

FORM 10-Q

SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, D.C. 20549

(Mark One)

☒

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

For the quarterly period ended June 30, 2005

OR

☐

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

For the transition period from _____ to _____

Commission File Number	Exact Name of Each Registrant as specified in its charter; State of Incorporation; Address; and Telephone Number	IRS Employer Identification No.
1-8962	PINNACLE WEST CAPITAL CORPORATION (an Arizona corporation) 400 North Fifth Street, P.O. Box 53999 Phoenix, Arizona 85072-3999 (602) 250-1000	86-0512431
1-4473	ARIZONA PUBLIC SERVICE COMPANY (an Arizona corporation) 400 North Fifth Street, P.O. Box 53999 Phoenix, Arizona 85072-3999 (602) 250-1000	86-0011170

Indicate by check mark whether each 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. Yes ☒ No ☐

Indicate by check mark whether each registrant is an accelerated filer (as defined in Exchange Act Rule 12b-2).

PINNACLE WEST CAPITAL CORPORATION	Yes <input checked="" type="checkbox"/>	No <input type="checkbox"/>
ARIZONA PUBLIC SERVICE COMPANY	Yes <input type="checkbox"/>	No <input checked="" type="checkbox"/>

Indicate the number of shares outstanding of each of the issuer’s classes of common stock as of the latest practicable date.	
PINNACLE WEST CAPITAL CORPORATION	Number of shares of common stock, no par value, outstanding as of August 8, 2005: 98,760,860
ARIZONA PUBLIC SERVICE COMPANY	Number of shares of common stock, \$2.50 par value, outstanding as of August 8, 2005: 71,264,947

Arizona Public Service Company meets the conditions set forth in General Instruction H(1)(a) and (b) of Form 10-Q and is therefore filing this form with the reduced disclosure format allowed under that General Instruction.

This combined Form 10-Q is separately filed by Pinnacle West Capital Corporation and Arizona Public Service Company. Each registrant is filing on its own behalf all of the information contained in this Form 10-Q that relates to such registrant. Neither registrant is filing any information that does not relate to such registrant, and therefore makes no representation as to any such information.

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GLOSSARY

ACC — Arizona Corporation Commission

ADEQ — Arizona Department of Environmental Quality

ALJ — Administrative Law Judge

APS — Arizona Public Service Company, a subsidiary of the Company

APS Energy Services — APS Energy Services Company, Inc., a subsidiary of the Company

CC&N — Certificate of Convenience and Necessity

Clean Air Act — Clean Air Act, as amended

Company — Pinnacle West Capital Corporation

DOE — United States Department of Energy

EITF — FASB's Emerging Issues Task Force

El Dorado — El Dorado Investment Company, a subsidiary of the Company

EPA — United States Environmental Protection Agency

ERMC — Energy Risk Management Committee

FASB — Financial Accounting Standards Board

FERC — United States Federal Energy Regulatory Commission

FIN — FASB Interpretation

Financing Order — ACC Order that authorized APS' \$500 million loan to Pinnacle West Energy in May 2003

GAAP — accounting principles generally accepted in the United States of America

IRS — United States Internal Revenue Service

March 2005 Form 10-Q — Pinnacle West/APS Quarterly Report on Form 10-Q for the fiscal quarter ended March 31, 2005

Moody's — Moody's Investors Service

MW — megawatt, one million watts

MWh — megawatt-hours, one million watts per hour

NAC — collectively, NAC Holding Inc. and NAC International Inc., subsidiaries of El Dorado that were sold in November 2004

Native Load — retail and wholesale sales supplied under traditional cost-based rate regulation

NPC — Nevada Power Company

NRC — United States Nuclear Regulatory Commission

Nuclear Waste Act — Nuclear Waste Policy Act of 1982, as amended

OCI — other comprehensive income

Off-System Sales — sales of electricity from generation owned by the Company that is over and above the amount required to serve the Company's retail customers and traditional wholesale contracts

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Palo Verde — Palo Verde Nuclear Generating Station, also known as ANPP

Pinnacle West — Pinnacle West Capital Corporation, the Company

Pinnacle West Energy — Pinnacle West Energy Corporation, a subsidiary of the Company

PPL Sundance — PPL Sundance Energy, LLC

PRP — potentially responsible party

PSA — power supply adjuster

PWEC Dedicated Assets — the following Pinnacle West Energy power plants, each of which is dedicated to serving APS’ customers: Redhawk Units 1 and 2, West Phoenix Units 4 and 5 and Saguaro Unit 3

PX — California Power Exchange

RFP — request for proposals

Salt River Project — Salt River Project Agricultural Improvement and Power District

SEC — United States Securities and Exchange Commission

SFAS — Statement of Financial Accounting Standards

Silverhawk — Silverhawk Power Station, a 570-megawatt, natural gas-fueled, combined-cycle electric generating facility located 20 miles north of Las Vegas, Nevada

Standard & Poor’s — Standard & Poor’s Corporation

SunCor — SunCor Development Company, a subsidiary of the Company

Sundance Plant -450-megawatt generating facility located approximately 55 miles southeast of Phoenix, Arizona

Superfund — Comprehensive Environmental Response, Compensation and Liability Act

T&D — transmission and distribution

Track B Order — ACC order dated March 14, 2003 regarding competitive solicitation requirements for power purchases by Arizona’s investor-owned electric utilities

Trading — energy-related activities entered into with the objective of generating profits on changes in market prices

2004 Settlement Agreement — an agreement settling APS’ general rate case

2004 Form 10-K — Pinnacle West/APS Annual Report on Form 10-K for the fiscal year ended December 31, 2004

VIE — variable interest entity

PART I — FINANCIAL INFORMATION

ITEM 1. FINANCIAL STATEMENTS

PINNACLE WEST CAPITAL CORPORATION CONDENSED CONSOLIDATED STATEMENTS OF INCOME (unaudited) (dollars and shares in thousands, except per share amounts)

	Three Months Ended June 30,	
	2005	2004
OPERATING REVENUES		
Regulated electricity segment	\$ 579,652	\$ 519,929
Marketing and trading segment	71,172	110,156
Real estate segment	84,753	66,084
Other revenues	20,259	9,414
Total	<u>755,836</u>	<u>705,583</u>
OPERATING EXPENSES		
Regulated electricity segment purchased power and fuel	160,590	151,642
Marketing and trading segment purchased power and fuel	57,593	88,067
Operations and maintenance	153,097	138,595
Real estate operations segment	68,593	62,217
Depreciation and amortization	85,142	102,012
Taxes other than income taxes	34,638	32,308
Other expenses	17,556	7,575
Total	<u>577,209</u>	<u>582,416</u>
OPERATING INCOME	<u>178,627</u>	<u>123,167</u>
OTHER		
Allowance for equity funds used during construction	2,952	2,184
Other income (Note 14)	8,684	36,496
Other expense (Note 14)	(3,846)	(3,371)
Total	<u>7,790</u>	<u>35,309</u>
INTEREST EXPENSE		
Interest charges	49,781	42,061
Capitalized interest	(3,544)	(2,681)
Total	<u>46,237</u>	<u>39,380</u>
INCOME FROM CONTINUING OPERATIONS BEFORE INCOME TAXES	140,180	119,096
INCOME TAXES	55,024	45,028
INCOME FROM CONTINUING OPERATIONS	85,156	74,068
Loss from discontinued operations — net of income tax benefit of \$37,710 and \$798 (Note 17)	(58,421)	(1,428)
NET INCOME	<u>\$ 26,735</u>	<u>\$ 72,640</u>
WEIGHTED-AVERAGE COMMON SHARES OUTSTANDING — BASIC	96,192	91,315
WEIGHTED-AVERAGE COMMON SHARES OUTSTANDING — DILUTED	96,299	91,400
EARNINGS PER WEIGHTED — AVERAGE COMMON SHARE OUTSTANDING		
Income from continuing operations — basic	\$ 0.89	\$ 0.81
Net income — basic	0.28	0.80
Income from continuing operations — diluted	0.88	0.81
Net income — diluted	0.28	0.79
DIVIDENDS DECLARED PER SHARE	\$ —	\$ —

See Notes to Pinnacle West's Condensed Consolidated Financial Statements.

PINNACLE WEST CAPITAL CORPORATION
CONDENSED CONSOLIDATED STATEMENTS OF INCOME
(unaudited)
(dollars and shares in thousands, except per share amounts)

	Six Months Ended June 30,	
	2005	2004
OPERATING REVENUES		
Regulated electricity segment	\$ 995,682	\$ 935,393
Marketing and trading segment	160,429	198,840
Real estate segment	156,809	116,547
Other revenues	30,394	20,319
Total	<u>1,343,314</u>	<u>1,271,099</u>
OPERATING EXPENSES		
Regulated electricity segment purchased power and fuel	239,013	240,253
Marketing and trading segment purchased power and fuel	128,402	155,832
Operations and maintenance	308,181	275,981
Real estate operations segment	125,069	109,510
Depreciation and amortization	176,535	203,115
Taxes other than income taxes	69,203	62,638
Other expenses	25,930	16,325
Total	<u>1,072,333</u>	<u>1,063,654</u>
OPERATING INCOME	<u>270,981</u>	<u>207,445</u>
OTHER		
Allowance for equity funds used during construction	5,555	4,186
Other income (Note 14)	9,487	47,330
Other expense (Note 14)	(8,232)	(9,316)
Total	<u>6,810</u>	<u>42,200</u>
INTEREST EXPENSE		
Interest charges	96,042	88,617
Capitalized interest	(6,833)	(4,180)
Total	<u>89,209</u>	<u>84,437</u>
INCOME FROM CONTINUING OPERATIONS BEFORE INCOME TAXES	188,582	165,208
INCOME TAXES	<u>73,685</u>	<u>60,439</u>
INCOME FROM CONTINUING OPERATIONS	114,897	104,769
Loss from discontinued operations — net of income tax benefit of \$41,120 and \$330 (Note 17)	(63,714)	(703)
NET INCOME	<u>\$ 51,183</u>	<u>\$ 104,066</u>
WEIGHTED-AVERAGE COMMON SHARES OUTSTANDING — BASIC	94,089	91,304
WEIGHTED-AVERAGE COMMON SHARES OUTSTANDING — DILUTED	94,189	91,391
EARNINGS PER WEIGHTED — AVERAGE COMMON SHARE OUTSTANDING		
Income from continuing operations — basic	\$ 1.22	\$ 1.15
Net income — basic	0.54	1.14
Income from continuing operations — diluted	1.22	1.15
Net income — diluted	0.54	1.14
DIVIDENDS DECLARED PER SHARE	\$ 0.95	\$ 0.90

See Notes to Pinnacle West's Condensed Consolidated Financial Statements.

PINNACLE WEST CAPITAL CORPORATION
CONDENSED CONSOLIDATED BALANCE SHEETS
(unaudited)
(dollars in thousands)

	June 30, 2005	December 31, 2004
ASSETS		
CURRENT ASSETS		
Cash and cash equivalents	\$ 300,403	\$ 163,366
Investment in debt securities	329,719	181,175
Customer and other receivables	335,316	367,863
Allowance for doubtful accounts	(4,574)	(4,896)
Accrued utility revenues	130,565	93,227
Materials and supplies (at average cost)	105,630	101,333
Fossil fuel (at average cost)	26,596	20,512
Assets from risk management and trading activities (Note 10)	305,711	166,896
Assets held for sale (Note 17)	241,943	—
Other current assets	80,581	47,654
Total current assets	1,851,890	1,137,130
INVESTMENTS AND OTHER ASSETS		
Real estate investments — net	349,129	382,398
Assets from long-term risk management and trading activities (Note 10)	314,309	224,341
Decommissioning trust accounts	276,746	267,700
Other assets	110,685	107,212
Total investments and other assets	1,050,869	981,651
PROPERTY, PLANT AND EQUIPMENT		
Plant in service and held for future use	10,668,777	10,486,648
Less accumulated depreciation and amortization	3,582,292	3,365,954
Total	7,086,485	7,120,694
Construction work in progress	299,330	258,119
Intangible assets, net of accumulated amortization	112,154	105,486
Nuclear fuel, net of accumulated amortization	53,459	51,188
Net property, plant and equipment	7,551,428	7,535,487
DEFERRED DEBITS		
Deferred purchased power and fuel regulatory asset	33,785	—
Other regulatory assets	139,690	135,051
Other deferred debits	105,343	107,428
Total deferred debits	278,818	242,479
TOTAL ASSETS	\$ 10,733,005	\$ 9,896,747

See Notes to Pinnacle West's Condensed Consolidated Financial Statements.

PINNACLE WEST CAPITAL CORPORATION
CONDENSED CONSOLIDATED BALANCE SHEETS
(unaudited)
(dollars in thousands)

	June 30, 2005	December 31, 2004
LIABILITIES AND EQUITY		
CURRENT LIABILITIES		
Accounts payable	\$ 264,252	\$ 373,526
Accrued taxes	316,180	245,611
Accrued interest	39,851	38,795
Short-term borrowings	93,388	71,030
Current maturities of long-term debt	652,213	617,165
Customer deposits	57,480	55,558
Deferred income taxes	9,057	9,057
Liabilities from risk management and trading activities (Note 10)	245,978	113,406
Liabilities held for sale (Note 17)	30,683	—
Other current liabilities	212,925	101,748
Total current liabilities	1,922,007	1,625,896
LONG-TERM DEBT LESS CURRENT MATURITIES	2,772,458	2,584,985
DEFERRED CREDITS AND OTHER		
Deferred income taxes	1,238,113	1,227,553
Regulatory liabilities	524,107	506,646
Liability for asset retirements	259,524	251,612
Pension liability	251,680	234,445
Liabilities from long term risk management and trading activities (Note 10)	137,264	156,262
Unamortized gain — sale of utility plant	48,045	50,333
Other	327,379	308,819
Total deferred credits and other	2,786,112	2,735,670
COMMITMENTS AND CONTINGENCIES (Notes 5, 12 and 13)		
COMMON STOCK EQUITY		
Common stock, no par value	2,038,608	1,769,047
Treasury stock	(1,340)	(428)
Total common stock	2,037,268	1,768,619
Accumulated other comprehensive income (loss):		
Minimum pension liability adjustment	(81,788)	(81,788)
Derivative instruments	132,007	59,243
Total accumulated other comprehensive income (loss)	50,219	(22,545)
Retained earnings	1,164,941	1,204,122
Total common stock equity	3,252,428	2,950,196
TOTAL LIABILITIES AND EQUITY	\$ 10,733,005	\$ 9,896,747

See Notes to Pinnacle West's Condensed Consolidated Financial Statements.

PINNACLE WEST CAPITAL CORPORATION
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS
(unaudited)
(dollars in thousands)

	Six Months Ended June 30,	
	2005	2004
CASH FLOWS FROM OPERATING ACTIVITIES		
Net Income	\$ 51,183	\$ 104,066
Adjustment to reconcile net income to net cash provided by operating activities:		
Silverhawk impairment loss	91,057	—
Equity earnings in Phoenix Suns partnership	—	(34,594)
Depreciation and amortization	181,994	205,745
Deferred purchased power and fuel	(33,785)	—
Nuclear fuel amortization	3,619	14,501
Allowance for equity funds used during construction	(5,555)	(4,186)
Deferred income taxes	(36,209)	23,854
Change in mark-to-market valuations	(17,436)	2,413
Changes in current assets and liabilities:		
Customer and other receivables	37,682	26,335
Accrued utility revenues	(37,338)	(37,429)
Materials, supplies and fossil fuel	(15,773)	2,760
Other current assets	(33,031)	27,097
Accounts payable	(107,299)	(11,041)
Accrued taxes	70,268	18,938
Accrued interest	1,056	(13,442)
Other current liabilities	113,099	31,839
Proceeds from the sale of real estate assets	41,259	29,266
Real estate investments	(39,968)	(24,851)
Change in risk management and trading activities — assets	16,360	12,402
Change in risk management and trading activities — liabilities	5,603	1,119
Change in pension liability	7,238	29,673
Change in other long-term assets	6,017	(26,178)
Change in other long-term liabilities	34,105	18,133
Net cash flow provided by operating activities	<u>334,146</u>	<u>396,420</u>
CASH FLOWS FROM INVESTING ACTIVITIES		
Capital expenditures	(302,880)	(264,571)
Purchase of Sundance	(185,046)	—
Proceeds from the sale of 25% of Silverhawk	—	93,378
Capitalized interest	(6,833)	(9,031)
Purchases of investment securities	(1,579,906)	(293,145)
Proceeds from sale of investment securities	1,431,348	285,195
Other	(5,326)	(12,863)
Net cash flow used for investing activities	<u>(648,643)</u>	<u>(201,037)</u>
CASH FLOWS FROM FINANCING ACTIVITIES		
Issuance of long-term debt	664,003	476,268
Short-term borrowings and payments — net	16,253	41,721
Dividends paid on common stock	(90,364)	(82,192)
Repayment of long-term debt	(430,673)	(602,831)
Common stock equity issuance	271,069	—
Other	21,246	6,738
Net cash flow provided by (used for) financing activities	<u>451,534</u>	<u>(160,296)</u>
NET INCREASE IN CASH AND CASH EQUIVALENTS	137,037	35,087
CASH AND CASH EQUIVALENTS AT BEGINNING OF PERIOD	163,366	136,929
CASH AND CASH EQUIVALENTS AT END OF PERIOD	<u>\$ 300,403</u>	<u>\$ 172,016</u>
Supplemental disclosure of cash flow information		
Cash paid during the period for:		
Income taxes paid — net of refunds	\$ 7,733	\$ 7,300
Interest paid, net of amounts capitalized	\$ 132,994	\$ 119,458

See Notes to Pinnacle West's Condensed Consolidated Financial Statements.

PINNACLE WEST CAPITAL CORPORATION
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

1. Consolidation and Nature of Operations

The condensed consolidated financial statements include the accounts of Pinnacle West and our wholly-owned subsidiaries: APS, Pinnacle West Energy, APS Energy Services, SunCor and El Dorado. All significant intercompany accounts and transactions between the consolidated companies have been eliminated. Our accounting records are maintained in accordance with GAAP. The preparation of financial statements in accordance with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities, disclosure of contingent assets and liabilities at the date of the financial statements and reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates. We have reclassified certain prior year amounts to conform to the current year presentation.

2. Condensed Consolidated Financial Statements

Our unaudited condensed consolidated financial statements reflect all adjustments which we believe are necessary for the fair presentation of our financial position, results of operations and cash flows for the periods presented. We suggest that these condensed consolidated financial statements and notes to condensed consolidated financial statements be read along with the consolidated financial statements and notes to consolidated financial statements included in our 2004 Form 10-K.

3. Quarterly Fluctuations

Weather conditions cause significant seasonal fluctuations in our revenues. In addition, real estate, trading and wholesale marketing activities can have significant impacts on our results for interim periods. For these reasons, results for interim periods do not necessarily represent results to be expected for the year.

4. Changes in Liquidity

On January 15, 2005, APS repaid its \$100 million 6.25% Notes due 2005. APS used cash on hand to repay these notes.

On March 1, 2005, Maricopa County, Arizona Pollution Control Corporation issued \$164 million of variable interest rate pollution control bonds, 2005 Series A-E, due 2029. The bonds were issued to refinance \$164 million of outstanding pollution control bonds. The Series A-E bonds are payable solely from revenues obtained from APS pursuant to a loan agreement between APS and Maricopa County, Arizona Pollution Control Corporation. These bonds are classified as long-term debt on our Condensed Consolidated Balance Sheets.

On April 11, 2005, Pinnacle West Energy issued \$500 million of Floating Rate Senior Notes due April 1, 2007. Pinnacle West has unconditionally guaranteed these notes. Pinnacle West Energy used the proceeds of this issuance to repay a \$500 million loan from APS. See "ACC Financing Order" in Note 5. APS intends to transfer \$500 million in connection with Pinnacle West Energy's transfer of the PWEC Dedicated Assets to APS. In the interim, APS intends to invest the proceeds or use them for general corporate purposes. See "APS General Rate Case" in Note 5 for information regarding APS' acquisition of the PWEC Dedicated Assets.

PINNACLE WEST CAPITAL CORPORATION
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

On May 2, 2005, Pinnacle West redeemed at par all of its \$165 million Floating Rate Senior Notes due November 1, 2005. Pinnacle West used cash on hand to redeem the notes.

On May 2, 2005, Pinnacle West issued 6,095,000 shares of its common stock at an offering price of \$42 per share, resulting in net proceeds of approximately \$248 million. Pinnacle West used the net proceeds for general corporate purposes, including making capital contributions to APS, which, in turn, used such funds to pay a portion of the approximately \$190 million purchase price to acquire the Sundance Plant and for other capital expenditures incurred to meet the growing needs of APS' service territory.

On August 1, 2005, APS repaid \$300 million of its 7.625% Notes due 2005. APS used cash on hand to repay these notes.

APS had \$566 million of pollution control bonds outstanding under which interest rates are reset on a daily, weekly or annual basis as of June 30, 2005. The holders of \$223 million of these bonds have the right to cause APS to purchase their bonds on the applicable reset date if the bonds are not remarketed. Of these bonds, \$50 million is classified as current maturities of long-term debt. The remaining \$173 million of bonds are classified as long-term debt because APS has the intent and ability, as demonstrated by credit agreements in place that extend for more than one year, to refinance any bonds that APS is required to purchase.

The following is a list of principal payments due on Pinnacle West's consolidated long-term debt and capitalized lease requirements as of June 30, 2005:

- \$352 million in 2005;
- \$389 million in 2006;
- \$674 million in 2007;
- \$6 million in 2008;
- \$1 million in 2009; and
- \$2.012 billion thereafter.

We have investments in auction rate securities in which interest rates are reset on a short-term basis; however, the underlying contract maturity dates extend beyond three months. We classify the investments in auction rate securities as investments in debt securities on our Condensed Consolidated Balance Sheets. The purchase and sale activities related to these investments have been reclassified on the Condensed Consolidated Statements of Cash Flows for the prior-year period to show purchases and sales on a gross basis.

PINNACLE WEST CAPITAL CORPORATION
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

5. Regulatory Matters

Electric Industry Restructuring

State

APS General Rate Case

On April 7, 2005, the ACC issued an order in the general rate case that APS filed on June 27, 2003. The order became final and non-appealable on April 28, 2005. In its order, the ACC approved the 2004 Settlement Agreement, with certain revisions. Certain key financial components of the order include:

- APS received an annual retail rate increase of approximately \$75.5 million, or 4.21%, which was effective as of April 1, 2005. This increase does not include the impact of the PSA (discussed below).
- The PSA provides for the annual adjustment of rates to reflect variations in fuel and purchased power costs, subject to specified parameters and procedures, including the following:
 - APS will record deferrals for recovery or refund to the extent actual fuel and purchased power costs vary from \$0.020743 per kWh (basic fuel amount);
 - The above deferrals are subject to a 90/10 sharing arrangement in which APS must absorb 10% of the costs above the base fuel amount and may retain 10% of the benefit from the costs that are below the base fuel amount;
 - amounts to be recovered or refunded through the annual PSA adjustment are limited to a cumulative plus or minus \$0.004 per kWh over the life of the PSA;
 - in addition, the ACC order provides for a PSA surcharge mechanism as follows:
 - each time the accumulated pretax net deferrals reach \$50 million, APS must notify the ACC, but prior to the deferral balance exceeding \$100 million, APS must file with the ACC to recover or refund such deferral balance through a surcharge;
 - amounts recovered or refunded through any surcharge are not included in the \$0.004 per kWh PSA annual adjustment limit;
 - the recoverable amount of net fuel and purchased power costs through base rates and the \$0.004 per kWh adjustment is capped at \$776.2 million per year - PSA surcharge amounts are not included in the \$776.2 million annual limits on fuel and purchased power recovery (APS does not expect such costs to exceed \$776.2 million in 2005);

PINNACLE WEST CAPITAL CORPORATION
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

- the PSA will remain in effect for a minimum five-year period, but the ACC may eliminate the PSA at any time, if appropriate, in the event APS files a rate case before the expiration of the five-year period or if APS does not comply with the terms of the PSA;
 - APS filed a request for a PSA surcharge on July 22, 2005 (see discussion below); and
 - the first regular annual adjustment to the PSA would be on April 1, 2006, and is expected to be for the full \$0.004 per kWh permitted by the ACC's order, which is in addition to the PSA surcharge requested on July 22, 2005.
- The 2004 Settlement Agreement included a self-build moratorium for generating plants to be in service prior to January 1, 2015. The ACC order modified that moratorium to include the acquisition of a generating unit, or an interest in a generating unit, from any utility or merchant generator without prior ACC approval.
 - APS was authorized to acquire Redhawk Units 1 and 2, West Phoenix Units 4 and 5, and Saguaro Unit 3, which are dedicated to serving APS' customers (the "PWEC Dedicated Assets") from Pinnacle West Energy, with a net carrying value of approximately \$850 million, and to rate base the PWEC Dedicated Assets at a rate base value of \$700 million, which will result in a mandatory rate base disallowance of approximately \$150 million. This transfer was approved by the FERC on June 15, 2005 and completed on July 29, 2005. As a result, for financial reporting purposes, APS will recognize a one-time, after-tax net plant write-off of approximately \$90 million during the third quarter of 2005.
 - To bridge the time between the effective date of the rate increase and the actual date the PWEC Dedicated Assets transfer, effective April 1, 2005, APS and PWEC entered into a cost-based purchase power agreement (the "Bridge PPA"), which was based on the value of the PWEC Dedicated Assets. When the Bridge PPA became effective, prior power purchase agreements entered into between APS and PWEC were terminated. The Bridge PPA was terminated on July 29, 2005, upon Pinnacle West Energy's transfer of the PWEC Dedicated Assets to APS.
 - Effective April 1, 2005, APS adopted longer service lives in accordance with the 2004 Settlement Agreement for certain depreciable assets. This change is expected to have the effect of reducing annual depreciation expense for financial reporting purposes by approximately \$30 million. Also in accordance with the 2004 Settlement Agreement, we adopted longer service lives for the PWEC Dedicated Assets, which is expected to have the effect of reducing annual depreciation expense for financial reporting purposes by approximately \$10 million.

Power Supply Adjuster

On July 22, 2005, APS filed an Application for Surcharge with the ACC requesting recovery of \$100 million in deferred purchased power and fuel costs under the PSA approved by the ACC in APS' recent general rate case. As required by the ACC order approving the PSA, APS filed the Application for Surcharge after the PSA "bank balance" reached \$50 million and before it reached

PINNACLE WEST CAPITAL CORPORATION
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

\$100 million, which APS expects to occur by mid-August of this year. APS proposes to recover the \$100 million PSA bank balance over a 24-month period beginning with the billing cycle one of November 2005. The requested PSA surcharge represents an approximate 2.2% temporary increase in overall APS retail revenues.

Equity Infusion Notice

On July 20, 2005, Pinnacle West filed a Notice with the ACC indicating its intent to infuse more than \$100 million of equity into APS during each of 2005, 2006 and subsequent years. Under Arizona law and decisions, Pinnacle West is required to give such notice at least 120 days prior to such an equity infusion into APS. The ACC may, but need not, take action on this Notice. If the ACC takes no action within the 120 day notice period, Pinnacle West may thereafter make the proposed equity infusions, at management's discretion.

ACC Financing Order

On May 12, 2003, APS issued \$500 million of debt pursuant to the Financing Order and made a \$500 million loan to Pinnacle West Energy. Pinnacle West Energy distributed the net proceeds of that loan to the Company to fund the repayment of a portion of the debt incurred to finance the construction of the PWEC Dedicated Assets. On April 11, 2005, this loan was repaid with the proceeds of a new debt issuance by Pinnacle West Energy. See "Capital Needs and Resources — By Company — Pinnacle West Energy" in Part I, Item 2 below.

The ACC granted the Financing Order subject to various conditions. One of these conditions is that APS must maintain a common equity ratio of at least 40% and may not pay common dividends if such payment would reduce its common equity ratio below that threshold, unless otherwise waived by the ACC. This condition is an ongoing requirement and was not affected by Pinnacle West Energy's repayment of APS' \$500 million loan.

Retail Electric Competition Rules

In 1999, the ACC approved rules for the introduction of retail electric competition in Arizona. The rules include the following major provisions:

- They apply to virtually all Arizona electric utilities regulated by the ACC, including APS.
- Effective January 1, 2001, retail access became available to all APS retail electricity customers.

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- Electric service providers that get CC&N's from the ACC can supply only competitive services, including electric generation, but not electric transmission and distribution.
- Affected utilities must file ACC tariffs that unbundle rates for noncompetitive services.
- The ACC shall allow a reasonable opportunity for recovery of unmitigated stranded costs.

On November 27, 2000, a Maricopa County, Arizona, Superior Court judge issued a final judgment holding that the rules are unconstitutional and unlawful in their entirety due to failure to establish a fair value rate base for competitive electric service providers and because certain of the rules were not submitted to the Arizona Attorney General for certification. The judgment also invalidates all ACC orders authorizing competitive electric service providers, including APS Energy Services, to operate in Arizona. The ACC and other parties aligned with the ACC appealed the ruling to the Arizona Court of Appeals, and in January 2004, the Court invalidated some, but not all, of the rules as either violative of Arizona's constitutional requirement that the ACC consider the "fair value" of a utility's property in setting rates or as being beyond the ACC's constitutional and statutory powers. Other rules were set aside for failure to submit such regulations to the Arizona Attorney General for certification as required by statute. A request for the Arizona Supreme Court to review the Court of Appeals decision was denied on January 4, 2005. To date, the ACC has taken no action on either the rules or the orders authorizing competitive electric service providers in response to the now final Court of Appeals decision. As a result, at present only limited electric retail competition exists in Arizona and only with certain entities not regulated by the ACC.

Track B Order

On March 14, 2003, the ACC issued the Track B Order, which required APS to solicit bids for certain estimated amounts of capacity and energy for periods beginning July 1, 2003. By May 6, 2003, APS entered into contracts to meet all or a portion of its requirements for the years 2003 through 2006 as follows:

- (1) Pinnacle West Energy agreed to provide 1,700 MW in July through September of 2003 and in June through September of 2004, 2005 and 2006, by means of a unit contingent contract.
- (2) PPL EnergyPlus, LLC agreed to provide 112 MW in July through September of 2003 and 150 MW in June through September of 2004 and 2005, by means of a unit contingent contract.
- (3) Panda Gila River LP agreed to provide 450 MW in October of 2003 and 2004 and May of 2004 and 2005, and 225 MW from November 2003 through April 2004 and from November 2004 through April 2005, by means of firm call options.

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With final ACC approval of the 2004 Settlement Agreement, the Track B contract with Pinnacle West Energy was cancelled, effective April 1, 2005 and replaced by the Bridge PPA. Also, the Track B contract with PPL was cancelled upon closing of the purchase of the Sundance Plant. On May 13, 2005, APS acquired the Sundance Plant from PPL Sundance for a purchase price of approximately \$190 million.

General

Although some very limited retail competition existed in APS' service area in 1999 and 2000, there are currently no active retail competitors providing unbundled energy or other utility services to APS' customers. As a result, we cannot predict when, and the extent to which, additional competitors will re-enter APS' service territory.

Federal

In July 2002, the FERC adopted a price mitigation plan that constrains the price of electricity in the wholesale spot electricity market in the western United States. The FERC adopted a price cap of \$250 per MWh for the period subsequent to October 31, 2002. Sales at prices above the cap must be justified and are subject to potential refund.

On July 31, 2002, the FERC issued a Notice of Proposed Rulemaking for Standard Market Design for wholesale electric markets and, on April 28, 2003, the FERC Staff issued an additional white paper on the proposed Standard Market Design. On July 19, 2005, the FERC terminated the rulemaking proceeding.

On August 11, 2004, Pinnacle West, APS, Pinnacle West Energy, and APS Energy Services (collectively, the "Pinnacle West Companies") submitted to the FERC an update to its three-year market-based rate review, pursuant to the FERC's order implementing a new generation market power analysis. On December 20, 2004, the FERC issued an order approving market-based rates for control areas other than those of APS, Public Service Company of New Mexico and Tucson Electric Company. The order required the Pinnacle West Companies to submit additional data with respect to these control areas, and on February 18, 2005, the Pinnacle West Companies submitted such data. On April 11, 2005, APS and a group of APS wholesale electric customers, the Arizona Districts, submitted a settlement that resolved concerns raised by the Arizona Districts in the proceeding. On May 2, 2005, a protest and a motion to intervene were filed by the Yavapai-Apache Energy Office with respect to the settlement between APS and the Arizona Districts. On April 5, 2005, the FERC issued a deficiency letter seeking further information from the Pinnacle West Companies relating to the APS control area and the Pinnacle West Companies filed a response on April 22, 2005. The notice period for filing comments on that response expired on May 5, 2005, and no additional comments were filed. We cannot currently predict the outcome of this proceeding, but we do not believe that the outcome will have a material adverse effect on our financial position, results of operations or cash flows.

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6. Retirement Plans and Other Benefits

Pinnacle West sponsors a qualified defined benefit and account balance pension plan, a nonqualified supplemental excess benefit retirement plan, and other postretirement benefit plans for the employees of Pinnacle West and our subsidiaries.

The following table provides details of the plans' benefit costs for the three and six months ended June 30, 2005 and 2004. Also included is the portion of these costs charged to expense, including administrative costs and excluding amounts billed to electric plant participants or amounts capitalized as overhead construction (dollars in millions):

	Pension Benefits				Other Benefits			
	Three Months Ended June 30,		Six Months Ended June 30,		Three Months Ended June 30,		Six Months Ended June 30,	
	2005	2004	2005	2004	2005	2004	2005	2004
Service cost-benefits earned during the period	\$ 11	\$ 11	\$ 23	\$ 22	\$ 5	\$ 4	\$ 11	\$ 8
Interest cost on benefit obligation	21	21	44	43	9	7	17	14
Expected return on plan assets	(21)	(21)	(44)	(42)	(8)	(6)	(16)	(12)
Amortization of:								
Transition (asset) obligation	(1)	(1)	(2)	(2)	1	1	2	1
Prior service cost	1	1	1	1	—	—	—	—
Net actuarial loss	4	4	10	9	2	2	5	4
Net periodic benefit cost	<u>\$ 15</u>	<u>\$ 15</u>	<u>\$ 32</u>	<u>\$ 31</u>	<u>\$ 9</u>	<u>\$ 8</u>	<u>\$ 19</u>	<u>\$ 15</u>
Portion of cost charged to expense	<u>\$ 6</u>	<u>\$ 7</u>	<u>\$ 13</u>	<u>\$ 14</u>	<u>\$ 4</u>	<u>\$ 3</u>	<u>\$ 8</u>	<u>\$ 7</u>
APS share of costs charged to expense	<u>\$ 6</u>	<u>\$ 6</u>	<u>\$ 12</u>	<u>\$ 12</u>	<u>\$ 3</u>	<u>\$ 3</u>	<u>\$ 7</u>	<u>\$ 6</u>

Contributions

Our minimum required pension contribution in 2005 is approximately \$53 million. Of this amount, we have contributed approximately \$27 million through July 2005. The contribution to be made to other postretirement benefit plans in 2005 is estimated to be approximately \$37 million. Of this amount, we contributed approximately \$18 million through July 2005. APS' share is approximately 92% of both plans.

7. Business Segments

We have three principal business segments (determined by products, services and the regulatory environment):

- our regulated electricity segment, which consists of traditional regulated retail and wholesale electricity businesses (primarily electricity service to Native Load customers) and related activities and includes electricity generation, transmission and distribution;

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- our marketing and trading segment, which consists of our competitive energy business activities, including wholesale marketing and trading and APS Energy Services' commodity-related energy services; and
- our real estate segment, which consists of SunCor's real estate development and investment activities.

Financial data for the three and six months ended June 30, 2005 and 2004 and at June 30, 2005 and December 31, 2004 by business segment is provided as follows (dollars in millions):

	Three Months Ended June 30,		Six Months Ended June 30,	
	2005	2004	2005	2004
Operating Revenues:				
Regulated electricity (a)	\$ 580	\$ 520	\$ 996	\$ 935
Marketing and trading (a)	71	110	160	199
Real estate	85	66	157	117
Other	20	10	30	20
Total	<u>\$ 756</u>	<u>\$ 706</u>	<u>\$ 1,343</u>	<u>\$ 1,271</u>
Net Income (Loss):				
Regulated electricity (a)	\$ 69	\$ 40	\$ 83	\$ 55
Marketing and trading (a)(b)	(55)	6	(54)	19
Real estate	12	4	20	6
Other (c)	1	23	2	24
Total	<u>\$ 27</u>	<u>\$ 73</u>	<u>\$ 51</u>	<u>\$ 104</u>

- (a) Effective April 1, 2005, Off-System Sales of approximately \$12 million that would have previously been reported in the marketing and trading segment are now included in the regulated electricity segment in accordance with the retail rate settlement.
- (b) The 2005 periods include a \$59 million (after-tax) loss in discontinued operations related to the pending sale of Silverhawk.
- (c) The 2004 periods include \$21 million (after-tax) gain related to the sale of a limited partnership interest in the Phoenix Suns.

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	As of June 30, 2005	As of December 31, 2004
Assets:		
Regulated electricity	\$ 9,467	\$ 8,674
Marketing and trading	763	746
Real estate	477	454
Other	26	23
Total	<u>\$ 10,733</u>	<u>\$ 9,897</u>

8. New Accounting Standards

In December 2004, the FASB issued SFAS No. 123(R), "Share-Based Payment." The standard establishes accounting for transactions in which an entity exchanges its equity instruments for goods or services. It also addresses transactions in which an entity incurs liabilities in exchange for goods or services that are based on the fair value of the entity's equity instruments or that may be settled by the issuance of those equity instruments. SFAS No. 123(R) is effective for us as of January 1, 2006. We have evaluated the impacts of this new guidance and do not believe it will have a material impact on our financial statements.

In March 2005, the FASB issued FIN No. 47, "Accounting for Conditional Asset Retirement Obligations." FIN No. 47 clarifies that an entity must record a liability for the fair value of an asset retirement obligation for which the timing and (or) method of settlement are conditional on a future event if the liability's fair value can be reasonably estimated. FIN No. 47 is effective no later than the end of fiscal years ending after December 15, 2005. We are currently evaluating the new guidance, but do not expect the adoption of this interpretation to have a material impact on our financial statements.

9. Variable Interest Entities

In 1986, APS entered into agreements with three separate VIE lessors in order to sell and lease back interests in Palo Verde Unit 2. The leases are accounted for as operating leases in accordance with GAAP. We are not the primary beneficiary of the Palo Verde VIEs and, accordingly, do not consolidate them.

APS is exposed to losses under the Palo Verde sale leaseback agreements upon the occurrence of certain events that APS does not consider to be reasonably likely to occur. Under certain circumstances (for example, the NRC issuing specified violation orders with respect to Palo Verde or the occurrence of specified nuclear events), APS would be required to assume the debt associated with the transactions, make specified payments to the equity participants, and take title to the leased Unit 2 interests, which, if appropriate, may be required to be written down in value. If such an event had occurred as of June 30, 2005, APS would have been required to assume approximately \$245 million of debt and pay the equity participants approximately \$191 million.

10. Derivative and Energy Trading Accounting

We are exposed to the impact of market fluctuations in the commodity price of electricity, natural gas, coal and emissions allowances and in interest rates. We manage risks associated with

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these market fluctuations by utilizing various instruments that qualify as derivatives, including exchange-traded futures and options and over-the-counter forwards, options and swaps. As part of our overall risk management program, we use such instruments to hedge our exposure to changes in interest rates and to hedge purchases and sales of electricity, fuels, and emissions allowances and credits. As of June 30, 2005, we hedged exposures to the price variability of the commodities for a maximum of four years. The changes in market value of such contracts have a high correlation to price changes in the hedged transactions. In addition, subject to specified risk parameters monitored by the ERM, we engage in marketing and trading activities intended to profit from market price movements.

Cash Flow Hedges

The changes in the fair value of our hedged positions included in the Condensed Consolidated Statements of Income for the three and six months ended June 30, 2005 and 2004 were comprised of the following (dollars in thousands):

	Three Months Ended June 30,		Six Months Ended June 30,	
	2005	2004	2005	2004
Gains on the ineffective portion of derivatives qualifying for hedge accounting	\$ 4,514	\$ 88	\$ 11,837	\$ 1,472
Gains (losses) from the change in options' time value excluded from measurement of effectiveness	(1,189)	(17)	(331)	63
Gains from the discontinuance of cash flow hedges	—	—	385	1,137

During the twelve months ending June 30, 2006, we estimate that a net gain of \$87 million before income taxes will be reclassified from accumulated other comprehensive income as an offset to the effect of market price changes for the related hedged transactions.

Our assets and liabilities from risk management and trading activities are presented in two categories, consistent with our business segments:

- Regulated Electricity — non-trading derivative instruments that hedge our purchases and sales of electricity and fuel for APS' Native Load requirements of our regulated electricity business segment; and
- Marketing and Trading — both non-trading and trading derivative instruments of our competitive business segment.

The following table summarizes our assets and liabilities from risk management and trading activities at June 30, 2005 and December 31, 2004 (dollars in thousands):

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June 30, 2005

	Current Assets	Investments	Current Liabilities	Other Liabilities	Net Asset (Liability)
Regulated electricity:					
Mark-to-market	\$ 121,482	\$ 68,458	\$ (55,495)	\$ (8,346)	\$ 126,099
Options and futures — at cost	2,555	4	(11,123)	—	(8,564)
Marketing and trading:					
Mark-to-market	181,674	245,533	(147,094)	(128,918)	151,195
Options and futures and emission allowances - - at cost	—	314	(32,266)	—	(31,952)
Total	<u>\$ 305,711</u>	<u>\$ 314,309</u>	<u>\$ (245,978)</u>	<u>\$ (137,264)</u>	<u>\$ 236,778</u>

December 31, 2004

	Current Assets	Investments	Current Liabilities	Other Liabilities	Net Asset (Liability)
Regulated electricity:					
Mark-to-market	\$ 45,220	\$ 19,417	\$ (19,191)	\$ (12,000)	\$ 33,446
Options and margin account	18,821	118	(8,879)	—	10,060
Marketing and trading:					
Mark-to-market	102,855	204,512	(68,008)	(132,683)	106,676
Emission allowances - - at cost and margin account	—	294	(17,328)	(11,579)	(28,613)
Total	<u>\$ 166,896</u>	<u>\$ 224,341</u>	<u>\$ (113,406)</u>	<u>\$ (156,262)</u>	<u>\$ 121,569</u>

Cash or other assets may be required to serve as collateral against our open positions on certain energy-related contracts. Collateral provided to counterparties was \$6 million at June 30, 2005 and \$1 million at December 31, 2004, and is included in other current assets on the Condensed Consolidated Balance Sheets. Collateral provided to us by counterparties was \$122 million at June 30, 2005 and \$24 million at December 31, 2004, and is included in other current liabilities on the Condensed Consolidated Balance Sheets.

Fair Value Hedges

On January 29, 2004, we entered into two fixed-for-floating interest rate swap transactions on our \$300 million 6.4% Senior Notes. The purpose of these hedges is to protect against significant fluctuations in the fair value of our debt. Our interest rate swaps are considered to be fully effective with any resulting gains or losses on the derivative offset by a similar loss or gain amount on the underlying fair value of our debt. The fair value of the interest rate swaps was a loss of approximately \$2.7 million at June 30, 2005 and is included in other current liabilities with the corresponding offset in current maturities of long-term debt on the Condensed Consolidated Balance Sheets.

