DYNEGY HOLDINGS INC
Form 10-Q
August 08, 2011
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UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

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

For the quarterly period ended June 30, 2011

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

For the transition period from to

DYNEGY INC.

DYNEGY HOLDINGS INC.

(Exact name of registrant as specified in its charter)

Entity	Commission File Number	State of Incorporation	I.R.S. Employer Identification No.
Dynegy Inc.	001-33443	Delaware	20-5653152
Dynegy Holdings Inc.	000-29311	Delaware	94-3248415

1000 Louisiana, Suite 5800	
Houston, Texas	**77002**
(Address of principal executive offices)	(Zip Code)

(713) 507-6400

(Registrant s telephone number, including area code)

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days.

Dynegy Inc.	Yes x No o
Dynegy Holdings Inc.	Yes x No o

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files).

Dynegy Inc.	Yes x No o
Dynegy Holdings Inc.	Yes x No o

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. See definitions of large accelerated filer, accelerated filer and smaller reporting company in Rule 12b-2 of the Exchange Act.

	Large accelerated filer	Accelerated filer	Non-accelerated filer (Do not check if a smaller reporting company)	Smaller reporting company
Dynegy Inc.	o	x	o	o
Dynegy Holdings Inc.	o	o	x	o

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act).

Dynegy Inc.	Yes o No x
Dynegy Holdings Inc.	Yes o No x

Indicate the number of shares outstanding of Dynegy Inc. s classes of common stock, as of the latest practicable date: Common stock, $0.01 par value per share, 122,435,022 shares outstanding as of August 1, 2011. All of Dynegy Holdings Inc. s outstanding common stock is owned by Dynegy Inc.

This combined Form 10-Q is separately filed by Dynegy Inc. and Dynegy Holdings Inc. Information contained herein relating to any individual registrant is filed by such registrant on its own behalf. Each registrant makes no representation as to information relating to a registrant other than itself.

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DYNEGY INC. and DYNEGY HOLDINGS INC.

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EXPLANATORY NOTE

This report includes the combined filing of Dynegy Inc. (Dynegy) and Dynegy Holdings Inc. (DHI). DHI is the principal subsidiary of Dynegy, providing nearly 100 percent of Dynegy s total consolidated revenue for the six-month period ended June 30, 2011 and constituting nearly 100 percent of Dynegy s total consolidated asset base as of June 30, 2011. Unless the context indicates otherwise, throughout this report, the terms the Company , we , us , our and ours are used to refer to both Dynegy and DHI and their direct and indirect subsidiaries. Discussions or areas this report that apply only to Dynegy, DHI or specific subsidiaries are clearly noted in such section.

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DEFINITIONS

As used in this Form 10-Q, the abbreviations contained herein have the meanings set forth below.

ASU	Accounting Standards Update
BACT	Best available control technology
BART	Best available retrofit technology
BTA	Best technology available
CAA	Clean Air Act
CAIR	Clean Air Interstate Rule
CAISO	The California Independent System Operator
CAMR	Clean Air Mercury Rule
CARB	California Air Resources Board
CAVR	The Clean Air Visibility Rule
CCR	Coal Combustion Residuals
CEQA	California Environmental Quality Act
CERCLA	The Comprehensive Environmental Response, Compensation and Liability Act of 1980, as amended
CO_2	Carbon Dioxide
CSAPR	Cross-State Air Pollution Rule
CWA	Clean Water Act
DHI	Dynegy Holdings Inc.
DMSLP	Dynegy Midstream Services L.P.
EBITDA	Earnings before interest, taxes, depreciation and amortization
EPA	Environmental Protection Agency
FERC	Federal Energy Regulatory Commission
GAAP	Generally Accepted Accounting Principles of the United States of America
GEN	Our power generation business
GEN-MW	Our power generation business - Midwest segment
GEN-NE	Our power generation business - Northeast segment
GEN-WE	Our power generation business - West segment
GHG	Greenhouse Gas
HAPs	Hazardous air pollutants, as defined by the Clean Air Act
ICC	Illinois Commerce Commission
IMA	In-market asset availability
ISO	Independent System Operator
ISO-NE	Independent System Operator New England
MACT	Maximum achievable control technology
MGGA	Midwest Greenhouse Gas Accord
MGGRP	Midwestern Greenhouse Gas Reduction Program
MISO	Midwest Independent Transmission System Operator, Inc.
MMBtu	One million British thermal units
MW	Megawatts
MWh	Megawatt hour
NOL	Net operating loss
NO_x	Nitrogen oxide
NPDES	National Pollutant Discharge Elimination System
NRG	NRG Energy, Inc.
NSPS	New Source Performance Standard
NYISO	New York Independent System Operator
NYSDEC	New York State Department of Environmental Conservation
OAL	Office of Administrative Law

OTC	Over-the-counter
PJM	PJM Interconnection, LLC
PPEA	Plum Point Energy Associates, LLC
PPEA Holding	Plum Point Energy Associates Holding Company, LLC
PSD	Prevention of significant deterioration
RACT	Reasonably available control technology
RCRA	Resource Conservation and Recovery Act
RGGI	Regional Greenhouse Gas Initiative
RMR	Reliability Must Run
SEC	U.S. Securities and Exchange Commission
SIP	State Implementation Plan
SO_2	Sulfur dioxide
SPDES	State Pollutant Discharge Elimination System
VaR	Value at Risk
VIE	Variable Interest Entity
WCI	Western Climate Initiative

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PART I. FINANCIAL INFORMATION

Item 1 FINANCIAL STATEMENTS DYNEGY INC. AND DYNEGY HOLDINGS INC.

