	\$ 22	\$ 25
Accrued retirement cost	5	9
Allowance for doubtful accounts	14	18
Other	<u>2</u>	<u>2</u>
	<u>43</u>	<u>54</u>
<b>Deferred Tax Liabilities</b>		
PP&E	26	17
Mark-to-market	6	2
Other	<u>7</u>	<u>6</u>
	<u>39</u>	<u>25</u>
<b>Net deferred tax asset</b>	<u>\$ 4</u>	<u>\$ 29</u>

Details of the components of income tax expense, a reconciliation of federal income taxes derived from statutory tax rates applied to income from continuing operations for accounting purposes, and details of taxes other than income are as follows:

	2003	2002	2001
<b>Income Tax Expense</b>			
Current-Federal	\$ 19	\$ 12	\$ 50
Current-State	<u>5</u>	<u>6</u>	<u>11</u>
	<u>24</u>	<u>18</u>	<u>61</u>
Deferred-Federal	18	14	5
Deferred-State	<u>3</u>	<u>3</u>	<u>2</u>
	<u>21</u>	<u>17</u>	<u>7</u>
	<u>\$ 45</u>	<u>\$ 35</u>	<u>\$ 68</u>
Total income tax expense-Federal	\$ 37	\$ 26	\$ 55
Total income tax expense-State	<u>8</u>	<u>9</u>	<u>13</u>
	<u>\$ 45</u>	<u>\$ 35</u>	<u>\$ 68</u>

Susquehanna units. If approved, the operating licenses would be extended from 2022 to 2042 for Unit 1 and from 2024 to 2044 for Unit 2.

## 7. Financial Instruments

At December 31, 2003 and 2002, the carrying value of cash and cash equivalents, nuclear plant decommissioning trust fund, other investments and short-term debt approximated fair value due to the short-term nature of the instruments, variable interest rates associated with the financial instruments or the carrying value of the instruments being based on established market prices. Price risk management assets and liabilities are valued using either exchange traded market quotes or prices obtained through third party brokers and are recorded at fair value. Financial instruments where the carrying amount on the Balance Sheet and the estimated fair value (based on quoted market prices for the securities where available and estimates based on current rates offered to PPL where quoted market prices are not available) are different, are set forth below:

(PPL)

	December 31, 2003		December 31, 2002	
	Carrying Amount	Fair Value	Carrying Amount	Fair Value
<b>Liabilities</b>				
Long-term debt	\$ 7,859	\$ 8,589	\$ 6,267	\$ 6,267
Long-term debt with affiliate trusts	681	612		
Company-obligated mandatorily redeemable preferred securities of subsidiary trusts holding solely company debentures			661	
Preferred stock with sinking fund requirements			31	

(PPL Energy Supply)

	December 31, 2003		December 31, 2002	
	Carrying Amount	Fair Value	Carrying Amount	Fair Value
<b>Liabilities</b>				
Long-term debt	\$ 4,146	\$ 4,530	\$ 2,231	\$ 2,231
Long-term debt with affiliate trust	89	87		
Company-obligated mandatorily redeemable preferred securities of subsidiary trusts holding solely company debentures			86	

	2003	2002	2001
<b>Reconciliation of Income Tax Expense:</b>			
Indicated federal income tax on pre-tax income at statutory tax rate - 35%	\$ 40	\$ 29	\$ 60
Increase/(decrease) due to:			
State income taxes	5	7	9
Other		(1)	(1)
	5	6	8
<b>Total income tax expense</b>	<b>\$ 45</b>	<b>\$ 35</b>	<b>\$ 68</b>
<b>Effective income tax rate</b>	<b>39.5%</b>	<b>42.7%</b>	<b>39.8%</b>
<b>Taxes, Other than Income</b>			
Property taxes	\$ 14	\$ 15	\$ 14
Generation taxes	2	2	2
	\$ 16	\$ 17	\$ 16

## 6. Nuclear Decommissioning Costs

(PPL and PPL Energy Supply)

The cost to decommission the Susquehanna station is based on a 2002 site-specific study to dismantle and decommission each unit immediately following final shutdown. PPL Susquehanna's 90% share of the total estimated cost of decommissioning the Susquehanna station was approximately \$936 million measured in 2002 dollars. This estimate includes decommissioning the radiological portions of the station and the cost of removal of non-radiological structures and materials.

Beginning in January 1999, in accordance with the PUC Final Order, approximately \$130 million of decommissioning costs are being recovered from customers through the CTC over the 11-year life of the CTC rather than the remaining life of Susquehanna. The recovery will include a return on unamortized decommissioning costs. Effective January 1, 2003, PPL adopted SFAS 143 "Accounting for Asset Retirement Obligations." In connection with the adoption, the previously recorded liability for nuclear decommissioning of \$296 million was reversed and a liability of \$202 million was recorded. Accretion expense, as determined under the provisions of SFAS 143, was \$16 million in 2003 and is included in "Other operation and maintenance." In 2002 and 2001, decommissioning expenses were \$22 million and \$24 million, and were recorded as a component of depreciation expense. Accrued nuclear decommissioning expenses, as determined under the provisions of SFAS 143, were \$218 million at December 31, 2003, and are included in "Deferred Credits and Other Noncurrent Liabilities - Other." See Note 21 for additional information on SFAS 143.

Amounts collected from PPL Electric's customers for decommissioning, less applicable taxes, are deposited in external trust funds for investment and can be used only for future decommissioning costs.

In November 2001, PPL Susquehanna notified the NRC that it intends to file for 20-year license renewals for each of the

(PPL Electric)

	December 31, 2003		December 31, 2002	
	Carrying Amount	Fair Value	Carrying Amount	Fair Value
Liabilities				
Long-term debt	\$ 2,937	\$ 3,215	\$ 3,175	\$ 3,476
Preferred stock with sinking fund requirements			31	30

(PPL Montana)

At December 31, 2003 and 2002, the carrying value of cash and cash equivalents, and the revolving line of credit approximated fair value due to either the short-term nature of the instruments or variable interest rates associated with the financial instruments. Price risk management assets and liabilities are valued using either exchange traded market quotes or prices obtained through third party brokers and are recorded at fair value.

## 8. Credit Arrangements and Financing Activities

### Credit Arrangements

(PPL, PPL Energy Supply and PPL Electric)

In order to enhance liquidity, and as credit support to its commercial paper program, PPL Electric maintained a \$400 million 364-day credit facility which matured in June 2003. PPL Electric replaced its facility with a \$200 million, 364-day facility maturing in June 2004 and a \$100 million three-year credit facility maturing in June 2006. PPL Energy Supply maintains three credit facilities: a \$300 million three-year credit facility maturing in June 2006, (this credit facility replaced a \$300 million 364-day credit facility which matured in June 2003), a \$500 million three-year credit facility maturing in June 2004 and a \$300 million three-year credit facility maturing in June 2005. Both PPL Electric and PPL Energy Supply have the ability to cause the lenders to issue letters of credit under their respective facilities. At December 31, 2003, no cash borrowings were outstanding under any credit facilities of PPL Electric or PPL Energy Supply. At December 31, 2003, PPL Electric had \$42 million of letters of credit outstanding under its \$100 million three-year facility, and PPL Energy Supply had \$87 million of letters of credit outstanding under its \$500 million three-year facility.

(PPL and PPL Energy Supply)

In October 2003, WPD (South West) replaced its expiring credit facility with a new £100 million 364-day credit facility maturing in October 2004 and extended its £150 million five-year credit facility to October 2008. At December 31, 2003, WPD (South West) had £27 million (\$48 million based on current exchange rates) of outstanding borrowings under its 364-day credit facility and no outstanding borrowings under its five-year credit facility. At December 31, 2003, WPD (South West) had uncommitted credit line borrowings of £25 million (\$44 million based on

current exchange rates) in separate agreements with lender banks.

WPD (South West) maintained a £250 million bridge facility, which expired in April 2003, for short-term liquidity. This bridge facility was paid down with the proceeds from the issuance of long-term bonds and borrowings under another credit facility. The long-term bond issuance is discussed in more detail under "Financing Activities."

(PPL Montana)

PPL Montana has a \$100 million three-year credit facility with another PPL Energy Supply subsidiary on market terms to meet its liquidity needs. At December 31, 2003, PPL Montana had no outstanding borrowings under that credit facility.

(PPL, PPL Energy Supply, PPL Electric and PPL Montana)

The subsidiaries of PPL are separate legal entities. PPL's subsidiaries are not liable for the debts of PPL. Accordingly, creditors of PPL may not satisfy their debts from the assets of the subsidiaries absent a specific contractual undertaking by a subsidiary to pay PPL's creditors or as required by applicable law or regulation. Similarly, absent a specific contractual undertaking or as required by applicable law or regulation, PPL is not liable for the debts of its subsidiaries. Accordingly, creditors of PPL's subsidiaries may not satisfy their debts from the assets of PPL absent a specific contractual undertaking by PPL to pay the creditors of its subsidiaries or as required by applicable law or regulation.

Similarly, the subsidiaries of PPL Energy Supply, PPL Electric and PPL Montana are separate legal entities. These subsidiaries are not liable for the debts of PPL Energy Supply, PPL Electric and PPL Montana. Accordingly, creditors of PPL Energy Supply, PPL Electric and PPL Montana may not satisfy their debts from the assets of their subsidiaries absent a specific contractual undertaking by a subsidiary to pay the creditors or as required by applicable law or regulation. In addition, absent a specific contractual undertaking or as required by applicable law or regulation, PPL Energy Supply, PPL Electric and PPL Montana are not liable for the debts of their subsidiaries. Accordingly, creditors of these subsidiaries may not satisfy their debts from the assets of PPL Energy Supply, PPL Electric or PPL Montana absent a specific contractual undertaking by that parent to pay the creditors of its subsidiaries or as required by applicable law or regulation.

### Financing Activities

(PPL)

PPL Capital Funding retired the following medium-term notes, at par, during 2003:

- all of its \$60 million 6.375% Series due March 2003;
- all of its \$20 million 6.23% Series due October 2003; and
- all of its \$5 million 6.40% Series due October 2003.

In November 2003, PPL launched an offer to exchange up to \$573 million aggregate stated amount of its outstanding PEPS Units for up to \$573 million aggregate stated amount of its PEPS Units, Series B and a cash payment by PPL of \$0.375 for each validly tendered and accepted outstanding PEPS Unit. The exchange offer, which closed in January 2004, resulted in 3,975,160 PEPS Units, or 17.28% of the 23 million outstanding PEPS Units, being exchanged. PPL conducted the exchange offer to reduce its future interest expense.

During the twelve months ended December 31, 2003, PPL issued \$426 million of common stock, including \$109 million through its Structured Equity Shelf Program and \$270 million through a public offering in May 2003. In this public offering, PPL issued 7.1 million shares of common stock for \$38.25 per share. PPL received net proceeds of approximately \$261 million, which were used to repurchase commercial paper of PPL Energy Supply and for general corporate purposes.

*(PPL and PPL Energy Supply)*

In March 2003, WPD (South West) issued £200 million of 5.875% bonds due 2027. The proceeds from this issuance were used to repay £200 million of borrowings under its bridge facility. Additionally, in May 2003, WPD (South West) issued an additional £50 million of 5.875% bonds due 2027. WPD (South West) used the proceeds from this issuance to pay down short-term borrowings. The issuance of this long-term debt resulted in an \$11 million write-off of unamortized swap restructuring costs in the second quarter of 2003.

In May 2003, PPL Energy Supply issued \$400 million of 2.625% Convertible Senior Notes due 2023, which are guaranteed by PPL and convertible into PPL common stock. The convertible notes were sold in a Rule 144A private offering to qualified institutional buyers, and PPL Energy Supply and PPL subsequently registered the resale of the notes with the SEC for the benefit of the holders. See Note 4 for additional information on the convertibility features of the notes. PPL Energy Supply used the proceeds from the private offering of the convertible notes to repurchase commercial paper and for general corporate purposes.

During the twelve months ended December 31, 2003, WPD retired \$53 million of 7.375% Unsecured Bonds due 2028.

At December 31, 2003, PPL Energy Supply had no commercial paper outstanding.

During the twelve months ended December 31, 2003, PPL Energy Supply distributed approximately \$1.2 billion to its parent company, PPL Energy Funding, and received capital contributions of \$261 million.

*(PPL and PPL Electric)*

In February 2003, the Lehigh County Industrial Development Authority (LCIDA) issued \$90 million of 3.125% Pollution Control Revenue Refunding Bonds due November 2008 on

behalf of PPL Electric. The proceeds of the bonds were used to refund the LCIDA's \$90 million, 6.40% Pollution Control Revenue Refunding Bonds due 2021. In order to secure its obligations to repay the LCIDA, PPL Electric issued \$90 million aggregate principal amount of its Senior Secured under its 2001 Senior Secured Bond Indenture, having terms corresponding to the terms of the LCIDA bonds.

In February 2003, PPL Electric retired \$19 million of its outstanding First Mortgage Bonds, 6-7/8% Series due February 2003, at par value.

In April 2003 and December 2003, as permitted by the 1945 First Mortgage Bond Indenture, PPL Electric retired approximately \$46 million aggregate principal amount of its First Mortgage Bonds, 7-7/8% Series due 2023, and \$19 million aggregate principal amount of its First Mortgage Bonds, 6.75% Series due 2023. Both issues were retired at par value, plus accrued interest, through the application of cash deposited with the trustee to release certain transmission lines and other equipment from the lien of the 1945 First Mortgage Bond Indenture.

In May 2003, PPL Electric issued \$100 million of 4.30% Senior Secured Bonds due 2013. The proceeds were used for general corporate purposes including the refunding of higher-cost securities.

PPL Electric redeemed all outstanding shares of the following preferred stock, at par value of \$100 per share plus accumulated and unpaid dividends, in accordance with the mandatory sinking fund requirements or through the optional redemption provisions of each series:

- in April 2003, \$10 million of 6.15% Series Preferred Stock;
- in July 2003, \$4 million of 6.33% Series Preferred Stock; and
- in October 2003, \$17 million of 6.125% Series Preferred Stock.

In January 2004, PPL Electric notified holders of its intent to redeem on March 1, 2004 approximately \$6 million aggregate principal amount of its 7.30% First Mortgage Bonds. This issue will be retired at par value, plus any accrued and unpaid interest through the application of cash deposited with the trustee to release certain transmission lines and other equipment from the lien of the 1945 First Mortgage Bond Indenture.

During the twelve months ended December 31, 2003, PPL Transition Bond Company made principal payments on transition bonds totaling \$255 million.

During the twelve months ended December 31, 2003, PPL Electric received a capital contribution of \$75 million from PPL

At December 31, 2003, PPL Electric had no commercial paper outstanding.

*(PPL Montana)*

During the twelve months ended December 31, 2003, PPL Montana repaid \$26 million under its revolving line of credit with an affiliate. Also during this period, PPL Montana distributed \$5 million to its parent company, PPL Montana Holdings, LLC.

## **Dividends and Dividend Restrictions**

*(PPL)*

In February 2003, PPL announced an increase of its quarterly common stock dividend, effective April 1, 2003, from 36 cents per share to 38.5 cents per share (equivalent to \$1.54 per annum). Future dividends, declared at the discretion of the Board of Directors, will be dependent upon future earnings, cash flows, financial requirements and other factors.

*(PPL, PPL Energy Supply and PPL Montana)*

The PPL Montana Colstrip lease places certain restrictions on PPL Montana's ability to declare dividends. At this time, PPL believes that these covenants will not limit PPL Montana's ability to operate as desired and will not affect PPL's ability to meet any of its cash obligations. Certain of PPL Global's international subsidiaries also have financing arrangements which limit their ability to pay dividends. However, PPL does not, at this time, expect that any of such limitations would significantly impact its ability to meet its cash obligations.

*(PPL and PPL Electric)*

PPL Electric's 2001 Senior Secured Bond Indenture restricts dividend payments in the event that PPL Electric fails to meet interest coverage ratios or fails to comply with certain separateness formalities undertaken in connection with its strategic initiative (see Note 19 for additional information). PPL Electric does not, at this time, expect that any of such limitations would significantly impact its ability to declare dividends.

## **9. Acquisitions, Development and Divestitures**

### **Domestic Generation Projects** *(PPL and PPL Energy Supply)*

In 2001, PPL Global made a decision to cancel approximately 2,100 MW of previously planned generation development in Pennsylvania and Washington state. These projects were in the early stage of development and would have had an estimated capital cost of approximately \$1.3 billion. The charge for cancellation of these generation projects, which was primarily due to cancellation fees under turbine purchase contracts, was approximately \$150 million, or \$88 million after-tax, and was reported on the Statement of Income as "Cancellation of generation projects," a component of "Other charges." At June 30, 2002, PPL Global had completed payment of the cancellation fees.

In November 2002, PPL Global evaluated its options with respect to six unassigned turbines and SCRs that were complete or substantially complete. These units were intended to be used at the Kings Park site on Long Island, New York. At that time, given low energy prices and the unavailability of a power contract, PPL Global was reevaluating its options with respect to the Kings Park project.

Due to the uncertainty of the project and the absence of other viable projects, a valuation based upon replacement costs of the turbines and the SCRs was completed. This resulted in the recognition of a \$44 million impairment charge, which is reported on the Statement of Income as "Write-down of generation assets," a component of "Other charges." A deferred income tax benefit of \$18 million was recognized on the write-down.

In January 2003, PPL announced that it had decided not to proceed with development of the 300 MW Kings Park project. In March, PPL Global sold its interest in Kings Park Energy, LLC. At that time, the six unassigned gas combustion turbine generators and SCRs to be used at the Kings Park site were retained as spare parts.

In April 2003, PPL Susquehanna completed the replacement of the Unit 2 steam turbine at the Susquehanna station. This project provides a nominal power increase of 50 MW of generation capacity, of which PPL Susquehanna has a 90% undivided interest. An additional turbine upgrade is in progress for Unit 1 and is expected to be completed in 2004. Through December 31, 2003, a total of approximately \$125 million had been incurred on these projects.

In October 2003, PPL Maine entered into an agreement in principle with a coalition of government agencies and private groups to sell three of its nine hydroelectric dams in Maine. If the agreement is finalized, a non-profit organization designated by the coalition would have a five-year option to purchase the dams for approximately \$25 million, and PPL Maine would receive rights to increase energy output at its other hydroelectric dams in Maine. The coalition has indicated that it plans to remove or bypass the dams subject to the agreement in order to restore runs of Atlantic salmon and other migratory fish to the Penobscot River. Any final agreement will require several approvals by the FERC.

In November 2003, PPL Generation sold four of the six spare gas combustion turbine generators and related equipment for approximately \$33 million. PPL Generation received substantially all of the proceeds in January 2004. The pre-tax loss on the sale of about \$3 million is included in "Other Income - net" on the Statement of Income.

See Note 22 for a discussion of the Lower Mt. Bethel facility.

## International Energy Projects (PPL and PPL Energy Supply)

### Acquisitions

#### WPD

On September 6, 2002, PPL Global acquired the remaining 49% equity interest in WPDH Limited and WPDL from Mirant for approximately \$236 million, including acquisition costs. The acquisition of Mirant's 49% interest provides PPL Global with complete ownership of WPD.

Prior to the acquisition, PPL Global held 51% of the equity interest in WPD but shared control with Mirant pursuant to a shareholders' agreement. The shareholders' agreement was terminated in connection with the closing of the acquisition. No regulatory approvals were required for this transaction.

The purchase of Mirant's interest in WPD was accounted for as a step-acquisition and resulted in the consolidation of WPD's accounts by PPL and PPL Energy Supply.

The assets acquired and liabilities assumed were recorded at estimated fair value as determined by management based on information available at the time of acquisition. As of October 1, 2003, management completed its review and determination of the fair values assigned to assets acquired and liabilities assumed. The fair value of PP&E, based on an independent appraisal, was approximately \$800 million lower than the preliminary valuation. Accordingly, PP&E was reduced, with offsetting increases in goodwill and reductions in deferred income taxes.

The following table summarizes the final allocation of purchase price based on fair values of the assets acquired and liabilities assumed at the date of acquisition, plus the book value of assets and liabilities underlying PPL Global's previous 51% equity ownership:

Current assets	\$	236
Investments (a)		(450)
PP&E		2,629
Goodwill		740
Other intangibles		4
Other		244
Total assets acquired		<u>3,403</u>
Current liabilities		767
Long-term debt		1,668
Other		732
Total liabilities assumed		<u>3,167</u>
Net assets acquired	\$	<u>236</u>

(a) Includes the reversal of PPL Global's equity investment.

The goodwill reflected above includes the remaining value of PPL Global's 51% share of the goodwill recognized by WPD on

its acquisition of Hyder, in addition to the \$568 million of non-deductible goodwill arising upon acquisition of Mirant's 49% interest.

The PPL income statements for 2003 and 2002 include consolidated WPD results for the twelve-month periods ended November 30, 2003 and 2002. This reflects PPL Global's policy of recording the results of foreign controlled subsidiaries on a one-month lag. The portion of earnings attributable to Mirant, \$73 million for the year ended December 31, 2002, is reported on the Statement of Income in "Minority Interest."

#### TransEmel

Emel acquired the remaining 40% interest in a provider of transmission service to northern Chile in July 2003 at a net cost of \$3 million, bringing its total ownership interest in TransEmel to 100%. As a result of this acquisition, the operating results of TransEmel have been consolidated from the beginning of the year. The portion of earnings attributable to the minority shareholder is reported on the Statement of Income in "Minority Interest."

### Write-down of International Energy Projects

#### CEMAR

In 2001, PPL Global estimated that the long-term viability of its CEMAR investment was jeopardized and that there was minimal probability of positive future cash flows. At that time, PPL Global recorded an impairment loss of \$217 million in the carrying value of its net assets in CEMAR, including a \$179 million charge to "Write-down of international energy projects," a component of "Other charges" on the Statement of Income. In March 2002, PPL Global recorded a further impairment loss of \$6 million, which was also charged to "Write-down of international energy projects." In June 2002, PPL made a decision to exit the investment. At that time, PPL Global's remaining portion of its CEMAR investment, which related to foreign currency translation adjustments (CTA), was written-off. The \$94 million charge was recorded in "Write-down of international energy projects." Accounting guidance prohibits the inclusion of CTA in impairment calculations prior to designating such assets as held for disposal.

On August 21, 2002, ANEEL authorized an administrative intervention in CEMAR and fully assumed operational and financial control of the company. In its public announcement relating to the intervention, ANEEL said that its intervention and control of CEMAR would last for an initial term of 180 days and that it could be extended.

The intervenor appointed by ANEEL issued a public statement and schedule for the transfer of the ownership interest in CEMAR to a new owner. Although the schedule announced by the intervenor reflected a closing for the transfer of control of CEMAR to a third party on December 20, 2002, the closing did not occur. The deadline for the sale process was extended to February 17, 2003, the same day the initial term of the

intervention was scheduled to end. No conforming bids were submitted to ANEEL by the February 17 deadline due to three outstanding injunctions preventing the sale process from continuing. ANEEL publicly announced a 180-day extension of initial intervention on February 14, citing the continuing unresolved financial crisis of CEMAR as the primary reason for the extension. As of February 11, 2003, due to the inability to discharge their obligations under the continuing intervention, PPL-related officers and directors of CEMAR resigned from their respective positions.

In April 2003, PPL learned that the Brazilian Federal Appellate Court hearing the appeal of one of the above-mentioned injunctions accepted ANEEL's arguments and cancelled the injunction. In June, ANEEL's officials indicated to PPL that the other two injunctions outstanding against the sale process had been lifted as well. The intervenor appointed by ANEEL issued a public statement and revised schedule for the transfer of the ownership interest in CEMAR to a new owner. In July, ANEEL pre-qualified a Brazilian private equity fund, GP Investimentos (GP), as the sole qualified bidder. However, on August 12, ANEEL announced that it could not proceed with GP's offer because, among other reasons, it was unacceptable to CEMAR's creditors. On August 16, ANEEL extended the intervention for up to an additional 180 days. On September 4, ANEEL published a revised schedule for the sale of CEMAR to a third party by the end of 2003. On December 16, 2003, a federal judge enjoined the sale process to allow another party (MT Baker) 30 days to submit a bid for CEMAR. However, GP was the only party that submitted a bid by the revised deadline. On February 3, 2004, ANEEL announced that it had accepted the bid of GP. Before assuming control of CEMAR, GP must complete negotiations with CEMAR's creditors and other third parties. ANEEL has extended the closing date for the sale of CEMAR to GP to March 30, 2004. At this time, PPL Global cannot predict when or if GP will complete these negotiations and assume control of CEMAR.

PPL Global no longer controls or manages CEMAR, and PPL Global has deconsolidated the financial assets and liabilities of CEMAR from its financial statements. Consistent with the cost method of accounting, PPL Global is no longer recording CEMAR's operating results.

At December 31, 2003, the negative investment in CEMAR of \$18 million was included in "Deferred Credits and Other Noncurrent Liabilities - Other." Any negative carrying value will be reversed upon the final sale or other disposition of the company.

#### *WPD/Teesside*

WPD has an equity interest in Teesside Power Limited (Teesside), the owner of the 1,875 MW Teesside Power Station, located in northeast England. Through its European affiliates, Enron was an owner, operator and power purchaser of the station's output. As a result of Enron being placed into receivership in the U.K. and its default on obligations under the power purchase agreements, in 2001, WPD wrote off its entire

equity investment in Teesside. PPL Global's share of the impairment loss was \$21 million and is included in "Write-down of international energy projects" on the Statement of Income.

In connection with the Enron bankruptcy and the probable resulting loss of Teesside cash flows, PPL and its subsidiaries evaluated the carrying value of WPD. Fair value, measured using discounted cash flows, was compared to the carrying value to determine whether impairment existed at December 31, 2001. Fair value was determined considering the loss of the value of the future cash flows from the Teesside Power Station and a forecasted reduction in future operating cash flows at WPD. The probability-weighted impairment loss was \$117 million, after-tax. The pre-tax charge was \$134 million, and was recorded as a charge to "Write-down of international energy projects."

In 2002, PPL Global recognized an \$8 million tax benefit on the worthlessness of WPD's investment in Teesside.

#### *Other*

In 2002, PPL Global evaluated certain investments for impairment and recorded a \$5 million impairment charge in connection with its investment in CGE, a \$4 million impairment of a corporate joint venture's investment in Brazil, and a \$4 million write-down of certain non-electrical assets in Bolivia.

#### Discontinued Operations

In December 2003, PPL Global's Board of Managers authorized PPL Global to sell its investment in a Latin American telecommunications company, and approved a plan of sale. It was determined that the viability of this non-strategic business was uneconomical. PPL Global believes a sale is probable within one year.

As a result, PPL Global recorded a write-down in the carrying value of the company's net assets to their estimated fair value of approximately \$1 million. This write-down, totaling approximately \$18 million, as well as operating results of the Latin American telecommunications company, which was a loss of approximately \$2 million for 2003, are reflected as "Loss from Discontinued Operations" on the Statement of Income. The results of operations have been classified as discontinued operations for all periods presented. The assets and liabilities of the discontinued operation totaled \$5 million and \$4 million at December 31, 2003, and are included in "Current Assets - Other" and "Current Liabilities - Other" on the Balance Sheet. Balance Sheet amounts have not been reclassified at December 31, 2002.

#### Sales of Property

In the second quarter of 2003, a subsidiary of WPD sold certain Hyder properties. PPL Global received approximately \$17 million from the sales, and recorded a pre-tax gain of about \$2

million. This gain is included in "Other Income - net" on the Statement of Income.

**Other (PPL)**

In April 2003, a subsidiary of PPL Telecom acquired the fiber optic network of a Fairfax, Virginia-based company for approximately \$21 million, consisting of \$9 million in cash and a \$12 million capital lease obligation for the right to use portions of a fiber optic network. The 1,330-route-mile metropolitan area fiber network connects New York, northern New Jersey, Philadelphia, Baltimore and Washington, D.C. The acquisition required certain regulatory approvals and authorizations in the area served by the network.

**10. Leases**

**Colstrip Generating Plant (PPL, PPL Energy Supply and PPL Montana)**

PPL Montana leases a 50% interest in Colstrip Units 1 and 2 and a 30% interest in Unit 3, under four 36-year non-cancelable operating leases. These leases provide two renewal options based on the economic useful life of the generation assets. PPL Montana is required to pay all expenses associated with the operations of the generation units. The leases place certain restrictions on PPL Montana's ability to incur additional debt, sell assets and declare dividends and require PPL Montana to maintain certain financial ratios related to cash flow and net worth. The amount outstanding under these leases at December 31, 2003 was \$295 million. There are no residual value guarantees in these leases. However, upon an event of default or an event of loss, the lessee could be required to pay a termination value of amounts sufficient to allow the lessor to repay amounts owing on the lessor notes and make the lessor whole for its equity investment and anticipated return on investment. The events of default include payment defaults, breaches of representations or covenants, acceleration of other indebtedness of PPL Montana, change in control of PPL Montana and certain bankruptcy events. The termination value is estimated to be \$583 million at December 31, 2003.

**Other Leases**

*(PPL, PPL Energy Supply, PPL Electric and PPL Montana)*

In addition to the leasing arrangements discussed above, PPL and its subsidiaries also have leases for vehicles, office space, land, buildings, personal computers and other equipment. Rental expense for all operating leases was as follows:

	<u>PPL</u>	<u>PPL Energy Supply</u>	<u>PPL Electric</u>	<u>PPL Montana</u>
2003	\$ 85	\$ 63	\$ 21	\$ 21
2002	62	46	15	21
2001	52	36	15	21

Total future minimum rental payments for all operating leases are estimated as follows:

	<u>PPL</u>	<u>PPL Energy Supply</u>	<u>PPL Electric</u>	<u>PPL Montana</u>
2004	\$ 79	\$ 65	\$ 13	\$
2005	68	57	11	
2006	63	54	8	
2007	56	50	6	
2008	56	51	4	
Thereafter	505	498	8	
	\$ 827	\$ 775	\$ 50	\$

*(PPL)*

In connection with the acquisition of the fiber optic network discussed in Note 9, a subsidiary of PPL Telecom assumed a \$1 million capital lease obligation through 2020 for the right to use portions of the fiber optic network. Total future minimum rental payments for this capital lease are estimated at \$1 million for each of the years from 2004 through 2008, and \$15 million thereafter.

*(PPL and PPL Energy Supply)*

See Note 22 for discussion of synthetic leases.

**11. Stock-Based Compensation**

*(PPL, PPL Energy Supply, PPL Electric and PPL Montana)*

Under the PPL Incentive Compensation Plan (ICP) and the Incentive Compensation Plan for Key Employees (ICPKE) (together, the "Plans"), restricted shares of PPL common stock, restricted stock units and stock options may be granted to officers and other key employees of PPL, PPL Electric and other affiliated companies. Awards under the Plans are made by the Compensation and Corporate Governance Committee (CCGC) of the PPL Board of Directors, in the case of the ICP, and by the PPL Corporate Leadership Council (CLC), in the case of the ICPKE. The ICP limits the total number of awards that may be granted under it after April 23, 1999 to 7,884,715 awards, or 5% of the total shares of common stock that were outstanding at April 23, 1999. The ICPKE limits the total number of awards that may be granted under it after April 25, 2003, to 8,286,804 awards, or 5% of the total shares of common stock that were outstanding at January 1, 2003, reduced by outstanding awards for which common stock was not yet issued as of April 25, 2003. In addition, each Plan limits the number of shares available for awards in any calendar year to 2% of the outstanding common stock of PPL on the first day of such calendar year. The maximum number of options that can be awarded under each Plan to any single eligible employee in any calendar year is 1.5 million shares. Any portion of these options that has not been granted may be carried over and used in any subsequent year. If any award lapses, is forfeited or the rights of the participant terminate, the shares of common stock underlying such an award are again available for grant. Shares delivered under the Plans may be in the form of authorized and unissued common stock, common stock held in treasury by PPL

or common stock purchased on the open market (including private purchases) in accordance with applicable securities laws.

## Restricted Stock

Restricted shares of PPL common stock are outstanding shares with full voting and dividend rights. Restricted stock awards are subject to a restriction or vesting period as determined by the CCGC in the case of the ICP, and the CLC in the case of the ICPKE. In addition, the shares are subject to forfeiture or accelerated payout under Plan provisions for termination, retirement, disability and death of employees. Restricted shares vest fully if control of PPL changes, as defined by the plans.

## Restricted Stock Units

In 2003, the Plans were amended to allow for the grant of restricted stock units. Restricted stock units are awards based on the fair market value of PPL common stock. Actual PPL common shares will be issued upon completion of a restriction or vesting period as determined by the CCGC in the case of the ICP, and the CLC in the case of the ICPKE. Recipients of restricted stock units may also be granted the right to receive dividend equivalents through the end of the restriction period or until the award is forfeited. Restricted stock units are subject to forfeiture or accelerated payout under the Plan provisions for termination, retirement, disability and death of employees. Restricted stock units vest fully if control of PPL changes, as defined by the Plans.

A summary of restricted stock/unit grants follows:

Restricted Stock/ Units Granted	Restricted Shares Granted	Weighted Average Fair Value	Restricted Units Granted	Weighted Average Fair Value
<b>2003</b>				
PPL	42,090	\$36.23	139,732	\$35.09
PPL Energy Supply	10,110	\$36.23	77,306	\$35.11
PPL Electric	2,850	\$36.23	21,170	\$35.07
PPL Montana			3,970	\$35.07
<b>2002</b>				
PPL	147,735	\$34.12		
PPL Energy Supply	82,211	\$34.45		
PPL Electric	18,860	\$33.71		
PPL Montana	2,830	\$33.74		
<b>2001</b>				
PPL	202,590	\$43.09		
PPL Energy Supply	141,289	\$42.68		
PPL Electric	19,410	\$44.79		
PPL Montana	1,630	\$45.09		

Compensation expense related to restricted stock and restricted stock unit awards was \$5 million, \$5 million and \$6 million for PPL for 2003, 2002 and 2001. At December 31, 2003, there were 491,014 restricted shares and 135,078 restricted units outstanding. These awards currently vest from three to 25 years from the date of grant.

Compensation expense related to restricted stock/unit awards for PPL Energy Supply in 2003, 2002 and 2001 was \$4 million, \$4 million and \$5 million. Compensation expense related to restricted stock/unit awards for PPL Electric was \$1 million for 2003, 2002 and 2001. Such compensation expense for PPL Montana was insignificant for all periods reported.

## Stock Options

*(PPL, PPL Energy Supply, PPL Electric and PPL Montana)*

Under the Plans, stock options may also be granted with an option exercise price per share not less than the fair market value of PPL's common stock on the date of grant. The options are exercisable beginning one year after the date of grant, assuming the individual is still employed by PPL or a subsidiary, in installments as determined by the CCGC in the case of the ICP, and the CLC in the case of the ICPKE. Options outstanding at December 31, 2003 vest over a three-year period from the date of grant in equal installments. The CCGC and CLC have discretion to accelerate the exercisability of the options. All options expire no later than ten years from the grant date. The options become exercisable immediately if control of PPL changes, as defined by the Plans.

A summary of stock option activity follows:

	2003		2002		2001	
	Number of Options	Weighted Average Exercise Price	Number of Options	Weighted Average Exercise Price	Number of Options	Weighted Average Exercise Price
<b>PPL</b>						
Outstanding at beginning of year	3,008,685	\$32.09	2,255,051	\$31.36	1,969,301	\$23.64
Granted	816,110	36.23	840,430	33.49	922,860	43.16
Exercised	(860,915)	24.09	(62,710)	22.82	(548,424)	23.49
Forfeited	(51,622)	35.32	(24,086)	36.18	(88,686)	31.31
Outstanding at end of year	2,912,258	35.56	3,008,685	32.09	2,255,051	31.36
Options exercisable at end of year	1,354,075		1,400,701		306,544	
Weighted-average fair value of options granted	\$11.92		\$11.68		\$10.42	
<b>PPL Energy Supply</b>						
Outstanding at beginning of year	903,549	32.78	675,179	31.64	655,755	23.27
Granted	266,760	36.23	304,480	33.49	306,130	43.16
Exercised	(253,805)	24.41	(61,160)	22.72	(167,446)	23.92
Forfeited	(51,622)	35.32	(14,950)	37.07	(53,100)	29.91
Transferred					(66,160)	22.88
Outstanding at end of year	864,882	36.14	903,549	32.78	675,179	31.64
Options exercisable at end of year	366,209		381,657		88,436	
Weighted-average fair value of options granted	\$11.92		\$11.68		\$10.42	
<b>PPL Electric</b>						
Outstanding at beginning of year	232,376	34.40	163,942	34.92	105,400	24.53
Granted	66,630	36.23	77,570	33.49	92,450	43.16
Transferred	3,114	26.84				
Exercised	(75,927)	26.68			(33,908)	25.04
Forfeited			(9,136)	36.20		
Outstanding at end of year	226,193	37.42	232,376	34.40	163,942	34.92
Options exercisable at end of year	87,488		95,561		16,924	
Weighted-average fair value of options granted	\$11.92		\$11.68		\$10.42	
<b>PPL Montana</b>						
Outstanding at beginning of year	25,110	30.41	21,720	26.18	100,420	21.79
Granted	21,000	36.23	9,390	33.49	5,860	43.16
Exercised			(6,000)	19.91		
Forfeited					(16,390)	19.91
Transferred					(68,170)	22.68
Outstanding at end of year	46,110	33.06	25,110	30.41	21,720	26.18
Options exercisable at end of year	16,898		6,527		6,287	
Weighted-average fair value of options granted	\$11.92		\$11.68		\$10.42	

The following table summarizes information about stock options at December 31, 2003:

	Options Outstanding			Options Exercisable	
	Range of Exercise Prices	Number Outstanding at 12/31/03	Weighted-Avg. Remaining Contractual Life	Number Exercisable at 12/31/03	Weighted-Avg. Exercise Price
	\$19.00-\$24.00	206,415	6.1	206,415	\$22.26
	\$25.00-\$29.00	327,712	5.3	327,712	26.84
	\$30.00-\$35.00	705,403	8.1	193,547	33.49
	\$36.00-\$39.00	816,110	9.1		36.23
	\$40.00-\$45.00	856,618	7.1	626,401	43.16

The estimated fair value of each option granted was calculated using a Black-Scholes option-pricing model. The weighted average assumptions used in the model were as follows:

	2003	2002	2001
Risk-free interest rate	3.81%	5.35%	5.46%
Expected option life	7.75 yrs.	10 yrs.	10 yrs.
Expected stock volatility	39.94%	39.11%	30.24%
Dividend yield	3.48%	3.34%	4.28%

Total options outstanding had a weighted-average remaining life of 7.6 years at December 31, 2003.