Credit Risk

We are exposed to losses in the event of nonperformance or nonpayment by counterparties. We have risk management and trading contracts with many counterparties, including one counterparty for which a worst case exposure represents approximately 16% of Pinnacle West's \$620 million of risk management and trading assets as of June 30, 2005. Our risk management process assesses and monitors the financial exposure of these and all other counterparties. Despite the fact that the great majority of trading counterparties are rated as investment grade by the credit rating agencies, including the counterparty discussed above, there is still a possibility that one or more of these companies could default, resulting in a material impact on consolidated earnings for a given period. Counterparties in the portfolio consist principally of major energy companies, municipalities, local distribution companies and financial institutions. We maintain credit policies that we believe minimize overall credit risk to within acceptable limits. Determination of the credit quality of our counterparties is based upon a number of factors, including credit ratings and our evaluation of their financial condition. In many contracts, we employ collateral requirements and standardized agreements that allow for the netting of positive and negative exposures associated with a single counterparty. Valuation adjustments are established representing our estimated credit losses on our overall exposure to counterparties.

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11. Comprehensive Income

Components of comprehensive income for the three and six months ended June 30, 2005 and 2004, are as follows (dollars in thousands):

	Three Months Ended June 30,		Six Months Ended June 30,	
	2005	2004	2005	2004
Net income	\$ 26,735	\$ 72,640	\$ 51,183	\$ 104,066
Other comprehensive income (loss):				
Unrealized gain (loss) on derivative instruments (a)	(24,220)	25,721	135,424	73,287
Reclassification of realized gain to income (b)	(9,769)	(6,318)	(15,688)	(6,480)
Income tax (expense) benefit related to items of other comprehensive income	13,334	(7,620)	(46,972)	(26,235)
Total other comprehensive income (loss)	(20,655)	11,783	72,764	40,572
Comprehensive income	\$ 6,080	\$ 84,423	\$ 123,947	\$ 144,638

(a) These amounts primarily include unrealized gains and losses on contracts used to hedge our forecasted electricity and gas requirements to serve Native Load.

(b) These amounts primarily include the reclassification of unrealized gains and losses to realized for contracted commodities delivered during the period.

12. Commitments and Contingencies
Palo Verde Nuclear Generating Station
Spent Nuclear Fuel and Waste Disposal

Nuclear power plant operators are required to enter into spent fuel disposal contracts with the DOE, and the DOE is required to accept and dispose of all spent nuclear fuel and other high-level radioactive wastes generated by domestic power reactors. Although the Nuclear Waste Act required the DOE to develop a permanent repository for the storage and disposal of spent nuclear fuel by 1998, the DOE has announced that the repository cannot be completed before 2010 and it does not intend to begin accepting spent nuclear fuel prior to that date. In

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November 1997, the United States Court of Appeals for the District of Columbia Circuit (D.C. Circuit) issued a decision preventing the DOE from excusing its own delay, but refused to order the DOE to begin accepting spent nuclear fuel. Based on this decision and the DOE's delay, a number of utilities, including APS (on behalf of itself and the other Palo Verde owners), filed damages actions against the DOE in the Court of Federal Claims. Arizona Public Service Company v. United States of America, United States Court of Federal Claims, 03-2832C.

APS currently estimates it will incur \$147 million (in 2004 dollars) over the life of Palo Verde for its share of the costs related to the on-site interim storage of spent nuclear fuel. At June 30, 2005, APS had a regulatory asset of \$10 million which represents amounts spent for on-site interim spent fuel storage net of amounts recovered in rates per the ACC rate order that was effective April 1, 2005.

California Energy Market Issues and Refunds in the Pacific Northwest

FERC

In July 2001, the FERC ordered an expedited fact-finding hearing to calculate refunds for spot market transactions in California during a specified time frame. APS was a seller and a purchaser in the California markets at issue, and to the extent that refunds are ordered, APS should be a recipient as well as a payor of such amounts. The FERC is still considering the evidence and refund amounts have not yet been finalized. APS does not anticipate material changes in its exposure and still believes, subject to the finalization of the revised proxy prices, that it will be entitled to a net refund.

On March 19, 2002, the State of California filed a complaint with the FERC alleging that wholesale sellers of power and energy, including the Company, failed to properly file rate information at the FERC in connection with sales to California from 2000 to the present under market-based rates. State of California v. British Columbia Power Exchange et al., Docket No. EL02-71-000. The complaint requests the FERC to require the wholesale sellers to refund any rates that are "found to exceed just and reasonable levels." This complaint was dismissed by the FERC and the State of California appealed the matter to the Ninth Circuit Court of Appeals. In an order issued September 9, 2004, the Ninth Circuit upheld the FERC's authority to permit market-based rates, but rejected the FERC's claim that it was without authority to consider retroactive refunds when a utility has not strictly adhered to the quarterly reporting requirements of the market-based rate system. On September 9, 2004, the Ninth Circuit remanded the case to the FERC for further proceedings. State of California ex rel. Bill Lockyer, Attorney General v. FERC, No. 02-73093. Several of the intervenors in this appeal filed a petition for rehearing of this decision on October 25, 2004. The petition for rehearing has not been acted upon, and the outcome of the further proceedings cannot be predicted at this time.

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The FERC also ordered an evidentiary proceeding to discuss and evaluate possible refunds for the Pacific Northwest. The FERC affirmed the ALJ's conclusion that the prices in the Pacific Northwest were not unreasonable or unjust and refunds should not be ordered in this proceeding. This decision has now been appealed to the Ninth Circuit Court of Appeals. Although the FERC ruling in the Pacific Northwest matter is being appealed and the FERC has not yet calculated the specific refund amounts due in California, we do not expect that the resolution of these issues, as to the amounts alleged in the proceedings, will have a material adverse impact on our financial position, results of operations or cash flows.

On March 26, 2003, FERC made public a Final Report on Price Manipulation in Western Markets, prepared by its staff and covering spot markets in the West in 2000 and 2001. The report stated that a significant number of entities who participated in the California markets during the 2000-2001 time period, including APS, may potentially have been involved in arbitrage transactions that allegedly violated certain provisions of the Independent System Operator tariff. After reviewing the matter, along with the data supplied by APS, the FERC staff moved to dismiss the claims against APS and to dismiss the proceeding. The motion to dismiss was granted by the FERC on January 22, 2004. Certain parties have sought rehearing of this order, and that request is pending.

California Civil Energy Market Litigation

The State of California and others have filed various claims, which have now been consolidated, against several power suppliers to California alleging antitrust violations. Wholesale Electricity Antitrust Cases I and II, Superior Court in and for the County of San Diego, Proceedings Nos. 4204-00005 and 4204-00006. Two of the suppliers who were named as defendants in those matters, Reliant Energy Services, Inc. (and other Reliant entities) and Duke Energy and Trading, LLP (and other Duke entities), filed cross-claims against various other participants in the PX and California independent system operator markets, including APS, attempting to expand those matters to such other participants. On December 13, 2002, the judge remanded the case to state court for the second time and the matter was appealed. On December 8, 2004, the Ninth Circuit issued its opinion on immunity on certain unrelated defendants. The cross-defendants will not be required to respond until the Court rules on pending motions. APS believes the claims by Reliant and Duke as they relate to APS are without merit.

APS was also named in a lawsuit regarding wholesale contracts in California, which, after being moved to state court, has been removed to the federal court for a second time. James Millar, et al. v. Allegheny Energy Supply, et al., San Francisco Superior Court, Case No. 407867, U.S. District Court (Northern District) C-04-0519 SBA. The First Amended Complaint alleges basically that the contracts entered into were the result of an unfair and unreasonable market, in violation of California unfair competition laws. The defendants have filed a motion in the state court requesting that the case be dismissed and expect a ruling prior to trial within the next several months. The PX has filed a lawsuit against the State of California regarding the seizure of forward contracts and the State has filed a cross complaint against APS and numerous other PX participants. Cal PX v. The State of California, Superior Court in and for the County of Sacramento, JCCP No. 4203. Various motions continue to be filed, and we currently believe these claims will have no material adverse impact on our financial position, results of operations or cash flows.

Natural Gas Supply

Pursuant to the terms of a comprehensive settlement entered into in 1996 with El Paso Natural Gas Company, the rates charged for natural gas transportation are subject to a rate moratorium through December 31, 2005.

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On July 9, 2003 the FERC issued an order that altered the capacity rights of parties to the 1996 settlement but maintained the cost responsibility provisions agreed to by parties to that settlement. On December 28, 2004, the D.C. Court of Appeals upheld the FERC's authority to alter the capacity rights of parties to the settlement. With respect to the FERC's authority to maintain the cost responsibility provisions of the settlement, a party has sought appellate review and is seeking to reallocate the costs responsibility associated with the changed contractual obligations in a way that would be less favorable to APS and Pinnacle West Energy than under the FERC's July 9, 2003 order. Should this party prevail on this point, APS and Pinnacle West Energy's annual capacity cost could be increased by approximately \$3 million per year, from September 2003 through December 2005.

Consistent with its obligations under the 1996 settlement, El Paso filed a new rate case on June 30, 2005, which proposes new rates and new services to become effective on January 1, 2006. Protests were filed on July 12, 2005.

Navajo Nation Litigation

In June 1999, the Navajo Nation served Salt River Project with a lawsuit naming Salt River Project, several Peabody Coal Company entities (collectively, "Peabody"), Southern California Edison Company and other defendants, and citing various claims in connection with the renegotiations of the coal royalty and lease agreements under which Peabody mines coal for the Navajo Generating Station and the Mohave Generating Station. The Navajo Nation v. Peabody Holding Company, Inc., et al., United States District Court for the District of Columbia, CA-99-0469-EGS (the "D.C. Lawsuit"). APS is a 14% owner of the Navajo Generating Station, which Salt River Project operates. The D.C. Lawsuit alleges, among other things, that the defendants obtained a favorable coal royalty rate by improperly influencing the outcome of a federal administrative process under which the royalty rate was to be adjusted. The suit seeks \$600 million in damages, treble damages, punitive damages of not less than \$1 billion, and the ejection of defendants "from all possessory interests and Navajo Tribal lands arising out of the [primary coal lease]". In July 2001, the court dismissed all claims against Salt River Project.

In January, 2005, Peabody served APS with a lawsuit naming APS and the other Navajo Generating Station participants and seeking, among other things, a declaration that the participants "are obligated to reimburse Peabody for any royalty, tax, or other obligation arising out of the D.C. Lawsuit". Peabody Western Coal Company v. Salt River Project Agricultural Improvement and Power District, et al., Circuit Court for the City of St. Louis, Division No. 1, Cause No. 042-08561. Based on APS' ownership interest in the Navajo Generating Station, APS could be liable for up to 14% of any such obligation. Because the litigation is in preliminary stages, APS cannot currently predict the outcome of this matter.

Environmental Matters

Superfund Superfund establishes liability for the cleanup of hazardous substances found contaminating the soil, water or air. Those who generated, transported or disposed of hazardous substances at a contaminated site are among those who are PRPs. PRPs may be strictly, and often jointly and severally, liable for clean-up. On September 3, 2003, the EPA advised APS that the EPA considers APS to be a PRP in the Motorola 52nd Street Superfund Site, Operable Unit 3 (OU3) in Phoenix, Arizona. APS has facilities that are within this Superfund site. APS

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and Pinnacle West have agreed with the EPA to perform certain investigative activities of the APS facilities within OU3. Because the investigation has not yet been completed and ultimate remediation requirements are not yet finalized, neither APS nor Pinnacle West can currently estimate the expenditures which may be required.

Litigation

We are party to various other claims, legal actions and complaints arising in the ordinary course of business, including but not limited to environmental matters related to the Clean Air Act, Navajo Nation issues and EPA and ADEQ issues. In our opinion, the ultimate resolution of these matters will not have a material adverse effect on our financial position, results of operations or cash flows.

13. Nuclear Insurance

The Palo Verde participants have insurance for public liability resulting from nuclear energy hazards to the full limit of liability under federal law. This potential liability is covered by primary liability insurance provided by commercial insurance carriers in the amount of \$300 million and the balance by an industry-wide retrospective assessment program. If losses at any nuclear power plant covered by the programs exceed the accumulated funds, APS could be assessed retrospective premium adjustments. The maximum assessment per reactor under the program for each nuclear incident is approximately \$101 million, subject to an annual limit of \$10 million per incident. Based on APS' interest in the three Palo Verde units, APS' maximum potential assessment per incident for all three units is approximately \$88 million, with an annual payment limitation of approximately \$9 million.

The Palo Verde participants maintain "all risk" (including nuclear hazards) insurance for property damage to, and decontamination of, property at Palo Verde in the aggregate amount of \$2.75 billion, a substantial portion of which must first be applied to stabilization and decontamination. APS has also secured insurance against portions of any increased cost of generation or purchased power and business interruption resulting from a sudden and unforeseen outage of any of the three units. The insurance coverage discussed in this and the previous paragraph is subject to certain policy conditions and exclusions.

Possible Price-Anderson Act Changes

Versions of comprehensive energy bills signed by the President on August 8, 2005 contain provisions that would amend the Price-Anderson Act, addressing public liability from nuclear energy hazards in ways that would increase the annual limit on retrospective assessments from \$10.0 million to \$15.0 million per reactor per incident with APS' annual exposure per incident increasing from \$9.0 million to \$13 million.

14. Other Income and Other Expense

The following table provides detail of other income and other expense for the three and six months ended June 30, 2005 and 2004 (dollars in thousands):

PINNACLE WEST CAPITAL CORPORATION
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

	Three Months Ended June 30,		Six Months Ended June 30,	
	2005	2004	2005	2004
Other income:				
Investment gains – net (a)	\$ 923	\$ 34,863	\$ —	\$ 37,081
Interest income	3,872	374	5,191	3,597
SunCor joint venture earnings	2,370	2,006	2,342	3,191
Asset sales	142	(1,189)	383	2,462
Miscellaneous	1,377	442	1,571	999
Total other income	\$ 8,684	\$ 36,496	\$ 9,487	\$ 47,330
Other expense:				
Non-operating costs (b)	\$ (3,058)	\$ (3,831)	\$ (6,156)	\$ (6,658)
Asset sales	(249)	1,871	(313)	(268)
Investment losses – net	—	—	(326)	—
Miscellaneous	(539)	(1,411)	(1,437)	(2,390)
Total other expense	\$ (3,846)	\$ (3,371)	\$ (8,232)	\$ (9,316)

(a) The three and six months ended June 30, 2004 include a \$35 million gain (\$21 million after tax) related to the sale of a limited partnership interest in the Phoenix Suns.

(b) As defined by the FERC, includes below-the-line non-operating utility costs (primarily community relations and other costs excluded from utility rate recovery).

15. Guarantees

We have issued parental guarantees and letters of credit and obtained surety bonds on behalf of our unregulated subsidiaries. Our parental guarantees related to Pinnacle West Energy consist of equipment and performance guarantees related to our generation construction program, and long-term service agreement guarantees for new power plants. Our credit support instruments enable APS Energy Services to offer commodity energy and energy-related products. Non-performance or non-payment under the original contract by our unregulated subsidiaries would require us to perform under the guarantee or surety bond. No liability is currently recorded on the Condensed Consolidated Balance Sheets related to Pinnacle West's guarantees on behalf of its subsidiaries. Our guarantees have no recourse or collateral provisions to allow us to recover amounts paid under the guarantee. The amounts and approximate terms of our guarantees and surety bonds for each subsidiary at June 30, 2005 are as follows (dollars in millions):

PINNACLE WEST CAPITAL CORPORATION
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

	Guarantees		Surety Bonds	
	Amount	Term	Amount	Term
	(in years)		(in years)	
Parental:				
Pinnacle West Energy	\$ 17	1	\$ —	—
APS Energy Services	26	1	83	1
Total	<u>\$ 43</u>		<u>\$ 83</u>	

At June 30, 2005, we had entered into approximately \$37 million of letters of credit which support various transmission and construction agreements. These letters of credit expire in 2005 and 2006. We intend to provide from either existing or new facilities for the extension, renewal or substitution of the letters of credit to the extent required. At June 30, 2005, Pinnacle West had approximately \$4 million of letters of credit related to workers' compensation expiring in 2006.

APS has entered into various agreements that require letters of credit for financial assurance purposes. At June 30, 2005, approximately \$200 million of letters of credit were outstanding to support existing pollution control bonds of approximately \$200 million. The letters of credit are available to fund the payment of principal and interest of such debt obligations. In July 2004, \$150 million of these letters of credit were renewed for a three-year term and expire in 2007. The remainder expire in 2005. APS has also entered into approximately \$100 million of letters of credit to support certain equity lessors in the Palo Verde sale leaseback transactions (see Note 9 for further details on the Palo Verde sale leaseback transactions). These letters of credit expire in 2010. Additionally, APS has approximately \$5 million of letters of credit related to counterparty collateral requirements expiring in 2006. APS intends to provide from either existing or new facilities for the extension, renewal or substitution of the letters of credit to the extent required.

We enter into agreements that include indemnification provisions relating to liabilities arising from or related to certain of our agreements. APS has agreed to indemnify the equity participants and other parties in the Palo Verde sale leaseback transactions with respect to certain tax matters. Generally, a maximum obligation is not explicitly stated in the indemnification provisions and therefore, the overall maximum amount of the obligation under such indemnification provisions cannot be reasonably estimated. Based on historical experience and evaluation of the specific indemnities, we do not believe that any material loss related to such indemnification provisions is likely.

See Note 4 for information regarding Pinnacle West's guarantee of \$500 million of Pinnacle West Energy's debt obligations.

16. Earnings Per Share

The following table presents earnings per weighted average common share outstanding for the three and six months ended June 30, 2005 and 2004:

PINNACLE WEST CAPITAL CORPORATION
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

	Three Months Ended June 30,		Six Months Ended June 30,	
	2005	2004	2005	2004
Basic earnings per share:				
Income from continuing operations	\$ 0.89	\$ 0.81	\$ 1.22	\$ 1.15
Loss from discontinued operations	(0.61)	(0.01)	(0.68)	(0.01)
Earnings per share – basic	<u>\$ 0.28</u>	<u>\$ 0.80</u>	<u>\$ 0.54</u>	<u>\$ 1.14</u>
Diluted earnings per share:				
Income from continuing operations	\$ 0.88	\$ 0.81	\$ 1.22	\$ 1.15
Loss from discontinued operations	(0.60)	(0.02)	(0.68)	(0.01)
Earnings per share – diluted	<u>\$ 0.28</u>	<u>\$ 0.79</u>	<u>\$ 0.54</u>	<u>\$ 1.14</u>

Dilutive stock options increased average common shares outstanding by approximately 107,000 shares and 85,000 shares for the three months ended June 30, 2005 and June 30, 2004, respectively, and by approximately 100,000 shares and 87,000 shares for the six months ended June 30, 2005 and June 30, 2004, respectively.

Options to purchase 491,984 shares for the three-month period ended June 30, 2005 and 503,859 shares of common stock for the six month period ended June 30, 2005 were outstanding but were not included in the computation of earnings per share because the options' exercise prices were greater than the average market price of the common shares. Options to purchase shares of common stock that were not included in the computation of diluted earnings per share for that same reason were 2,325,165 shares for the three-month period ended June 30, 2004 and 2,355,287 shares for the six-month period ended June 30, 2004.

17. Discontinued Operations

Silverhawk (marketing and trading segment) – In June 2005, we entered into an agreement to sell our 75% interest in Silverhawk to NPC. Closing of the sale is subject to regulatory approvals, including approval by the Nevada Public Utilities Commission and the FERC, which are expected to occur by this fall. As a result of this pending sale, we recorded an after-tax loss from discontinued operations of approximately \$55 million. The assets held for sale at June 30, 2005 are \$207 million, of which property, plant and equipment accounted for approximately \$200 million. Liabilities held for sale relate to accounts payable in the amount of \$2 million.

SunCor (real estate segment) – In 2005, SunCor sold commercial properties, which are required to be reported as discontinued operations on Pinnacle West's Condensed Consolidated Statements of Income in accordance with SFAS No. 144. The assets held for sale at June 30, 2005 relate to property in the amount of \$35 million. Liabilities held for sale relate to current maturities of long-term debt in the amount of \$29 million.

NAC (other segment) – In 2004, we sold our investment in NAC.

The following table provides revenue and income (loss) before income taxes and after income taxes classified as discontinued operations on Pinnacle West's Condensed Consolidated Statements of Income for the three and six months ended June 30, 2005 and 2004 (dollars in millions):

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	Three Months Ended June 30,		Six Months Ended June 30,	
	2005	2004	2005	2004
Revenue:				
Silverhawk	\$ 15	\$ 5	\$ 43	\$ 5
SunCor – commercial operations	3	2	4	4
NAC	—	11	—	19
Total revenue	<u>\$ 18</u>	<u>\$ 18</u>	<u>\$ 47</u>	<u>\$ 28</u>
Income (loss) before taxes:				
Silverhawk	\$ (97)	\$ (4)	\$ (107)	\$ (4)
SunCor – commercial operations	1	—	2	1
NAC	—	2	—	2
Total loss before taxes	<u>\$ (96)</u>	<u>\$ (2)</u>	<u>\$ (105)</u>	<u>\$ (1)</u>
Income (loss) after taxes:				
Silverhawk	\$ (59)	\$ (2)	\$ (65)	\$ (3)
SunCor – commercial operations	1	—	1	1
NAC	—	1	—	1
Total loss after taxes	<u>\$ (58)</u>	<u>\$ (1)</u>	<u>\$ (64)</u>	<u>\$ (1)</u>

ARIZONA PUBLIC SERVICE COMPANY
CONDENSED STATEMENTS OF INCOME
(unaudited)
(dollars in thousands)

	Three Months Ended June 30,	
	2005	2004
ELECTRIC OPERATING REVENUES		
Regulated electricity	\$ 581,757	\$ 523,973
Marketing and trading	7,000	45,685
Total	<u>588,757</u>	<u>569,658</u>
OPERATING EXPENSES		
Regulated electricity purchased power and fuel	201,871	162,667
Marketing and trading purchased power and fuel	3,349	45,886
Operations and maintenance	138,314	126,871
Depreciation and amortization	76,808	88,385
Income taxes	41,772	32,371
Other taxes	31,322	29,874
Total	<u>493,436</u>	<u>486,054</u>
OPERATING INCOME	<u>95,321</u>	<u>83,604</u>
OTHER INCOME (DEDUCTIONS)		
Income taxes	(1,549)	(1,301)
Allowance for equity funds used during construction	2,952	2,184
Other income (Note S-4)	7,005	4,668
Other expense (Note S-4)	(2,876)	(1,220)
Total	<u>5,532</u>	<u>4,331</u>
INTEREST DEDUCTIONS		
Interest on long-term debt	35,612	31,997
Interest on short-term borrowings	2,055	1,215
Debt discount, premium and expense	1,188	1,188
Capitalized interest	(2,000)	(1,399)
Total	<u>36,855</u>	<u>33,001</u>
NET INCOME	<u>\$ 63,998</u>	<u>\$ 54,934</u>
See Notes to Pinnacle West's Condensed Consolidated Financial Statements and Supplemental Notes to Arizona Public Service Company's Condensed Financial Statements.		

ARIZONA PUBLIC SERVICE COMPANY
CONDENSED STATEMENTS OF INCOME
(unaudited)
(dollars in thousands)

	Six Months Ended June 30,	
	2005	2004
ELECTRIC OPERATING REVENUES		
Regulated electricity	\$ 1,000,191	\$ 944,272
Marketing and trading	29,858	66,488
Total	<u>1,030,049</u>	<u>1,010,760</u>
OPERATING EXPENSES		
Regulated electricity purchased power and fuel	283,785	251,259
Marketing and trading purchased power and fuel	31,651	71,644
Operations and maintenance	280,608	252,783
Depreciation and amortization	159,022	177,233
Income taxes	58,152	49,733
Other taxes	62,767	57,454
Total	<u>875,985</u>	<u>860,106</u>
OPERATING INCOME	<u>154,064</u>	<u>150,654</u>
OTHER INCOME (DEDUCTIONS)		
Income taxes	(2,386)	(3,770)
Allowance for equity funds used during construction	5,555	4,186
Other income (Note S-4)	12,664	15,903
Other expense (Note S-4)	(6,234)	(6,124)
Total	<u>9,599</u>	<u>10,195</u>
INTEREST DEDUCTIONS		
Interest on long-term debt	71,129	67,643
Interest on short-term borrowings	3,246	3,716
Debt discount, premium and expense	2,192	2,383
Capitalized interest	(3,947)	(2,256)
Total	<u>72,620</u>	<u>71,486</u>
NET INCOME	<u>\$ 91,043</u>	<u>\$ 89,363</u>

See Notes to Pinnacle West's Condensed Consolidated Financial Statements and Supplemental Notes to Arizona Public Service Company's Condensed Financial Statements.

ARIZONA PUBLIC SERVICE COMPANY
CONDENSED BALANCE SHEETS
(unaudited)
(dollars in thousands)

	June 30, 2005	December 31, 2004
ASSETS		
UTILITY PLANT		
Electric plant in service and held for future use	\$ 9,617,099	\$ 9,120,407
Less accumulated depreciation and amortization	3,475,696	3,266,181
Total	6,141,403	5,854,226
Construction work in progress	293,610	249,243
Intangible assets, net of accumulated amortization	96,800	103,701
Nuclear fuel, net of accumulated amortization	53,459	51,188
Utility plant – net	6,585,272	6,258,358
INVESTMENTS AND OTHER ASSETS		
Note receivable from Pinnacle West Energy (Notes 5 and S-5)	—	498,489
Decommissioning trust accounts	276,746	267,700
Assets from long-term risk management and trading activities (Note S-2)	75,236	20,123
Other assets	61,086	61,364
Total investments and other assets	413,068	847,676
CURRENT ASSETS		
Cash and cash equivalents	204,597	49,575
Investment in debt securities	272,783	181,175
Accounts receivable:		
Service customers	178,304	214,487
Other	73,093	63,131
Allowance for doubtful accounts	(3,228)	(3,444)
Accrued utility revenues	120,678	76,154
Materials and supplies (at average cost)	88,663	83,893
Fossil fuel (at average cost)	26,590	20,506
Assets from risk management and trading activities (Note S-2)	133,685	70,430
Other current assets	9,634	10,187
Total current assets	1,104,799	766,094
DEFERRED DEBITS		
Deferred purchased power and fuel regulatory asset	33,785	—
Other regulatory assets	139,690	135,051
Unamortized debt issue costs	22,951	21,832
Other deferred debits	72,566	69,541
Total deferred debits	268,992	226,424
TOTAL ASSETS	\$ 8,372,131	\$ 8,098,552

See Notes to Pinnacle West's Condensed Consolidated Financial Statements and Supplemental Notes to Arizona Public Service Company's Condensed Financial Statements.

ARIZONA PUBLIC SERVICE COMPANY
CONDENSED BALANCE SHEETS
(unaudited)
(dollars in thousands)

	June 30, 2005	December 31, 2004
CAPITALIZATION AND LIABILITIES		
CAPITALIZATION		
Common stock	\$ 178,162	\$ 178,162
Additional paid-in capital	1,346,804	1,246,804
Retained earnings	908,739	860,196
Accumulated other comprehensive income (loss):		
Minimum pension liability adjustment	(71,087)	(71,087)
Derivative instruments	65,771	18,327
Common stock equity	2,428,389	2,232,402
Long-term debt less current maturities	2,266,465	2,267,094
Total capitalization	<u>4,694,854</u>	<u>4,499,496</u>
CURRENT LIABILITIES		
Current maturities of long-term debt	351,395	451,247
Accounts payable	153,340	215,076
Accrued taxes	373,337	292,521
Accrued interest	30,105	33,332
Customer deposits	53,500	51,804
Deferred income taxes	9,057	9,057
Liabilities from risk management and trading activities (Note S-2)	74,250	34,292
Other current liabilities	156,451	91,441
Total current liabilities	<u>1,201,435</u>	<u>1,178,770</u>
DEFERRED CREDITS AND OTHER		
Deferred income taxes	1,137,253	1,108,571
Regulatory liabilities	524,107	506,646
Liability for asset retirements	259,524	251,612
Pension liability	219,812	203,668
Customer advances for construction	60,851	59,185
Unamortized gain — sale of utility plant	48,045	50,333
Liabilities from long term risk management and trading activities (Note S-2)	19,722	13,124
Other	206,528	227,147
Total deferred credits and other	<u>2,475,842</u>	<u>2,420,286</u>
COMMITMENTS AND CONTINGENCIES (Notes 5, 12, 13 and S-5)		
TOTAL LIABILITIES AND EQUITY	<u><u>\$ 8,372,131</u></u>	<u><u>\$ 8,098,552</u></u>

See Notes to Pinnacle West's Condensed Consolidated Financial Statements and Supplemental Notes to Arizona Public Service Company's Condensed Financial Statements.

ARIZONA PUBLIC SERVICE COMPANY
CONDENSED STATEMENTS OF CASH FLOWS
(unaudited)
(dollars in thousands)

	Six Months Ended June 30,	
	2005	2004
CASH FLOWS FROM OPERATING ACTIVITIES		
Net income	\$ 91,043	\$ 89,363
Items not requiring cash:		
Depreciation and amortization	159,022	177,233
Deferred purchased power and fuel	(33,785)	—
Nuclear fuel amortization	3,619	14,501
Allowance for equity funds used during construction	(5,555)	(4,186)
Deferred income taxes	(1,926)	8,770
Change in mark-to-market valuations	(12,191)	4,423
Changes in current assets and liabilities:		
Accounts receivable	32,301	(4,630)
Accrued utility revenues	(44,524)	(38,126)
Materials, supplies and fossil fuel	(10,854)	3,416
Other current assets	2,566	(2,836)
Accounts payable	(61,798)	28,686
Accrued taxes	80,816	54,242
Accrued interest	(3,227)	(9,500)
Other current liabilities	68,372	5,519
Increase in regulatory assets	(4,699)	(5,205)
Change in risk management and trading activities – assets	16,387	7,203
Change in risk management and trading activities – liabilities	2,244	—
Change in pension liability	6,458	26,141
Change in other long-term assets	12,038	7,007
Change in other long-term liabilities	(4,923)	3,934
Net cash flow provided by operating activities	<u>291,384</u>	<u>365,955</u>
CASH FLOWS FROM INVESTING ACTIVITIES		
Capital expenditures	(301,098)	(224,259)
Purchase of Sundance Plant	(185,046)	—
Capitalized interest	(3,947)	(2,256)
Repayment of loan by Pinnacle West Energy	500,000	—
Purchases of investment securities	(769,166)	(124,000)
Proceeds from sale of investment securities	677,558	94,050
Other	(11,163)	(13,657)
Net cash flow used for investing activities	<u>(92,862)</u>	<u>(270,122)</u>
CASH FLOWS FROM FINANCING ACTIVITIES		
Issuance of long-term debt	163,975	476,240
Equity infusion	100,000	—
Dividends paid on common stock	(42,500)	(85,000)
Repayment and reacquisition of long-term debt	(264,975)	(385,133)
Net cash flow provided by (used for) financing activities	<u>(43,500)</u>	<u>6,107</u>
NET INCREASE IN CASH AND CASH EQUIVALENTS	<u>155,022</u>	<u>101,940</u>
CASH AND CASH EQUIVALENTS AT BEGINNING OF PERIOD	<u>49,575</u>	<u>141,952</u>
CASH AND CASH EQUIVALENTS AT END OF PERIOD	<u><u>\$ 204,597</u></u>	<u><u>\$ 243,892</u></u>
Supplemental disclosure of cash flow information:		
Cash paid (received) during the year for:		
Income taxes refunded	\$ (8,829)	\$ (1,726)
Interest, net of amounts capitalized	\$ 73,656	\$ 78,604

See Notes to Pinnacle West's Condensed Consolidated Financial Statements and Supplemental Notes to Arizona Public Service Company's Condensed Financial Statements.

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Certain notes to APS' Condensed Financial Statements are combined with the Notes to Pinnacle West's Condensed Consolidated Financial Statements. Listed below are the Condensed Consolidated Notes to Pinnacle West's Condensed Consolidated Financial Statements, the majority of which also relate to APS' Condensed Financial Statements. In addition, listed below are the Supplemental Notes which are required disclosures for APS and should be read in conjunction with Pinnacle West's Condensed Consolidated Notes.

	Condensed Consolidated Footnote Reference	APS' Supplemental Footnote Reference
Consolidation and Nature of Operations	Note 1	—
Condensed Consolidated Financial Statements	Note 2	—
Quarterly Fluctuations	Note 3	—
Changes in Liquidity	Note 4	Note S-1
Regulatory Matters	Note 5	—
Retirement Plans and Other Benefits	Note 6	—
Business Segments	Note 7	—
New Accounting Standards	Note 8	—
Variable Interest Entities	Note 9	—
Derivative and Energy Trading Accounting	Note 10	Note S-2
Comprehensive Income	Note 11	Note S-3
Commitments and Contingencies	Note 12	—
Nuclear Insurance	Note 13	—
Other Income and Other Expense	Note 14	Note S-4
Guarantees	Note 15	—
Earnings Per Share	Note 16	—
Discontinued Operations	Note 17	—
Related Party Transactions	—	Note S-5

S-1. Changes in Liquidity

The following is a list of principal payments due on APS' total long-term debt and capitalized lease requirements:

- \$351 million in 2005;
- \$86 million in 2006;
- \$174 million in 2007;
- \$1 million in 2008;
- \$1 million in 2009; and
- \$2.012 billion, thereafter.

S-2. Derivative and Energy Trading Accounting

APS is exposed to the impact of market fluctuations in the commodity price of electricity, natural gas and coal. As part of its overall risk management program, APS uses various commodity

ARIZONA PUBLIC SERVICE COMPANY
SUPPLEMENTAL NOTES TO THE CONDENSED FINANCIAL STATEMENTS

instruments that qualify as derivatives to hedge purchases and sales of electricity and fuels. As of June 30, 2005, APS hedged exposures to these risks for a maximum of three years.

Cash Flow Hedges

The changes in the fair value of APS' hedged positions included in the APS Condensed Statements of Income for the three and six months ended June 30, 2005 and 2004 were comprised of the following (dollars in thousands):

	Three Months Ended June 30,		Six Months Ended June 30,	
	2005	2004	2005	2004
Gains on the ineffective portion of derivatives qualifying for hedge accounting	\$ 4,512	\$ 124	\$ 11,930	\$ 1,535
Gains (losses) from the change in options' time value excluded from measurement of effectiveness	(1,189)	(17)	(331)	63
Gains from the discontinuance of cash flow hedges	—	—	302	575

During the twelve months ending June 30, 2006, we estimate that a net gain of \$54 million before income taxes will be reclassified from accumulated other comprehensive income as an offset to the effect of market price changes for the related hedged transactions.

APS' assets and liabilities from risk management and trading activities are presented in two categories, consistent with Pinnacle West's business segments:

- Regulated Electricity – non-trading derivative instruments that hedge APS' purchases and sales of electricity and fuel for its Native Load requirements; and
- Marketing and Trading – both non-trading and trading derivative instruments.

The following table summarizes APS' assets and liabilities from risk management and trading activities at June 30, 2005 and December 31, 2004 (dollars in thousands):

June 30, 2005

	Current Assets	Investments	Current Liabilities	Other Liabilities	Net Asset (Liability)
Regulated Electricity:					
Mark-to-market	\$ 121,482	\$ 68,458	\$ (55,495)	\$ (8,346)	\$ 126,099
Options and futures — at cost	2,555	4	(11,123)	—	(8,564)
Marketing and Trading:					
Mark-to-market	9,648	6,774	(7,632)	(11,376)	(2,586)
Total	<u>\$ 133,685</u>	<u>\$ 75,236</u>	<u>\$ (74,250)</u>	<u>\$ (19,722)</u>	<u>\$ 114,949</u>

ARIZONA PUBLIC SERVICE COMPANY
SUPPLEMENTAL NOTES TO THE CONDENSED FINANCIAL STATEMENTS

December 31, 2004

	Current Assets	Investments	Current Liabilities	Other Liabilities	Net Asset (Liability)
Regulated Electricity:					
Mark-to-market	\$ 45,220	\$ 19,417	\$ (19,191)	\$ (12,000)	\$ 33,446
Options and futures — at cost	18,821	118	(8,879)	—	10,060
Marketing and Trading:					
Mark-to-market	6,389	581	(6,222)	(1,124)	(376)
Other — at cost	—	7	—	—	7
Total	<u>\$ 70,430</u>	<u>\$ 20,123</u>	<u>\$ (34,292)</u>	<u>\$ (13,124)</u>	<u>\$ 43,137</u>

Cash or other assets may be required to serve as collateral against APS' open positions on certain energy-related contracts. No collateral was provided to counterparties at June 30, 2005 or December 31, 2004. Collateral provided to us by counterparties was \$90 million at June 30, 2005 and \$6 million at December 31, 2004, and is included in other current liabilities on the Condensed Balance Sheets.

S-3. Comprehensive Income

Components of APS' comprehensive income for the three and six months ended June 30, 2005 and 2004, are as follows (dollars in thousands):

	Three Months Ended June 30,		Six Months Ended June 30,	
	2005	2004	2005	2004
Net income	<u>\$ 63,998</u>	<u>\$ 54,934</u>	<u>\$ 91,043</u>	<u>\$ 89,363</u>
Other comprehensive income (loss):				
Unrealized gains (losses) on derivative instruments (a)	(24,147)	17,836	84,070	48,078
Reclassification of realized gain to income (b)	(4,437)	(4,963)	(5,819)	(6,829)
Income tax (expense) benefit related to items of other comprehensive income	<u>11,253</u>	<u>(5,076)</u>	<u>(30,807)</u>	<u>(16,267)</u>
Total other comprehensive income (loss)	<u>(17,331)</u>	<u>7,797</u>	<u>47,444</u>	<u>24,982</u>
Comprehensive income	<u>\$ 46,667</u>	<u>\$ 62,731</u>	<u>\$ 138,487</u>	<u>\$ 114,345</u>

(a) These amounts primarily include unrealized gains and losses on contracts used to hedge our forecasted electricity and gas requirements to serve Native Load.

(b) These amounts primarily include the reclassification of unrealized gains and losses to realized for contracted commodities delivered during the period.

ARIZONA PUBLIC SERVICE COMPANY
SUPPLEMENTAL NOTES TO THE CONDENSED FINANCIAL STATEMENTS

S-4. Other Income and Other Expense

The following table provides detail of APS' other income and other expense for the three and six months ended June 30, 2005 and 2004 (dollars in thousands):

	Three Months Ended June 30,		Six Months Ended June 30,	
	2005	2004	2005	2004
Other income:				
Interest income	\$ 4,177	\$ 5,015	\$ 9,600	\$ 10,053
Asset sales	142	(1,189)	383	2,462
Investment gains – net	981	350	479	2,397
Miscellaneous	1,705	492	2,202	991
Total other income	<u>\$ 7,005</u>	<u>\$ 4,668</u>	<u>\$ 12,664</u>	<u>\$ 15,903</u>
Other expense:				
Non-operating costs(a)	\$ (2,708)	\$ (2,310)	\$ (5,335)	\$ (4,542)
Asset sales	(249)	1,871	(313)	(268)
Miscellaneous	81	(781)	(586)	(1,314)
Total other expense	<u>\$ (2,876)</u>	<u>\$ (1,220)</u>	<u>\$ (6,234)</u>	<u>\$ (6,124)</u>

(a) As defined by the FERC, includes below-the-line non-operating utility costs (primarily community relations and other costs excluded from utility rate recovery).

S-5. Related Party Transactions

From time to time, APS enters into transactions with Pinnacle West or Pinnacle West's subsidiaries. The following table summarizes the amounts included in the APS Condensed Statements of Income and Condensed Balance Sheets related to transactions with affiliated companies (dollars in millions):

ARIZONA PUBLIC SERVICE COMPANY
SUPPLEMENTAL NOTES TO THE CONDENSED FINANCIAL STATEMENTS

	Three Months Ended June 30,		Six Months Ended June 30,	
	2005	2004	2005	2004
Electric operating revenues:				
Pinnacle West – marketing and trading	\$ 2	\$ 4	\$ 3	\$ 8
Pinnacle West Energy	1	—	2	1
Total	<u>\$ 3</u>	<u>\$ 4</u>	<u>\$ 5</u>	<u>\$ 9</u>
Purchased power and fuel costs:				
Pinnacle West Energy	\$ 39	\$ 19	\$ 47	\$ 29
Total	<u>\$ 39</u>	<u>\$ 19</u>	<u>\$ 47</u>	<u>\$ 29</u>
Other:				
Pinnacle West Energy interest income	\$ —	\$ 4	\$ 5	\$ 9
Total	<u>\$ —</u>	<u>\$ 4</u>	<u>\$ 5</u>	<u>\$ 9</u>
			As of June 30, 2005	As of December 31, 2004
Net intercompany receivables (payables):				
Pinnacle West Energy			\$ (13)	\$ 467
Pinnacle West – marketing and trading			9	19
APS Energy Services			7	9
Pinnacle West			(8)	(5)
Total			<u>\$ (5)</u>	<u>\$ 490</u>

Electric revenues include sales of electricity to affiliated companies at contract prices. Purchased power includes purchases of electricity from affiliated companies at contract prices. The Company purchases electricity from and sells electricity to APS Energy Services; however, these transactions are settled net and reported net in accordance with 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 EITF Issue No. 2-3.”

Intercompany receivables primarily include amounts related to the \$500 million loan APS made to Pinnacle West Energy and intercompany sales of electricity. This loan was settled in May 2005. Intercompany payables primarily include amounts related to the intercompany purchases of electricity. Intercompany receivables and payables are generally settled on a current basis in cash.

ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

INTRODUCTION

The following discussion should be read in conjunction with Pinnacle West's Condensed Consolidated Financial Statements and Arizona Public Service Company's Condensed Financial Statements and the related Notes that appear in Item 1 of this report.

OVERVIEW

Pinnacle West owns all of the outstanding common stock of APS. APS is a vertically-integrated electric utility that provides retail and wholesale electric service to most of the state of Arizona, with the major exceptions of about one-half of the Phoenix metropolitan area, the Tucson metropolitan area and Mohave County in northwestern Arizona. Through its marketing and trading division, APS also generates, sells and delivers electricity to wholesale customers in the western United States. APS has historically accounted for a substantial part of our revenues and earnings. Customer growth in APS' service territory is about three times the national average and remains a fundamental driver of our revenues and earnings.

Pinnacle West Energy is our unregulated generation subsidiary. Pursuant to the ACC's April 7, 2005 order in APS' general rate case, on July 29, 2005, Pinnacle West Energy transferred the PWEC Dedicated Assets to APS. See "APS General Rate Case" in Note 5. As a result, Pinnacle West Energy's remaining generating plant is Silverhawk, a 570 MW combined cycle plant located north of Las Vegas, Nevada. See Note 17 of Notes to Condensed Consolidated Financial Statements for a discussion of the pending sale of our 75% ownership interest in this plant.

As part of the ACC order in APS' general rate case, the ACC approved the PSA, which permits APS to defer for recovery or refund fuel and purchased power costs, subject to specified parameters and procedures. On July 22, 2005, APS filed an Application for Surcharge with the ACC requesting the recovery of \$100 million in deferred fuel and purchased power costs over a 24-month period beginning with billing cycle one of November, 2005. See "APS General Rate Case" in Note 5. APS expects to file another general rate case in late 2005.