DYNEGY INC.

CONDENSED CONSOLIDATED BALANCE SHEETS

(unaudited) (in millions, except share data)

	June 30, 2011	December 31, 2010
ASSETS		
Current Assets		
Cash and cash equivalents	$ 399	$ 291
Restricted cash and investments	878	81
Short-term investments	106	106
Accounts receivable, net of allowance for doubtful accounts of $31 and $32, respectively	169	230
Accounts receivable, affiliates		1
Inventory	125	121
Assets from risk-management activities	989	1,199
Deferred income taxes	12	12
Broker margin account	202	80
Prepayments and other current assets	137	123
Total Current Assets	3,017	2,244
Property, Plant and Equipment	8,700	8,593
Accumulated depreciation	(2,499)	(2,320)
Property, Plant and Equipment, Net	6,201	6,273
Other Assets		
Restricted cash and investments	9	859
Assets from risk-management activities	84	72
Intangible assets	116	141
Other long-term assets	436	424
Total Assets	$ 9,863	$ 10,013
LIABILITIES AND STOCKHOLDERS EQUITY		
Current Liabilities		
Accounts payable	$ 111	$ 134
Accrued interest	51	36
Accrued liabilities and other current liabilities	86	109
Liabilities from risk-management activities	1,043	1,138
Notes payable and current portion of long-term debt	1,008	148
Total Current Liabilities	2,299	1,565
Long-term debt	3,852	4,426
Long-term debt, affiliates	200	200
Long-Term Debt	4,052	4,626

Other Liabilities				
Liabilities from risk-management activities		123		99
Deferred income taxes		509		641
Other long-term liabilities		321		336
Total Liabilities		7,304		7,267
Commitments and Contingencies (Note 7)				
Stockholders Equity				
Common Stock, $0.01 par value, 420,000,000 shares authorized at June 30, 2011 and December 31, 2010; 123,009,079 and 121,687,198 shares issued and outstanding at June 30, 2011 and December 31, 2010, respectively		1		1
Additional paid-in capital		6,071		6,067
Subscriptions receivable		(2)		(2)
Accumulated other comprehensive loss, net of tax		(51)		(53)
Accumulated deficit		(3,389)		(3,196)
Treasury stock, at cost, 728,408 and 628,014 shares at June 30, 2011 and December 31, 2010, respectively		(71)		(71)
Total Stockholders Equity		2,559		2,746
Total Liabilities and Stockholders Equity	$	9,863	$	10,013

See the notes to condensed consolidated financial statements.

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DYNEGY INC.

CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS

(unaudited) (in millions, except per share data)

	Three Months Ended June 30, 2011	Three Months Ended June 30, 2010	Six Months Ended June 30, 2011	Six Months Ended June 30, 2010
Revenues	$ 326	$ 239	$ 831	$ 1,097
Cost of sales	(225)	(231)	(503)	(539)
Operating and maintenance expense, exclusive of depreciation shown separately below	(106)	(118)	(216)	(231)
Depreciation and amortization expense	(75)	(90)	(201)	(165)
Impairment and other charges	(1)	(1)	(1)	(1)
General and administrative expenses	(25)	(28)	(65)	(59)
Operating income (loss)	(106)	(229)	(155)	102
Losses from unconsolidated investments				(34)
Interest expense	(89)	(91)	(178)	(180)
Other income and expense, net	3	1	4	2
Loss from continuing operations before income taxes	(192)	(319)	(329)	(110)
Income tax benefit (Note 10)	76	128	136	63
Loss from continuing operations	(116)	(191)	(193)	(47)
Income from discontinued operations, net of taxes				1
Net loss	$ (116)	$ (191)	$ (193)	$ (46)
Loss Per Share (Note 11):				
Basic loss per share:				
Loss from continuing operations	$ (0.95)	$ (1.59)	$ (1.58)	$ (0.39)
Income from discontinued operations				0.01
Basic loss per share	$ (0.95)	$ (1.59)	$ (1.58)	$ (0.38)
Diluted loss per share:				
Loss from continuing operations	$ (0.95)	$ (1.59)	$ (1.58)	$ (0.39)
Income from discontinued operations				0.01
Diluted loss per share	$ (0.95)	$ (1.59)	$ (1.58)	$ (0.38)
Basic shares outstanding	122	120	122	120
Diluted shares outstanding	122	121	122	121

See the notes to condensed consolidated financial statements.

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DYNEGY INC.

CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS

(unaudited) (in millions)

	Six Months Ended June 30, 2011	Six Months Ended June 30, 2010
CASH FLOWS FROM OPERATING ACTIVITIES:		
Net loss	$ (193)	$ (46)
Adjustments to reconcile net loss to net cash flows from operating activities:		
Depreciation and amortization	209	172
Impairment and other charges	1	1
Losses from unconsolidated investments, net of cash distributions		34
Risk-management activities	127	8
Deferred income taxes	(135)	(62)
Other	24	30
Changes in working capital:		
Accounts receivable	60	14
Inventory	(4)	3
Broker margin account	(92)	255
Prepayments and other assets	1	8
Accounts payable and accrued liabilities	(55)	(36)
Changes in non-current assets	(33)	(17)
Changes in non-current liabilities	4	4
Net cash provided by (used in) operating activities	(86)	368
CASH FLOWS FROM INVESTING ACTIVITIES:		
Capital expenditures	(128)	(201)
Unconsolidated investments		(15)
Maturities of short-term investments	217	27
Purchases of short-term investments	(247)	(331)
Decrease (increase) in restricted cash and investments	53	(10)
Other investing	10	9
Net cash used in investing activities	(95)	(521)
CASH FLOWS FROM FINANCING ACTIVITIES:		
Proceeds from long-term borrowings, net of financing costs	399	(5)
Repayments of borrowings	(113)	(31)
Net proceeds from issuance of capital stock	3	
Net cash provided by (used in) financing activities	289	(36)
Net increase (decrease) in cash and cash equivalents	108	(189)
Cash and cash equivalents, beginning of period	291	471
Cash and cash equivalents, end of period	$ 399	$ 282

Other non-cash investing activity:				
Non-cash capital expenditures	$	(7)	$	6
Other non-cash financing activity:				
Deferred financing fees	$	(4)		

See the notes to condensed consolidated financial statements.

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DYNEGY INC.

CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME (LOSS)

(unaudited) (in millions)

	Three Months Ended June 30, 2011		Three Months Ended June 30, 2010	
Net loss	$	(116)	$	(191)
Amortization of unrecognized prior service cost and actuarial gain (net of tax expense of $1 and $1)		1		
Other comprehensive income, net of tax		1		
Comprehensive loss	$	(115)	$	(191)

	Six Months Ended June 30, 2011		Six Months Ended June 30, 2010	
Net loss	$	(193)	$	(46)
Amortization of unrecognized prior service cost and actuarial gain (net of tax expense of $1 and $1)		2		2
Other comprehensive income, net of tax		2		2
Comprehensive loss	$	(191)	$	(44)

See the notes to condensed consolidated financial statements.

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DYNEGY HOLDINGS INC.

CONDENSED CONSOLIDATED BALANCE SHEETS

(unaudited) (in millions)

	June 30, 2011	December 31, 2010
ASSETS		
Current Assets		
Cash and cash equivalents	$ 354	$ 253
Restricted cash and investments	878	81
Short-term investments	94	90
Accounts receivable, net of allowance for doubtful accounts of $12 and $13, respectively	168	229
Accounts receivable, affiliates		1
Inventory	125	121
Assets from risk-management activities	989	1,199
Deferred income taxes	4	3
Broker margin account	202	80
Prepayments and other current assets	136	123
Total Current Assets	2,950	2,180
Property, Plant and Equipment	8,700	8,593
Accumulated depreciation	(2,499)	(2,320)
Property, Plant and Equipment, Net	6,201	6,273
Other Assets		
Restricted cash and investments	9	859
Assets from risk-management activities	84	72
Intangible assets	116	141
Other long-term assets	436	424
Total Assets	$ 9,796	$ 9,949
LIABILITIES AND STOCKHOLDERS EQUITY		
Current Liabilities		
Accounts payable	$ 111	$ 134
Accrued interest	51	36
Accrued liabilities and other current liabilities	85	106
Liabilities from risk-management activities	1,043	1,138
Notes payable and current portion of long-term debt	1,008	148
Total Current Liabilities	2,298	1,562
Long-term debt	3,852	4,426
Long-term debt, affiliates	200	200
Long-Term Debt	4,052	4,626
Other Liabilities		
Liabilities from risk-management activities	123	99
Deferred income taxes	474	606
Other long-term liabilities	321	337
Total Liabilities	7,268	7,230
Commitments and Contingencies (Note 7)		
Stockholder s Equity		
Capital Stock, $1 par value, 1,000 shares authorized at June 30, 2011 and December 31, 2010		
Additional paid-in capital	5,135	5,135

Affiliate receivable	(812)	(814)
Accumulated other comprehensive loss, net of tax	(51)	(53)
Accumulated deficit	(1,744)	(1,549)
Total Stockholder s Equity	2,528	2,719
Total Liabilities and Stockholder s Equity	$ 9,796	$ 9,949

See the notes to condensed consolidated financial statements.

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DYNEGY HOLDINGS INC.

CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS

(unaudited) (in millions)

	Three Months Ended June 30, 2011	Three Months Ended June 30, 2010	Six Months Ended June 30, 2011	Six Months Ended June 30, 2010
Revenues	$ 326	$ 239	$ 831	$ 1,097
Cost of sales	(225)	(231)	(503)	(539)
Operating and maintenance expense, exclusive of depreciation shown separately below	(106)	(118)	(216)	(231)
Depreciation and amortization expense	(75)	(90)	(201)	(165)
Impairment and other charges	(1)	(1)	(1)	(1)
General and administrative expenses	(23)	(28)	(64)	(59)
Operating income (loss)	(104)	(229)	(154)	102
Losses from unconsolidated investments				(34)
Interest expense	(89)	(91)	(178)	(180)
Other income and expense, net	3	1	4	2
Loss from continuing operations before income taxes	(190)	(319)	(328)	(110)
Income tax benefit (Note 10)	75	128	133	56
Loss from continuing operations	(115)	(191)	(195)	(54)
Income from discontinued operations, net of taxes				1
Net loss	$ (115)	$ (191)	$ (195)	$ (53)

See the notes to condensed consolidated financial statements.

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DYNEGY HOLDINGS INC.

CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS

(unaudited) (in millions)

	Six Months Ended June 30, 2011	Six Months Ended June 30, 2010
CASH FLOWS FROM OPERATING ACTIVITIES:		
Net loss	$ (195)	$ (53)
Adjustments to reconcile net loss to net cash flows from operating activities:		
Depreciation and amortization	209	172
Impairment and other charges	1	1
Losses from unconsolidated investments, net of cash distributions		34
Risk-management activities	127	8
Deferred income taxes	(132)	(55)
Other	22	27
Changes in working capital:		
Accounts receivable	60	19
Inventory	(4)	3
Broker margin account	(92)	255
Prepayments and other assets	1	8
Accounts payable and accrued liabilities	(54)	(37)
Changes in non-current assets	(33)	(17)
Changes in non-current liabilities	4	4
Net cash provided by (used in) operating activities	(86)	369
CASH FLOWS FROM INVESTING ACTIVITIES:		
Capital expenditures	(128)	(201)
Unconsolidated investments		(15)
Maturities of short-term investments	201	28
Purchases of short-term investments	(235)	(316)
Decrease (increase) in restricted cash and investments	53	(10)
Affiliate transactions		(2)
Other investing	10	8
Net cash used in investing activities	(99)	(508)
CASH FLOWS FROM FINANCING ACTIVITIES:		
Proceeds from long-term borrowings, net of financing costs	399	(5)
Repayments of borrowings	(113)	(31)
Net cash provided by (used in) financing activities	286	(36)
Net increase (decrease) in cash and cash equivalents	101	(175)
Cash and cash equivalents, beginning of period	253	419
Cash and cash equivalents, end of period	$ 354	$ 244

Other non-cash investing activity:				
Non-cash capital expenditures	$	(7)	$	6
Other non-cash financing activity:				
Deferred financing fees	$	(4)		

See the notes to condensed consolidated financial statements.

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DYNEGY HOLDINGS INC.

CONDENSED CONSOLIDATED OF COMPREHENSIVE INCOME (LOSS)

(unaudited) (in millions)

	Three Months Ended June 30, 2011	Three Months Ended June 30, 2010
Net loss	$ (115)	$ (191)
Amortization of unrecognized prior service cost and actuarial gain (net of tax expense of $1 and $1)	1	
Other comprehensive income, net of tax	1	
Comprehensive loss	$ (114)	$ (191)

	Six Months Ended June 30, 2011	Six Months Ended June 30, 2010
Net loss	$ (195)	$ (53)
Amortization of unrecognized prior service cost and actuarial gain (net of tax expense of $1 and $1)	2	2
Other comprehensive income, net of tax	2	2
Comprehensive loss	$ (193)	$ (51)

See the notes to condensed consolidated financial statements.

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DYNEGY INC. and DYNEGY HOLDINGS INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(Unaudited)

For the Interim Periods Ended June 30, 2011 and 2010

Note 1 Accounting Policies

Basis of Presentation

The accompanying unaudited condensed consolidated financial statements have been prepared in accordance with the instructions to interim financial reporting as prescribed by the SEC. The year-end condensed consolidated balance sheet data was derived from audited consolidated financial statements but does not include all disclosures required by accounting principles generally accepted in the United States of America. These interim financial statements should be read together with the consolidated financial statements and notes thereto included in Dynegy s and DHI s annual report on Form 10-K for the year ended December 31, 2010, filed on March 8, 2011, which we refer to as each registrant s Form 10-K .

The unaudited condensed consolidated financial statements contained in this report include all material adjustments of a normal and recurring nature that, in the opinion of management, are necessary for a fair presentation of the results for the interim periods. The results of operations for the interim periods presented in this Form 10-Q are not necessarily indicative of the results to be expected for the full year or any other interim period due to seasonal fluctuations in demand for our energy products and services, changes in commodity prices, timing of maintenance and other expenditures and other factors. The preparation of consolidated financial statements in conformity with generally accepted accounting principles (GAAP) requires management to make informed estimates and judgments that affect our reported financial position and results of operations based on currently available information. We review significant estimates and judgments affecting our consolidated financial statements on a recurring basis and record the effect of any necessary adjustments. Uncertainties with respect to such estimates and judgments are inherent in the preparation of financial statements. Estimates and judgments are used in, among other things, (i) developing fair value assumptions, including estimates of future cash flows and discount rates, (ii) analyzing tangible and intangible assets for possible impairment, (iii) estimating the useful lives of our assets, (iv) assessing future tax exposure and the realization of deferred tax assets, (v) determining amounts to accrue for contingencies, guarantees and indemnifications, (vi) estimating various factors used to value our pension assets and liabilities and (vii) determining the primary beneficiary of variable interest entities (VIEs). Actual results could differ materially from our estimates.