There were 77,428 stock units outstanding at December 31, 2003. Compensation expense for all periods reported was insignificant.

### PPL Energy Supply

Range of Exercise Prices	Options Outstanding		Options Exercisable		
	Number Outstanding at 12/31/03	Weighted-Avg. Remaining Contractual Life	Weighted-Avg. Exercise Prices	Number Exercisable at 12/31/03	Weighted-Avg. Exercise Price
\$19.00-\$24.00	45,056	6.1	\$20.87	45,056	\$20.87
\$25.00-\$29.00	57,200	6.3	26.84	57,200	26.84
\$30.00-\$35.00	235,882	8.1	33.49	74,741	33.49
\$36.00-\$39.00	266,760	9.1	36.23		
\$40.00-\$45.00	259,984	7.1	43.16	189,212	43.16

Total options outstanding had a weighted-average remaining life of 7.1 years at December 31, 2003.

### Stock Appreciation Rights

*(PPL and PPL Energy Supply)*

WPD uses stock appreciation rights to compensate senior management employees. Stock appreciation rights are granted with a reference price to PPL's common stock at the date of grant. These awards vest over a three-year period and have a 10-year term, during which time employees are entitled to receive a cash payment of any appreciation in the price of PPL's common stock over the grant date value. At December 31, 2003, there were 70,815 stock appreciation rights outstanding. Compensation expense for all periods reported was insignificant.

### PPL Electric

Range of Exercise Prices	Options Outstanding		Options Exercisable		
	Number Outstanding at 12/31/03	Weighted-Avg. Remaining Contractual Life	Weighted-Avg. Exercise Prices	Number Exercisable at 12/31/03	Weighted-Avg. Exercise Price
\$25.00-\$29.00	9,166	5.3	\$26.84	9,166	\$26.84
\$30.00-\$35.00	60,503	8.1	33.49	15,371	33.49
\$36.00-\$39.00	66,630	9.1	36.23		
\$40.00-\$45.00	89,894	7.1	43.16	62,951	43.16

Total options outstanding had a weighted-average remaining life of 7.9 years at December 31, 2003.

### Method of Accounting

*(PPL, PPL Energy Supply, PPL Electric and PPL Montana)*

Effective January 1, 2003, PPL and its subsidiaries adopted the fair value method of accounting for stock-based compensation, as prescribed by SFAS 123, "Accounting for Stock-Based Compensation," using the prospective method of transition permitted by SFAS 148, "Accounting for Stock-Based Compensation - Transition and Disclosure, an amendment of FASB Statement No. 123." Prior to 2003, PPL applied the intrinsic value method, permitted under SFAS 123 and defined in APB Opinion No. 25, "Accounting for Stock Issued to Employees" and related interpretations. See Note 1 for additional information related to the adoption of the fair value method.

### PPL Montana

Range of Exercise Prices	Options Outstanding		Options Exercisable		
	Number Outstanding at 12/31/03	Weighted-Avg. Remaining Contractual Life	Weighted-Avg. Exercise Prices	Number Exercisable at 12/31/03	Weighted-Avg. Exercise Price
\$19.00-\$24.00	9,860	6.2	\$19.91	9,860	\$19.91
\$30.00-\$35.00	9,390	8.1	33.49	3,131	33.49
\$36.00-\$39.00	21,000	9.1	36.23		
\$40.00-\$45.00	5,860	7.1	43.16	3,907	43.16

Total options outstanding had a weighted-average remaining life of 8.0 years at December 31, 2003.

### 12. Retirement and Postemployment Benefits

*(PPL, PPL Energy Supply, PPL Electric and PPL Montana)*

#### Pension and Other Postretirement Benefits

PPL and certain of its subsidiaries sponsor various pension and other postretirement and postemployment benefit plans. PPL follows the guidance of SFAS 87, "Employers' Accounting for Pensions," and SFAS 106, "Employers' Accounting for Postretirement Benefits Other Than Pensions," when accounting for these benefits.

PPL and certain of its subsidiaries also provide supplemental retirement benefits to directors, executives and other key management employees through unfunded nonqualified retirement plans.

The majority of employees of PPL's domestic subsidiaries will become eligible for certain health care and life insurance benefits upon retirement through contributory plans. Postretirement benefits under the PPL Retiree Health Plans (covering retirees of PPL Electric and various other affiliated

### Director Stock Units

*(PPL)*

Under the Directors Deferred Compensation Plan, stock units are used to compensate members of PPL's Board of Directors who are not employees of PPL. Such stock units represent shares of PPL's common stock to which board members are entitled after they cease serving as a member of the Board of Directors. Board members are also entitled to defer any or all of their cash compensation into stock units. The stock unit accounts of each board member are increased based on dividends paid or other distributions on PPL's common stock.

PPL companies) and the North Penn Gas Plans are paid from funded VEBA trusts sponsored by the respective companies.

At December 31, 2003, PPL Electric had a regulatory asset of \$5 million relating to postretirement benefits that is being amortized and recovered in rates, with a remaining life of nine years. PPL Electric also maintains an additional liability for the cost of health care of retired miners of former subsidiaries that had been engaged in coal mining. At December 31, 2003, the liability was \$28 million. The liability is the net of \$57 million of estimated future benefit payments offset by \$29 million of available assets in a PPL Electric-funded VEBA trust.

PPL Energy Supply subsidiaries engaged in the mechanical contracting business make contributions to various multi-employer pension and health and welfare plans, depending on an employee's status. Contributions of \$23 million, \$30 million

and \$21 million were made in 2003, 2002 and 2001. The change in contributions from year to year is primarily the result of the changes in the workforce at the mechanical contracting companies. The contribution rates have also increased from year to year.

In the third quarter of 2002, PPL Global acquired complete ownership of WPD. Included in the fully consolidated financial results of PPL Energy Supply for 2003 and 2002 is the impact of the various pension plans WPD sponsors in the U.K.

The following disclosures distinguish between PPL's domestic and international pension plans.

PPL uses a December 31 measurement date for its domestic pension and other postretirement benefit plans and its international pension plans.

Net pension and other postretirement benefit costs (credits) were as follows:

	Pension Benefits						Other Postretirement Benefits		
	2003		2002		2001		2003	2002	2001
	Domestic	International	Domestic	International	Domestic	International			
<b>PPL</b>									
Service cost	\$ 42	\$ 14	\$ 40	\$ 13	\$ 38	\$ 1	\$ 7	\$ 5	\$ 5
Interest cost	105	124	99	98	91	3	31	26	22
Expected return on plan assets	(143)	(188)	(147)	(179)	(140)	(3)	(13)	(12)	(11)
Net amortization and deferral	(6)	4	(31)	3	(50)		25	15	12
Net periodic pension and postretirement costs/(credits) prior to special termination benefits	(2)	(46)	(39)	(65)	(61)	1	50	34	2
Special termination benefits	9		62		3			4	
Net periodic pension and postretirement benefit cost/(credit)	\$ 7	\$ (46)	\$ 23	\$ (65)	\$ (58)	\$ 1	\$ 50	\$ 38	\$ 28
<b>PPL Energy Supply</b>									
Service cost	\$ .3	\$ 14	\$ 2	\$ 13	\$ 2	\$ 1			
Interest cost	4	124	4	98	4	3	\$ 1	\$ 1	\$ 1
Expected return on plan assets	(4)	(188)	(3)	(179)	(3)	(3)			
Net amortization and deferral	1	4		3					
Net periodic pension and postretirement benefit cost/(credit)	\$ 4	\$ (46)	\$ 3	\$ (65)	\$ 3	\$ 1	\$ 1	\$ 1	\$ 1
<b>PPL Montana</b>									
Service cost	\$ 2		\$ 2		\$ 2				
Interest cost	4		3		3		\$ 1	\$ 1	\$ 1
Expected return on plan assets	(3)		(2)		(2)				
Net amortization and deferral	1								
Net periodic pension and postretirement benefit cost	\$ 4		\$ 3		\$ 3		\$ 1	\$ 1	\$ 1

Net periodic pension cost charged (credited) to operating expense, excluding amounts charged to construction and other non-expense accounts, were:

	2003		2002		2001	
	Domestic	Int'l	Domestic	Int'l	Domestic	Int'l
PPL (a)	\$ (2)	\$ (40)	\$ (31)	\$ (58)	\$ (48)	\$ 1
PPL Energy Supply (b)	2	(40)	(9)	(58)	(16)	1
PPL Electric (c)	(4)		(17)		(24)	
PPL Montana	4		3		3	

- (a) The domestic amounts for 2003 and 2002 exclude the \$9 million and \$62 million cost of special termination benefits, which are included separately in the Statement of Income, within the "Workforce reduction" charge for those years.
- (b) In addition to the specific plans sponsored by PPL Energy Supply, PPL Generation subsidiaries and PPL EnergyPlus are also allocated a portion of the costs of pension plans sponsored by PPL Services, included in the PPL total cost above, based on their participation in those plans.
- (c) PPL Electric is also allocated a portion of the costs of pension plans sponsored by PPL Services, included in the PPL total cost above, based on participation in those plans.

In 2001, PPL changed its method of amortizing unrecognized gains or losses in the annual pension expense or income determined under SFAS 87, "Employers' Accounting for Pensions" for its primary domestic pension plan. Under the old method, the net unrecognized gains or losses in excess of 10% of the greater of the plan's projected benefit obligation or the market-related value of plan assets were amortized on a straight-line basis over the estimated average future service period of plan participants. Market-related value of assets is calculated by rolling forward the prior year market-related value with contributions, disbursements and expected return on investments. This expected value is then compared to the actual fair value of assets. One fifth of the difference between the actual value of assets and the expected value is added (or subtracted if negative) to the expected value to arrive at the new market-related value.

Under the new method, a second corridor is utilized for the net unrecognized gains or losses in excess of 30% of the plan's projected benefit obligation. The net unrecognized gains or losses outside the second corridor are now amortized on a straight-line basis over a period equal to one-half of the average future service period of the plan participants. The new method is preferable under SFAS 87 because it provides more current recognition of gains and losses, thereby lessening the accumulation of unrecognized gains and losses.

The pro forma effect of retroactive application of this change in accounting principle would have been:

	2001	
	Net Income	EPS
PPL	\$ (10)	\$ (.07)
PPL Energy Supply	(3)	N/A
PPL Electric	(5)	N/A

The international plans adopted the double corridor approach when PPL gained control of WPD. This had no effect on prior figures.

Other post retirement benefit costs charged to operating expense, excluding amounts charged to construction and other non-expense accounts, were:

	2003	2002	2001
PPL	\$ 43	\$ 27	\$ 21
PPL Energy Supply (a)	14	9	8
PPL Electric (b)	20	13	10
PPL Montana	1	1	

(a) In addition to the specific plans sponsored by PPL Energy Supply, PPL Generation subsidiaries and PPL EnergyPlus are also allocated a portion of the costs of other postretirement benefit plans sponsored by PPL Services, included in the PPL total cost above, based on their participation in those plans.

(b) PPL Electric is also allocated a portion of the costs of other postretirement benefit plans sponsored by PPL Services, included in the PPL total cost above, based on participation in those plans.

The following assumptions were used in the valuation of the benefit obligations at December 31 and determination of net periodic benefit cost for the years ended December 31:

PPL Pension Benefits	2003		2002		2001	
	Domestic	Int'l	Domestic	Int'l	Domestic	Int'l
Discount rate						
- obligations	6.25%	5.50%	6.75%	5.75%	7.25%	10.24%
- cost	6.75%	5.75%	7.25%	5.75%	7.50%	10.24%
Expected return on plan assets						
- obligations	9.0%	8.30%	9.0%	8.31%	9.2%	10.24%
- cost	9.0%	8.31%	9.2%	8.31%	9.2%	10.24%
Rate of compensation increase						
- obligations	4.0%	3.75%	4.0%	3.75%	4.25%	7.12%
- cost	4.0%	3.75%	4.25%	3.75%	4.75%	7.12%

Other Postretirement Benefits	2003	2002	2001
Discount rate			
- obligations	6.25%	6.75%	7.25%
- cost	6.75%	7.25%	7.50%
Expected return on plan assets			
- obligations	7.80%	7.80%	7.60%
- cost	7.80%	7.60%	7.60%
Rate of compensation increase			
- obligations	4.0%	4.0%	4.25%
- cost	4.0%	4.25%	4.75%

PPL Energy Supply Pension Benefits	2003		2002		2001	
	Domestic	Int'l	Domestic	Int'l	Domestic	Int'l
Discount rate						
- obligations	6.25%	5.50%	6.75%	5.75%	7.25%	10.24%
- cost	6.75%	5.75%	7.25%	5.75%	7.50%	10.24%
Expected return on plan assets						
- obligations	9.0%	8.30%	9.0%	8.31%	9.2%	10.24%
- cost	9.0%	8.31%	9.2%	8.31%	9.2%	10.24%
Rate of compensation increase						
- obligations	4.0%	3.75%	4.0%	3.75%	4.25%	7.12%
- cost	4.0%	3.75%	4.25%	3.75%	4.75%	7.12%

Other Postretirement Benefits	2003	2002	2001
Discount rate			
- obligations	6.25%	6.75%	7.25%
- cost	6.75%	7.25%	7.50%
Expected return on plan assets	N/A	N/A	N/A
Rate of compensation increase			
- obligations	4.0%	4.0%	4.25%
- cost	4.0%	4.25%	4.75%

PPL Montana Pension Benefits	2003	2002	2001
	Discount rate		
- obligations	6.25%	6.75%	7.25%
- cost	6.75%	7.25%	7.50%
Expected return on plan assets			
- obligations	9.0%	9.0%	9.2%
- cost	9.0%	9.2%	9.2%
Rate of compensation increase			
- obligations	4.0%	4.0%	4.25%
- cost	4.0%	4.25%	4.75%

<b>Other Postretirement Benefits</b>	<b>2003</b>	<b>2002</b>	<b>2001</b>
Discount rate			
- obligations	6.25%	6.75%	7.25%
- cost	6.75%	7.25%	7.50%
Expected return on plan assets	N/A	N/A	N/A
Rate of compensation increase			
- obligations	4.0%	4.0%	4.25%
- cost	4.0%	4.25%	4.75%

**PPL, PPL Energy Supply and PPL Montana**

**Assumed health care cost trend rates at December 31,**

	<b>2003</b>	<b>2002</b>	<b>2001</b>
Health care cost trend rate assumed for next year			
- obligations	11%	12%	7%
- cost	12%	7%	7.25%
Rate to which the cost trend rate is assumed to decline (the ultimate trend rate)			
- obligations	5%	5%	6%
- cost	5%	6%	6%
Year that the rate reaches the ultimate trend rate			
- obligations	2010	2010	2006
- cost	2010	2006	2006

A one-percentage point change in the assumed health care costs trend assumption would have the following effects in 2003:

	<b>One Percentage Point</b>	
	<b>Increase</b>	<b>Decrease</b>
<b>PPL</b>		
Effect on service cost and interest cost components	\$ 3	\$ (29)
Effect on postretirement benefit obligation	34	(29)
<b>PPL Energy Supply</b>		
Effect on service cost and interest cost components		
Effect on postretirement benefit obligation	1	(1)
<b>PPL Montana</b>		
Effect on service cost and interest cost components		
Effect on postretirement benefit obligation	1	(1)

The expected long-term rate of return for PPL's domestic pension plans considers the plans' historical experience, but is primarily based on the plans' mix of assets and expectations for long-term returns of those asset classes.

(PPL)

The expected long-term rate of return for PPL's other postretirement benefit plans is based on the VEBA trusts' mix of assets and expectations for long-term returns of those asset classes considering that a portion of those assets are taxable.

(PPL and PPL Energy Supply)

The expected rate of return for PPL's international pension plan considers that a portfolio largely invested in equities would be expected to achieve an average rate of return in excess of a portfolio largely invested in long-term bonds. The historical experience has been an excess return of 2% to 4% per annum on average over the return on long-term bonds.

(PPL)

The funded status of the PPL plans was as follows:

	<b>Pension Benefits</b>				<b>Other Postretirement Benefits</b>	
	<b>2003</b>		<b>2002</b>		<b>2003</b>	<b>2002</b>
	<b>Domestic</b>	<b>International</b>	<b>Domestic</b>	<b>International</b>		
<b>Change in Benefit Obligation</b>						
Benefit Obligation, January 1	\$ 1,558	\$ 2,126	\$ 1,279	\$ 37	\$ 423	\$ 330
Service cost	42	14	40	13	7	5
Interest cost	105	124	99	98	31	26
Participant contributions		5		4	1	1
Plan amendments	3		80	39	48	21
Actuarial (gain)/loss	127	101	76	(53)	30	59
Special termination benefits	9		62			4
Acquisition/divestitures				1,970		
Settlements/curtailments				(30)		
Actual expense paid	(1)		(1)			
Net benefits paid	(71)	(131)	(77)	(128)	(28)	(23)
Currency conversion		235		176		
Benefit Obligation, December 31	<u>1,772</u>	<u>2,474</u>	<u>1,558</u>	<u>2,126</u>	<u>512</u>	<u>423</u>

	Pension Benefits				Other Postretirement Benefits	
	2003		2002		2003	2002
	Domestic	International	Domestic	International		
<b>Change in Plan Assets</b>						
Plan assets at fair value, January 1	1,376	1,757	1,633	21	163	155
Actual return on plan assets	329	332	(182)	(335)	27	(11)
Employer contributions	20		3	1	56	41
Participant contributions		5		4	1	1
Acquisition/divestitures				2,050		
Settlements/curtailments				(21)		
Actual expense paid	(1)		(1)			
Net benefits paid	(71)	(131)	(77)	(128)	(28)	(23)
Currency conversion		201		165		
Plan assets at fair value, December 31	<u>1,653</u>	<u>2,164</u>	<u>1,376</u>	<u>1,757</u>	<u>219</u>	<u>163</u>
<b>Funded Status</b>						
Funded Status of Plan	(119)	(310)	(182)	(369)	(293)	(260)
Unrecognized actuarial (gain)/loss	(187)	477	(144)	497	134	123
Unrecognized prior service cost	167	33	178	34	76	39
Unrecognized transition assets	(27)		(31)		78	87
Currency conversion		57		26		
Net amount recognized at end of year	<u>\$ (166)</u>	<u>\$ 257</u>	<u>\$ (179)</u>	<u>\$ 188</u>	<u>\$ (5)</u>	<u>\$ (11)</u>
<b>Amounts recognized in the Balance Sheet consist of:</b>						
Prepaid benefit cost	\$ 4	\$ 257	\$ 1	\$ 219	\$ 4	
Accrued benefit liability	(170)		(180)	(31)	(9)	(11)
Additional minimum liability	(28)	(516)	(29)	(453)		
Intangible asset	9	37	5	37		
Accumulated other comprehensive income (pre-tax)	19	434	24	416		
Cumulative translation adjustment		45				
Net amount recognized at end of year	<u>\$ (166)</u>	<u>\$ 257</u>	<u>\$ (179)</u>	<u>\$ 188</u>	<u>\$ (5)</u>	<u>\$ (11)</u>
<b>Total accumulated benefit obligation for defined benefit pension plans</b>	<b>\$ 1,553</b>	<b>\$ 2,423</b>	<b>\$ 1,376</b>	<b>\$ 2,022</b>		

Information for pension plans with projected and accumulated benefit obligations in excess of plan assets follows:

	2003		2002	
	Domestic	Int'l	Domestic	Int'l
Projected benefit obligation pensions	\$ 1,765	\$ 2,474	\$ 1,551	\$ 2,126
Accumulated benefit obligation	\$ 1,546	\$ 2,423	\$ 1,369	\$ 2,022
Fair value of assets	\$ 1,646	\$ 2,164	\$ 1,369	\$ 1,757

Information for pension plans with accumulated benefit obligations in excess of plan assets follows:

	2003		2002	
	Domestic	Int'l	Domestic	Int'l
Projected benefit obligation pensions	\$ 142	\$ 2,474	\$ 122	\$ 2,126
Accumulated benefit obligation	\$ 130	\$ 2,423	\$ 110	\$ 2,022
Fair value of assets	\$ 76	\$ 2,164	\$ 46	\$ 1,757

Information for other postretirement benefit plans with accumulated postretirement benefit obligations in excess of plan assets follows:

	2003	2002
Accumulated postretirement benefit obligation	\$ 512	\$ 423
Fair value of assets	\$ 219	\$ 163

(PPL Energy Supply)

The funded status of the PPL Energy Supply plans was as follows:

	Pension Benefits				Other Postretirement Benefits	
	2003		2002		2003	2002
	Domestic	International	Domestic	International		
<b>Change in Benefit Obligation</b>						
Benefit Obligation, January 1	\$ 58	\$ 2,126	\$ 51	\$ 37	\$ 9	\$ 5
Service cost	3	14	2	13		
Interest cost	4	124	4	98	1	1
Participant contributions		5		4		
Plan amendments				39		
Actuarial (gain)/loss		101	2	(53)	1	3
Acquisitions/divestitures				1,970		
Settlements/curtailments				(30)		
Net benefits paid	(1)	(131)	(1)	(128)		
Net transfer out	(2)					
Currency conversion		235		176		
Benefit Obligation, December 31	<u>62</u>	<u>2,474</u>	<u>58</u>	<u>2,126</u>	<u>11</u>	<u>9</u>
<b>Change in Plan Assets</b>						
Plan assets at fair value, January 1	30	1,757	33	21		
Actual return on plan assets	9	332	(3)	(335)		
Employer contributions	15		1	1		
Participant contributions		5		4		
Acquisition/divestitures				2,050		
Settlements/curtailments				(21)		
Net benefits paid	(1)	(131)	(1)	(128)		
Currency conversion		201		165		
Plan assets at fair value, December 31	<u>53</u>	<u>2,164</u>	<u>30</u>	<u>1,757</u>		
<b>Funded Status</b>						
Funded Status of Plan	(9)	(310)	(28)	(369)	(11)	(9)
Unrecognized actuarial loss	9	477	14	497	4	3
Unrecognized prior service cost	4	33	4	34		
Currency conversion		57		26		
Net amount recognized at end of year	<u>\$ 4</u>	<u>\$ 257</u>	<u>\$ (10)</u>	<u>\$ 188</u>	<u>\$ (7)</u>	<u>\$ (6)</u>
<b>Amounts recognized in the Balance Sheet consist of:</b>						
Prepaid benefit cost	\$ 4	\$ 257	\$ 1	\$ 219		
Accrued benefit liability			(11)	(31)	(7)	(6)
Additional minimum liability	(11)	(516)	(13)	(453)		
Intangible asset	3	37	3	37		
Accumulated other comprehensive income (pre-tax)	8	434	10	416		
Cumulative translation adjustment		45				
Net amount recognized at end of year	<u>\$ 4</u>	<u>\$ 257</u>	<u>\$ (10)</u>	<u>\$ 188</u>	<u>\$ (7)</u>	<u>\$ (6)</u>
<b>Total accumulated benefit obligation for defined benefit pension plans</b>	<u>\$ 62</u>	<u>\$ 2,423</u>	<u>\$ 52</u>	<u>\$ 2,022</u>		

Information for pension plans with projected and accumulated benefit obligations in excess of plan assets follows:

	2003		2002	
	Domestic	Int'l	Domestic	Int'l
Projected benefit obligation pensions	\$ 55	\$ 2,474	\$ 51	\$ 2,126
Accumulated benefit obligation	\$ 55	\$ 2,423	\$ 46	\$ 2,022
Fair value of assets	\$ 46	\$ 2,164	\$ 23	\$ 1,757

Information for other postretirement benefit plans with accumulated postretirement benefit obligations in excess of plan assets follows:

	2003	2002
Accumulated postretirement benefit obligation	\$ 11	\$ 9
Fair value of assets	\$ 0	\$ 0

In addition to the plans sponsored by PPL Energy Supply, PPL Generation subsidiaries and PPL EnergyPlus are allocated a portion of the liabilities and costs of the pension and other postretirement benefit plans sponsored by PPL Services based on their participation in those plans. The pension liabilities assumed by PPL Energy Supply for these plans total \$55 million and \$58 million at December 31, 2003 and 2002. The prepaid other postretirement benefit costs assumed by PPL Energy Supply for these plans total \$1 million at December 31, 2003.

The other postretirement benefit liabilities assumed by PPL Energy Supply for these plans totaled \$3 million at December 31, 2002.

(PPL Montana)

The funded status of the PPL Montana plans was as follows:

	Pension Benefits		Other Postretirement Benefits	
	2003	2002	2003	2002
<b>Change in Benefit Obligation</b>				
Benefit Obligation, January 1	\$ 49	\$ 41	\$ 9	\$ 5
Service cost	2	2		
Interest cost	4	3	1	1
Plan amendments	1			
Actuarial gain		4	1	3
Benefits paid	(1)	(1)		
Benefit Obligation, December 31	<u>55</u>	<u>49</u>	<u>11</u>	<u>9</u>
<b>Change in Plan Assets</b>				
Plan assets at fair value, January 1	23	26		
Actual return on plan assets	9	(3)		
Employer contributions	15	1		
Benefits paid	(1)	(1)		
Plan assets at fair value, December 31	<u>46</u>	<u>23</u>		

	Pension Benefits		Other Postretirement Benefits	
	2003	2002	2003	2002
<b>Funded Status</b>				
Funded status of plan	(9)	(26)	(11)	(9)
Unrecognized actuarial gain	8	15	4	3
Unrecognized prior service cost	3	3		
Net amount recognized at end of year	<u>\$ 2</u>	<u>\$ (8)</u>	<u>\$ (7)</u>	<u>\$ (6)</u>
<b>Amounts recognized in the Balance Sheet consist of:</b>				
Accrued benefit liability	\$ 2	\$ (8)	\$ (7)	\$ (6)
Additional minimum liability	(11)	(13)		
Intangible asset	3	3		
Accumulated other comprehensive income	8	10		
Net amount recognized at end of year	<u>\$ 2</u>	<u>\$ (8)</u>	<u>\$ (7)</u>	<u>\$ (6)</u>
<b>Total accumulated benefit obligation for defined benefit pension plans</b>	55	44		

Information for pension plans with projected and accumulated benefit obligations in excess of plan assets follows:

	2003	2002
Projected benefit obligation	\$ 55	\$ 49
Accumulated benefit obligation	\$ 55	\$ 44
Fair value of plan assets	\$ 46	\$ 23

Information for other postretirement benefit plans with accumulated postretirement benefit obligations in excess of plan assets follows:

	2003	2002
Accumulated postretirement benefit obligation	\$ 11	\$ 9
Fair value of assets	\$ 0	\$ 0

(PPL Electric)

Although PPL Electric does not directly sponsor any pension or other postretirement benefit plans, PPL Electric is allocated a portion of the liabilities and costs of plans sponsored by PPL Services based on participation in those plans. At December 31, 2003 and 2002, the recorded balance of PPL Electric's allocated share of the total pension liability was \$74 million and \$71 million. At December 31, 2003, the balance in PPL Electric's allocated share of the total prepaid other postretirement benefit cost was \$2 million. At December 31, 2002, the balance in PPL Electric's allocated share of the total other postretirement benefit liability was \$1 million.

**Plan Assets - Domestic Pension Plans (PPL, PPL Energy Supply and PPL Montana)**

The asset allocation for the PPL Retirement Plan Master Trust and the target allocation, by asset category, are detailed below.

Asset Category	Percentage of plan assets at December 31,		Target asset allocation
	2003	2002	
Equity securities	73%	66%	70%
Debt securities	22%	29%	25%
Real estate and other	5%	5%	5%
Total	100%	100%	100%

The domestic pension plan assets are managed by outside investment managers and are rebalanced as necessary to maintain the target asset allocation ranges. PPL's investment strategy with respect to the domestic pension assets is to achieve a satisfactory risk adjusted return on assets that, in combination with PPL's funding policy and tolerance for return volatility, will ensure that sufficient dollars are available to provide benefit payments.

**Plan Assets - Domestic Other Postretirement Benefit Plans (PPL)**

The asset allocation for the PPL other postretirement benefit plans by asset category, are detailed below.

Asset Category	Percentage of plan assets at December 31,	
	2003	2002
Equity securities	56%	52%
Debt securities	44%	48%
Total	100%	100%

PPL's investment strategy with respect to its other postretirement benefit obligations is to fund the VEBA trusts with voluntary contributions and to invest in a tax efficient manner utilizing a prudent mix of assets. Based on the current VEBA and postretirement plan structure, a targeted asset allocation range of 50% to 60% equity and 40% to 50% debt is maintained.

**Plan Assets - International Pension Plans (PPL and PPL Energy Supply)**

WPD operates three defined benefit plans, the WPD Group segment of the Electricity Supply Pension Scheme (ESPS), the Western Power Utilities Pension Scheme (WPUPS), and the Infracore 1992 Scheme (Infracore). The assets of all three schemes are held separately from those of WPD in trustee-administered funds.

PPL's international pension plan asset allocation and target allocation are detailed below.

Asset Category	Percentage of plan assets at December 31,		Target asset allocation
	2003	2002	
Equity securities	75%	75%	75%
Debt securities	21%	21%	23%
Real estate and other	4%	4%	2%
Total	100%	100%	100%

In consultation with its investment advisor and with WPD, the group trustees of the WPD Group of the ESPS have drawn up Statement of Investment Principles (the Statement) to comply with the requirements of U.K. legislation.

The group trustees' primary investment objective is to maximize investment returns within the constraint of avoiding excessive volatility in the funding position.

**Expected Cash Flows - Domestic Pension Plans**

(PPL)

There are no contributions required for PPL's primary domestic pension plan or any of PPL's other domestic subsidiary pension plans. However, PPL subsidiaries expect to contribute approximately \$9 million to their pension plans in 2004 to ensure future compliance with minimum funding requirements.

PPL sponsors various non-qualified supplemental pension plans for which no assets are segregated from corporate assets. PPL expects to make approximately \$2 million of benefit payments under these plans in 2004.

(PPL Energy Supply and PPL Montana)

There are no contributions required for the PPL Montana pension plan. However, PPL Montana expects to contribute approximately \$7 million to the plan in 2004 to ensure future compliance with minimum funding requirements.

**Expected Cash Flows - Domestic Other Postretirement Benefit Plans (PPL)**

PPL is not required to make contributions to its other postretirement benefit plans, but has historically funded these plans in amounts equal to the postretirement benefit costs recognized. Continuation of this past practice would provide for PPL to contribute \$35 million to its other postretirement benefit plans in 2004.

**Expected Cash Flows - International Pension Plans (PPL and PPL Energy Supply)**

The pension plans of WPD are subject to formal actuarial valuations every three years, which are used to determine funding requirements. WPD expects to make contributions approximately \$3 million in 2004. Future contributions will be evaluated in accordance with these formal actuarial valuations.

the next of which will be performed as of March 31, 2004 in respect of WPD's principal pension scheme, the ESPS, to determine contribution requirements for 2005 and forward.

**Medicare Prescription Drug, Improvement and Modernization Act of 2003** *(PPL, PPL Energy Supply, PPL Electric and PPL Montana)*

On December 8, 2003, the Medicare Prescription Drug, Improvement and Modernization Act of 2003 (the Act) was signed into law. The Act introduces a prescription drug benefit under Medicare and also provides for a federal subsidy to sponsors of retiree health care benefit plans that provide an actuarially equivalent level of prescription drug benefits. The subsidy would be 28% of eligible drug costs for retirees that are over age 65 and covered under PPL's other postretirement benefit plans.

The impact of the Act on the provisions of SFAS 106 has yet to be determined by the FASB. PPL has elected to defer recognition of the potential impact of the Act, as allowed under FSP FAS 106-1, "Accounting and Disclosure Requirements Related to the Medicare Prescription Drug, Improvement and Modernization Act of 2003," which was issued by the FASB in January 2004. Thus, the measures of PPL's accumulated postretirement benefit obligations and net postretirement benefit costs in the financial statements and accompanying notes do not reflect the effects of the Act. PPL could be required to change previously reported information upon issuance of final accounting guidance related to the Act, as PPL's other postretirement benefit plans provide prescription drug coverage to retirees that may be eligible for the federal subsidy.

**Savings Plans** *(PPL, PPL Energy Supply, PPL Electric and PPL Montana)*

Substantially all employees of PPL's domestic subsidiaries are eligible to participate in deferred savings plans (401(k)s). Contributions to the plans charged to operating expense approximated the following:

	2003	2002	2001
PPL	\$ 11	\$ 11	\$ 10
PPL Energy Supply	6	6	5
PPL Electric	2	2	2
PPL Montana	2	1	1

**Employee Stock Ownership Plan** *(PPL, PPL Energy Supply and PPL Electric)*

PPL sponsors a non-leveraged ESOP, in which substantially all employees, excluding those of PPL Global, PPL Montana, PPL Gas Utilities and the mechanical contractors, are enrolled after one year of credited service. Dividends paid on ESOP shares are treated as ordinary dividends by PPL. Under existing income tax laws, PPL is permitted to deduct the amount of those dividends for income tax purposes and to contribute the resulting tax savings (dividend-based contribution) to the ESOP.

The dividend-based contribution is used to buy shares of PPL's common stock and is expressly conditioned upon the deductibility of the contribution for federal income tax purposes. Contributions to the ESOP are allocated to eligible participants' accounts as of the end of each year, based 75% on shares held in existing participants' accounts and 25% on the eligible participants' compensation.

Amounts charged as compensation expense for ESOP contributions approximated \$5 million in each of 2003 and 2002 and \$4 million in 2001. These amounts were offset by the dividend-based contribution tax savings and had no impact on PPL's earnings.

ESOP shares outstanding at December 31, 2003 totaled 4,841,488, or 3% of total common shares outstanding, and are included in all EPS calculations.

**Postemployment Benefits**

*(PPL, PPL Energy Supply and PPL Electric)*

Certain PPL subsidiaries provide health and life insurance benefits to disabled employees and income benefits to eligible spouses of deceased employees. Postemployment benefits charged to operating expenses were not significant in 2003, 2002 or 2001.

*(PPL and PPL Energy Supply)*

Certain of PPL Global subsidiaries, including Emel, EC, Elfec and Integra, provide limited non-pension benefits to all current employees. All active employees are entitled to benefits in the event of termination or retirement in accordance with government-sponsored programs. These plans generally obligate a company to pay one month's salary per year of service to employees in the event of involuntary termination. Under certain plans, employees with five or more years of service are entitled to this payment in the event of voluntary or involuntary termination. There is no limit on the number of years of service in the calculation of the benefit obligation.

The liabilities for these plans are accounted for under the guidance of EITF 88-1 "Determination of Vested Benefit Obligation for a Defined Benefit Pension Plan" using, what is commonly referred to as, the "shut down" method, where a company records the undiscounted obligation as if it were payable at each balance sheet date. The combined liabilities for these plans at December 31, 2003 and 2002 were \$8 million and \$6 million, and are recorded in "Deferred Credits and Noncurrent Liabilities - Other" on the Balance Sheet.

**13. Jointly-Owned Facilities**

*(PPL and PPL Energy Supply)*

At December 31, 2003, subsidiaries of PPL and PPL Energy Supply owned undivided interests in the facilities listed below.

The Balance Sheets of PPL and PPL Energy Supply include the amounts noted in the table below:

	Ownership Interest	Electric Plant in Service	Other Property	Accumulated Depreciation	Construction Work in Progress
<u>PPL Generation</u>					
Generating Stations					
Susquehanna	90.00%	\$ 4,320		\$ 3,541	\$ 63
Conemaugh	16.25%	191		70	1
Keystone	12.34%	97		49	1
Wyman Unit 4	8.33%	15		4	
Merrill Creek Reservoir	8.37%		\$ 22	13	

Each PPL Generation subsidiary provided its own funding for its share of the facility. Each receives a portion of the total output of the generating stations equal to its percentage ownership. The share of fuel and other operating costs associated with the stations is reflected on the Statement of Income.

*(PPL, PPL Energy Supply and PPL Montana)*

PPL Montana is the operator of the jointly-owned, coal-fired generating units comprising the Colstrip steam generation facility. At December 31, 2003 and 2002, PPL Montana had a 50% undivided leasehold interest in Colstrip Units 1 and 2 and a 30% undivided leasehold interest in Colstrip Unit 3 under operating leases. See Note 10 for additional information.

PPL Montana's share of direct expenses associated with the operation and maintenance of these facilities is included in the corresponding operating expenses on the Statement of Income. Each joint-owner in these facilities provides its own financing. As operator of all Colstrip Units, PPL Montana invoices each joint-owner for their respective portion of the direct expenses. The amount due from joint-owners was approximately \$9 million and \$8 million at December 31, 2003 and 2002.