SunCor, our real estate development subsidiary, has been and is expected to be an important source of earnings and cash flow, particularly during the years 2003 through 2005 due to accelerated asset sales activity.

Our subsidiary, APS Energy Services, provides competitive commodity-related energy services and energy-related products and services to commercial and industrial retail customers in the western United States.

El Dorado, our investment subsidiary, owns minority interests in several energy-related investments and Arizona community-based ventures.

We continue to focus on solid operational performance in our electricity generation and delivery activities. In the generation area, 2004 represented the thirteenth consecutive year Palo Verde was the largest power producer in the United States. In the delivery area, we focus on superior reliability and customer satisfaction while expanding our transmission and distribution system to

meet growth and sustain reliability. We plan to expand long-term resources to meet our retail customers' growing electricity needs.

See "Pinnacle West Consolidated – Factors Affecting Our Financial Outlook" below for a discussion of several factors that could affect our future financial results.

EARNINGS CONTRIBUTION BY BUSINESS SEGMENT

We have three principal business segments (determined by products, services and the regulatory environment):

- our regulated electricity segment, which consists of traditional regulated retail and wholesale electricity businesses (primarily electric service to Native Load customers) and related activities and includes electricity generation, transmission and distribution.
- our marketing and trading segment, which consists of our competitive energy business activities, including wholesale marketing and trading and APS Energy Services' commodity-related energy services; and
- our real estate segment, which consists of SunCor's real estate development and investment activities.

The following table summarizes net income for the three months and six months ended June 30, 2005 and 2004 (dollars in millions):

	Three Months Ended June 30,		Six Months Ended June 30,	
	2005	2004	2005	2004
Regulated electricity	\$ 69	\$ 40	\$ 83	\$ 55
Marketing and trading	4	8	11	22
Real estate	11	4	19	5
Other (a)	1	22	2	23
Income from continuing operations	85	74	115	105
Silverhawk discontinued operations – net of income taxes (see "Pending Sale of Silverhawk" below)	(59)	(2)	(65)	(3)
Real estate discontinued operations – net of income taxes	1	—	1	1
Other segment discontinued operations- net of income taxes	—	1	—	1
Net income	<u>\$ 27</u>	<u>\$ 73</u>	<u>\$ 51</u>	<u>\$ 104</u>

(a) The 2004 periods include \$21 million (after-tax) gain related to the sale of a limited partnership interest in the Phoenix Suns.

General

Throughout the following explanations of our results of operations, we refer to “gross margin.” With respect to our regulated electricity segment and our marketing and trading segment, gross margin refers to electric operating revenues less purchased power and fuel costs. “Gross margin” is a “non-GAAP financial measure,” as defined in accordance with SEC rules. Exhibit 99.3 reconciles this non-GAAP financial measure to operating income, which is the most directly comparable financial measure calculated and presented in accordance with GAAP. We view gross margin as an important performance measure of the core profitability of our operations. This measure is a key component of our internal financial reporting and is used by our management in analyzing our business segments. We believe that investors benefit from having access to the same financial measures that our management uses. In addition, we have reclassified certain prior-period amounts to conform to our current-period presentation.

Pending Sale of Silverhawk

In June 2005, we entered into an agreement to sell our 75% interest in Silverhawk to NPC. Closing of the sale is subject to regulatory approvals, including approval by the Nevada Public Utilities Commission and the FERC, which are expected to occur by this fall. As a result of this pending sale, we recorded an after-tax loss from discontinued operations of approximately \$55 million. We have also reclassified Silverhawk operations in the current and prior periods to discontinued operations.

Deferred Purchased Power and Fuel Costs

APS’ retail rate case settlement became effective April 1, 2005. As part of the settlement, the ACC approved a 4.2% annual retail rate increase and a PSA that provides mechanisms for adjusting rates to reflect variations in fuel and purchased power costs. In accordance with the PSA, APS defers for future rate recovery 90% of the difference between actual purchased power and fuel costs and the amount for such costs currently included in base rates. As of June 30, 2005, APS had deferred \$34 million of pretax purchased power and fuel costs.

Operating Results – Three-month period ended June 30, 2005 compared with three-month period ended June 30, 2004

Our consolidated net income for the three months ended June 30, 2005 was \$27 million compared with \$73 million for the prior-year period. The current-quarter net income included a loss from discontinued operations of \$58 million which is primarily related to the pending sale and operations of Silverhawk (see discussion above). Income from continuing operations increased \$11 million in the period-to-period comparison reflecting the following changes in earnings by segment:

- Regulated Electricity Segment – Income from continuing operations increased approximately \$29 million primarily due to a retail price increase effective April 1, 2005, higher retail sales volumes due to customer growth, the absence of regulatory asset amortization, deferred purchased power and fuel costs, net of higher costs, in accordance with the retail rate settlement, and lower depreciation due to lower depreciation rates. These positive factors were partially offset by higher operations and maintenance costs primarily related to generation, customer service, and benefit costs.

- Marketing and Trading Segment – Income from continuing operations decreased approximately \$4 million primarily due to lower realized margins on wholesale sales.
- Real Estate Segment – Income from continuing operations increased approximately \$7 million primarily due to increased parcel sales.
- Other Segment – Income from continuing operations decreased approximately \$21 million primarily due to an after-tax gain related to the sale of El Dorado’s limited partnership interest in the Phoenix Suns recorded in the prior-year period.

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Additional details on the major factors that increased (decreased) net income are contained in the following table (dollars in millions).

	Increase (Decrease)	
	Pretax	After Tax
Regulated electricity segment gross margin:		
Retail price increase effective April 1, 2005	\$ 28	\$ 17
Higher retail sales volumes due to customer growth, excluding weather effects	13	8
Deferred purchased power and fuel costs, net of higher costs, in accordance with the retail rate settlement	8	5
Miscellaneous items, net	2	1
Net increase in regulated electricity segment gross margin	51	31
Marketing and trading segment gross margin:		
Lower realized margins on wholesale sales primarily due to lower unit margins and lower sales volumes	(6)	(4)
Miscellaneous items, net	(3)	(1)
Net decrease in marketing and trading segment gross margin	(9)	(5)
Net increase in gross margin for regulated electricity and marketing and trading segments	42	26
Higher real estate segment contribution primarily related to increased parcel sales	12	7
Lower other income due to sale of limited partnership interest in Phoenix Suns recorded in prior-year period	(35)	(21)
Higher operation and maintenance expense due to generation, customer service and benefit costs	(15)	(9)
Depreciation and amortization decreases primarily due to:		
Absence of regulatory asset amortization	10	6
Lower depreciation rates (see Note 5) partially offset by higher depreciable assets	7	4
Higher interest expense, net of capitalized financing costs, primarily due to higher debt balances and interest rates	(6)	(4)
Miscellaneous items, net	6	2
Net increase in income from continuing operations	\$ 21	11
Discontinued operations primarily related to the pending sale of Silverhawk (see discussion above)		(57)
Net decrease in net income		\$ (46)

Regulated Electricity Segment Revenues

Regulated electricity segment revenues were \$60 million higher for the three months ended June 30, 2005 compared with the prior-year period primarily as a result of:

- a \$28 million increase in retail revenues due to a price increase effective April 1, 2005;
- an \$18 million increase in retail revenues related to customer growth, excluding weather effects;
- a \$12 million increase in Off-System Sales primarily due to sales previously reported in the marketing and trading segment now classified as sales in the regulated electricity segment in accordance with the retail rate settlement; and
- a \$2 million increase due to miscellaneous factors.

Marketing and Trading Segment Revenues

Marketing and trading segment revenues were \$39 million lower for the three months ended June 30, 2005 compared with the prior-year period primarily as a result of:

- a \$25 million decrease in revenues from Off-System Sales primarily due to lower sales volumes and sales previously reported in the marketing and trading segment now classified as sales in the regulated electricity segment in accordance with the retail rate settlement;
- a \$7 million decrease in energy trading revenues on realized sales of electricity primarily due to lower delivered electricity prices and lower sales volumes;
- a \$5 million decrease from lower volumes and prices for competitive retail sales in California; and
- a \$2 million decrease on future mark-to-market gains due to higher price volatility.

Real Estate Revenues

Real estate revenues were \$19 million higher for the three months ended June 30, 2005 compared with the prior-year period primarily due to increased parcel sales.

Operating Results – Six-month period ended June 30, 2005 compared with six-month period ended June 30, 2004

Our consolidated net income for the six months ended June 30, 2005 was \$51 million compared with \$104 million for the prior-year period. The current year period net income included a loss from discontinued operations of \$64 million which is primarily related to the pending sale and operations of Silverhawk (see discussion above). Income from continuing operations increased \$10 million in the period-to-period comparison reflecting the following changes in earnings by segment:

- Regulated Electricity Segment – Income from continuing operations increased approximately \$28 million primarily due to a retail price increase effective April 1, 2005, higher retail sales volumes due to customer growth, the absence of regulatory asset amortization, deferred purchased power and fuel costs, net of higher costs, in

accordance with the retail rate settlement, and lower depreciation due to lower depreciation rates. These positive factors were partially offset by higher operations and maintenance costs primarily related to generation, customer service, and benefit costs, and higher property taxes due to increased plant in service.

- Marketing and Trading Segment – Income from continuing operations decreased approximately \$11 million primarily due to lower realized margins on wholesale sales and competitive retail sales in California.
- Real Estate Segment – Income from continuing operations increased approximately \$14 million primarily due to increased parcel sales.
- Other Segment – Income from continuing operations decreased approximately \$21 million primarily due to an after-tax gain related to the sale of El Dorado’s limited partnership interest in the Phoenix Suns recorded in the prior-year period.

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Additional details on the major factors that increased (decreased) net income are contained in the following table (dollars in millions).

	Increase (Decrease)	
	Pretax	After Tax
Regulated electricity segment gross margin:		
Retail price increase effective April 1, 2005	\$ 28	\$ 17
Higher retail sales volumes due to customer growth, excluding weather effects	20	12
Deferred purchased power and fuel costs, net of higher costs, in accordance with the retail rate settlement	15	9
Miscellaneous items, net	(1)	(1)
Net increase in regulated electricity segment gross margin	62	37
Marketing and trading segment gross margin:		
Lower unit margins on competitive retail sales in California	(7)	(4)
Lower realized margins on wholesale sales primarily due to lower unit margins and lower sales volumes	(5)	(3)
Miscellaneous items, net	1	—
Net decrease in marketing and trading segment gross margin	(11)	(7)
Net increase in gross margin for regulated electricity and marketing and trading segments	51	30
Higher real estate segment contribution primarily related to increased parcel sales	24	14
Lower other income due to sale of limited partnership interest in Phoenix Suns recorded in the prior-year period	(35)	(21)
Operations and maintenance increases primarily due to:		
Generation costs, including planned maintenance	(11)	(7)
Customer service costs, including planned maintenance	(10)	(6)
Benefit costs	(8)	(5)
Miscellaneous items, net	(3)	(2)
Depreciation and amortization decreases primarily due to:		
Absence of regulatory asset amortization	19	11
Lower depreciation rates (see Note 5) partially offset by higher depreciable assets	8	5
Higher property taxes due to increased plant in service	(7)	(4)
Miscellaneous items, net	(5)	(5)
Net increase in income from continuing operations	\$ 23	10
Discontinued operations primarily related to the pending sale of Silverhawk (see discussion above)		(63)
Net decrease in net income		\$ (53)

Regulated Electricity Segment Revenues

Regulated electricity segment revenues were \$60 million higher for the six months ended June 30, 2005 compared with the prior-year period primarily as a result of:

- a \$28 million increase in retail revenues related to customer growth, excluding weather effects;
- a \$28 million increase in retail revenues due to a price increase effective April 1, 2005;
- a \$12 million increase in Off-System Sales primarily due to sales previously reported in the marketing and trading segment now classified as sales in the regulated electricity segment in accordance with the retail rate settlement;
- a \$9 million decrease in retail revenues related to milder weather; and
- a \$1 million increase due to miscellaneous factors.

Marketing and Trading Segment Revenues

Marketing and trading segment revenues were \$38 million lower for the six months ended June 30, 2005 compared with the prior-year period primarily as a result of:

- a \$19 million decrease in revenues from Off-System Sales primarily due to lower sales volumes, prices and sales previously reported in the marketing and trading segment now classified as sales in the regulated electricity segment in accordance with the retail rate settlement;
- a \$14 million decrease from lower volumes and prices on competitive retail sales in California; and
- a \$5 million decrease in energy trading revenues on realized sales of electricity primarily due to lower delivered electricity prices and lower volumes.

Real Estate Revenues

Real estate revenues were \$40 million higher for the six months ended June 30, 2005 compared with the prior-year period primarily due to increased parcel sales.

LIQUIDITY AND CAPITAL RESOURCES

Capital Needs and Resources – Pinnacle West Consolidated

Capital Expenditure Requirements

The following table summarizes the actual capital expenditures for the six months ended June 30, 2005 and estimated capital expenditures for the next three years.

CAPITAL EXPENDITURES
(dollars in millions)

	Six Months Ended June 30,	Estimated for the Year Ended December 31,		
	2005	2005	2006	2007
APS Delivery	\$ 203	\$ 390	\$ 395	\$ 440
Generation (a) (b)	259	352	158	195
Other (c)	16	30	7	6
Subtotal	478	772	560	641
Pinnacle West Energy (a)	1	7	—	—
SunCor (d)	45	114	61	63
Other	1	8	7	4
Total	\$ 525	\$ 901	\$ 628	\$ 708

- (a) As discussed in Note 5 under “APS General Rate Case,” as part of the ACC’s order in APS’ general rate case, APS received rate base treatment of the PWEC Dedicated Assets. The estimated capital expenditures related to the PWEC Dedicated Assets are reflected in APS generation for the years 2005, 2006 and 2007.
- (b) The six months ended June 30, 2005 includes \$190 million for the acquisition of the Sundance Plant. See Note 4 for a discussion of APS’ acquisition of the Sundance Plant.
- (c) Primarily information systems and facilities projects.
- (d) Consists primarily of capital expenditures for land development and retail and office building construction reflected in “Real estate investments” on the Condensed Consolidated Statements of Cash Flows.

Delivery capital expenditures are comprised of T&D infrastructure additions and upgrades, capital replacements, new customer construction and related information systems and facility costs. Examples of the types of projects included in the forecast include T&D lines and substations, line extensions to new residential and commercial developments and upgrades to customer information systems. Major transmission projects are driven by strong regional customer growth. APS will begin major projects each year for the next several years, and expects to spend about \$200 million on major transmission projects during the 2005 to 2007 time frame. These amounts are included in “APS-Delivery” in the table above. Completion of these projects is expected by at least 2008.

Generation capital expenditures are comprised of various improvements to APS’ existing fossil and nuclear plants, the acquisition of the Sundance Plant and the replacement of Palo Verde steam generators (see below). Examples of the types of projects included in this category are additions, upgrades and capital replacements of various power plant equipment such as turbines, boilers and environmental equipment. Generation also includes nuclear fuel expenditures of approximately \$30 million annually for 2005 through 2007.

Replacement of the steam generators in Palo Verde Unit 2 was completed during the fall outage of 2003 at a cost to APS of approximately \$70 million. The Palo Verde owners have approved the manufacture of two additional sets of steam generators. These generators will be installed in Unit 1 (scheduled completion in the fall of 2005) and Unit 3 (scheduled completion in the fall of 2007). Our portion of steam generator expenditures for Units 1 and 3 is approximately \$140 million, which will be spent through 2008. In 2005 through 2007, approximately \$95 million of the costs for steam generator replacements at Units 1 and 3 are included in the generation capital expenditures table above and will be funded with internally-generated cash or external financings.

Contractual Obligations

Our future contractual obligations have not changed materially from the amounts disclosed in Part II, Item 7 of the 2004 Form 10-K with the exception of our aggregate:

- purchased power and fuel commitments, which increased from approximately \$855 million at December 31, 2004 to \$1.0 billion at June 30, 2005 primarily due to increased commitment for the years 2005 through 2007; and
- nuclear decommissioning funding requirements, which increased from approximately \$201 million at December 31, 2004 to \$386 million at June 30, 2005 for the years 2005 and thereafter.

See Note 4 for a list of payments due on total long-term debt and capitalized lease requirements.

Off-Balance Sheet Arrangements

In 1986, APS entered into agreements with three separate VIE lessors in order to sell and lease back interests in Palo Verde Unit 2. The leases are accounted for as operating leases in accordance with GAAP. We are not the primary beneficiary of the Palo Verde VIEs and, accordingly, do not consolidate them.

APS is exposed to losses under the Palo Verde sale leaseback agreements upon the occurrence of certain events that APS does not consider to be reasonably likely to occur. Under certain circumstances (for example, the NRC issuing specified violation orders with respect to Palo Verde or the occurrence of specified nuclear events), APS would be required to assume the debt associated with the transactions, make specified payments to the equity participants, and take title to the leased Unit 2 interests, which, if appropriate, may be required to be written down in value. If such an event had occurred as of June 30, 2005, APS would have been required to assume approximately \$245 million of debt and pay the equity participants approximately \$191 million.

Guarantees and Letters of Credit

We and certain of our subsidiaries have issued guarantees and letters of credit in support of our unregulated businesses. We have also obtained surety bonds on behalf of APS Energy Services. We have not recorded any liability on our Condensed Consolidated Balance Sheets with respect to these obligations. We generally agree to indemnification provisions related to liabilities arising from or related to certain of our agreements, with limited exceptions depending on the particular agreement. See Note 15 for additional information regarding guarantees and letters of credit.

See “Pinnacle West Energy” below for information regarding Pinnacle West’s guarantee of \$500 million of Pinnacle West Energy’s debt obligations.

Credit Ratings

The ratings of securities of Pinnacle West and APS as of August 8, 2005 are shown below and are considered to be “investment-grade” ratings. The ratings reflect the respective views of the rating agencies, from which an explanation of the significance of their ratings may be obtained. There is no assurance that these ratings will continue for any given period of time. The ratings may be revised or withdrawn entirely by the rating agencies, if, in their respective judgments, circumstances so warrant. Any downward revision or withdrawal may adversely affect the market price of Pinnacle West’s or APS’ securities and serve to increase those companies’ cost of and access to capital. It may also require additional collateral related to certain derivative instruments (see Note 10).

	<u>Moody's</u>	<u>Standard & Poor's</u>
Pinnacle West		
Senior unsecured	Baa2	BBB-
Commercial paper	P-2	A-2
Outlook	Stable	Stable
APS		
Senior unsecured	Baa1	BBB
Secured lease obligation bonds	Baa1	BBB
Commercial paper	P-2	A-2
Outlook	Stable	Stable

Debt Provisions

Pinnacle West’s and APS’ debt covenants related to their respective bank financing arrangements include a debt-to-total-capitalization ratio and an interest coverage test. Pinnacle West and APS comply with these covenants and each anticipates it will continue to meet these and other significant covenant requirements. These covenants require that the ratio of debt to total capitalization cannot exceed 65% for the Company and for APS. At June 30, 2005, the ratio was approximately 53% for Pinnacle West and 51% for APS. The provisions regarding interest coverage require a minimum cash coverage of two times the interest requirements for each of the Company and APS. The interest coverage is approximately 4 times under the Company’s and APS’ bank financing agreements. Failure to comply with such covenant levels would result in an event of default which, generally speaking, would require the immediate repayment of the debt subject to the covenants.

Neither Pinnacle West’s nor APS’ financing agreements contain “ratings triggers” that would result in an acceleration of the required interest and principal payments in the event of a ratings downgrade. However, in the event of a ratings downgrade, Pinnacle West and/or APS may be subject to increased interest costs under certain financing agreements.

All of Pinnacle West’s bank agreements contain “cross-default” provisions that would result in defaults and the potential acceleration of payment under these loan agreements if Pinnacle West or APS were to default under other agreements. All of APS’ bank agreements contain cross-default

provisions that would result in defaults and the potential acceleration of payment under these bank agreements if APS were to default under other agreements. Pinnacle West's and APS' credit agreements generally contain provisions under which the lenders could refuse to advance loans in the event of a material adverse change in financial condition or financial prospects, except that Pinnacle West and APS do not have a material adverse change restriction for revolver borrowings equal to outstanding commercial paper amounts.

See Note 4 for further discussions.

Capital Needs and Resources — By Company

Pinnacle West (Parent Company)

Our primary cash needs are for dividends to our shareholders; interest payments and optional and mandatory repayments of principal on our long-term debt. The level of our common dividends and future dividend growth will be dependent on a number of factors including, but not limited to, payout ratio trends, free cash flow and financial market conditions.

Our primary sources of cash are dividends from APS, external financings and cash distributions from our other subsidiaries, primarily SunCor. We expect SunCor to make cash distributions to the parent company of approximately \$80 to \$100 million in 2005 based on anticipated asset sales activities. As discussed in Note 5 under "ACC Financing Order," APS must maintain a common equity ratio of at least 40% and may not pay common dividends if the payment would reduce its common equity below that threshold. As defined in the Financing Order, common equity ratio is common equity divided by common equity plus long-term debt, including current maturities of long-term debt. At June 30, 2005, APS' common equity ratio as defined was approximately 48%.

Pinnacle West sponsors a qualified pension plan for the employees of Pinnacle West and our subsidiaries. We contribute at least the minimum amount required under IRS regulations, but no more than the maximum tax-deductible amount. The minimum required funding takes into consideration the value of the fund assets and our pension obligation. We contributed \$35 million in 2004. APS and other subsidiaries fund their share of the pension contribution, of which APS represents approximately 92% of the total funding amounts described above. The assets in the plan are comprised of common stocks, bonds and real estate. Future year contribution amounts are dependent on fund performance and fund valuation assumptions. Our minimum required pension contribution in 2005 is approximately \$53 million. Of this amount, we have contributed approximately \$27 million through July 2005. The contribution to be made to other post retirement benefit plans in 2005 is estimated to be approximately \$37 million. Of this amount, we contributed approximately \$18 million through July 2005. APS' share is approximately 92% of both plans.

On May 2, 2005, Pinnacle West redeemed at par all of its \$165 million Floating Rate Senior Notes due November 1, 2005. The Company used cash on hand to redeem the notes.

On May 2, 2005, Pinnacle West issued 6,095,000 shares of its common stock at an offering price of \$42 per share, resulting in net proceeds of approximately \$248 million. Pinnacle West used the net proceeds for general corporate purposes, including making capital contributions to APS, which, in turn, used such funds to pay a portion of the approximately \$190 million purchase price to acquire the Sundance Plant and for other capital expenditures incurred to meet the growing needs of

APS' service territory.

On July 13, 2005, the Pinnacle West Board of Directors declared a quarterly dividend of \$0.475 per share of common stock, payable on September 1, 2005, to shareholders of record on August 1, 2005.

APS

APS' capital requirements consist primarily of capital expenditures and optional and mandatory redemptions of long-term debt. See "ACC Financing Order" in Note 5 for a discussion of the \$500 million loan from APS to Pinnacle West Energy authorized by the ACC pursuant to the Financing Order. This loan was repaid on April 11, 2005.

APS pays for its capital requirements with cash from operations and, to the extent necessary, external financings. APS has historically paid for its dividends to Pinnacle West with cash from operations. See "Pinnacle West (Parent Company)" above for a discussion of the common equity ratio that APS must maintain in order to pay dividends to Pinnacle West.

On January 15, 2005, APS repaid its \$100 million 6.25% Notes due 2005. APS used cash on hand to redeem these notes.

On March 1, 2005, Maricopa County, Arizona Pollution Control Corporation issued \$164 million of variable interest rate pollution control bonds, 2005 Series A-E, due 2029. The bonds were issued to refinance \$164 million of outstanding pollution control bonds. The Series A-E bonds are payable solely from revenues obtained from APS pursuant to a loan agreement between APS and Maricopa County, Arizona Pollution Control Corporation. These bonds are classified as long-term debt on our Condensed Consolidated Balance Sheets.

On August 1, 2005, APS repaid \$300 million of its 7.625% Notes due 2005. APS used cash on hand to repay these notes.

Although provisions in APS' articles of incorporation and ACC financing orders establish maximum amounts of preferred stock and debt that APS may issue, APS does not expect any of these provisions to limit its ability to meet its capital requirements.

See "Deferred Purchased Power and Fuel Costs" above and "APS General Rate Case" in Note 5 for information regarding the PSA approved by the ACC.

Pinnacle West Energy

Pinnacle West Energy expects minimal capital expenditures over the next three years. See the capital expenditures table above for actual capital expenditures during the six months ended June 30, 2005 and projected capital expenditures for the next three years (the estimated capital expenditures related to the PWEC Dedicated Assets are reflected in APS).

See “ACC Financing Order” in Note 5 for a discussion of the \$500 million loan from APS to Pinnacle West Energy authorized by the ACC pursuant to the Financing Order. On April 11, 2005 Pinnacle West Energy issued \$500 million Floating Rate Senior Notes due April 1, 2007. Pinnacle West has unconditionally guaranteed these notes. Pinnacle West Energy used the proceeds of this issuance to repay the APS loan. Pinnacle West Energy intends to repay the Floating Rate Senior Note with \$500 million expected to be received from APS in connection with Pinnacle West Energy’s transfer of the PWEC Dedicated Assets to APS.

See Note 17 of Notes to Condensed Consolidated Financial Statements above for a discussion of the pending sale of our 75% ownership interest in Silverhawk.

Other Subsidiaries

During the past three years, SunCor funded its cash requirements with cash from operations and its own external financings. SunCor’s capital needs consist primarily of capital expenditures for land development and retail and office building construction. See the capital expenditures table above for actual capital expenditures during the six months ended June 30, 2005 and projected capital expenditures for the next three years. SunCor expects to fund its capital requirements with cash from operations and external financings.

We expect SunCor to make cash distributions to the parent company of approximately \$80 to \$100 million in 2005 based on anticipated asset sales activities.

El Dorado expects minimal capital requirements over the next three years and intends to focus on prudently realizing the value of its existing investments.

APS Energy Services expects minimal capital expenditures over the next three years.

CRITICAL ACCOUNTING POLICIES

In preparing the financial statements in accordance with GAAP, management must often make estimates and assumptions that affect the reported amounts of assets, liabilities, revenues, expenses and related disclosures at the date of the financial statements and during the reporting period. Some of those judgments can be subjective and complex, and actual results could differ from those estimates. Our most critical accounting policies include the impacts of regulatory accounting and the determination of the appropriate accounting for our pension and other postretirement benefits and derivatives accounting. There have been no changes to our critical accounting policies since our 2004 Form 10-K. See “Critical Accounting Policies” in Item 7 of the 2004 Form 10-K for further details about our critical accounting policies.

PINNACLE WEST CONSOLIDATED – FACTORS AFFECTING OUR FINANCIAL OUTLOOK

Factors Affecting Operating Revenues, Purchased Power and Fuel Costs

General Electric operating revenues are derived from sales of electricity in regulated retail markets in Arizona and from competitive retail and wholesale power markets in the western United States. These revenues are affected by electricity sales volumes related to customer mix, customer

growth and average usage per customer as well as electricity prices and variations in weather from period to period. Competitive sales of energy and energy-related products and services are made by APS Energy Services in western states that have opened to competition.

Customer and Sales Growth The customer and sales growth referred to in this paragraph applies to Native Load customers and sales to them. Customer growth in APS' service territory averaged about 3.4% a year for the three years 2002 through 2004; we currently expect customer growth to average about 3.8% per year from 2005 to 2007. We currently estimate that total retail electricity sales in kilowatt-hours will grow 5.0% on average, from 2005 through 2007, before the effects of weather variations. Customer growth for the six-month period ended June 30, 2005 compared with the prior year period was 4.1%.

Actual sales growth, excluding weather-related variations, may differ from our projections as a result of numerous factors, such as economic conditions, customer growth and usage patterns. Our experience indicates that a reasonable range of variation in our kilowatt-hour sales projection attributable to such economic factors can result in increases or decreases in annual net income of up to \$10 million.

Weather In forecasting retail sales growth, we assume normal weather patterns based on historical data. Historical extreme weather variations have resulted in annual variations in net income in excess of \$20 million. However, our experience indicates that the more typical variations from normal weather can result in increases or decreases in annual net income of up to \$10 million.

Retail Rate Matters See "APS General Rate Case" in Note 5 for a discussion of the ACC's order in APS' general rate case and "Power Supply Adjuster" for information regarding APS' application to the ACC requesting recovery of \$100 million in deferred fuel and purchased power costs under the PSA. APS expects to file another general rate case in late 2005.

Purchased Power and Fuel Costs See "APS General Rate Case" in Note 5 for information regarding the PSA approved by the ACC. Purchased power and fuel costs are impacted by our electricity sales volumes, existing contracts for purchased power and generation fuel, our power plant performance, transmission availability or constraints, prevailing market prices, new generating plants being placed in service and our hedging program for managing such costs. See "Natural Gas Supply" in Note 12 for more information on fuel costs.

Wholesale Power Market Conditions The marketing and trading division focuses primarily on managing APS' purchased power and fuel risks in connection with its costs of serving retail customer demand. The marketing and trading division, subject to specified parameters, markets, hedges and trades in electricity, fuels and emission allowances and credits. Our future earnings will be affected by the strength or weakness of the wholesale power market.

Other Factors Affecting Financial Results

Operations and Maintenance Expenses Operations and maintenance expenses are impacted by growth, power plant additions and operations, inflation, outages, higher trending pension and other postretirement benefit costs and other factors.

Depreciation and Amortization Expenses Depreciation and amortization expenses are impacted by net additions to utility plant and other property, which includes generation construction

or acquisition, changes in depreciation and amortization rates (see Note 5), and changes in regulatory asset amortization. See Note 17 for information on the pending sale of Silverhawk. See Note 4 for information on APS' acquisition of the Sundance Plant in 2005 and "Requests for Proposals" in Part II, Item 5 of this report for more information on requests for proposals to acquire additional long-term resources in 2006 and 2007.

Property Taxes Taxes other than income taxes consist primarily of property taxes, which are affected by tax rates and the value of property in-service and under construction. The average property tax rate for APS, which currently owns the majority of our property, was 9.2% of assessed value for 2004 and 9.3% for 2003. We expect property taxes to increase as new power plants, the acquisition of the Sundance Plant and our additions to transmission and distribution facilities phase-in to the property tax base.

Interest Expense Interest expense is affected by the amount of debt outstanding and the interest rates on that debt. The primary factors affecting borrowing levels in the next several years are expected to be our capital requirements and our internally generated cash flow. Capitalized interest offsets a portion of interest expense while capital projects are under construction. We stop accruing capitalized interest on a project when it is placed in commercial operation. We placed new power plants in commercial operation in 2001, 2002, 2003 and 2004. Interest expense is also affected by interest rates on variable-rate debt and interest rates on the refinancing of the Company's future liquidity needs.

Retail Competition Although some very limited retail competition existed in APS' service area in 1999 and 2000, there are currently no active retail competitors providing unbundled energy or other utility services to APS' customers. As a result, we cannot predict when, and the extent to which, additional competitors will re-enter APS' service territory.

Subsidiaries In the case of SunCor, efforts to accelerate asset sales activities in 2004 were successful. A portion of these sales have been, and additional amounts may be required to be, reported as discontinued operations on our Condensed Consolidated Statements of Income. SunCor's net income was \$45 million in 2004. See Note 17 for further discussion. We anticipate SunCor's earnings contributions in 2005 to be approximately \$50 million after income taxes.

El Dorado's historical results are not indicative of future performance.

General Our financial results may be affected by a number of broad factors. See "Forward-Looking Statements" for further information on such factors, which may cause our actual future results to differ from those we currently seek or anticipate.

Market Risks

Our operations include managing market risks related to changes in interest rates, commodity prices and investments held by our nuclear decommissioning trust fund.

Interest Rate and Equity Risk

Our major financial market risk exposure is to changing interest rates. Changing interest rates will affect interest paid on variable-rate debt and interest earned by our nuclear decommissioning trust fund. Our policy is to manage interest rates through the use of a combination of fixed-rate and floating-rate debt.

Commodity Price Risk

We are exposed to the impact of market fluctuations in the commodity price and transportation costs of electricity, natural gas, coal and emissions allowances. We manage risks associated with these market fluctuations by utilizing various commodity instruments that qualify as derivatives, including exchange-traded futures and options and over-the-counter forwards, options and swaps. Our ERM, consisting of officers and key management personnel, oversees company-wide energy risk management activities and monitors the results of marketing and trading activities to ensure compliance with our stated energy risk management and trading policies. As part of our risk management program, we use such instruments to hedge purchases and sales of electricity, fuels and emissions allowances and credits. The changes in market value of such contracts have a high correlation to price changes in the hedged commodities. In addition, subject to specified risk parameters monitored by the ERM, we engage in marketing and trading activities intended to profit from market price movements.

The mark-to-market value of derivative instruments related to our risk management and trading activities are presented in two categories consistent with our business segments:

- Regulated Electricity – non-trading derivative instruments that hedge our purchases and sales of electricity and fuel for APS’ Native Load requirements of our regulated electricity business segment; and
- Marketing and Trading – non-trading and trading derivative instruments of our competitive business segment.

The following tables show the pretax changes in mark-to-market of our non-trading and trading derivative positions for the six months ended June 30, 2005 and 2004 (dollars in millions):

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	Six Months Ended June 30, 2005		Six Months Ended June 30, 2004	
	Regulated Electricity	Marketing and Trading	Regulated Electricity	Marketing and Trading
Mark-to-market of net positions at beginning of period	\$ 33	\$ 107	\$ —	\$ 69
Change in mark-to-market gains for future period deliveries	4	12	11	13
Changes in cash flow hedges recorded in OCI	84	(9)	48	25
Ineffective portion of changes in fair value	12	—	1	1
Mark-to-market (gains) losses realized during the period	(7)	41	3	(10)
Mark-to-market of net positions at end of period	<u>\$ 126</u>	<u>\$ 151</u>	<u>\$ 63</u>	<u>\$ 98</u>

The tables below show the fair value of maturities of our non-trading and trading derivative contracts (dollars in millions) at June 30, 2005 by maturities and by the type of valuation that is performed to calculate the fair values. See Note 1, “Derivative Accounting,” in Item 8 of our 2004 Form 10-K for more discussion of our valuation methods.

Regulated Electricity

Source of Fair Value	2005	2006	2007	Total fair value
Prices actively quoted	\$ 39	\$ 54	\$ 28	\$ 121
Prices provided by other external sources	—	4	3	7
Prices based on models and other valuation methods	(1)	(1)	—	(2)
Total by maturity	<u>\$ 38</u>	<u>\$ 57</u>	<u>\$ 31</u>	<u>\$ 126</u>

Marketing and Trading

Source of Fair Value	2005	2006	2007	2008	2009	Total fair value
Prices actively quoted	\$ 28	\$ —	\$ —	\$ —	\$ —	\$ 28
Prices provided by other external sources	—	66	83	41	(1)	189
Prices based on models and other valuation methods	(5)	(21)	(30)	(10)	—	(66)
Total by maturity	<u>\$ 23</u>	<u>\$ 45</u>	<u>\$ 53</u>	<u>\$ 31</u>	<u>\$ (1)</u>	<u>\$ 151</u>

The table below shows the impact that hypothetical price movements of 10% would have on the market value of our risk management and trading assets and liabilities included on Pinnacle

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West's Condensed Consolidated Balance Sheets at June 30, 2005 and December 31, 2004 (dollars in millions).

Commodity	June 30, 2005 Gain (Loss)		December 31, 2004 Gain (Loss)	
	Price Up 10%	Price Down 10%	Price Up 10%	Price Down 10%
Mark-to-market changes reported in earnings (a):				
Electricity	\$ (3)	\$ 2	\$ (4)	\$ 4
Natural gas	1	(1)	2	(2)
Other	1	(1)	1	(1)
Mark-to-market changes reported in OCI (b):				
Electricity	44	(44)	35	(35)
Natural gas	72	(72)	43	(43)
Total	<u>\$ 115</u>	<u>\$ (116)</u>	<u>\$ 77</u>	<u>\$ (77)</u>

- (a) These contracts are primarily structured sales activities hedged with a portfolio of forward purchases that protects the economic value of the sales transactions.
- (b) These contracts are hedges of our forecasted purchases of natural gas and electricity. The impact of these hypothetical price movements would substantially offset the impact that these same price movements would have on the physical exposures being hedged.

Credit Risk

We are exposed to losses in the event of nonperformance or nonpayment by counterparties. We have risk management and trading contracts with many counterparties, including one counterparty for which a worst case exposure represents approximately 16% of Pinnacle West's \$620 million of risk management and trading assets as of June 30, 2005. See Note 1, "Derivative Accounting" in Item 8 of our 2004 Form 10-K for a discussion of our credit valuation adjustment policy. See Note 10 for further discussion of credit risk.

ARIZONA PUBLIC SERVICE COMPANY – RESULTS OF OPERATIONS

General

Throughout the following explanations of our results of operations, we refer to "gross margin." Gross margin refers to electric operating revenues less purchased power and fuel costs. Gross margin is a "non-GAAP financial measure," as defined in accordance with SEC rules. Exhibit 99.4 reconciles this non-GAAP financial measure to operating income, which is the most directly comparable financial measure calculated and presented in accordance with GAAP. We view gross margin as an important performance measure of the core profitability of our operations. This measure is a key component of our internal financial reporting and is used by our management in analyzing our business. We believe that investors benefit from having access to the same financial

measures that our management uses. In addition, we have reclassified certain prior-period amounts to conform to our current-period presentation.

Deferred Purchased Power and Fuel Costs

APS' retail rate case settlement became effective April 1, 2005. As part of the settlement, the ACC approved a 4.2% annual retail rate increase and a PSA that provides mechanisms for adjusting rates to reflect variations in fuel and purchased power costs. In accordance with the PSA, APS defers for future rate recovery 90% of the difference between actual purchased power and fuel costs and the amount for such costs currently included in base rates. As of June 30, 2005, APS had deferred \$34 million of pretax purchased power and fuel costs.

Operating Results – Three-month period ended June 30, 2005 compared with three-month period ended June 30, 2004

APS' net income for the three months ended June 30, 2005 was \$64 million compared with \$55 million for the prior-year period. The \$9 million increase in the period-to-period comparison is due to a retail price increase effective April 1, 2005, higher retail sales volumes due to customer growth, the absence of regulatory asset amortization, and lower depreciation due to lower depreciation rates. These positive factors were partially offset by higher purchased power and fuel costs, net of deferred costs, in accordance with the retail rate settlement, higher operations and maintenance costs primarily related to generation, customer service, and benefit costs and lower realized margins on wholesale sales.

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Additional details on the major factors that increased (decreased) net income are contained in the following table (dollars in millions):

	Increase (Decrease)	
	Pretax	After Tax
Gross margin:		
Retail price increase effective April 1, 2005	\$ 28	\$ 17
Higher retail sales volumes due to customer growth, excluding weather effects	13	8
Higher purchased power and fuel costs, net of deferred costs, in accordance with the retail rate settlement	(23)	(14)
Higher margins on energy trading primarily due to higher wholesale electricity prices	3	2
Miscellaneous items, net	1	—
Net increase in gross margin	22	13
Higher operation and maintenance expense due to generation, customer service and benefit costs	(11)	(7)
Depreciation and amortization decreases primarily due to:		
Absence of regulatory asset amortization	10	6
Lower depreciation rates (see note 5) partially offset by higher depreciable assets	2	1
Higher interest expense, net of capitalized financing costs, primarily due to higher debt balances and interest rates	(3)	(2)
Miscellaneous items, net	(1)	(2)
Net increase in net income	<u>\$ 19</u>	<u>\$ 9</u>

Regulated Electricity Revenues

Regulated electricity revenues were \$58 million higher for the three months ended June 30, 2005 compared with the prior-year period primarily as a result of:

- a \$28 million increase in retail revenues due to a price increase effective April 1, 2005;
- an \$18 million increase in retail revenues related to customer growth, excluding weather effects; and
- a \$12 million increase in Off-System Sales primarily due to sales previously reported in marketing and trading now classified as sales in regulated electricity in accordance with the retail rate settlement.

Marketing and Trading Revenues

Marketing and trading revenues were \$39 million lower for the three months ended June 30, 2005 compared with the prior-year period primarily as a result of:

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- a \$25 million decrease in revenues from Off-System Sales primarily due to lower sales volumes and sales previously reported in marketing and trading now classified as sales in the regulated electricity in accordance with the retail rate settlement;
- a \$15 million decrease in energy trading revenues on realized sales of electricity primarily due to lower delivered electricity prices and lower sales volumes; and
- a \$1 million increase on future mark-to-market gains due to higher price volatility.

Operating Results – Six-month period ended June 30, 2005 compared with six-month period ended June 30, 2004

APS' net income for the six months ended June 30, 2005 was \$91 million compared with \$89 million for the prior-year period. The \$2 million increase in the period-to-period comparison is due to a retail price increase effective April 1, 2005, higher retail sales volumes due to customer growth, the absence of regulatory asset amortization, and lower depreciation due to lower depreciation rates. These positive factors were partially offset by higher purchased power and fuel costs, net of deferred costs, in accordance with the retail rate settlement, higher operations and maintenance costs primarily related to generation, customer service, and benefit costs, lower realized margins on wholesale sales, and higher property taxes due to increased plant in service.

Additional details on the major factors that increased (decreased) net income are contained in the following table (dollars in millions):

	Increase (Decrease)	
	Pretax	After Tax
Gross margin:		
Retail price increase effective April 1, 2005	\$ 28	\$ 17
Higher retail sales volumes due to customer growth, excluding weather effects	20	12
Higher purchased power and fuel costs, net of deferred costs, in accordance with the retail rate settlement	(24)	(15)
Higher margins on energy trading primarily due to lower wholesale electricity prices	5	3
Miscellaneous items, net	(2)	(1)
Net increase in gross margin	27	16
Operations and maintenance increases primarily due to:		
Generation costs, including planned maintenance	(9)	(5)
Customer service costs, including planned maintenance	(10)	(6)
Benefit costs	(7)	(4)
Miscellaneous items, net	(2)	(2)
Depreciation and amortization decreases primarily due to:		
Absence of regulatory asset amortization	19	11
Higher depreciable assets partially offset by lower depreciation rates (see Note 5)	(1)	—
Higher property taxes due to increased plant in service	(5)	(3)
Miscellaneous items, net	(3)	(5)
Net increase in net income	\$ 9	\$ 2

Regulated Electricity Revenues

Regulated electricity revenues were \$56 million higher for the six months ended June 30, 2005 compared with the prior-year period primarily as a result of:

- a \$28 million increase in retail revenues related to customer growth, excluding weather effects;
- a \$28 million increase in retail revenues due to a price increase effective April 1, 2005;
- a \$12 million increase in Off-System Sales due to increased volumes for plants dedicated to APS customers and sales previously reported in marketing and trading now classified as sales in regulated electricity in accordance with the retail rate settlement;
- a \$9 million decrease in retail revenues related to milder weather; and
- a \$3 million decrease due to miscellaneous factors.

Marketing and Trading Revenues

Marketing and trading revenues were \$37 million lower for the six months ended June 30, 2005 compared with the prior-year period primarily as a result of:

- an \$18 million decrease in revenues from Off-System Sales primarily due to lower sales volumes, prices, and sales previously reported in marketing and trading now classified as sales in regulated electricity in accordance with the retail rate settlement;
- a \$17 million decrease in energy trading revenues on realized sales of electricity primarily due to lower delivered electricity prices and lower volumes; and
- a \$2 million decrease due to miscellaneous factors.