Going Concern. Our accompanying unaudited condensed consolidated financial statements have been prepared assuming that we will continue as a going concern, which contemplates realization of assets and the satisfaction of liabilities in the normal course of business for the twelve month period following the date of these unaudited condensed consolidated financial statements. However, continued low power prices over the past two years have had a significant adverse impact on our business and continue to negatively impact our projected future liquidity.

We recently completed a reorganization of our subsidiaries and in connection therewith, certain of our subsidiaries (GasCo and CoalCo, as defined in Note 13 Subsequent Events) entered into two new credit facilities on August 5, 2011 which resulted in the repayment in full and termination of commitments under DHI s Fifth Amended and Restated Credit Agreement. However, these new credit facilities contain certain restrictions related to distributions to their respective parent companies, including Dynegy and DHI (please read Note 13 Subsequent Events for further discussion). Although these new credit facilities are designed to provide sufficient operating liquidity for GasCo and CoalCo for the foreseeable future, there still remain significant debt service requirements for the unsecured notes and debentures at DHI as well as the operating lease payment obligations related to the Danskammer and Roseton operating leases at a wholly-owned subsidiary of DHI. We currently project that we will have minimal liquidity at DHI subsequent to funding of the debt service requirements and operating lease payment obligations beyond the next eighteen months absent a significant positive change in the forecasted operating results of the Roseton and Danskammer facilities.

DYNEGY INC. and DYNEGY HOLDINGS INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

(Unaudited)

For the Interim Periods Ended June 30, 2011 and 2010

The August 2011 reorganization represents our first step in addressing our liquidity concerns. Over the next eighteen months, under the strategic direction of the Finance and Restructuring Committee of Dynegy s Board of Directors, we may participate in additional debt restructuring activities, which may include direct or indirect transfers of our subsidiaries equity interests, refinancing of existing debt and lease obligations, and/or further reorganizations of our subsidiaries as well as other similar initiatives. However, we cannot provide any assurances that we will be successful in accomplishing any such activities.

Our ability to continue as a going concern is dependent on many factors, including, among other things, GasCo and CoalCo generating sufficient positive operating results to enable GasCo and CoalCo to make certain restricted distributions to their parents (as described in Note 13 Subsequent Events), Roseton and Danskammer producing positive operating results, successfully executing any further restructuring strategies, and continuing to execute the company-wide cost reduction initiatives that are ongoing. The accompanying unaudited condensed consolidated financial statements do not include any adjustments that might result from the outcome of the foregoing uncertainties.

Accounting Principles Not Yet Adopted

Fair Value Measurement Disclosures. In May 2011, the FASB issued Accounting Standards Update (ASU) No. 2011-04 Fair Value Measurement (Topic 820): Amendments to Achieve Common Fair Value Measurement and Disclosure Requirements in U.S. GAAP and IFRSs (ASU No. 2011-04). This authoritative guidance changes the wording used to describe the requirements in GAAP for measuring fair value and for disclosing information about fair value measurements. ASU No. 2011-04 is effective for interim and annual periods beginning after December 15, 2011. We do not expect the implementation of this guidance to have a significant impact on our financial condition, results of operations or cash flows.

Presentation of Comprehensive Income. In June 2011, the FASB issued ASU 2011-05 Comprehensive Income (Topic 220): Presentation of Comprehensive Income (ASU No. 2011-05). The FASB s objective in issuing this guidance is to improve the comparability, consistency, and transparency of financial reporting and to increase the prominence of items reported in other comprehensive income. ASU No. 2011-05 eliminates the option of presenting components of other comprehensive income as part of the statement of changes in stockholders equity. The standard requires that all nonowner changes in stockholders equity be presented either in a single continuous statement of comprehensive income or in two separate but consecutive statements. ASU 2011-05 is effective for fiscal years, and interim periods within those years, beginning after December 15, 2011. We do not expect the implementation of this guidance to have a significant impact on our financial condition, results of operations or cash flows.

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DYNEGY INC. and DYNEGY HOLDINGS INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

(Unaudited)

For the Interim Periods Ended June 30, 2011 and 2010

Note 2 Investments

The amortized cost basis, unrealized gains and losses and fair values of investments in available for sale investments is shown in the tables below:

	Investments as of June 30, 2011 (in millions)			
	Cost Basis	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
Available for Sale investments:				
Commercial Paper	$ 45	$	$	$ 45
Certificates of Deposit	13			13
U.S. Treasury and Government Securities (1)	151			151
Total DHI	$ 209	$	$	$ 209
Commercial Paper	2			2
Certificates of Deposit	8			8
Corporate Securities	2			2
Total Dynegy	$ 221	$	$	$ 221

(1) Includes $115 million in Broker margin account on our unaudited condensed consolidated balance sheets in support of transactions with our futures clearing manager.