At December 31, 2003, Montana Power continued to own a 30% leasehold interest in Colstrip Unit 4. As part of the purchase of generation assets from Montana Power, PPL Montana and Montana Power entered into a reciprocal sharing agreement to govern each party's responsibilities regarding the operation of Colstrip Units 3 and 4, and each party is responsible for 15% of the respective operating and construction costs, regardless of whether a particular cost is specified to Colstrip Unit 3 or 4. However, each party is responsible for its own fuel-related costs.

## 14. Commitments and Contingent Liabilities

### Energy Purchases and Sales Commitments

#### Liability for Above Market NUG Contracts (PPL, PPL Energy Supply and PPL Electric)

In 1998, PPL Electric recorded a loss accrual for above market contracts with NUGs of \$854 million, due to its generation business being deregulated. Effective January 1999, PPL Electric began reducing this liability as an offset to "Energy purchases" on the Statement of Income. This reduction is based on the estimated timing of the purchases from the NUGs and projected market prices for this generation. The final existing NUG contract expires in 2014. In connection with the corporate realignment in 2000, the remaining balance of this liability was transferred to PPL EnergyPlus. At December 31, 2003, the remaining liability associated with the above market NUG contracts was \$352 million.

#### Wholesale Energy Commitments

*(PPL, PPL Energy Supply and PPL Montana)*

As part of the purchase of generation assets from Montana Power, PPL Montana assumed a power purchase agreement and a power sales agreement (for the Flathead Irrigation Project), which were still in effect at December 31, 2003. In accordance with purchase accounting guidelines, PPL Montana recorded liabilities of \$66 million as the estimated fair value of these agreements at the acquisition date. These liabilities are being reduced over the terms of the agreements, through 2010, as adjustments to "Wholesale energy marketing" revenues and "Energy purchases" on the Statement of Income. The unamortized balance of the liability related to the power purchase agreement at December 31, 2003 was \$57 million and is included in "Wholesale energy commitments" on the Balance Sheet.

On July 1, 2002, PPL EnergyPlus began to sell to NorthWestern an aggregate of 450 MW of energy to be supplied by PPL Montana. Under two five-year agreements, PPL EnergyPlus is supplying 300 MW of around-the-clock electricity and 150 MW of unit-contingent on-peak electricity. PPL Montana also makes short-term energy sales to NorthWestern. Following NorthWestern's credit downgrades to below investment grade late-2002, PPL Montana and NorthWestern agreed to modify the payment provisions of the energy contracts such that NorthWestern would pay PPL Montana on a weekly basis, in arrears.

In September 2003, NorthWestern filed a voluntary petition for relief seeking to reorganize under Chapter 11 of the U.S. Bankruptcy Code. NorthWestern made its filing in federal bankruptcy court in Delaware. Between the time of NorthWestern's last weekly payment and the bankruptcy filing date, PPL Montana made approximately \$1.6 million of energy sales to NorthWestern.

Following the date that NorthWestern filed for bankruptcy, PPL Montana and NorthWestern agreed to amend the power supply agreements to, among other things, eliminate the weekly payment arrangements and resume more typical monthly invoicing and payment arrangements. The amendments were contingent on NorthWestern's assumption of the power supply agreements in its bankruptcy proceeding.

In September 2003, NorthWestern filed a motion with the bankruptcy court seeking, among other things, to assume the two five-year power supply agreements (as amended) and to pay PPL Montana for the approximately \$1.6 million of energy sales made immediately prior to the time of the bankruptcy filing. In October 2003, the bankruptcy court entered an order granting NorthWestern's motion. NorthWestern has, in accordance with the terms of the judge's order, paid PPL Montana for the pre-filing energy sales, and the parties have resumed monthly invoicing and payment arrangements.

*(PPL Montana)*

In June 2003, the FASB issued DIG Issue C20, "Scope Exceptions: Interpretation of the Meaning of Not Clearly and Closely Related in Paragraph 10(b) Regarding Contracts with a Price Adjustment Feature," which became effective October 1, 2003. DIG Issue C20 clarified that prior guidance did not permit the use of a broad market index to serve as a proxy for an ingredient or direct factor. Thus, DIG Issue C20 required that contracts that had been accounted for as normal, but were not eligible for normal treatment because they contained pricing linked to a broad market index, must be reflected on the balance sheet at their fair value, with an offsetting amount reflected in income as of the date of adoption. The power sales agreement referenced above for the Flathead Irrigation Project has a price escalator based upon the Consumer Price Index. Consequently, a pre-tax mark-to-market loss of \$2 million was recognized for this contract. This represented the difference between the current market value of the contract and the liability previously recorded in connection with the purchase of the Montana assets. This mark-to-market loss was recorded as a "Cumulative Effect of a Change in Accounting Principle" on the Statement of Income of PPL Montana.

*(PPL and PPL Energy Supply)*

As a result of New Jersey's Electric Discount and Energy Competition Act, its Board of Public Utilities authorized and made available to power suppliers, on a competitive basis, the opportunity to provide Basic Generation Service (BGS) to all non-shopping New Jersey customers. In February 2003, PPL EnergyPlus was awarded 34-month fixed-price BGS and 10-month hourly energy price BGS for a fixed percentage of customer load (approximately 1,000 MW) for Atlantic City Electric Company, Jersey Central Power & Light Company and Public Service Electric & Gas Company. These contracts commenced in August 2003.

In April 2003, PPL EnergyPlus entered into an agreement with Arizona Public Service Company to provide 112 MW of

capacity and associated electricity from July through September of 2003 and 150 MW from June through September of 2004 and 2005.

In May 2003, PPL EnergyPlus entered into agreements with Tucson Electric Power Company to provide 37 MW of capacity and associated electricity from June through December of 2003 and 75 MW from January 2004 through December 2006.

In May 2003, PPL EnergyPlus entered into a 20-year agreement with Community Energy, Inc. to purchase energy from its Bear Creek wind power project in northeastern Pennsylvania. The project is expected to produce up to 20 MW and be completed in 2004.

In September 2003, Connecticut Light and Power Company (CL&P) issued a request for proposals seeking energy supply for CL&P's Transitional Standard Offer retail customer load. In October 2003, PPL EnergyPlus was awarded a three-year, fixed-price contract beginning in January 2004 to supply 12.5% of CL&P's Transitional Standard Offer load. During peak hours, PPL EnergyPlus' obligation to supply CL&P's Transitional Standard Offer load may reach 625 MW.

## **Legal Matters**

*(PPL, PPL Energy Supply, PPL Electric and PPL Montana)*

PPL and its subsidiaries are involved in numerous legal proceedings, claims and litigation in the ordinary course of business. PPL and its subsidiaries cannot predict the ultimate outcome of such matters, or whether such matters may result in material liabilities.

## **Tax Assessment Appeals**

*(PPL and PPL Energy Supply)*

Pursuant to changes in PURTA enacted in 1999, PPL subsidiaries have filed a number of tax assessment appeals in various Pennsylvania counties where PPL facilities are located. These appeals challenge existing local tax assessments, which now comprise the basis for payment of the PURTA tax on PPL's properties. Also, as of January 1, 2000, generation facilities are no longer taxed under PURTA, and these local assessments will be used directly to determine local real estate tax liability for PPL's power plants. In July 1999, PPL filed retroactive appeals for tax years 1998 and 1999, as permitted by the new law. In addition, PPL has filed appeals for 2000 and beyond, as permitted under normal assessment procedures. It is anticipated that assessment appeals may now be an annual occurrence.

Hearings on the pending appeals were held by the boards of assessment appeals in each county, and decisions have now been rendered by all counties. To the extent the appeals were denied or PPL was not otherwise satisfied with the results, PPL filed further appeals from the board decisions with the appropriate county Courts of Common Pleas.

Of the two pending proceedings in Pennsylvania, only the appeal concerning the assessed value of the Susquehanna nuclear station will result in annual local taxes exceeding \$1 million. PPL's appeal of the Susquehanna station assessment was decided in its favor by the Luzerne County Court of Common Pleas, and PPL subsequently settled with the local taxing authorities, resulting in annual local tax liability of approximately \$3 million for tax years 2000 and beyond and no additional PURTA tax liability for tax years 1998 and 1999. However, the settlement of the tax liability for tax years 1998 and 1999 was subject to the outcome of claims asserted by certain intervenors which are described below.

In August 2000, over PPL's objections, the Luzerne County Court of Common Pleas permitted Philadelphia City and County, the Philadelphia School District and the Southeastern Pennsylvania Transportation Authority (SEPTA) (collectively, the "Philadelphia parties") to intervene in the case because a change in the assessment of the plant affected the amount they collected under PURTA for the tax years 1998 and 1999. Based on the appraisal obtained by the Philadelphia parties, PPL would have been required to pay up to an extra \$213 million in PURTA taxes for 1998 and 1999. The court ruled in PPL's favor concerning the assessed value of the plant, and this determination was affirmed by the Commonwealth Court in October 2003. The Philadelphia parties subsequently petitioned the Commonwealth Court for reargument, and this request was denied. The Philadelphia parties did not seek further appellate review of this matter.

*(PPL, PPL Energy Supply and PPL Montana)*

PPL Montana is currently protesting certain property tax assessments by the Montana Department of Revenue (MDOR) on its generation facilities. The tax liabilities in dispute are approximately \$2 million for 2000 and 2001, \$9 million for 2002 and \$6 million for 2003. PPL Montana's dispute with respect to most of the 2002 and 2003 tax liability is based on the assessed value used by the MDOR for PPL Montana's hydroelectric facilities versus the assessed value used for the facilities of another hydroelectric generator in the state. The state tax appeals board is scheduled to hear the 2000 and 2001 disputes in April 2004, while the hearing for the 2002 dispute is scheduled for May 2004. A hearing for the 2003 dispute has not yet been scheduled.

Montana Power Shareholders' Litigation *(PPL, PPL Energy Supply and PPL Montana)*

In August 2001, a purported class-action lawsuit was filed by a group of shareholders of Montana Power against Montana Power, the directors of Montana Power, certain advisors and consultants of Montana Power and PPL Montana. The plaintiffs allege, among other things, that Montana Power was required to, and did not, obtain shareholder approval of the sale of Montana Power's generation assets to PPL Montana in 1999. Although most of the claims in the complaint are against Montana Power, its board of directors, and its consultants and advisors, two claims are asserted against PPL Montana. In the first claim,

plaintiffs seek a declaration that because Montana Power shareholders did not vote on the 1999 sale of generating assets to PPL Montana, that sale "was null and void ab initio." The second claim alleges that PPL Montana was privy to and participated in a strategy whereby Montana Power would transfer generation assets to PPL Montana without first obtaining Montana Power shareholder approval, and that PPL Montana has made net profits in excess of \$100 million as the result of this alleged illegal sale. In the second claim, plaintiffs request that the court impose a "resulting and/or constructive trust" on both the generation assets themselves and all profits, plus interest on the amounts subject to the trust. This lawsuit is currently pending in the U.S. District Court of Montana, Butte Division. PPL, PPL Energy Supply and PPL Montana cannot predict the outcome of this matter.

NorthWestern Corporation Litigation *(PPL, PPL Energy Supply and PPL Montana)*

In connection with the acquisition of the Montana generation assets, the Montana Power APA, which was previously assigned to PPL Montana by PPL Global, includes a provision concerning the proposed purchase by PPL Montana of a portion of NorthWestern's interest in the 500-kilovolt Colstrip Transmission System (CTS) for \$97 million. During 2002, PPL Montana had been in discussions with NorthWestern regarding the proposed purchase of the CTS and the claims that PPL Montana believes it has against NorthWestern arising from the Montana Power APA and related agreements. Notwithstanding such discussions, in September 2002, NorthWestern filed a lawsuit against PPL Montana in Montana state court seeking specific performance of PPL Montana's purchase of the CTS, or alternatively, damages for breach of contract. Pursuant to PPL Montana's application, the matter was removed to the U.S. District Court of Montana, Butte Division. Following removal, NorthWestern asserted additional claims for damages against PPL Montana, and PPL Montana filed defenses denying liability for NorthWestern's claims as well as counterclaims against NorthWestern seeking damages PPL Montana believes it has suffered under the Montana Power APA and related agreements. This matter currently is scheduled for trial in the Montana federal district court in mid-2005.

In September 2003, NorthWestern filed a petition in Delaware for reorganization under the U.S. Bankruptcy Code, which has resulted in an automatic stay of PPL Montana's counterclaims against NorthWestern. PPL Montana has applied to the bankruptcy court for relief from the automatic stay. In December 2003, NorthWestern filed a motion to transfer this litigation from the Montana federal district court to the federal district court in Delaware where NorthWestern's bankruptcy proceeding is pending. PPL Montana has opposed the motion for transfer, which will be decided by the Montana federal district court. NorthWestern and PPL Montana also have stipulated in NorthWestern's bankruptcy proceeding that the automatic stay of PPL Montana's counterclaims will be lifted ten days after the Montana federal district court rules on the transfer motion. PPL, PPL Energy Supply and PPL Montana cannot predict the outcome of this litigation.

## Montana Hydroelectric Litigation (*PPL, PPL Energy Supply and PPL Montana*)

In October 2003, a lawsuit was filed against PPL Montana, PPL Services, Avista Corporation, PacifiCorp and nine John Doe defendants in the U.S. District Court of Montana, Missoula Division, by two residents allegedly acting in a representative capacity on behalf of the State of Montana. In January 2004, the complaint was amended to, among other things, include the Great Falls school districts as additional plaintiffs. The action seeks a declaratory judgment, compensatory damages for unjust enrichment, trespass and negligence, and attorneys fees on a "private attorney general" theory for use of state and/or "school trust" lands without the compensation required by law and to require defendants to adequately compensate the state and/or the State School Trust fund for full market value of lands occupied. Generally, the suit is founded on allegations that the bed of navigable rivers is state-owned property following admission to statehood, and that the use thereof for placement of dam structures, affiliated structures and reservoirs should trigger lease payments for use of land underneath. The plaintiffs allege that the State Land Board and Department of Natural Resources and Conservation failed to exercise their duty to administer riverbeds for the maximum benefit of public education and/or the state. No specific amount of damages has been claimed. PPL Montana and PPL Services cannot predict the outcome of this litigation.

## **Regulatory Issues**

### California ISO and Western Markets (*PPL, PPL Energy Supply and PPL Montana*)

Through its subsidiaries, PPL has made approximately \$18 million of sales to the California ISO, of which \$17 million has not been paid to PPL subsidiaries. Given the myriad of electricity supply problems presently faced by the California electric utilities and the California ISO, PPL cannot predict whether or when it will receive payment. As of December 31, 2003, PPL has fully reserved for possible underrecoveries of payments for these sales.

Regulatory proceedings arising out of the California electricity supply situation have been filed at the FERC. The FERC has determined that all sellers of energy into markets operated by the California ISO and the California Power Exchange, including PPL Montana, should be subject to refund liability for the period beginning October 2, 2000 through June 20, 2001 and initiated an evidentiary hearing concerning refund amounts. In April 2003, the FERC changed the manner in which this refund liability is to be computed and ordered further proceedings to determine the exact amounts that the sellers, including PPL Montana, would be required to refund.

In June 2003, the FERC took several actions as a result of a number of related investigations. The FERC terminated proceedings pursuant to which it had been considering whether to order refunds for spot market bilateral sales made in the Pacific Northwest, including sales made by PPL Montana,

during the period December 2000 through June 2001. The FERC explained that the totality of the circumstances made refunds unfeasible and inequitable, and that it had provided adequate relief by adopting a price cap throughout the western U.S. The FERC also denied pending complaints against long-term contracts in the western U.S. In these complaints, various power buyers challenged selected long-term contracts that they entered into during 2000 and 2001, complaining that the power prices were too high and reflected manipulation of those energy markets. The FERC found that the complainants had not met their burden of showing that changing or canceling the contracts was "in the public interest" and that the dysfunction in the California markets did not justify changing these long-term contracts. In two separate orders, the FERC also ordered 65 different companies, agencies or municipalities to show cause why they should not be ordered to disgorge profits for "gaming" or anomalous market behavior during 2000 and 2001. These orders to show cause address both unilateral and joint conduct identified as the "Enron trading strategies." Neither PPL EnergyPlus nor PPL Montana was included in these orders to show cause, and they previously have explained in responses to data requests from the FERC that they have not engaged in such trading strategies. Finally, the FERC issued a new investigation order directing its staff to investigate any bids made into the California markets in excess of \$250/MWh during the period from May 2000 to October 2000, a period of time prior to the period examined in connection with most of the proceedings described above. To their knowledge, neither PPL EnergyPlus nor PPL Montana is being investigated by the FERC under this new order.

Litigation arising out of the California electricity supply situation has been filed in California courts against sellers of energy to the California ISO. The plaintiffs and intervenors in these legal proceedings allege, among other things, abuse of market power, manipulation of market prices, unfair trade practices and violations of state antitrust laws, and seek other relief, including treble damages and attorneys' fees. While PPL's subsidiaries have not been named by the plaintiffs in these legal proceedings alleging abuses of market power, manipulation of market prices, unfair trade practices and violations of state antitrust laws, PPL Montana was named by a defendant in its cross-complaint in a consolidated court proceeding, which combined into one master proceeding several of the lawsuits alleging antitrust violations and unfair trade practices. This generator denies that any unlawful, unfair or fraudulent conduct occurred but asserts that, if it is found liable, the other generators and power marketers, including PPL Montana, caused, contributed to and/or participated in the plaintiffs' alleged losses.

In May 2003, the Port of Seattle filed a lawsuit in the U.S. District Court for the Western District of Washington against eighteen defendants, including PPL Montana. The lawsuit asserts claims against all defendants under the federal and state antitrust laws, the federal Racketeer Influenced and Corrupt Organizations Act and for common law fraud. The complaint centers on many of the same alleged activities that are the basis for the litigation arising out of the California electricity supply

situation described above. The Port of Seattle is seeking actual, trebled and punitive damages, as well as attorneys' fees. PPL Montana and several other defendants have filed a motion to dismiss this complaint that has not been ruled on by the court. In December 2003, this matter was transferred to the U.S. District Court for the Southern District of California for inclusion with proceedings already centralized and pending in that court.

In February 2004, the Montana Public Service Commission initiated a limited investigation of the Montana retail electricity market for the years 2000 and 2001, focusing on how that market was affected by transactions involving the possible manipulation of the electricity grid in the western U.S. The investigation includes all public utilities and licensed electricity suppliers in Montana, as well as other entities that may possess relevant information. Through its subsidiaries, PPL is a licensed electricity supplier in Montana and a wholesale supplier in the western U.S. As with the other investigations taking place as a result of the issues arising out of the electricity supply situation in California and other western states, PPL and its subsidiaries believe that they have not engaged in any improper trading or marketing practices affecting the Montana retail electricity market.

While PPL and its subsidiaries believe that they have not engaged in any improper trading practices, they cannot predict whether, or the extent to which, any PPL subsidiaries will be the target of any additional governmental investigations or named in other lawsuits or refund proceedings, the outcome of any such lawsuits or proceedings or whether the ultimate impact on them of the electricity supply situation in California and other western states will be material.

#### PJM Capacity Transactions (PPL, PPL Energy Supply and PPL Electric)

In November 2001, the PJM Market Monitor publicly released a report prepared for the PUC entitled "Capacity Market Questions" relating to the pricing of installed capacity in the PJM daily market during the first quarter of 2001. The report concluded that PPL EnergyPlus (identified in the report as "Entity 1") was able to exercise market power to raise the market-clearing price above the competitive level during that period. PPL EnergyPlus does not agree with the Market Monitor's conclusions that it exercised market power, and the Market Monitor acknowledged in his report that PJM's standards and rules did not prohibit PPL EnergyPlus' conduct. In November 2001, the PUC issued an Investigation Order directing its Law Bureau to conduct an investigation into the PJM capacity market and the allegations in the Market Monitor's report. In June 2002, the PUC issued an investigation report alleging, among other things, that PPL had unfairly manipulated electricity markets in early 2001. The PUC stated that it was not authorized to, and was not attempting to, adjudicate the merits of PPL's defenses to its allegations, but referred the matter to the U.S. Department of Justice - Antitrust Division (DOJ), the FERC and the Pennsylvania Attorney General.

In June 2003, the DOJ notified PPL that it had closed its investigation in this matter. Also in June, the Pennsylvania Attorney General's office completed its investigation and notified the PUC that PPL did not violate antitrust or other law in its capacity market activities. The FERC already has completed two investigations related to these capacity market questions and has found no reason to take action against PPL. PPL continues to believe that the PUC's report is inaccurate, that its conclusions are groundless, and that PPL acted ethically and legally, in compliance with all applicable laws and regulations.

In September 2002, PPL was served with a complaint filed by Utilimax.com, Inc., which was a member of PJM, in the U.S. District Court for the Eastern District of Pennsylvania against PPL and PPL EnergyPlus alleging, among other things, violations of the federal antitrust laws in connection with the capacity transactions described in the Market Monitor's report. The court dismissed the complaint with prejudice in July 2003, and Utilimax has appealed the court's dismissal to the U.S. Court of Appeals for the Third Circuit.

In December 2002, PPL was served with a complaint against PPL, PPL EnergyPlus and PPL Electric filed in the U.S. District Court for the Eastern District of Pennsylvania by a group of 10 Pennsylvania boroughs that apparently alleges, in broad terms, similar violations of the federal antitrust laws. These boroughs were wholesale customers of PPL Electric. In addition, in November 2003, PPL and PPL EnergyPlus were served with a complaint which was filed in the same court by Joseph Martorano, III (d/b/a ENERCO), that also alleges violation of the federal antitrust laws. The complaint indicates that ENERCO provides consulting and energy procurement services to clients in Pennsylvania and New Jersey. Although PPL, PPL EnergyPlus and PPL Electric believe the claims in these complaints are without merit, they cannot predict the outcome of these matters.

#### New England Investigation (PPL and PPL Energy Supply)

In January 2004, PPL became aware of an investigation by the Connecticut Attorney General and the FERC's Office of Market Oversight and Investigation (OMOI) regarding allegations that natural gas-fired generators located in New England illegally sold natural gas instead of generating electricity during the week of January 12, 2004. Subsequently, PPL and other generators were served with a data request by OMOI. The data request indicated that PPL was not under suspicion of a regulatory violation but that OMOI was conducting an initial investigation. PPL has responded to this data request. While PPL does not believe that it committed any regulatory or other violations concerning the subject matter of the investigation, PPL cannot predict the outcome of the investigation.

#### FERC Market-Based Rate Authority (PPL and PPL Energy Supply)

In December 1998, the FERC issued an order authorizing PPL EnergyPlus to make wholesale sales of electric power and related products at market-based rates. In that order, the FERC

directed PPL EnergyPlus to file an updated market analysis within three years of the date of the order, and every three years thereafter. PPL EnergyPlus filed its initial updated market analysis in December 2001. Several parties thereafter filed interventions and protests requesting that, in light of the PJM Market Monitor's report described above, PPL EnergyPlus be required to provide additional information demonstrating that it has met the FERC's market power tests necessary for PPL EnergyPlus to continue its market-based rate authority. PPL EnergyPlus has responded that the FERC does not require the economic test suggested by the intervenors and that, in any event, it would meet such economic test if required by the FERC. PPL EnergyPlus cannot predict the outcome of this matter.

#### FERC Proposed Rules (PPL, PPL Energy Supply, PPL Electric and PPL Montana)

In July 2002, the FERC issued a Notice of Proposed Rulemaking entitled "Remedying Undue Discrimination through Open Access Transmission Service and Standard Electricity Market Design." The proposed rule is currently available for public comment and contains a proposed implementation date of July 31, 2003. However, since the issuance of the proposed rule, the FERC has delayed the implementation date. This far-reaching proposed rule, in its current form, purports to establish uniform transmission rules and a standard market design by, among other things:

- enacting standard transmission tariffs and uniform market mechanisms,
- monitoring and mitigating "market power,"
- managing transmission congestion through pricing and tradable financial rights,
- requiring independent operational control over transmission facilities,
- forming state advisory committees on regional transmission organizations and resource adequacy, and
- exercising FERC jurisdiction over all transmission service.

In April 2003, the FERC issued a white paper describing certain modifications to the proposed rule. The FERC has requested comments and is holding numerous public comment sessions concerning the white paper.

If adopted, this proposed rule may have a significant impact on PPL and its subsidiaries, which cannot be predicted at this time.

In November 2003, the FERC adopted a proposed rule to condition all new and existing electric market-based tariffs and authorizations to include provisions prohibiting the seller from engaging in anticompetitive behavior or the exercise of market power. The FERC order adopts a list of market behavior rules that apply to all electric market-based rate tariffs and authorizations, including those of PPL EnergyPlus and any other PPL subsidiaries that hold market-based rate authority. PPL does not expect this rule to have a significant impact on its subsidiaries.

#### Montana Hydroelectric License Contingencies (PPL Montana)

PPL Montana has 11 hydroelectric facilities and one storage reservoir licensed by the FERC pursuant to the Federal Power Act under long-term licenses which expire on varying dates from 2009 through 2040. Pursuant to Section 8(e) of the Federal Power Act, the FERC approved the transfer from Montana Power to PPL Montana of all pertinent licenses and any amendments in connection with the Montana APA.

The Kerr Dam Project license was jointly issued by the FERC to Montana Power and the Confederated Salish and Kootenai Tribes of the Flathead Reservation in 1985, and required Montana Power to hold and operate the project for 30 years. The license required Montana Power, and subsequently PPL Montana as a result of the purchase of the Kerr Dam from Montana Power, to continue to implement a plan to mitigate the impact of the Kerr Dam on fish, wildlife and the habitat. Under this arrangement, PPL Montana has a remaining commitment to spend approximately \$22 million between 2004 and 2015.

PPL Montana entered into a Memorandum of Understanding (MOU) with state, federal and private entities related to the issuance in 2000 of the FERC renewal license for the nine dams for the Missouri-Madison project. The MOU requires PPL Montana to implement plans to mitigate the impact of its projects on fish, wildlife and the habitat, and to increase recreational opportunities. The MOU was created to maximize collaboration between the parties and possibilities for matching funds. Under this arrangement, PPL Montana has a remaining commitment to spend approximately \$17 million between 2004 and 2010.

#### Wallingford Deactivation (PPL and PPL Energy Supply)

In January 2003, PPL negotiated an agreement with the ISO - New England that would declare that four of the five units at PPL's Wallingford, Connecticut facility are "reliability must run" units and put those units under cost-based rates. This agreement and the cost-based rates are subject to the FERC's approval, and PPL filed a request with the FERC for such approval. PPL requested authority for cost-based rates because the current and anticipated wholesale prices in New England are insufficient to cover the costs of keeping these units available for operation. In March 2003, PPL filed an application with the New England Power Pool to temporarily deactivate these four units. In May 2003, FERC denied PPL's request for cost-based rates in light of FERC's changes to the market and bid mitigation rules of the ISO - New England made in a similar case involving generating units owned by NRG Energy, Inc. PPL subsequently has explained to the FERC that its changes to the market and bid mitigation rules of ISO - New England will not provide sufficient revenues to PPL, and PPL continues to seek approval of its cost-based rates. However, PPL has informed the New England Power Pool that it will not pursue its request to temporarily deactivate certain Wallingford units. In February 2004, PPL appealed the FERC's denial of its request

for cost-based rates to the U.S. Court of Appeals for the D.C. Circuit. PPL cannot predict the outcome of this matter.

### IRS Synthetic Fuels Tax Credits (PPL and PPL Energy Supply)

Through one of its subsidiaries, PPL operates a synfuel facility in Somerset, Pennsylvania and receives tax credits pursuant to Section 29 of the Internal Revenue Code based on its sale of synfuel to unaffiliated third-party purchasers. Section 29 of the Internal Revenue Code provides tax credits for the production and sale of solid synthetic fuels produced from coal. To qualify for the Section 29 tax credits, the synthetic fuel must meet three primary conditions: (i) there must be a significant chemical change in the coal feedstock, (ii) the product must be sold to an unaffiliated entity, and (iii) the production facility must have been placed in service before July 1, 1998. Section 29 tax credits are currently scheduled to expire at the end of 2007.

PPL received a private letter ruling from the IRS in November 2001 pursuant to which, among other things, the IRS concluded that the synthetic fuel produced at the Somerset facility qualifies for Section 29 tax credits. PPL uses the Covol technology to produce synfuel at the Somerset facility, and the IRS issued the private letter ruling after its review and approval of that technology. In reliance on this private letter ruling, PPL has sold synfuel produced at the Somerset facility resulting in an aggregate of approximately \$147 million of tax credits as of December 31, 2003. PPL has estimated that the Somerset facility will contribute approximately \$0.13 to its EPS in each year from 2004 through 2007. PPL also purchases synfuel from unaffiliated third parties, at prices below the market price of coal, for use at its coal-fired power plants.

In June 2003, the IRS announced that it had reason to question the scientific validity of certain test procedures and results that have been presented to it by taxpayers with interests in synfuel operations as evidence that the required significant chemical change has occurred, and that it was reviewing information regarding these test procedures and practices. In conjunction with such review, the IRS suspended the issuance of private letter rulings concerning whether a significant chemical change has occurred for requests relying on the procedures and results being reviewed. In addition, the IRS indicated that it might revoke existing private letter rulings that relied on the procedures and results under review if it determined that those test procedures and results do not demonstrate that a significant chemical change has occurred.

In October 2003, the IRS announced that it had completed its review of the scientific validity of test procedures and results presented by taxpayers as evidence of significant chemical change and determined that the test procedures and results used by taxpayers are scientifically valid, if the procedures are applied in a consistent and unbiased manner. Further, the IRS announced that it will continue to issue rulings on significant chemical change under applicable IRS guidelines, despite some question by the IRS as to whether those processes result in the level of significant chemical change required by Section 29 of

the Internal Revenue Code and IRS revenue rulings. Finally, the IRS indicated that it would require taxpayers to comply with certain sampling and data/record retention practices to obtain maintain a ruling on significant chemical change.

PPL believes that the October IRS announcement confirms PPL is justified in its reliance on the private letter ruling for the Somerset facility, that the test results that PPL presented to the IRS in connection with its private letter ruling are scientifically valid and that PPL has operated the Somerset facility in compliance with the private letter ruling and Section 29 of the Internal Revenue Code.

In October 2003, following the IRS announcement, it was reported that the U.S. Senate Permanent Subcommittee on Investigations, of the Committee on Governmental Affairs, has begun an investigation of the synthetic fuel industry and its producers. PPL cannot predict when the investigation will be completed or the potential results of the investigation.

### U.K. Electricity Regulation (PPL and PPL Energy Supply)

The principal legislation governing the structure of the electricity industry in Great Britain is the Electricity Act 1989 (the "Electricity Act"), as amended by the Utilities Act 2000 (the "Utilities Act").

The provisions in the Utilities Act include the replacement of individual gas and electricity regulators with the Gas and Electricity Markets Authority (the "Regulator"). The principal objective of the Regulator is to protect the interests of consumers, wherever appropriate, by promoting effective competition in electricity generation and supply. There currently is no competition in electricity distribution, but recently a small operator has applied to the Regulator for a license to operate in Great Britain.

Each distribution business constitutes a natural regional monopoly and is subject to control on the prices it can charge and the quality of supply it must provide. The operations of WPD are regulated under its distribution licenses, pursuant to which income generated is subject to an allowed revenue regulatory framework that provides economic incentives to minimize operating, capital and financing costs. Under the Electricity Act, WPD is under a statutory duty to offer terms to connect any customer requiring electricity within their area and to maintain that connection. The allowed revenue that is recovered from electricity supply businesses through charges by the Distribution Network Operator (DNO) made for the use of the distribution network is regulated on the basis of the Retail Price Index (RPI) minus X formula. The allowed revenue is increased by RPI minus X during the tenure of each price control period. (RPI is a measure of inflation and equals the percentage change in the U.K. RPI between the six-month period of July to December in the previous year. The X factor established by the Regulator following review and represents annual efficiency factor.) The Regulator currently sets the Distribution Price Control Formula for five-year periods.

The current Distribution Price Control Formula permits DNOs, within a review period, to partially retain additional revenues due to increased distribution of units and to retain all increases in operating profit due to efficient operations and the reduction in expenses (including financing costs). The Regulator may reduce this increase in operating profit through a one-off price reduction in the first year of the new pricing regime, if the Regulator determines that it is not a function of efficiency savings, or if genuine efficiency savings have been made and the Regulator determines that customers should benefit through lower prices.

In December 1999, the Regulator published final price proposals for distribution price control for the 12 DNOs in England and Wales. These proposals represented a reduction to distribution prices of 20% for WPD (South West) and 26% for WPD (South Wales) effective April 2000, followed by a reduction in real terms (i.e., before inflation is taken into account) of 3% each year from April 2001. This price control is scheduled to operate until March 2005.

Improvements in quality of supply form an important part of the final proposals. Revised targets for system performance, in terms of the security and availability of supply, were proposed with new targets for reductions in minutes lost and interruptions.

The Regulator has introduced a quality of service incentive plan for the period from April 2002 to March 2005. Companies will be penalized annually up to 2% of revenue for failing to meet their quality of supply targets for the incentive plan. The plan includes a mechanism for rewarding companies which exceed their targets based on their rate of improvement of performance during the period and a process for rewarding exceptional performance by specifying how the targets will be reset.

Distribution businesses must also meet the Guaranteed and Overall Standards of Performance, which are set by the Regulator to ensure an appropriate level of quality of supply. If a company fails to provide the level of service specified, it must make a fixed payment to the retail customer affected.

In June 2003, the Regulator published a report on the quality of supply from April 2001 through March 2002. The report confirms that WPD (South West) and WPD (South Wales) met or exceeded such standards and that no payments were required to be made by either company.

Any significant lowering of rates implemented by the Regulator after the current price control ends in March 2005 could lower the amount of revenue WPD generates in relation to its operational cost and could materially lower the income of WPD.

## Environmental Matters - Domestic

*(PPL, PPL Energy Supply, PPL Electric and PPL Montana)*

Due to the environmental issues discussed below or other environmental matters, PPL subsidiaries may be required to modify, replace or cease operating certain facilities to comply with statutes, regulations and actions by regulatory bodies or courts. In this regard, PPL subsidiaries also may incur capital expenditures or operating expenses in amounts which are not now determinable, but which could be significant.

Air *(PPL, PPL Energy Supply and PPL Montana)*

The Clean Air Act deals, in part, with acid rain, attainment of federal ambient ozone standards and toxic air emissions in the U.S. PPL's subsidiaries are in substantial compliance with the Clean Air Act. The Bush administration and certain members of Congress have made proposals regarding possible amendments to the Clean Air Act. These amendments could require significant further reductions in nitrogen oxide, sulfur dioxide and mercury and could possibly require measures to limit carbon dioxide. In addition, several states have taken their own actions requiring mandatory carbon dioxide emission reductions. Pennsylvania and Montana have not, at this time, established any formal programs to address carbon dioxide and other greenhouse gases.

The Pennsylvania DEP has finalized regulations requiring further seasonal (May-June) nitrogen oxide reductions to 80% from 1990 levels starting in 2003. These regulations are pursuant to EPA's 1998 State Implementation Plan (SIP) call to 22 eastern states, including Pennsylvania, to revise their state implementation plans. PPL achieved the 2003 nitrogen oxide reductions with the installation of SCR technology on the Montour units, and may install SCR or other additional nitrogen oxide reduction technology on one or more Brunner Island units at a later date.

The EPA has also developed new standards for ambient levels of ozone and fine particulates in the U.S. These standards have been upheld following court challenges. The new particulates standard may require further reductions in sulfur dioxide and year-round nitrogen oxide reductions commencing in 2010-2012 at SIP-call levels in Pennsylvania for certain PPL subsidiaries, and at slightly less stringent levels in Montana. The revised ozone standard is not expected to have a material effect on facilities of PPL subsidiaries.

The EPA has proposed mercury and nickel regulations and is expected to finalize these regulations in 2004. The cost of complying with these regulations is not now determinable, but could be significant.

In 1999, the EPA initiated enforcement actions against several utilities, asserting that older, coal-fired power plants operated by those utilities have, over the years, been modified in ways that subject them to more stringent "New Source" requirements under the Clean Air Act. The EPA has since issued notices of

violation and commenced enforcement activities against other utilities. The future direction of the EPA's enforcement initiative is presently unclear. Therefore, at this time, PPL is unable to predict whether such EPA enforcement actions will be brought with respect to any of its affiliates' plants. However, the EPA regional offices that regulate plants in Pennsylvania (Region III) and Montana (Region VIII) have indicated an intention to issue information requests to all utilities in their jurisdiction. The Region VIII office issued such a request to PPL Montana's Corette plant in 2000 and the Colstrip plant in 2003. The Region III office issued such a request to PPL Generation's Martins Creek plant in 2002. PPL and its subsidiaries have responded to the Corette and Martins Creek information requests and are in the process of responding to the Colstrip information request. The EPA has taken no further action following the Martins Creek and Corette submittals. PPL cannot presently predict what, if any, action the EPA might take in this regard. Should the EPA or any state initiate one or more enforcement actions against PPL or its subsidiaries, compliance with any such enforcement actions could result in additional capital and operating expenses in amounts which are not now determinable, but which could be significant.

In 2003, the EPA issued changes to its "New Source" regulations that clarify what projects are exempt from "New Source" requirements as routine maintenance and repair. Under these clarifications, any project to replace existing equipment with functionally equivalent equipment would be considered routine maintenance and excluded from "New Source" review if the cost of the replaced equipment does not exceed 20% of the replacement cost of the entire process unit, the basic design is not changed and no permit limit is exceeded. These clarifications would substantially reduce the uncertainties under the prior "New Source" regulations; however, they have been stayed by the U.S. Court of Appeals for the District of Columbia Circuit. PPL is therefore continuing to operate under the "New Source" regulations as they existed prior to the EPA's clarifications.