ARIZONA PUBLIC SERVICE COMPANY – LIQUIDITY AND CAPITAL RESOURCES

Contractual Obligations

APS' future contractual obligations have not changed materially from the amounts disclosed in Part II, Item 7 of the 2004 Form 10-K with the exception of our aggregate:

- purchased power and fuel commitments, which increased from approximately \$948 million at December 31, 2004 to \$1.1 billion at June 30, 2005 primarily due to increased commitments for the years 2005 through 2007; and
- nuclear decommissioning funding requirements which increased from approximately \$201 million at December 31, 2004 to \$386 million at June 30, 2005 for the years 2005 and thereafter.

See Note S-1 for a list of APS' payments due on total long-term debt and capitalized lease requirements.

RISK FACTORS

Exhibit 99.1 and Exhibit 99.2, which are hereby incorporated by reference, contain a discussion of risk factors affecting Pinnacle West and APS, respectively.

FORWARD-LOOKING STATEMENTS

This document contains forward-looking statements based on current expectations, and neither Pinnacle West nor APS assumes any obligation to update these statements or make any further statements on any of these issues, except as required by applicable law. These forward-looking statements are often identified by words such as “estimate,” “predict,” “hope,” “may,” “believe,” “anticipate,” “plan,” “expect,” “require,” “intend,” “assume” and similar words. Because actual results may differ materially from expectations, we caution readers not to place undue reliance on these statements. A number of factors could cause future results to differ materially from historical results, or

from results or outcomes currently expected or sought by Pinnacle West or APS. In addition to the “Risk Factors” described in Exhibits 99.1 and 99.2 to this report, these factors include, but are not limited to:

- state and federal regulatory and legislative decisions and actions, including by the ACC and the FERC;
- the ongoing restructuring of the electric industry, including the introduction of retail electric competition in Arizona and decisions impacting wholesale competition;
- the outcome of regulatory, legislative and judicial proceedings relating to the restructuring;
- market prices for electricity and natural gas;
- power plant performance and outages;
- transmission outages and constraints;
- weather variations affecting local and regional customer energy usage;
- customer growth and energy usage;
- regional economic and market conditions, including the results of litigation and other proceedings resulting from the California energy situation, volatile purchased power and fuel costs and the completion of generation and transmission construction in the region, which could affect customer growth and the cost of power supplies;
- the cost of debt and equity capital and access to capital markets;
- the uncertainty that current credit ratings will remain in effect for any given period of time;
- our ability to compete successfully outside traditional regulated markets (including the wholesale market);
- the performance of our marketing and trading activities due to volatile market liquidity and any deteriorating counterparty credit and the use of derivative contracts in our business (including the interpretation of the subjective and complex accounting rules related to these contracts);
- changes in accounting principles generally accepted in the United States of America and the interpretation of those principles;
- the performance of the stock market and the changing interest rate environment, which affect the amount of required contributions to Pinnacle West’s pension plan and APS’ nuclear decommissioning trust funds, as well as the reported costs of providing pension and other postretirement benefits;
- technological developments in the electric industry;
- the strength of the real estate market in SunCor’s market areas, which include Arizona, Idaho, New Mexico and Utah; and
- other uncertainties, all of which are difficult to predict and many of which are beyond the control of Pinnacle West and APS.

Item 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

See “Pinnacle West Consolidated – Factors Affecting Our Financial Outlook” in Item 2 above for a discussion of quantitative and qualitative disclosures about market risks.

Item 4. CONTROLS AND PROCEDURES

(a) Disclosure Controls and Procedures

The term “disclosure controls and procedures” means controls and other procedures of a company that are designed to ensure that information required to be disclosed by a company in the reports that it files or submits under the Securities Exchange Act of 1934 (the “Exchange Act”) (15 U.S.C. 78a *et seq.*) is recorded, processed, summarized and reported, within the time periods specified in the SEC’s rules and forms. Disclosure controls and procedures include, without limitation, controls and procedures designed to ensure that information required to be disclosed by a company in the reports that it files or submits under the Exchange Act is accumulated and communicated to a company’s management, including its principal executive and principal financial officers, or persons performing similar functions, as appropriate to allow timely decisions regarding required disclosure.

Pinnacle West’s management, with the participation of Pinnacle West’s Chief Executive Officer and Chief Financial Officer, have evaluated the effectiveness of Pinnacle West’s disclosure controls and procedures as of June 30, 2005. Based on that evaluation, Pinnacle West’s Chief Executive Officer and Chief Financial Officer have concluded that, as of that date, Pinnacle West’s disclosure controls and procedures were effective.

APS’ management, with the participation of APS’ Chief Executive Officer and Chief Financial Officer, have evaluated the effectiveness of APS’ disclosure controls and procedures as of June 30, 2005. Based on that evaluation, APS’ Chief Executive Officer and Chief Financial Officer have concluded that, as of that date, APS’ disclosure controls and procedures were effective.

(b) Changes In Internal Control Over Financial Reporting

The term “internal control over financial reporting” (defined in SEC Rule 13a-15(f)) refers to the process of a company that is designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with GAAP.

No change in Pinnacle West’s or APS’ internal control over financial reporting occurred during the fiscal quarter ended June 30, 2005 that materially affected, or is reasonably likely to materially affect, Pinnacle West’s or APS’ internal control over financial reporting.

Part II — OTHER INFORMATION**Item 1. LEGAL PROCEEDINGS**

See Note 12 of Notes to Condensed Consolidated Financial Statements in Part I, Item 1 of this report in regard to pending or threatened litigation or other disputes.

Item 4. SUBMISSION OF MATTERS TO A VOTE OF SECURITY HOLDERS**Directors**

At our Annual Meeting of Shareholders held on May 18, 2005, the following persons were elected as directors:

Class II (Term to expire at 2008 Annual Meeting)	Votes For	Votes Against	Abstentions and Broker Non-Votes
Edward N. Basha, Jr.	77,333,734	1,359,058	N/A
Michael L. Gallagher	70,656,769	8,036,023	N/A
Bruce J. Nordstrom	77,456,120	1,236,672	N/A
William J. Post	76,929,393	1,763,399	N/A

Continuing Directors

The terms of Jack E. Davis, Pamela Grant, Martha O. Hesse, and William S. Jamieson, Jr. will expire in 2006. The terms of Roy A. Herberger, Jr., Humberto S. Lopez, Kathryn L. Munro, and William L. Stewart will expire in 2007.

Independent Auditors

At the same meeting, a proposal for the ratification of the selection of Deloitte & Touche LLP as independent Auditors of the Company was submitted to the shareholders, and the voting was as follows:

Proposal for the ratification of Deloitte & Touche LLP	Votes For	Votes Against	Abstentions and Broker Non-Votes
	75,880,147	2,031,585	781,060

Item 5. OTHER INFORMATION**Construction and Financing Programs**

See “Liquidity and Capital Resources” in Part I, Item 2 of this report for a discussion of construction and financing programs of the Company and its subsidiaries.

Regulatory Matters

See Note 5 of Notes to Condensed Consolidated Financial Statements in Part I, Item 1 of this report for a discussion of regulatory developments.

In connection with the FERC proceeding under which APS received approval to acquire the Sundance Plant, APS committed to an independent market monitoring plan that provides for an independent expert to monitor APS' generation dispatch and operation of its transmission system and report to the FERC any potentially anti-competitive conduct. The plan took effect upon closing of the transaction and will continue in effect until the FERC approves a regional market monitoring plan or five years, whichever is earlier.

Environmental Matters

See "Environmental Matters — Superfund" in Note 12 of Notes to Condensed Consolidated Financial Statements in Part I, Item 1 of this report for a discussion of a Superfund site.

Regional Haze Rules

On June 15, 2005, EPA issued the Clean Air Visibility Rule, which amends the 1999 regional haze rules by providing guidelines, known as the BART guidelines, for states to use in determining which facilities must install controls and the type of controls the facilities must use. See "Environmental Matters — Regional Haze Rules" in Part I, Item 1 of the 2004 Form 10-K. The Company is currently evaluating the potential impact of this rule.

On August 1, 2005, the EPA proposed a rule to, among other things, revise a previously-adopted rule that would have allowed nine western states and tribes to follow a regional haze implementation plan for "Class I Areas" different from that provided for in the Clean Air Visibility Rule. See "EPA Environmental Regulation - Regional Haze Rules" in Part I, Item 1 of the 2004 Form 10-K for additional information about the previously-adopted rule. The Company is currently evaluating the impact of the proposed rule.

Navajo Nation Environmental Issues

On October 16, 1995, the Four Corners participants and the Navajo Generating Station participants each filed a lawsuit in the District Court of the Navajo Nation, Window Rock District, challenging the applicability of the Navajo Nation Air Pollution Prevention and Control Act, the Navajo Nation Safe Drinking Water Act and the Navajo Nation Pesticide Act (collectively, the Navajo Acts). See "Environmental Matters — Navajo Nation Environmental Issues", in Part I, Item 1 of the 2004 Form 10-K. On May 18, 2005, APS, Salt River Project and the Navajo Nation executed a Voluntary Compliance Agreement ("VCA") to resolve their disputes regarding the Navajo Nation Air Pollution Prevention and Control Act for the Four Corners Power Plant and the Navajo Generating Station. The fundamental premise of the VCA is that the Navajo Nation EPA may regulate air issues for the Four Corners Power Plant only because the participants have agreed to submit to such regulation for the term of the agreement and under certain circumstances. If EPA approves the Navajo Nation's air programs consistent with the VCA, APS would dismiss the pending litigation in the Navajo Nation Supreme Court and would dismiss the pending litigation in the Navajo Nation District Court to the extent the claims relate to the Clean Air Act. The Agreement does not address or resolve any dispute relating to the other Navajo Acts.

The Four Corners region, in which the Four Corners Plant is located, has been experiencing drought conditions. See "Water Supply" in Part I, Item 1 of the 2004 Form 10-K. APS has signed an agreement with area stakeholders to minimize the effect of the drought on the operations of the plant in 2005. The effect of the drought cannot be fully assessed at this time, and APS cannot predict the ultimate outcome, if any, of the drought or whether the drought will adversely affect the amount of power available, or the price thereof, from Four Corners.

Maricopa County Environmental Issues

During the period from November 2004 through March 2005, the Maricopa County Air Quality Department ("MCAQD") issued a series of Notices of Violation ("NOVs") to APS' West Phoenix Power Plant that generally allege that the plant failed to comply with applicable permit requirements. APS is currently engaged in discussions with MCAQD concerning the NOVs. We do not expect the resolution of these matters to have a material adverse effect on our financial position, results of operations, or cash flows.

Regional Transmission Organizations (“RTO”)

On October 16, 2001, APS and other owners of electric transmission lines in the southwestern U.S. filed with the FERC a request for a declaratory order confirming that their proposal to form WestConnect RTO, LLC would satisfy the FERC’s requirements for the formation of an RTO. See “Regulation and Competition — Wholesale — Regional Transmission Organizations” in Part I, Item 1 of the 2004 Form 10-K. On July 1, 2005, FERC issued an order in response to a request from Bonneville Power Administration and utilities in the Northwest, regarding Grid West, a proposed regional organization for the Northwest region. In that order, FERC agreed that a regional organization for the Northwest region would not need to satisfy all of the RTO requirements established in the December 1999 order. APS is currently evaluating the impact of this order on its RTO initiative.

Federal Energy Legislation

On August 8, 2005, the President signed the Energy Policy Act of 2005 into law. Due to its recent enactment and because many provisions require implementing regulations, the Company is unable to predict the impact of the Act on its operations.

Requests for Proposals

APS continually assesses its need for additional capacity resources to assure system reliability. Under the terms of the 2004 Settlement Agreement, APS committed to seek proposals from the competitive wholesale market for filling its future resource needs. The current reliability RFP identifies the amount of capacity and energy needed to reliably meet expected customer demands and sought proposals for at least 1,000 MW of new generating capacity for 2007 and beyond. Bid responses were submitted by July 18, 2005. Short-listed bidders will be notified by August 30, 2005, and winning bidders will be notified in mid-October.

APS also has in process a renewable RFP seeking at least 100 MW of renewable capacity with a capability of producing at least 250,000 MWH annually. In accordance with the terms of the 2004 Settlement Agreement, power must be deliverable to the APS transmission system and its pricing must not exceed 125% of conventional resource alternatives. A final decision, which is expected in mid-September 2005, is subject to ACC approval if an out-of-state provider is selected.

Item 6. EXHIBITS

(a) Exhibits

<i><u>Exhibit No.</u></i>	<i><u>Registrant(s)</u></i>	<i><u>Description</u></i>
12.1	Pinnacle West	Ratio of Earnings to Fixed Charges
12.2	APS	Ratio of Earnings to Fixed Charges
31.1	Pinnacle West	Certificate of William J. Post, Chief Executive Officer, pursuant to Rule 13a-14(a) and Rule 15d-14(a) of the Securities Exchange Act, as amended
31.2	Pinnacle West	Certificate of Donald E. Brandt, Chief Financial Officer, pursuant to Rule 13a-14(a) and Rule 15d-14(a) of the Securities Exchange Act, as amended
31.3	APS	Certificate of Jack E. Davis, Chief Executive Officer, pursuant to Rule 13a-14(a) and Rule 15d-14(a) of the Securities Exchange Act, as amended
31.4	APS	Certificate of Donald E. Brandt, Chief Financial Officer, pursuant to Rule 13a-14(a) and Rule 15d-14(a) of the Securities Exchange Act, as amended
32.1	Pinnacle West	Certification of Chief Executive Officer and Chief Financial Officer, pursuant to 18 U.S.C. Section 1850, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002
32.2	APS	Certification of Chief Executive Officer and Chief Financial Officer, pursuant to 18 U.S.C. Section 1850, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002
99.1	Pinnacle West	Pinnacle West Risk Factors
99.2	APS	APS Risk Factors
99.3	Pinnacle West	Reconciliation of Operating Income to Gross Margin

[Table of Contents](#)

<i>Exhibit No.</i>	<i>Registrant(s)</i>	<i>Description</i>
99.4	APS	Reconciliation of Operating Income to Gross Margin
99.5	Pinnacle West	Purchase Agreement by and among Pinnacle West Energy Corporation and GenWest, L.L.C. and Nevada Power Company, dated June 21, 2005
99.6	APS	Amended and Restated Reimbursement Agreement among Arizona Public Service Company, The Banks party thereto and JPMorgan Chase Bank, N.A., as Administrative Agent and Issuing Bank, and Barclays Bank PLC, as Syndication Agent, dated as of May 19, 2005.

In addition, the Company hereby incorporates the following Exhibits pursuant to Exchange Act Rule 12b-32 and Regulation §229.10(d) by reference to the filings set forth below:

<i>Exhibit No.</i>	<i>Registrant(s)</i>	<i>Description</i>	<i>Previously Filed as Exhibit a</i>	<i>Date Effective</i>
3.1	Pinnacle West	Articles of Incorporation, restated as of July 29, 1988	19.1 to Pinnacle West's September 1988 Form 10-Q Report, File No. 1-8962	11-14-88
3.2	Pinnacle West	Pinnacle West Capital Corporation Bylaws, amended as of June 23, 2004	3.1 to Pinnacle West's June 30, 2004 Form 10-Q Report, File No. 1-8962	8-9-04
3.3	APS	Articles of Incorporation, restated as of May 25, 1988	4.2 to APS' Form S-3 Registration Nos. 33-33910 and 33-55248 by means of September 24, 1993 Form 8-K Report, File No. 1-4473	9-29-93
3.4	APS	Arizona Public Service Company Bylaws, amended as of June 23, 2004	3.1 to APS' June 30, 2004 Form 10-Q Report, File No. 1-4473	8-9-04

^a Reports filed under File Nos. 1-4473 and 1-8962 were filed in the office of the Securities and Exchange Commission located in Washington, D.C.

SIGNATURES

Pursuant to the requirements of the Securities Exchange Act of 1934, each registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

PINNACLE WEST CAPITAL CORPORATION
(Registrant)

Dated: August 9, 2005

By: /s/ Donald E. Brandt
Donald E. Brandt
Executive Vice President and Chief
Financial Officer
(Principal Financial Officer
and Officer Duly Authorized to sign this Report)

ARIZONA PUBLIC SERVICE COMPANY
(Registrant)

Dated: August 9, 2005

By: /s/ Donald E. Brandt
Donald E. Brandt
Executive Vice President and Chief
Financial Officer
(Principal Financial Officer
and Officer Duly Authorized to sign this Report)

EXHIBIT INDEX

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In addition, the Company hereby incorporates the following Exhibits pursuant to Exchange Act Rule 12b-32 and Regulation §229.10(d) by reference to the filings set forth below:

<i>Exhibit No.</i>	<i>Registrant(s)</i>	<i>Description</i>	<i>Previously Filed as Exhibit ^a</i>	<i>Date Effective</i>
3.1	Pinnacle West	Articles of Incorporation, restated as of July 29, 1988	19.1 to Pinnacle West's September 1988 Form 10-Q Report, File No. 1-8962	11-14-88
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^a Reports filed under File Nos. 1-4473 and 1-8962 were filed in the office of the Securities and Exchange Commission located in Washington, D.C.

PINNACLE WEST CAPITAL CORPORATION
COMPUTATION OF EARNINGS TO FIXED CHARGES
(\$000's)

	Six Months Ended June 30, 2005	2004	2003	Twelve Months Ended December 31, 2002	2001	2000
Earnings:						
Income From Continuing Operations	\$ 114,897	\$ 246,591	\$ 225,384	\$ 236,563	\$ 327,367	\$ 302,332
Income Taxes	73,685	136,142	102,202	152,145	213,535	194,200
Fixed Charges	111,010	214,803	225,041	219,178	211,958	202,804
Total Earnings	<u>\$ 299,592</u>	<u>\$ 597,536</u>	<u>\$ 552,627</u>	<u>\$ 607,886</u>	<u>\$ 752,860</u>	<u>\$ 699,336</u>
Fixed Charges:						
Interest Expense	\$ 96,042	\$ 183,527	\$ 193,973	\$ 187,039	\$ 175,822	\$ 166,447
Estimated Interest Portion of Annual Rents	14,968	31,276	31,068	32,139	36,136	36,357
Total Fixed Charges	<u>\$ 111,010</u>	<u>\$ 214,803</u>	<u>\$ 225,041</u>	<u>\$ 219,178</u>	<u>\$ 211,958</u>	<u>\$ 202,804</u>
Ratio of Earnings to Fixed Charges (rounded down)	<u>2.69</u>	<u>2.78</u>	<u>2.45</u>	<u>2.77</u>	<u>3.55</u>	<u>3.44</u>

ARIZONA PUBLIC SERVICE COMPANY
COMPUTATION OF EARNINGS TO FIXED CHARGES
(\$000's)

	Six Months Ended June 30, <u>2005</u>	<u>2004</u>	<u>2003</u>	Twelve Months Ended December 31, <u>2002</u>	<u>2001</u>	<u>2000</u>
Earnings:						
Income From Continuing Operations	\$ 91,043	\$ 199,627	\$ 180,937	\$ 199,343	\$ 280,688	\$ 306,594
Income Taxes	60,538	120,030	86,854	126,805	183,136	195,665
Fixed Charges	91,171	181,372	181,793	168,985	166,939	179,381
Total Earnings	<u>\$ 242,752</u>	<u>\$ 501,029</u>	<u>\$ 449,584</u>	<u>\$ 495,133</u>	<u>\$ 630,763</u>	<u>\$ 681,640</u>
Fixed Charges:						
Interest Charges	\$ 74,375	\$ 146,983	\$ 147,610	\$ 133,878	\$ 130,525	\$ 141,886
Amortization of Debt Discount	2,192	4,854	3,337	2,888	2,650	2,105
Estimated Interest Portion of Annual Rents	14,604	29,535	30,846	32,219	33,764	35,390
Total Fixed Charges	<u>\$ 91,171</u>	<u>\$ 181,372</u>	<u>\$ 181,793</u>	<u>\$ 168,985</u>	<u>\$ 166,939</u>	<u>\$ 179,381</u>
Ratio of Earnings to Fixed Charges (rounded down)	<u>2.66</u>	<u>2.76</u>	<u>2.47</u>	<u>2.93</u>	<u>3.77</u>	<u>3.79</u>

CERTIFICATION

I, William J. Post, certify that:

1. I have reviewed this Quarterly Report on Form 10-Q of Pinnacle West Capital Corporation;
 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)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) 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) designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
 - c) 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
 - d) 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 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: August 9, 2005.

/s/ William J. Post

William J. Post

Chairman and Chief Executive Officer

CERTIFICATION

I, Donald E. Brandt, certify that:

1. I have reviewed this Quarterly Report on Form 10-Q of Pinnacle West Capital Corporation;
 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)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) 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) designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
 - c) 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
 - d) 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 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: August 9, 2005.

/s/ Donald E. Brandt

Donald E. Brandt
Executive Vice President &
Chief Financial Officer

CERTIFICATION

I, Jack E. Davis, certify that:

1. I have reviewed this Quarterly Report on Form 10-Q of Arizona Public Service Company;
 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)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) 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) designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
 - c) 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
 - d) 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 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: August 9, 2005.

/s/ Jack E. Davis

Jack E. Davis

President and Chief Executive Officer

CERTIFICATION

I, Donald E. Brandt, certify that:

1. I have reviewed this Quarterly Report on Form 10-Q of Arizona Public Service Company;
 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)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) 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) designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
 - c) 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
 - d) 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 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: August 9, 2005.

/s/ Donald E. Brandt

Donald E. Brandt

Executive Vice President &

Chief Financial Officer

**CERTIFICATION
OF
CHIEF EXECUTIVE OFFICER
AND
CHIEF FINANCIAL OFFICER
PURSUANT TO 18 U.S.C. 1350,
AS ADOPTED PURSUANT TO
SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002**

I, William J. Post, certify, pursuant to 18 U.S.C. 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, that the Quarterly Report on Form 10-Q of Pinnacle West Capital Corporation for the fiscal quarter ended June 30, 2005, fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934 and that the information contained in such Quarterly Report on Form 10-Q fairly presents, in all material respects, the financial condition and results of operations of Pinnacle West Capital Corporation.

Date: August 9, 2005.

/s/ William J. Post

William J. Post

Chairman and Chief Executive Officer

I, Donald E. Brandt, certify, pursuant to 18 U.S.C. 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, that the Quarterly Report on Form 10-Q of Pinnacle West Capital Corporation for the fiscal quarter ended June 30, 2005 fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934 and that the information contained in such Quarterly Report on Form 10-Q fairly presents, in all material respects, the financial condition and results of operations of Pinnacle West Capital Corporation.

Date: August 9, 2005.

/s/ Donald E. Brandt

Donald E. Brandt

Executive Vice President and
Chief Financial Officer

**CERTIFICATION
OF
CHIEF EXECUTIVE OFFICER
AND
CHIEF FINANCIAL OFFICER
PURSUANT TO 18 U.S.C. 1350,
AS ADOPTED PURSUANT TO
SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002**

I, Jack E. Davis, certify, pursuant to 18 U.S.C. 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, that the Quarterly Report on Form 10-Q of Arizona Public Service Company for the fiscal quarter ended June 30, 2005 fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934 and that the information contained in such Quarterly Report on Form 10-Q fairly presents, in all material respects, the financial condition and results of operations of Arizona Public Service Company.

Date: August 9, 2005.

/s/ Jack E. Davis

Jack E. Davis

President and Chief Executive Officer

I, Donald E. Brandt, certify, pursuant to 18 U.S.C. 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, that the Quarterly Report on Form 10-Q of Arizona Public Service Company for the fiscal quarter ended June 30, 2005 fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934 and that the information contained in such Quarterly Report on Form 10-Q fairly presents, in all material respects, the financial condition and results of operations of Arizona Public Service Company.

Date: August 9, 2005.

/s/ Donald E. Brandt

Donald E. Brandt

Executive Vice President and
Chief Financial Officer

PINNACLE WEST RISK FACTORS**(Report on Form 10-Q for the fiscal quarter ended June 30, 2005)**

Set forth below and in other documents we file with the Securities and Exchange Commission are risks and uncertainties that could affect our financial results.

Deregulation or restructuring of the electric industry may result in increased competition, which could have a significant adverse impact on our business and our financial results.

In 1999, the Arizona Corporation Commission (the “ACC”) approved rules for the introduction of retail electric competition in Arizona. Retail competition could have a significant adverse financial impact on us due to an impairment of assets, a loss of retail customers, lower profit margins or increased costs of capital. Although some very limited retail competition existed in the service area of Arizona Public Service Company (“APS”) in 1999 and 2000, there are currently no active retail competitors offering unbundled energy or other utility services to APS’ customers. As a result, we cannot predict when, and the extent to which, additional competitors will re-enter APS’ service territory.

As a result of changes in federal law and regulatory policy, competition in the wholesale electricity market has greatly increased due to a greater participation by traditional electricity suppliers, non-utility generators, independent power producers, and wholesale power marketers and brokers. This increased competition could affect our load forecasts, plans for power supply and wholesale energy sales and related revenues. As a result of the changing regulatory environment and the relatively low barriers to entry, we expect wholesale competition to increase. As competition continues to increase, our financial position and results of operations could be adversely affected.

We are subject to complex government regulation that may have a negative impact on our business and our results of operations.

We are, directly and through our subsidiaries, subject to governmental regulation that may have a negative impact on our business and results of operations. We are a “holding company” within the meaning of the Public Utility Holding Company Act of 1935 (“PUHCA”); however, we are exempt from the provisions of PUHCA (except Section 9(a)(2) thereof) by virtue of our filing of an annual exemption statement with the Securities and Exchange Commission (the “SEC”).

APS is subject to comprehensive regulation by several federal, state and local regulatory agencies, which significantly influence its operating environment and may affect its ability to recover costs from utility customers. APS is required to have numerous permits, approvals and certificates from the agencies that regulate APS’ business. The FERC, the Nuclear Regulatory Commission (“NRC”), the Environmental Protection Agency (“EPA”), and the ACC regulate many aspects of our utility operations, including siting and construction of facilities, customer service and the rates that APS can charge customers. We believe the necessary permits, approvals and certificates have been obtained for APS’ existing operations. However, changes in regulations or the imposition of additional regulations could have an adverse impact on our results of operations. We are also unable to predict the impact on our business and operating results from pending or future regulatory activities of any of these agencies.

We are subject to numerous environmental laws and regulations that may increase our cost of operations, impact our business plans, or expose us to environmental liabilities.

We are subject to numerous environmental laws and regulations affecting many aspects of our present and future operations, including air emissions, water quality, wastewater discharges, solid waste, and hazardous waste. These laws and regulations can result in increased capital, operating, and other costs, particularly with regard to enforcement efforts focused on power plant emissions obligations. These laws and regulations generally require us to obtain and comply with a wide variety of environmental licenses, permits, inspections and other approvals. Both public officials and private individuals may seek to enforce applicable environmental laws and regulations. We cannot predict the outcome (financial or operational) of any related litigation that may arise.

In addition, we may be a responsible party for environmental clean up at sites identified by a regulatory body. We cannot predict with certainty the amount and timing of all future expenditures related to environmental matters

because of the difficulty of estimating clean-up costs. There is also uncertainty in quantifying liabilities under environmental laws that impose joint and several liability on all potentially responsible parties.

We cannot be sure that existing environmental regulations will not be revised or that new regulations seeking to protect the environment will not be adopted or become applicable to us. Revised or additional regulations that result in increased compliance costs or additional operating restrictions, particularly if those costs are not fully recoverable from APS' customers, could have a material adverse effect on our results of operations.

There are inherent risks in the operation of nuclear facilities, such as environmental, health and financial risks and the risk of terrorist attack.

Through APS, we have an ownership interest in and operate, on behalf of a group of owners, the Palo Verde Nuclear Generating Station ("Palo Verde"), which is the largest nuclear electric generating facility in the United States. Palo Verde is subject to environmental, health and financial risks such as the ability to dispose of spent nuclear fuel, the ability to maintain adequate reserves for decommissioning, potential liabilities arising out of the operation of these facilities, and the costs of securing the facilities against possible terrorist attacks and unscheduled outages due to equipment and other problems. We maintain nuclear decommissioning trust funds and external insurance coverage to minimize our financial exposure to some of these risks; however, it is possible that damages could exceed the amount of insurance coverage.

The NRC has broad authority under federal law to impose licensing and safety-related requirements for the operation of nuclear generation facilities. In the event of noncompliance, the NRC has the authority to impose fines or shut down a unit, or both, depending upon its assessment of the severity of the situation, until compliance is achieved. In addition, although we have no reason to anticipate a serious nuclear incident at Palo Verde, if an incident did occur, it could materially and adversely affect our results of operations or financial condition. A major incident at a nuclear facility anywhere in the world could cause the NRC to limit or prohibit the operation or licensing of any domestic nuclear unit.

The uncertain outcome regarding the creation of regional transmission organizations, or RTOs, may materially impact our operations, cash flows or financial position.

In a December 1999 order, the FERC established characteristics and functions that must be met by utilities in forming and operating RTOs. The characteristics for an acceptable RTO include independence from market participants, operational control over a region large enough to support efficient and nondiscriminatory markets and exclusive authority to maintain short-term reliability. Additionally, in a pending notice of proposed rulemaking, the FERC is considering implementing a standard market design for wholesale markets. On October 16, 2001, APS and other owners of electric transmission lines in the southwestern U.S. filed with the FERC a request for a declaratory order confirming that their proposal to form WestConnect RTO, LLC would satisfy the FERC's requirements for the formation of an RTO. On October 10, 2002, the FERC issued an order finding that the WestConnect proposal, if modified to address specified issues, could meet the FERC's RTO requirements and provide the basic framework for a standard market design for the southwestern U.S. Since that time, APS has been evaluating a phased approach to RTO implementation in the desert Southwest. APS is currently participating with other entities in the southwestern U.S. in a cost/benefit analysis of implementing the WestConnect RTO, the results of which are expected to be completed in 2005.

If APS ultimately joins an RTO, APS could incur increased transmission-related costs and receive reduced transmission service revenues; APS may be required to expand its transmission system according to decisions made by the RTO rather than its internal planning process; and APS may experience other impacts on its operations, cash flows or financial position that will not be quantifiable until the final tariffs and other material terms of the RTO are known.

Recent events in the energy markets that are beyond our control may have negative impacts on our business.

As a result of the energy crisis in California during the summer of 2001, the recent volatility of natural gas prices in North America, the filing of bankruptcy by the Enron Corporation, and investigations by governmental authorities into energy trading activities, companies generally in the regulated and unregulated utility businesses have been under an increased amount of public and regulatory scrutiny. The capital markets and rating agencies also have increased their level of scrutiny. We believe that we are in material compliance with all applicable laws, but it

is difficult or impossible to predict or control what effect these or related issues may have on our business or our access to the capital markets.

Our results of operations can be adversely affected by milder weather.

Weather conditions directly influence the demand for electricity and affect the price of energy commodities. Electric power demand is generally a seasonal business. In Arizona, demand for power peaks during the hot summer months, with market prices also peaking at that time. As a result, our overall operating results fluctuate substantially on a seasonal basis. In addition, we have historically sold less power, and consequently earned less income, when weather conditions are milder. As a result, unusually mild weather could diminish our results of operations and harm our financial condition.

Our cash flow largely depends on the performance of our subsidiaries.

We conduct our operations primarily through subsidiaries. Substantially all of our consolidated assets are held by such subsidiaries. Accordingly, our cash flow is dependent upon the earnings and cash flows of these subsidiaries and their distributions to us. The subsidiaries are separate and distinct legal entities and have no obligation to make distributions to us.

The debt agreements of some of our subsidiaries may restrict their ability to pay dividends, make distributions or otherwise transfer funds to us. An ACC financing order requires APS to indefinitely maintain a common equity ratio of at least 40% and does not allow APS to pay common dividends if the payment would reduce its common equity below that threshold. As defined in the ACC financing order approving the arrangement, common equity ratio is common equity divided by common equity plus long-term debt, including current maturities of long-term debt. At June 30, 2005, APS' common equity ratio, as defined, was approximately 48%.

Our debt securities are structurally subordinated to the debt securities and other obligations of our subsidiaries.

Because we are structured as a holding company, all existing and future debt and other liabilities of our subsidiaries will be effectively senior in right of payment to our debt securities. None of the indentures under which we or our subsidiaries may issue debt securities limits our ability or the ability of our subsidiaries to incur additional debt in the future. The assets and cash flows of our subsidiaries will be available, in the first instance, to service their own debt and other obligations. Our ability to have the benefit of their assets and cash flows, particularly in the case of any insolvency or financial distress affecting our subsidiaries, would arise only through our equity ownership interests in our subsidiaries and only after their creditors have been satisfied.

If we are not able to access capital at competitive rates, our ability to implement our financial strategy will be adversely affected.

We rely on access to short-term money markets, longer-term capital markets and the bank markets as a significant source of liquidity and for capital requirements not satisfied by the cash flow from our operations. We believe that we will maintain sufficient access to these financial markets based upon current credit ratings. However, certain market disruptions or a downgrade of our credit ratings may increase our cost of borrowing or adversely affect our ability to access one or more financial markets. Such disruptions could include:

- an economic downturn;
- capital market conditions generally;
- the bankruptcy of an unrelated energy company;
- increased market prices for electricity and gas;
- terrorist attacks or threatened attacks on our facilities or those of unrelated energy companies; or
- the overall health of the utility industry.

Changes in economic conditions could result in higher interest rates, which would increase our interest expense on our debt and reduce funds available to us for our current plans. Additionally, an increase in our leverage could adversely affect us by:

- increasing the cost of future debt financing;
- increasing our vulnerability to adverse economic and industry conditions;
- requiring us to dedicate a substantial portion of our cash flow from operations to payments on our debt, which would reduce funds available to us for operations, future business opportunities or other purposes; and
- placing us at a competitive disadvantage compared to our competitors that have less debt.

A significant reduction in our credit ratings could materially and adversely affect our business, financial condition and results of operations.

We cannot be sure that any of our current ratings will remain in effect for any given period of time or that a rating will not be lowered or withdrawn entirely by a rating agency if, in its judgment, circumstances in the future so warrant. Any downgrade could increase our borrowing costs, which would diminish our financial results. We would likely be required to pay a higher interest rate in future financings, and our potential pool of investors and funding sources could decrease. In addition, borrowing costs under certain of our existing credit facilities depend on our credit ratings. A downgrade could also require us to provide additional support in the form of letters of credit or cash or other collateral to various counterparties. If our short-term ratings were to be lowered, it could limit our access to the commercial paper market. We note that the ratings from rating agencies are not recommendations to buy, sell or hold our securities and that each rating should be evaluated independently of any other rating.

The use of derivative contracts in the normal course of our business and changing interest rates and market conditions could result in financial losses that negatively impact our results of operations.

Our operations include managing market risks related to commodity prices and, subject to specified risk parameters, engaging in marketing and trading activities intended to profit from market price movements. We are exposed to the impact of market fluctuations in the price and transportation costs of electricity, natural gas, coal, and emissions allowances. We have established procedures to manage risks associated with these market fluctuations by utilizing various commodity derivatives, including exchange-traded futures and options and over-the-counter forwards, options, and swaps. As part of our overall risk management program, we enter into derivative transactions to hedge purchases and sales of electricity, fuels, and emissions allowances and credits. The changes in market value of such contracts have a high correlation to price changes in the hedged commodity.

We are exposed to losses in the event of nonperformance or nonpayment by counterparties. We use a risk management process to assess and monitor the financial exposure of all counterparties. Despite the fact that the majority of trading counterparties are rated as investment grade by the rating agencies, there is still a possibility that one or more of these companies could default, resulting in a material adverse impact on our earnings for a given period.

Changing interest rates will affect interest paid on variable-rate debt and interest earned by our pension plan and nuclear decommissioning trust funds. Our policy is to manage interest rates through the use of a combination of fixed-rate and floating-rate debt. The pension plan is also impacted by the discount rate, which is the interest rate used to discount future pension obligations. Continuation of recent decreases in the discount rate would result in increases in pension costs, cash contributions, and charges to other comprehensive income. The pension plan and nuclear decommissioning trust funds also have risks associated with changing market values of equity investments. A significant portion of the pension costs and all of the nuclear decommissioning costs are recovered in regulated electricity prices.

Actual results could differ from estimates used to prepare our financial statements.

In preparing our financial statements in accordance with accounting principles generally accepted in the United States of America, management must often make estimates and assumptions that affect the reported amounts of assets, liabilities, revenues, expenses and related disclosures at the date of the financial statements and during the reporting period. Some of those judgments can be subjective and complex, and actual results could differ from those estimates. We consider the following accounting policies to be our most critical because of the uncertainties, judgments and complexities of the underlying accounting standards and operations involved.

- **Regulatory Accounting** — Regulatory accounting allows for the actions of regulators, such as the ACC and the FERC, to be reflected in our financial statements. Their actions may cause us to capitalize costs that would otherwise be included as an expense in the current period by unregulated companies. If future recovery of costs ceases to be probable, the assets would be written off as a charge in current period earnings. We had approximately \$174 million of regulatory assets on our Condensed Consolidated Balance Sheets at June 30, 2005.
- **Pensions and Other Postretirement Benefit Accounting** — Changes in our actuarial assumptions used in calculating our pension and other postretirement benefit liability and expense can have a significant impact on our earnings and financial position. The most relevant actuarial assumptions are the discount rate used to measure our liability and net periodic cost, the expected long-term rate of return on plan assets used to estimate earnings on invested funds over the long-term, and the assumed healthcare cost trend rates. We review these assumptions on an annual basis and adjust them as necessary.
- **Derivative Accounting** — Derivative accounting requires evaluation of rules that are complex and subject to varying interpretations. Our evaluation of these rules, as they apply to our contracts, will determine whether we use accrual accounting (for contracts designated as normal) or fair value (mark-to-market) accounting. Mark-to-market accounting requires that changes in the fair value are recognized periodically in income unless certain hedge criteria are met. For fair value hedges, the gain or loss on the derivative as well as the offsetting loss or gain on the hedged item associated with the hedged risk are recognized in earnings. For cash flow hedges, changes in the fair value of the derivative are recognized in common stock equity (as a component of other comprehensive income (loss)).

The market price of our common stock may be volatile.

The market price of our common stock could be subject to significant fluctuations in response to factors such as the following, some of which are beyond our control:

- variations in our quarterly operating results;
- operating results that vary from the expectations of management, securities analysts and investors;
- changes in expectations as to our future financial performance, including financial estimates by securities analysts and investors;
- developments generally affecting industries in which we operate, particularly the energy distribution and energy generation industries;
- announcements by us or our competitors of significant contracts, acquisitions, joint marketing relationships, joint ventures or capital commitments;
- announcements by third parties of significant claims or proceedings against us;
- favorable or adverse regulatory developments;
- our dividend policy;
- future sales of our equity or equity-linked securities; and
- general domestic and international economic conditions.

In addition, the stock market in general has experienced volatility that has often been unrelated to the operating performance of a particular company. These broad market fluctuations may adversely affect the market price of our common stock.

Our common stock price could be affected because a substantial number of our shares could be available for sale in the future.

Sales in the public market of a substantial number of shares of common stock could depress the market price of the common stock and could impair our ability to raise capital through the sale of additional equity securities. Because of the number of shares of our common stock that we are authorized to issue under our articles of incorporation, a substantial number of shares of our common stock could be available for future sale.

We may enter into credit and other agreements from time to time that restrict our ability to pay dividends.

Payment of dividends on our common stock may be restricted by credit and other agreements entered into by us from time to time. At June 30, 2005, there were no material restrictions on our ability to pay dividends under any such agreement.

Certain provisions of our articles of incorporation and bylaws and of Arizona law make it more difficult for shareholders to change the composition of our board and may discourage takeover attempts that could be beneficial to us and our shareholders.

Certain provisions of our articles of incorporation and bylaws and of Arizona law make it more difficult for shareholders to change the composition of our board and may discourage unsolicited attempts to acquire us, which could preclude our shareholders from receiving a change of control premium. These provisions include the following:

- provisions of our bylaws and Arizona law that restrict our ability to engage in a wide range of “business combination” transactions with an “interested shareholder” (generally, any person who owns 10% or more of our outstanding voting power or any of our affiliates or associates) or any affiliate or associate of an interested shareholder, unless specific conditions are met;
- anti-greenmail provisions of Arizona law and our bylaws that prohibit us from purchasing shares of our voting stock from beneficial owners of more than 5% of our outstanding shares unless specified conditions are satisfied;
- provisions of our bylaws and Arizona law that provide that shareholder action may be taken only at an annual or special meeting or by unanimous written consent, and provisions of our bylaws that provide that a special meeting of shareholders may only be called by a majority of our Board of Directors, the Chairman of our Board of Directors, or our President;
- advance notice procedures for nominating candidates to our Board of Directors or presenting matters at shareholder meetings;
- provisions of our articles and bylaws that provide for a staggered Board of Directors;
- provisions of our bylaws that provide that shareholders may only remove a director with or without cause if the votes cast in favor of such removal exceed the votes cast against such removal (with special requirements, based on cumulative voting rights, if less than the entire board is to be removed); and
- the ability of our Board of Directors to issue additional shares of common stock and shares of preferred stock and to determine the price and, with respect to preferred stock, the other terms, including preferences and voting rights, of those shares without shareholder approval.

In addition, we have adopted a shareholder rights plan that may have the effect of discouraging unsolicited takeover proposals, including takeover proposals that could result in a premium over the market price of our common stock.

While these provisions have the effect of encouraging persons seeking to acquire control of us to negotiate with our Board of Directors, they could enable the board to hinder or frustrate a transaction that some, or a majority, of our shareholders might believe to be in their best interests and, in that case, may prevent or discourage attempts to remove and replace incumbent directors.

APS RISK FACTORS**(Report on Form 10-Q for the fiscal quarter ended June 30, 2005)**

Set forth below and in other documents we file with the Securities and Exchange Commission are risks and uncertainties that could affect our financial results.

Deregulation or restructuring of the electric industry may result in increased competition, which could have a significant adverse impact on our business and our financial results.

In 1999, the Arizona Corporation Commission (the “ACC”) approved rules for the introduction of retail electric competition in Arizona. Retail competition could have a significant adverse financial impact on us due to an impairment of assets, a loss of retail customers, lower profit margins or increased costs of capital. Although some very limited retail competition existed in our service area in 1999 and 2000, there are currently no active retail competitors offering unbundled energy or other utility services to our customers. As a result, we cannot predict when, and the extent to which, additional competitors will re-enter our service territory.

As a result of changes in federal law and regulatory policy, competition in the wholesale electricity market has greatly increased due to a greater participation by traditional electricity suppliers, non-utility generators, independent power producers, and wholesale power marketers and brokers. This increased competition could affect our load forecasts, plans for power supply and wholesale energy sales and related revenues. As a result of the changing regulatory environment and the relatively low barriers to entry, we expect wholesale competition to increase. As competition continues to increase, our financial position and results of operations could be adversely affected.

We are subject to complex government regulation that may have a negative impact on our business and our results of operations.