	Investments as of December 31, 2010 (in millions)			
	Cost Basis	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
Available for Sale investments:				

Commercial Paper	$	41	$		$		$	41
Certificates of Deposit		12						12
Corporate Securities		2						2
U.S. Treasury and Government Securities (1)		120						120
Total DHI	$	175	$		$		$	175
Commercial Paper		4						4
Certificates of Deposit		8						8
Corporate Securities		4						4
Total Dynegy	$	191	$		$		$	191

(1) Includes $85 million in Broker margin account on our consolidated balance sheets in support of transactions with our futures clearing manager.

During the three and six months ended June 30, 2011**,** we received proceeds of $36 million from the sale of available for sale securities for which we realized less than $1 million of gains for the three and six months ended June 30, 2011.

Note 3 Risk Management Activities, Derivatives and Financial Instruments

The nature of our business necessarily involves market and financial risks. Specifically, we are exposed to commodity price variability related to our power generation business. Our commercial team manages these commodity price risks with financially settled and other types of contracts consistent with our commodity risk management policy. Our commercial team also uses financial instruments in an attempt to capture the benefit of fluctuations in market prices in the geographic regions where our assets operate. Our treasury team manages our financial risks and exposures associated with interest expense variability.

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DYNEGY INC. and DYNEGY HOLDINGS INC.

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(Unaudited)

For the Interim Periods Ended June 30, 2011 and 2010

Our commodity risk management strategy gives us the flexibility to sell energy and capacity through a combination of spot market sales and near-term contractual arrangements (generally over a rolling 1 to 3 year time frame). Our commodity risk management goal is to protect cash flow in the near-term while keeping the ability to capture value longer-term. Increasing collateral requirements and our liquidity position could impact our ability to effectively employ our risk management strategy. Many of our contractual arrangements are derivative instruments and must be accounted for at fair value. We also manage commodity price risk by entering into capacity forward sales arrangements, tolling arrangements, RMR contracts, fixed price coal purchases and other arrangements that do not receive fair value accounting treatment because these arrangements do not meet the definition of a derivative or are designated as normal purchase normal sales . As a result, the gains and losses with respect to these arrangements are not reflected in the unaudited condensed consolidated statements of operations until the settlement dates.

Quantitative Disclosures Related to Financial Instruments and Derivatives

The following disclosures and tables present information concerning the impact of derivative instruments on our unaudited condensed consolidated balance sheets and statements of operations. In the table below, commodity contracts primarily consist of derivative contracts related to our power generation business that we have not designated as accounting hedges, that are entered into for purposes of economically hedging future fuel requirements and sales commitments and securing commodity prices. As of June 30, 2011, our commodity derivatives were comprised of both long and short positions; a long position is a contract to purchase a commodity, while a short position is a contract to sell a commodity. As of June 30, 2011, we had net long/(short) commodity derivative contracts outstanding in the following quantities:

Contract Type	**Hedge Designation**	**Quantity (in millions)**	**Unit of Measure**		**Net Fair Value (in millions)**
Commodity contracts:					
Electric energy (1)	Not designated	(39)	MW	$	109
Natural gas (1)	Not designated	227	MMBtu	$	(187)
Heat rate derivatives	Not designated	(4)/39	MW/MMBtu	$	(22)
Other (2)	Not designated	3	Misc.	$	7

(1) Mainly comprised of swaps, options and physical forwards.

(2) Comprised of emissions, coal, crude oil and fuel oil options, swaps and physical forwards.

Derivatives on the Balance Sheet. We execute a significant volume of transactions through a futures clearing manager. Our daily cash payments (receipts) to (from) our futures clearing manager consist of three parts: (i) fair value of open positions (exclusive of options) (Daily Cash Settlements); (ii) initial margin requirements related to open positions (exclusive of options) (Initial Margin); and (iii) fair value and margin requirements related to options (Options , and collectively with Initial Margin, Collateral). We do not offset fair value amounts recognized for derivative instruments executed with the same counterparty under a master netting agreement and we do not elect to offset the fair value amounts recognized for the Daily Cash Settlements paid or received against the fair value amounts recognized for derivative instruments executed with the same counterparty under a master netting agreement.

As a result, our unaudited condensed consolidated balance sheets present derivative assets and liabilities, as well as related Daily Cash Settlements and Collateral, as applicable, on a gross basis. As of June 30, 2011, of the approximately $202 million included in the Broker margin account on our unaudited condensed consolidated balance sheets, approximately $137 million represents Collateral and approximately $61 million represents Daily Cash Settlements. As of December 31, 2010, of the approximately $80 million included in the Broker margin account on our unaudited condensed consolidated balance sheets, approximately $75 million represented Collateral offset by approximately $5 million of Daily Cash Settlements. We use short-term investments to collateralize a portion of our collateral requirements. The broker requires that we post approximately 103 percent of any collateral requirement collateralized with short-term investments. Accordingly, our Broker margin account includes approximately $3 million related to this requirement at June 30, 2011 and December 31, 2010. Additionally, we posted $1 million and $7 million of short-term investments which were not utilized as collateral at June 30, 2011 and December 31, 2010, respectively.