The New Jersey DEP and some New Jersey residents raised environmental concerns with respect to the Martins Creek plant, particularly with respect to sulfur dioxide emissions and the opacity of the plant's plume. These issues were raised in the context of an appeal by the New Jersey DEP of the Air Quality Plan Approval issued by the Pennsylvania DEP to the adjacent Lower Mt. Bethel facility, which is currently under construction. In October 2003, PPL finalized an agreement with the New Jersey DEP and the Pennsylvania DEP pursuant to which it will reduce sulfur dioxide emissions from its Martins Creek power plant. Under the agreement, PPL Martins Creek will shut down the plant's two coal-fired generating units by September 2007 and may repower them any time after shutting them down so long as it follows all applicable state and federal requirements, including installing the best available pollution control technology. PPL Martins Creek also will reduce the fuel sulfur content for those units as well as the plant's two oil-fired units beginning in 2004. In addition, PPL will donate to a non-profit organization 70% of the excess emission allowances and emission reduction credits that result from shutting down or

repowering the coal units. As a result of the agreement, the New Jersey DEP has withdrawn its challenge to the Air Quality Plan Approval for the Lower Mt. Bethel facility. The agreement will not result in material costs to PPL. The agreement does not address the issues raised by the New Jersey DEP regarding the visible opacity of emissions from the Martins Creek plant. If it is determined that actions must be taken to address the visible opacity of these emissions, such actions could result in costs that are not now determinable, but which could be significant.

In addition to the opacity concerns raised by the New Jersey DEP, the Pennsylvania DEP also has raised concerns about the opacity of emissions from the Martins Creek and Montour plants. PPL is discussing these concerns with the Pennsylvania DEP. If it is determined that actions must be taken to address the Pennsylvania DEP's concerns, such actions could result in costs that are not now determinable, but which could be significant.

In December 2003, PPL Montana, as operator of the Colstrip facility, received an Administrative Compliance Order (ACO) from the EPA pursuant to the Clean Air Act. The ACO alleges that Units 3 and 4 of the facility have been in violation of the Clean Air Act permit at Colstrip since 1980. The permit required Colstrip to submit for review and approval by the EPA an analysis and proposal for reducing emissions of nitrogen oxides (NO<sub>x</sub>) to address visibility concerns if and when EPA promulgates Best Available Retrofit Technology requirements for NO<sub>x</sub>. The EPA is asserting that regulations it promulgated in 1980 triggered this requirement. PPL believes that the ACO is unfounded and is discussing the matter with the EPA. The ACO does not expressly seek penalties, and it is unclear at this time what, if any, additional control technology the EPA may consider to be required. Accordingly, the costs to install any additional controls for NO<sub>x</sub>, if required, are not now determinable, but could be significant.

#### Water/Waste (PPL, PPL Energy Supply and PPL Montana)

A final permit for water discharges (NPDES permit) has been issued to the Brunner Island generating plant. The permit contains a provision requiring further studies on the thermal impact of the cooling water discharge from the plant. These studies are underway and are expected to be completed in 2006. The Pennsylvania DEP has stated that it believes the studies to date show that the temperature of the discharge must be lowered. The Pennsylvania DEP has also stated that it believes the plant is in violation of a permit condition prohibiting the discharge from changing the river temperature by more than two degrees per hour. PPL is discussing these matters with the agency. Depending on the outcome of these discussions, the plant could be subject to additional capital and operating costs that are not now determinable, but which could be significant.

The Pennsylvania DEP has issued a water quality certification and a draft NPDES permit to PPL Holtwood, LLC in the FERC license renewal proceeding for its Lake Wallenpaupack hydroelectric facility. PPL has appealed the certification and is discussing both the certification and the NPDES permit with the

Pennsylvania DEP. If these discussions are unsuccessful, PPL expects to appeal the permit as well. Depending on the outcome of these appeals, each of the certification and the NPDES permit could impose additional costs on PPL, which are not now determinable, but which could be significant.

The EPA has significantly tightened the water quality standard for arsenic. The revised standard may require several PPL subsidiaries to either further treat wastewater or take abatement action at their power plants, or both. The cost of complying with the revised standard is not now determinable, but could be significant.

The EPA recently finalized requirements for new or modified water intake structures. These requirements will affect where generating facilities are built, will establish intake design standards, and could lead to requirements for cooling towers at new and modified power plants. If the source of water for the plants is surface water, these rules could impose significant capital and operating costs on PPL subsidiaries. Another new rule, expected to be finalized in 2004, will address existing structures. PPL has begun preliminary studies to evaluate options to comply with the expected rule. Each of these rules could impose additional costs on PPL subsidiaries, which are not now determinable, but which could be significant.

### Superfund and Other Remediation

*(PPL and PPL Energy Supply)*

Under the Pennsylvania Clean Streams Law, subsidiaries of PPL Generation are obligated to remediate acid mine drainage at former mine sites and may be required to take additional measures to prevent potential acid mine drainage at previously capped refuse piles. One PPL subsidiary is pumping and treating mine water at two mine sites. Another PPL subsidiary plans to install passive wetlands treatment at a third site, and the Pennsylvania DEP has suggested that it may require that PPL subsidiary to pump and treat the mine water at that third site. At December 31, 2003, PPL had accrued \$29 million to cover the costs of pumping and treating groundwater at two mine sites for 50 years and for installing passive wetlands treatment at the third site.

*(PPL, PPL Energy Supply and PPL Electric)*

In 1995, PPL Electric and PPL Generation entered into a consent order with the Pennsylvania DEP to address a number of sites that were not being addressed under another regulatory program such as Superfund, but for which PPL Electric or PPL Generation may be liable for remediation. This may include potential PCB contamination at certain PPL Electric substations and pole sites; potential contamination at a number of coal gas manufacturing facilities formerly owned or operated by PPL Electric; oil or other contamination which may exist at some of PPL Electric's former generating facilities; and potential contamination at abandoned power plant sites owned by PPL Generation. As of December 31, 2003, work has been completed for 94% of the sites included in the consent order.

Additional sites formerly owned or operated by PPL Electric are added to the consent order on a case-by-case basis.

In 1996, PPL Gas Utilities entered into a similar consent order with the Pennsylvania DEP to address a number of sites where subsidiaries of PPL Gas Utilities may be liable for remediation. The sites primarily include former coal gas manufacturing facilities. Subsidiaries of PPL Gas Utilities are also investigating the potential for any mercury contamination from gas meters and regulators. Accordingly, PPL Gas Utilities and the Pennsylvania DEP have agreed to add 72 meter/regulation sites to the consent order. As of December 31, 2003, PPL Gas Utilities had addressed 24% of the sites under its consent order.

At December 31, 2003, PPL Electric and PPL Gas Utilities had accrued approximately \$3 million and \$9 million, representing the estimated amounts they will have to spend for site remediation, including those sites covered by each company's consent orders mentioned above. Depending on the outcome of investigations at sites where investigations have not begun or have not been completed, the costs of remediation and other liabilities could be substantial. PPL also could face other non-remediation liabilities at sites included in the consent order or other contaminated sites, the costs of which are not now determinable, but which could be significant.

*(PPL, PPL Energy Supply and PPL Montana)*

In conjunction with its 1999 sale of generating assets to PPL Montana, Montana Power prepared a Phase I and Phase II Environmental Site Assessment. The assessment identified various groundwater remediation issues. Based upon subsequent assessments and actions taken by PPL Montana, the costs to PPL Montana of the groundwater remediation measures identified in those assessments are expected to be approximately \$3 million. However, additional expenditures could be required in amounts which are not now determinable, but which could be significant.

In May 2003, approximately 40 plaintiffs brought an action in the Montana Second Judicial District Court, Butte-Silver Bow County, against PPL Montana and the other owners of the Colstrip plant alleging property damage from freshwater pond seepage and contamination from wastewater ponds at the plant. This action has been moved to the Montana Sixteenth Judicial District Court, Rosebud County. This action could result in PPL Montana and the other Colstrip owners being liable for damages and being required to take additional remedial measures, the costs of which are not now determinable, but which could be significant.

In 1999, the Montana Supreme Court held in favor of several citizens' groups that the right to a clean and healthful environment is a fundamental right guaranteed by the Montana Constitution. The court's ruling could result in significantly more stringent environmental laws and regulations, as well as an increase in citizens' suits under Montana's environmental laws. The effect on PPL Montana of any such changes in laws or

regulations or any such increase in legal actions is not currently determinable, but it could be significant.

Future cleanup or remediation work at sites currently under review, or at sites not currently identified, may result in material additional operating costs for PPL subsidiaries that cannot be estimated at this time.

#### Asbestos (PPL and PPL Energy Supply)

There have been increasing litigation claims throughout the U.S. based on exposure to asbestos against companies that manufacture or distribute asbestos products or that have these products on their premises. Certain of PPL's generation subsidiaries and certain of its energy services subsidiaries, such as those that have supplied, may have supplied or installed asbestos material in connection with the repair or installation of process piping and heating, ventilating and air conditioning systems, have been named as defendants in asbestos-related lawsuits. PPL cannot predict the outcome of these lawsuits or whether additional claims may be asserted against its subsidiaries in the future. PPL does not expect that the ultimate resolution of the current lawsuits will have a material adverse effect on its financial condition.

#### Electric and Magnetic Fields (PPL, PPL Energy Supply and PPL Electric)

Concerns have been expressed by some members of the public regarding the potential health effects of EMFs. These fields are emitted by all devices carrying electricity, including electric transmission and distribution lines and substation equipment. Government officials in the U.S. and the U.K. have focused attention on this issue. PPL and its subsidiaries support the current efforts to determine whether EMFs cause any human health problems and are taking steps to reduce EMFs, where practical, in the design of new transmission and distribution facilities. PPL is unable to predict what effect, if any, the EMF issue might have on its operations and facilities either in the U.S. or abroad, and the associated cost, or what, if any, liabilities it might incur related to the EMF issue.

#### Lower Mt. Bethel (PPL and PPL Energy Supply)

In August 2002, the Northampton County Court of Common Pleas issued a decision concerning the permissible noise levels from the Lower Mt. Bethel facility when it becomes operational. Specifically, the court's decision sets certain permissible noise levels required for plant operation. PPL appealed the court's decision to the Commonwealth Court, and an intervenor in the lawsuit cross-appealed the court's decision. In May 2003, the Commonwealth Court remanded the case to the Court of Common Pleas for further findings of fact concerning the zoning application relating to the construction of the facility. In September 2003, the Court of Common Pleas ruled in PPL's favor while also reaffirming its decision on the noise levels, and the intervenor has appealed this ruling to the Commonwealth Court. The Lower Mt. Bethel facility is expected to be operational in 2004. However, PPL and PPL Energy Supply

cannot predict the outcome of the ongoing litigation concerning the facility or its ultimate impact on the Lower Mt. Bethel facility, but such impact may be material.

#### **Environmental Matters - International** (PPL and PPL Energy Supply)

##### U.K.

WPD's distribution businesses are subject to numerous regulatory and statutory requirements with respect to environmental matters. PPL believes that WPD has taken and continues to take measures to comply with the applicable laws and governmental regulations for the protection of the environment. There are no material legal or administrative proceedings pending against WPD with respect to environmental matters. See "Environmental Matters - Domestic - Electric and Magnetic Fields" for a discussion of EMFs.

##### Latin America

Certain of PPL's affiliates have electric distribution operations in Latin America. PPL believes that these affiliates have taken and continue to take measures to comply with the applicable laws and governmental regulations for the protection of the environment. There are no material legal or administrative proceedings pending against PPL's affiliates in Latin America with respect to environmental matters.

##### **Other**

#### Nuclear Insurance (PPL and PPL Energy Supply)

PPL Susquehanna is a member of certain insurance programs which provide coverage for property damage to members' nuclear generating stations. Facilities at the Susquehanna station are insured against property damage losses up to \$2.75 billion under these programs. PPL Susquehanna is also a member of an insurance program which provides insurance coverage for the cost of replacement power during prolonged outages of nuclear units caused by certain specified conditions. Under the property and replacement power insurance program, PPL Susquehanna could be assessed retroactive premiums in the event of the insurers' adverse loss experience. At December 31, 2003, this maximum assessment was about \$40 million.

PPL Susquehanna's public liability for claims resulting from a nuclear incident at the Susquehanna station is limited to about \$10.9 billion under provisions of The Price Anderson Amendments Act of 1988. PPL Susquehanna is protected against this liability by a combination of commercial insurance and an industry assessment program. In the event of a nuclear incident at any of the reactors covered by The Price Anderson Amendments Act of 1988, PPL Susquehanna could be assessed up to \$201 million per incident, payable at \$20 million per year.

## Guarantees and Other Assurances

*(PPL, PPL Energy Supply and PPL Electric)*

In the normal course of business, PPL, PPL Energy Supply and PPL Electric enter into agreements that provide financial performance assurance to third parties on behalf of certain subsidiaries. Such agreements include, for example, guarantees, stand-by letters of credit issued by financial institutions and surety bonds issued by insurance companies. These agreements are entered into primarily to support or enhance the creditworthiness attributed to a subsidiary on a stand-alone basis, thereby facilitating the extension of credit to accomplish the subsidiaries' intended commercial purposes.

*(PPL, PPL Energy Supply, PPL Electric and PPL Montana)*

PPL, PPL Energy Supply, PPL Electric and PPL Montana provide certain guarantees that are required to be disclosed in accordance with FIN 45, "Guarantor's Accounting and Disclosure Requirements for Guarantees, Including Indirect Guarantees of Indebtedness of Others, an Interpretation of FASB Statements No. 5, 57, and 107 and Rescission of FASB Interpretation No. 34." See Note 22 for a discussion of FIN 45. The guarantees provided as of December 31, 2003 are discussed below. In accordance with the provisions of FIN 45, the fair values of guarantees related to arrangements entered into prior to January 1, 2003, as well as guarantees excluded from the initial recognition and measurement provisions of FIN 45, are not recorded in the financial statements.

*(PPL)*

PPL fully and unconditionally guarantees the debt securities of PPL Capital Funding, a wholly-owned financing subsidiary of PPL, including PPL Capital Funding's medium-term notes and the notes issued by PPL Capital Funding in connection with the PEPS Units and PEPS Units, Series B. PPL also fully and unconditionally guarantees all of the obligations of PPL Capital Funding Trust I, an unconsolidated wholly-owned financing subsidiary of PPL, under the trust preferred securities that are a component of the PEPS Units. The aggregate face value of the trust's outstanding preferred securities was \$575 million at December 31, 2003. See the Statement of Company-Obligated Mandatorily Redeemable Securities for a discussion of the terms of the trust preferred securities of PPL Capital Funding Trust I and Note 8 for a description of the exchange offer involving the PEPS Units and PEPS Units, Series B and the remarketing of the trust preferred securities of PPL Capital Funding Trust I.

*(PPL and PPL Energy Supply)*

WPD LLP guarantees all of the obligations of SIUK Capital Trust I, an unconsolidated wholly-owned financing subsidiary of WPD LLP, under its trust preferred securities. The aggregate face value of the trust's outstanding preferred securities was \$82 million at December 31, 2003. See the Statement of Company-Obligated Mandatorily Redeemable Securities for a discussion

of the terms of the trust preferred securities of SIUK Capital Trust I.

*(PPL Energy Supply)*

PPL Energy Supply has entered into several standby letter of credit arrangements under its \$500 million three-year credit facility for the purposes of protecting various third parties against nonperformance by PPL and PPL Gas Utilities. As of December 31, 2003, the aggregate maximum exposure related to these standby letters of credit was \$13 million. These letters of credit expire in 2004.

*(PPL and PPL Energy Supply)*

PPL Generation has entered into certain partnership arrangements for the sale of coal to third parties. PPL Generation has also executed support agreements, which expire in 2007, for the benefit of these third-party purchasers pursuant to which it guarantees the partnerships' obligations in an amount up to its pro rata ownership interest in the partnerships. PPL Generation's maximum aggregate exposure under these support arrangements was approximately \$9 million as of December 31, 2003.

PPL Susquehanna is contingently obligated to pay \$40 million related to potential retroactive premiums that could be assessed under its nuclear insurance programs. Additionally, under the Price Anderson Amendments Act of 1988, PPL Susquehanna could be assessed up to \$201 million for each incident at any of the nuclear reactors covered by this Act. See "Nuclear Insurance" for additional information.

PPL EnergyPlus enters into written put option contracts under which, in exchange for a premium received, it agrees to purchase a specified quantity of a commodity for a specified price if the counterparty exercises the option. The aggregate carrying value of such contracts that were outstanding as of December 31, 2003 was insignificant. These option contracts expire from June 2004 through August 2004. The aggregate maximum amount of payments that PPL EnergyPlus could be required to make if the options are exercised by the counterparties under these contracts is \$3 million.

Certain acquisition agreements relating to the acquisition of mechanical contractors contain provisions that require a PPL Energy Supply subsidiary to make contingent payments to the former owners based upon the profitability of the business unit. The maximum amount of potential payments is not explicitly stated in the acquisition agreements. These arrangements expire at the end of 2004. Based on current expectations, PPL Energy Supply estimates that any amounts to be paid under these arrangements for future performance of the business units will be insignificant.

Certain agreements relating to the purchase of ownership interests in synfuel projects contain provisions that require certain PPL Energy Supply subsidiaries to make contingent purchase price payments to the former owners. These payments

are non-recourse to PPL, PPL Energy Supply and their other subsidiaries and are based primarily upon production levels of the synfuel projects. The maximum amounts of potential payments are not explicitly stated in the agreements. These arrangements expire in 2007. Based on current expectations, PPL Energy Supply estimates that the subsidiaries could pay up to an aggregate of approximately \$60 million under these arrangements. As of December 31, 2003, PPL Energy Supply's Balance Sheet reflects a liability of approximately \$4 million related to the contingent purchase price obligations of a subsidiary of PPL Energy Supply.

*(PPL and PPL Electric)*

PPL Electric provides a guarantee in the amount of approximately \$7 million, as of December 31, 2003, related to debt of an unconsolidated entity. The guarantee expires in June 2008.

*(PPL, PPL Energy Supply, PPL Electric and PPL Montana)*

PPL Electric and PPL Montana lease certain equipment under master operating lease agreements. The term for each piece of equipment leased by PPL Electric ranges from one to three years, after which time the lease term may be extended for certain equipment either (i) from month-to-month until terminated or (ii) for up to two additional years. The term for each piece of equipment leased by PPL Montana is one year, after which time the lease term may be extended from month-to-month until terminated. Under these lease arrangements, PPL Electric and PPL Montana provide residual value guarantees to the lessors. PPL Electric and PPL Montana generally could be required to pay a residual value guarantee if the proceeds received from the sale of a piece of equipment, upon termination of the lease, are less than the expected residual value of the equipment. As of December 31, 2003, the maximum aggregate amount of future payments that could be required to be made as a result of these residual value guarantees was approximately \$88 million for PPL Electric and \$4 million for PPL Montana. As of December 31, 2003, the aggregate carrying value of residual value guarantees issued subsequent to December 31, 2002 was \$16 million for PPL Electric and was insignificant for PPL Montana and is included in "Current Liabilities - Other" on the respective Balance Sheets. These guarantees generally expire within one year, unless the lease terms are extended.

PPL, PPL Energy Supply, PPL Electric and PPL Montana and their subsidiaries provide other miscellaneous guarantees through contracts entered into in the normal course of business. These guarantees are primarily in the form of various indemnifications or warranties related to services or equipment, and vary in duration. Except as otherwise noted below, the obligated amounts of these guarantees often are not explicitly stated; therefore, the overall maximum amount of the obligation under such guarantees cannot be reasonably estimated. Historically, PPL, PPL Energy Supply, PPL Electric and PPL Montana and their subsidiaries have not made any significant payments with respect to these types of guarantees. As of December 31, 2003, the aggregate fair value of these

indemnifications related to arrangements entered into subsequent to December 31, 2002 was insignificant. These guarantees include the following:

- The companies' or their subsidiaries' leasing arrangements including those discussed above, contain certain indemnifications in favor of the lessors (e.g., tax and environmental matters).
- In connection with their issuances of securities, the companies and their subsidiaries engage underwriters, purchasers and purchasing agents to whom they provide indemnification for damages incurred by such parties arising from the companies' material misstatements or omissions in the related offering documents. In addition, in connection with these securities offerings and other financing transactions, the companies also engage trustees or custodial, escrow or other agents to act for the benefit of the investors or to provide other agency services. The companies and their subsidiaries typically provide indemnification to these agents for any liability or expenses incurred by them in performing their obligations.
- PPL EnergyPlus is party to numerous energy trading or purchase and sale agreements pursuant to which the parties indemnify each other for any damages arising from events that occur while the indemnifying party has title to the electricity or natural gas. For example, in the case of the party that is delivering the product, such party would be responsible for damages arising from events occurring prior to delivery.
- In connection with their sales of various businesses, WPD and its affiliates have provided the purchasers with indemnifications that are standard for such transactions, including indemnifications for certain pre-existing liability and environmental and tax matters. In addition, in connection with certain of these sales, WPD and its affiliates have agreed to continue their obligations under existing third-party guarantees, either for a set period of time following the transactions or upon the condition that the purchasers make reasonable efforts to terminate the guarantees. They also have guaranteed the payment of up to £19 million, or \$34 million at current exchange rates, under a contract that expires in 2005 assigned as part of one of these sales. Finally, WPD and its affiliates remain secondarily responsible for lease payments under certain leases that they have assigned to third parties.

PPL, on behalf of itself and its subsidiaries, maintains insurance that covers liability assumed under contract for bodily injury and property damage. The coverage requires a \$4 million deductible per occurrence and provides maximum aggregate coverage of approximately \$175 million. This insurance may be applicable to certain obligations under the contractual arrangements discussed above.

## 15. Related Party Transactions

### Affiliate Trusts

(PPL and PPL Energy Supply)

See Note 22 for a discussion of the implementation of FIN 46, "Consolidation of Variable Interest Entities, an Interpretation of ARB No. 51." Adoption of this statement on December 31, 2003 for certain entities required the deconsolidation of wholly-owned trusts that had issued preferred securities. As a result, the subordinated debt securities of PPL Capital Funding, in the case of PPL Capital Funding Trust I, and WPD LLP, in the case of SIUK Capital Trust I, which support the trust preferred securities, are no longer eliminated in consolidation. As of December 31, 2003, \$681 million is reflected as "Long-term Debt with Affiliate Trusts" on PPL's Balance Sheet, and \$89 million is reflected as "Long-term Debt with Affiliate Trust" on the Balance Sheet of PPL Energy Supply.

### PLR Contracts (PPL Energy Supply and PPL Electric)

PPL Electric has power sales agreements with PPL EnergyPlus, effective January 1, 2002, to supply all of PPL Electric's PLR load through 2009. Under these contracts, PPL EnergyPlus will provide electricity at the pre-determined capped prices that PPL Electric is authorized to charge its PLR customers. These purchases totaled \$1.4 billion in 2003 and 2002, including nuclear decommissioning recovery and amortization of an upfront contract payment. These purchases totaled \$1.3 billion in 2001, also including nuclear decommissioning recovery, under the first PLR contract. These purchases are included in the Statement of Income as "Energy purchases from affiliate" by PPL Electric and as revenues from "Wholesale energy marketing to affiliates" by PPL Energy Supply.

Under the PLR contracts, PPL Electric is required to make performance assurance deposits with PPL EnergyPlus when the market price of electricity is less than the contract price by more than its contract collateral threshold. Conversely, PPL EnergyPlus is required to make performance assurance deposits with PPL Electric when the market price of electricity is greater than the contract price by more than its contract collateral threshold. At December 31, 2003, PPL Electric's deposit with PPL Energy Supply was \$2 million, which is included in "Current Assets - Other" for PPL Electric's Balance Sheet and in "Current Liabilities - Other" for PPL Energy Supply. PPL Energy Supply pays interest equal to the three-month LIBOR plus 3% on this deposit, which is included in the Statement of Income as "Interest Expense with Affiliate."

In 2001, PPL Electric made a \$90 million payment to PPL EnergyPlus in connection with the PLR contracts. The upfront payment is being amortized by both parties over the term of the PLR contracts. The unamortized balance of this payment, and other payments under the contract, was \$70 million at December 31, 2003 and \$81 million at December 31, 2002. This balance is reported on the Balance Sheet as "Prepayment on PLR energy

supply from affiliate" by PPL Electric and as "Deferred revenue on PLR energy supply from affiliate" by PPL Energy Supply.

### NUG Purchases (PPL Energy Supply and PPL Electric)

PPL Electric has a reciprocal contract with PPL EnergyPlus to sell electricity purchased under contracts with NUGs. PPL Electric purchases electricity from the NUGs at contractual rates and then sells the electricity at the same price to PPL EnergyPlus. These purchases totaled \$152 million in 2003, \$160 million in 2002 and \$176 million in 2001. These amounts are included in the Statement of Income as revenues from "Wholesale electric to affiliate" by PPL Electric, and as "Energy purchases from affiliates" by PPL Energy Supply.

### Montana Retail Supply (PPL Montana)

PPL Montana had a Memorandum of Understanding (MOU) with PPL EnergyPlus regarding the supply of energy to satisfy PPL EnergyPlus' obligations under its retail contracts. This MOU will remain in effect until terminated by mutual consent of the parties, or upon 90 days written notice of termination given by either party to the other party. Under the MOU, energy sales to PPL EnergyPlus were \$64 million in 2003, \$68 million in 2002 and \$80 million in 2001. These amounts are included in revenues from "Wholesale energy marketing to affiliate" on the Statement of Income.

### Brokering and Contract Management Agreement (PPL Montana)

Under a brokering and contract management agreement between PPL Montana and PPL EnergyPlus, PPL Montana paid PPL EnergyPlus \$4 million in 2003, \$7 million in 2002 and \$5 million in 2001. PPL Montana records this expense as "Other operation and maintenance" on the Statement of Income.

### Allocations of Corporate Service Costs (PPL Energy Supply, PPL Electric and PPL Montana)

PPL Services provides corporate functions such as financial, legal, human resources and information services. PPL Services bills the respective PPL subsidiaries for the cost of such services when they can be specifically identified. The cost of these services that is not directly charged to PPL subsidiaries is allocated to certain of the subsidiaries using a three-factor method based on an average of the subsidiaries' relative invested capital, operation and maintenance expenses, and number of employees. PPL Services allocated the following charges to PPL Energy Supply, PPL Electric and PPL Montana:

	2003	2002	2001
<b>Direct expenses</b>			
PPL Energy Supply	\$ 94	\$ 88	\$ 80
PPL Electric	60	56	68
PPL Montana	9	12	7
<b>Overhead costs</b>			
PPL Energy Supply	63	38	39
PPL Electric	27	28	28
PPL Montana	6	4	3

## Intercompany Borrowings

### *(PPL Energy Supply)*

PPL Energy Supply, primarily through its financing subsidiary, PPL Investment Corporation, had notes receivable from affiliates of PPL totaling \$2 million at December 31, 2003, and \$655 million at December 31, 2002. Interest earned on loans to affiliates, included in "Other Income - net" on the Statement of Income, was \$16 million, \$22 million and \$57 million in 2003, 2002 and 2001.

### *(PPL Electric)*

In 2001, PPL Electric made a \$150 million demand loan, requiring monthly interest payments at an annual interest rate of 4.0%, from excess cash to PPL Energy Funding. The loan was terminated on November 30, 2003. Intercompany interest income, included in "Other Income - net" on the Statement of Income, was \$3 million, \$9 million and \$5 million in 2003, 2002 and 2001.

### *(PPL Montana)*

In 2002, PPL Montana entered into a \$100 million three-year credit facility with PPL Investment Corporation on market terms to meet its liquidity needs. At December 31, 2003, there was no outstanding balance. At December 31, 2002 there was a \$26 million outstanding balance, which is shown as "Revolving line of credit with affiliate" on the Balance Sheet.

### **Trademark Royalties** *(PPL Energy Supply)*

In the fourth quarter of 2002, a PPL subsidiary that owns PPL trademarks began billing certain affiliates which use these trademarks. PPL Energy Supply was allocated \$39 million of this license fee in 2003 and \$8 million in 2002, which is primarily included in "Other Operation and Maintenance" on the Statement of Income.

### **Other** *(PPL Energy Supply and PPL Electric)*

PPL Energy Supply owns no domestic transmission or distribution facilities, other than facilities to interconnect its generation with the electric transmission system. Therefore, PPL EnergyPlus and other PPL Generation subsidiaries must pay PJM, the operator of the transmission system, to deliver the energy these subsidiaries supply to retail and wholesale customers in PPL Electric's franchised territory in eastern and central Pennsylvania.

## 16. Other Income - Net

### *(PPL)*

The breakdown of PPL's "Other Income - net" was as follows:

	2003	2002	2001
<b>Other Income</b>			
Interest income	\$ 12	\$ 28	\$ 1
Equity earnings (loss)		2	
Realized earnings on nuclear decommissioning trust	20		
Gain by WPD on the disposition of property	3	6	
Hyder-related activity	8		
Rental income	4		
Reduction of reserves for receivables from Enron	10		
Legal claim settlements	3		
Miscellaneous – domestic	11	7	1
Miscellaneous – international	10	5	12
<b>Total</b>	<b>81</b>	<b>48</b>	<b>30</b>
<b>Other Deductions</b>			
Asset valuation write-down	3	1	
Non-operating taxes other than income	1	3	5
Miscellaneous – domestic	7	10	15
Miscellaneous – international	10	4	
<b>Other Income - net</b>	<b>\$ 60</b>	<b>\$ 30</b>	<b>\$ 16</b>

### *(PPL Energy Supply)*

The breakdown of PPL Energy Supply's "Other Income - net" was as follows:

	2003	2002	2001
<b>Other Income</b>			
Affiliated interest income	\$ 16	\$ 22	\$ 57
Interest income	8	17	6
Reduction of reserves for receivables from Enron	10		
Gain by WPD on the disposition of property	3	6	
Legal claim settlements	3		
Realized earnings on nuclear decommissioning trust	20		
Rental income	4		
Equity earnings	4	3	3
Hyder-related activity	8		
Miscellaneous – domestic	2	2	6
Miscellaneous – international	10	5	12
<b>Total</b>	<b>88</b>	<b>55</b>	<b>84</b>
<b>Other Deductions</b>			
Asset valuation write-down	3	1	
Non-operating taxes other than income	1	2	2
Miscellaneous – domestic	1	4	9
Miscellaneous – international	10	4	
<b>Other Income - net</b>	<b>\$ 73</b>	<b>\$ 44</b>	<b>\$ 73</b>

*(PPL Electric)*

The breakdown of PPL Electric's "Other Income - net" was as follows:

	2003	2002	2001
<b>Other Income</b>			
Affiliated interest income	\$ 3	\$ 9	\$ 5
Interest income	4	8	7
Non-operating income - affiliates			5
Miscellaneous		1	1
Total	7	18	18
<b>Other Deductions</b>			
Miscellaneous	1	2	2
<b>Other Income - net</b>	<u>\$ 6</u>	<u>\$ 16</u>	<u>\$ 16</u>

*(PPL Montana)*

"Other Income - net" was \$9 million for the year ended 2003, primarily due to a \$6 million reduction of the reserve provided against the Enron receivables. See Note 17 for additional information.

## 17. Derivative Instruments and Hedging Activities

*(PPL, PPL Energy Supply and PPL Montana)*

PPL, PPL Energy Supply and PPL Montana adopted SFAS 133, "Accounting for Derivative Instruments and Hedging Activities," on January 1, 2001. Upon adoption and in accordance with the transition provisions of SFAS 133, PPL Energy Supply recorded a cumulative-effect credit of \$11 million in earnings, included as an increase to "Wholesale energy marketing" revenues and a decrease to "Energy purchases" on the Statement of Income. PPL Energy Supply and PPL Montana also recorded cumulative-effect charges of \$182 million and \$156 million, respectively, in "Accumulated other comprehensive loss," a component of Member's Equity.

In April 2003, the FASB issued SFAS 149, "Amendment of Statement 133 on Derivative Instruments and Hedging Activities," which amends and clarifies SFAS 133 to improve financial accounting and reporting for derivative instruments and hedging activities. To ensure that contracts with comparable characteristics are accounted for similarly, SFAS 149 clarifies the circumstances under which a contract with an initial net investment meets the characteristics of a derivative, clarifies when a derivative contains a financing component, amends the definition of an "underlying" and amends certain other existing pronouncements. Additionally, SFAS 149 placed additional limitations on the use of the normal purchase or normal sale exception. SFAS 149 was effective for contracts entered into or modified and for hedging relationships designated after June 30, 2003, except certain provisions relating to forward purchases or sales of when-issued securities or other securities that did not yet exist. PPL adopted SFAS 149 as of July 1, 2003. The adoption of SFAS 149 did not have a

significant impact on PPL, PPL Energy Supply or PPL Montana.

## Management of Market Risk Exposures

Market risk is the potential loss PPL may incur as a result of price changes associated with a particular financial or commodity instrument. PPL is exposed to market risk from:

- commodity price risk for energy and energy-related products associated with the sale of electricity from its generating assets and other electricity marketing activities, the purchase of fuel for the generating assets and energy trading activities;
- interest rate risk associated with variable-rate debt and the fair value of fixed-rate debt used to finance operations, as well as the fair value of debt securities invested in by PPL's nuclear decommissioning fund;
- foreign currency exchange rate risk associated with investments in affiliates in Latin America and Europe, as well as purchases of equipment in currencies other than U.S. dollars; and
- equity securities price risk associated with the fair value of equity securities invested in by PPL's nuclear decommissioning fund.

PPL has a risk management policy approved by the Board of Directors to manage market risk and counterparty credit risk. The RMC, comprised of senior management and chaired by the Vice President-Risk Management, oversees the risk management function. Key risk control activities designed to ensure compliance with risk policies and detailed programs include, but are not limited to, credit review and approval, validation of transactions and market prices, verification of risk and transaction limits, sensitivity analyses, and daily portfolio reporting, including open positions, mark-to-market valuations, and other risk measurement metrics. In addition, efforts are ongoing to develop systems to improve the timeliness, quality and breadth of market and credit risk information.

PPL utilizes forward contracts, futures contracts, options and swaps as part of its risk management strategy to minimize unanticipated fluctuations in earnings caused by commodity price, interest rate and foreign currency volatility. All derivatives are recognized on the balance sheet at their fair value, unless they meet SFAS 133 criteria for exclusion (see discussion in "Related Implementation Issues" below).

## Fair Value Hedges

PPL Energy Supply and PPL Montana enter into financial or physical contracts to hedge a portion of the fair value of firm commitments of forward electricity sales. These contracts range in maturity through 2006. Additionally, PPL and PPL Energy Supply enter into financial contracts to hedge fluctuations in market value of existing debt issuances. These contracts range in maturity through 2029.

PPL, PPL Energy Supply and PPL Montana recognized the following net gains/(losses), after-tax, resulting from hedges of firm commitments that no longer qualified as fair value hedges

(reported in "Wholesale energy marketing" revenues and "Energy purchases" on the Statement of Income):

	<u>2003</u>	<u>2002</u>	<u>2001</u>
PPL	\$ 1		\$ 7
PPL Energy Supply	1		7
PPL Montana	(1)		

PPL, PPL Energy Supply and PPL Montana did not recognize any gains/(losses) resulting from the ineffective portion of fair value hedges for the twelve months ended December 31, 2003, 2002 or 2001.

### Cash Flow Hedges

PPL Energy Supply and PPL Montana enter into financial and physical contracts, including forwards, futures and swaps, to hedge the price risk associated with electric, gas and oil commodities. These contracts range in maturity through 2010. Additionally, PPL and PPL Energy Supply enter into financial interest rate swap contracts to hedge interest expense associated with both existing and anticipated debt issuances. These swaps range in maturity through 2014. PPL and PPL Energy Supply also enter into foreign currency forward contracts to hedge exchange rates associated with firm commitments denominated in foreign currencies and to hedge the net investment of foreign operations. These forward contracts range in maturity through 2028.

Cash flow hedges may be discontinued because it is probable that the original forecasted transaction will not occur by the end of the originally specified time period. PPL, PPL Energy Supply and PPL Montana discontinued certain cash flow hedges which resulted in the following net gain/(loss), after tax, reclassifications from other comprehensive income (reported in "Wholesale energy marketing" revenues, "Energy purchases" and "Interest Expense" on the Statement of Income):

	<u>2003</u>	<u>2002</u>	<u>2001</u>
PPL	\$ (7)	\$ (9)	\$ (14)
PPL Energy Supply	(7)		(14)
PPL Montana			7

Due to hedge ineffectiveness, PPL, PPL Energy Supply and PPL Montana reclassified the following net gains/(losses), after tax, from other comprehensive income (reported in "Wholesale energy marketing" revenues and "Energy purchases" on the Statement of Income):

	<u>2003</u>	<u>2002</u>	<u>2001</u>
PPL		\$ (2)	
PPL Energy Supply		(2)	
PPL Montana			

As of December 31, 2003, the deferred net gain/(loss), after tax, on derivative instruments in "Accumulated other comprehensive income" expected to be reclassified into earnings during the

next twelve months was \$(1) million, \$5 million and \$5 million for PPL, PPL Energy Supply and PPL Montana.