We are subject to governmental regulation that may have a negative impact on our business and results of operations. We are a “subsidiary company” of a “holding company” within the meaning of the Public Utility Holding Company Act of 1935 (“PUHCA”); however, we are exempt from the provisions of PUHCA (except Section 9(a)(2) thereof) by virtue of the filing of an annual exemption statement with the Securities and Exchange Commission (the “SEC”) by our parent company, Pinnacle West Capital Corporation (“Pinnacle West”).

We are subject to comprehensive regulation by several federal, state and local regulatory agencies, which significantly influence our operating environment and may affect our ability to recover costs from utility customers. We are required to have numerous permits, approvals and certificates from the agencies that regulate our business. The FERC, the Nuclear Regulatory Commission (“NRC”), the Environmental Protection Agency (“EPA”), and the ACC regulate many aspects of our utility operations, including siting and construction of facilities, customer service and the rates that we can charge customers. We believe the necessary permits, approvals and certificates have been obtained for our existing operations. However, changes in regulations or the imposition of additional regulations could have an adverse impact on our results of operations. We are also unable to predict the impact on our business and operating results from pending or future regulatory activities of any of these agencies.

We are subject to numerous environmental laws and regulations that may increase our cost of operations, impact our business plans, or expose us to environmental liabilities.

We are subject to numerous environmental laws and regulations affecting many aspects of our present and future operations, including air emissions, water quality, wastewater discharges, solid waste, and hazardous waste. These laws and regulations can result in increased capital, operating, and other costs, particularly with regard to enforcement efforts focused on power plant emissions obligations. These laws and regulations generally require us to obtain and comply with a wide variety of environmental licenses, permits, inspections and other approvals. Both public officials and private individuals may seek to enforce applicable environmental laws and regulations. We cannot predict the outcome (financial or operational) of any related litigation that may arise.

In addition, we may be a responsible party for environmental clean up at sites identified by a regulatory body. We cannot predict with certainty the amount and timing of all future expenditures related to environmental matters because of the difficulty of estimating clean-up costs. There is also uncertainty in quantifying liabilities under environmental laws that impose joint and several liability on all potentially responsible parties.

We cannot be sure that existing environmental regulations will not be revised or that new regulations seeking to protect the environment will not be adopted or become applicable to us. Revised or additional regulations that result in increased compliance costs or additional operating restrictions, particularly if those costs are not fully recoverable from our customers, could have a material adverse effect on our results of operations.

There are inherent risks in the operation of nuclear facilities, such as environmental, health and financial risks and the risk of terrorist attack.

We have an ownership interest in and operate, on behalf of a group of owners, the Palo Verde Nuclear Generating Station (“Palo Verde”), which is the largest nuclear electric generating facility in the United States. Palo Verde is subject to environmental, health and financial risks such as the ability to dispose of spent nuclear fuel, the ability to maintain adequate reserves for decommissioning, potential liabilities arising out of the operation of these facilities, and the costs of securing the facilities against possible terrorist attacks and unscheduled outages due to equipment and other problems. We maintain nuclear decommissioning trust funds and external insurance coverage to minimize our financial exposure to some of these risks; however, it is possible that damages could exceed the amount of insurance coverage.

The NRC has broad authority under federal law to impose licensing and safety-related requirements for the operation of nuclear generation facilities. In the event of noncompliance, the NRC has the authority to impose fines or shut down a unit, or both, depending upon its assessment of the severity of the situation, until compliance is achieved. In addition, although we have no reason to anticipate a serious nuclear incident at Palo Verde, if an incident did occur, it could materially and adversely affect our results of operations or financial condition. A major incident at a nuclear facility anywhere in the world could cause the NRC to limit or prohibit the operation or licensing of any domestic nuclear unit.

The uncertain outcome regarding the creation of regional transmission organizations, or RTOs, may materially impact our operations, cash flows or financial position.

In a December 1999 order, the FERC established characteristics and functions that must be met by utilities in forming and operating RTOs. The characteristics for an acceptable RTO include independence from market participants, operational control over a region large enough to support efficient and nondiscriminatory markets and exclusive authority to maintain short-term reliability. Additionally, in a pending notice of proposed rulemaking, the FERC is considering implementing a standard market design for wholesale markets. On October 16, 2001, we and other owners of electric transmission lines in the southwestern U.S. filed with the FERC a request for a declaratory order confirming that our proposal to form WestConnect RTO, LLC would satisfy the FERC’s requirements for the formation of an RTO. On October 10, 2002, the FERC issued an order finding that the WestConnect proposal, if modified to address specified issues, could meet the FERC’s RTO requirements and provide the basic framework for a standard market design for the southwestern U.S. Since that time, we have been evaluating a phased approach to RTO implementation in the desert Southwest. We are currently participating with other entities in the southwestern U.S. in a cost/benefit analysis of implementing the WestConnect RTO, the results of which are expected to be completed in 2005.

If we ultimately join an RTO, we could incur increased transmission-related costs and receive reduced transmission service revenues; we may be required to expand our transmission system according to decisions made by the RTO rather than our internal planning process; and we may experience other impacts on our operations, cash flows or financial position that will not be quantifiable until the final tariffs and other material terms of the RTO are known.

Recent events in the energy markets that are beyond our control may have negative impacts on our business.

As a result of the energy crisis in California during the summer of 2001, the recent volatility of natural gas prices in North America, the filing of bankruptcy by the Enron Corporation, and investigations by governmental authorities into energy trading activities, companies generally in the regulated and unregulated utility businesses have been under an increased amount of public and regulatory scrutiny. The capital markets and rating agencies also have increased their level of scrutiny. We believe that we are in material compliance with all applicable laws, but it is difficult or impossible to predict or control what effect these or related issues may have on our business or our access to the capital markets.

Our results of operations can be adversely affected by milder weather.

Weather conditions directly influence the demand for electricity and affect the price of energy commodities. Electric power demand is generally a seasonal business. In Arizona, demand for power peaks during the hot summer months, with market prices also peaking at that time. As a result, our overall operating results fluctuate substantially on a seasonal basis. In addition, we have historically sold less power, and consequently earned less income, when weather conditions are milder. As a result, unusually mild weather could diminish our results of operations and harm our financial condition.

If we are not able to access capital at competitive rates, our ability to implement our financial strategy will be adversely affected.

We rely on access to short-term money markets, longer-term capital markets and the bank markets as a significant source of liquidity and for capital requirements not satisfied by the cash flow from our operations. We believe that we will maintain sufficient access to these financial markets based upon current credit ratings. However, certain market disruptions or a downgrade of our credit ratings may increase our cost of borrowing or adversely affect our ability to access one or more financial markets. Such disruptions could include:

- an economic downturn;
- capital market conditions generally;
- the bankruptcy of an unrelated energy company;
- increased market prices for electricity and gas;
- terrorist attacks or threatened attacks on our facilities or those of unrelated energy companies; or
- the overall health of the utility industry.

Changes in economic conditions could result in higher interest rates, which would increase our interest expense on our debt and reduce funds available to us for our current plans. Additionally, an increase in our leverage could adversely affect us by:

- increasing the cost of future debt financing;
- increasing our vulnerability to adverse economic and industry conditions;
- requiring us to dedicate a substantial portion of our cash flow from operations to payments on our debt, which would reduce funds available to us for operations, future business opportunities or other purposes; and
- placing us at a competitive disadvantage compared to our competitors that have less debt.

A significant reduction in our credit ratings could materially and adversely affect our business, financial condition and results of operations.

We cannot be sure that any of our current ratings will remain in effect for any given period of time or that a rating will not be lowered or withdrawn entirely by a rating agency if, in its judgment, circumstances in the future so warrant. Any downgrade could increase our borrowing costs, which would diminish our financial results. We would likely be required to pay a higher interest rate in future financings, and our potential pool of investors and funding sources could decrease. In addition, borrowing costs under certain of our existing credit facilities depend on our credit ratings. A downgrade could also require us to provide additional support in the form of letters of credit or cash or other collateral to various counterparties. If our short-term ratings were to be lowered, it could limit our access to the commercial paper market. We note that the ratings from rating agencies are not recommendations to buy, sell or hold our securities and that each rating should be evaluated independently of any other rating.

The use of derivative contracts in the normal course of our business and changing interest rates and market conditions could result in financial losses that negatively impact our results of operations.

Our operations include managing market risks related to commodity prices and, subject to specified risk parameters, engaging in marketing and trading activities intended to profit from market price movements. We are exposed to the impact of market fluctuations in the price and transportation costs of electricity, natural gas, coal, and emissions allowances. We have established procedures to manage risks associated with these market fluctuations by

utilizing various commodity derivatives, including exchange-traded futures and options and over-the-counter forwards, options, and swaps. As part of our overall risk management program, we enter into derivative transactions to hedge purchases and sales of electricity, fuels, and emissions allowances and credits. The changes in market value of such contracts have a high correlation to price changes in the hedged commodity.

We are exposed to losses in the event of nonperformance or nonpayment by counterparties. We use a risk management process to assess and monitor the financial exposure of all counterparties. Despite the fact that the majority of trading counterparties are rated as investment grade by the rating agencies, there is still a possibility that one or more of these companies could default, resulting in a material adverse impact on our earnings for a given period.

Changing interest rates will affect interest paid on variable-rate debt and interest earned by our pension plan and nuclear decommissioning trust funds. Our policy is to manage interest rates through the use of a combination of fixed-rate and floating-rate debt. The pension plan is also impacted by the discount rate, which is the interest rate used to discount future pension obligations. Continuation of recent decreases in the discount rate would result in increases in pension costs, cash contributions, and charges to other comprehensive income. The pension plan and nuclear decommissioning trust funds also have risks associated with changing market values of equity investments. A significant portion of the pension costs and all of the nuclear decommissioning costs are recovered in regulated electricity prices.

Actual results could differ from estimates used to prepare our financial statements.

In preparing our financial statements in accordance with accounting principles generally accepted in the United States of America, management must often make estimates and assumptions that affect the reported amounts of assets, liabilities, revenues, expenses and related disclosures at the date of the financial statements and during the reporting period. Some of those judgments can be subjective and complex, and actual results could differ from those estimates. We consider the following accounting policies to be our most critical because of the uncertainties, judgments and complexities of the underlying accounting standards and operations involved.

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- **Pensions and Other Postretirement Benefit Accounting** — Changes in our actuarial assumptions used in calculating our pension and other postretirement benefit liability and expense can have a significant impact on our earnings and financial position. The most relevant actuarial assumptions are the discount rate used to measure our liability and net periodic cost, the expected long-term rate of return on plan assets used to estimate earnings on invested funds over the long-term, and the assumed healthcare cost trend rates. We review these assumptions on an annual basis and adjust them as necessary.
- **Derivative Accounting** — Derivative accounting requires evaluation of rules that are complex and subject to varying interpretations. Our evaluation of these rules, as they apply to our contracts, will determine whether we use accrual accounting (for contracts designated as normal) or fair value (mark-to-market) accounting. Mark-to-market accounting requires that changes in the fair value are recognized periodically in income unless certain hedge criteria are met. For fair value hedges, the gain or loss on the derivative as well as the offsetting loss or gain on the hedged item associated with the hedged risk are recognized in earnings. For cash flow hedges, changes in the fair value of the derivative are recognized in common stock equity (as a component of other comprehensive income (loss)).

PINNACLE WEST CAPITAL CORPORATION
NON-GAAP MEASURE RECONCILIATION — OPERATING INCOME (GAAP MEASURE) TO GROSS MARGIN (NON-GAAP MEASURE)
(in thousands)

	THREE MONTHS ENDED JUNE 30,		Pretax Increase (Decrease)	After Tax Increase (Decrease)
	2005	2004		
RECONCILIATION OF REGULATED ELECTRICITY SEGMENT GROSS MARGIN				
Operating Income (closest GAAP measure)	\$ 178,627	\$ 123,167	\$ 55,460	\$ 33,703
Plus:				
Operations and maintenance	153,097	138,595	14,502	8,813
Real estate segment operations	68,593	62,217	6,376	3,875
Depreciation and amortization	85,142	102,012	(16,870)	(10,252)
Taxes other than income taxes	34,638	32,308	2,330	1,416
Other expenses	17,556	7,575	9,981	6,065
Marketing and trading segment purchased power and fuel	57,593	88,067	(30,474)	(18,519)
Less:				
Real estate segment revenues	84,753	66,084	18,669	11,345
Other revenues	20,259	9,414	10,845	6,591
Marketing and trading segment revenues	71,172	110,156	(38,984)	(23,691)
Regulated electricity segment gross margin	\$ 419,062	\$ 368,287	\$ 50,775	\$ 30,856
RECONCILIATION OF MARKETING AND TRADING SEGMENT GROSS MARGIN				
Operating Income (closest GAAP measure)	\$ 178,627	\$ 123,167	\$ 55,460	\$ 33,703
Plus:				
Operations and maintenance	153,097	138,595	14,502	8,813
Real estate segment operations	68,593	62,217	6,376	3,875
Depreciation and amortization	85,142	102,012	(16,870)	(10,252)
Taxes other than income taxes	34,638	32,308	2,330	1,416
Other expenses	17,556	7,575	9,981	6,065
Regulated electricity segment purchased power and fuel	160,590	151,642	8,948	5,438
Less:				
Real estate segment revenues	84,753	66,084	18,669	11,345
Other revenues	20,259	9,414	10,845	6,591
Regulated electricity segment revenues	579,652	519,929	59,723	36,294
Marketing and trading segment gross margin	\$ 13,579	\$ 22,089	\$ (8,510)	\$ (5,172)

PINNACLE WEST CAPITAL CORPORATION
NON-GAAP MEASURE RECONCILIATION — OPERATING INCOME (GAAP MEASURE) TO GROSS MARGIN (NON-GAAP MEASURE)
(in thousands)

	SIX MONTHS ENDED JUNE 30,		Pretax Increase (Decrease)	After Tax Increase (Decrease)
	2005	2004		
RECONCILIATION OF REGULATED ELECTRICITY SEGMENT GROSS MARGIN				
Operating Income (closest GAAP measure)	\$ 270,981	\$ 207,445	\$ 63,536	\$ 38,611
Plus:				
Operations and maintenance	308,181	275,981	32,200	19,568
Real estate segment operations	125,069	109,510	15,559	9,455
Depreciation and amortization	176,535	203,115	(26,580)	(16,153)
Taxes other than income taxes	69,203	62,638	6,565	3,990
Other expenses	25,930	16,325	9,605	5,837
Marketing and trading segment purchased power and fuel	128,402	155,832	(27,430)	(16,669)
Less:				
Real estate segment revenues	156,809	116,547	40,262	24,467
Other revenues	30,394	20,319	10,075	6,123
Marketing and trading segment revenues	160,429	198,840	(38,411)	(23,342)
Regulated electricity segment gross margin	\$ 756,669	\$ 695,140	\$ 61,529	\$ 37,391
RECONCILIATION OF MARKETING AND TRADING SEGMENT GROSS MARGIN				
Operating Income (closest GAAP measure)	\$ 270,981	\$ 207,445	\$ 63,536	\$ 38,611
Plus:				
Operations and maintenance	308,181	275,981	32,200	19,568
Real estate segment operations	125,069	109,510	15,559	9,455
Depreciation and amortization	176,535	203,115	(26,580)	(16,153)
Taxes other than income taxes	69,203	62,638	6,565	3,990
Other expenses	25,930	16,325	9,605	5,837
Regulated electricity segment purchased power and fuel	239,013	240,253	(1,240)	(754)
Less:				
Real estate segment revenues	156,809	116,547	40,262	24,467
Other revenues	30,394	20,319	10,075	6,123
Regulated electricity segment revenues	995,682	935,393	60,289	36,638
Marketing and trading segment gross margin	\$ 32,027	\$ 43,008	\$ (10,981)	\$ (6,674)

ARIZONA PUBLIC SERVICE COMPANY
NON-GAAP MEASURE RECONCILIATION — OPERATING INCOME (GAAP MEASURE) TO GROSS MARGIN (NON-GAAP MEASURE)
(in thousands)

	THREE MONTHS ENDED JUNE 30,		Pretax Increase (Decrease)	After Tax Increase (Decrease)
	2005	2004		
RECONCILIATION OF GROSS MARGIN				
Operating Income (closest GAAP measure)	\$ 95,321	\$ 83,604	\$ 11,717	\$ 7,104
Plus:				
Operations and maintenance	138,314	126,871	11,443	6,938
Depreciation and amortization	76,808	88,385	(11,577)	(7,019)
Income taxes	41,772	32,371	9,401	5,700
Other taxes	31,322	29,874	1,448	878
Gross margin	<u>\$ 383,537</u>	<u>\$ 361,105</u>	<u>\$ 22,432</u>	<u>\$ 13,601</u>

ARIZONA PUBLIC SERVICE COMPANY

NON-GAAP MEASURE RECONCILIATION — OPERATING INCOME (GAAP MEASURE) TO GROSS MARGIN (NON-GAAP MEASURE)
(in thousands)

	SIX MONTHS ENDED JUNE 30,		Pretax Increase (Decrease)	After Tax Increase (Decrease)
	2005	2004		
RECONCILIATION OF GROSS MARGIN				
Operating Income (closest GAAP measure)	\$ 154,064	\$ 150,654	\$ 3,410	\$ 2,067
Plus:				
Operations and maintenance	280,608	252,783	27,825	16,870
Depreciation and amortization	159,022	177,233	(18,211)	(11,041)
Income taxes	58,152	49,733	8,419	5,104
Other taxes	62,767	57,454	5,313	3,221
Gross margin	<u>\$ 714,613</u>	<u>\$ 687,857</u>	<u>\$ 26,756</u>	<u>\$ 16,221</u>

PURCHASE AGREEMENT

BY AND AMONG

PINNACLE WEST CAPITAL CORPORATION

PINNACLE WEST ENERGY CORPORATION

AND

GENWEST, LLC,

as Sellers,

AND

NEVADA POWER COMPANY,

as Purchaser

JUNE 21, 2005

SILVERHAWK POWER PLANT

Clark County, Nevada

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Exhibit I	Form of Assignment Agreement
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Exhibit K	Form of Interim PPA

PURCHASE AGREEMENT
Silverhawk Power Plant

THIS PURCHASE AGREEMENT is made and entered into effective as of June 21, 2005 (the "Effective Date"), by and among PINNACLE WEST CAPITAL CORPORATION, an Arizona corporation ("PWCC"), PINNACLE WEST ENERGY CORPORATION, an Arizona corporation ("PWEC"), GENWEST, LLC, a Delaware limited liability company ("GenWest"), and NEVADA POWER COMPANY, an electric utility organized under the laws of the State of Nevada ("Purchaser"). PWCC, PWEC and GenWest are also each referred to herein individually as a "Seller" and collectively as the "Sellers". PWCC, PWEC and GenWest, on the one hand, and Purchaser, on the other hand, are also each referred to herein as a "Party" and collectively as the "Parties".

RECITALS

A. GenWest owns an undivided 75% interest in an operating natural gas-fueled combined-cycle generation plant located at the APEX Industrial Park, approximately 25 miles northeast of Las Vegas, Nevada, known as the Silverhawk Power Plant. SNWA owns an undivided 25% interest in the Silverhawk Power Plant.

B. PWEC is a wholly owned subsidiary of PWCC. PWEC owns all the outstanding membership interests in GenWest.

C. Purchaser desires to purchase substantially all the assets of GenWest.

D. The Parties have determined to set forth in this Agreement the terms and conditions of their agreements regarding the foregoing.

AGREEMENTS

For and in consideration of the Recitals set forth above, the respective covenants and agreements of the Parties herein set forth, and other good and valuable consideration, the receipt and sufficiency of which are hereby acknowledged by the Parties, the Parties, intending to be legally bound, do hereby agree as follows:

ARTICLE I

DEFINITIONS; USAGE

Section 1.1 Definitions. Unless the context shall otherwise require, capitalized terms used in this Agreement shall have the meanings assigned to them in this Section 1.1.

"2003 Settlement Agreement" means the Settlement Agreement, dated as of January 31, 2003, among Purchaser, SCE, Duke Energy Moapa, LLC, GenWest, Las Vegas Cogeneration II, Mirant Las Vegas, LLC and Reliant Energy Bighorn, LLC, by which they resolved issues set for hearing in FERC Docket No. ER02-2344-000 and certain SCE-related issues set for hearing in FERC Docket Nos. ER02-1741-000 and ER02-1742-000, 25% of the rights and obligations of GenWest under which were assigned to and assumed by SNWA pursuant to the Bill of Sale.

"2005 Settlement Agreement" means the settlement agreement filed with FERC on May 23, 2005 among Purchaser, Purchaser's Chuck Lenzie Generating Station, Valley Electric Association, Inc., SCE, GenWest, Las Vegas Cogeneration II, Mirant Las Vegas, LLC, Reliant Energy Wholesale Generation, LLC and SNWA, which attached the Amended and Restated 2003 Settlement Agreement and is intended to resolve the issues set for hearing in FERC Docket Nos. ER02-1741-000 and ER02-1742-000 that were not resolved in the 2003 Settlement Agreement, among other issues.

"Acquisition Proposal" shall mean any proposal or offer made by any Person other than Purchaser to acquire all or a substantial part of the Project, the assets owned solely by GenWest, any equity interest in GenWest, or any interest of PWCC or PWEC in the Assumed Agreements.

"Additional Pre-Closing Permitted Mechanics Liens" means any mechanics', carriers', workers', repairers' and other similar Liens, other than liens described in item (vii) of the definition of Permitted Liens, arising or incurred in the ordinary course of business, and not in violation of the Co-Tenancy Agreement or the O&M Agreement relating to obligations which are not yet due and payable or the validity of which are being contested in good faith by appropriate proceedings, which in all cases shall be removed prior to Closing without any cost to or liability of Purchaser or adverse effect on the Purchased Assets.

"Adjustment Amount" has the meaning given to it in Section 2.2.4(a) of this Agreement.

"Adjustment Statement" has the meaning given to it in Section 2.2.4(a) of this Agreement.

"Affiliate" of any Person means any other Person directly or indirectly Controlling, directly or indirectly Controlled by or under direct or indirect common Control with such Person.

"Agency Agreement" means the Agency Agreement, dated July 1, 2004, among SNWA, GenWest and PWEC.

"Agreement" means this Purchase Agreement by and between Sellers and Purchaser.

"Amended and Restated 2003 Settlement Agreement" means the amendment and restatement of the 2003 Settlement Agreement, entered into among Purchaser, Purchaser's Chuck Lenzie Generating Station, SCE, GenWest, Las Vegas Cogeneration II, Mirant Las Vegas, LLC, Reliant Energy Wholesale Generation, LLC and SNWA, which is attached to the 2005 Settlement Agreement and was filed with FERC on May 23, 2005.

"APS" means Arizona Public Service Company.

"APS Switchyard Agreement" means the Agreement for Engineering, Procurement and Construction for Facility Switchyard (Agreement No. 760200017), dated December 16, 2002, between GenWest and APS, 25% of the rights and obligations under which were assigned to and assumed by SNWA pursuant to the Bill of Sale, as amended by Change Order No. 1 dated December 12, 2003 and Change Order No. 2 dated June 30, 2004.

"Assignment Agreement" has the meaning given to it in Section 2.4.1(a)(iv) of this Agreement.

"Assumed Agreements" means the Assumed Joint Facility Agreements, the Assumed GenWest Agreements, the Assumed PWCC Agreements, and the Assumed PWEC Agreements.

"Assumed GenWest Agreements" means those GenWest Agreements which are listed on Schedule I, Part B attached hereto.

"Assumed Joint Facility Agreements" means those Joint Facility Agreements which are listed on Schedule I, Part A attached hereto and the Post-Effective Date Assumed Joint Facility Agreements.

"Assumed PWCC Agreements" means the Transmission Services Agreement and the Reliant Agreement.

"Assumed PWEC Agreements" means the TSA 100 Assignment Agreement, the TSA 101 Assignment Agreement, the O&M Agreement, and the Agency Agreement.

"Bill of Sale" means the Bill of Sale, Assignment and Assumption Agreement, dated May 17, 2004, between GenWest and SNWA.

"BLM" means the Bureau of Land Management.

"Books and Records" means all drafts of the Co-Tenancy Agreement, the O&M Agreement and the Well Development Agreement that can be reasonably and practically provided, books, records, files, documents, instruments, papers, correspondence that can be reasonably and practically provided, journals, deeds, licenses, supplier, contractor and subcontractor lists, supplier design interface information, computer files and programs, other than PWCC's or APS' enterprise-wide computer programs, retrieval programs, the information listed on Part D of Schedule II of this Agreement to the extent in existence, environmental studies, environmental reports, construction reports, annual operating plans, monthly operating reports, operating logs, operations and maintenance records, purchase orders, safety and maintenance manuals, incident reports, injury reports, engineering design plans, blue prints and as-built plans, records drawings, drawings, specifications, test reports, quality documentation and reports, hazardous waste disposal records, procedures and similar items, in each case, in all formats in which they are available, including electronic; provided, however, that any such data currently contained in computer systems shall be provided in electronic format as either fixed form or character delimited data and shall include record descriptions, to the extent the computer systems of Purchaser and the Sellers are compatible in allowing such data provision, in each case excluding documents subject to attorney-client privilege.

"Business Day" means any day except Saturday, Sunday or a weekday that banks in Las Vegas, Nevada, Phoenix, Arizona or New York, New York are closed.

"Closing" has the meaning given to it in Section 2.4 of this Agreement.

"Closing Date" has the meaning given to it in Section 2.4 of this Agreement.

"Code" means the Internal Revenue Code of 1986, as amended.

"Construction and Equipment Supply Contracts" means (i) the Equipment Supply Agreement (Contract No. 750200136), dated February 16, 2001, between GenWest and Siemens Westinghouse Power Corporation for Combustion Turbine Equipment, as amended by Change Orders Nos. 1 through 8, 25% of the rights and obligations under which were assigned to and assumed by SNWA pursuant to the Bill of Sale; (ii) the Equipment Supply Agreement (Contract No. 760200010), dated March 21, 2002, between GenWest and Alstom, as amended by Change Orders Nos. 1 through 3 (the "Alstom Agreement"), 25% of the rights and obligations under which were assigned to and assumed by SNWA pursuant to the Bill of Sale, (iii) Contract (Contract No. 750200434), dated as of October 12, 2001, between GenWest and General Electric Company, as amended by Change Orders Numbers 1 through 6, 25% of the rights and obligations under which were assigned to and assumed by SNWA pursuant to the Bill of Sale, (iv) Agreement for Engineering, Procurement and Construction of the Silverhawk Facility (Contract No. 760200009), dated as of June 11, 2002, between GenWest and LG Constructors, Inc., as amended by Contract Amendment No. 1, dated March 13, 2003, Contract Amendment No. 2, dated March 17, 2003, Contract Amendment No. 3, dated April 30, 2004, and by Change Orders Nos. 1 through 12, 25% of the rights and obligations under which were assigned to and assumed by SNWA pursuant to the Bill of Sale, (v) the APS Switchyard Agreement, and (vi) Silverhawk Combined Cycle Equipment Supply Agreement (Contract No. 760200013), dated March 7, 2002, between GenWest and Hamon Cooling Towers, Inc., as amended by Change Order No. 1 and the Settlement Agreement dated May 12, 2004, 25% of the rights and obligations under which were assigned to and assumed by SNWA pursuant to the Bill of Sale.

"Contemplated Assumed Agreement Amendments" means the contemplated amendments to certain Assumed Agreements, which are listed on Section 1.1.1(a) of Sellers' Disclosure Schedule (i) substantially in the form provided to Purchaser prior to the Effective Date, or (ii) otherwise within the relevant scope described in Section 1.1.1(a) of Sellers' Disclosure Schedule and, in the case of this clause (ii), will otherwise have no adverse effect on the rights or obligations of Purchaser under such Assumed Agreements or on the other Purchased Assets.

"Continued Employee Books and Records" means the Books and Records related to Project Employees that are to be hired by Purchaser following the Closing, regarding skill and development training; seniority histories; disciplinary histories; salary and benefit information; Occupational Safety and Health Administration reports and records; and active medical restriction forms.

"Control" of any Person means the possession, directly or indirectly, of the power either to (a) vote fifty percent (50%) or more of the securities or interests having ordinary voting power for the election of directors (or other comparable controlling body) of such Person or (b) direct or

cause the direction of management or policies of such Person, whether through the ownership of voting securities or interests, by contract or otherwise, excluding in each case, any secured lender of such Person.

"Co-Tenancy Agreement" means the Silverhawk Power Plant Co-Tenancy Agreement, dated January 17, 2002, by and between GenWest and SNWA.

"Deed" has the meaning given to it in Section 2.4.1(b)(v) of this Agreement.

"Default Rate" has the meaning given to it in Section 12.2 of this Agreement.

"Designated Assumed Agreements" means each of the following Assumed Agreements: the Co-Tenancy Agreement, the Kern River Contracts, the O&M Agreement, the Reliant Agreement, the Water Supply Agreement, the Mirant Master Agreement, and the Real Property Documents.

"Dry Lake Documents" shall mean the Contemplated Assumed Agreement Amendments in respect of the Real Property Purchase Agreement and the Well Development Agreement.

"Easements" shall mean (i) that certain Grant of Easement from HDL 8, LLC to GenWest for the access road, recorded on July 23, 2002 in Book 20020723, Instrument No. 02463 of the Official Records of Clark County, Nevada, (ii) that certain Grant of Easement from GDL 7, LLC to GenWest for the access road, recorded on July 24, 2002 in Book 20020724, Instrument No. 03124 of the Official Records of Clark County, Nevada, and (iii) that certain Grant of Easement from Mirant Las Vegas to GenWest for the access road, recorded on July 31, 2002 in Book 20020731, Instrument No. 01299 of the Official Records of Clark County, Nevada, 25% of the rights and obligations under each of which was assigned to SNWA pursuant to the SNWA Deed.

"Effective Date" has the meaning given to it in the preamble of this Agreement.

"Environmental Condition" means the presence or Release to the environment of Hazardous Materials, including any migration of Hazardous Materials through air, soil or water.

"Environmental Law" means (i) the Comprehensive Environmental Response, Compensation and Liability Act, 42 U.S.C. Section 9601 et seq., (ii) the Resource Conservation and Recovery Act, 42 U.S.C. Section 6901 et seq., (iii) the Federal Water Pollution Control Act, 33 U.S.C. Section 1251 et seq., (iv) the Clean Air Act, 42 U.S.C. Section 7401 et seq., (v) the Hazardous Materials Transportation Authorization Act of 1994, 49 U.S.C. Section 5101 et seq., (vi) the Occupational Safety and Health Act, 29 U.S.C. Section 651 et seq., (vii) the Toxic Substances Control Act, 15 U.S.C. Sections 2601 through 2629, (viii) the Oil Pollution Act, 33 U.S.C. Section 2701 et seq., (ix) the Emergency Planning and Community Right-to-Know Act, 42 U.S.C. Section 11001 et seq., (x) the Safe Drinking Water Act, 42 U.S.C. Sections 300f through 300j, and (xi) and all other Laws of any Governmental Authority having jurisdiction over the assets in question addressing pollution or protection of human health, safety or the environment.

"ERISA" means the Employee Retirement Income Security Act of 1974, as amended.

"ERISA Affiliate" means any entity that, together with any Seller would be deemed a single employer within the meaning of Code Section 414 or ERISA Section 4001(b).

"Estimated Adjustment" has the meaning given to it in Section 2.2.3 of this Agreement.

"Estimated Closing Statement" has the meaning given to it in Section 2.2.3 of this Agreement.

"Estimated Hot Gas Path Parts Expenditures Amount" has the meaning given to it in Section 2.2.3.

"Estimated Post-April RRSU Payment Amount" has the meaning given to it in Section 2.2.3 of this Agreement.

"Estimated Post-September Capital Expenditures Amount" has the meaning given to it in Section 2.2.3 of this Agreement.

"Estimated Purchase Price" has the meaning given to it in Section 2.2.2 of this Agreement.

"Estimated Stores and Inventory Amount" has the meaning given to it in Section 2.2.3 of this Agreement.

"Excluded Assets" has the meaning given to it in Section 2.1.3 of this Agreement.

"Excluded Liabilities" has the meaning given to it in Section 2.1.4 of this Agreement.

"Existing Letters of Credit" mean (i) Letter of Credit No. NZS507752 issued by Wells Fargo Bank N.A. for benefit of GenWest, on behalf of CH2M Hill Companies, Ltd., in the amount of \$500,000, 25% of the rights and obligations under which were assigned to and assumed by SNWA pursuant to the Bill of Sale, and (ii) Letter of Credit No. SM206052W dated December 11, 2003, issued by Wachovia Bank National Association, in the amount of \$2,479,236, in favor of GenWest, on behalf of Alstom Power Inc., 25% of the rights and obligations under which were assigned to and assumed by SNWA pursuant to the Bill of Sale.

"Facility" or "Silverhawk Power Plant" means the Silverhawk Power Plant consisting of an operating natural gas-fired, combined cycle, electric generation plant, and the pipeline interconnections, electrical interconnections and all other related equipment and other associated property located within the Site as described in Schedule II, Part B, Item 1.

"Facility Agreements" means the GenWest Agreements and the Joint Facility Agreements.

"Facility Permits" has the meaning given to it in Section 3.1.15(a) of this Agreement.

"Fault Current Upgrade MOUs" means (i) the Revised MOU I, and (ii) the Regional Required System Upgrades Western Memorandum of Understanding, dated November 3, 2003, between Purchaser and GenWest, as amended by the Memorandum of Understanding between

Purchaser and GenWest, dated March 24, 2005, attached to the Western Settlement Agreement and approved by FERC on June 1, 2005 (also known as MOU II).

"Federal Power Act" means the Federal Power Act of 1935.

"FERC" means the Federal Energy Regulatory Commission.

"FERC Approval" means the final approval to be issued by FERC under Section 203 of the Federal Power Act with respect to the transactions contemplated hereby, provided that the terms of the approval imposing obligations on a Party or in respect of its assets shall be satisfactory to such Party in its sole discretion.

"Financing" means financing which makes available funds to Purchaser in connection with the acquisition of the Purchased Assets, on terms substantially similar to those currently available in the capital markets to Purchaser on the Effective Date and in a principal amount equal to the Purchase Price, and otherwise on terms satisfactory to Purchaser, in its sole discretion.

"GAAP" means generally accepted accounting principles in the United States of America applied on a consistent basis.

"GenWest" has the meaning given to it in the preamble to this Agreement.

"GenWest Agreements" means any agreements, leases, licenses, indentures, security agreements, deeds of trust or other contracts entered into by GenWest for its own benefit, and not in common with or for the benefit of SNWA, including in connection with GenWest's Interest in the Project, excluding any agreements between GenWest and any of its Affiliates other than the O&M Agreement and excluding any agreements that are fully performed except for customary surviving provisions, including those relating to confidentiality, indemnification, dispute resolution, audit rights, and limitation on liabilities, in each case that do not have an adverse effect on the Purchased Assets.

"Governmental Authority" means any federal, state or local governmental entity, authority or agency, court, tribunal, regulatory commission or other body, whether legislative, judicial or executive (or a combination or permutation thereof), provided; however, that SNWA shall not be considered a Governmental Authority for purposes of this definition.

"Hamon Consent" shall mean the consent obtained from Hamon Cooling Towers, Inc., consenting to the assignment of the Silverhawk Combined Cycle Equipment Supply Agreement (Contract No. 760200013), dated March 7, 2002, between GenWest and Hamon Cooling Towers, Inc., 25% of the rights and obligations under which were assigned to and assumed by SNWA pursuant to the Bill of Sale, as amended by Change Order No. 1 and the Settlement Agreement dated May 12, 2004, in the form attached hereto as Exhibit A or otherwise in form and substance reasonably satisfactory to Purchaser and Sellers.

"Hazardous Materials" means (i) any substance, emission or material including asbestos, now or hereafter defined as, listed as or specified in a Law as a "regulated substance," "hazardous substance," "toxic substance," "pesticide," "hazardous waste," "hazardous material"

or any similar or like classification or categorization under any Law including by reason of ignitability, corrosivity, reactivity, carcinogenicity or reproductive or other toxicity of any kind, (ii) any products or substances containing petroleum, asbestos, or polychlorinated biphenyls or (iii) any substance, emission or material determined to be hazardous or harmful by a Governmental Authority with appropriate jurisdiction.

"HMH Letter" means the Letter from HMH, Inc. dated May 13, 2004, with the following subject: "GBS from GENWEST, LLC to SOUTHERN NEVADA WATER AUTHORITY AT APEX."

"Hot Gas Path Parts Adjustment Amount" has the meaning given to it in Section 2.2.4(a) of this Agreement.

"Hot Gas Path Parts Expenditures Amount" means 75% of any expenditures for the purchase of parts required for the hot gas path parts inspection scheduled to take place during the spring and fall outages in 2007 under the Long Term Maintenance Agreement.

"HSR Act" means the Hart-Scott-Rodino Antitrust Improvements Act of 1976.

"Indemnified Party" has the meaning given in Section 7.3.1 of this Agreement.

"Indemnifying Party" has the meaning given in Section 7.3.1 of this Agreement.

"Independent Accounting Firm" means such nationally recognized, independent accounting firm as is mutually appointed by Purchaser and Sellers for purposes of this Agreement.

"Intellectual Property" means (i) patents and industrial designs (including any continuations, divisionals, continuations-in-part, renewals, reissues, and applications for any of the foregoing), (ii) copyrights (including any registrations and applications for any of the foregoing), (iii) software (whether in source code or object code form), (iv) information technology and information systems, or (v) technology, trade secrets or other confidential information, know-how, proprietary processes, formulae, algorithms, models, or methodologies, and licenses or other rights to the foregoing.

"Interconnection and Operation Agreement" means the Interconnection and Operation Agreement, Third Revised Service Agreement No. 02-00107 under Sierra Pacific Resources Operating Companies' Open Access Transmission Tariff, dated January 15, 2004 (effective from May 30, 2002), between GenWest and Purchaser, 25% of the rights and obligations under which were assigned to and assumed by SNWA pursuant to the Bill of Sale.

"Interconnection Contracts" means (i) the Interconnection and Operation Agreement, (ii) the Fault Current Upgrade MOUs, (iii) the Settlement Agreements, and (iv) the SCE Tax Agreement.

"Interest" has the meaning assigned to it in the Co-Tenancy Agreement.

"Interim PPA" means the Power Purchase Agreement, dated as of the date hereof, between GenWest and Purchaser.

"Joint Facility Agreements" means any agreements, leases, licenses, indentures, security agreements, deeds of trust or other contracts relating to the development, construction, ownership, operation or maintenance of the Facility entered into by GenWest or an Affiliate of GenWest, in each case for the joint benefit of GenWest and SNWA, excluding any agreements that are fully performed except for customary surviving provisions, including those relating to confidentiality, indemnification, dispute resolution, audit rights, and limitation on liabilities, in each case that do not have an adverse effect on the Purchased Assets.

"Kern River Consent" shall mean the consent obtained from Kern River Gas Transmission Company consenting to the assignment of the Kern River Contracts, in the form attached hereto as Exhibit B or otherwise in form and substance reasonably satisfactory to Purchaser and Sellers.

"Kern River Contracts" shall mean: (i) Power Supply Agreement, dated November 20, 2003, between Kern River Gas Transmission Company and GenWest, 25% of the rights and obligations under which were assigned to and assumed by SNWA pursuant to the Bill of Sale, (ii) the Facilities Agreement, dated March 13, 2003, between Kern River Gas Transmission Company and GenWest, as amended by Revised Exhibit C, which was assigned to PWEC, as Operating Agent on June 6, 2005, and (iii) the Signal Letter Agreement, dated May 8, 2003, between Kern River Gas Transmission Company and GenWest, 25% of the rights and obligations under which were assigned to and assumed by SNWA pursuant to the Bill of Sale.

"Las Vegas Valley Water District Consent" shall mean the consent obtained from Las Vegas Valley Water District consenting to the assignment of the Water Supply Agreement, in the form attached hereto as Exhibit C or otherwise in form and substance reasonably satisfactory to Purchaser and Sellers.

"Law" means any statute, law, treaty, rule, code, common law, ordinance, regulation, permit, interpretation, certificate or order of any Governmental Authority, or any judgment, decision, decree, injunction, writ, order or like action of any court, arbitrator or other Governmental Authority including each Environmental Law.

"Liability" means any indebtedness, obligations and other liabilities of a Person (whether absolute, accrued, contingent, fixed or otherwise, or whether due or to become due).

"Lien" shall mean any mortgage, pledge, deed of trust, hypothecation, assignment, deposit arrangement, charge, security interest, encumbrance, defect in title, lien (statutory or other), or preference, priority or other security agreement of any kind or nature whatsoever, including without limitation any conditional sale or other title retention agreement, any financing lease having substantially the same effect as any of the foregoing, or the filing of any financing statement or similar instrument under the Uniform Commercial Code as in effect in any relevant jurisdiction or comparable Law of any jurisdiction, domestic or foreign.

"Long Term Maintenance Agreement" or "LTMA" means the Program Parts, Shop Repairs and Scheduled Outage Services Contract for a 2X1 501F Combined Cycle Project for the

Silverhawk Power Plant Project (Contract No. 760200022), dated as of August 8, 2000, between PWEC, as Operating Agent, and Siemens Westinghouse Power Corporation.

"Loss" means any damage, fine, penalty, deficiency, Liability, loss or expense (including interest, court costs, reasonable fees of attorneys, accountants and other experts or other reasonable expenses of litigation or other proceedings or of any claim, default or assessment).

"Lube Oil Storage Facility" means the facility to be constructed for the storage of lube oil pursuant to the Engineering, Procurement and Construction Agreement for Construction of Pre-Engineered Steel Buildings (Agreement No. 760200205), dated December 2, 2004, between Gillard Construction, Inc. and PWEC, as Operating Agent.

"Lugo Capacitor Work" has the meaning given to it in Section 2.5.4(c).

"Master Declaration" means Declaration of Covenants, Conditions and Restrictions for APEX Industrial Park, dated April 6, 2001, and recorded on April 10, 2001, in Book 20010410 as Document No. 01425 of Official Records of Clark County, Nevada, as amended by the Second Amendment to the Declaration of Covenants and Restrictions for APEX Industrial Park, recorded on July 9, 2002, in Book 20020709 as Document No. 00078 of Official Records of Clark County, Nevada.

"Material Adverse Effect" means a material adverse effect on (i) the Facility or the Purchased Assets or the operation or condition thereof, (ii) the ability of Sellers to perform their obligations under this Agreement or any of the other Transaction Agreements or (iii) the validity or enforceability of this Agreement or any of the other Transaction Agreements, or the rights or remedies of Purchaser hereunder or thereunder, provided, however, that the term Material Adverse Effect shall not include (x) any change resulting from changes in general international or national economic, financial or market conditions, or (y) any effect having a disproportionate impact on the Facility compared to other generating facilities in Purchaser's control area, to the extent resulting from the voluntary action of Purchaser relating to the transmission of power from the Facility.

"Materials and Equipment" means the Non-Shared Materials and Equipment and the Shared Materials and Equipment.

"Mirant Back-Up Well Arrangements" shall mean the Contemplated Assumed Agreement Amendment in respect of the Mirant Master Agreement.

"Mirant Consent" shall mean the consent obtained from Mirant Las Vegas, LLC consenting to the assignment of the Mirant Master Agreement, in the form attached hereto as Exhibit D or otherwise in form and substance reasonably satisfactory to Purchaser and Sellers.