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DYNEGY INC. and DYNEGY HOLDINGS INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

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The following table presents the fair value and balance sheet classification of derivatives in the unaudited condensed consolidated balance sheet as of June 30, 2011, and December 31, 2010 segregated between designated, qualifying hedging instruments and those that are not, and by type of contract segregated by assets and liabilities.

Contract Type	Balance Sheet Location	June 30, 2011	December 31, 2010
		(in millions)	
Derivatives designated as hedging instruments:			
Derivative Assets:			
Interest rate contracts	Assets from risk management activities	$	$ 1
Total derivatives designated as hedging instruments			1
Derivatives not designated as hedging instruments:			
Derivative Assets:			
Commodity contracts	Assets from risk management activities	1,073	1,265
Interest rate contracts	Assets from risk management activities		5
Derivative Liabilities:			
Commodity contracts	Liabilities from risk management activities	(1,166)	(1,231)
Interest rate contracts	Liabilities from risk management activities		(6)
Total derivatives not designated as hedging instruments		(93)	33
Total derivatives, net		$ (93)	$ 34

Impact of Derivatives on the Consolidated Statements of Operations

The following discussion and tables present the disclosure of the location and amount of gains and losses on derivative instruments in our unaudited condensed consolidated statements of operations for the three and six months ended June 30, 2011 and 2010 segregated between designated, qualifying hedging instruments and those that are not, by type of contract.

Cash Flow Hedges. We may enter into financial derivative instruments that qualify, and that we may elect to designate, as cash flow hedges. Interest rate swaps have been used to convert floating interest rate obligations to fixed interest rate obligations. We had no cash flow hedges in place during the three and six months ended June 30, 2011 and 2010.

Fair Value Hedges. We also enter into derivative instruments that qualify, and that we may elect to designate, as fair value hedges. We use interest rate swaps to convert a portion of our non-prepayable fixed-rate debt into floating-rate debt. These derivatives and the corresponding hedged debt matured April 1, 2011. During the three and six months ended June 30, 2011 and 2010, there was no ineffectiveness from changes in the fair value of hedge positions and no amounts were excluded from the assessment of hedge effectiveness. During the three and six months ended June 30, 2011 and 2010, there were no gains or losses related to the recognition of firm commitments that no longer qualified as fair value hedges.

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NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

(Unaudited)

For the Interim Periods Ended June 30, 2011 and 2010

The impact of interest rate swap contracts designated as fair value hedges and the related hedged item on our unaudited condensed consolidated statement of operations for the three and six months ended June 30, 2011 and 2010 was immaterial.

Financial Instruments Not Designated as Hedges. We elect not to designate derivatives related to our power generation business and certain interest rate instruments as cash flow or fair value hedges. Thus, we account for changes in the fair value of these derivatives within the consolidated statements of operations (herein referred to as mark-to-market accounting treatment). As a result, these mark-to-market gains and losses are not reflected in the unaudited condensed consolidated statements of operations in the same period as the underlying activity for which the derivative instruments serve as economic hedges.

For the three-month period ended June 30, 2011, our revenues included approximately $129 million of mark-to-market losses related to this activity compared to $258 million of mark-to-market losses in the same period in the prior year. For the six months ended June 30, 2011, our revenues included approximately $127 million of mark-to-market losses related to this activity compared to $5 million of mark-to-market losses in the same period in the prior year.

The impact of derivative financial instruments that have not been designated as hedges on our unaudited condensed consolidated statement of operations for the three months ended June 30, 2011 and 2010 is presented below. Note that this presentation does not reflect the expected gains or losses arising from the underlying physical transactions associated with these financial instruments. Therefore, this presentation is not indicative of the economic gross margin we expect to realize when the underlying physical transactions settle.

Derivatives Not Designated as Hedging Instruments	Location of Loss Recognized in Income on Derivatives	Amount of Loss Recognized in Income on Derivatives for the Three Months Ended June 30, 2011	2010
		(in millions)	
Commodity contracts	Revenues	$ (89)	$ (185)

The impact of derivative financial instruments that have not been designated as hedges on our unaudited condensed consolidated statement of operations for the six months ended June 30, 2011 and 2010 is presented below. Note that this presentation does not reflect the expected gains or losses arising from the underlying physical transactions associated with these financial instruments. Therefore, this presentation is not indicative of the economic gross margin we expect to realize when the underlying physical transactions settle.

Derivatives Not Designated as Hedging Instruments	Location of Gain (Loss) Recognized in Income on Derivatives	Amount of Gain (Loss) Recognized in Income on Derivatives for the Six Months Ended June 30, 2011	2010
		(in millions)	
Commodity contracts	Revenues	$ (70)	$ 140

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DYNEGY INC. and DYNEGY HOLDINGS INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

(Unaudited)

For the Interim Periods Ended June 30, 2011 and 2010

Note 4 Fair Value Measurements

The following tables set forth by level within the fair value hierarchy our financial assets and liabilities that were accounted for at fair value on a recurring basis as of June 30, 2011 and December 31, 2010. These financial assets and liabilities are classified in their entirety based on the lowest level of input that is significant to the fair value measurement. Our assessment of the significance of a particular input to the fair value measurement requires judgment, and may affect the valuation of fair value assets and liabilities and their placement within the fair value hierarchy levels.