The following table shows the change in accumulated unrealized gains or losses on derivatives in other comprehensive income for the following periods:

	<u>2003</u>	<u>2002</u>
<b>PPL</b>		
Beginning accumulated derivative gain	\$ 7	\$ 2
Net change associated with current period hedging activities and other	129	1
Net change associated with net investment hedges	(2)	(1)
Net change from reclassification into earnings	(98)	(2)
Ending accumulated derivative gain	<u>\$ 36</u>	<u>\$ 2</u>

<b>PPL Energy Supply</b>		
Beginning accumulated derivative gain	\$ 23	\$ 4
Net change associated with current period hedging activities and other	131	(1)
Net change associated with net investment hedges	(2)	(1)
Net change from reclassification into earnings	(96)	(1)
Ending accumulated derivative gain	<u>\$ 56</u>	<u>\$ 2</u>

<b>PPL Montana</b>		
Beginning accumulated derivative gain	\$ 4	\$ 3
Net change associated with current period hedging activities and other	8	(2)
Net change from reclassification into earnings	(1)	(1)
Ending accumulated derivative gain	<u>\$ 11</u>	<u>\$ 3</u>

### Related Implementation Issues

For energy contracts that meet the definition of a derivative, the circumstances and intent existing at the time that energy transactions are entered into determine their accounting designation. The following summarizes the electricity guidelines that have been provided to the traders who are responsible for contract designation for derivative energy contracts in accordance with SFAS 149:

- Any wholesale and retail contracts to sell electricity and the related capacity that are expected to be delivered from PPL's generation or that are approved by the RMC as being a strategic element of PPL's overall marketing strategy are considered "normal." These transactions are not recorded in the financial statements and have no earnings impact until delivery.
- Physical electricity-only transactions can receive cash flow hedge treatment if all of the qualifications under SFAS 133 are met. Any unrealized gains or losses on transactions receiving cash flow hedge treatment are recorded in other comprehensive income.
- Physical electricity purchases that increase PPL's long position and any energy sale or purchase judged a "market call" are considered speculative, with unrealized gains or

losses recorded immediately through earnings.

- Financial transactions, which can be settled in cash, cannot be considered "normal" because they do not require physical delivery. These transactions receive cash flow hedge treatment if they lock in the price PPL will receive or pay for energy expected to be generated or purchased in the spot market. Any unrealized gains or losses on transactions that receive cash flow hedge treatment are recorded in other comprehensive income.

Transactions that do not qualify for hedge accounting treatment are marked to market through earnings.

In June 2001, the FASB issued definitive guidance on DIG Issue C15, "Scope Exceptions: Normal Purchases and Normal Sales Exception for Certain Option-Type Contracts and Forward Contracts in Electricity." DIG Issue C15 provides additional guidance on the classification and application of derivative accounting rules relating to purchases and sales of electricity utilizing forward and option contracts. This guidance became effective as of July 1, 2001. In December 2001, the FASB revised the guidance in DIG Issue C15, principally related to the eligibility of options for the normal purchases and normal sales exception. The revised guidance was effective April 1, 2002. In November 2003, the FASB again revised the guidance in DIG Issue C15 to clarify the application of derivative accounting rules for contracts that may involve capacity. The guidance is effective January 1, 2004 for PPL. PPL does not expect this guidance to have a significant impact on its financial statements.

In June 2003, the FASB issued DIG Issue C20, "Scope Exceptions: Interpretation of the Meaning of Not Clearly and Closely Related in Paragraph 10(b) Regarding Contracts with a Price Adjustment Feature," which became effective October 1, 2003. DIG Issue C20 addresses a requirement in SFAS 133 that contracts that qualify for normal treatment must feature pricing that is clearly and closely related to the asset being sold. Diversity in practice had developed among companies. DIG Issue C20 permits normal treatment if a price adjustment factor, such as a broad market index (e.g., Consumer Price Index), is not extraneous to both the cost and the fair value of the asset being sold and is not significantly disproportionate in terms of the magnitude and direction when compared with the asset being sold. However, DIG Issue C20 also stated that prior guidance did not permit the use of a broad market index to serve as a proxy for an ingredient or direct factor. Thus, DIG Issue C20 required that contracts that had been accounted for as normal but were not eligible for normal treatment under prior guidance be reflected on the balance sheet at their fair value, with an offsetting amount reflected in income as of the date of adoption. These contracts could then be evaluated under the provisions of DIG Issue C20 to determine whether they could qualify for normal treatment prospectively. PPL, PPL Energy Supply and PPL Montana recorded a pre-tax charge to income of \$2 million in the fourth quarter of 2003 to comply with the provisions of DIG Issue C20.

In December 2001, the FASB revised guidance on DIG Issue C16, "Scope Exceptions: Applying the Normal Purchases and Normal Sales Exception to Contracts that Combine a Forward Contract and a Purchased Option Contract." DIG Issue C16 provides additional guidance on the classification and application of SFAS 133, "Accounting for Derivative Instruments and Hedging Activities," relating to purchases and sales of electricity utilizing forward contracts and options, as well as the eligibility of fuel contracts for the normal purchases and normal sales exception. The revised guidance was effective April 1, 2002. PPL had no financial statement impact from the revised guidance on fuel contracts classified as normal.

PPL adopted the final provisions of EITF 02-3, "Issues Involved in Accounting for Derivative Contracts Held for Trading Purposes and Contracts Involved in Energy Trading and Risk Management Activities," during the fourth quarter of 2002. As such, PPL reflects its net realized and unrealized gains and losses associated with all derivatives that are held for trading purposes in the "Net energy trading margins" line on the Statement of Income. Non-derivative contracts that met the definition of energy trading activities as defined by EITF 98-10, "Accounting for Energy Trading and Risk Management Activities" are reflected in the financial statements using the accrual method of accounting. Under the accrual method of accounting, unrealized gains and losses are not reflected in the financial statements. Prior periods were reclassified. No cumulative effect adjustment was required upon adoption.

PPL Energy Supply and PPL Montana have adopted the final provisions of EITF 03-11, "Reporting Realized Gains and Losses on Derivative Instruments That Are Subject to FASB Statement No. 133 and Not 'Held for Trading Purposes' as Defined in Issue No. 02-3," prospectively as of October 1, 2003. As a result of this adoption, non-trading bilateral sales of electricity at major market delivery points are netted with purchases that offset the sales at those same delivery points. A major market delivery point is any delivery point with liquid pricing available. The impact of adopting EITF 03-11 was a reduction in both "Wholesale energy marketing" revenues and "Energy purchases" by \$105 million in PPL's and PPL Energy Supply's Statement of Income and by \$18 million in PPL Montana's Statement of Income.

### **Credit Concentration**

PPL, PPL Energy Supply and PPL Montana enter into contracts with many entities for the purchase and sale of energy. Most of these contracts are considered a normal part of doing business and, as such, the mark-to-market value of these contracts is not reflected in the financial statements. However, the mark-to-market value of these contracts is considered when committing to new business from a credit perspective.

PPL, PPL Energy Supply and PPL Montana have credit exposures to energy trading partners. The majority of these exposures were the mark-to-market value of multi-year contracts for energy sales. Therefore, if these counterparties fail to perform their obligations under such contracts, the companies

would not experience an immediate financial loss, but would experience lower revenues in future years to the extent that replacement sales could not be made at the same prices as sales under the defaulted contracts.

At December 31, 2003, PPL had a credit exposure of \$234 million to energy trading partners. Eight counterparties accounted for 51% of this exposure. No other individual counterparty accounted for more than 4% of the exposure. With one exception, each of the eight primary counterparties had an investment grade credit rating from Standard & Poor's Ratings Services (S&P). The non-investment grade counterparty, NorthWestern, has filed for Chapter 11 bankruptcy protection. NorthWestern has assumed the power supply agreements in its bankruptcy proceeding. NorthWestern has remained current on all post-bankruptcy obligations with PPL Montana. Payment on all pre-bankruptcy obligations was received in October 2003. See Note 14 under "Wholesale Energy Commitments" for additional information regarding the NorthWestern bankruptcy proceeding.

At December 31, 2003, PPL Energy Supply had a credit exposure of \$508 million to energy trading partners. Nine counterparties accounted for 77% of this exposure. No other individual counterparty accounted for more than 2% of the exposure. The largest exposure, \$274 million, was to PPL Electric, under the long-term contract to supply PPL Electric's PLR load. With one exception, the other eight counterparties have an investment grade credit rating from S&P. The non-investment grade counterparty, NorthWestern, has filed for Chapter 11 bankruptcy protection, as discussed above.

At December 31, 2003, PPL Montana had a credit exposure of \$75 million to energy trading partners. Four counterparties accounted for 79% of this exposure. No other individual counterparty accounted for more than 3% of the exposure. Three of the four counterparties have an investment grade credit rating from S&P. The non-investment grade counterparty, NorthWestern, has filed for Chapter 11 bankruptcy protection, as discussed above.

PPL, PPL Energy Supply and PPL Montana have the right to request collateral from each of these counterparties, except for one government agency, in the event their credit ratings fall below investment grade or, in one case, below current levels. PPL Montana and NorthWestern have mutually agreed not to request collateral from each other while NorthWestern's Chapter 11 bankruptcy proceeding is pending. It is also the policy of PPL, PPL Energy Supply and PPL Montana to enter into netting agreements with all of their counterparties to minimize credit exposure.

### **Enron Bankruptcy**

In connection with the December 2001 bankruptcy filings by Enron Corporation and its affiliates (collectively "Enron"), PPL EnergyPlus and PPL Montana terminated certain electricity, gas and other trading agreements with Enron. PPL EnergyPlus' 2001 after-tax earnings exposure associated with termination of

these contracts was approximately \$8 million, which was recorded in "Wholesale energy marketing" and "Energy purchases" in the Statement of Income. PPL Montana had no 2001 earnings effect associated with the termination of these contracts. Additionally, at the time that these trading agreements were terminated, they were at prices more favorable to PPL EnergyPlus and PPL Montana than current market prices, and PPL established a reserve for uncollectible accounts in the aggregate amount of \$50 million. In October 2002, PPL EnergyPlus and PPL Montana filed proofs of claim in Enron's bankruptcy proceedings for approximately \$21 million and \$5 million, respectively. These claims were against Enron North America and Enron Power Marketing (the "Enron Subsidiaries"), and against Enron Corporation, which had guaranteed the Enron Subsidiaries' performance (the "Enron Corporation Guarantees").

During 2003, PPL EnergyPlus, PPL Montana and Enron engaged in discussions regarding the amount of claims that would be allowed against the Enron Subsidiaries. Although no formal agreement on such amounts has been reached, based on informal discussions with Enron's counsel, PPL EnergyPlus and PPL Montana believe that their claims against the Enron Subsidiaries will eventually be allowed in the bankruptcy at approximately \$21 million and \$25 million, respectively. Accordingly, PPL reduced its receivables from Enron, and the associated reserve for uncollectible accounts, by \$4 million. PPL also determined that it is probable that PPL EnergyPlus and PPL Montana will recover approximately \$4 million and \$6 million, respectively, of these receivables from the Enron Subsidiaries, and may collect additional amounts under the Enron Corporation Guarantees. Therefore, PPL determined it was appropriate to reduce its reserve by an additional \$10 million.

In November 2003, Enron Corporation filed suits against each of PPL EnergyPlus and PPL Montana, asserting that the Enron Corporation Guarantees should be avoided as fraudulent transfers. If Enron Corporation were successful in these suits, PPL EnergyPlus' and PPL Montana's claims against Enron Corporation under the Enron Corporation Guarantees would be allowed in the bankruptcy proceeding.

### **18. Goodwill and Other Intangible Assets**

On January 1, 2002, PPL and its subsidiaries adopted SFAS 142, "Goodwill and Other Intangible Assets," which eliminated the amortization of goodwill and other acquired intangible assets with indefinite economic useful lives. SFAS 142 requires an annual impairment test of goodwill at the reporting unit level which compares the carrying value of the reporting unit to its fair value. A reporting unit is a segment or one level below a segment. Intangible assets other than goodwill that are not subject to amortization are also required to undergo an annual impairment test. PPL changed the classification of certain intangible assets on the balance sheet upon adopting SFAS 142. Previously reported information has been restated to conform to the current presentation. The following information is disclosed in accordance with SFAS 142.

## Acquired Intangible Assets

(PPL)

The carrying amount and the accumulated amortization of acquired intangible assets were as follows:

	December 31, 2003		December 31, 2002	
	Carrying Amount	Accumulated Amortization	Carrying Amount	Accumulated Amortization
Land and transmission rights	\$ 256	\$ 94	\$ 245	\$ 90
Emission allowances	49		41	
Licenses and other	51	4	37	3
	<u>\$ 356</u>	<u>\$ 98</u>	<u>\$ 323</u>	<u>\$ 93</u>

Current intangible assets are included in "Current Assets - Other," and long-term intangible assets are included in "Other intangibles" on the Balance Sheet.

Amortization expense was approximately \$6 million for 2003 and 2002. Amortization expense is estimated at \$6 million per year for 2004 through 2008.

(PPL Energy Supply)

The carrying amount and the accumulated amortization of acquired intangible assets were as follows:

	December 31, 2003		December 31, 2002	
	Carrying Amount	Accumulated Amortization	Carrying Amount	Accumulated Amortization
Land and transmission rights	\$ 45	\$ 15	\$ 49	\$ 14
Emission allowances	49		41	
Licenses and other	50	4	36	3
	<u>\$ 144</u>	<u>\$ 19</u>	<u>\$ 126</u>	<u>\$ 17</u>

Current intangible assets are included in "Current Assets - Other," and long-term intangible assets are included in "Other intangibles" on the Balance Sheet.

Amortization expense was approximately \$2 million for 2003 and 2002. Amortization expense is estimated at \$3 million per year for 2004 through 2008.

(PPL Electric)

The carrying amount and the accumulated amortization of acquired intangible assets were as follows:

	December 31, 2003		December 31, 2002	
	Carrying Amount	Accumulated Amortization	Carrying Amount	Accumulated Amortization
Land and transmission rights	\$ 193	\$ 77	\$ 192	\$ 74

Intangible assets are shown as "Intangibles" on the Balance Sheet.

Amortization expense was approximately \$2 million for 2003 and 2002. Amortization expense is estimated at \$2 million per year for 2004 through 2008.

(PPL Montana)

The carrying amount and the accumulated amortization of acquired intangible assets were as follows:

	December 31, 2003		December 31, 2002	
	Carrying Amount	Accumulated Amortization	Carrying Amount	Accumulated Amortization
Emission allowances	\$ 18		\$ 18	
Licenses and other	27	\$ 1	22	\$ 1
	<u>\$ 45</u>	<u>\$ 1</u>	<u>\$ 40</u>	<u>\$ 1</u>

Current intangible assets are included in "Prepayments and other," and long-term intangible assets are included in "Intangibles" on the Balance Sheet.

Amortization expense was approximately \$1 million for 2003 and 2002. Amortization expense is estimated at \$1 million per year for 2004 through 2008.

**Goodwill (PPL and PPL Energy Supply)**

The changes in the carrying amounts of goodwill by segment were as follows:

	PPL Energy Supply			Delivery(a)	PPL	
	Supply	International	Total		Total	
Balance as of January 1, 2002	\$ 72	\$ 257	\$ 329	\$ 55	\$ 384	
Goodwill acquired	13	6	19		19	
Interest in WPD goodwill (b)		225	225		225	
Effect of foreign currency exchange rates		(4)	(4)		(4)	
Impairment losses		(150)	(150)		(150)	
Balance as of December 31, 2002	\$ 85	\$ 334	\$ 419	\$ 55	\$ 474	
Effect of foreign currency exchange rates		92	92		92	
Purchase accounting adjustments (b)	8	500	508		508	
Discontinued operations		(6)	(6)		(6)	
Balance as of December 31, 2003	\$ 93	\$ 920	\$ 1,013	\$ 55	\$ 1,068	

(a) The Delivery segment is not part of PPL Energy Supply.

(b) See Note 9 for additional information.

Goodwill is included in "Goodwill" on the Balance Sheet.

The reporting units of the Supply, Delivery and International segments completed the transition impairment test in the first quarter of 2002. A transition goodwill impairment loss of \$150 million was recognized in the Latin American reporting unit within the International segment, and is reported as a "Cumulative Effects of Changes in Accounting Principles" on the Statement of Income. The fair value of the reporting unit was estimated using the expected present value of future cash flows.

In December 2003, the PPL Global Board of Managers authorized the sale of its investment in a Latin American telecommunications company. As a result of this decision, PPL Global wrote off \$6 million of goodwill.

### Reconciliation of Prior Periods to Exclude Amortization

*(PPL and PPL Energy Supply)*

The following table reconciles reported earnings for 2001 to earnings adjusted to exclude amortization expense related to goodwill and equity method goodwill. Those expenses were no longer recorded in 2002 or 2003 in accordance with SFAS 142. PPL and PPL Energy Supply were not affected by changes in amortization periods for other intangible assets.

	2003	2002	2001
<b>PPL</b>			
Income from continuing operations	\$ 719	\$ 360	\$ 169
Goodwill amortization			
Equity method goodwill amortization			
Pro forma income from continuing operations	\$ 719	\$ 360	\$ 185
Reported net income	\$ 734	\$ 208	\$ 179
Goodwill amortization			13
Equity method goodwill amortization			3
Adjusted net income	\$ 734	\$ 208	\$ 195
<b>Basic EPS:</b>			
Income from continuing operations	\$ 4.16	\$ 2.36	\$ 1.16
Goodwill amortization			0.09
Equity method goodwill amortization			0.02
Pro forma income from continuing operations	\$ 4.16	\$ 2.36	\$ 1.27
Reported net income	\$ 4.25	\$ 1.37	\$ 1.23
Goodwill amortization			0.09
Equity method goodwill amortization			0.02
Adjusted net income	\$ 4.25	\$ 1.37	\$ 1.34
<b>Diluted EPS:</b>			
Income from continuing operations	\$ 4.15	\$ 2.36	\$ 1.15
Goodwill amortization			0.09
Equity method goodwill amortization			0.02
Pro forma income from continuing operations	\$ 4.15	\$ 2.36	\$ 1.26
Reported net income	\$ 4.24	\$ 1.36	\$ 1.22
Goodwill amortization			0.09
Equity method goodwill amortization			0.02
Adjusted net income	\$ 4.24	\$ 1.36	\$ 1.33
<b>PPL Energy Supply</b>			
Income from continuing operations	\$ 712	\$ 431	\$ 171
Goodwill amortization			12
Equity method goodwill amortization			3
Pro forma income from continuing operations	\$ 712	\$ 431	\$ 186
Reported net income	\$ 727	\$ 279	\$ 174
Goodwill amortization			12
Equity method goodwill amortization			3
Adjusted net income	\$ 727	\$ 279	\$ 189

*(PPL Electric and PPL Montana)*

PPL Electric and PPL Montana had no goodwill at December 31, 2003, 2002 and 2001. The adoption of SFAS 142 would not have affected prior period earnings of PPL Electric and PPL Montana.

## 19. Strategic Initiative

*(PPL, PPL Energy Supply and PPL Electric)*

In August 2001, PPL completed a strategic initiative to confirm the structural separation of PPL Electric from PPL and PPL's other affiliated companies. This initiative enabled PPL Electric to reduce business risk by securing a supply contract adequate to meet its PLR obligations, enabled PPL Electric to lower its capital costs, enabled PPL EnergyPlus to lock in an electric supply agreement at current favorable prices, and enabled PPL to raise capital at attractive rates for its unregulated businesses, while allowing PPL to retain valuable advantages related to operating both energy supply and energy delivery businesses.

In connection with this initiative, PPL Electric:

- obtained a long-term electric supply contract to meet its PLR obligations, at prices generally equal to the pre-determined "capped" rates it is authorized to charge its PLR customers from 2002 through 2009 under the 1998 PUC settlement order;
- agreed to limit its businesses to electric transmission and distribution and activities relating to or arising out of those businesses;
- adopted amendments to its Articles of Incorporation and Bylaws containing corporate governance and operating provisions designed to reinforce its corporate separateness from affiliated companies;
- appointed an independent director to its Board of Directors and required the unanimous consent of the Board of Directors, including the consent of the independent director, to amendments to these corporate governance and operating provisions or to the commencement of any insolvency proceeding, including any filing of a voluntary petition in bankruptcy or other similar actions;
- appointed an independent compliance administrator to review, on a semi-annual basis, its compliance with the new corporate governance and operating requirements contained in its amended Articles of Incorporation and Bylaws; and
- adopted a plan of division pursuant to the Pennsylvania Business Corporation Law. The plan of division resulted in two separate corporations. PPL Electric was the surviving corporation and a new Pennsylvania corporation was created. Under the plan of division, \$5 million of cash and certain of PPL Electric's potential liabilities were allocated to the new corporation. PPL has guaranteed the obligations of the new corporation with respect to such liabilities.

The enhancements to PPL Electric's legal separation from its affiliates are intended to minimize the risk that a court would order PPL Electric's assets and liabilities to be substantively consolidated with those of PPL or another affiliate of PPL in the event that PPL or another PPL affiliate were to become a debtor in a bankruptcy case.

At a special meeting of PPL Electric's shareowners held on July 17, 2001, the plan of division and the amendments to PPL

Electric's Articles of Incorporation and Bylaws were approved, and became effective upon filing the articles of division and the plan of division with the Secretary of State of the Commonwealth of Pennsylvania. This filing was made in August 2001.

As part of the strategic initiative, PPL Electric solicited bids to contract with energy suppliers to meet its obligation to deliver energy to its customers from 2002 through 2009. In June 2001, PPL Electric announced that PPL EnergyPlus was the low bidder, among six bids examined, and was selected to provide the energy supply requirements of PPL Electric from 2002 through 2009. Under this contract, PPL EnergyPlus will provide electricity at pre-determined capped prices that PPL Electric is authorized to charge its PLR customers, and received a \$90 million payment to offset differences between the revenues expected under the capped prices and projected market prices through the life of the supply agreement (as projected by PPL EnergyPlus at the time of its bid). The contract resulted in PPL EnergyPlus having an eight-year contract at current market prices. PPL has guaranteed the obligations of PPL EnergyPlus under the new contract.

In July 2001, the energy supply contract was approved by the PUC and accepted for filing by the FERC.

Also in July 2001, PPL Electric filed a shelf registration statement with the SEC to issue up to \$900 million in debt. In August 2001, PPL Electric sold \$800 million of senior secured bonds under this registration statement. The offering consisted of two series of bonds: \$300 million of 5-7/8% Series due 2007 and \$500 million of 6-1/4% Series due 2009. PPL Electric used a portion of the proceeds from these debt issuances to make the \$90 million up-front payment to PPL EnergyPlus, and \$280 million was used to repurchase a portion of its common stock from PPL. The remainder of the proceeds was used for general corporate purposes.

Taken collectively, the steps in the strategic initiative were intended to protect the customers of PPL Electric from volatile energy prices and lower its cost of capital. PPL's shareowners also benefited from this initiative because it provided low-cost capital to the higher-growth, unregulated side of PPL's business.

## 20. Workforce Reduction

*(PPL, PPL Energy Supply, PPL Electric and PPL Montana)*

In an effort to improve operational efficiency and reduce costs, PPL and its subsidiaries commenced a workforce reduction assessment in June 2002 that was expected to eliminate up to 598 employees, or about 7% of PPL's U.S. workforce, at an estimated cost of \$74 million. The program was broad-based and impacted all employee groups except certain positions that are key to providing high-quality service to PPL's electricity delivery customers. Linemen, electricians and line foremen, for example, were not affected by the reductions. An additional \$1 million workforce reduction charge was recorded in September 2002, when plans specific to PPL Global and PPL Montana

subsidiaries were finalized which were expected to impact 26 employees. These additional reductions increased PPL's total charge for workforce reductions to \$75 million for the elimination of up to 624 positions.

PPL recorded the charges in the Statement of Income as "Workforce reduction" for the year ended December 31, 2002. These charges reduced net income by \$44 million after taxes. The program provides primarily for enhanced early retirement benefits and/or one-time special pension separation allowances based on an employee's age and years of service. These features of the program will be paid from the PPL Retirement Plan pension trust and increased PPL's pension and postretirement benefit liabilities by \$65 million. The remaining \$10 million of costs related primarily to non-pension benefits, such as severance payments and outplacement costs, which will be paid by PPL.

PPL Energy Supply expected to ultimately eliminate up to 221 employees and recorded charges of \$40 million in June 2002 and \$1 million in September 2002. These charges reduced net income by \$24 million for the year ended December 31, 2002. Included in these charges was a \$10 million allocation of costs associated with the elimination of employees of PPL Services.

PPL Electric expected to ultimately eliminate up to 260 employees and recorded a charge of \$33 million, which reduced net income by \$19 million for the year ended December 31, 2002. Included in the charge was a \$6 million allocation of costs associated with the elimination of employees of PPL Services.

In the third quarter of 2003, PPL Electric recorded an additional \$9 million, or \$5 million after-tax, charge for the completion of the workforce reduction program that commenced in 2002. This additional charge covers the final 94 employees anticipated to be separated as part of the Automated Meter Reader implementation project. The charge was related to pension enhancements, which will be paid from the PPL Retirement Plan pension trust.

PPL Montana expected to ultimately eliminate up to ten employees and recorded an insignificant charge for the year ended December 31, 2002.

As of December 31, 2003, 490 employees of PPL subsidiaries were terminated. Approximately 129 positions, which are primarily bargaining unit, will be evaluated for termination over the next six months, due to the timing of the Automated Meter Reader implementation and the displacement process under the bargaining unit contract. Substantially all of the accrued non-pension benefits have been paid.

## 21. Asset Retirement Obligations

*(PPL, PPL Energy Supply, PPL Electric and PPL Montana)*

In 2001, the FASB issued SFAS 143, "Accounting for Asset Retirement Obligations," which addresses the accounting for

obligations associated with the retirement of tangible long-lived assets. SFAS 143 requires legal obligations associated with the retirement of long-lived assets to be recognized as a liability in the financial statements. The initial obligation should be measured at the estimated fair value. An equivalent amount should be recorded as an increase in the value of the capital asset and allocated to expense over the useful life of the asset. Until the obligation is settled, the liability should be increased through the recognition of accretion expense in the income statement, for changes in the obligation due to the passage of time.

*(PPL and PPL Energy Supply)*

PPL and PPL Energy Supply adopted SFAS 143 effective January 1, 2003. Application of the new rules resulted in an increase in net PP&E of \$32 million, reversal of previously recorded liabilities of \$304 million, recognition of asset retirement obligations of \$229 million, recognition of a deferred tax liability of \$44 million and a cumulative effect of adoption that increased net income by \$63 million or \$0.36 per share. In 2003, as a result of applying SFAS 143, PPL and PPL Energy Supply recognized \$18 million of accretion expense and an insignificant amount of depreciation expense.

PPL and PPL Energy Supply identified various legal obligations to retire long-lived assets, the largest of which relates to the decommissioning of the Susquehanna station. PPL and PPL Energy Supply identified and recorded other asset retirement obligations related to significant interim retirements at the Susquehanna station, and various environmental requirements for coal piles, ash basins and other waste basin retirements.

PPL and PPL Energy Supply also identified legal retirement obligations that were not measurable at this time. These items included the retirement of certain transmission assets and a reservoir. These retirement obligations were not measurable due to indeterminable dates of retirement.

Amounts collected from PPL Electric's customers for decommissioning, less applicable taxes, are deposited in external trust funds for investment and can only be used for future decommissioning costs. The fair value of the nuclear decommissioning trust was \$357 million and \$287 million as of December 31, 2003 and 2002.

PPL's and PPL Energy Supply's asset retirement obligations are included in "Deferred Credits and Other Noncurrent Liabilities - Other" on the Balance Sheet. The changes in the carrying amounts of asset retirement obligations were as follows:

Asset retirement obligation at January 1, 2003	\$ 229
Add: Accretion expense	18
Less: Settlement	<u>5</u>
Asset retirement obligation at December 31, 2003	<u>\$ 242</u>

*(PPL Electric)*

PPL Electric adopted SFAS 143 effective January 1, 2003 and did not record any asset retirement obligations upon adoption.

PPL Electric identified legal retirement obligations for the retirement of certain transmission assets that were not measurable at this time due to indeterminable dates of retirement.

*(PPL Montana)*

PPL Montana adopted SFAS 143 effective January 1, 2003. PPL Montana recorded asset retirement obligations associated with various environmental requirements for coal piles, ash basins and other waste basin retirements. The impact of these asset retirement obligations was insignificant.

**Reconciliation of Prior Annual Periods** *(PPL and PPL Energy Supply)*

The pro forma asset retirement obligation liability balances, calculated as if SFAS 143 had been adopted on January 1, 2001 (rather than January 1, 2003), were \$229 million, \$211 million and \$196 million as of December 31, 2002, December 31, 2001 and January 1, 2001.

The pro forma income statement effects of the application of SFAS 143, calculated as if it had been adopted prior to January 1, 2001 (rather than January 1, 2003) are presented below:

	For the Years Ended December 31,		
	2003	2002	2001
<b>PPL</b>			
Income from continuing operations	\$ 719	\$ 360	\$ 169
Pro forma income from continuing operations	\$ 719	\$ 351	\$ 167
Reported net income	\$ 734	\$ 208	\$ 179
Pro forma net income	\$ 671	\$ 199	\$ 177
<b>Basic EPS:</b>			
Income from continuing operations	\$ 4.16	\$ 2.36	\$ 1.16
Pro forma income from continuing operations	\$ 4.16	\$ 2.30	\$ 1.15
Reported net income	\$ 4.25	\$ 1.37	\$ 1.23
Pro forma net income	\$ 3.89	\$ 1.31	\$ 1.21
<b>Diluted EPS:</b>			
Income from continuing operations	\$ 4.15	\$ 2.36	\$ 1.15
Pro forma income from continuing operations	\$ 4.15	\$ 2.30	\$ 1.14
Reported net income	\$ 4.24	\$ 1.36	\$ 1.22
Pro forma net income	\$ 3.88	\$ 1.31	\$ 1.21
<b>PPL Energy Supply</b>			
Income from continuing operations	\$ 712	\$ 431	\$ 171
Pro forma income from continuing operations	\$ 712	\$ 422	\$ 169
Reported net income	\$ 727	\$ 279	\$ 174
Pro forma net income	\$ 664	\$ 270	\$ 172

## 22. New Accounting Standards

**SFAS 143** *(PPL, PPL Energy Supply, PPL Electric and PPL Montana)*

See Note 21 for a discussion of SFAS 143, "Accounting for Asset Retirement Obligations," and the impact of its adoption.

**SFAS 146** *(PPL, PPL Energy Supply, PPL Electric and PPL Montana)*

In 2002, the FASB issued SFAS 146, "Accounting for Costs Associated with Exit or Disposal Activities." SFAS 146 addresses financial accounting and reporting for costs associated with exit or disposal activities and nullifies EITF Issue No. 94-3, "Liability Recognition for Certain Employee Termination Benefits and Other Costs to Exit an Activity (including Certain Costs Incurred in a Restructuring)." SFAS 146 requires the recognition of a liability for costs associated with exit or disposal activities when the liability is incurred rather than at the date of a commitment to an exit or disposal plan. SFAS 146 also establishes that the initial liability should be measured at its estimated fair value. The provisions of SFAS 146 are effective for exit or disposal activities initiated after December 31, 2002, with earlier application encouraged. PPL and its subsidiaries adopted SFAS 146 effective January 1, 2003. SFAS 146 did not have an impact on PPL or its subsidiaries during 2003.

**SFAS 148** *(PPL, PPL Energy Supply, PPL Electric and PPL Montana)*

In 2002, the FASB issued SFAS 148, "Accounting for Stock-Based Compensation - Transition and Disclosure, an Amendment of FASB Statement No. 123." SFAS 148 provides three transition methods for adopting the fair value method of accounting for stock-based compensation prescribed under SFAS 123 and enhances the required disclosures regarding stock-based compensation effective for fiscal years ending after December 15, 2002. SFAS 148 also requires certain disclosures in financial reports issued for interim periods beginning after December 15, 2002.

PPL and its subsidiaries elected to adopt the fair value method of accounting for stock-based compensation as of January 1, 2003 using the prospective method of transition, as permitted by SFAS 148. The prospective method provides that PPL and its subsidiaries will recognize expense for all stock-based compensation awards granted, modified or settled on or after January 1, 2003. See Note 1 for a discussion of the change in accounting for stock-based compensation and the disclosures required by SFAS 148.

**SFAS 149** *(PPL, PPL Energy Supply and PPL Montana)*

See Note 17 for a discussion of SFAS 149, "Amendment of Statement 133 on Derivative Instruments and Hedging Activities," and the impact of its adoption.

## SFAS 150

*(PPL, PPL Energy Supply, PPL Electric and PPL Montana)*

In May 2003, the FASB issued SFAS 150, "Accounting for Certain Financial Instruments with Characteristics of Both Liabilities and Equity." SFAS 150 establishes standards for classifying and measuring certain financial instruments that have characteristics of both liabilities and equity. The standards established by it require certain financial instruments that, under previous guidance, could be classified as equity or "mezzanine" equity to now be classified as liabilities on the balance sheet. SFAS 150 requires the following freestanding financial instruments to be classified as liabilities (or assets in some circumstances):

- mandatorily redeemable financial instruments,
- financial instruments that embody obligations to repurchase equity shares in exchange for cash or other assets, including written put options and forward purchase contracts, and
- certain financial instruments that embody obligations to issue a variable number of shares.

SFAS 150 also requires disclosure regarding the nature and terms of those instruments and settlement alternatives. Except as discussed below, SFAS 150 is effective for all financial instruments entered into or modified after May 31, 2003 and is otherwise effective at the beginning of the first interim period beginning after June 15, 2003. In November 2003, the FASB issued FSP FAS 150-3, "Effective Date, Disclosures, and Transition for Mandatorily Redeemable Financial Instruments of Certain Nonpublic Entities and Certain Mandatorily Redeemable Noncontrolling Interests under FASB Statement No. 150, 'Accounting for Certain Financial Instruments with Characteristics of Both Liabilities and Equity,'" which, as it relates to public entities, deferred indefinitely certain provisions of SFAS 150 related to certain mandatorily redeemable noncontrolling interests. SFAS 150 prohibits the restatement of financial statements for periods prior to its adoption.

*(PPL, PPL Energy Supply and PPL Electric)*

In accordance with SFAS 150, effective July 1, 2003, PPL changed its classification of the trust preferred securities of PPL Capital Funding Trust I, which were issued as a component of the PEPS Units, PPL Energy Supply changed its classification of the trust preferred securities issued by SIUK Capital Trust I and PPL Electric changed its classification of its preferred stock with sinking fund requirements. These securities are mandatorily redeemable financial instruments, as they require the issuer to redeem the securities for cash on a specified date. Thus, they should be classified as liabilities, as a component of long-term debt, instead of "mezzanine" equity, on the balance sheet. As of December 31, 2003, no amounts were included in long-term debt for any of these securities because of the following: PPL deconsolidated PPL Capital Funding Trust I in accordance with FASB Interpretation No. 46, "Consolidation of Variable Interest Entities, an Interpretation of ARB No. 51,"

PPL Energy Supply deconsolidated SIUK Capital Trust I in accordance with FIN 46 and there was no preferred stock with sinking fund requirements of PPL Electric outstanding (due to preferred stock redemptions discussed in Note 8). As a result of the deconsolidation of the trusts, the subordinated debt securities that support the trust preferred securities, rather than the trust preferred securities themselves, are reflected in long-term debt as of December 31, 2003. See "FIN 46 and FIN 46(R)" for a discussion of the deconsolidation of the trusts.

SFAS 150 also requires the distributions on these mandatorily redeemable securities to be included as a component of "Interest Expense" instead of "Distributions on Preferred Securities" in the Statement of Income effective July 1, 2003. "Interest Expense" for 2003 includes distributions on these securities totaling \$27 million for PPL, \$5 million for PPL Energy Supply and an insignificant amount for PPL Electric. Periods ending prior to July 1, 2003 have not been restated to conform to these presentations since SFAS 150 specifically prohibits the restatement of financial statements for periods prior to its adoption.

**FIN 45** *(PPL, PPL Energy Supply, PPL Electric and PPL Montana)*

In 2002, the FASB issued Interpretation No. 45, "Guarantor's Accounting and Disclosure Requirements for Guarantees, Including Indirect Guarantees of Indebtedness of Others, an Interpretation of FASB Statements No. 5, 57, and 107 and Rescission of FASB Interpretation No. 34." FIN 45 clarifies upon issuance of certain types of guarantees, the guarantor recognizes an initial liability for the fair value of the obligation it assumes under the guarantee. The offsetting entry will be dependent upon the circumstances under which the guarantee is issued, and the initial liability should typically be reduced as the guarantor is released from risk under the guarantee. FIN 45 also requires a guarantor to make significant new disclosures for guarantees even if the likelihood of the guarantor's having to make payments is remote. The provisions relating to the initial recognition and measurement of guarantee obligations must be applied on a prospective basis for guarantees issued or modified after December 31, 2002. PPL and its subsidiaries adopted FIN 45 effective January 1, 2003. FIN 45 did not have a significant impact on earnings in 2003. See Note 14 for disclosure of guarantees and other assurances existing as of December 31, 2003.

**FIN 46 and FIN 46(R)** *(PPL, PPL Energy Supply, PPL Electric and PPL Montana)*

In January 2003, the FASB issued Interpretation No. 46, "Consolidation of Variable Interest Entities, an Interpretation of ARB No. 51." FIN 46 clarifies that variable interest entities, defined therein, that do not disperse risks among the parties involved should be consolidated by the entity that is determined to be the primary beneficiary. FIN 46 also requires certain disclosures to be made by the primary beneficiary and by an enterprise that holds a significant variable interest in a variable interest entity but is not the primary beneficiary. FIN 46 appli

immediately to variable interest entities created after January 31, 2003 and to variable interest entities in which an enterprise obtains an interest after January 31, 2003. For variable interest entities in which an enterprise holds a variable interest that was required before February 1, 2003, FIN 46 was originally required to be adopted no later than the first fiscal year or interim period beginning after June 15, 2003. However, in October 2003, the FASB issued FSP FIN 46-6, "Effective Date of FASB Interpretation No. 46, Consolidation of Variable Interest Entities," which delayed the effective date for applying the provisions of FIN 46 to interests held by public entities in variable interest entities or potential variable interest entities created before February 1, 2003 until the end of the first interim period ending after December 15, 2003.