"Mirant Master Agreement" means the Master Project Development and Operating Agreement, dated September 26, 2001, as amended on March 19, 2003, between GenWest and Mirant Las Vegas, LLC (Contract No. 750200436), as supplemented by Supplement Nos. 1 through 7, 25% of the rights and obligations under which was assigned to and assumed by SNWA pursuant to the Bill of Sale.

"Moenkopi Capacitor Work" has the meaning given to it in Section 2.5.4(b).

"New Warehouse" means the warehouse being constructed at the Site pursuant to the Engineering, Procurement and Construction Agreement for Construction of Pre-Engineered Steel Buildings (Agreement No. 760200205), dated December 2, 2004, between Gillard Construction, Inc. and PWEC, as Operating Agent.

"Non-Shared Assets" means the Non-Shared Materials and Equipment, Non-Shared Books and Records, Continued Employee Books and Records (to the extent they may be provided to Purchaser in accordance with Law), Assumed GenWest Agreements, Assumed PWCC Agreements, Assumed PWEC Agreements, Non-Shared Intellectual Property, and all third-party warranties and related assignments and other assets owned separately by GenWest and not in common with or for the benefit of SNWA, whether or not located on the Real Property.

"Non-Shared Books and Records" means Books and Records owned separately by GenWest, and not in common with or for the benefit of SNWA, in connection with GenWest's Interest in the Project, or by PWEC in connection with its role as Operating Agent under the Co-Tenancy Agreement, excluding any such Non-Shared Books and Records constituting or relating solely to Excluded Assets; provided, however, that if such Non-Shared Books and Records contain information related to the Purchased Assets and Excluded Assets, the portion relating to the Excluded Assets may be redacted.

"Non-Shared Intellectual Property" means Intellectual Property owned separately by GenWest and not in common with or for the benefit of SNWA, in connection with GenWest's Interest in the Project.

"Non-Shared Materials and Equipment" shall include the equipment, machinery, apparatus, furniture, computer hardware, vehicles, Stores and Inventory, tools, dies, construction in progress, and other tangible personal property, including such additional items of tangible personal property as acquired prior to the Closing Date, owned separately by GenWest and not in common with or for the benefit of SNWA, in connection with GenWest's Interest in the Project, including the Non-Shared Materials and Equipment listed in Schedule II, Part A.

"O&M Agreement" means the Facility Operating and Maintenance Agreement, dated as of April 18, 2002, among PWEC, as Operating Agent, and GenWest and SNWA as Participants in the Silverhawk Power Plant.

"Objectionable Survey Matters" has the meaning given to it in Section 4.1(g) of this Agreement.

"Objectionable Title Matters" has the meaning given to it in Section 4.1(g) of this Agreement.

"Operating Agent" has the meaning given to it in the Co-Tenancy Agreement.

"Other Transfer Taxes" has the meaning given to it in Section 8.2 of this Agreement.

"Overlap Period" has the meaning given to it in Section 8.4 of this Agreement.

"Overlap Period Taxes" has the meaning given to it in Section 8.4 of this Agreement.

"Participant" has the meaning given to it in the Co-Tenancy Agreement.

"Party" or "Parties" has the meaning given to it in the preamble to this Agreement.

"Permits" means permits, licenses, approvals, certificates, letter rulings, orders, decrees, judgments, writs, injunctions or similar actions of any Governmental Authority.

"Permitted Liens" means (i) those exceptions to title to the Purchased Assets set forth in Section 1.1.1(b) of the Sellers' Disclosure Schedule, (ii) zoning, entitlement, conservation restriction and other land use and environmental regulations by any Governmental Authority, (iii) Liens for Taxes not yet delinquent, (iv) items 3 through 25, and items 27 through 28 set forth in Schedule B of that certain Title Report dated as of June 2, 2005, Order Number 05-02-1673-CLB 2nd Amendment, of Nevada Title Company, (v) Liens created under Section 3.6, Section 3.8.1, Section 3.8.2, Section 10.2, Section 11.3, and Section 14.2(h) of the Co-Tenancy Agreement, (vi) any Lien expressly applying only to SNWA's interest in the Project, (vii) mechanics', carriers', workers', repairers' and other similar Liens arising or incurred under Assumed Agreements in the ordinary course of business and not in violation of the Co-Tenancy Agreement or the O&M Agreement relating to obligations (x) which are not yet due and payable or (y) which do not exceed \$500,000 in the aggregate and the validity of which is being contested in good faith by appropriate proceedings, and (viii) prior to Closing only, Additional Pre-Closing Permitted Mechanics Liens.

"Person" means any individual, corporation, partnership, joint venture, association, joint stock company, trust, limited liability company, unincorporated organization, Governmental Authority or any other form of entity.

"Post-April RRSU Payment Amount" means amounts of payments by GenWest pursuant to the Fault Current Upgrade MOUs beginning on May 1, 2005 and ending on the Closing Date, less (a) any refunds received by GenWest in respect of such payments prior to Closing, and (b) any amounts paid by GenWest beginning on May 1, 2005 and ending on the Closing Date attributable to SNWA's Interest.

"Post-Effective Date Assumed Joint Facility Agreements" has the meaning given to it in Section 4.11(a) of this Agreement.

"Post-Effective Date Permits" has the meaning given to it in Section 4.11(a) of this Agreement.

"Post-September Capital Expenditures Adjustment Amount" has the meaning given to it in Section 2.2.4(a) of this Agreement.

"Post-September Capital Expenditures Amount" means 75% of the aggregate amount of all funds expended on the following capital expenditures for the Project, beginning on October 1, 2005 and ending on the Closing Date: (a) capital expenditures made in the ordinary course of

business, pursuant to the Co-Tenancy Agreement, and not exceeding \$500,000 in the aggregate, (b) unscheduled capital expenditures made with the prior written consent of Purchaser, and (c) capital expenditures made at Purchaser's request, but excluding in each case any expenditures for construction of the New Warehouse or the Lube Oil Storage Facility, expenditures for Stores and Inventory, Hot Gas Path Parts Expenditures and such capital expenditures included in payments made by Purchaser under the Interim PPA.

"Pre-Closing Books and Records" has the meaning given to it in Section 2.5.2 of this Agreement.

"Pre-Closing Taxes" has the meaning given to it in Section 8.4 of this Agreement.

"Pre-Closing Tax Period" shall mean any taxable period ending on or before the Closing Date, or with respect to any taxable period that begins on or before the Closing Date and ends after the Closing Date, the portion of such taxable period ending on the Closing Date.

"Project" means the Facility and all Real Property, Shared Materials and Equipment, Shared Books and Records, Assumed Joint Facility Agreements, Transferred Permits, Shared Intellectual Property, and all third-party warranties and related assignments and other assets owned jointly by GenWest and SNWA or by either of GenWest or SNWA, in each case for their joint benefit, whether or not located on the Real Property.

"Project Employee Books and Records" means the Books and Records related to Project Employees regarding skill and development training; seniority histories, disciplinary histories, salary and benefit information, Occupational Safety and Health Administration reports and records, and active medical restriction forms.

"Project Employees" means individuals employed by PWEC at the Facility.

"Property Taxes" has the meaning given to it in Section 8.3 of this Agreement.

"PUCN" means the Public Utilities Commission of Nevada.

"PUCN Approval" means the final order to be issued by PUCN approving (i) Purchaser's acquisition of the Purchased Assets on terms consistent with this Agreement, (ii) the Interim PPA in the form executed by Purchaser and GenWest, (iii) the financing of the Purchased Assets, and (iv) any long-term firm gas transportation arrangements and electric transmission and related upgrades required in connection with such acquisition, in each case on terms satisfactory to Purchaser, in its sole discretion.

"Purchase Price" has the meaning given to it in Section 2.2.1 of this Agreement.

"Purchased Assets" has the meaning given to it in Section 2.1.1 of this Agreement.

"Purchaser" has the meaning given to it in the preamble of this Agreement.

"Purchaser Consent Representative" means the person appointed by Purchaser and notified to Sellers with appropriate contact information for the purpose of giving consents and receiving notices required pursuant to Section 4.2(f) of this Agreement.

"Purchaser Indemnified Party" has the meaning given to it in Section 7.1 of this Agreement.

"Purchaser's Disclosure Schedule" means the schedule delivered to Sellers by Purchaser herewith and dated as of the Effective Date, containing all lists, descriptions, exceptions and other information and materials as are required to be included therein by Purchaser pursuant to this Agreement, attached hereto as Schedule VII.

"Purchaser's Knowledge" means the actual knowledge of the Persons listed on Section 1.1.1(c) of the Purchaser's Disclosure Schedule; provided, however, each such Person shall be deemed to have knowledge of a matter of which such Person has received written notice.

"Purchaser's RRSU Refund Portion" has the meaning given to it in Section 2.5.4.

"PWCC" has the meaning given to it in the preamble of this Agreement.

"PWEC" has the meaning given to it in the preamble of this Agreement.

"Real Property" means the Site (including all buildings, structures and other improvements located thereon) and the Easements.

"Real Property Documents" means (i) the Real Property Purchase Agreement, (ii) the Easements, (iii) the Well Development Agreement, (iv) the Master Declaration, (v) Grant of Easement from GenWest in favor of Kern River Gas Transmission Company, for right of way easement, recorded December 20, 2002, in Book 20021220 as Document No. 01148 of Official Records of Clark County, Nevada, and (vi) the Grant of Easement from GenWest to Nevada Power Company and Central Telephone Company, for electrical and communication facilities, recorded September 25, 2003, in Book 20030925 as Document No. 00111 of Official Records of Clark County, Nevada.

"Real Property Purchase Agreement" means the Real Property Purchase Agreement, dated August 23, 2001, between GDL 7, LLC and GenWest for the purchase of the real property comprising the Site, 25% of the rights and obligations under which were assigned to and assumed by SNWA pursuant to the Bill of Sale.

"Real Property Transfer Taxes" has the meaning given to it in Section 8.2 of this Agreement.

"Related Person" means (i) with respect to Sellers and Purchaser, their respective Affiliates, and the employees, officers, directors, agents, representatives, licensees and invitees of Sellers, Purchaser and their respective Affiliates, and (ii) with respect to Purchaser, the employees, officers, directors, agents, representatives, licensees and invitees of its lenders, advisors and subcontractors.

"Release" shall mean any release, spill, emission, discharge, leaking, pumping, injection, deposit, disposal, discharge, dispersal, leaching or migration into the indoor or outdoor environment (including, without limitation, ambient air, surface water, groundwater, and surface or subsurface strata) or into or out of any property, including the movement of Hazardous Materials through or in air, soil, surface water, groundwater or property.

"Reliant Agreement" means the Agreement Regarding Exchange and Assignment of Transmission Services Agreements, dated August 26, 2002, between PWEC and Reliant Energy Services, Inc., which was assigned to PWCC pursuant to the Assignment and Assumption Agreement between PWEC and PWCC dated April 9, 2003.

"Reliant Consent" shall mean the consent obtained from Reliant Energy Services, Inc. consenting to the assignment of the Reliant Agreement, in the form attached hereto as Exhibit E or otherwise in form and substance reasonably satisfactory to Purchaser and Sellers.

"Remediation" means actions undertaken to address a Release of Hazardous Materials to the environment, including the following activities: (i) monitoring, investigation, assessment, treatment, cleanup, containment, removal, mitigation, response or restoration work, (ii) obtaining any Permits, consents, approvals or authorizations of any Governmental Authority necessary to conduct any such activity, (iii) preparing and implementing any plans or studies for any such activity, (iv) obtaining a written notice from a Governmental Authority that no material additional work is required by such Governmental Authority, (v) the use, implementation, application, installation, operation or maintenance of remedial technologies applied to the surface or subsurface soils, excavation and treatment or disposal of soils at off-site locations, systems for long-term treatment of surface water or groundwater, engineering controls or institutional controls, and (vi) any other activities reasonably determined to be necessary or appropriate or required under Environmental Laws to address a Release of Hazardous Materials.

"Required Consents" shall mean the following: the SNWA Consent, the Kern River Consent, the Las Vegas Valley Water District Consent, the Siemens Consent, the SCE Consent, the Reliant Consent, the Mirant Consent, the Hamon Consent, and any other consents required pursuant to Section 4.11(a) of this Agreement.

"Restrictions Declaration" means Use Restrictions Declaration dated as of July 8, 2002, between GDL 7, LLC and GenWest, as recorded on July 9, 2002, in Book 20020709 as Document No. 00079 of Official Records of Clark County, Nevada.

"Retained Information" has the meaning given to it in Section 2.5.2(b) of this Agreement.

"Revised MOU I" means the Revised RRSU Memorandum of Understanding between Purchaser and GenWest filed as Attachment B to the 2003 Settlement Agreement ("MOU I"), as amended by the revised memorandum of understanding between Purchaser and GenWest entered into pursuant to the 2005 Settlement Agreement and the Amended and Restated 2003 Settlement Agreement, conforming MOU I with the revisions agreed to in the 2005 Settlement Agreement and the Amended and Restated 2003 Settlement Agreement.

"RRSU" means Regional Required System Upgrades.

"RRSU Adjustment Amount" has the meaning given to it in Section 2.2.4(a) of this Agreement.

"SCE" means Southern California Edison Company.

"SCE Consent" shall mean the consent obtained from SCE consenting to the assignment of the Settlement Agreements, excluding the Western Settlement Agreement, and the SCE Tax Agreement in the form attached hereto as Exhibit F, or otherwise in form and substance reasonably satisfactory to Purchaser and Sellers.

"SCE RRSU Refund" means any service credits and cash refunds provided by SCE with respect to the payments made under the Revised MOU I and SCE Tax Agreement relating to the Silverhawk Power Plant, pursuant to paragraphs 26 through 33 of the 2003 Settlement Agreement and the Amended and Restated 2003 Settlement Agreement.

"SCE Tax Agreement" means the Tax Agreement, dated effective January 31, 2003, among GenWest, SCE and Purchaser, 25% of the rights and obligations under which were assigned to and assumed by SNWA pursuant to the Bill of Sale, as such is modified by the revised SCE Tax Agreement included as Attachment C to the Amended and Restated 2003 Settlement Agreement.

"Section 4.2(d) Action" has the meaning given to it in Section 4.2(c).

"Seller" and "Sellers" each has the meaning given to it in the preamble to this Agreement.

"Sellers' Disclosure Schedule" means the schedule delivered to Purchaser by Sellers herewith and dated as of the Effective Date, containing all lists, descriptions, exceptions and other information and materials as are required to be included therein by Sellers pursuant to this Agreement attached hereto as Schedule VI.

"Sellers' Indemnified Party" has the meaning given to it in Section 7.2 of this Agreement.

"Sellers' Knowledge" means the actual knowledge of the Persons listed on Section 1.1.1(d) of the Sellers' Disclosure Schedule; provided, however, each such Person shall be deemed to have knowledge of a matter of which such Person received written notice.

"Sellers' Releases" means releases to be sought by Sellers from (i) SNWA under the Co-Tenancy Agreement, the O&M Agreement, and the Agency Agreement, (ii) Reliant Energy Services, Inc. under the Reliant Agreement, (iii) Siemens Westinghouse Power Corporation under the Long Term Maintenance Agreement, (iv) Purchaser with respect to any obligations of SNWA under the Interconnection and Operation Agreement, each of which releases shall be from all liability for actions taken after the Closing Date, except for clause (iv), which shall be from all liability for actions taken after the effective date of the Bill of Sale.

"Sellers' Releases Deadline" has the meaning given to it in Section 4.1(i).

"Sellers' RRSU Refund Portion" has the meaning given to it in Section 2.5.4.

"Sellers' Support Obligations" means (i) the Irrevocable Letter of Credit No. P-243249, dated November 26, 2003, issued by JPMorgan Chase Bank on behalf of GenWest, (ii) the Irrevocable Letter of Credit No. P-226706, dated June 18, 2002, issued by JPMorgan Chase Bank on behalf of GenWest, (iii) the Irrevocable Letter of Credit No. TS-07001845 dated January 2, 2002, issued by Credit Suisse First Boston on behalf of PWEC, and (iv) the Irrevocable Letter of Credit No. P-230876 dated October 11, 2002, issued by JPMorgan Chase Bank on behalf of PWEC..

"Settlement Agreements" means the 2003 Settlement Agreement, the Amended and Restated 2003 Settlement Agreement, the 2005 Settlement Agreement, and the Western Settlement Agreement.

"Shared Books and Records" means Books and Records relating specifically to the construction, ownership, operation or maintenance of the Facility that are not Non-Shared Books and Records, excluding any such Shared Books and Records constituting or relating solely to Excluded Assets; provided, however, that if such Books and Records contain information related to the Purchased Assets and Excluded Assets, the portion relating to the Excluded Assets may be redacted.

"Shared Intellectual Property" means Intellectual Property owned jointly by GenWest and SNWA or by either of GenWest or SNWA, in each case for their joint benefit.

"Shared Materials and Equipment" shall include the equipment, machinery, apparatus, furniture, computer hardware, vehicles, Stores and Inventory, tools, dies, construction in progress, and other tangible personal property required, including such additional items of tangible personal property as acquired prior to the Closing Date, used, or to be used for or in the operation or maintenance of the Facility that are not Non-Shared Materials and Equipment, including the Shared Materials and Equipment listed in Schedule II, Part B, which schedule does not include Stores and Inventory.

"Siemens Consent" shall mean the consent obtained from Siemens Westinghouse Power Corporation consenting to the assignment of (i) the Equipment Supply Agreement (Contract No. 750200136), dated February 16, 2001, between GenWest and Siemens Westinghouse Power Corporation for Combustion Turbine Equipment, as amended by Change Orders Nos. 1 through 8, 25% of the rights and obligations under which were assigned to and assumed by SNWA pursuant to the Bill of Sale, (ii) the Contract, dated April 20, 2004, between Siemens Westinghouse and PWEC, as Operating Agent, for water injection equipment, as amended by Change Order No. 1, dated July 8, 2004, and (iii) the Long Term Maintenance Agreement, in the form attached hereto as Exhibit G or otherwise in form and substance reasonably satisfactory to Purchaser and Sellers.

"Site" means that certain real property located in Clark County, Nevada, upon which the Facility is located, within Lot 23 of the APEX Industrial Park, as further described in Schedule III.

"Site Description Error" means the errors in the legal description of the Site, and in the legal description of the access road easement over a portion of APEX Industrial Park, Assessor's

Parcel Number 103-04-010-002, granted pursuant to that Grant of Easement, dated July 23, 2002 by HDL 8, LLC to GenWest, which errors are to be corrected as identified in the markups attached as Exhibit 2 and Exhibit 3 to Schedule III.

"SNWA" means the Southern Nevada Water Authority.

"SNWA Consent" shall mean the consent obtained from SNWA consenting to the Transfer of GenWest's Interest and amending the Co-Tenancy Agreement and the O&M Agreement, in the form attached hereto as Exhibit H or otherwise in form and substance reasonably satisfactory to Purchaser and Sellers.

"SNWA Deed" means the Grant, Bargain, Sale Deed dated May 14, 2004, between GenWest and SNWA.

"Stores and Inventory" means supplies, inventories, materials, lubricants, chemicals, filters, fittings, connectors, seals, gaskets, repair and replacement parts, which are located at the Site or in transit, or deliverable to the Facility pursuant to the Assumed Agreements, as of the Closing Date, and used, or to be used, in connection with the operation and maintenance of the Facility. Certain items of Stores and Inventory as of the Effective Date are listed on Schedule II, Part C.

"Stores and Inventory Adjustment Amount" has the meaning given to it in Section 2.2.4(a) of this Agreement.

"Stores and Inventory Amount" means an amount equal to 75% of the value of Stores and Inventory, which amount shall not exceed the Stores and Inventory Cap Amount. For purposes of determining value, new Stores and Inventory shall be valued at the original delivered cost, while used Stores and Inventory shall be valued at a portion of the original delivered costs based on the remaining useable life of such Stores and Inventory. In the case of used Stores and Inventory that are supplied under the Long Term Maintenance Agreement, value shall be determined by reference to the parts life list set forth in Exhibit B of the Long Term Maintenance Agreement. The "Stores and Inventory Amount" (i) shall include amounts for Stores and Inventory to the extent such Stores and Inventory have been paid for before or after Closing by GenWest and SNWA and (ii) shall exclude in all cases any amounts for Stores and Inventory included in Post-September Capital Expenditures or included in payments made by Purchaser under the Interim PPA and any amounts included in the Hot Gas Path Parts Expenditures Amount.

"Stores and Inventory Cap Amount" means an amount equal to \$5,460,000.

"Survey" has the meaning given to it in Section 4.1(g) of this Agreement.

"Tax" or "Taxes" means any and all taxes, including any interest, penalties, or other additions to tax that may become payable in respect thereof, imposed by any federal, state or local government or any agency or political subdivision of any such government, which taxes shall include all income taxes, profits taxes, taxes on gains, alternative minimum taxes, estimated taxes, payroll and employee withholding taxes, unemployment insurance taxes, social security taxes, welfare taxes, disability taxes, severance taxes, license charges, taxes on stock, sales and

use taxes, ad valorem taxes, value added taxes, excise taxes, franchise taxes, gross receipts taxes, business license taxes, occupation taxes, real or personal property taxes, stamp taxes, environmental taxes, transfer taxes, workers' compensation taxes, and other taxes, fees, duties, levies, customs, tariffs, imposts, assessments, obligations and charges of the same or of a similar nature to any of the foregoing.

"Tax Claim" has the meaning given to it in Section 8.7 of this Agreement.

"Tax Returns" means any return, report, information return, claim for refund or other document (including any related or supporting information) supplied to or required to be supplied to any Taxing Authority with respect to Taxes, including any attachments, amendments and supplements thereto.

"Taxing Authority" means, with respect to any Tax, the governmental entity or political subdivision thereof that imposes such Tax, and the agency (if any) charged with the collection of such Tax for such entity or subdivision.

"Title Insurance Commitment" has the meaning given to it in Section 4.1(g) of this Agreement.

"Title Insurance Policy" has the meaning given to it in Section 4.1(g) of this Agreement.

"Transaction Agreements" means the following agreements:

- (a) this Agreement;
- (b) the Deed;
- (c) the Assignment Agreement;
- (d) the Interim PPA; and
- (e) the Required Consents.

"Transfer" has the meaning assigned to it in the Co-Tenancy Agreement.

"Transfer Taxes" has the meaning given to it in Section 8.2 of this Agreement.

"Transferred Intellectual Property" means the Non-Shared Intellectual Property and GenWest's undivided seventy-five percent (75%) interest in the Shared Intellectual Property.

"Transferred Permits" means those Permits set forth in Schedule IV, interests in which are to be conveyed by the Sellers to Purchaser as part of the Purchased Assets.

"Transmission Services Agreement" means the Service Agreement for Long-Term Firm Point-To-Point Transmission Service, Service Agreement No. 101A, dated December 12, 2002, as amended December 19, 2003, and effective July 31, 2003, between Purchaser and PWCC, which was originally assigned to PWEC by Reliant Energy Services, Inc. pursuant to the TSA

101 Assignment Agreement and later assigned to PWCC pursuant to the Assignment and Assumption Agreement, dated April 9, 2003, between PWEC and PWCC.

"TSA 100 Assignment Agreement" means the Assignment and Assumption Agreement (TSA-100), dated as of September 17, 2002, between PWEC and Reliant Energy Services, Inc.

"TSA 101 Assignment Agreement" means the Assignment and Assumption Agreement (TSA-101), dated as of September 17, 2002, between PWEC and Reliant Energy Services, Inc.

"Water Permit" means the Permanent Point of Diversion Permit for the Facility to be issued by State of Engineer of Nevada, an application for which was filed on May 12, 2005, as such application may be amended or modified as may be agreed to by Purchaser and Sellers.

"Water Supply Agreement" means the Water Supply Agreement, effective August 7, 2001, between the Las Vegas Valley Water District and GenWest, 25% of the rights and obligations under which were assigned to and assumed by SNWA pursuant to the Bill of Sale.

"Well Development Agreement" means the Well Development Agreement, dated May 17, 2002, between GenWest and Dry Lake Water, LLC, 25% of the rights and obligations under which were assigned to and assumed by SNWA pursuant to the Bill of Sale.

"Western Settlement Agreement" means the Settlement Agreement, dated as of March 21, 2005, entered into among Purchaser, Valley Electric Association, Inc., Purchaser's Chuck Lenzie Generating Station, GenWest, Las Vegas Cogeneration II, LLC, Mirant Las Vegas, LLC, Reliant Energy Wholesale Generation, LLC, and SNWA, which resolves issues in FERC Docket No. ER04-152-000.

Section 1.2 Rules as to Usage. Except as otherwise expressly provided herein, the following rules shall apply to the usage of terms in this Agreement:

(a) The terms defined above have the meanings set forth above for all purposes, and such meanings are equally applicable to both the singular and plural forms of the terms defined. If a term is defined as one part of speech (such as a noun), it shall have a corresponding meaning when used as another part of speech (such as a verb).

(b) "Include," "includes" and "including" shall be deemed to be followed by "without limitation" whether or not they are in fact followed by such words or words of like import.

(c) "Writing," "written" and comparable terms refer to printing, typing, and other means of reproducing in a visible form.

(d) Any Law defined or referred to herein means such Law as from time to time amended, modified or supplemented, including by succession of comparable successor Law and any rules and regulations promulgated thereunder.

(e) References to a Person are also to its permitted successors and assigns.

(f) Any term defined above by reference to any agreement, instrument or Law has such meaning whether or not such agreement, instrument or Law is in effect.

(g) "Hereof," "herein," "hereunder" and comparable terms refer, unless otherwise expressly indicated, to the entire agreement or instrument in which such terms are used and not to any particular article, section or other subdivision thereof or exhibit or schedule or other attachment thereto. References in an instrument to "Article," "Section," or another subdivision or to an exhibit or schedule or other attachment are, unless the context otherwise requires, to an article, section, subsection or subdivision of or an exhibit or schedule or other attachment to such agreement or instrument.

(h) Pronouns, whenever used in any agreement or instrument that is governed by this Agreement and of whatever gender, shall include all Persons. References to any gender include, unless the context otherwise requires, references to all genders.

(i) The word "or" will have the inclusive meaning represented by the phrase "and/or." "Shall" and "will" have equal force and effect.

(j) Whenever the consent or approval of any Party is required pursuant to this Agreement, unless expressly stated that such consent or approval is to be given in the sole discretion of such Party, such consent or approval shall not be unreasonably withheld or delayed.

(k) Whenever this Agreement refers to a number of days, such number shall refer to calendar days unless Business Days are specified. Whenever any action must be taken hereunder on or by a day that is not a Business Day, then such action may be validly taken on or by the next day that is a Business Day.

(l) All accounting terms used herein and not expressly defined herein shall have the meanings given to them under GAAP.

Section 1.3 Schedules and Exhibits. This Agreement consists of the Articles contained herein and the Schedules and Exhibits attached hereto, all of which comprise part of one and the same agreement with equal force and effect.

ARTICLE II

SALE AND PURCHASE; PRICE; CLOSING

Section 2.1 Sale and Purchase; Definition of Purchased Assets; Assumed Liability.

Section 2.1.1 Purchased Property. On the terms and subject to the conditions set forth in this Agreement, at the Closing, the Sellers shall sell, transfer, convey, assign and deliver to Purchaser, free and clear of all Liens (other than Permitted Liens), and Purchaser or its designated Affiliate will purchase and pay for (a) an undivided seventy-five percent (75%) interest in the Project and (b) a 100% interest in the Non-Shared Assets, excluding the Excluded Assets (sub-clauses (a) and (b) collectively, the "Purchased Assets").

Section 2.1.2 Assignment and Assumption of Assumed Agreements. On the terms and subject to the conditions set forth in this Agreement, effective as of the Closing, Sellers shall assign to Purchaser and Purchaser shall assume all of Sellers' rights under the Assumed Agreements, and (a) in the case of Assumed Agreements other than the Interconnection Contracts, all of Sellers' obligations arising after the Closing under such Assumed Agreements, and (b) in the case of Interconnection Contracts, all of Sellers' obligations under the Interconnection Contracts, other than (x) any refund liability of GenWest in connection with the proceedings on remand from the United States Court of Appeals for the D.C. Circuit in FERC Docket No. ER02-1913 or a subsequent ruling by FERC or a court on this issue, except for that portion of such liability for which SNWA is responsible under the Co-Tenancy Agreement, and (y) any refund liability of GenWest to SCE pursuant to paragraph 31 of the 2003 Settlement Agreement and the Amended and Restated 2003 Settlement Agreement, with respect to refunds received by GenWest, except for that portion of such liability for which SNWA is responsible under the Co-Tenancy Agreement. For the avoidance of doubt, (i) with respect to indemnity obligations under Assumed Agreements, other than Interconnection Contracts as provided above, Purchaser shall only assume liability for events that occur after the Closing, and (ii) Purchaser shall not be deemed to assume any Liabilities of Sellers pursuant to this Agreement or the transactions contemplated hereby, except as set forth in this Section 2.1.2.

Section 2.1.3 Retention of Certain Assets. Sellers shall have no obligation to transfer any interest or rights in those agreements, assets and properties described in Schedule V, Part A attached hereto (the "Excluded Assets") and Purchaser shall have no Liability with respect thereto. The Parties acknowledge and agree that Sellers shall have the right on or prior to the Closing Date to retain or to transfer and assign to one or more of Sellers' Affiliates, their interests in the Excluded Assets.

Section 2.1.4 Excluded Liabilities. On and after the Closing, and without further Liability or obligation of Purchaser, Sellers or their Affiliates, as the case may be, shall retain the duties, obligations and Liabilities, direct or indirect, known or unknown, absolute or contingent, under those agreements and other matters set forth in Schedule V, Part B attached hereto (the "Excluded Liabilities").

Section 2.2 Purchase Price.

Section 2.2.1 Amount. In consideration of the sale, assignment, conveyance, transfer and delivery to Purchaser as of the Closing of the Sellers' right, title and interest in the Purchased Assets, Purchaser shall pay to GenWest an amount equal to the sum of (a) \$207,620,000, (b) the Stores and Inventory Amount, (c) the Post-September Capital Expenditures Amount, (d) the Post-April RRSU Payment Amount and (e) the Hot Gas Path Parts Expenditures Amount (collectively, the "Purchase Price").

Section 2.2.2 Payment of Estimated Purchase Price. At the Closing, Purchaser shall pay or cause to be paid to GenWest an amount which shall be the sum of the following (the "Estimated Purchase Price"): (i) \$207,620,000, and (ii) the undisputed portions of the Estimated Stores and Inventory Amount, the Estimated Post-September Capital Expenditures Amount, the Estimated Post-April RRSU Payment Amount, and the Estimated Hot Gas Path Parts Expenditures Amount.

Section 2.2.3 Estimated Adjustment. At least ten (10) Business Days prior to the Closing Date, Sellers in consultation with Purchaser shall conduct an inventory survey, which may be observed by Purchaser, and prepare and deliver to Purchaser an estimated closing statement certified to be a good faith estimate by a duly authorized officer of GenWest (the "Estimated Closing Statement"). The Estimated Closing Statement shall set forth in reasonable detail: (i) Sellers' best estimate of the Stores and Inventory Amount (the "Estimated Stores and Inventory Amount"), which statement shall include a description, part number, quantity on hand, average unit cost (adjusted for remaining useable life, if used) and extended value (quantity times average unit cost) with respect to each class of inventory, including the assumptions and calculations used by Sellers in such estimate, (ii) Sellers' best estimate of the Post-September Capital Expenditures Amount, including the assumptions and calculations used by Sellers in such estimate (the "Estimated Post-September Capital Expenditures Amount"), (iii) Sellers' best estimate of the Post-April RRSU Payment Amount, including the assumptions and calculations used by Sellers in such estimate (the "Estimated Post-April RRSU Payment Amount"), and (iv) Sellers' best estimate of the Hot Gas Path Parts Expenditures Amount, including the assumptions and calculations used by Sellers in such estimate (the "Estimated Hot Gas Path Parts Expenditures Amount", together with the Estimated Stores and Inventory Amount, the Estimated Post-September Capital Expenditures Amount, and the Estimated Post-April RRSU Payment Amount, the "Estimated Adjustment"). Within five (5) Business Days following the delivery of the Estimated Closing Statement by Sellers to Purchaser, Purchaser may object in good faith to the Estimated Adjustment in writing. If Purchaser objects to the Estimated Adjustment, the Parties shall attempt to resolve their differences by negotiation. If the Parties are unable to do so within two (2) Business Days prior to the Closing Date (or if Purchaser does not object to the Estimated Adjustment), the amount of the Estimated Adjustment not in dispute shall be included in the Estimated Purchase Price. The disputed portion shall be paid as a post-Closing adjustment to the extent required by Section 2.2.4.

Section 2.2.4 Purchase Price Adjustment.

(a) Within 60 days after the Closing, Purchaser in consultation with Sellers shall prepare and deliver to the Sellers a statement (the "Adjustment Statement"), which reflects (i) the difference between (A) the Stores and Inventory Amount as of the Closing Date, based on an inventory survey conducted by Purchaser within 30 days after the Closing Date, which may be observed by Sellers, and (B) the undisputed Estimated Stores and Inventory Amount (such difference is referred to as the "Stores and Inventory Adjustment Amount"), (ii) the difference between (A) the Post-September Capital Expenditures Amount and (B) the undisputed Estimated Post-September Capital Expenditures Amount (such difference is referred to as the "Post-September Capital Expenditures Adjustment Amount"), (iii) the difference between (A) the Post-April RRSU Payment Amount and (B) the undisputed Estimated Post-April RRSU Payment Amount (such difference is referred to as the "RRSU Adjustment Amount"), and (iv) the difference between (A) the Hot Gas Path Parts Expenditures Amount and (B) the undisputed Estimated Hot Gas Path Parts Expenditures Amount (such difference is referred to as the "Hot Gas Path Parts Adjustment Amount"). The Stores and Inventory Adjustment Amount, the Post-September Capital Expenditures Adjustment Amount, the RRSU Adjustment Amount, and the Hot Gas Path Parts Adjustment Amount are referred to collectively as the "Adjustment Amount." The Adjustment Statement shall be prepared using GAAP and the methodologies set forth in the definition of Stores and Inventory Amount. The Parties agree to

cooperate in connection with the preparation of the Adjustment Statement and related information, and shall provide each other with such books, records and information as may be reasonably requested from time to time in connection therewith and in connection with Sellers' review thereof.

(b) Sellers may dispute the Adjustment Amount; provided, however, that Sellers shall notify Purchaser in writing of the disputed amount, and the basis of such dispute, within ten (10) Business Days of Sellers' receipt of the Adjustment Statement. In the event of a dispute with respect to any part of the Adjustment Amount, Purchaser and Sellers shall attempt to reconcile their differences and any resolution by them as to any disputed amounts shall be final, binding and conclusive on the Parties. If Purchaser and Sellers are unable to reach a resolution of such differences within 30 days of receipt of Sellers' written notice of dispute to Purchaser, Purchaser and Sellers shall submit the amounts remaining in dispute for determination and resolution to the Independent Accounting Firm, which shall be instructed to determine and report to the Parties, within 30 days after such submission, and such report shall be final, binding and conclusive on the Parties hereto with respect to the amounts disputed. The fees and disbursements of the Independent Accounting Firm shall be shared equally by Purchaser and Sellers.

(c) Within ten (10) Business Days after Sellers' receipt of the Adjustment Statement, the Party owing the Adjustment Amount shall pay all undisputed amounts. If there is a dispute with respect to any amount of the Adjustment Statement, within five (5) Business Days after the final determination of any amounts on the Adjustment Statement, the Party owing the Adjustment Amount shall pay to the other Party an amount equal to the disputed Adjustment Amount as finally determined to be payable with respect to the Adjustment Statement. Any amount paid under this Section 2.2.4 shall be paid with interest for the period from, and including, the Closing Date to, but excluding, the date of payment, calculated at the lesser of (a) the prime rate under "Money Rates" as reported in the Wall Street Journal on the first business day of the month during which interest is payable plus two percent (2%) or (b) the maximum rate of interest permitted to be charged by applicable Law.

Section 2.2.5 Amounts in Respect of Mechanics' Liens.

Notwithstanding anything in this Section 2.2 or Section 2.4.1 to the contrary, Purchaser may withhold from the Estimated Purchase Price an amount equal to the value of all mechanics', carriers', workers', repairers' and other similar Liens in existence at Closing on the Purchased Assets, other than those arising or incurred under Assumed Agreements in the ordinary course of business, not in violation of the Co-Tenancy Agreement or the O&M Agreement relating to obligations which are not yet due and payable. To the extent such Liens are not remedied by Sellers within 90 days after Closing or such earlier date notified at least five (5) Business Days in advance by Purchaser to Sellers as is reasonably necessary for Purchaser, Purchaser shall be entitled to apply the portion of the Estimated Purchase Price so withheld to remedy any such Liens, in satisfaction of payment to Sellers of such portion of the Purchase Price. Upon all such Liens having been remedied by Sellers or by Purchaser pursuant to the preceding sentence, Purchaser shall pay to GenWest any remaining amounts of the Purchase Price retained by Purchaser under this Section 2.2.5.

Section 2.2.6 Method of Payment of Purchase Price. Payment of the Estimated Purchase Price and the Adjustment Amount shall be made in United States dollars, by wire transfer of immediately available federal funds to an account located in the United States as GenWest or, if applicable, Purchaser may specify by notice.

Section 2.2.7 Proration.

(a) Purchaser and Sellers agree that the following items relating to the Purchased Assets shall be prorated as of the Closing Date, with Sellers liable to the extent such items relate to any time period through the Closing Date, and Purchaser liable to the extent such items relate to periods commencing after the Closing Date (measured in the same units used to compute the item in question, otherwise measured by calendar days):

(i) any real and personal property ad valorem taxes imposed on tangible or intangible property with respect to the Purchased Assets as provided in Section 8.3, Section 8.4 and Section 8.5;

(ii) any costs or assessments imposed by the Master Declaration or Restrictions Declaration;

(iii) any assessment by any Governmental Authority for paving, roadways, sidewalk or other improvements or maintenance costs related to the Site; and

(iv) any rent payments made after the Effective Date in respect of BLM grants;

(v) any charges for water, telephone, electricity and other utilities;

(vi) (1) any annual Permit, license and registration fees with respect to the Transferred Permits listed on Part B of Schedule IV and (2) any prepayments under the Assumed Agreements listed on Part E of Schedule I; provided, however, that any payments owing by Purchaser with respect to the prorated amounts under this Section 2.2.7(a)(vi)(2) shall not exceed \$100,000 in the aggregate.

(b) In connection with the prorations referred to in (a) above, in the event that actual figures are not available at the Closing Date, the proration shall be based upon the amounts accrued through the Closing Date or paid for the most recent year (or other appropriate period) for which actual amounts paid are available. Such prorated amounts shall be re-prorated and paid to the appropriate Party within 60 days of the date that the previously unavailable actual figures become available. Sellers and Purchaser agree to furnish each other with such documents and other records as may be reasonably requested in order to confirm all adjustment and proration calculations made pursuant to this Section 2.2.7. Prorated amounts shall be based on GenWest's share of the amount to be prorated, as determined under the O&M Agreement.

Section 2.3 Allocation of Purchase Price. The Purchase Price shall be allocated among the Purchased Assets as of the Closing Date in accordance with a schedule to be prepared by Purchaser, subject to the consent of Sellers, using the allocation method provided by Section

1060 of the Code and the regulations thereunder. The Parties shall cooperate to comply with all substantive and procedural requirements of Section 1060 of the Code and the regulations thereunder, and except for any adjustment to the Purchase Price, the allocation shall be adjusted only if and to the extent necessary to comply with such requirements. Purchaser and Sellers agree that they will not take nor will they permit any Affiliate to take, for Tax purposes, any position inconsistent with such allocation; provided, however, that (i) Purchaser's cost may differ from the total amount allocated hereunder to reflect the inclusion in the total cost of items (for example, capitalized acquisition costs) not included in the total amount so allocated, and (ii) the amount realized by Sellers may differ from the amount allocated to reflect transaction costs that reduce the amount realized for federal income Tax purposes.

Section 2.4 The Closing. The closing of the transactions contemplated herein (the "Closing") will take place at Purchaser's offices in Las Vegas, Nevada, at 10:00 a.m. local time on the date as soon as practicable (but in no event longer than ten (10) Business Days, subject to an additional ten (10) Business Day extension at the election of Purchaser in the event of an amendment or update to the Sellers' Disclosure Schedule pursuant to Section 4.11(b)(iii) which occurs less than 10 days prior to the Closing Date) after the conditions to the Closing set forth in Section 5.1 and Section 5.2 have been satisfied or waived, or at such other place, time or date as Purchaser and Sellers mutually agree (the "Closing Date"). The Closing shall be deemed effective as of 12:01 A.M. Las Vegas time on the day after the Estimated Purchase Price has been paid to GenWest and the Deed and the Assignment Agreement have been executed and delivered to Purchaser.

Section 2.4.1 Closing.

(a) At the Closing, Purchaser will (x) pay to GenWest the Estimated Purchase Price in accordance with Section 2.2 and (y) execute and deliver (as applicable) the following items to Sellers:

- (i) True and complete copies of the PUCN Approval;
- (ii) True and complete copies of the FERC Approval;
- (iii) True and complete copies of evidence of the expiration or early termination of the waiting period under the HSR Act;
- (iv) A bill of sale, assignment and assumption agreement in the form of Exhibit I (the "Assignment Agreement");
- (v) The originals of the Sellers' Support Obligations;
- (vi) A State of Nevada Declaration of Value in the form required by Nevada Revised Statutes Section 375.060;
- (vii) A Certificate of Good Standing with respect to Purchaser, as of a recent date, issued by the Secretary of State of the State of Nevada;

(viii) Copies, certified by the Secretary or Assistant Secretary of Purchaser, of corporate resolutions authorizing the execution and delivery of this Agreement and all of the other agreements and instruments, in each case, to be executed and delivered by Purchaser in connection herewith;

(ix) A certificate of the Secretary or Assistant Secretary of Purchaser identifying the name and title and bearing the signatures of the officers of Purchaser authorized to execute and deliver this Agreement and the other agreements and instruments contemplated hereby;

(x) A certificate addressed to Sellers dated the Closing Date executed by the duly authorized officer of Purchaser to the effect that the conditions set forth in Section 5.2.1 and Section 5.2.2 have been satisfied by Purchaser; and

(xi) Any amounts for which Purchaser is liable pursuant to Section 2.2.7 of this Agreement.

(b) At the Closing, Sellers will execute and deliver (as applicable) to Purchaser the following items:

(i) The Required Consents;

(ii) True and complete copies of the FERC Approval;

(iii) True and complete copies of evidence of the expiration or the early termination of the waiting period under the HSR Act;

(iv) The Assignment Agreement;

(v) A grant, bargain and sale deed (the "Deed") in the form of Exhibit J and any memorandum of documents or other documents necessary to convey title to the Real Property, including the indemnity described in Section 4.1(g) hereto;

(vi) A certification of non-foreign status for PWEC in the form and manner which complies with the requirements of Section 1445 of the Code and the regulations promulgated thereunder;

(vii) A State of Nevada Declaration of Value in the form required by Nevada Revised Statutes Section 375.060;

(viii) Certificates of Good Standing with respect to the Sellers, as of a recent date, issued by the Secretary of State of the State of Arizona in the case of PWCC and PWEC, and by the Secretary of State of the State of Delaware in the case of GenWest;

(ix) Copies, certified by the Secretary or Assistant Secretary of each Seller, of resolutions authorizing the execution and delivery of this Agreement and all of the other agreements and instruments, in each case, to be executed and delivered by Sellers in connection herewith;

(x) A certificate of the Secretary or Assistant Secretary of each Seller identifying the name and title and bearing the signatures of the officers of each Seller authorized to execute and deliver this Agreement and the other agreements and instruments contemplated hereby;

(xi) A certificate addressed to Purchaser dated the Closing Date executed by the duly authorized officers of each Seller to the effect that the conditions set forth in Section 5.1.1 and Section 5.1.2 have been satisfied by Sellers;

(xii) updated record drawings that include the as-built or redlined drawing changes reflecting the design of the Facility as of ten (10) days prior to Closing;

(xiii) any amounts for which the Sellers are liable pursuant to Section 2.2.7 and Section 4.2(b)(i)(z) of this Agreement; and

(xiv) letters of credit in favor of Purchaser replacing the Existing Letters of Credit, to the extent such letters of credit are required under the applicable Assumed Agreement.