	Fair Value as of June 30, 2011 (in millions)			
	Level 1	Level 2	Level 3	Total
Assets:				
Assets from commodity risk management activities:				
Electricity derivatives	$	$ 325	$ 48	$ 373
Natural gas derivatives		658		658
Other derivatives		42		42
Total assets from commodity risk management activities		1,025	48	1,073
DHI Short-term investments:				
Commercial paper		45		45
Certificates of deposit		13		13
U.S. Treasury and government securities (1)		151		151
Total DHI short-term investments		209		209
Total DHI		1,234	48	1,282
Dynegy Short-term investments:				
Commercial paper		2		2
Corporate Securities		2		2
Certificates of deposit		8		8

Total Dynegy	$	$ 1,246	$ 48	$ 1,294
Liabilities:				
Liabilities from commodity risk management activities:				
Electricity derivatives	$	$ (250)	$ (13)	$ (263)
Natural gas derivatives		(845)		(845)
Heat rate derivatives			(23)	(23)
Other derivatives		(35)		(35)
Total Dynegy and DHI	$	$ (1,130)	$ (36)	$ (1,166)

(1) Includes $115 million in Broker margin account on our consolidated balance sheets in support of transactions with our futures clearing manager.

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DYNEGY INC. and DYNEGY HOLDINGS INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

(Unaudited)

For the Interim Periods Ended June 30, 2011 and 2010

	Fair Value as of December 31, 2010			
	Level 1	Level 2	Level 3	Total
	(in millions)			
Assets:				
Assets from commodity risk management activities:				
Electricity derivatives	$	$ 526	$ 77	$ 603
Natural gas derivatives		613	5	618
Other derivatives		44		44
Total assets from commodity risk management activities		1,183	82	1,265
Assets from interest rate swaps		6		6
DHI Short-term investments:				
Commercial paper		41		41
Certificates of deposit		12		12
Corporate securities		2		2
U.S. Treasury and government securities (1)		120		120
Total DHI short-term investments		175		175
Total DHI		1,364	82	1,446
Dynegy Short-term investments:				
Commercial paper		4		4
Certificates of deposit		8		8
Corporate securities		4		4
Total Dynegy	$	$ 1,380	$ 82	$ 1,462
Liabilities:				
Liabilities from commodity risk management activities:				
Electricity derivatives	$	$ (311)	$ (28)	$ (339)
Natural gas derivatives		(825)		(825)
Heat rate derivatives			(31)	(31)
Other derivatives		(36)		(36)
	$	$ (1,172)	$ (59)	$ (1,231)

Total liabilities from commodity risk management activities				
Liabilities from interest rate swaps		(6)		(6)
Total Dynegy and DHI	$	$ (1,178)	$ (59)	$ (1,237)

(1) Includes $85 million in Broker margin account on our consolidated balance sheets in support of transactions with our futures clearing manager.

We primarily apply the market approach for recurring fair value measurements and endeavor to utilize the best available information. Accordingly, we utilize valuation techniques that maximize the use of observable inputs and minimize the use of unobservable inputs. For example, assets and liabilities from risk management activities may include exchange-traded derivative contracts and OTC derivative contracts. Some exchange-traded derivatives are valued using broker or dealer quotations, or market transactions in either the listed or OTC markets. In such cases, these exchange-traded derivatives are classified within Level 2. OTC derivative trading instruments include swaps, forwards, options and complex structures that are valued at fair value. In certain instances, these instruments may utilize models to measure fair value. Generally, we use a similar model to value similar instruments. Valuation models utilize various inputs that include quoted prices for similar assets or liabilities in active markets, quoted prices for identical or similar assets or liabilities in markets that are not active, other observable inputs for the asset or liability, and market-corroborated inputs. Where observable inputs are available for substantially the full term of the asset or liability, the instrument is categorized in Level 2. Certain OTC derivatives trade in less active markets with a lower availability of pricing information. In addition, complex or structured transactions, such as heat-rate call options, can introduce the need for internally-developed model inputs that might not be observable in or corroborated by the market. When such inputs have a significant impact on the measurement of fair value, the instrument is categorized in Level 3. We have consistently used this valuation technique for all periods presented. Please read Note 2 Summary of Significant Accounting Policies Fair Value Measurements in our Form 10-K for further discussion.

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NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

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The following tables set forth a reconciliation of changes in the fair value of financial instruments classified as Level 3 in the fair value hierarchy:

	Three Months Ended June 30, 2011			
	Electricity Derivatives	Natural Gas Derivatives	Heat Rate Derivatives	Total
	(in millions)			
Balance at March 31, 2011	$ 48	$ 5	$ (26)	$ 27
Total losses included in earnings	(12)	(5)	(1)	(18)
Settlements	(1)		4	3
Balance at June 30, 2011				