In December 2003, the FASB revised FIN 46 by issuing Interpretation No. 46 (revised December 2003), which is known as FIN 46(R) and replaces FIN 46. FIN 46(R) does not change the general consolidation concepts of FIN 46. Among other things, FIN 46(R) again changes the effective date for applying the provisions of FIN 46 to certain entities, clarifies certain provisions of FIN 46 and provides additional scope exceptions for certain types of businesses. For entities to which the provisions of FIN 46 have not been applied as of December 24, 2003, FIN 46(R) provides that a public entity that is not a small business issuer should apply the provisions of FIN 46 or FIN 46(R) as follows: (i) FIN 46(R) shall be applied to all entities no later than the end of the first reporting period that ends after March 15, 2004, and (ii) FIN 46 or FIN 46(R) should be applied to entities that are considered to be SPEs no later than the end of the first reporting period that ends after December 15, 2003.

As permitted by FIN 46(R), PPL and its subsidiaries adopted FIN 46 effective December 31, 2003 for entities created before February 1, 2003 that are considered to be SPEs. This adoption resulted in the consolidation of the lessors under the operating leases for the Sundance, University Park and Lower Mt. Bethel generation facilities, as well as the deconsolidation of two wholly-owned trusts. See below for further discussion. Also, as permitted by FIN 46(R), PPL and its subsidiaries deferred the application of FIN 46 for other entities and plans to adopt FIN 46(R) for all entities on March 31, 2004.

PPL and its subsidiaries are in the process of evaluating entities in which they hold a variable interest in accordance with FIN 46(R). PPL and its subsidiaries are currently not aware of any variable interest entities that are not consolidated as of December 31, 2003 but which they will be required to consolidate in accordance with FIN 46(R) effective March 31, 2004. As they continue to evaluate the impact of applying FIN 46(R), PPL and its subsidiaries may identify additional entities that they would need to consolidate.

*(PPL and PPL Energy Supply)*

### Additional Entities Consolidated

The lessors under the operating leases for the Sundance, University Park and Lower Mt. Bethel generation facilities are

variable interest entities that are considered to be SPEs. PPL Energy Supply is the primary beneficiary of these entities. Consequently, PPL Energy Supply was required to consolidate the financial statements of the lessors effective December 31, 2003. Upon initial consolidation, PPL Energy Supply recognized \$1.1 billion of additional assets and liabilities on its balance sheet and a charge of \$27 million, after-tax, as a cumulative effect of a change in accounting principle. The additional assets consist principally of the generation facilities, and the additional liabilities consist principally of the lease financing. See below for a discussion of the leases.

In May 2001, a subsidiary of PPL Energy Supply entered into a lease arrangement, as lessee, for the development, construction and operation of commercial power generation facilities. The lessor was created for the sole purpose of owning the facilities and incurring the related financing costs. The \$660 million operating lease arrangement covers the 450 MW gas-powered Sundance project near Coolidge, Arizona and the 540 MW gas-powered University Park project near University Park, Illinois. These facilities were substantially complete in July 2002, at which time the initial lease term commenced. See the Statement of Long-term Debt for a discussion of the related financing.

In December 2001, another subsidiary of PPL Energy Supply entered into a \$455 million operating lease arrangement, as lessee, for the development, construction and operation of a 600 MW gas-fired combined-cycle generation facility located in Lower Mt. Bethel Township, Northampton County, Pennsylvania. The lessor was created for the sole purpose of owning the facilities and incurring the related financing costs. The initial lease term commences on the date of commercial operation, which is expected to occur in 2004, and ends in December 2013. See the Statement of Long-term Debt for a discussion of the related financing.

### Entities Deconsolidated

Effective December 31, 2003, PPL deconsolidated PPL Capital Funding Trust I, and PPL Energy Supply deconsolidated SIUK Capital Trust I. These trusts are considered to be SPEs and were deconsolidated because PPL and PPL Energy Supply are not the primary beneficiaries of the trusts under current interpretations of FIN 46. Therefore, the "Company-obligated Mandatorily Redeemable Preferred Securities of Subsidiary Trusts Holding Solely Company Debentures" amounting to \$661 million (for PPL) and \$86 million (for PPL Energy Supply), which would have been recorded as a component of long-term debt in 2003 in accordance with SFAS 150 if the trusts were consolidated, are not reflected in PPL's and PPL Energy Supply's Balance Sheet at December 31, 2003. Instead, the subordinated debt securities that support the trust preferred securities are reflected in "Long-term Debt with Affiliate Trust(s)" as of December 31, 2003. See below for further discussion.

The trusts hold subordinated debt securities of PPL Capital Funding, in the case of PPL Capital Funding Trust I, and WPD LLP, in the case of SIUK Capital Trust I. As a result of deconsolidating the trusts, the subordinated debt securities are

no longer eliminated in the consolidated financial statements. As of December 31, 2003, \$681 million is reflected as "Long-term Debt with Affiliate Trusts" in PPL's Balance Sheet, and \$89 million is reflected as "Long-term Debt with Affiliate Trust" in PPL Energy Supply's Balance Sheet.

The effect on the Balance Sheet as a result of deconsolidating the trusts was an increase in both total assets and total liabilities of \$21 million for PPL and \$3 million for PPL Energy Supply. The increase in assets relates to the investments in the common securities of the trusts, which are no longer eliminated in the consolidated financial statements. The increase in liabilities consists primarily of the difference between the carrying value of the preferred securities issued by the trusts compared to the carrying value of the subordinated debt securities of PPL Capital Funding and WPD LLP. The deconsolidation of the trusts did not impact the earnings of PPL and PPL Energy Supply.

See the Statement of Company-Obligated Mandatorily Redeemable Securities for a discussion of the trusts and their preferred securities, as well as the subordinated debt securities issued to the trusts.

#### **EITF 03-11** (*PPL, PPL Energy Supply and PPL Montana*)

In August 2003, the FASB ratified EITF 03-11, "Reporting Realized Gains and Losses on Derivative Instruments That Are Subject to FASB Statement No. 133, Accounting for Derivative Instruments and Hedging Activities, and Not 'Held for Trading Purposes' as Defined in EITF Issue No. 02-3, 'Issues Involved in Accounting for Derivative Contracts Held for Trading Purposes and Contracts Involved in Energy Trading and Risk Management Activities.'" EITF 03-11 addresses whether realized gains and losses on physically settled derivative contracts not "held for trading purposes" should be reported in the income statement on a gross or net basis. It requires that each entity make this determination for itself based on the relevant facts and circumstances in the context of the various activities of the entity rather than based solely on the terms of the individual contracts. EITF 03-11 is effective for transactions entered into on or after October 1, 2003. See Note 17 for a discussion of the impact of the adoption of EITF 03-11.

**FSP FAS 106-1** (*PPL, PPL Energy Supply, PPL Electric and PPL Montana*)

See Note 12 for a discussion of FSP FAS 106-1, "Accounting and Disclosure Requirements Related to the Medicare Prescription Drug, Improvement and Modernization Act of 2003."

## SCHEDULE II - VALUATION AND QUALIFYING ACCOUNTS AND RESERVES

### PPL Corporation

(Millions of Dollars)

Column A	Column B	Column C		Column D	Column E
Description	Balance at Beginning of Period	Additions		Deductions	Balance at End of Period
		Charged to Income	Other		
<b>Year Ended December 31, 2003</b>					
Reserves deducted from assets in the					
Balance Sheet					
Uncollectible accounts including unbilled revenues.....	\$ 112	\$ 31		\$ 47 (a)	\$ 96 (b)
Obsolete inventory - Materials and supplies.....	1	3		1	3
Mark-to-market valuation reserves.....	3		\$ 2	1	4
Deferred tax valuation allowance.....	327	4	48	91	288
<b>Year Ended December 31, 2002</b>					
Reserves deducted from assets in the					
Balance Sheet					
Uncollectible accounts including unbilled revenues.....	125	32	7 (c)	52 (d)	112 (b)
Obsolete inventory - Materials and supplies.....	1				1
Mark-to-market valuation reserves.....	7			4	3
Deferred tax valuation allowance.....	132	30	182 (c)	17	327
<b>Year Ended December 31, 2001</b>					
Reserves deducted from assets in the					
Balance Sheet					
Uncollectible accounts including unbilled revenues.....	70	98		43	125 (b)
Obsolete inventory - Materials and supplies.....	4			3	1
Mark-to-market valuation reserves.....	2	5			7
Deferred tax valuation allowance.....	8	61	67	4	132

(a) See Note 17 to the financial statements regarding a reduction in the Enron receivable reserve.

(b) Includes reserves for customer accounts receivable, California ISO, the Enron receivables and other.

(c) Includes the reserve recorded upon the acquisition of a controlling interest in WPD.

(d) Includes the removal of reserves upon the deconsolidation of CEMAR.

**SCHEDULE II - VALUATION AND QUALIFYING ACCOUNTS AND RESERVES**  
**PPL Energy Supply, LLC**

(Millions of Dollars)

Column A	Column B	Column C		Column D	Column E
Description	Balance at Beginning of Period	Additions		Deductions	Balance at End of Period
		Charged to Income	Other		
<u>Year Ended December 31, 2003</u>					
Reserves deducted from assets in the					
Balance Sheet					
Uncollectible accounts including unbilled revenues.....	\$ 88	\$ 5		\$ 22 (a)	\$ 71 (b)
Obsolete inventory - Materials and supplies.....	1	3		1	3
Mark-to-market valuation reserves.....	3		\$ 2	1	4
Deferred tax valuation allowance.....	327	4	48	91	288
<u>Year Ended December 31, 2002</u>					
Reserves deducted from assets in the					
Balance Sheet					
Uncollectible accounts including unbilled revenues.....	104	5	7 (c)	28 (d)	88 (b)
Obsolete inventory - Materials and supplies.....	1				1
Mark-to-market valuation reserves.....	7			4	3
Deferred tax valuation allowance.....	132	30	182 (c)	17	327
<u>Year Ended December 31, 2001</u>					
Reserves deducted from assets in the					
Balance Sheet					
Uncollectible accounts including unbilled revenues.....	52	67		15	104 (b)
Obsolete inventory - Materials and supplies.....	4			3	1
Mark-to-market valuation reserves.....	2	5			7
Deferred tax valuation allowance.....	8	61	67	4	132

- (a) See Note 17 to the financial statements regarding a reduction in the Enron receivable reserve.
- (b) Includes reserves for customer accounts receivable, California ISO, the Enron receivables and other.
- (c) Includes the reserve recorded upon the acquisition of a controlling interest in WPD.
- (d) Includes the removal of reserves upon the deconsolidation of CEMAR.

**SCHEDULE II - VALUATION AND QUALIFYING ACCOUNTS AND RESERVES**  
**PPL Electric Utilities Corporation**

(Millions of Dollars)

Column A	Column B	Column C		Column D	Column E
Description	Balance at Beginning of Period	Additions		Deductions	Balance at End of Period
		Charged to Income	Other		
<u>Year Ended December 31, 2003</u>					
Reserves deducted from assets in the Balance Sheet					
Uncollectible accounts .....	\$ 23	\$ 24		\$ 23	\$ 24
<u>Year Ended December 31, 2002</u>					
Reserves deducted from assets in the Balance Sheet					
Uncollectible accounts .....	19	25		21	23
<u>Year Ended December 31, 2001</u>					
Reserves deducted from assets in the Balance Sheet					
Uncollectible accounts .....	16	30		27	19

**SCHEDULE II - VALUATION AND QUALIFYING ACCOUNTS AND RESERVES**  
**PPL Montana, LLC**

(Millions of Dollars)

Column A	Column B	Column C		Column D	Column E
Description	Balance at Beginning of Period	Additions		Deductions	Balance at End of Period
		Charged to Income	Other		
<u>Year Ended December 31, 2003</u>					
Reserves deducted from assets in the Balance Sheet					
Uncollectible accounts including unbilled revenues.....	\$ 47			\$ 10 (a)	\$ 37 (b)
Obsolete inventory - Materials and supplies.....	1				1
<u>Year Ended December 31, 2002</u>					
Reserves deducted from assets in the Balance Sheet					
Uncollectible accounts including unbilled revenues.....	47				47 (b)
Obsolete inventory - Materials and supplies.....	1				1
Mark-to-market valuation reserves.....	1			1	
<u>Year Ended December 31, 2001</u>					
Reserves deducted from assets in the Balance Sheet					
Uncollectible accounts including unbilled revenues.....	18	\$ 30		1	47 (b)
Obsolete inventory - Materials and supplies.....	2			1	1
Mark-to-market valuation reserves.....		1			1

(a) See Note 17 to the financial statements regarding a reduction in the Enron receivable reserve.

(b) Includes reserves for customer accounts receivable, California ISO, the Enron receivables and other.

# QUARTERLY FINANCIAL, COMMON STOCK PRICE AND DIVIDEND DATA (Unaudited)

## PPL Corporation and Subsidiaries

(Millions of Dollars, except per share data)

	For the Quarters Ended (a)			
	March 31	June 30	Sept. 30	Dec. 31
<b>2003</b>				
Operating revenues as previously reported.....	\$ 1,487	\$ 1,338	\$ 1,456	
Reclassification (b) .....	5	4	2	
Discontinued operations (c) .....	(2)	(1)	(1)	
	<u>1,490</u>	<u>1,341</u>	<u>1,457</u>	\$ 1,299
Operating income as previously reported .....	357	285	362	
Discontinued operations (c) .....		1	1	
Other .....	2			
	<u>359</u>	<u>286</u>	<u>363</u>	332
Income from continuing operations .....	176	116	172	255
Net income .....	239	116	171	208
Basic earnings per common share: (d)				
Income from continuing operations .....	1.06	0.68	0.97	1.44
Net income .....	1.43	0.68	0.97	1.17
Diluted earnings per common share: (d)				
Income from continuing operations .....	1.06	0.67	0.97	1.44
Net income .....	1.43	0.67	0.97	1.17
Dividends declared per common share (e).....	0.385	0.385	0.385	0.385
Price per common share				
High .....	\$ 38.10	\$ 44.34	\$ 43.12	\$ 43.89
Low .....	31.65	35.04	38.45	38.88
<b>2002</b>				
Operating revenues as previously reported.....	\$ 1,354	\$ 1,299	\$ 1,492	
Reclassification (b) .....	3	5	4	
Discontinued operations (c) .....	(1)	(1)	(1)	
	<u>1,356</u>	<u>1,303</u>	<u>1,495</u>	\$ 1,327
Operating income as previously reported .....	400	178	394	
Discontinued operations (c) .....			1	
	<u>400</u>	<u>178</u>	<u>395</u>	273
Income (loss) from continuing operations .....	147	(27)	123	117
Net income (loss) .....	(3)	(27)	122	116
Basic earnings per common share: (d)				
Income (loss) from continuing operations .....	1.00	(0.18)	0.81	0.71
Net income (loss) .....	(0.02)	(0.18)	0.81	0.71
Diluted earnings per common share: (d)				
Income (loss) from continuing operations .....	1.00	(0.18)	0.80	0.71
Net income (loss) .....	(0.02)	(0.18)	0.80	0.71
Dividends declared per common share (e).....	0.36	0.36	0.36	0.36
Price per common share				
High .....	\$ 39.85	\$ 39.95	\$ 37.60	\$ 36.26
Low .....	31.40	28.97	26.00	26.47

(a) Quarterly results can vary depending on weather and the forward pricing of power. In addition, earnings in 2003 and 2002 were affected by unusual items. Accordingly, comparisons among quarters of a year may not be indicative of overall trends and changes in operations.

(b) Relates to the reclassification of equity losses from an unconsolidated affiliate from revenue to operating and maintenance expenses.

(c) Each quarter in 2002 and 2003 has been restated to reflect the loss from discontinued Latin American telecommunications operations.

(d) The sum of the quarterly amounts may not equal annual earnings per share due to changes in the number of common shares outstanding during the year or rounding.

(e) PPL has paid quarterly cash dividends on its common stock in every year since 1946. The dividends declared per share in 2003 were \$1.54 and in 2002 were \$1.44. In February 2003, PPL announced an increase to its quarterly common stock dividend, payable April 1, 2003, to 38.5 cents per share (equivalent to \$1.54 per annum.) In February 2004, PPL announced an increase to its quarterly common stock dividend, payable April 1, 2004, to 41 cents per share (equivalent to \$1.64 per annum). Future dividends, declared at the discretion of the Board of Directors, will be dependent upon future earnings, cash flows, financial requirements and other factors.

**QUARTERLY FINANCIAL DATA (Unaudited)**  
**PPL Electric Utilities Corporation and Subsidiaries**

(Millions of Dollars)

	For the Quarters Ended (a)			
	March 31	June 30	Sept. 30	Dec. 31
<b>2003</b>				
Operating revenues .....	\$ 753	\$ 637	\$ 704	\$ 694
Operating income.....	99	54	41	57
Income (loss) available to PPL .....	29		(6)	2
<b>2002</b>				
Operating revenues .....	\$ 697	\$ 651	\$ 715	\$ 685
Operating income.....	89	39	87	60
Income (loss) available to PPL .....	20	(8)	24	3

(a) PPL Electric's business is seasonal in nature, with peak sales periods generally occurring in the winter and summer months. In addition, earnings in certain quarters were affected by unusual items. Accordingly, comparisons among quarters of a year may not be indicative of overall trends and changes in operations.

**ITEM 9. CHANGES IN AND DISAGREEMENTS WITH ACCOUNTANTS  
ON ACCOUNTING AND FINANCIAL DISCLOSURE**

**PPL Corporation, PPL Energy Supply, LLC, PPL Electric Utilities Corporation and PPL Montana, LLC**

None.

**ITEM 9A. CONTROLS AND PROCEDURES**

**PPL Corporation, PPL Energy Supply, LLC, PPL Electric Utilities Corporation and PPL Montana, LLC**

(a) Evaluation of disclosure controls and procedures.

The registrants' principal executive officers and principal financial officers, based on their evaluation of the registrants' disclosure controls and procedures (as defined in Rules 13a-15(e) and 15d-15(e) of the Securities Exchange Act of 1934) have concluded that, as of December 31, 2003, the registrants' disclosure controls and procedures are adequate and effective to ensure that material information relating to the registrants and their consolidated subsidiaries is recorded, processed, summarized and reported within the time periods specified by the SEC's rules and forms, particularly during the period for which this annual report has been prepared.

(b) Change in internal controls over financial reporting.

The registrants' principal executive officers and principal financial officers have concluded that there were no changes in the registrants' internal controls over financial reporting during the registrant's fourth fiscal quarter that have materially affected, or are reasonably likely to materially affect, the registrant's internal control over financial reporting.

**PART III**

**ITEM 10. DIRECTORS AND EXECUTIVE OFFICERS OF THE REGISTRANT**

**PPL Corporation**

Additional information for this item will be set forth in the sections entitled "Nominees for Directors," "Directors Continuing in Office," "Section 16(a) Beneficial Ownership Reporting Compliance" and "Board Committees - Audit Committee" in PPL's 2004 Notice of Annual Meeting and Proxy Statement, which will be filed with the SEC not later than 120 days after December 31, 2003, and which information is incorporated herein by reference. Information required by this item concerning the executive officers of PPL is set forth at the end of Part I of this report.

PPL has adopted a code of ethics entitled "Standards of Conduct and Integrity" that applies to all directors, managers, trustees, officers (including the principal executive officers, principal financial officers and principal accounting officers), employees and agents of PPL and PPL's subsidiaries for which it has operating control (including PPL Energy Supply, PPL Electric and PPL Montana). The "Standards of Conduct and Integrity" are posted on PPL's Internet Web site: [www.pplweb.com/corporategovernance.htm](http://www.pplweb.com/corporategovernance.htm) and are available in print to any shareholder who requests them.

PPL also has adopted its "Guidelines of Corporate Governance," which address, among other things, director qualification standards and director and board committee responsibilities. These guidelines, and the charters of each of the committees of PPL's board of directors, are posted on PPL's Internet Web site: [www.pplweb.com/corporategovernance.htm](http://www.pplweb.com/corporategovernance.htm) and are available in print to any shareholder who requests them.

**PPL Energy Supply, LLC**

Item 10 is omitted as PPL Energy Supply meets the conditions set forth in General Instruction (I)(1)(a) and (b) of Form 10-K.

**PPL Electric Utilities Corporation**

Information for this item will be set forth in the sections entitled "Nominees for Directors" and "Directors Continuing in Office" in PPL Electric's 2004 Notice of Annual Meeting and Information Statement, which will be filed with the SEC not later than 120 days after

December 31, 2003, and which information is incorporated herein by reference. Information required by this item concerning the executive officers of PPL Electric is set forth at the end of Part I of this report.

**PPL Montana, LLC**

Item 10 is omitted as PPL Montana meets the conditions set forth in General Instruction (I)(1)(a) and (b) of Form 10-K.

**ITEM 11. EXECUTIVE COMPENSATION**

**PPL Corporation**

Information for this item will be set forth in the sections entitled "Compensation of Directors," "Board Committees - Audit Committee," "Summary Compensation Table," "Option Grants in Last Fiscal Year" and "Retirement Plans for Executive Officers" in PPL's 2004 Notice of Annual Meeting and Proxy Statement, which will be filed with the SEC not later than 120 days after December 31, 2003, and which information is incorporated herein by reference.

**PPL Energy Supply, LLC**

Item 11 is omitted as PPL Energy Supply meets the conditions set forth in General Instruction (I)(1)(a) and (b) of Form 10-K.

**PPL Electric Utilities Corporation**

Information for this item will be set forth in the sections entitled "Compensation of Directors," "Summary Compensation Table," "Option Grants in Last Fiscal Year" and "Retirement Plans for Executive Officers" in PPL Electric's 2004 Notice of Annual Meeting and Information Statement, which will be filed with the SEC not later than 120 days after December 31, 2003, and which information is incorporated herein by reference.

**PPL Montana, LLC**

Item 11 is omitted as PPL Montana meets the conditions set forth in General Instruction (I)(1)(a) and (b) of Form 10-K.

**ITEM 12. SECURITY OWNERSHIP OF CERTAIN BENEFICIAL OWNERS AND MANAGEMENT AND RELATED STOCKHOLDER MATTERS**

**PPL Corporation**

Information for this item will be set forth in the section entitled "Stock Ownership" in PPL's 2004 Notice of Annual Meeting and Proxy Statement, which will be filed with the SEC not later than 120 days after December 31, 2003, and which information is incorporated herein by reference. In addition, provided below in tabular format is information as of December 31, 2003 with respect to compensation plans (including individual compensation arrangements) under which equity securities of PPL are authorized for issuance.

**Equity Compensation Plan Information**

	Number of securities to be issued upon exercise of outstanding options, warrants and rights (3)	Weighted-average exercise price of outstanding options, warrants and rights (3)	Number of securities remaining available for future issuance under equity compensation plans (4)
Equity compensation plans approved by security holders (1)	2,022,388 - ICP <u>889,870</u> - ICPKE 2,912,258 - Total	\$34.99 - ICP \$36.86 - ICPKE \$35.56 - Combined	4,364,191 - ICP 7,100,710 - ICPKE <u>7,416,806</u> - DDCP 18,881,707 - Total
Equity compensation plans not approved by security holders (2)			

(1) Includes (a) the Amended and Restated Incentive Compensation Plan (ICP), under which stock options, restricted stock, restricted stock units, dividend equivalents and other stock-based awards may be awarded to executive officers of PPL; (b) the Amended and

Restated Incentive Compensation Plan for Key Employees (ICPKE), under which stock options, restricted stock, restricted stock units, dividend equivalents and other stock-based awards may be awarded to non-executive key employees of PPL and its subsidiaries; and (c) the Directors Deferred Compensation Plan (DDCP), under which stock units may be awarded to directors of PPL. See Note 11 to the financial statements for additional information.

- (2) All of PPL's current compensation plans under which equity securities of PPL are authorized for issuance have been approved by PPL's shareholders.
- (3) Relates to common stock issuable upon the exercise of stock options awarded under the ICP and ICPKE as of December 31, 2003. In addition, as of December 31, 2003, the following other securities had been awarded and are outstanding under the ICP, DDCP and ICPKE: 182,653 shares of restricted stock under the ICP; 308,361 shares of restricted stock and 135,078 restricted stock units under the ICPKE; and 77,428 stock units under the DDCP.
- (4) Based upon the following aggregate award limitations under the ICP, ICPKE and DDCP: (a) under the ICP, 7,884,715 awards (i.e., 5% of the total PPL common stock outstanding as of April 23, 1999) granted after April 23, 1999; (b) under the ICPKE, 8,286,804 awards (i.e., 5% of the total PPL common stock outstanding as of January 1, 2003) granted after April 25, 2003, reduced by outstanding awards for which common stock was not yet issued as of such date; and (c) under the DDCP, 7,526,428 securities. In addition, each of the ICP and ICPKE includes an annual award limitation of 2% of total PPL common stock outstanding as of January 1 of each year.

#### **PPL Energy Supply, LLC**

Item 12 is omitted as PPL Energy Supply meets the conditions set forth in General Instruction (I)(1)(a) and (b) of Form 10-K.

#### **PPL Electric Utilities Corporation**

Information for this item will be set forth in the section entitled "Stock Ownership" in PPL Electric's 2004 Notice of Annual Meeting and Information Statement, which will be filed with the SEC not later than 120 days after December 31, 2003, and which information is incorporated herein by reference.

#### **PPL Montana, LLC**

Item 12 is omitted as PPL Montana meets the conditions set forth in General Instruction (I)(1)(a) and (b) of Form 10-K.

### **ITEM 13. CERTAIN RELATIONSHIPS AND RELATED TRANSACTIONS**

#### **PPL Corporation**

None.

#### **PPL Energy Supply, LLC**

Item 13 is omitted as PPL Energy Supply meets the conditions set forth in General Instruction (I)(1)(a) and (b) of Form 10-K.

#### **PPL Electric Utilities Corporation**

None.

#### **PPL Montana, LLC**

Item 13 is omitted as PPL Montana meets the conditions set forth in General Instruction (I)(1)(a) and (b) of Form 10-K.

### **ITEM 14. PRINCIPAL ACCOUNTANT FEES AND SERVICES**

#### **PPL Corporation**

Information for this item will be set forth in the section entitled "Fees to Independent Auditor for 2003 and 2002" in PPL's 2004 Notice of Annual Meeting and Proxy Statement, which will be filed with the SEC not later than 120 days after December 31, 2003, and which information is incorporated herein by reference.

## **PPL Energy Supply, LLC**

### **Audit Fees**

The aggregate fees billed by PricewaterhouseCoopers LLP for the fiscal years ended December 31, 2003 and December 31, 2002 for professional services rendered for the audit of PPL Energy Supply's annual financial statements and review of financial statements included in PPL Energy Supply's Quarterly Reports on Form 10-Q and for services in connection with statutory and regulatory filings or engagements, including comfort letters and consents for financings and filings made with the SEC, for those fiscal years were \$1,576,000 and \$1,284,000, respectively.

### **Audit-Related Fees**

The aggregate fees billed for the fiscal years ended December 31, 2003 and December 31, 2002 for assurance and related services rendered by PricewaterhouseCoopers LLP that are related to the performance of the audit or review of PPL Energy Supply's financial statements were \$116,000 and \$217,000, respectively. These services principally related to audits of employee benefit plans and consultation to ensure appropriate accounting and reporting in connection with various business and financing transactions.

### **Tax Fees**

The aggregate fees billed for the fiscal years ended December 31, 2003 and December 31, 2002 for professional services rendered by PricewaterhouseCoopers LLP for tax-related services were \$792,000 and \$1,386,000, respectively. These fees principally related to international tax consulting and advisory services.

### **All Other Fees**

There were no additional fees billed by PricewaterhouseCoopers LLP for the fiscal year ended December 31, 2003. The aggregate fees billed by PricewaterhouseCoopers LLP for the fiscal year ended December 31, 2002 for services rendered to PPL Energy Supply other than the Audit Fees, Audit-Related Fees and Tax Fees included above were \$355,000. These fees related to financial information system implementation and design services at an international affiliate. PricewaterhouseCoopers LLP no longer provides this type of service to PPL Energy Supply or any of its affiliates.

During 2002, the Audit Committee of PPL adopted procedures for pre-approving audit and non-audit services to be provided by the independent auditor for PPL and its subsidiaries. The procedures are designed to safeguard the continued independence of the independent auditor. More specifically, the use of the independent auditor to perform either audit or non-audit services is prohibited unless specifically approved in advance by the Audit Committee of PPL. As a result of this approval process, the Audit Committee of PPL has established specific categories of services and authorization levels. All services outside of the specified categories and all amounts exceeding the authorization levels are reviewed by the Chair of the Audit Committee of PPL, who serves as the Committee designee to review and approve audit and non-audit related services during the year. A listing of the approved audit and non-audit services is reviewed with the full Audit Committee of PPL no later than at its next meeting.

The Audit Committee of PPL reviewed all 2003 and 2002 audit and non-audit related fees. Since July 2002, when the Sarbanes-Oxley Act of 2002 was signed into law, the Audit Committee of PPL approved 100% of all fees. There were no services provided by the independent auditor during that time that would fall within the All Other Fees category.

## **PPL Electric Utilities Corporation**

Information for this item will be set forth in the section entitled "Fees to Independent Auditor for 2003 and 2002" in PPL Electric's 2004 Notice of Annual Meeting and Information Statement, which will be filed with the SEC not later than 120 days after December 31, 2003, and which information is incorporated herein by reference.

## **PPL Montana, LLC**

### **Audit Fees**

The aggregate fees billed by PricewaterhouseCoopers LLP for the fiscal years ended December 31, 2003 and December 31, 2002 for professional services rendered for the audit of PPL Montana's annual financial statements and review of financial statements included in PPL Montana's Quarterly Reports on Form 10-Q and for services in connection with statutory and regulatory filings or engagements,

including comfort letters and consents for financings and filings made with the SEC, for those fiscal years were \$131,000 and \$135,000, respectively.

#### **Audit-Related Fees**

The aggregate fees billed for the fiscal years ended December 31, 2003 and December 31, 2002 for assurance and related services rendered by PricewaterhouseCoopers LLP that are related to the performance of the audit or review of PPL Montana's financial statements, were \$8,000 and \$7,000, respectively. These services principally related to audits of employee benefit plans.

#### **Tax Fees**

PricewaterhouseCoopers LLP did not render any professional services for tax-related matters for PPL Montana for the fiscal years ended December 31, 2003 and December 31, 2002.

#### **All Other Fees**

PricewaterhouseCoopers LLP did not render any professional services for any other matters for the fiscal years ended December 31, 2003 and December 31, 2002, other than the Audit Fees included above.

During 2002, the Audit Committee of PPL adopted procedures for pre-approving audit and non-audit services to be provided by the independent auditor for PPL and its subsidiaries. The procedures are designed to safeguard the continued independence of the independent auditor. More specifically, the use of the independent auditor to perform either audit or non-audit services is prohibited unless specifically approved in advance by the Audit Committee of PPL. As a result of this approval process, the Audit Committee of PPL has established specific categories of services and authorization levels. All services outside of the specified categories and all amounts exceeding the authorization levels are reviewed by the Chair of the Audit Committee of PPL, who serves as the Committee designee to review and approve audit and non-audit related services during the year. A listing of the approved audit and non-audit services is reviewed with the full Audit Committee of PPL no later than at its next meeting.

The Audit Committee of PPL reviewed all 2003 and 2002 audit and non-audit related fees. Since July 2002, when the Sarbanes-Oxley Act of 2002 was signed into law, the Audit Committee of PPL approved 100% of all fees. There were no services provided by the independent auditor during that time that would fall within Tax Fees or the All Other Fees category.

**PART IV**

**ITEM 15. EXHIBITS, FINANCIAL STATEMENT SCHEDULES, AND REPORTS ON FORM 8-K**

**PPL Corporation, PPL Energy Supply, LLC, PPL Electric Utilities Corporation and PPL Montana, LLC**

(a) The following documents are filed as part of this report:

1. Financial Statements - Refer to the "Index to Item 8. Financial Statements and Financial Statement Schedules" for an index of the financial statements included in this report.
2. Supplementary Data and Supplemental Financial Statement Schedule - included in response to Item 8.

Schedule II - Valuation and Qualifying Accounts and Reserves for the Three Years Ended December 31, 2003

All other schedules are omitted because of the absence of the conditions under which they are required or because the required information is included in the financial statements or notes thereto.

3. Exhibits

Exhibit Index on page 199.

(b) Reports on Form 8-K:

The following Reports on Form 8-K were filed (\*) or furnished (\*\*), as indicated, during the three months ended December 31, 2003:

**\*\* Report dated October 23, 2003 - PPL**

Item 12. Disclosure of Results of Operations and Financial Condition

PPL issued a press release announcing its results for the quarter ended September 30, 2003, a tightening of the range for its 2003 earnings forecast, and its 2004 earnings forecast.

Item 7. Financial Statements and Exhibits

Press release announcing PPL's results for the quarter ended September 30, 2003, a tightening of the range for PPL's 2003 earnings forecast, and PPL's 2004 earnings forecast.

**\* Report dated December 12, 2003 - PPL Montana**

Item 9. Rating Agency Decision

Standard & Poor's Ratings Services' (S&P) downgrade of PPL Montana's 8.903% Pass Through Certificates due 2020 to BBB- from BBB.

Item 7. Financial Statements and Exhibits

Report on downgrade by S&P on December 12, 2003.

**\*\* Report dated December 19, 2003 - PPL**

Item 5. Other Events

PPL issued a press release announcing the extension of the duration of its exchange offer for its outstanding 7-3/4% PEPS Units.

Item 7. Financial Statements and Exhibits

Exhibit of (1) Press releases announcing the extension of the duration of the Exchange Offer and certain modifications to the Exchange Offer and (2) Instructions for Soliciting Dealers.

## SHAREOWNER AND INVESTOR INFORMATION

**Annual Meetings:** The annual meeting of shareowners of PPL Corporation is held each year on the fourth Friday of April. The 2004 meeting for PPL Corporation will be held on Friday, April 23, 2004, at Lehigh University's Stabler Arena, at the Goodman Campus Complex located in Lower Saucon Township, outside Bethlehem, Pennsylvania. The 2004 meeting for PPL Electric will be held on Tuesday, April 20, 2004, at the offices of the company at Two North Ninth Street, Allentown, Pennsylvania.

**Proxy and Information Statement Material:** A proxy statement and information statement and notice of PPL's and PPL Electric's annual meetings are mailed to all shareowners of record as of February 27, 2004.

**Dividends:** Subject to the declaration of dividends on PPL common stock by the PPL Board of Directors or its Executive Committee and PPL Electric preferred stock by the PPL Electric Board of Directors, dividends are paid on the first day of April, July, October and January. Dividend checks are mailed in advance of those dates with the intention that they arrive as close as possible to the payment dates. The 2004 record dates for dividends are expected to be March 10, June 10, September 10, and December 10.

**Direct Deposit of Dividends:** Shareowners may choose to have their dividend checks deposited directly into their checking or savings account. Quarterly dividend payments are electronically credited on the dividend date, or the first business day thereafter.

**Dividend Reinvestment Plan:** Shareowners may choose to have dividends on their PPL common stock or PPL Electric preferred stock reinvested in PPL common stock instead of receiving the dividend by check.

**Certificate Safekeeping:** Shareowners participating in the Dividend Reinvestment Plan may choose to have their common stock certificates forwarded to PPL for safekeeping.

**Lost Dividend or Interest Checks:** Dividend or interest checks lost by investors, or those that may be lost in the mail, will be replaced if the check has not been located by the 10th business day following the payment date.

**Transfer of Stock or Bonds:** Stock or bonds may be transferred from one name to another or to a new account in the name of another person. Please contact Investor Services regarding transfer instructions.

**Bondholder Information:** Much of the information and many of the procedures detailed here for shareowners also apply to bondholders. Questions related to bondholder accounts should be directed to Investor Services.

**Lost Stock or Bond Certificates:** Please contact Investor Services for an explanation of the procedure to replace lost stock or bond certificates.

**PPL Annual Report:** Published and mailed in mid-March to all shareowners of record.

**Periodic Mailings:** Letters regarding new investor programs, special items of interest, or other pertinent information are mailed on a non-scheduled basis as necessary.

**Duplicate Mailings:** The annual report and other investor publications are mailed to each investor account. If you have more than one account, or if there is more than one investor in your household, you may contact Investor Services to request that only one publication be delivered to your address. Please provide account numbers for all duplicate mailings.

**Shareowner Information Line:** Shareowners can get detailed corporate and financial information 24 hours a day using the Shareowner Information Line. They can hear timely recorded messages about earnings, dividends and other company news releases; request information by fax; and request printed materials in the mail.

The toll-free Shareowner Information Line is 1-800-345-3085.

Other PPL publications, such as the annual and quarterly reports to the Securities and Exchange Commission (Forms 10-K and 10-Q) will be mailed upon request.

Shareowners can also obtain information free of charge from PPL's Internet home page ([www.pplweb.com](http://www.pplweb.com)). Shareowners can access PPL Securities and Exchange Commission filings, news releases, stock quotes and historical performance. Visitors to our Web site can provide their E-mail address and indicate their desire to receive future earnings or news releases automatically.