(c) If requested by Purchaser or Sellers, the Closing shall be consummated through an escrow with Purchaser's title company acting as escrow holder, which may include delivery to the escrow holder of the items in Sections 2.4.1(a) and 2.4.1(b) of this Agreement and payment to the escrow holder of the Estimated Purchase Price, Transfer Taxes and any amounts owing under Section 2.2.7 and Section 4.1(g), notwithstanding other provisions in this Agreement to the contrary. Escrow shall close once all conditions to Closing have been satisfied or waived and the escrow holder shall have recorded the Deed.

Section 2.5 Further Assurances; Post-Closing Cooperation.

Section 2.5.1 Further Assurances. Subject to the terms and conditions of this Agreement, at any time or from time to time after the Closing, at either Party's request and without further consideration, the other Party shall execute and deliver to such Party such other instruments of sale, transfer, conveyance, assignment and confirmation, provide such materials and information and take such other actions as such Party may reasonably deem necessary or desirable in order more effectively (a) to transfer, convey and assign to Purchaser, and to confirm Purchaser's title to, the Purchased Assets, (b) to effectuate the assumption by Purchaser of the Assumed Agreements, and (c) otherwise to consummate the transactions contemplated by this Agreement. Purchaser shall provide to GenWest all invoices and supporting documentation received with respect to Assumed Agreements, which relate to any obligations arising thereunder prior to the Closing Date or any other obligation that remains with Sellers. In the event that either Party receives a payment from SNWA due to the other Party, such Party will promptly remit such payment to the other Party and advise SNWA thereof in writing.

Section 2.5.2 Pre-Closing Books and Records.

(a) Following Closing, each Party will afford the other Party, its counsel and its accountants, during normal business hours, reasonable access to the Shared Books and

Records and the Non-Shared Books and Records with respect to periods prior to Closing (the "Pre-Closing Books and Records") and the right to make copies and extracts therefrom, to the extent that such access may be reasonably required by the requesting Party in connection with (i) the preparation of Tax Returns, (ii) compliance with the requirements of any Governmental Authority, (iii) any Excluded Liabilities or (iv) any rights and obligations arising under Article VII, Article VIII or Article X hereof; provided, however, that nothing in this Agreement shall be deemed to obligate either Party to maintain the Pre-Closing Books and Records.

(b) Purchaser acknowledges and consents to the retention by Sellers of information made available to Purchaser relating to the Purchased Assets (the "Retained Information"). From and after the Closing Date, Sellers shall, and shall cause their representatives to, treat the Retained Information as strictly confidential (except to the extent compelled to disclose by judicial or administrative process or by other requirements of Law, any stock exchange or any other self-regulatory organization); provided, however, that in no event shall the foregoing restrict any Seller from using or disclosing any Retained Information in connection with any claim arising under or in connection with this Agreement or any Excluded Liabilities.

Section 2.5.3 Delivery of Books and Records. No later than the Closing Date (or in the case of Books and Records not immediately required for the operation and maintenance of the Facility that cannot be reasonably and practicably delivered at the Closing, as soon as reasonably practicable thereafter, but no later than 30 days after the Closing Date), Sellers shall deliver any Shared Books and Records, Non-Shared Books and Records, and Continued Employee Books and Records (to the extent they may be provided to Purchaser in accordance with Law) that are not located at the Site to Purchaser at Purchaser's offices in Las Vegas, Nevada, the Site or another location as designated by Purchaser in or near Las Vegas, Nevada. As soon as reasonably practicable after the Closing, Sellers shall deliver to Purchaser updated record drawings that include the as-built or redlined drawing changes reflecting the design of the Facility as of the Closing.

Section 2.5.4 RRSU Payments Refunds. At any time after Closing, in the event any SCE RRSU Refund is received by any Party, Sellers shall be entitled to receive the Sellers' RRSU Refund Portion of such SCE RRSU Refund, and Purchaser shall be entitled to receive the Purchaser's RRSU Refund Portion of such SCE RRSU Refund as set forth below:

(a) For any SCE RRSU Refund associated with the Eldorado 500kV substation breaker upgrades, "Sellers' RRSU Refund Portion" shall be 75% and "Purchaser's RRSU Refund Portion" shall be 25%, which portion Purchaser shall pay to SNWA pursuant to the terms of the Co-Tenancy Agreement; provided, however, that if at any time SCE shall separately remit to SNWA its portion of any SCE RRSU Refund, the "Sellers' RRSU Refund Portion" shall be 100% with respect to such SCE RRSU Refund.

(b) For any SCE RRSU Refund associated with the Moenkopi 500 kV series capacitor upgrades ("Moenkopi Capacitor Work"):

(i) "Sellers' RRSU Refund Portion" shall be equal to the product of (1) the amount of the SCE RRSU Refund in respect of the Moenkopi Capacitor Work,

and (2) the amount of payments by GenWest under Revised MOU I prior to May 1, 2005 in respect of the Moenkopi Capacitor Work (other than amounts attributable to SNWA's Interest prior to May 1, 2005), less any SCE RRSU Refunds received by GenWest prior to Closing in connection with such payments, divided by the sum of the payments made by GenWest or Purchaser under Revised MOU I before, on or after May 1, 2005 in respect of the Moenkopi Capacitor Work (including amounts attributable to SNWA's Interest), less any SCE RRSU Refunds received by GenWest prior to Closing in connection with such payments made by it (including refunds in respect of SNWA's Interest).

(ii) "Purchaser's RRSU Refund Portion" shall be equal to the product of (1) the amount of the SCE RRSU Refund in respect of the Moenkopi Capacitor Work, and (2) the sum of payments by GenWest or Purchaser under Revised MOU I on or after May 1, 2005 in respect of the Moenkopi Capacitor Work (including amounts attributable to SNWA's Interest), plus payments by GenWest under Revised MOU I prior to May 1, 2005 in respect of the Moenkopi Capacitor Work solely attributable to SNWA's Interest, less any SCE RRSU Refunds received by GenWest prior to Closing in connection with any such payments made by it (including refunds in respect of SNWA's Interest), divided by the sum of the payments made by GenWest or Purchaser under Revised MOU I before, on or after May 1, 2005 in respect of the Moenkopi Capacitor Work (including amounts attributable to SNWA's Interest), less any SCE RRSU Refunds received by GenWest prior to Closing in connection with such payments made by it (including refunds in respect of SNWA's Interest). Sellers' RRSU Refund Portion and Purchaser's RRSU Refund Portion shall be determined on the later of the Closing Date or the date upon which refunds in respect of the Moenkopi Capacitor Work commence.

(c) For any SCE RRSU Refund associated with the Lugo 500 kV series capacitor upgrades ("Lugo Capacitor Work"):

(i) "Sellers' RRSU Refund Portion" shall be equal to the product of (1) the amount of the SCE RRSU Refund in respect of the Lugo Capacitor Work, and (2) the amount of payments by GenWest under Revised MOU I prior to May 1, 2005 in respect of the Lugo Capacitor Work (other than amounts attributable to SNWA's Interest prior to May 1, 2005), less any SCE RRSU Refunds received by GenWest prior to Closing in connection with such payments, divided by the sum of the payments made by GenWest or Purchaser under Revised MOU I before, on or after May 1, 2005 in respect of the Lugo Capacitor Work (including amounts attributable to SNWA's Interest), less any SCE RRSU Refunds received by GenWest prior to Closing in connection with such payments made by it (including refunds in respect of SNWA's Interest).

(ii) "Purchaser's RRSU Refund Portion" shall be equal to the product of (1) the amount of the SCE RRSU Refund in respect of the Lugo Capacitor Work, and (2) the sum of payments by GenWest or Purchaser under Revised MOU I on or after May 1, 2005 in respect of the Lugo Capacitor Work (including amounts attributable to SNWA's Interest), plus payments by GenWest under Revised MOU I prior to May 1, 2005 in respect of the Lugo Capacitor Work solely attributable to SNWA's Interest, less any SCE RRSU Refunds received by GenWest prior to Closing in connection with any such payments made by it (including refunds in respect of SNWA's Interest), divided by the sum of the payments made by GenWest or Purchaser under Revised MOU I before, on or after May 1, 2005 in respect of the

Lugo Capacitor Work (including amounts attributable to SNWA's Interest), less any SCE RRSU Refunds received by GenWest prior to Closing in connection with such payments made by it (including refunds in respect of SNWA's Interest). Sellers' RRSU Refund Portion and Purchaser's RRSU Refund Portion shall be determined on the later of the Closing Date or the date upon which refunds in respect of the Lugo Capacitor Work commence.

(d) In the event that the SCE RRSU Refunds for the Moenkopi Capacitor Work and the Lugo Capacitor Work are not separated as contemplated above, the Parties shall cooperate in good faith to allocate the SCE RRSU Refunds on the same principles as provided above. Each Party shall pay over to the other Party a portion of the amount received by such Party to effect the foregoing. Purchaser shall pay any refund received by it attributable to SNWA's Interest to SNWA in accordance with the Co-Tenancy Agreement. Payments under this Section 2.5.4 shall be made within ten (10) days of the receipt of such SCE RRSU Refunds.

Section 2.5.5 Site Description Error Indemnity. Sellers shall indemnify Purchaser for any Losses incurred by Purchaser arising from or in connection with any failure of Sellers to correct the Site Description Error prior to Closing, and reimburse Purchaser for any costs incurred by Purchaser following Closing in connection with remedying such failure. Purchaser shall consult with Sellers about any remedial action to be taken by Purchaser in connection with correcting the Site Description Error following Closing and shall use commercially reasonable efforts to remedy the Site Description Error in a cost-effective manner.

Section 2.5.6 Drainage Encroachment Indemnity. Sellers shall indemnify Purchaser for any Losses incurred by Purchaser arising from or in connection with any failure of Sellers to correct the matters described in Section 4.1(n) hereto prior to Closing, and reimburse Purchaser for any costs incurred by Purchaser following Closing in connection with remedying such failure. Purchaser shall consult with Sellers about any remedial action to be taken by Purchaser in connection with correcting such matters following Closing and shall use commercially reasonable efforts to remedy the matters in a cost-effective manner.

ARTICLE III

REPRESENTATIONS AND WARRANTIES

Section 3.1 Representations and Warranties of Sellers. Except as specifically set forth in the Sellers' Disclosure Schedule attached hereto as Schedule VI, each of the Sellers, jointly and severally, represents and warrants to Purchaser that all of the statements contained in this Section 3.1 with respect to the Sellers are true and correct as of the Effective Date, and will be true and correct as of the Closing Date as though made on and as of the Closing Date. Each exception and other response to this Agreement set forth in the Sellers' Disclosure Schedule is identified by reference to, or has been grouped under a heading referring to, a specific individual section of this Agreement, and, except as otherwise specifically stated with respect to such exception, relates only to such section. The inclusion of an exception or other response to this Agreement set forth in the Sellers' Disclosure Schedule does not necessarily mean that such disclosure would otherwise constitute a breach of this Agreement; rather, such disclosure is made for the purposes of comprehensively informing Purchaser of matters it should consider in connection with the purchase of the Purchased Assets.

Section 3.1.1 Existence. PWCC is a corporation duly formed, validly existing and in good standing under the Laws of the State of Arizona. PWECC is a corporation duly formed, validly existing and in good standing under the Laws of the State of Arizona and is licensed to do business as a corporation in the State of Nevada. GenWest is a limited liability company duly qualified, validly existing and in good standing under the Laws of the State of Delaware, is licensed to do business as a limited liability company in the State of Nevada, and has full limited liability company power and authority to own and use the Purchased Assets.

Section 3.1.2 Authority. Each Seller has full corporate or limited liability company power and authority to execute and deliver this Agreement and the Transaction Agreements to which it is or will be a party, to perform its obligations hereunder and thereunder and to consummate the transactions contemplated hereby and thereby. The execution and delivery by each Seller of this Agreement and the Transaction Agreements to which it is or will be a party, and the performance by such Seller of its obligations hereunder and thereunder, have been duly and validly authorized by all necessary corporate or company action.

Section 3.1.3 Binding Agreement. This Agreement and the Transaction Agreements to which it is or will be a party have been or will be when delivered duly executed and delivered by each Seller and, assuming due and valid authorization, execution and delivery thereof by Purchaser and each other party thereto, this Agreement and the Transaction Agreements to which it is or will be a party are or will be when delivered valid and binding obligations of such Seller enforceable against such Seller in accordance with their terms, except (i) as limited by applicable bankruptcy, insolvency, reorganization, moratorium, fraudulent conveyance and other similar Laws of general application affecting enforcement of creditors' rights generally, and (ii) general equitable principles, including that the availability of the remedy of specific performance or injunctive or other forms of equitable relief may be subject to equitable defenses and would be subject to the discretion of the court before which any proceeding therefor may be brought.

Section 3.1.4 No Conflicts. Subject to the receipt of the Required Consents, FERC Approval, the expiration or early termination of the waiting period under the HSR Act, and receipt of the other consents and actions listed in Section 3.1.5 of Sellers' Disclosure Schedule, the execution and delivery by each Seller of this Agreement do not, and the execution and delivery by such Seller of the Transaction Agreements to which it is or will be a party, the performance by such Seller of its obligations under this Agreement and such Transaction Agreements and the consummation of the transactions contemplated hereby and thereby shall not:

(a) Conflict with or result in a violation or breach of any of the terms, conditions or provisions of such Seller's organizational documents;

(b) Result in a default (or give rise to any right of termination, cancellation or acceleration) under any of the terms, conditions or provisions of any Assumed Agreement, note, bond, deed of trust, indenture, license, agreement, lease or other instrument or obligation to which such Seller is party or by which such Seller, or any of the Purchased Assets may be bound, except for such defaults (or rights of termination, cancellation or acceleration) as

to which requisite waivers or consents have been obtained in writing (true and correct copies of which waivers or consents have been furnished to Purchaser);

(c) Conflict with or result in a violation or breach of any term or provision of any Law applicable to such Seller or the Purchased Assets; or

(d) Result in the imposition or creation of any Lien upon any of the Purchased Assets, other than in favor of Purchaser.

Section 3.1.5 Approvals and Filings. Except for the Required Consents, FERC Approval and expiration or early termination of the waiting period under the HSR Act and as set forth in Section 3.1.5 of Sellers' Disclosure Schedule, no consent or approval of, filing with or notice to any Governmental Authority or other Person by any Seller is required in connection with the execution, delivery and performance by any Seller of this Agreement or any of the Transaction Agreements to which it is a party or the consummation of the transactions contemplated hereby or thereby.

Section 3.1.6 Sellers' Known Liabilities. Except as set forth in Section 3.1.6 of Sellers' Disclosure Schedule, to Sellers' Knowledge none of the Sellers has any Liability that has, or could be reasonably likely to have, a Material Adverse Effect.

Section 3.1.7 Reports. Since the date of its formation and except with respect to electronic quarterly reporting of its transactions to FERC, GenWest has filed or caused to be filed with the applicable state or local utility commissions or regulatory bodies and the FERC, all material forms, statements, reports and documents (including all exhibits, amendments and supplements thereto) required to be filed by it with respect to the Project under each of the applicable state public utility laws and the Federal Power Act and the respective rules and regulations thereunder.

Section 3.1.8 Legal Proceedings. Except as set forth in Section 3.1.8 to Sellers' Disclosure Schedule, there are no actions or proceedings (including orders, judgments and writs), and to Sellers' Knowledge, no claims or investigations, outstanding or pending in any Governmental Authority to which a Seller is a party or, to Sellers' Knowledge, (a) outstanding or pending in any Governmental Authority to which any counterparty to a Designated Assumed Agreement is a party, or (b) threatened against a Seller or any of its assets and properties, in each case which could be reasonably expected to (x) result in the issuance of an order restraining, enjoining or otherwise prohibiting or making illegal the consummation of the transactions contemplated by this Agreement or any of the Transaction Agreements, (y) adversely affect the ownership, construction, operation or maintenance of the Facility or the use of the Real Property, or (z) individually or in the aggregate, have a Material Adverse Effect.

Section 3.1.9 Compliance with Laws. Each of the Sellers, and to Sellers' Knowledge, its contractors, agents and representatives, is not in violation of or in default under any Law applicable to it, the Project or the Purchased Assets, the effect of which, individually or in the aggregate, could be reasonably expected to have a Material Adverse Effect. Except as set forth in Section 3.1.9 of Sellers' Disclosure Schedule, none of the Sellers has received notification alleging that it is in violation of any Law, in the case of GenWest, applicable to it,

the Project or the Purchased Assets, and in the case of PWCC and PWEC, applicable to the Project or the Purchased Assets.

Section 3.1.10 Title to Personal Property. GenWest owns, possesses and will be conveying good and valid title to all the Purchased Assets (tangible and intangible) constituting personal property, free and clear of all Liens, except Permitted Liens.

Section 3.1.11 Real Property.

(a) Schedule III contains a legal description of the Real Property subject to the errors described in the HMM Letter. GenWest owns, possesses and will be conveying good, valid and marketable fee title to an undivided seventy-five percent (75%) interest in the Site, free and clear of all Liens other than Permitted Liens. GenWest holds good and valid title to an undivided seventy-five percent (75%) interest in the Easements, free and clear of all Liens other than (i) encumbrances of record or that would be revealed by an accurate survey and (ii) Permitted Liens.

(b) Neither the whole nor any portion of the Real Property is subject to any governmental decree or order to be sold or is being condemned, expropriated or otherwise taken by any public authority with or without payment of compensation therefor, nor, to Sellers' Knowledge, has any such condemnation, expropriation or taking been proposed. Except as provided in the agreements listed in Section 3.1.11 Part A of Sellers' Disclosure Schedule, none of the Sellers is a party to any lease, assignment or similar arrangement under which any of the Sellers is a lessor, assignor or otherwise makes available for use by any third party any portion of the Real Property. Except as set forth in Section 3.1.11 Part B of Sellers' Disclosure Schedule, none of the Sellers has received any notice of, or other writing referring to, any requirements or recommendations by any insurance company that has issued a policy covering any part of the Real Property or by any board of fire underwriters or other body exercising similar functions, requiring or recommending any repairs or work to be done on any part of the Real Property, which repair or work has not been completed and accepted. Sellers have not consented to the lease of, or creation of any Lien on, any of the Project by SNWA, except as described in clause (v) of the definition of Permitted Liens.

(c) Except as set forth in Section 3.1.11 Part C of Sellers' Disclosure Schedule, Sellers have obtained all real estate licenses, easements and rights of way, including proofs of dedication, required to use the Real Property in the manner in which the Real Property is currently being used and required for the ownership, construction, operation and maintenance of the Facility.

(d) To Sellers' Knowledge, there is no action, proceeding or litigation pending or threatened (i) to modify the zoning of, or other governmental rules or restrictions applicable to, the Real Property or the use or development thereof, or (ii) for any street widening or changes in highway or traffic lanes or patterns in the immediate vicinity of the Real Property, in each case, except for such actions, proceedings or litigations which, individually or in the aggregate, could not be reasonably likely to have a Material Adverse Effect.

(e) The parcels constituting the Site are assessed separately from all other adjacent property not constituting the Site for purposes of real property taxes assessed to, or paid by, GenWest. Except as set forth in Section 3.1.11 Part D of Sellers' Disclosure Schedule, to Sellers' Knowledge, the Site complies with all applicable subdivision, zoning, land parcelization and local governmental taxation or separate assessment requirements.

(f) Other than Permitted Liens and as set forth in Section 3.1.11 Part E of Sellers' Disclosure Schedule, there are no commitments to or agreements by Sellers with any Governmental Authority affecting the use or ownership of the Real Property and to Sellers' Knowledge, there are no commitments to or agreements with any Governmental Authority by any other party affecting the use or ownership of the Real Property.

(g) Except as set forth in Section 3.1.11 Part F of Sellers' Disclosure Schedule, none of the Sellers is a party to any agreement for the sale, exchange, encumbrance, lease or transfer of any of the Real Property or any portion of the same.

(h) Except as set forth in Section 3.1.11 Part G of Sellers' Disclosure Schedule, Sellers are in compliance with all applicable conditions, covenants and restrictions that encumber the Real Property.

Section 3.1.12 Condition of Materials and Equipment. Except as set forth in Section 3.1.12 Part A of Sellers' Disclosure Schedule, all Materials and Equipment are currently located on the Real Property and no Materials and Equipment intended for the Facility are being held by third parties pending payment by Sellers. To Sellers' Knowledge, Sellers have not failed to disclose to Purchaser any fact relating to the operation or condition of the Facility or the Site that could be reasonably likely to have a Material Adverse Effect. To the Sellers' Knowledge, the Facility has been operated in accordance with Good Electric Operating Practices as such term is defined in the O&M Agreement. Except for the Excluded Assets, the Purchased Assets are sufficient to own, operate and maintain the Project as currently owned, operated and maintained by the Sellers. Except as listed in Section 3.1.12 Part B of Sellers' Disclosure Schedule and except for the Excluded Assets and assets replaced by assets of comparable or superior quality and value, to Sellers' Knowledge, none of the Sellers have sold, transferred or otherwise disposed of any assets used by any of the Sellers solely in the operation or maintenance of the Facility.

Section 3.1.13 Warranty Matters. Section 3.1.13 of the Sellers' Disclosure Schedule identifies all warranties by any vendor, materialman, supplier, contractor or subcontractor relating to the Purchased Asset or any component thereof with a value of \$50,000 or more and specifies the following information with respect to each such warranty: (a) each of the Purchased Assets or any component thereof to which the warranty is applicable but only to the extent such item has a value of \$50,000 or more, (b) the contract or agreement pursuant to which the warranty was given or made (a true and complete copy of each such contract or agreement has been provided to Purchaser), (c) a description of any warranty work done under the applicable warranty, the date thereof and the applicable warranty period for the warranty work, and (d) whether such warranty is transferable to Purchaser. To Sellers' Knowledge, there are no events that have occurred or conditions applicable that constitute or may constitute a defense to the continuing effectiveness of each such warranty.

Section 3.1.14 Facility Agreements; Assumed Agreements. Section 3.1.14 Part A of Sellers' Disclosure Schedule contains a list of all Facility Agreements in effect, true and complete copies of which (together with all amendments, supplements, schedules and exhibits) have heretofore been furnished to Purchaser, other than item 40b on Schedule I. Except as set forth in Section 3.1.14 Part B of Sellers' Disclosure Schedule, each Assumed Agreement is in full force and effect and constitutes a legal, valid and binding agreement of the applicable Seller and to Sellers' Knowledge, of each other party thereto, enforceable in accordance with its terms (subject to applicable bankruptcy, insolvency or other similar Laws relating to or affecting the enforcement of creditors' rights generally and to general principles of equity), and no material term or condition thereof has been amended from the form thereof delivered to Purchaser or waived. Except as set forth in Section 3.1.14 Part C of Sellers' Disclosure Schedule and except with respect to Assumed Agreements to which Purchaser is party, (a) none of Sellers is in violation or breach of or default under, or with notice or lapse of time or both, would be in violation or breach of or default under, any Assumed Agreement and, (b) to Sellers' Knowledge, no other party to any Assumed Agreement with a contingent liability or payment obligation in excess of \$1,000, is in violation or breach of or default under, or with notice or lapse of time or both, would be in violation or breach of or default under, any such Assumed Agreement. Other than the Required Consents, FERC Approval, the expiration or early termination of the waiting period under the HSR Act, or as set forth in Section 3.1.5 of Sellers' Disclosure Schedules, no consent or approval of, filing with or notice to any Governmental Authority or other Person by any Seller is required which has not been duly obtained or made for the assignment of the Assumed Agreements to Purchaser as contemplated hereby, true and correct copies of such consents have been provided to Purchaser.

Section 3.1.15 Permits.

(a) Section 3.1.15 Part A of the Sellers' Disclosure Schedule sets forth all Permits that Sellers are required to obtain under applicable Law in connection with the ownership, operation, maintenance or use of the Facility (the "Facility Permits").

(b) Except as set forth in Section 3.1.15 Part B of Sellers' Disclosure Schedule, Facility Permits are properly in the name of the Facility, GenWest, GenWest and SNWA jointly, or PWEC. Except as set forth in Section 3.1.15 Part C of Sellers' Disclosure Schedule, the information set forth in each application submitted by or on behalf of any of the Sellers and, to Sellers' Knowledge, any other Person, in connection with each such Facility Permit was accurate and complete in all material respects at the time of the last submission. Except as set forth in Section 3.1.15 Part D of Sellers' Disclosure Schedule, all modifications to Facility Permits required to remain in compliance with Law have been made for the ownership, operation, maintenance or use of the Facility. Except as set forth in Section 3.1.15 Part E of Sellers' Disclosure Schedule, GenWest and PWEC are in full compliance with each Facility Permit and each Facility Permit (i) is in full force and effect, (ii) is not subject to any legal proceeding or to any unsatisfied condition that (x) is not reasonably expected to be satisfied or (y) could reasonably be expected to allow material modification or revocation thereof, and (iii) is final and all applicable appeal periods have expired or terminated.

(c) Except for the approvals, notices and filings set forth in Section 3.1.15 Part F of Sellers' Disclosure Schedule, GenWest's and PWEC's interests in each Transferred

Permit may be transferred to Purchaser or Purchaser as Operating Agent, as the case may be, as contemplated by this Agreement without the consent or approval of, filing with or notice to any Governmental Authority or other Person by any of the Sellers other than those that have been duly obtained or made, true and correct copies of which have been provided to Purchaser. Upon the effectiveness of the notices and other filings set forth in Section 3.1.15 Part F of Sellers' Disclosure Schedule and as otherwise set forth in such Section 3.1.15 Part F of Sellers' Disclosure Schedule, (i) Purchaser's interest in each Transferred Permit will be properly in the name of Purchaser or Purchaser as Operating Agent, as the case may be, (ii) each Transferred Permit will be in full force and effect, (iii) each Transferred Permit will not be subject to any legal proceeding or to any unsatisfied condition that (x) is not reasonably expected to be satisfied or (y) could reasonably be expected to allow material modification or revocation thereof, and (iv) each Transferred Permit will be final and have all applicable appeal periods expired or terminated. Upon the effectiveness of the notices and other filings set forth in Section 3.1.15 Part F of the Sellers' Disclosure Schedule, the transfer of GenWest's or PWEC's interests in each Transferred Permit to Purchaser or Purchaser as Operating Agent, as the case may be, shall not breach the terms thereof or result in the forfeiture or impairment of any rights thereunder.

(d) Other than as provided in Section 3.1.15 Part G of Sellers' Disclosure Schedule, Sellers have not made any modifications, and are not aware of any modifications to the Facility by any Person, that could reasonably be expected to cause the Facility to violate any applicable Law or Permit.

Section 3.1.16 Insurance. Section 3.1.16 of Sellers' Disclosure Schedule sets forth a true and complete list and description of all insurance policies in force on the Effective Date with respect to the Purchased Assets, together with a statement of the aggregate amount of claims paid out and claims pending, under each such insurance policy, in each case relating to the Purchased Assets. All policies are in full force and effect, all premiums due thereon have been paid and the Sellers are otherwise in compliance in all material respects with the terms and provisions of such policies. Furthermore, as they relate to the Purchased Assets, (a) Sellers have not received any notice of cancellation or non-renewal of any such policy nor is the termination of any such policies threatened, (b) there is no claim pending under any of such policies as to which coverage has been questioned, denied or disputed by the underwriters of such policies, (c) Sellers have not received any notice from any of its insurance carriers that any insurance premiums in respect of such policies will be increased in the future or that any insurance coverage presently provided for will not be available to the Sellers in the future on substantially the same terms as now in effect, and (d) Sellers have not received notice that the Facility or any Materials and Equipment or the operation thereof will not be insurable or will be subject to exclusions arising from actual or potential defects in the Purchased Assets.

Section 3.1.17 Environmental Matters.

(a) Sellers have made available to Purchaser all of the environmental site assessment reports and studies that were obtained by or in the possession of Sellers, which relate to environmental matters in connection with ownership, construction, operation or maintenance of the Facility. All such reports and studies are listed in Section 3.1.17 Part A of Sellers' Disclosure Schedule.

(b) Except for the Facility Permits, none of the Sellers has entered into or agreed to any judicial or administrative consent decree or order, and is not subject to any outstanding judgment, decree, or judicial or administrative order relating to compliance with any Environmental Law or to investigation or cleanup of Hazardous Materials under any Environmental Law, in each case relating to the Facility or the Real Property.

(c) Except as disclosed in Section 3.1.17 Part B of Sellers' Disclosure Schedule, there are no claims, actions, proceedings (including orders, judgments and writs) or investigations pending in any Governmental Authority to which a Seller is a party and with respect to such claims and investigations, of which a Seller has Knowledge or, to Sellers' Knowledge, (x) outstanding or pending in any Governmental Authority to which any counterparty to a Designated Assumed Agreement is a party or (y) threatened against a Seller or any of its assets and properties, under any Environmental Law relating to the Facility or the Real Property.

(d) All Permits related to the Purchased Assets issued to any Seller and in effect under any Environmental Law are set forth in Section 3.1.17 Part C of Sellers' Disclosure Schedule. Except as set forth in Section 3.1.17 Part D of Sellers' Disclosure Schedule, Sellers and, to Sellers' Knowledge, their contractors, agents or representatives have obtained all Permits required under the Environmental Laws for the ownership, construction, operation, maintenance or use of the Facility, all such Permits are in effect to the extent required under any Environmental Law, no appeal nor any other action is pending to revoke any such Permit and Sellers and, to Sellers' Knowledge, their contractors, agents and representatives are in full compliance with all terms and conditions of all such Permits. Except as set forth in Section 3.1.17 Part E of Sellers' Disclosure Schedule, Sellers, and to Sellers' Knowledge, their contractors, agents and representatives, have filed for a renewal on a timely basis of any Facility Permits required pursuant to applicable Environmental Law.

(e) Except as set forth in Section 3.1.17 Part F of Sellers' Disclosure Schedule, Sellers, and to Sellers' Knowledge, their contractors, agents and representatives, have been and are in compliance with all applicable Environmental Laws with respect to the Facility or the Real Property. To Sellers' Knowledge, except for matters described in the reports listed in Section 3.1.17 Part A of Sellers' Disclosure Schedule, any former owners of or tenants on the Real Property, and their contractors, agents or representatives, did not violate applicable Environmental Laws with respect to their ownership, construction, operation or maintenance of the Facility or the Real Property.

(f) Except as set forth in Section 3.1.17 Part G of Sellers' Disclosure Schedule, none of the Sellers, or to Sellers' Knowledge, its contractors, agents or representatives, or to Sellers' Knowledge, any other Person, has Released, discharged, or otherwise disposed, of any Hazardous Materials on, beneath or adjacent to the Real Property, except for Releases of Hazardous Materials that could not reasonably be expected to result in a claim or a requirement to engage in a material Remediation.

(g) Except as set forth in Section 3.1.17 Part H of the Sellers' Disclosure Schedule, to Sellers' Knowledge, there are no facts, circumstances or conditions related to the Facility that exist now or as of the Closing Date that would make it reasonably likely that the

Facility will not be able to comply with applicable Environmental Law, including but not limited to, the terms and conditions of Permits issued with respect to the Facility pursuant to applicable Environmental Law.

Section 3.1.18 Labor Matters. Except as specifically set forth in Section 3.1.18 of Sellers' Disclosure Schedule:

(a) All of the Project Employees are employees of PWEC.

(b) GenWest is neither party to, nor bound by, any labor agreement, collective bargaining agreement, work rules or practices, or any other labor-related agreements or arrangements with any labor union or labor organization. There are no labor agreements, collective bargaining agreements, work rules or practices, or any other labor-related agreements or arrangements that pertain to any Project Employee and no Project Employee is represented by any labor organization.

(c) No labor union, labor organization, Project Employees or group of employees of GenWest has made a pending demand for recognition or certification, and there are no representation or certification proceedings or petitions seeking a representation proceeding presently pending or threatened in writing to be brought or filed with the National Labor Relations Board or any other labor relations tribunal or authority. To Sellers' Knowledge, there have been no labor union organizing activities with respect to any Project Employees or any employees of GenWest.

(d) From May 17, 2004, there has been no actual or, to Sellers' Knowledge, threatened, arbitrations, grievances, labor disputes, strikes, lockouts, slowdowns or work stoppages against or affecting GenWest or the Project.

(e) With respect to the Project Employees, none of Sellers, or their respective employees, agents or representatives have committed any material unfair labor practice as defined in the National Labor Relations Act.

(f) With respect to the Project Employees, Sellers are in compliance in all material respects with all applicable Laws relating to employment and employment practices, including, without limitation, all Laws respecting terms and conditions of employment, health and safety, wages and hours, child labor, immigration, employment discrimination, disability rights or benefits, equal opportunity, plant closures and layoffs, affirmative action, workers' compensation, labor relations, employee leave issues and unemployment insurance.

(g) With respect to the Project Employees, none of the Sellers are or have been: (i) a "contractor" or "subcontractor" (as defined by Executive Order 11246), (ii) required to comply with Executive Order 11246, or (iii) required to maintain an affirmative action plan.

(h) With respect to the Project Employees, Sellers are and have been in compliance in all material respects with all notice and other requirements under the Workers' Adjustment and Retraining Notification Act and any similar state or local law relating to plant closings and layoffs.

Section 3.1.19 Employee Matters. No claim is pending, or to Sellers' Knowledge threatened, in which any individual or Governmental Authority asserts, or in the case of any threatened claim, may assert, that any individual is or was an employee of GenWest. Neither Purchaser nor any of its Affiliates will incur any Liability under or otherwise in respect of any employee compensation or benefit plan, program, agreement or arrangement (including any employee benefit plan within the meaning of ERISA Section 3(3)) established or maintained by Sellers or their ERISA Affiliates. Each such plan, program, agreement or arrangement maintained in respect of any individual performing services in respect of the Facility or otherwise in respect of the Purchased Assets has been maintained substantially in accordance with its terms and applicable Law, including ERISA and the Code.

Section 3.1.20 Brokers. All negotiations relative to this Agreement and the transactions contemplated hereby have been carried out by Sellers directly with Purchaser without the intervention of any Person on behalf of Sellers in such manner as to give rise to any valid claim by any Person against Purchaser for a finder's fee, brokerage commission or similar payment.

Section 3.1.21 Intellectual Property. Section 3.1.21 Part A of Sellers' Disclosure Schedule sets forth a complete list of all Shared Intellectual Property and all Non-Shared Intellectual Property. GenWest owns all interest or has non-exclusive use rights in the Non-Shared Intellectual Property and an undivided 75% interest in such ownership in or rights to the Shared Intellectual Property. Except as set forth in Section 3.1.21 Part B of Sellers' Disclosure Schedule, none of the Sellers owns or otherwise has, and has not acquired specifically for the purposes of the Facility or the Purchased Assets, any right to use any Intellectual Property that is used in or is necessary, required or in the case of GenWest, beneficial for the ownership, operation or maintenance of the Facility as currently owned, operated and maintained, other than such as may be included in the Purchased Assets. Except as set forth in Section 3.1.21 of Sellers' Disclosure Schedule and except for the Excluded Assets that constitute Intellectual Property, the Intellectual Property conveyed to Purchaser pursuant hereto ("Transferred Intellectual Property") includes any and all Intellectual Property necessary for the ownership, operation or maintenance of the Facility as currently owned, operated and maintained. To Sellers' Knowledge, the ownership, operation and maintenance of the Facility as currently owned, operated and maintained does not infringe upon, misappropriate, or otherwise violate either directly or indirectly (such as through contributory infringement or inducement to infringe) any Intellectual Property rights of any third Person, and the Sellers have not received written notice by any Person of any pending or threatened claims, suits, actions, mediations, arbitrations, orders or other adversarial proceedings (a) alleging infringement, misappropriation or other violation by the Sellers of Intellectual Property rights of any Person or (b) challenging the Sellers' ownership or use of, or the validity, enforcement, registrability or maintenance of, any Transferred Intellectual Property. To Sellers' Knowledge, except as provided in the Assumed Agreements, none of the Sellers has entered into any consents, judgments, orders, indemnifications, forbearances to sue, settlement agreements, licenses or other arrangements which (i) restrict GenWest's right to use any Transferred Intellectual Property, (ii) restrict the transfer or licensing by GenWest of the Transferred Intellectual Property, (iii) restrict GenWest's business as it pertains to the Facility in order to accommodate a third Person's Intellectual Property rights, or (iv) permit any third Person to use any Transferred Intellectual Property. The intended use by the Sellers of any Transferred Intellectual Property is in accordance with any and all applicable

grants, licenses, agreements, instruments or other arrangements pursuant to which the Sellers acquired the right to use such Transferred Intellectual Property. Service and all other fees to be paid by Sellers with respect to the Transferred Intellectual Property have been paid as required to any Person.

Section 3.2 Representations and Warranties of Purchaser. Except as specifically set forth in the Purchaser's Disclosure Schedule attached hereto as Schedule VII, Purchaser hereby represents and warrants to Sellers that all of the statements contained in this Section 3.2 are true and correct as of the Effective Date (unless another date is expressly indicated), and will be true and correct as of the Closing Date as though made on and as of the Closing Date. Each exception and other response to this Agreement set forth in the Purchaser's Disclosure Schedule is identified by reference to, or has been grouped under a heading referring to, a specific individual section of this Agreement, and, except as otherwise specifically stated with respect to such exception, relates only to such section.

Section 3.2.1 Existence. Purchaser is a corporation, duly formed, validly existing and in good standing under the Laws of the State of Nevada and has full power and authority to conduct its business as it is now being conducted and to own, lease and operate its assets and properties.

Section 3.2.2 Authority. Purchaser has full power and authority to execute and deliver this Agreement and the Transaction Agreements to which it is or will be a party, to perform its obligations hereunder and thereunder and to consummate the transactions contemplated hereby and thereby. The execution and delivery by Purchaser of this Agreement and the Transaction Agreements to which it is or will be a party, and the performance by Purchaser of its obligations hereunder and thereunder, have been duly and validly authorized by all necessary corporate action.

Section 3.2.3 Binding Agreement. This Agreement and the Transaction Agreements to which Purchaser is or will be a party have been or will be when delivered duly and validly executed and delivered by Purchaser and, assuming due and valid authorization, execution and delivery thereof by Sellers and each other party thereto, this Agreement and the Transaction Agreements to which Purchaser is or will be a party are or will be when delivered valid and binding obligations of Purchaser enforceable against Purchaser in accordance with their terms, except (a) as limited by applicable bankruptcy, insolvency, reorganization, moratorium, fraudulent conveyance and other similar Laws of general application affecting enforcement of creditors' rights generally and, (b) general equitable principles, including that the availability of the remedy of specific performance or injunctive or other forms of equitable relief may be subject to equitable defenses and would be subject to the discretion of the court before which any proceeding therefor may be brought.

Section 3.2.4 No Conflicts. Subject to the receipt of the Required Consents, PUCN Approval, FERC Approval, and the expiration or early termination of the waiting period under the HSR Act, the execution and delivery by Purchaser of this Agreement do not, and the execution and delivery by Purchaser of the Transaction Agreements to which it is or will be a party, the performance by Purchaser of its obligations under this Agreement and such

Transaction Agreements and the consummation of the transactions contemplated hereby and thereby shall not:

(a) Conflict with or result in a violation or breach of any of the terms, conditions or provisions of Purchaser's articles of incorporation and by-laws;

(b) Result in a default (or give rise to any right of termination, cancellation or acceleration) under any of the terms, conditions or provisions of any note, bond, deed of trust, indenture, license, agreement, lease or other instrument or obligation to which Purchaser or any of its Affiliates is a party or by which any of their respective assets and properties may be bound, except for such defaults (or rights of termination, cancellation or acceleration) as to which requisite waivers or consents have been obtained in writing (true and correct copies of which waivers and consents have been furnished to Sellers); or

(c) Conflict with or result in a violation or breach of any term or provision of any Law applicable to Purchaser or any of its Affiliates or any of their respective assets and properties.

Section 3.2.5 Approvals and Filings. Except for the Required Consents, PUCN Approval, FERC Approval, and the expiration or early termination of the waiting period under the HSR Act, no consent or approval of, filing with or notice to any Governmental Authority or other Person is required in connection with the execution, delivery and performance by Purchaser of this Agreement or any of the Transaction Agreements to which it is a party or the consummation by Purchaser of the transactions contemplated hereby or thereby.

Section 3.2.6 Legal Proceedings. Except as set forth in Section 3.2.6 of Purchaser's Disclosure Schedule, there are no actions or proceedings (including orders, judgments and writs), and to Purchaser's Knowledge, no claims or investigations, outstanding or pending in any Governmental Authority to which Purchaser is a party or, to Purchaser's Knowledge, threatened against Purchaser or any of its assets and properties, which would be reasonably expected to result in the issuance of an order restraining, enjoining or otherwise prohibiting or making illegal the consummation of the transactions contemplated by this Agreement or any of the Transaction Agreements.

Section 3.2.7 Brokers. All negotiations relative to this Agreement and the transactions contemplated hereby have been carried out by Purchaser directly with Sellers without the intervention of any Person on behalf of Purchaser in such manner as to give rise to any valid claim by any Person against Sellers for a finder's fee, brokerage commission or similar payment.

ARTICLE IV

COVENANTS

Section 4.1 Efforts to Close and Fulfillment of Conditions. After the Effective Date and prior to Closing:

(a) Each Party shall use commercially reasonable efforts and proceed diligently and in good faith to take, or cause to be taken, all actions, and to do, or cause to be done, all things necessary, proper or advisable under Law to consummate and make effective the purchase, sale, assignment, conveyance, transfer and delivery of the Purchased Assets, the assumption of the Assumed Agreements pursuant to this Agreement, and the effectiveness of the Interim PPA. Such actions shall include each Party using its commercially reasonable efforts to ensure satisfaction of the conditions precedent to its obligations hereunder, as soon as practicable after the Effective Date.

(b) Each Party shall provide reasonable cooperation to the other Party in obtaining consents, approvals or actions of, making all filings with and giving all notices to Governmental Authorities or other Persons required of the other Party to consummate the transactions contemplated hereby and by the Transaction Agreements. The Parties shall use their commercially reasonable efforts to respond promptly and accurately to any requests for additional information made by any such Governmental Authority. The Parties agree that they shall consult with each other with respect to the transfer to Purchaser or the obtaining by Purchaser or the Sellers of FERC Approval, PUCN Approval, Permits, consents, approvals and authorizations of all third parties and Governmental Authorities, including the HSR Act filing.