**Investor Services:** For any questions you have or additional information you require about PPL and its subsidiaries, please call the Shareowner Information Line, or write to:

Manager-Investor Services  
PPL Services Corporation  
Two North Ninth Street  
Allentown, PA 18101

**Internet Access:** For updated information throughout the year, check out our home page at <http://www.pplweb.com>. You may also contact Investor Services via E-mail at [invserv@pplweb.com](mailto:invserv@pplweb.com).

Registered shareowners can access account information by visiting [shareowneronline.com](http://shareowneronline.com).

**Listed Securities:**  
**New York Stock Exchange**

**PPL Corporation:**

Common Stock (Code: PPL)

7-3/4% PEPS<sup>SM</sup> Units

(Code: PPLPrE)

7-3/4% PEPS<sup>SM</sup> Units, Series B

(Code: PPLPrF)

**PPL Electric Utilities Corporation:**

4-1/2% Preferred Stock

(Code: PPLPRB)

4.40% Series Preferred Stock

(Code: PPLPRA)

**Philadelphia Stock Exchange**

**PPL Corporation:**

Common Stock

**Fiscal Agents:**  
**Stock Transfer Agents and Registrars**

Wells Fargo Bank Minnesota, N.A.

Shareowner Services

161 North Concord Exchange

South St. Paul, MN 55075-1139

PPL Services Corporation

Investor Services Department

**Dividend Disbursing Office and Dividend Reinvestment Plan Agent**

PPL Services Corporation

Investor Services Department

**Mortgage Bond Trustee**

Deutsche Bank Trust Company Americas

Attn: Security Transfer Unit

648 Grassmere Park Road

Nashville, TN 37211

**Indenture Trustee**

JPMorgan Chase Bank

450 West 33rd Street

New York, NY 10001

**Bond Interest Paying Agent**

PPL Services Corporation

Investor Services Department

SIGNATURES

Pursuant to the requirements of Section 13 or 15(d) of the Securities Exchange Act of 1934, the Registrant has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

PPL Corporation  
(Registrant)

By /s/ William F. Hecht

William F. Hecht -

Chairman, President  
and Chief Executive  
Officer

Pursuant to the requirements of the Securities Exchange Act of 1934, this report has been signed below by the following persons on behalf of the Registrant and in the capacities and on the date indicated.

TITLE

By /s/ William F. Hecht

Principal Executive Officer and Director

William F. Hecht -  
Chairman, President  
and Chief Executive  
Officer

By /s/ John R. Biggar

Principal Financial Officer and Director

John R. Biggar -  
Executive Vice President  
and Chief Financial Officer

By /s/ Mark D. Woods

Principal Accounting Officer

Mark D. Woods -  
Controller

Directors:

Frederick M. Bernthal  
John W. Conway  
E. Allen Deaver  
Louise K. Goeser

Stuart Heydt  
W. Keith Smith  
Susan M. Stalneckner

By /s/ William F. Hecht

William F. Hecht, Attorney-in-fact

Date: March 1, 2004

SIGNATURES

Pursuant to the requirements of Section 13 or 15(d) of the Securities Exchange Act of 1934, the Registrant has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

**PPL Energy Supply, LLC**  
(Registrant)

By /s/ William F. Hecht  
William F. Hecht -  
President

Pursuant to the requirements of the Securities Exchange Act of 1934, this report has been signed below by the following persons on behalf of the Registrant and in the capacities and on the date indicated.

TITLE

By /s/ William F. Hecht  
William F. Hecht -  
President

Principal Executive Officer and Manager

By /s/ James E. Abel  
James E. Abel -  
Treasurer

Principal Financial Officer and Manager

By /s/ Mark D. Woods  
Mark D. Woods -  
Controller

Principal Accounting Officer and Manager

Managers:

/s/ John R. Biggar  
John R. Biggar

/s/ Lawrence E. De Simone  
Lawrence E. De Simone

/s/ Robert J. Grey  
Robert J. Grey

Date: March 1, 2004

SIGNATURES

Pursuant to the requirements of Section 13 or 15(d) of the Securities Exchange Act of 1934, the Registrant has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

PPL Electric Utilities Corporation  
(Registrant)

By /s/ John F. Sipics  
John F. Sipics -  
President

Pursuant to the requirements of the Securities Exchange Act of 1934, this report has been signed below by the following persons on behalf of the Registrant and in the capacities and on the date indicated.

TITLE

By /s/ John F. Sipics  
John F. Sipics -  
President

Principal Executive Officer and Director

By /s/ James E. Abel  
James E. Abel -  
Treasurer

Principal Financial Officer

/s/ Mark D. Woods  
Mark D. Woods -  
Controller

Principal Accounting Officer

Directors:

/s/ William F. Hecht  
William F. Hecht

/s/ Dean A. Christiansen  
Dean A. Christiansen

/s/ Robert J. Grey  
Robert J. Grey

/s/ John R. Biggar  
John R. Biggar

/s/ Lawrence E. De Simone  
Lawrence E. De Simone

/s/ James H. Miller  
James H. Miller

/s/ Paul T. Champagne  
Paul T. Champagne

Date: March 1, 2004

**SIGNATURES**

Pursuant to the requirements of Section 13 or 15(d) of the Securities Exchange Act of 1934, the Registrant has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

**PPL Montana, LLC**  
(Registrant)

By /s/ James H. Miller  
James H. Miller -  
President

Pursuant to the requirements of the Securities Exchange Act of 1934, this report has been signed below by the following persons on behalf of the Registrant and in the capacities and on the date indicated.

**TITLE**

By /s/ James H. Miller  
James H. Miller -  
President

Principal Executive Officer and Manager

By /s/ James E. Abel  
James E. Abel -  
Treasurer

Principal Financial Officer and Manager

By /s/ Charles S. Baker  
Charles S. Baker -  
Controller

Principal Accounting Officer

Managers:

/s/ Albert J. Fioravanti  
Albert J. Fioravanti

/s/ Bradley E. Spencer  
Bradley E. Spencer

Date: March 1, 2004

## EXHIBIT INDEX

The following Exhibits indicated by an asterisk preceding the Exhibit number are filed herewith. The balance of the Exhibits have heretofore been filed with the Commission and pursuant to Rule 12(b)-32 are incorporated herein by reference. Exhibits indicated by a number in parentheses are filed or listed pursuant to Item 601(b)(10)(iii) of Regulation S-K.

- 3(a)-1 - Articles of Incorporation of PPL Corporation (Exhibit B to Proxy Statement of PPL Electric Utilities Corporation and Prospectus of PPL Corporation, dated March 9, 1995)
- 3(a)-2 - Articles of Amendment of PPL Corporation (Exhibit 3.2 to PPL Corporation Form S-3 (Registration Statement Nos. 333-54504, 333-54504-01 and 333-54504-02))
- 3(a)-3 - Amended and Restated Articles of Incorporation of PPL Electric Utilities Corporation (Exhibit 3(a)-3 to PPL Electric Utilities Corporation Form 10-K Report (File No. 1-905) for year ended December 31, 2001)
- 3(a)-4 - Certificate of Formation of PPL Energy Supply, LLC (Exhibit 3.1 to PPL Energy Supply, LLC Form S-4 (Registration Statement No. 333-74794))
- 3(a)-5 - Certificate of Formation of PPL Montana, LLC (Exhibit 3.1 to PPL Montana, LLC Form S-4 (Registration Statement No. 333-50350))
- 3(b)-1 - Bylaws of PPL Corporation (Exhibit 3(ii)(a) to PPL Corporation Form 10-Q Report (File No. 1-11459) for the quarter ended September 30, 1998)
- 3(b)-2 - Bylaws of PPL Electric Utilities Corporation (Exhibit 3(b)-2 to PPL Electric Utilities Corporation Form 10-K Report (File No. 1-905) for year ended December 31, 2001)
- 3(b)-3 - Limited Liability Company Agreement of PPL Energy Supply, LLC, dated March 20, 2001 (Exhibit 3.2 to PPL Energy Supply, LLC Form S-4 (Registration Statement No. 333-74794))
- 3(b)-4 - Limited Liability Company Agreement and Bylaws of PPL Montana, LLC, effective as of December 17, 1999 (Exhibit 3.2 to PPL Montana, LLC Form S-4 (Registration Statement No. 333-50350))
- 4(a)-1 - Amended and Restated Employee Stock Ownership Plan, effective January 1, 2000 (Exhibit 4(a) to PPL Corporation Form 10-K Report (File No. 1-11459) for year ended December 31, 2000)
- 4(a)-2 - Amendment No. 1 to said Employee Stock Ownership Plan, effective January 1, 2000 (Exhibit 4(a)-2 to PPL Corporation Form 10-K Report (File No. 1-11459) for year ended December 31, 2001)
- 4(a)-3 - Amendment No. 2 to said Employee Stock Ownership Plan, dated October 8, 2002 (Exhibit 4(a)-3 to PPL Corporation Form 10-K Report (File No. 1-11459) for year ended December 31, 2002)
- \*4(a)-4 - Amendment No. 3 to said Employee Stock Ownership Plan, dated April 1, 2003
- \*4(a)-5 - Amendment No. 4 to said Employee Stock Ownership Plan, dated May 7, 2003
- 4(b)-1 - Mortgage and Deed of Trust, dated as of October 1, 1945, between PPL Electric Utilities Corporation and Bankers Trust Company (as successor Trustee) (Exhibit 2(a)-4 to Registration Statement No. 2-60291)
- 4(b)-2 - Supplement, dated as of July 1, 1954, to said Mortgage and Deed of Trust (Exhibit 2(b)-5 to Registration Statement No. 219255)
- 4(b)-3 - Supplement, dated as of July 1, 1991, to said Mortgage and Deed of Trust (Exhibit 4(a) to PPL Electric Utilities Corporation Form 8-K Report (File No. 1-905) dated July 29, 1991)
- 4(b)-4 - Supplement, dated as of May 1, 1992, to said Mortgage and Deed of Trust (Exhibit 4(a) to PPL Electric Utilities Corporation Form 8-K Report (File No. 1-905) dated June 1, 1992)

- 4(b)-5 - Supplement, dated as of November 1, 1992, to said Mortgage and Deed of Trust (Exhibit 4(b)-29 to PPL Electric Utilities Corporation Form 10-K Report (File 1-905) for the year ended December 31, 1992)
- 4(b)-6 - Supplement, dated as of April 1, 1993, to said Mortgage and Deed of Trust (Exhibit 4(a) to PPL Electric Utilities Corporation Form 8-K Report (File No. 1-905) dated April 30, 1993)
- 4(b)-7 - Supplement, dated as of February 15, 1994, to said Mortgage and Deed of Trust (Exhibit 4(a) to PPL Electric Utilities Corporation Form 8-K Report (File No. 1-905) dated March 11, 1994)
- 4(b)-8 - Supplement, dated as of March 1, 1994, to said Mortgage and Deed of Trust (Exhibit 4(b) to PPL Electric Utilities Corporation Form 8-K Report (File No. 1-905) dated March 11, 1994)
- 4(b)-9 - Supplement, dated as of March 15, 1994, to said Mortgage and Deed of Trust (Exhibit 4(a) to PPL Electric Utilities Corporation Form 8-K Report (File No. 1-905) dated March 30, 1994)
- 4(b)-10 - Supplement, dated as of September 1, 1994, to said Mortgage and Deed of Trust (Exhibit 4(a) to PPL Electric Utilities Corporation Form 8-K (File No. 1-905) dated October 3, 1994)
- 4(b)-11 - Supplement, dated as of October 1, 1994, to said Mortgage and Deed of Trust (Exhibit 4(a) to PPL Electric Utilities Corporation Form 8-K Report (File No. 1-905) dated October 3, 1994)
- 4(b)-12 - Supplement, dated as of August 1, 1995, to said Mortgage and Deed of Trust (Exhibit 6(a) to PPL Electric Utilities Corporation Form 10-Q Report (File No. 1-905) for the quarter ended September 30, 1995)
- 4(b)-13 - Supplement, dated as of April 1, 1997, to said Mortgage and Deed of Trust (Exhibit 4(b)-17 to PPL Electric Utilities Corporation Form 10-K Report (File No. 1-905) for the year ended December 31, 1997)
- 4(b)-14 - Supplement, dated as of May 5, 1998, to said Mortgage and Deed of Trust (Exhibit 4.3 to PPL Electric Utilities Corporation Form 8-K Report (File No. 1-905) dated May 1, 1998)
- 4(b)-15 - Supplement, dated as of June 1, 1999, to said Mortgage and Deed of Trust (Exhibit 4(b)-19 to PPL Electric Utilities Corporation Form 10-K Report (File No. 1-905) for the year ended December 31, 1999)
- 4(b)-16 - Supplement, dated as of August 1, 2001, to said Mortgage and Deed of Trust (Exhibit 4.5 to PPL Electric Utilities Corporation Form 8-K Report (File No. 1-905) dated August 21, 2001)
- 4(b)-17 - Supplement, dated as of January 1, 2002, to said Mortgage and Deed of Trust (Exhibit 4(b)-19 to PPL Electric Utilities Corporation Form 10-K Report (File No. 1-905) for year ended December 31, 2001)
- 4(b)-18 - Supplement, dated as of February 1, 2003, to said Mortgage and Deed of Trust (Exhibit 4(b)-20 to PPL Electric Utilities Corporation Form 10-K Report (File No. 1-905) for year ended December 31, 2002)
- 4(b)-19 - Supplement, dated as of May 1, 2003, to said Mortgage and Deed of Trust (Exhibit 10(c) to PPL Electric Utilities Corporation Form 10-Q Report (File No. 1-905) for quarter ended June 30, 2003)
- 4(c)-1 - Indenture, dated as of November 1, 1997, among PPL Corporation, PPL Capital Funding, Inc. and JPMorgan Chase Bank (formerly The Chase Manhattan Bank), as Trustee (Exhibit 4.1 to PPL Corporation Form 8-K Report (File No. 1-11459) dated November 12, 1997)
- 4(c)-2 - Supplement, dated as of November 1, 1997, to said Indenture (Exhibit 4.2 to PPL Corporation Form 8-K Report (File No. 1-11459) dated November 12, 1997)
- 4(c)-3 - Supplement, dated as of March 1, 1999, to said Indenture (Exhibit 4.3 to Registration Statement Nos. 333-87847, 333-87847-01 and 333-87847-02)

- 4(c)-4 - Supplement, dated as of October 1, 1999, to said Indenture (Exhibit 4(c)-4 to PPL Corporation Form 10-K Report (File No. 1-11459) for the year ended December 31, 1999)
- 4(c)-5 - Supplement, dated as of June 1, 2000, to said Indenture (Exhibit 4 to PPL Corporation Form 10-Q Report (File No. 1-11459) for the quarter ended June 30, 2000)
- 4(c)-6 - Supplement, dated as of January 21, 2003, to said Indenture (Exhibit 99.1 to PPL Corporation Form 8-K Report (File No. 1-11459) dated January 22, 2003)
- 4(d)-1 - Junior Subordinated Indenture, dated as of April 1, 1997, between PPL Electric Utilities Corporation and JPMorgan Chase Bank (formerly The Chase Manhattan Bank), as Trustee (Exhibit 4.1 to Registration Statement No. 333-20661)
- 4(d)-2 - Amended and Restated Trust Agreement, dated as of April 8, 1997, among PPL Electric Utilities Corporation, JPMorgan Chase Bank (formerly The Chase Manhattan Bank), as Property Trustee, Chase Manhattan Bank (Delaware), as Delaware Trustee, and John R. Biggar and James E. Abel, as Administrative Trustees (Exhibit 4.4 to Registration Statement No. 333-20661)
- 4(d)-3 - Guarantee Agreement, dated as of April 8, 1997, between PPL Electric Utilities Corporation and JPMorgan Chase Bank (formerly The Chase Manhattan Bank), as Trustee (Exhibit 4.6 to Registration Statement No. 333-20661)
- 4(e)-1 - Amended and Restated Trust Agreement, dated as of June 13, 1997, among PPL Electric Utilities Corporation, JPMorgan Chase Bank (formerly The Chase Manhattan Bank), as Property Trustee, Chase Manhattan Bank (Delaware), as Delaware Trustee, and John R. Biggar and James E. Abel, as Administrative Trustees (Exhibit 4.4 to Registration Statement No. 333-27773)
- 4(e)-2 - Guarantee Agreement, dated as of June 13, 1997, between PPL Electric Utilities Corporation and JPMorgan Chase Bank (formerly The Chase Manhattan Bank), as Trustee (Exhibit 4.6 to Registration Statement No. 333-27773)
- 4(f)-1 - Subordinated Indenture, dated as of May 9, 2001, between PPL Capital Funding, Inc., PPL Corporation and JPMorgan Chase Bank (formerly The Chase Manhattan Bank), as Trustee (Exhibit 4.1 to PPL Corporation Form 8-K Report (File No. 1-11459) dated May 9, 2001)
- 4(f)-2 - Supplement, dated as of May 9, 2001, to said Subordinated Indenture (Exhibit 4.2 to PPL Corporation Form 8-K Report (File No. 1-11459) dated May 9, 2001)
- 4(f)-3 - Trust Securities Guarantee Agreement, dated as of May 9, 2001 (Exhibit 4.10 to PPL Corporation Form 8-K Report (File No. 1-11459) dated May 9, 2001)
- 4(f)-4 - Amended and Restated Trust Agreement, dated as of May 9, 2001, among PPL Corporation, PPL Capital Funding, Inc., JPMorgan Chase Bank (formerly The Chase Manhattan Bank), as Property Trustee, Chase Manhattan Bank USA National Association, as Delaware Trustee, John R. Biggar and James E. Abel, as Administrative Trustees, and the several Holders of the Trust Securities (Exhibit 4.8 to PPL Corporation Form 8-K Report (File No. 1-11459) dated May 9, 2001)
- 4(g)-1 - Indenture, dated as of August 1, 2001, by PPL Electric Utilities Corporation and JPMorgan Chase Bank (formerly The Chase Manhattan Bank), as Trustee (Exhibit 4.1 to PPL Electric Utilities Corporation Form 8-K Report (File No. 1-905) dated August 21, 2001)
- 4(g)-2 - Supplement, dated as of August 1, 2001, to said Indenture (Exhibit 4.2 to PPL Electric Utilities Corporation Form 8-K Report (File No. 1-905) dated August 21, 2001)
- 4(g)-3 - Supplement, dated as of February 1, 2003, to said Indenture (Exhibit 4(g)-3 to PPL Electric Utilities Corporation Form 10-K Report (File No. 1-905) for the year ended December 31, 2002)

- 4(g)-4 - Supplement, dated as of May 1, 2003, to said Indenture (Exhibit 10(d) to PPL Electric Utilities Corporation Form 10-Q Report (File No. 1-905) for the quarter ended June 30, 2002)
- 4(h)-1 - Indenture, dated as of October 1, 2001, by PPL Energy Supply, LLC and JPMorgan Chase Bank (formerly The Chase Manhattan Bank), as Trustee (Exhibit 4.1 to PPL Energy Supply, LLC Form S-4 (Registration Statement No. 333-74794))
- 4(h)-2 - Supplement, dated as of October 1, 2001, to said Indenture (Exhibit 4.2 to PPL Energy Supply, LLC Form S-4 (Registration Statement No. 333-74794))
- 4(h)-3 - Registration Rights Agreement between PPL Energy Supply, LLC and the Initial Purchasers (Exhibit 4.5 to PPL Energy Supply, LLC Form S-4 (Registration Statement No. 333-74794))
- 4(h)-4 - Registration Rights Agreement, dated as of May 21, 2003, by PPL Energy Supply, LLC, PPL Corporation and the Representatives of the Initial Purchasers (Exhibit 4.2 to PPL Energy Supply, LLC and PPL Corporation Form S-4 (Registration Statement No. 333-106200))
- 4(h)-5 - Indenture, dated as of May 21, 2003, by PPL Energy Supply, LLC, PPL Corporation and JPMorgan Chase Bank, as Trustee (Exhibit 4.3 to PPL Energy Supply, LLC and PPL Corporation Form S-4 (Registration Statement No. 333-106200))
- 10(a) - \$300 million Three-Year Credit Agreement, dated as of June 25, 2002, among PPL Energy Supply, LLC and the banks named therein (Exhibit 10(b) to PPL Energy Supply, LLC Form 10-Q Report (File No. 333-74794) for the quarter ended June 30, 2002)
- 10(b) - \$300 million Three-Year Credit Agreement, dated as of June 24, 2003, among PPL Energy Supply, LLC and the banks named therein (Exhibit 10(e) to PPL Energy Supply, LLC Form 10-Q Report (File No. 333-74794) for the quarter ended June 30, 2003)
- 10(c) - \$100 million Three-Year Credit Agreement, dated as of June 24, 2003, among PPL Electric Utilities Corporation and the banks named therein (Exhibit 10(f) to PPL Electric Utilities Corporation Form 10-Q Report (File No. 1-905) for the quarter ended June 30, 2003)
- 10(d) - \$200 million 364-Day Credit Agreement, dated as of June 24, 2003, among PPL Electric Utilities Corporation and the banks named therein (Exhibit 10(g) to PPL Electric Utilities Corporation Form 10-Q Report (File No. 1-905) for the quarter ended June 30, 2003)
- 10(e) - Credit Agreement dated as of October 31, 2002, among PPL Montana, LLC and PPL Investment Corporation (Exhibit 10(h) to PPL Montana, LLC Form 10-Q Report (File No. 333-50350) for the quarter ended June 30, 2003)
- 10(f) - \$150 Million Credit and Reimbursement Agreement, dated as of April 25, 2001, among PPL Montana, LLC and the banks named therein (Exhibit 10(d) to PPL Montana, LLC Form 10-Q Report (File No. 333-50350) for the quarter ended June 30, 2001)
- 10(g) - Generation Supply Agreement, dated as of June 20, 2001, between PPL Electric Utilities Corporation and PPL EnergyPlus, LLC (Exhibit 10.5 to PPL Energy Supply, LLC Form S-4 (Registration Statement No. 333-74794))
- 10(h) - Master Power Purchase and Sale Agreement, dated as of October 15, 2001, between The Montana Power Company and PPL Montana, LLC (Exhibit 10(g) to PPL Montana, LLC Form 10-K Report (File No. 333-50350) for year ended December 31, 2002)
- 10(i) - Amended and Restated Parent Guaranty, dated as of November 30, 2000, by PPL Corporation in favor of Large Scale Distributed Generation Statutory Trust (Exhibit 10(h) to PPL Corporation Form 10-K Report (File No. 1-11459) for year ended December 31, 2001)

- 10(j) - Amended and Restated PPL Energy Supply, LLC Guarantee, dated as of July 17, 2001, in favor of Large Scale Distributed Generation II Statutory Trust (Exhibit 10.6 to PPL Energy Supply, LLC Form S-4 (Registration Statement No. 333-74794))
- 10(k) - Amended and Restated Participation Agreement, dated as of July 17, 2001, among PPL Large Scale Distributed Generation II, LLC, Large Scale Distributed Generation II Statutory Trust, State Street Bank and Trust Company of Connecticut, National Association, as Trustee, First Union National Bank, as Administrative Agent, and the Financial Institutions named therein in the capacities indicated therein
- 10(l) - Guaranty, dated as of December 21, 2001, from PPL Energy Supply, LLC in favor of LMB Funding, Limited Partnership (Exhibit 10(j) to PPL Energy Supply, LLC Form 10-K Report (File No. 333-74794) for year ended December 31, 2001)
- \*10(m) - Agreement for Lease, dated as of December 21, 2001, between LMB Funding, Limited Partnership and Lower Mt. Bethel Energy, LLC
- \*10(m)-1 - Amendment No. 1 to Agreement for Lease, dated as of September 16, 2002, between LMB Funding, Limited Partnership and Lower Mt. Bethel Energy, LLC
- \*10(n) - Lease Agreement, dated as of December 21, 2001, between LMB Funding, Limited Partnership and Lower Mt. Bethel Energy, LLC
- \*10(n)-1 - Amendment No. 1 to Lease Agreement, dated as of September 16, 2002, between LMB Funding, Limited Partnership and Lower Mt. Bethel Energy, LLC
- 10(o) - Pollution Control Facilities Agreement, dated as of May 1, 1973, between PPL Electric Utilities Corporation and the Lehigh County Industrial Development Authority (Exhibit 5(z) to Registration Statement No. 2-60834)
- 10(p) - Amended and Restated Operating Agreement of the PJM Interconnection, LLC, dated February 6, 2002 (Exhibit 10(l) to PPL Corporation Form 10-K Report (File No. 1-11459) for year ended December 31, 2001)
- 10(q) - Amended and Restated Directors Deferred Compensation Plan, dated February 14, 2000 (Exhibit 10(h) to PPL Corporation Form 10-K Report (File No. 1-11459) for year ended December 31, 2000)
- 10(q)-1 - Amendment No. 1 to Amended and Restated Directors Deferred Compensation Plan, dated December 18, 2002 (Exhibit 10(m)-1 to PPL Corporation Form 10-K Report (File No. 1-11459) for year ended December 31, 2002)
- \* 10(q)-2 - Amendment No. 2 to Amended and Restated Directors Deferred Compensation Plan, dated January 1, 2004
- \* 10(r) - Amended and Restated Officers Deferred Compensation Plan, effective November 1, 2003
- \* 10(s) - Amended and Restated Supplemental Executive Retirement Plan, effective July 1, 2003
- 10(t) - Incentive Compensation Plan, amended and restated effective January 1, 2003 (Exhibit 10(p) to PPL Corporation Form 10-K Report (File No. 1-11459) for year ended December 31, 2002)
- 10(u) - Incentive Compensation Plan for Key Employees, amended and restated effective January 1, 2003 (Schedule B to Proxy Statement of PPL Corporation, dated March 17, 2003)
- 10(v) - Short-term Incentive Plan (Schedule B to Proxy Statement of PPL Corporation, dated March 12, 1999)
- 10(w) - Form of Severance Agreement entered into between PPL Corporation and the Executive Officers listed in this Form 10-K Report (Exhibit 10(r) to PPL Corporation Form 10-K Report (File No. 1-11459) for year ended December 31, 2001)

- 10(x) - Form for Retention Agreement entered into between PPL Corporation and Messrs. Champagne, De Simone, Miller and Petersen (Exhibit 10(s) to PPL Corporation Form 10-K Report (File No. 1-11459) for year ended December 31, 2001)
- 10(y) - Agreement dated January 15, 2003 between PPL Corporation and Mr. Miller regarding Supplemental Pension Benefits (Exhibit 10(u) to PPL Corporation Form 10-K Report (File No. 1-11459) for year ended December 31, 2002)
- 10(z) - Equity Contribution Agreement, among PPL Corporation, PPL Montana, LLC, and The Chase Manhattan Bank, as Trustee (Exhibit 10.15 to PPL Montana, LLC Form S-4 (Registration Statement No. 333-50350))
- 10(aa) - Facility Lease Agreement (BA 1/2) between PPL Montana, LLC and Montana OL3, LLC (Exhibit 4.7a to PPL Montana, LLC Form S-4 (Registration Statement No. 333-50350))
- 10(bb) - Facility Lease Agreement (BA 3) between PPL Montana, LLC and Montana OL4, LLC (Exhibit 4.8a to PPL Montana, LLC Form S-4 (Registration Statement No. 333-50350))
- 10(cc) - Services Agreement, dated as of July 1, 2000, among PPL Corporation, PPL Energy Funding Corporation and its direct and indirect subsidiaries in various tiers, PPL Capital Funding, Inc., PPL Gas Utilities Corporation, PPL Services Corporation and CEP Commerce, LLC (Exhibit 10.20 to PPL Energy Supply, LLC Form S-4 (Registration Statement No. 333-74794))
- 10(dd) - Pollution Control Facilities Loan Agreement, dated as of February 1, 2003, between PPL Electric Utilities Corporation and the Lehigh County Industrial Development Authority
- \*12(a) - PPL Corporation and Subsidiaries Computation of Ratio of Earnings to Fixed Charges
- \*12(b) - PPL Energy Supply, LLC and Subsidiaries Computation of Ratio of Earnings to Fixed Charges
- \*12(c) - PPL Electric Utilities Corporation and Subsidiaries Computation of Ratio of Earnings to Fixed Charges
- \*12(d) - PPL Montana, LLC and Subsidiaries Computation of Ratio of Earnings to Fixed Charges
- \*21(a) - Subsidiaries of PPL Corporation
- \*21(b) - Subsidiaries of PPL Electric Utilities Corporation
- \*23(a) - Consent of PricewaterhouseCoopers LLP - PPL Corporation
- \*23(b) - Consent of PricewaterhouseCoopers LLP - PPL Energy Supply, LLC
- \*23(c) - Consent of PricewaterhouseCoopers LLP - PPL Electric Utilities Corporation
- \*24 - Power of Attorney
- \*31(a) - Certificate of PPL's principal executive officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002
- \*31(b) - Certificate of PPL's principal financial officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002
- \*31(c) - Certificate of PPL Energy Supply's principal executive officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002
- \*31(d) - Certificate of PPL Energy Supply's principal financial officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002

- \*31(e) - Certificate of PPL Electric's principal executive officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002
- (f) - Certificate of PPL Electric's principal financial officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002
- \*31(g) - Certificate of PPL Montana's principal executive officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002
- \*31(h) - Certificate of PPL Montana's principal financial officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002
- \*32(a) - Certificate of PPL's principal executive officer pursuant to Section 906 of the Sarbanes-Oxley Act of 2002
- \*32(b) - Certificate of PPL's principal financial officer pursuant to Section 906 of the Sarbanes-Oxley Act of 2002
- \*32(c) - Certificate of PPL Energy Supply's principal executive officer pursuant to Section 906 of the Sarbanes-Oxley Act of 2002
- \*32(d) - Certificate of PPL Energy Supply's principal financial officer pursuant to Section 906 of the Sarbanes-Oxley Act of 2002
- \*32(e) - Certificate of PPL Electric's principal executive officer pursuant to Section 906 of the Sarbanes-Oxley Act of 2002
- \*32(f) - Certificate of PPL Electric's principal financial officer pursuant to Section 906 of the Sarbanes-Oxley Act of 2002
- 2(g) - Certificate of PPL Montana's principal executive officer pursuant to Section 906 of the Sarbanes-Oxley Act of 2002
- \*32(h) - Certificate of PPL Montana's principal financial officer pursuant to Section 906 of the Sarbanes-Oxley Act of 2002
- \*99 - PPL Corporate Organization (Selected Subsidiaries)

## PPL CORPORATION AND SUBSIDIARIES

COMPUTATION OF RATIO OF EARNINGS TO COMBINED FIXED CHARGES AND  
PREFERRED STOCK DIVIDENDS

(Millions of Dollars)

	<u>2003</u>	<u>2002</u>	<u>2001</u>	<u>2000</u>	<u>1999</u>
Fixed charges, as defined:					
Interest on long-term debt.....	\$ 417	\$ 486	\$ 351	\$ 323	\$ 233
Interest on short-term debt and other interest .....	25	71	44	64	47
Amortization of debt discount, expense and premium - net .....	41	25	17	5	4
Interest on capital lease obligations Charged to expense .....				4	9
Capitalized.....					1
Estimated interest component of operating rentals.....	52	39	36	25	20
Preferred security distributions of subsidiaries on a pre-tax basis.....	45	79	64	31	30
<b>Total fixed charges .....</b>	<b>\$ 580</b>	<b>\$ 700</b>	<b>\$ 512</b>	<b>\$ 452</b>	<b>\$ 344</b>
Earnings, as defined:					
Net income (a) .....	\$ 726	\$ 438	\$ 167	\$ 491	\$ 492
Preferred security dividend requirements .....	29	67	52	26	26
Less undistributed income (loss) of equity method investments .....	(18)	(23)	20	74	56
	773	528	199	443	462
Add:					
Income taxes .....	170	210	261	294	174
Amortization of capitalized interest on capital leases .....				2	2
Total fixed charges as above (excluding capitalized interest, capitalized interest on capital lease obligations and preferred security distributions of subsidiaries on a pre-tax basis).....	528	600	419	405	307
<b>Total earnings .....</b>	<b>\$ 1,471</b>	<b>\$ 1,338</b>	<b>\$ 879</b>	<b>\$ 1,144</b>	<b>\$ 945</b>
Ratio of earnings to fixed charges .....	<u>2.5</u>	<u>1.9</u>	<u>1.7</u>	<u>2.5</u>	<u>2.7</u>
Ratio of earnings to combined fixed charges and preferred stock dividends (b).....	<u>2.5</u>	<u>1.9</u>	<u>1.7</u>	<u>2.5</u>	<u>2.7</u>

(a) Net income excludes extraordinary item, minority interest, loss from discontinued operations and the cumulative effects of changes in accounting principles.

(b) PPL, the parent holding company, does not have any preferred stock outstanding; therefore, the ratio of earnings to combined fixed charges and preferred stock dividends is the same as the ratio of earnings to fixed charges.

## PPL ENERGY SUPPLY, LLC AND SUBSIDIARIES

## COMPUTATION OF RATIO OF EARNINGS TO FIXED CHARGES

(Millions of Dollars)

	2003 (b)	2002 (b)	2001 (b)	2000 (b)	1999
<b>Fixed charges, as defined:</b>					
Interest on long-term debt.....	\$ 149	\$ 169	\$ 36	\$ 54	\$ 20
Interest on short-term debt and other interest .....	25	52	33	75	32
Amortization of debt discount, expense and premium - net .....	31	9	2	11	1
Estimated interest component of operating rentals.....	38	23	19	9	
Preferred security distributions of subsidiaries on a pre-tax basis.....	8	12			
<b>Total fixed charges .....</b>	<b><u>\$ 251</u></b>	<b><u>\$ 265</u></b>	<b><u>\$ 90</u></b>	<b><u>\$ 149</u></b>	<b><u>\$ 53</u></b>
<b>Earnings, as defined:</b>					
Net income (loss) (a).....	\$ 719	\$ 509	\$ 168	\$ 246	\$ (20)
Preferred security dividend requirement.....	5	9			
Less undistributed income (loss) of equity method investments .....	(15)	(22)	20	74	56
	739	540	148	172	(76)
Income taxes (benefit) .....	185	266	274	125	(29)
<b>Total fixed charges as above (excluding capitalized interest and preferred security distributions of subsidiaries on a pre-tax basis) .....</b>	<b><u>237</u></b>	<b><u>234</u></b>	<b><u>66</u></b>	<b><u>135</u></b>	<b><u>52</u></b>
<b>Total earnings .....</b>	<b><u>\$ 1,161</u></b>	<b><u>\$ 1,040</u></b>	<b><u>\$ 488</u></b>	<b><u>\$ 432</u></b>	<b><u>\$ (53)</u></b>
<b>Ratio of earnings to fixed charges .....</b>	<b><u>4.6</u></b>	<b><u>3.9</u></b>	<b><u>5.4</u></b>	<b><u>2.9</u></b>	<b><u>(1.0)</u></b>
<b>Deficiency.....</b>				<b><u>\$ 106</u></b>	

(a) Net income (loss) excludes minority interest, loss from discontinued operations and the cumulative effects of changes in accounting principles.

(b) Due to the corporate realignment on July 1, 2000, data in 2000 and subsequent years are not comparable to 1999.

## PPL ELECTRIC UTILITIES CORPORATION AND SUBSIDIARIES

## COMPUTATION OF RATIO OF EARNINGS TO FIXED CHARGES

(Millions of Dollars)

	<u>2003 (b)</u>	<u>2002 (b)</u>	<u>2001 (b)</u>	<u>2000 (b)</u>	<u>1999</u>
Fixed charges, as defined:					
Interest on long-term debt.....	\$ 201	\$ 209	\$ 220	\$ 223	\$ 205
Interest on short-term debt and other interest .....	3	3	4	16	12
Amortization of debt discount, expense and premium - net .....	8	7	6	4	3
Interest on capital lease obligations					
Charged to expense .....				4	9
Capitalized .....					1
Estimated interest component of operating rentals.....	7	7	8	14	19
Preferred security distributions of subsidiaries on a pre-tax basis.....		13	23	23	23
Total fixed charges .....	<u>\$ 219</u>	<u>\$ 239</u>	<u>\$ 261</u>	<u>\$ 284</u>	<u>\$ 272</u>
Earnings, as defined:					
Net income (a) .....	\$ 25	\$ 39	\$ 114	\$ 250	\$ 444
Preferred security dividend requirements .....	3	16	26	26	37
Total earnings .....	<u>28</u>	<u>55</u>	<u>140</u>	<u>276</u>	<u>481</u>
Add:					
Income taxes .....	18	18	65	171	151
Amortization of capitalized interest on capital leases .....				2	2
Total fixed charges as above (excluding capitalized interest, capitalized interest on capital lease obligations and preferred security distributions of subsidiaries on a pre-tax basis).....	<u>219</u>	<u>225</u>	<u>238</u>	<u>257</u>	<u>243</u>
Total earnings .....	<u>\$ 265</u>	<u>\$ 298</u>	<u>\$ 443</u>	<u>\$ 706</u>	<u>\$ 877</u>
Ratio of earnings to fixed charges .....	<u>1.2</u>	<u>1.2</u>	<u>1.7</u>	<u>2.5</u>	<u>3.2</u>

(a) Net income excludes extraordinary item and the cumulative effect of a change in accounting principle.

(b) Due to the corporate realignment on July 1, 2000, data in 2000 and subsequent years are not comparable to 1999.

## PPL MONTANA, LLC AND SUBSIDIARIES

## COMPUTATION OF RATIO OF EARNINGS TO FIXED CHARGES

(Millions of Dollars)

	<u>2003</u>	<u>2002</u>	<u>2001</u>	<u>2000</u>
Fixed charges, as defined:				
Interest expense on credit facility.....	\$ 1	\$ 2	\$ 2	\$ 18
Amortization of debt expenses.....			1	3
Amortization of wholesale energy commitments.....	4	4	6	7
Estimated interest component of operating rentals .....	<u>15</u>	<u>15</u>	<u>15</u>	<u>6</u>
Total fixed charges .....	<u>\$ 20</u>	<u>\$ 21</u>	<u>\$ 24</u>	<u>\$ 34</u>
Earnings, as defined:				
Net income (a).....	\$ 69	\$ 47	\$ 103	\$ 86
Add:				
Income taxes .....	45	35	68	57
Total fixed charges as above .....	<u>20</u>	<u>21</u>	<u>24</u>	<u>34</u>
Total earnings.....	<u>\$ 134</u>	<u>\$ 103</u>	<u>\$ 195</u>	<u>\$ 177</u>
Ratio of earnings to fixed charges .....	<u>6.7</u>	<u>4.9</u>	<u>8.1</u>	<u>5.2</u>

(a) Net income excludes extraordinary item and the cumulative effect of a change in accounting principle.

CERTIFICATION

I, WILLIAM F. HECHT, the principal executive officer of PPL Corporation (the "registrant"), certify that:

1. I have reviewed this annual report on Form 10-K of the registrant for the year ended December 31, 2003;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) for the registrant and have:
  - a. Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
  - b. Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
  - c. Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and
5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):
  - a. All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
  - b. Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: March 1, 2004

/s/ William F. Hecht  
William F. Hecht  
Chairman, President and Chief Executive Officer  
PPL Corporation

CERTIFICATION

I, JOHN R. BIGGAR, the principal financial officer of PPL Corporation (the "registrant"), certify that:

1. I have reviewed this annual report on Form 10-K of the registrant for the year ended December 31, 2003;
2. **Based on my knowledge**, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) for the registrant and have:
  - a. Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
  - b. Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
  - c. Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and
5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):
  - a. All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
  - b. Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: March 1, 2004

/s/ John R. Biggar  
John R. Biggar  
Executive Vice President and Chief Financial Officer  
PPL Corporation

CERTIFICATION

I, WILLIAM F. HECHT, the principal executive officer of PPL Energy Supply, LLC (the "registrant"), certify that:

1. I have reviewed this annual report on Form 10-K of the registrant for the year ended December 31, 2003;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) for the registrant and have:
  - a. Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
  - b. Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
  - c. Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and
5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):
  - a. All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
  - b. Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: March 1, 2004

/s/ William F. Hecht

William F. Hecht

President

PPL Energy Supply, LLC

CERTIFICATION

I, JAMES E. ABEL, the principal financial officer of PPL Energy Supply, LLC (the "registrant"), certify that:

1. I have reviewed this annual report on Form 10-K of the registrant for the year ended December 31, 2003;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) for the registrant and have:
  - a. Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
  - b. Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
  - c. Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and
5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):
  - a. All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
  - b. Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: March 1, 2004

/s/ James E. Abel

James E. Abel

Treasurer

PPL Energy Supply, LLC

CERTIFICATION

I, JOHN F. SIPICS, the principal executive officer of PPL Electric Utilities Corporation (the "registrant"), certify that:

1. I have reviewed this annual report on Form 10-K of the registrant for the year ended December 31, 2003;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) for the registrant and have:
  - a. Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
  - b. Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
  - c. Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and
5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):
  - a. All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
  - b. Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: March 1, 2004

/s/ John F. Sipics

John F. Sipics

President

PPL Electric Utilities Corporation

CERTIFICATION

I, JAMES E. ABEL, the principal financial officer of PPL Electric Utilities Corporation (the "registrant"), certify that:

1. I have reviewed this annual report on Form 10-K of the registrant for the year ended December 31, 2003;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) for the registrant and have:
  - a. Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
  - b. Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
  - c. Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and
5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):
  - a. All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
  - b. Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: March 1, 2004

/s/ James E. Abel  
James E. Abel  
Treasurer  
PPL Electric Utilities Corporation

CERTIFICATION

I, JAMES H. MILLER, the principal executive officer of PPL Montana, LLC (the "registrant"), certify that:

1. I have reviewed this annual report on Form 10-K of the registrant for the year ended December 31, 2003;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) for the registrant and have:
  - a. Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
  - b. Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
  - c. Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and
5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):
  - a. All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
  - b. Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: March 1, 2004

/s/ James H. Miller

James H. Miller  
President  
PPL Montana, LLC

CERTIFICATION

I, JAMES E. ABEL, the principal financial officer of PPL Montana, LLC (the "registrant"), certify that:

1. I have reviewed this annual report on Form 10-K of the registrant for the year ended December 31, 2003;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) for the registrant and have:
  - a. Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
  - b. Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
  - c. Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and
5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):
  - a. All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
  - b. Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: March 1, 2004

/s/ James E. Abel

James E. Abel

Treasurer

PPL Montana, LLC

CERTIFICATE PURSUANT TO 18 U.S.C. SECTION 1350  
AS ADOPTED PURSUANT TO SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002  
FOR PPL CORPORATION'S 10-K FOR THE YEAR ENDED DECEMBER 31, 2003

In connection with the annual report on Form 10-K of PPL Corporation (the "Company") for the year ended December 31, 2003, as filed with the Securities and Exchange Commission on the date hereof (the "Covered Report"), I, the principal executive officer of the Company, pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, hereby certify that:

- The Covered Report fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934, as amended; and
- The information contained in the Covered Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

Date: March 1, 2004

/s/ William F. Hecht

William F. Hecht  
Chairman, President and  
Chief Executive Officer  
PPL Corporation

A signed original of this written statement required by Section 906 has been provided to the Company and will be retained by the Company and furnished to the Securities and Exchange Commission or its staff upon request.

CERTIFICATE PURSUANT TO 18 U.S.C. SECTION 1350  
AS ADOPTED PURSUANT TO SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002  
FOR PPL CORPORATION'S 10-K FOR THE YEAR ENDED DECEMBER 31, 2003

In connection with the annual report on Form 10-K of PPL Corporation (the "Company") for the year ended December 31, 2003, as filed with the Securities and Exchange Commission on the date hereof (the "Covered Report"), I, the principal financial officer of the Company, pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, hereby certify that:

- The Covered Report fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934, as amended; and
- The information contained in the Covered Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

Date: March 1, 2004

/s/ John R. Biggar

John R. Biggar  
Executive Vice President and  
Chief Financial Officer  
PPL Corporation

A signed original of this written statement required by Section 906 has been provided to the Company and will be retained by the Company and furnished to the Securities and Exchange Commission or its staff upon request.

CERTIFICATE PURSUANT TO 18 U.S.C. SECTION 1350  
AS ADOPTED PURSUANT TO SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002  
FOR PPL ENERGY SUPPLY, LLC'S 10-K FOR THE YEAR ENDED DECEMBER 31, 2003

In connection with the annual report on Form 10-K of PPL Energy Supply, LLC (the "Company") for the year ended December 31, 2003, as filed with the Securities and Exchange Commission on the date hereof (the "Covered Report"), I, the principal executive officer of the Company, pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, hereby certify that:

- The Covered Report fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934, as amended; and
- The information contained in the Covered Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

Date: March 1, 2004

/s/ William F. Hecht

William F. Hecht

President

PPL Energy Supply, LLC

A signed original of this written statement required by Section 906 has been provided to the Company and will be retained by the Company and furnished to the Securities and Exchange Commission or its staff upon request.

CERTIFICATE PURSUANT TO 18 U.S.C. SECTION 1350  
AS ADOPTED PURSUANT TO SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002  
FOR PPL ENERGY SUPPLY'S 10-K FOR THE YEAR ENDED DECEMBER 31, 2003

In connection with the annual report on Form 10-K of PPL Energy Supply, LLC (the "Company") for the year ended December 31, 2003, as filed with the Securities and Exchange Commission on the date hereof (the "Covered Report"), I, the principal financial officer of the Company, pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, hereby certify that:

- The Covered Report fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934, as amended; and
- The information contained in the Covered Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

Date: March 1, 2004

/s/ James E. Abel  
James E. Abel  
Treasurer  
PPL Energy Supply, LLC

A signed original of this written statement required by Section 906 has been provided to the Company and will be retained by the Company and furnished to the Securities and Exchange Commission or its staff upon request.

CERTIFICATE PURSUANT TO 18 U.S.C. SECTION 1350  
AS ADOPTED PURSUANT TO SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002  
FOR PPL ELECTRIC UTILITIES CORPORATION'S 10-K FOR THE YEAR ENDED DECEMBER 31, 2003

In connection with the annual report on Form 10-K of PPL Electric Utilities Corporation (the "Company") for the year ended December 31, 2003, as filed with the Securities and Exchange Commission on the date hereof (the "Covered Report"), I, the principal executive officer of the Company, pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, hereby certify that:

- The Covered Report fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934, as amended; and
- The information contained in the Covered Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

Date: March 1, 2004

/s/ John F. Sipics  
John F. Sipics  
President  
PPL Electric Utilities Corporation

A signed original of this written statement required by Section 906 has been provided to the Company and will be retained by the Company and furnished to the Securities and Exchange Commission or its staff upon request.

CERTIFICATE PURSUANT TO 18 U.S.C. SECTION 1350  
AS ADOPTED PURSUANT TO SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002  
FOR PPL ELECTRIC UTILITIES CORPORATION'S 10-K FOR THE YEAR ENDED DECEMBER 31, 2003

In connection with the annual report on Form 10-K of PPL Electric Utilities Corporation (the "Company") for the year ended December 31, 2003, as filed with the Securities and Exchange Commission on the date hereof (the "Covered Report"), I, the principal financial officer of the Company, pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, hereby certify that:

- The Covered Report fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934, as amended; and
- The information contained in the Covered Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

Date: March 1, 2004

/s/ James E. Abel  
James E. Abel  
Treasurer  
PPL Electric Utilities Corporation

A signed original of this written statement required by Section 906 has been provided to the Company and will be retained by the Company and furnished to the Securities and Exchange Commission or its staff upon request.

CERTIFICATE PURSUANT TO 18 U.S.C. SECTION 1350  
AS ADOPTED PURSUANT TO SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002  
FOR PPL MONTANA, LLC'S 10-K FOR THE YEAR ENDED DECEMBER 31, 2003

In connection with the annual report on Form 10-K of PPL Montana, LLC (the "Company") for the year ended December 31, 2003, as filed with the Securities and Exchange Commission on the date hereof (the "Covered Report"), I, the principal executive officer of the Company, pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, hereby certify that:

- The Covered Report fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934, as amended; and
- The information contained in the Covered Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

Date: March 1, 2004

/s/ James H. Miller

James H. Miller

President

PPL Montana, LLC

A signed original of this written statement required by Section 906 has been provided to the Company and will be retained by the Company and furnished to the Securities and Exchange Commission or its staff upon request.

CERTIFICATE PURSUANT TO 18 U.S.C. SECTION 1350  
AS ADOPTED PURSUANT TO SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002  
FOR PPL MONTANA, LLC'S 10-K FOR THE YEAR ENDED DECEMBER 31, 2003

In connection with the annual report on Form 10-K of PPL Montana, LLC (the "Company") for the year ended December 31, 2003, as filed with the Securities and Exchange Commission on the date hereof (the "Covered Report"), I, the principal financial officer of the Company, pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, hereby certify that:

- The Covered Report fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934, as amended; and
- The information contained in the Covered Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

Date: March 1, 2004

/s/ James E. Abel  
James E. Abel  
Treasurer  
PPL Montana, LLC

A signed original of this written statement required by Section 906 has been provided to the Company and will be retained by the Company and furnished to the Securities and Exchange Commission or its staff upon request.

**PPL Corporation - Corporate Organization**  
**(Selected Subsidiaries)**

## PPL Corporation

PPL Electric Utilities Corporation

PPL Transition Bond Company, LLC

CEP Commerce, LLC

PPL Gas Utilities Corporation

PPL Services Corporation

PPL Capital Funding, Inc.

PPL Properties, Inc.

Ninth Street &amp; Hamilton Corporation

PPL Energy Funding Corporation

CEP Reserves, Inc.

PPL Ventures, LLC

PPLSolutions, LLC

PPL Telcom, LLC

PPL Energy Supply, LLC

PPL Investment Corporation

PPL Global, LLC

PMDC Chile, Inc. *(includes Emel)*PPLG U.S. Latin America, Inc. *(includes Elfec and Integra)*PPLG El Salvador *(includes EC)*PMDC International Holdings, Inc. *(includes WPD)*

PPL EnergyPlus, LLC

PPL Synfuel Investments, LLC

PPL Energy Services Holdings, LLC

PPL Generation, LLC

PPL Holtwood, LLC

PPL Maine, LLC

PPL Interstate Energy Company

PPL Montana Holdings, LLC *(includes PPL Montana)*

PPL Susquehanna, LLC

PPL Martins Creek, LLC

PPL Brunner Island, LLC

PPL Montour, LLC

PPL Rights, Inc. *(jointly owned by PPL Montour, PPL Martins Creek and PPL Brunner Island)*

Lower Mount Bethel Energy, LLC

PPL Wallingford Energy LLC

PPL Sundance Energy, LLC

PPL Shoreham Energy, LLC

PPL Edgewood Energy, LLC

PPL Southwest Generation Holdings, LLC *(50% owner of Griffith Energy)*

PPL Coal Holdings Corporation

PPL Midwest Holdings, LLC *(includes University Park)*

Q.2. Supply projected capital requirements and sources of the filing utility, its parent and system - consolidated - for the test year and each of 3 comparable future years.

A.2. Attachment III-F-2 provides the requested information.

**PPL ELECTRIC UTILITIES CORPORATION**  
**REQUIREMENTS AND SOURCES OF FUNDS <sup>1/</sup>**

	<u>2004</u>	<u>2005</u>	<u>2006</u>	<u>2007</u>
<b>Capital Requirements</b>	(Millions of Dollars)			
Construction	\$ 166	\$ 183	\$ 203	\$ 217
Security Maturities, Redemptions and Sinking Funds	29	64	99	304
Prepayments	106	-	-	-
Other (including changes in working capital)	(126)	86	86	(79)
<b>Total Requirements</b>	<b>\$ 175</b>	<b>\$ 333</b>	<b>\$ 388</b>	<b>\$ 442</b>
<b>Sources</b>				
Total Internal	\$ 173	\$ 133	\$ 138	\$ 142
<b>Outside Financing</b>				
Long-term debt	-	200	250	300
Preferred Stock	-	-	-	-
Trust Preferred Securities	-	-	-	-
Common Stock	-	-	-	-
Contribution from Parent	-	-	-	-
Short-term debt change	2	-	-	-
<b>Total Outside</b>	<b>2</b>	<b>200</b>	<b>250</b>	<b>300</b>
<b>Total Fund Sources</b>	<b>\$ 175</b>	<b>\$ 333</b>	<b>\$ 388</b>	<b>\$ 442</b>

**PPL CORPORATION**  
**REQUIREMENTS AND SOURCES OF FUNDS <sup>1/</sup>**

	<u>2004</u>	<u>2005</u>	<u>2006</u>	<u>2007</u>
<b>Capital Requirements</b>	(Millions of Dollars)			
Construction	\$ 638	\$ 659	\$ 661	\$ 747
Nuclear Fuel Payments	56	59	62	63
Security Maturities, Redemptions and Sinking Funds	312	418	1,091	769
Prepayments	762	-	47	10
Trust Preferred Security Redemptions	575	-	-	-
Other (including changes in working capital)	(155)	89	225	84
<b>Total Requirements</b>	<b>\$ 2,188</b>	<b>\$ 1,225</b>	<b>\$ 2,086</b>	<b>\$ 1,673</b>
<b>Sources</b>				
Total Internal	\$ 763	\$ 646	\$ 712	\$ 879
Sale of Investments/Property	138	22	22	5
<b>Outside Financing</b>				
Long-term debt	769	556	1,351	788
PEPS Conversion	575	-	-	-
Short-term debt change	(57)	1	1	1
<b>Total Outside</b>	<b>1,287</b>	<b>557</b>	<b>1,352</b>	<b>789</b>
<b>Total Fund Sources</b>	<b>\$ 2,188</b>	<b>\$ 1,225</b>	<b>\$ 2,086</b>	<b>\$ 1,673</b>

<sup>1/</sup> Excludes Securitization

Q.3. State what coverage requirements or capital structure ratios are required in the most restrictive of applicable indentures/charter tests and how these measures have been computed.

A.3. PPL Electric's senior secured bond indenture includes provisions that restrict dividend payments and certain other distributions on, and redemptions of, its common stock and that require mandatory rates adjustment filings, in each case, if PPL Electric fails to meet interest coverage ratio tests. A summary of these provisions, including the manner in which the interest coverage ratios are computed, is provided in Attachment III-F-3.

## PPL ELECTRIC UTILITIES CORPORATION

### Summary of Indenture Provisions

PPL Electric Utilities Corporation (the "Company") issues senior secured bonds ("Senior Secured Bonds") under its Indenture established in 2001 (as amended and supplemented, the "2001 Indenture").<sup>1</sup> The outstanding Senior Secured Bonds have been issued pursuant to three supplements to the 2001 Indenture (each, a "Supplemental Indenture"). Each of these Supplemental Indentures includes interest coverage ratio tests that restrict certain payments and require mandatory rate adjustment filings. These provisions are summarized below:

The Company may not declare any dividends or commit to make any other distribution on or purchase or redeem any shares of its common stock, with certain exceptions, if and for so long as the average of the Interest Coverage Ratios for the four most recently ended fiscal quarters immediately preceding the date of declaration of any such restricted payment falls below 1.5. See Sections 102(a) and 202(a) of Supplemental Indenture No. 1 and Section 102(a) of Supplemental Indenture Nos. 2 and 3 (Attachment III-F-3, page 3).

If and for so long as the average of the Interest Coverage Ratios for the four consecutive fiscal quarters immediately preceding any date of determination falls below 1.5, the Company must file for rate relief with the Commission within 90 days, unless the Company is restricted from doing so by applicable law, regulation or

---

<sup>1</sup> The Company also issues senior secured debt, in the form of first mortgage bonds ("First Mortgage Bonds"), under its Mortgage and Deed of Trust established in 1945 (as amended and supplemented, the "1945 Mortgage"), which is a first mortgage lien on the transmission and distribution properties of the Company. The Company is making a transition from the 1945 Mortgage to the 2001 Indenture as its primary secured debt indenture as economic refunding opportunities arise and First Mortgage Bonds mature. Senior Secured Bonds issued under the 2001 Indenture are secured by:

- (a) First Mortgage Bonds issued under the 1945 Mortgage that have a principal amount equal to the principal amount of new Senior Secured Bonds being issued and that are held by the trustee under the 2001 Indenture; and
- (b) A lien in favor of the 2001 Indenture trustee on the Company's transmission and distribution properties, which lien is junior to the lien of the 1945 Mortgage.

The 2001 Indenture is intended to replace the 1945 Mortgage as soon as all of the Company's outstanding First Mortgage Bonds, excluding First Mortgage Bonds issued as collateral for Senior Secured Bonds, have been retired. When no remaining First Mortgage Bonds are outstanding under the 1945 Mortgage (except First Mortgage Bonds issued as collateral for the Senior Secured Bonds), the Company intends to cause the lien of the 1945 Mortgage to be discharged and for the lien of the 2001 Indenture to become a first lien on the Company's transmission and distribution properties, subject to certain permitted liens and exceptions. Thereafter, issuances of Senior Secured Bonds under the 2001 Indenture will not require collateralization with First Mortgage Bonds.

The 1945 Mortgage does not include any coverage requirements or capital structure ratios.

Commission policies or orders. See Sections 102(c) and 202(c) of Supplemental Indenture No. 1 and Section 102(c) of Supplemental Indenture Nos. 2 and 3 (Attachment III-F-3, page 3).

The "Interest Coverage Ratio" refers to the ratio of (i) the sum of the Company's funds from operations plus its gross interest expense (excluding intangible transition debt) to (ii) the Company's gross interest expense (excluding intangible transition debt). See Sections 106 and 206 of Supplemental Indenture No. 1 and Section 106 of Supplemental Indenture Nos. 2 and 3 (Attachment III-F-3, pages 3 and 4).

Details from Indenture

Sections 102 and 202 of Supplemental Indenture No. 1 to the 2001 Indenture, and Section 102 of Supplemental Indenture Nos. 2 and 3 to the 2001 Indenture:

So long as any [Senior Secured Bonds] remain Outstanding, each of the following shall be an additional covenant of the Company under the Indenture:

(a) The Company shall not declare any dividends on its shares of common stock or commit to make any other distribution on its shares of common stock (other than dividends and distributions payable in shares of its common stock), or purchase or redeem any shares of its common stock, other than with the proceeds of additional common stock financing (each such payment or distribution or purchase, a "Restricted Payment"), if and for so long as the average of the Interest Coverage Ratios for the four most recently ended fiscal quarters immediately preceding the date of declaration of any such Restricted Payment falls below 1.5. The Company shall not declare any cash dividend on shares of its common stock, or otherwise commit to making any other Restricted Payment, unless such dividend or other Restricted Payment is payable within 120 days of the date of declaration or other commitment.

...

(c) If and for so long as the average of the Interest Coverage Ratios for the four consecutive fiscal quarters immediately preceding any date of determination falls below 1.5, the Company shall initiate a filing for rate relief with the Pennsylvania Public Utility Commission ("PUC") within 90 days, unless the Company is not eligible for such rate relief under applicable law, regulation or orders or policies of the PUC then in effect.

...

Sections 106 and 206 of Supplemental Indenture No. 1 to the 2001 Indenture, and Section 106 of Supplemental Indenture Nos. 2 and 3 to the 2001 Indenture:

Definitions. For purposes of [Section 102 and 202 of the Supplemental Indentures],

...

"Funds from Operation" means for any period with respect to the Company and its consolidated subsidiaries, the aggregate amount of consolidated net income of the Company and its consolidated subsidiaries (x) plus deferred income taxes, depreciation and amortization expense, preferred dividends, extraordinary expense items, any non-recurring or non-cash charges to net income (whether or not an extraordinary item) and any expense associated with intangible transition charges, and (y) minus any deferred investment tax

credit, any extraordinary revenue items and any income associated with intangible transition charges, all computed in accordance with generally accepted accounting principles in effect on the date of original issue of the [Senior Secured Bonds];

"Gross Interest Expense" means for any period, the interest expense on indebtedness of the Company and its consolidated subsidiaries minus any interest expense associated with intangible transition debt;

...

"Interest Coverage Ratio" means the ratio of (i) the sum of Funds from Operation plus Gross Interest Expense to (ii) Gross Interest Expense.

...

- Q.4. A schedule of comparative financial data shall be supplied for the test year, the most immediately available annual historical period, prior to the test year, and the 2 calendar years most immediately preceding the test year. Changes in Moody's/S&P ratings, noted on this schedule, shall be accompanied by the Moody's/S&P writeup of such change, if available. The following financial data and ratios shall be supplied for the utility's parent, where applicable, if not available for the utility.
- a) Times interest earned ratio - pre-tax and post-tax basis.
  - b) Preferred stock dividend coverage ratio - post-tax basis.
  - c) Times fixed charges earned ratio - pre-tax basis.
  - d) Earnings per share.
  - e) Dividend per share.
  - f) Average dividend yield (52-week high/low common stock price).
  - g) Average book value per share.
  - h) Average market price per share.
  - i) Market price-book value ratio.
  - j) Earnings-book value ratio (per share basis, average book value).
  - k) Dividend payout ratio.
  - l) AFUDC as a % of earnings available for common equity.
  - m) Construction work in progress as a % of net utility plant.
  - n) Effective income tax rate.
  - o) Internal cash generations as a % of total capital requirements.

A.4. Attachment III-F-4a provides the requested comparative financial data.

Attachment III-F-4b provides the requested writeups from Moody's.  
Attachment III-F-4c provides the requested writeups from S&P.

PPL ELECTRIC UTILITIES CORPORATION

Comparative Financial Data

<u>Description/Purpose</u>	<u>2002</u>	<u>2003</u>	<u>2004</u>
a. Times interest earned ratio - pre-tax (a)	1.59	1.45	(c)
Times interest earned ratio - post-tax (a)	1.42	1.28	(c)
b. Preferred stock dividend coverage ratio - post-tax basis (a)	1.34	1.22	(c)
c. Times fixed charges earned ratio - pre-tax basis (a)	1.55	1.42	(c)
d. Earnings per share - diluted (b)	\$1.36	\$4.24	(c)
e. Dividend per share (b)	\$1.44	\$1.54	(c)
f. Average dividend yield			(c)
(52-week high/low common stock price) (b)	4.37%	4.05%	(c)
g. Average book value per share (b)	\$13.19	\$15.90	(c)
h. Average market price per share (b)	\$34.95	\$39.60	(c)
i. Market price-book value ratio (b)	2.65	2.49	(c)
j. Earnings-book value ratio			(c)
(per share basis, average book value) (b)	0.103	0.267	(c)
k. Dividend payout ratio (b)	1.059	0.363	(c)
l. AFUDC as a % of earnings available for common equity	4.36%	3.46%	(c)
m. Construction work in progress as a % of net utility plant	1.69%	1.05%	(c)
n. Effective income tax rate	39.1%	24.7%	(c)
o. Internal cash generations as a % of total capital requirements	88.5%	57.7%	(c)

(a) Excludes PPL Transition Bond Company, LLC.

(b) Information presented for PPL Corporation, as it is not applicable to PPL Electric.

(c) Requested data for the future test year is confidential because it deals with a release of projected financial information. This information will be provided to the PUC upon the issuance of an appropriate protective order concerning the confidentiality of such information and will be provided to any party to the rate proceeding upon the execution of an agreement with PPL Electric to hold such information in strict confidence and not to disclose it to any person, whether or not a party to the proceeding, who has not executed a similar confidentiality agreement with PPL Electric.





Moody's Investors Service

Global Credit Research

Rating Action

13 MAY 2003

Rating Action: PPL Electric Utilities Corporation

**MOODY'S DOWNGRADES DEBT RATINGS OF PPL ELECTRIC UTILITIES CORP. (TO Baa1 SR. SEC.); PPL ENERGY SUPPLY, LLC (TO Baa2 SR. UNSEC.); PPL CORP. (TO Baa3 SR. UNSEC.); AND PPL CAPITAL FUNDING, INC. (TO Baa3 SR. UNSEC.); ALL RATING OUTLOOKS ARE STABLE**

**Approximately \$7 Billion of Debt Affected**

New York, May 13, 2003 -- Moody's Investors Service has downgraded the debt ratings of PPL Electric Utilities Corporation, PPL Energy Supply, LLC, PPL Capital Funding, Inc., and PPL Corporation. Ratings downgraded include PPL Electric Utilities Corporation's first mortgage bonds and senior secured debt to Baa1 from A3; PPL Energy Supply, LLC's senior unsecured debt to Baa2 from Baa1, PPL Capital Funding, Inc.'s senior unsecured debt to Baa3 from Baa2; and PPL Corporation's senior unsecured debt to Baa3 from Baa2. PPL Capital Funding's debt obligations are fully and unconditionally guaranteed by PPL Corporation. The rating actions conclude the review for downgrade of PPL Electric Utilities, PPL Energy Supply, PPL Capital Funding and PPL Corporation that was initiated on April 29, 2003. The rating outlook is stable for all of these issuers.

PPL Electric Utilities Corporation's Prime-2 commercial paper rating was not under review and remains unchanged. PPL Energy Supply's Prime-2 commercial paper rating was also not under review and remains unchanged.

The downgrade reflects:

- (1) PPL's currently high financial leverage at the consolidated level;
- (2) PPL Energy Supply's modest exposure to merchant generation risk;
- (3) continued weakness in the wholesale power market and the associated financial impact on PPL Energy Supply; and
- (4) concerns regarding the amount of cash flow to be generated from PPL Energy Supply's non-regulated domestic operations and free cash flow that can be repatriated from its regulated delivery business abroad.

Moody's also notes that PPL Energy Supply's non-regulated investments now account for a larger proportion of PPL Corporation's total cash flow, as PPL Electric Utilities' financial performance has been affected by a rate cap implemented as part of a 1998 Pennsylvania Public Utility Commission restructuring order. Moody's expects the financial performance of PPL Electric Utilities to continue to be weak through December 31, 2004 when the current rate cap ends. In fact, PPL Electric Utilities' current financial profile has necessitated equity contributions from PPL Corporation, the parent company, in 2002 and 2003.

PPL Corporation's rating and outlook reflects plans for improving its balance sheet and cash flow, including proposed issuance of \$400 million of common stock in 2003 to retire indebtedness. Thus far in 2003, PPL has issued approximately \$115 million under its structured equity shelf and dividend reinvestment programs. PPL Energy Supply's rating and outlook reflect its ability to mitigate its modest merchant generation exposure through significant amounts of contracted power sale arrangements in the Pennsylvania-New

Jersey-Maryland region, in the Northwest, and in Arizona. The rating outlook also incorporates management's stated intention that PPL is not pursuing any further investments abroad and is in the process of completing its remaining new power plant development by early 2004 with no plans for further development. The rating and outlook for PPL Electric Utilities reflects Moody's expectation that the company will have more financial flexibility upon the expiration of the existing price cap on December 31, 2004 and then will begin strengthening the financial performance of the regulated utility operations.

As a regulated transmission and distribution utility, PPL Electric Utilities has a lower risk business profile. The supply and price risk of PPL Electric Utilities is mitigated by the regulatory treatment given to its "all requirements" or Provider of Last Resort (POLR) contract with PPL Energy Supply. The POLR contract, which was previously approved by the Pennsylvania Public Utility Commission, currently extends through December 31, 2009. More importantly, the POLR contract, with built-in price escalators, underpins a more predictable stream of cash flows to PPL Energy Supply through year-end 2009, as well as reducing the company's merchant exposure.

Moody's notes that PPL's management has already implemented a number of initiatives to strengthen the company's current credit quality and reduce high debt level. These include:

- (1) the issuance of over \$1 billion of common stock and mandatory convertible securities over the last few years;
- (2) plans to issue an additional \$400 million of common equity in 2003;
- (3) expected conversion of \$575 million in mandatory preferred securities into common equity in 2004;
- (4) a sizeable reduction in planned capital expenditures;
- (5) cancellation of projects under development;
- (6) workforce reductions; and
- (7) write-downs of some non-core investments.

The stable outlook for PPL Corporation and its affiliates is based upon the expectation that PPL Corporation will complete a planned issuance of \$400 million of common stock in 2003 and complete the mandatory conversion of \$575 million of preferred securities to common equity in 2004. The outlook also reflects Moody's expectation that the balance sheet and coverage ratios will improve over the next few years. In addition, the stable outlook for PPL Electric Utilities also reflects the expectation that the company's credit quality will begin to improve after the current price cap ends at year-end 2004.

Ratings downgraded include: PPL Electric Utilities Corporation's first mortgage bonds and senior secured debt to Baa1 from A3, shelf registration of senior secured debt to (P)Baa1 from (P)A3, senior unsecured debt to Baa2 from Baa1, preferred securities to Ba1 from Baa3, and shelf registration of preferred securities to (P)Ba1 from (P)Baa3; PPL Energy Supply, LLC's senior unsecured debt to Baa2 from Baa1, PPL Capital Funding, Inc.'s senior unsecured debt to Baa3 from Baa2, shelf registration of senior unsecured debt to (P)Baa3 from (P)Baa2, preferred securities to Ba1 from Baa3, and shelf registration of preferred securities to (P)Ba1 from (P)Baa3; and PPL Corporation's senior unsecured debt to Baa3 from Baa2, subordinated debt to Ba1 from Baa3, and shelf registration of subordinated debt to (P)Ba1 from (P)Baa3. PPL Capital Funding's debt obligations are fully and unconditionally guaranteed by PPL Corporation.

PPL Corporation, a diversified energy holding company, is headquartered in Allentown, Pennsylvania. PPL Electric Utilities Corporation is a regulated transmission and distribution utility subsidiary of PPL Corporation. PPL Energy Supply, LLC is an intermediate holding for PPL Corporation's non-regulated domestic generation business.

New York  
Daniel Gates  
Managing Director  
Corporate Finance Group  
Moody's Investors Service  
JOURNALISTS: 212-553-0376  
SUBSCRIBERS: 212-553-1653

New York  
Mo Ying W. Seto  
Senior Vice President  
Corporate Finance Group  
Moody's Investors Service  
JOURNALISTS: 212-553-0376  
SUBSCRIBERS: 212-553-1653

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**Research:****Summary: PPL Electric Utilities Corp.**

Publication date: 29-Apr-2003

Credit Analyst: Aneesh Prabhu, New York (1) 212-438-1285

Credit Rating: A-/Negative/A-2

**Rationale**

On April 29, 2003, Standard & Poor's Ratings Services affirmed its 'A-' corporate credit ratings on PPL Electric Utilities Corp. (PPLU). Standard & Poor's also assigned its 'A-' ratings to PPLU's \$100 million senior secured bonds to be offered in the near future. The bond proceeds will be used to redeem first mortgage bonds and preferred stock. The outlook is revised to negative to mirror the outlook on parent PPL Corp. and its other subsidiaries

Allentown, Pa.-based PPLU has about \$1.5 billion in rated debt as of Dec. 31, 2002.

The rating reflects PPLU's ring-fencing, which insulates the utility from PPL, low-risk transmission and distribution (T&D) electric operations, a large and stable residential and commercial customer base (78%), and a long-term power supply contract (2001-2009) with affiliate PPL Energy Supply LLC that eliminates volume and price risks. However, structural elements of the ring-fencing are not strong enough to completely isolate PPLU from PPL's credit quality. PPLU also has weak T&D ROEs due to capped rates through 2004.

PPLU has been insulated (ring-fenced) from the rest of PPL through legal and structural enhancements that transformed PPLU into a single-purpose entity bankruptcy remote from PPL. The ring-fencing results in a rating that is not equal with PPL and that is based on PPLU's stand-alone creditworthiness. However, the ring-fencing is not strong enough to support more than a two-notch differential between PPLU and PPL. PPLU is now rated two notches above PPL. If PPL is downgraded, PPLU's rating would be lowered as well. A negative outlook assignment for PPLU also mirrors the negative outlook on PPL and its subsidiaries.

As part of the Pennsylvania electric sector restructuring settlement agreement between PPLU and the Pennsylvania Public Utilities Commission (PPUC), PPLU agreed to a cap on its average T&D rates of 1.74 cents per kilowatt-hour (kWh) through 2004. The current ROE on the T&D rates is very low at about 5.5%, partly because PPLU pays ancillary service charges that are necessary to support the transmission of electricity from resources to load. Ancillary service charges are imposed under the PJM's open-access transmission tariffs but are not being recovered by PPLU because of the T&D rate cap. The rate cap established by the PPUC restructuring settlement expires on Jan. 1, 2005. The rate cap expiration is viewed as a credit positive, as it will allow PPLU to seek a base rate increase if the company chooses to do so. However, the outcome of such a rate case is uncertain.

PPLU is required, through 2009, to provide electricity at preset prices to its customers. As part of Pennsylvania deregulation, PPLU transferred its generation assets (about 8,000 MW) to PPL Energy Funding Inc. To mitigate supply risk, PPLU entered into a full-requirements, long-term supply contract with PPL EnergyPlus Co. to meet its provider of last resort obligation. While these supply rates vary by customer class, the settlement provides for average rates ranging from 4.28 cents per kWh in 2003 and increasing to 5.02 cents per kWh by 2009.

Standard & Poor's considers PPLU's competitive position as above average, because of the long-term contractual agreement that transfers all price and volumes risks to PPL EnergyPlus. PPLU's T&D rates are among the lowest in Pennsylvania. PPLU's largest industrial customers do not have plans for cogeneration, mitigating the possibility of these customers exiting the utility's system. Although there are competitive suppliers (like Sempra Energy, PowerChoice, and FirstEnergy Corp.) shopping levels in PPLU's territory have been low at around 4% to 5%.

The low-risk T&D business allows PPLEU to operate with a high debt-to-total capital ratio of 54% that will decrease over the next several years. Similarly, funds from operations (FFO) to total debt, at about 14%, and FFO interest coverage at around 3x in 2002 are weak but expected to improve to support a stand-alone credit quality at the 'A-' level in the post-2004 period.

### Liquidity.

PPLEU's liquidity position is viewed as strong. The utility has a \$400 million, 364-day credit facility, maturing June 2003 that includes a one-year term-out provision. There are no direct borrowings against this line. The credit facility also serves as a backstop for commercial paper. As of December 2002, PPLEU had \$15 million of commercial paper outstanding. In 2002, the utility employed cash flow from operations, a note repaid by an affiliate and equity contribution from PPL to retire about \$228 million of debt and about \$250 million of trust-preferred securities, and paid out \$67 million in dividends, leaving a cash balance of \$29 million at year-end 2002.

Future capital expenditures are estimated at about \$170 million per year. However, in 2002 and 2003, PPLEU is implementing automated meter readers at an additional cost of about \$70 million per year. Therefore, the company was not free cash flow positive in 2002 and will remain negative free cash flow in 2003. Free cash is expected to turn positive from 2004. PPLEU has about \$40 million of debt maturities and preferred-stock sinking fund payments in 2003 and only about \$25 million in 2004.

### ■ Outlook

The negative outlook mirrors the negative outlook for PPL and the maximum two-notch differential between PPLEU and PPL that currently exists. If PPL's ratings are lowered, PPLEU's ratings would be lowered also. The negative outlook also reflects PPLEU's need to improve its returns to maintain its financial position. A stable outlook revision is predicated on an improvement in PPL's credit quality and on regulatory clarity for PPLEU after 2004.

#### Ratings list:

PPL Electric Utilities Corp.

Corp. credit rating A-/Negative/A-2

#### NEW RATING

\$100 million senior secured bonds A-

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