(c) As promptly as practicable and, in any event, within 30 days after the Effective Date, Purchaser shall file with the PUCN all documents reasonably required to obtain the PUCN Approval. Purchaser shall use its commercially reasonable efforts to respond promptly and accurately to any requests for additional information made by the PUCN, and Sellers shall use its commercially reasonable efforts to cooperate with Purchaser in connection therewith. Purchaser shall consult with Sellers on all principal filings submitted by Purchaser to the PUCN in connection with the PUCN Approval. For the avoidance of doubt, Sellers shall not be entitled to receive any proprietary data related to current and forecasted operations of Purchaser, including production models, operating costs, and other similar information in connection with the preparation of the filing to the PUCN. Each Party shall bear its own costs and expenses of the preparation of such filing.

(d) At a time mutually agreed between Purchaser and Sellers, the Parties shall file with the FERC all documents reasonably required to obtain the FERC Approval. Each Party will bear its own costs and expenses of the preparation of such filing.

(e) At a time mutually agreed between Purchaser and Sellers, the Parties shall file or cause to be filed with the Federal Trade Commission and the United States Department of Justice all notifications required to be filed under the HSR Act and the rules and regulations promulgated thereunder, as amended from time to time, with respect to the transactions contemplated hereby. Each Party will bear its own costs and expenses of the preparation of such filing.

(f) Purchaser shall use commercially reasonable efforts to obtain the Financing. After the Effective Date and prior to Closing, Sellers shall use commercially reasonable efforts to assist Purchaser in connection with Purchaser's efforts to secure the Financing as follows: (i) by making all engineering and design materials related to the Facility or the Real Property available to Purchaser and its Related Persons as Purchaser reasonably

requests, (ii) by providing Purchaser and its Related Parties with access to the Facility, the Real Property, the Shared Books and Records and the Non-Shared Books and Records at all reasonable times, (iii) by making Sellers' personnel available to Purchaser and its Related Parties to provide information related to the Facility or the Real Property, including responding to questions and attending meetings as reasonably requested by Purchaser or its Related Parties, and (iv) by providing Purchaser and its Related Parties reasonable support with Sellers' suppliers, vendors and contractors to resolve technical and scope of supply issues related to the Facility by providing to Purchaser, when requested to do so by Purchaser, such existing information in connection with this Agreement and the Facility as may be reasonably required for any potential lender to Purchaser under a proposed financing arrangement; provided, however, that (A) any investigation shall be conducted after reasonable advance notice to Sellers and in such a manner as not to interfere unreasonably with the operation of the Purchased Assets, (B) Purchaser shall require each Person conducting or participating in any such investigation, including any Related Person, to comply with reasonably adopted procedures relating to safety and security, (C) Purchaser shall be required to indemnify Sellers for any damage to property or persons resulting from any such investigation to the extent that is the result of gross negligence or willful misconduct of Purchaser or its Related Persons and is not covered by insurance, (D) Sellers shall be entitled to have a representative present during the course of any such investigation, (E) the Sellers shall not be required to take any action which would constitute a waiver of the attorney-client privilege, and (F) Purchaser shall reimburse Sellers for any reasonable, out-of-pocket costs pre-approved by Purchaser and demonstrated to Purchaser's reasonable satisfaction that are incurred by Sellers in providing such assistance.

(g) Purchaser, at the cost and expense of the Sellers, in an amount not to exceed \$350,000, shall use commercially reasonable efforts to receive (i) on or before 30 days before the Closing Date, from the title company of Purchaser's choice a commitment for title insurance reasonably satisfactory to Purchaser (the "Title Insurance Commitment") and an ALTA/ACSM survey (the "Survey") of the Site prepared by a licensed professional surveyor selected by Purchaser, and (ii) on the Closing Date, a prepaid title insurance policy reasonably satisfactory to Purchaser (the "Title Insurance Policy"). Purchaser shall be responsible for the cost of the Title Insurance Commitment, resulting Title Insurance Policy, and the Survey in excess of such amount. Sellers shall remove or rectify prior to Closing as requested by Purchaser (i) any exceptions that appear in the Title Insurance Commitment (other than Permitted Liens and the standard pre-printed exceptions) that adversely affect the title to, or the proposed use and enjoyment of, the Site (the "Objectionable Title Matters"), or (ii) any easements, rights-of-way, encroachments, or other matters affecting the Site as shown by the Survey (other than Permitted Liens as shown by the Survey) that adversely affect the title to, or the proposed use and enjoyment of, the Site ("Objectionable Survey Matters"), which request must be provided within 15 Business Days of the later of the receipt of the Title Insurance Commitment or the Survey and be accompanied by the Title Insurance Commitment, the Survey and copies of any Objectionable Title Matters. In removing or rectifying such Objectionable Title Matters or Objectionable Survey Matters, Sellers shall not be obligated to expend an aggregate amount in excess of \$20,000,000 less the amount of any indemnities paid or payable by Sellers pursuant to Sections 4.2(d), 4.2(e) and 4.11(b)(iii); provided, however, that if the cost of removing or rectifying such Objectionable Title Matters or Objectionable Survey Matters exceeds \$20,000,000 less the amount of Losses described in Sections 4.2(d), 4.2(e) and 4.11(b)(iii) and such Objectionable Title Matters or Objectionable Survey Matters are not

removed or rectified, Sellers shall provide notice to Purchaser of such fact and Purchaser shall have the right to terminate this Agreement upon notice to Sellers, which right must be exercised within 20 Business Days following Purchaser's receipt of such notice from Sellers. Sellers agree to provide an indemnity in favor of Purchaser's title company for any Liens first appearing in public record or attaching subsequent to the effective date of the Title Insurance Commitment or related preliminary report which are caused by Sellers or within Sellers' Knowledge.

(h) Sellers shall use commercially reasonable efforts to obtain certificates, acknowledgements or undertakings reasonably requested by Purchaser from the following counterparties to the Assumed Agreements: SNWA, Kern River Transmission Company; Las Vegas Valley Water District; Siemens Westinghouse Power Corporation; Reliant Energy Services, Inc.; LG Constructors, Inc.; CH2M Hill Companies, Inc.; Southern California Edison Company; General Electric Company; Alstom Power, Inc.; Hamon Cooling Towers, Inc.; Hamon & Cie, S.A.; APS; Dry Lake Water, LLC; Mirant Las Vegas, LLC, and Gillard Construction, Inc. and any counterparty to a Post-Effective Date Assumed Joint Facility Agreement having a value exceeding \$100,000. Purchaser shall reimburse Sellers for any reasonable, out-of-pocket costs pre-approved by Purchaser and demonstrated to Purchaser's reasonable satisfaction that are incurred by Sellers in making such efforts.

(i) Sellers shall use commercially reasonable efforts to secure the Sellers' Releases as promptly as practicable after the Effective Date, but in any event within 45 days after the Effective Date ("Sellers' Releases Deadline"). If Sellers have not obtained the Sellers' Releases by the Sellers' Releases Deadline, Sellers shall have the right to terminate this Agreement by notice to Purchaser, which right must be exercised within 20 Business Days after the Sellers' Releases Deadline or it shall be deemed to be waived. If the Sellers' Releases are included in the Required Consents delivered at Closing, Purchaser shall not object to the Required Consents on the basis of such inclusion.

(j) Sellers shall use commercially reasonable efforts to execute the Dry Lake Documents as promptly as practicable after the Effective Date. If Sellers have not executed the Dry Lake Documents within 45 days after the Effective Date, Purchaser shall have the right to terminate this Agreement by notice to Sellers, which right must be exercised within 20 Business Days after the 45 days after the Effective Date, or it shall be deemed to be waived.

(k) Sellers shall use commercially reasonable efforts to obtain the SNWA Consent by September 30, 2005. If the SNWA Consent is not obtained by September 30, 2005, either Party shall have the right to terminate this Agreement by notice to the other Party, which right must be exercised within 20 Business Days after September 30, 2005 or it shall be deemed to be waived.

(l) Sellers, at the sole cost and expense of Sellers, shall use commercially reasonable efforts to obtain an ALTA/ACSM survey of the Site prepared by a licensed professional surveyor selected by Sellers as promptly as practicable following the Effective Date. The Parties shall consult with one another to determine whether a mutually acceptable surveyor could be used for such survey to also satisfy Purchaser's requirement to obtain a Survey pursuant to Section 4.1(g)(ii). If, following Sellers' review of such survey, Sellers conclude that the cost of removing or rectifying any easements, rights-of-way, encroachments, or other matters

affecting the Site that adversely affect the title to, or the proposed use and enjoyment of, the Site is reasonably expected by Sellers to exceed \$5,000,000, Sellers shall have the right to terminate this Agreement by notice to Purchaser, which right must be exercised within 60 days after the Effective Date. During such 60-day period, the Parties will consult regarding the extent of, and the potential remedies associated with, any adverse title matters reflected on the survey. The matters disclosed in the letter from HMM, Inc. dated May 13, 2004, attached as Exhibit 1 to Schedule III, shall be permitted exceptions to the survey obtained pursuant to this Section 4.1(1), as well as to the Survey to be obtained pursuant to Section 4.1(g)(ii), and shall not be deemed to be Objectionable Title Matters or Objectionable Survey Matters.

(m) Sellers shall use commercially reasonable efforts to correct the Site Description Error prior to Closing.

(n) To the extent that any portion of the as-built drainage improvements or rip-rap relating to the drainage improvements on the Site made pursuant to that certain Grant of Public Underground Drainage Easement in favor of County of Clark, recorded August 6, 2002, in Book 20020806 as Document No. 01065 of Official Records, is outside the Real Property, Sellers shall use commercially reasonable efforts to obtain an easement or other appropriate authorization for the same or to remove the encroachment. To the extent that any portion of such as-built drainage improvements or rip-rap within the Easements is not permitted by the Easements, Sellers shall use commercially reasonable efforts to either amend the Easements or to obtain new easements or other appropriate authorization to allow the as-built drainage improvements or rip-rap to remain within the Easements.

(o) Sellers shall use commercially reasonable efforts to execute the cover letter to BLM and submit to BLM the Request for Assignment of BLM Right of Way Grant Serial No. N-75607, issued by the BLM to GenWest on May 9, 2002 and BLM Right of Way Grant Serial No. N-75840, issued by BLM to GenWest on May 9, 2002, as soon as reasonably practicable after the Effective Date, in a form mutually agreed to by the Parties.

(p) Each Party shall give notice to the other promptly after becoming aware of (i) the occurrence or non-occurrence of any event whose occurrence or non-occurrence would be likely to cause any representation or warranty contained in this Agreement to be untrue or inaccurate in any material respect at any time from the Effective Date to the Closing Date and (ii) any failure of a Party to comply with or satisfy any covenant, condition or agreement to be complied with or satisfied by it hereunder; provided, however, that the delivery of any notice pursuant to this section shall not limit or otherwise affect the remedies available hereunder to the Party receiving such notice.

(q) Each of the Sellers and Purchaser agree to use reasonable endeavors to refrain from taking any action which could reasonably be expected to materially delay the consummation of the transactions contemplated by this Agreement.

(r) No separate consent by Purchaser under any agreement to which Purchaser and any Seller is party that is required to consummate the transactions contemplated by this Agreement and the assignment and assumption of the Assumed Agreements shall be required from Purchaser and by its execution and delivery of this Agreement, Purchaser hereby

grants each such consent. To the extent that at the Closing Purchaser assumes obligations of Sellers to Purchaser under Assumed Agreements to which Purchaser is a counterparty, Purchaser hereby releases Sellers from such obligations effective as of the Closing.

Section 4.2 Operation and Maintenance of Purchased Assets.

(a) After the Effective Date and prior to Closing, the Sellers shall operate and maintain the Facility in accordance with Sections 4.1, 4.2, 4.3, 4.5.2, 4.6, and 9.1 of the Co-Tenancy Agreement and otherwise in the ordinary course, consistent with past practices, methods, techniques and standards; provided, however, that with respect to Section 4.3.1 and Section 4.5.2 of the Co-Tenancy Agreement, the Sellers shall only be required to comply in all material respects.

(b) After the Effective Date and prior to Closing, the Sellers shall not, without the written consent of Purchaser:

(i) dispose of or assign any of the Purchased Assets, except to the extent permitted by the Co-Tenancy Agreement and the O&M Agreement; provided, however, that (y) the original value of such Purchased Assets, other than such Purchased Assets suffering loss, damage, other casualty or breakage, to which Section 4.9 applies, and other than assets replaced as part of routine maintenance or under the Long Term Maintenance Agreement by assets of comparable or superior quality and value, does not exceed \$6,000,000 in the aggregate and (z) Sellers' share of any consideration received by the Sellers in connection with such disposition or assignment shall be paid to Purchaser at Closing;

(ii) incur or permit to exist any Lien on any of the Purchased Assets, other than the Permitted Liens and Liens on the Easements permitted by Section 3.1.11(a);

(iii) enter into, amend, modify, terminate, grant any waiver under or give any consent or settle or compromise any claim with respect to (A) any Designated Assumed Agreement except for amendments constituting the Contemplated Assumed Agreement Amendments, or (B) any other Facility Agreements, except in the case of this clause (B), for any agreements, amendments, modifications, terminations, waivers, consents, settlements or compromises (w) necessary or appropriate to close out and settle any matters under the Construction and Equipment Supply Contracts, including any release or reduction in the Existing Letters of Credit, to the extent consistent with the Co-Tenancy Agreement and the O&M Agreement, other than any modification of paragraphs SC3 and SC4 in the Supplemental Terms and Conditions to the Alstom Agreement, (x) required by Law, in which event Section 4.2(e) shall apply, (y) entered into or made in the ordinary course of business, consistent with past practices, the Co-Tenancy Agreement and the O&M Agreement and that (1) do not require payments or have contingent liabilities, other than customary indemnity obligations, after Closing in the aggregate in excess of \$100,000, or (2) are terminated by the Sellers prior to Closing without any cost to or Liability of Purchaser or adverse effect on the Purchased Assets, or (z) with respect to modifications to GenWest Agreements existing as of the Effective Date, other than Assumed GenWest Agreements, entered into or made in the ordinary course of business and that do not adversely affect the Purchased Assets;

(iv) permit to lapse any rights to any Transferred Intellectual Property, except to the extent such rights are not required to fulfill Sellers' obligations pursuant to this Section 4.2;

(v) make any material modification to the Facility or the Real Property;

(vi) adopt a plan of complete or partial liquidation, dissolution, merger or consolidation, or with respect to PWCC and GenWest, sell or convey all or substantially all of its assets to any Person or with respect to PWCC and PWEC transfer its interest in GenWest; provided, however, that PWCC or PWEC may merge or consolidate with, and PWCC may sell or convey all or substantially all of their assets to any Person, provided that PWCC or PWEC, as the case may be, shall be the continuing corporation, or the successor corporation (if other than PWCC or PWEC, as the case may be) or the purchaser or assignee of all or substantially all of PWCC's assets shall be an entity organized and existing under the Laws of the United States of America or a state thereof, or the District of Columbia and such entity shall expressly assume the due and punctual performance and observance of all of the covenants and conditions to be performed by PWCC or PWEC, as the case may be, hereunder, by supplemental agreement in form reasonably satisfactory to Purchaser;

(vii) settle or compromise any litigation which could result in any cost to or liability of Purchaser or adverse effect on the Purchased Assets;

(viii) make any material change in the levels of Stores and Inventory maintained at the Facility for the applicable time of the year, except in the ordinary course of business, consistent with past practices and pursuant to the Co-Tenancy Agreement and the O&M Agreement; provided, however, that nothing in this provision shall require Sellers to maintain Stores and Inventory with a cost in excess of the Stores and Inventory Cap Amount;

(ix) modify or amend any Transferred Permit except as required by Law, in which event Section 4.2(e) shall apply; or

(x) enter into any agreement to do or engage in any of the foregoing.

(c) Notwithstanding anything in Section 4.2(b), Sellers may take any action (x) required to comply with the Co-Tenancy Agreement and the O&M Agreement or (y) that in Sellers' reasonable judgment is required or appropriate in connection with the ownership, operation and maintenance of the Project and that is in accordance with the Co-Tenancy Agreement and the O&M Agreement. With respect to any such actions taken outside the ordinary course of business or which may result in any non-compliance with Section 4.2(a) or (b) or any other provision of this Agreement (each a "Section 4.2(d) Action"), the provisions of Section 4.2(d) shall apply. Subject to compliance with Section 4.2(d), no action taken in accordance with this Section 4.2(c) shall be deemed to be a breach of this Agreement, including for purposes of Section 5.1.2.

(d) If Sellers take any Section 4.2(d) Action, Sellers shall promptly give notice thereof to Purchaser, which notice shall describe the action taken in detail. Sellers shall

indemnify Purchaser for all Losses including any adverse impact on, or any diminution in value of, the Purchased Assets attributable to such Section 4.2(d) Action, up to an aggregate amount equal to \$20,000,000 less any amounts paid or payable by Sellers pursuant to Sections 4.1(g), 4.2(e) and 4.11(b)(iii). If Purchaser reasonably expects such Losses, including such adverse impact or diminution in value, to exceed an amount equal to \$20,000,000 less the amount of Losses described in Sections 4.1(g), 4.2(e) and 4.11(b)(iii), Purchaser shall have the right to terminate this Agreement, which right must be exercised within 20 Business Days of receipt of notice of such action from the Sellers or such right shall be deemed waived.

(e) If any action is taken by Sellers which is expressly permitted by Section 4.2(b)(iii)(B)(x), or Section 4.2(b)(ix), Sellers shall promptly give notice thereof to Purchaser, which notice shall describe the action taken in detail. Sellers shall indemnify Purchaser for all Losses including any adverse impact on, or any diminution in value of, the Purchased Assets attributable to such action, up to an aggregate amount equal to \$10,000,000 less any amounts paid or payable by Sellers pursuant to Sections 4.1(g), 4.2(d) and 4.11(b)(iii). If Purchaser reasonably expects such Losses, including such adverse impact or diminution in value, to exceed an amount equal to \$10,000,000 less the amount of Losses described in Sections 4.1(g), 4.2(d) and 4.11(b)(iii), Purchaser shall have the right to terminate this Agreement upon notice to Sellers, which right must be exercised within 20 Business Days of receipt of notice of such action from the Sellers or such right shall be deemed waived.

(f) All notices of Sellers and requests by Sellers for consent or other action by Purchaser pursuant to this Section 4.2, other than pursuant to Section 4.2(d) and 4.2(e), and all responses of Purchaser pursuant thereto shall be made in writing to or by a Purchaser Consent Representative.

Section 4.3 Purchaser's Inspection Right. After the Effective Date and prior to Closing, Purchaser and its Related Persons shall have access, upon reasonable prior notice, to the Site and, if requested, to the Shared Books and Records and the Non-Shared Books and Records, all for purposes of inspection and review; provided, however, that (a) any investigation shall be conducted in such manner as not to interfere unreasonably with the operation of the Purchased Assets and with reasonable advance notice to Sellers, (b) Purchaser shall require each Person conducting or participating in any such investigation to comply with reasonably adopted procedures relating to safety and security, (c) Purchaser shall indemnify Sellers for any damage to property or persons resulting from any such investigation that is the result of gross negligence or willful misconduct of Purchaser or its Related Person and is not covered by insurance, (d) Sellers shall be entitled to have a representative present during the course of any such investigation, (e) the Sellers shall not be required to take any action that would constitute a waiver of the attorney-client privilege, and (f) Purchaser shall reimburse Sellers for the reasonable out-of-pocket costs pre-approved by Purchaser and demonstrated to Purchaser's reasonable satisfaction that are incurred by Sellers in providing such assistance.

Section 4.4 Intentionally Omitted.

Section 4.5 Cooperation with Facility Takeover and Transition of Operations. Within 30 days after the Effective Date, Purchaser shall deliver to Sellers a list of its proposed representatives to the joint transition team. Sellers will add its representatives to such team

within five Business Days after receipt of Purchaser's list. Such team will be responsible for preparing as soon as reasonably practicable after the Effective Date, and timely implementing, a transition plan which will identify and describe substantially all of the various transition activities that the Parties will cause to occur before and after the Closing and any other transfer of control matters that any Party reasonably believes should be addressed in such transition plan. Purchaser and Sellers shall use commercially reasonable efforts to cause their representatives on such transition team to cooperate in good faith and take all reasonable steps necessary to develop a mutually acceptable transition plan no later than 60 days after the Effective Date.

Section 4.6 Interim PPA. Concurrent with the execution and delivery of this Agreement, GenWest and Purchaser shall enter into the Interim PPA, substantially in the form of Exhibit K.

Section 4.7 Cooperation in Fault Current Upgrade Proceedings. During the period after the Effective Date and until Closing, Sellers shall consult with Purchaser regarding positions taken in proceedings involving the Fault Current Upgrade MOUs, including in FERC Dockets TX03-1, ER02-1741, ER02-1742, ER04-152, ER04-424, and ER02-2344.

Section 4.8 Employees. Purchaser may, but shall not be required to, offer employment to some, all or none of the Project Employees effective immediately after the Closing on terms and conditions determined by Purchaser in its sole discretion. Sellers shall provide Purchaser and its representatives reasonable access to the Project Employees to assist Purchaser in determining to which Project Employees, if any, it shall make such offers of employment, and, not less than 30 days before the Closing, to the extent permitted by applicable Law, Sellers shall provide Purchaser with the Project Employee Books and Records (to the extent they may be provided to Purchaser in accordance with Law and with respect to such Project Employees who consent thereto) to assist Purchaser in such determination.

Section 4.9 Risk of Loss. Prior to the effectiveness of Closing, all risk of loss, damage or other casualty to the Purchased Assets shall be borne by Sellers and Sellers shall promptly notify Purchasers of any such loss, damage or casualty or any other change in condition of the Purchased Assets that may lead to such loss, damage or other casualty. Sellers shall repair prior to the Closing Date to the previous condition of the Purchased Assets any such damage, loss or casualty to the Purchased Assets, or breakage of any component or components of the Purchased Assets in an aggregate amount up to \$20,000,000 less the amount of any indemnities paid or payable by Sellers under Section 4.11(b)(iii); provided, however, that any such event of damage, loss, casualty, or breakage less than \$500,000 shall not be counted towards such limit; provided further, however that if the aggregate amount of such damage, loss or breakage exceeds \$6,000,000 or an amount equal to \$20,000,000 less the amount of any indemnities paid or payable by Sellers under Section 4.11(b)(iii), and the Parties are unable to reach an agreement on a remedy for such damage, loss or breakage after 30 days of the occurrence of such loss, damage or breakage, Purchaser shall have the right to terminate this Agreement upon notice to Sellers, which right must be exercised within 20 Business Days of the end of such 30 day period or such right shall be deemed waived.

Section 4.10 Interim Reports. In connection with the continuing operation of the Facility, the Sellers shall use reasonable endeavors between the Effective Date and Closing to

consult in good faith on a regular and frequent basis with Purchaser and its representatives to report material operational developments and the general status of ongoing operations pursuant to procedures reasonably requested by Purchaser or such representatives. The Sellers acknowledge that any such consultation shall not constitute a waiver by Purchaser of any rights it may have under this Agreement or any other Transaction Agreement, and that Purchaser shall not have any Liability or responsibility for any actions of any Seller, or any of their respective officers, directors, employees or agents with respect to matters that are the subject of such consultations.

Section 4.11 Notification of Actions Taken; Update of Schedules.

(a) Sellers shall promptly notify Purchaser in the event Sellers enter into, amend, modify, terminate, grant any waiver under or give any consent or settle or compromise any claim with respect to any Facility Agreement or Permit after the Effective Date. Sellers shall provide Purchaser with copies of any such revised Facility Agreements or Permits as requested by Purchaser. Each Facility Agreement or amendment thereto that (i) is executed after the Effective Date, (ii) meets the requirements of Section 4.2(b)(iii)(A), Section 4.2(b)(iii)(B)(w), (x), or (y) or Section 4.2(c), (iii) has a term extending beyond the Closing Date, and (iv) constitutes a Joint Facility Agreement shall be an Assumed Agreement (the "Post-Effective Date Assumed Joint Facility Agreements"); provided, however, that Sellers shall pay prior to Closing, to the extent reasonably practicable, or otherwise as soon as reasonably practicable after Closing, for any Materials and Equipment purchased and delivered or services rendered prior to Closing. Any consent required to assign any such Post-Effective Date Assumed Joint Facility Agreement to Purchaser shall be a Required Consent. Sellers shall provide Purchaser with any new Permit obtained by Sellers after the Effective Date (the "Post-Effective Date Permits") promptly after receipt thereof. Each such Permit that (i) is entered into for the joint benefit of GenWest and SNWA and (ii) is requested by Purchaser to be transferred or is required by Law shall be a Transferred Permit to the extent permitted by Law. Prior to Closing or upon the request of either Party, the Parties shall update Schedule I (Assumed Agreements), Schedule II (Materials and Equipment) and Schedule IV (Transferred Permits) to reflect any changes in Assumed Agreements, Materials and Equipment and Transferred Permits pursuant to this Section 4.11.

(b) If Sellers become aware at any time before the Closing Date that a Sellers' Disclosure Schedule previously delivered by Sellers was inaccurate or incomplete when delivered or has become inaccurate or incomplete as a result of subsequent events, Sellers shall promptly deliver to Purchaser no later than 10 Business Days after such discovery an amendment or supplement to such schedule and any related documents; provided, however, that:

(i) if such amendment or supplement is based on events or matters that arose on or before the Effective Date, such amendment or supplement shall not be given effect for the purposes of determining the fulfillment of the condition precedent set forth in Section 5.1.1 or liability as set forth in Section 7.1(a) and (b) and the Sellers' Disclosure Schedule shall not be read for any purposes as so amended or supplemented;

(ii) if such amendment or supplement is based on events or matters that arise after the Effective Date and that are expressly permitted to occur under Section 4.2(b), or Section 4.2(c), such amendment or supplement shall be given effect for the purposes of

determining the fulfillment of the condition precedent set forth in Section 5.1.1 or determining liability as set forth in Section 7.1(a) and (b) and the Sellers' Disclosure Schedule shall be read for all purposes as so amended or supplemented;

(iii) if such amendment or supplement is based on events or matters that arise after the Effective Date, such events or matters are not expressly permitted under Section 4.2(b), or Section 4.2(c), and such events or matters result in Losses to the Purchaser Indemnified Parties, including any adverse impact on, or diminution in value of, the Purchased Assets, equal to or less than an aggregate amount equal to \$20,000,000 less any amounts paid or payable by Sellers pursuant to Sections 4.1(g), 4.2(d), 4.2(e), and 4.9, Sellers shall indemnify the Purchaser Indemnified Parties for all such Losses with respect to such events or matters and such amendment or supplement shall be given effect for purposes of determining the fulfillment of the condition precedent set forth in Section 5.1.1 or determining liability as set forth in Section 7.1(a) and (b) and the Sellers' Disclosure Schedule shall be read for all purposes as so amended or supplemented; provided, however, that if the amount of such Loss exceeds or is reasonably expected by Purchaser to exceed an aggregate amount equal to \$20,000,000 less the amount of Losses described in Sections 4.1(g), 4.2(d), 4.2(e) and 4.9, Purchaser shall have the right to terminate this Agreement upon notice to Sellers, which right must be exercised within 20 Business Days of receipt of such amendment or supplement from the Sellers or such right shall be deemed waived; provided further, if such right is waived, Sellers shall indemnify the Purchaser Indemnified Parties for all such Losses with respect to such events or matters, up to an amount equal to \$20,000,000 less any amounts paid or payable by Sellers pursuant to Sections 4.1(g), 4.2(d), 4.2(e) and 4.9, and such amendment or supplement shall be given effect for purposes of determining the fulfillment of the condition precedent set forth in Section 5.1.1 or determining liability as set forth in Section 7.1(a) and (b) and the Sellers' Disclosure Schedule shall be read for all purposes as so amended or supplemented.

Section 4.12 Exercise of Discretion. Promptly upon receipt of the PUCN Approval and the FERC Approval, but in each case no later than 15 Business Days after such receipt, Purchaser or Sellers, as applicable, shall give notice to the other of its approval or disapproval of the PUCN Approval or the terms of the FERC Approval that impose obligations on such Party or in respect of its assets, as the case may be. If no notice of disapproval is given within the time period specified above, Purchaser or Sellers, as applicable, will be deemed to have approved the PUCN Approval or the FERC Approval, as the case may be. In the event that any such Party shall give notice of disapproval of any such matter, as applicable, either Party hereto may give notice of the termination of this Agreement within ten (10) Business Days after such notice of disapproval is received.

Section 4.13 Cure of Material Adverse Effect. If a Material Adverse Effect shall have occurred and Sellers shall give notice to Purchaser that such Material Adverse Effect has been cured, Purchaser shall have 20 Business Days to determine whether such Material Adverse Effect has been cured to its sole satisfaction. If Purchaser has not given written notice to Sellers of its dissatisfaction with such cure within the time period specified above, Purchaser shall be deemed to be satisfied with such cure.

Section 4.14 No Solicitation of Competing Transaction. After the Effective Date and prior to Closing, Sellers shall not, directly or indirectly, solicit, initiate or participate in

discussions or negotiations with, any Person or group (other than Purchaser, any of its Affiliates or representatives) concerning any Acquisition Proposal. The Sellers shall not, and shall cause each Affiliate not to, enter into any agreement with respect to any Acquisition Proposal. The Sellers shall immediately notify, and shall cause the Affiliates to notify, Purchaser of any unsolicited proposal or inquiry, or amendment to any existing proposal or inquiry, received by Sellers and the Sellers shall immediately communicate to Purchaser, or cause the Affiliates to communicate to Purchaser, the terms of any unsolicited proposal or inquiry, or amendment to any existing proposal or inquiry, which any of them may receive in connection with such unsolicited proposal or inquiry or amendment to such existing proposal or inquiry.

ARTICLE V

CONDITIONS TO CLOSING

Section 5.1 Purchaser's Conditions Precedent. The obligations of Purchaser hereunder to execute or deliver the items it is required to deliver pursuant to Section 2.4.1(a) are subject to the fulfillment to the reasonable satisfaction of Purchaser, at or before the Closing, of each of the following conditions (all or any of which may be waived in whole or in part by Purchaser in its sole discretion):

Section 5.1.1 Representations and Warranties. Each of the representations and warranties made by Sellers in this Agreement and qualified by materiality or Sellers' Knowledge, shall be true and correct on and as of the Closing Date as though made on and as of the Closing Date. Each of the representations and warranties made by Sellers in this Agreement and not qualified by materiality or Sellers' Knowledge shall be true in all material respects on and as of the Closing Date as though made on and as of the Closing Date.

Section 5.1.2 Performance. Sellers shall have performed and complied with the agreements, covenants and obligations required by this Agreement to be so performed or complied with by Sellers at or before the Closing.

Section 5.1.3 Law. There shall not be in effect on the Closing Date any Law restraining, enjoining or otherwise prohibiting or making illegal the consummation of the transactions contemplated by this Agreement.

Section 5.1.4 PUCN Approval; FERC Approval; HSR Act Filing. The PUCN Approval and the FERC Approval shall have been duly obtained, made or given and shall be in full force and effect, and all terminations or expirations of the waiting period under the HSR Act necessary for the consummation of the transactions contemplated by this Agreement shall have occurred.

Section 5.1.5 Required Consents. The Required Consents shall have been duly obtained, made or given and shall be in full force and effect.

Section 5.1.6 Deliveries. Sellers shall have executed and delivered to Purchaser, or shall be standing ready to execute and deliver to Purchaser at the Closing the items set forth in Section 2.4.1(b) of this Agreement.

Section 5.1.7 Financing. On or before the Closing Date, Purchaser shall have obtained Financing.

Section 5.1.8 Material Adverse Effect. No Material Adverse Effect shall have occurred, which has not been cured by Sellers prior to the Closing Date to Purchaser's sole satisfaction.

Section 5.1.9 Title Insurance, Survey and Title Insurance Policy. Purchaser shall have received the Title Insurance Commitment, the Survey, and the Title Insurance Policy as contemplated by Section 4.1(g) and Sellers shall have remedied all Objectionable Title Matters and all Objectionable Survey Matters to Purchaser's satisfaction.

Section 5.1.10 Transferred Permits. Sellers shall have taken all actions to properly transfer to Purchaser their interest in the Transferred Permits, and Sellers' interests in the Transferred Permits listed on Part C of Schedule IV shall have been transferred to Purchaser. None of the Transferred Permits shall be subject to any conditions or stipulations that did not exist as of the Effective Date which could reasonably be expected to have an adverse effect on Purchaser or the ownership, operation or maintenance of the Facility or the Real Property.

Section 5.1.11 Mirant Back-Up Well Arrangements. The Sellers and Mirant Las Vegas, LLC shall have executed the Mirant Back-Up Well Arrangements.

Section 5.1.12 Water Permit. The Water Permit shall have been duly obtained if the Closing Date occurs after June 16, 2006.

Section 5.2 Sellers' Conditions Precedent. The obligations of Sellers hereunder to execute or deliver the items they are required to deliver pursuant to Section 2.4.1(b) of this Agreement are subject to the fulfillment, to the reasonable satisfaction of Sellers at or before the Closing, of each of the following conditions (all or any of which may be waived in whole or in part by Sellers in their sole discretion):

Section 5.2.1 Representations and Warranties. Each of the representations and warranties made by Purchaser in this Agreement and qualified by materiality or Purchaser's Knowledge, shall be true and correct on and as of the Closing Date as though made on and as of the Closing Date. Each of the representations and warranties made by Purchaser in this Agreement and not qualified by materiality or Purchaser's Knowledge shall be true in all material respects on and as of the Closing Date as though made on and as of the Closing Date.

Section 5.2.2 Performance. Purchaser shall have performed and complied with the agreements, covenants and obligations required by this Agreement to be so performed or complied with by Purchaser at or before the Closing.

Section 5.2.3 Law. There shall not be in effect on the Closing Date any Law restraining, enjoining or otherwise prohibiting or making illegal the consummation of the transactions contemplated by this Agreement.

Section 5.2.4 PUCN Approval; FERC Approval; HSR Act Filing. The PUCN Approval and the FERC Approval shall have been duly obtained, made or given and shall be in

full force and effect, and all terminations or expirations of waiting period imposed under the HSR Act necessary for the consummation of the transactions contemplated by this Agreement shall have occurred.

Section 5.2.5 Required Consents. The Required Consents shall have been duly obtained, made or given and shall be in full force and effect.

Section 5.2.6 Deliveries. Purchaser shall have executed and delivered to Sellers, or shall be standing ready to execute and deliver to Sellers at the Closing, the items set forth in Section 2.4.1(a) of this Agreement.

ARTICLE VI

TERMINATION

Section 6.1 Termination Prior to Closing. This Agreement may be terminated, and the transactions contemplated hereby may be abandoned:

(a) At any time before the Closing, by Sellers or Purchaser upon notice to the other Party, in the event that any non-appealable Law becomes effective restraining, enjoining, or otherwise prohibiting or making illegal the consummation of the transactions contemplated by this Agreement;

(b) At any time before Closing as provided in Section 4.1(g), Section 4.1(i), Section 4.1(j), Section 4.1(k), Section 4.1(l), Section 4.2(d), Section 4.2(e), Section 4.9, Section 4.11(b)(iii), or Section 4.12;

(c) At any time before the Closing, by Sellers or Purchaser upon notice to the other Party, in the event (i) of a breach hereof by the non-terminating Party which gives rise to (A) a Material Adverse Effect or (B) a material adverse effect on (1) the ability of Purchaser to perform its obligations under this Agreement or (2) the validity or enforceability of the rights and remedies of any Seller under this Agreement or under any of the other Transaction Agreements if, in the case of both clause (A) and (B), the non-terminating Party fails to cure such breach within 30 days following notification thereof by the terminating Party; provided, however, that if, at the end of such 30-day period, the non-terminating Party is endeavoring in good faith, and proceeding diligently, to cure such breach, the non-terminating Party shall have an additional 30 days in which to effect such cure; or (ii) that any condition to such Party's obligations under this Agreement (other than the payment of money to the other Party) becomes impossible or impracticable to satisfy with the use of commercially reasonable efforts if such impossibility or impracticability is not caused by a breach hereof by such Party; provided, however, that if it is reasonably possible that the circumstances giving rise to the impossibility or impracticability may be removed prior to the expiration of the time period provided in this Section 6.1(c) of this Agreement, then such notification may not be given until such time as the removal of such circumstances is no longer reasonably possible within such time period;

(d) At any time following September 30, 2006, by Sellers or Purchaser upon notice to the other Party if the Closing shall not have occurred on or before such date and

such failure to consummate is not caused by a breach of this Agreement by the terminating Party; or

(e) At any time following November 1, 2005, by Sellers or Purchaser upon notice to the other Party if the PUCN Approval has not been obtained permitting the Service Term (as defined in the Interim PPA) of the Interim PPA to commence.

Section 6.2 Effect of Termination or Breach Prior to Closing.

(a) If this Agreement is validly terminated pursuant to Section 6.1(a), Section 6.1(b), Section 6.1(c)(ii), Section 6.1(d), or Section 6.1(e) of this Agreement, there shall be no liability or obligation on the part of Sellers or Purchaser (or any of their respective Related Persons), except that the provisions of clause (C) of Section 4.1(f), clause (c) of Section 4.3, ARTICLE X (Dispute Resolution), ARTICLE XI (Limited Remedies and Damages), Section 12.1 (Notices), Section 12.2 (Payments), Section 12.3 (Entire Agreement), Section 12.4 (Expenses), Section 12.5 (Public Announcements), Section 12.6 (Confidentiality), Section 12.9 (No Construction Against Drafting Party), Section 12.10 (No Third Party Beneficiary), Section 12.11 (Headings), Section 12.12 (Invalid Provisions), Section 12.13 (Governing Law), Section 12.14 (No Assignment; Binding Effect), and this Section 6.2 shall continue to apply following any such termination.

(b) If this Agreement is validly terminated pursuant to Section 6.1(c)(i) of this Agreement, by Purchaser or Sellers as a result of a breach by the non-terminating Party, such termination shall be the sole remedy of the terminating Party; provided that if such breach results from a material and willful breach by the non-terminating Party of this Agreement, then subject to Section 11.2 and notwithstanding any other provision of this Agreement to the contrary, the non-terminating Party and the terminating Party shall be entitled to all rights and remedies available to it.

ARTICLE VII

INDEMNIFICATION

Section 7.1 Indemnification by Sellers. Subject to the limitations set forth in Section 6.2 (Effect of Termination or Breach Prior to Closing), Section 7.4 (Limitations of Liability), Section 8.4 (Sellers' Tax Indemnification), Section 9.1 (Survival), and Section 11.2 (Limitation of Liability) of this Agreement, Sellers agree to indemnify and hold Purchaser and its Related Persons specified in clause (i) of the definition of such term (each, a "Purchaser Indemnified Party"), harmless from and against (and to reimburse each Purchaser Indemnified Party as the same are incurred for) any and all Losses incurred by any Purchaser Indemnified Party resulting from any of the following:

(a) any inaccuracy or breach of a representation or warranty made by Sellers in this Agreement;

(b) the breach by Sellers of, or default in the performance by Sellers of, any covenant, agreement or obligation to be performed by Sellers pursuant to this Agreement or any of the other Transaction Agreements; or

(c) the Excluded Assets or the Excluded Liabilities.

Section 7.2 Indemnification by Purchaser. Subject to the limitations set forth in Section 6.2 (Effect of Termination or Breach Prior to Closing), Section 7.4 (Limitations of Liability), Section 8.5 (Purchaser's Tax Indemnification), Section 9.1 (Survival), and Section 11.2 (Limitation of Liability) of this Agreement, Purchaser hereby agrees to indemnify and hold Sellers and their Related Persons (each, a "Sellers' Indemnified Party"), harmless from and against (and to reimburse each Sellers' Indemnified Party as the same are incurred for) any and all Losses incurred by any Sellers' Indemnified Party resulting from any of the following:

(a) any inaccuracy or breach of a representation or warranty made by Purchaser in this Agreement;

(b) the breach by Purchaser of, or default in the performance by Purchaser of, any covenant, agreement or obligation to be performed by Purchaser pursuant to this Agreement or any of the other Transaction Agreements; or

(c) liability assumed by Purchaser under Assumed Agreements pursuant to Section 2.1.2.

Section 7.3 Method of Asserting Claims.

Section 7.3.1 Notification of Claims. If any Purchaser Indemnified Party or Sellers' Indemnified Party (each, an "Indemnified Party") asserts that a Party has become obligated to the Indemnified Party pursuant to Section 4.1(f)(C), Section 4.2(d), Section 4.2(e), Section 4.3(c), Section 4.11(b)(iii), Section 7.1 or Section 7.2 (as so obligated, an "Indemnifying Party"), or if any suit, action, investigation, claim or proceeding is begun, made or instituted as a result of which the Indemnifying Party may become obligated to the Indemnified Party hereunder, the Indemnified Party shall notify the Indemnifying Party promptly and shall cooperate with the Indemnifying Party, at the Indemnifying Party's expense, to the extent reasonably necessary for the resolution of such claim or in the defense of such suit, action or proceeding, including making available any information, documents and things in the possession of the Indemnified Party. Notwithstanding the foregoing notice requirement, the right to indemnification hereunder shall not be affected by any failure to give, or delay in giving, notice unless, and only to the extent that, the rights and remedies of the Indemnifying Party shall have been materially prejudiced as a result of such failure or delay. Any assertion by an Indemnified Party that an Indemnifying Party is liable to the Indemnified Party for indemnification pursuant to Section 7.1 or Section 7.2 above must be delivered to the Indemnifying Party prior to the expiration date (if applicable) of the representation, warranty, covenant, or agreement giving rise to such indemnification obligation, as provided in Section 9.1.

Section 7.3.2 Defense of Claims. In fulfilling its obligations under this Section 7.3, after the Indemnifying Party has provided each Indemnified Party with a written notice of its agreement to indemnify each Indemnified Party under this Section 7.3, as between such Indemnified Party and the Indemnifying Party, the Indemnifying Party shall have the right to investigate, defend, settle or otherwise handle, with the aforesaid cooperation, any claim, suit, action or proceeding, brought by a third party in such manner as the Indemnifying Party may

reasonably deem appropriate; provided, that (i) counsel retained by the Indemnifying Party is reasonably satisfactory to the Indemnified Party, (ii) the Indemnifying Party will not consent to any settlement or entry of judgment imposing any obligations on any Indemnified Parties, other than financial obligations for which such Person will be indemnified hereunder, unless such Person has consented in writing to such settlement or judgment (which consent may be given or withheld in its sole discretion), and (iii) the Indemnifying Party will not consent to any settlement or entry of judgment unless, in connection therewith, the Indemnifying Party obtains a full and unconditional release of the Indemnified Party from all liability with respect to such suit, action, investigation, claim or proceeding. Notwithstanding the Indemnifying Party's election to assume the defense or investigation of such claim, action or proceeding, the Indemnified Party shall have the right to employ separate counsel and to participate in the defense or investigation of such claim, action or proceeding, which participation shall be at the expense of the Indemnifying Party, if (a) on the advice of counsel to the Indemnified Party use of counsel of the Indemnifying Party's choice could reasonably be expected to give rise to a material conflict of interest, (b) the Indemnifying Party shall not have employed counsel reasonably satisfactory to the Indemnified Party to represent the Indemnified Party within a reasonable time after notice of the assertion of any such claim or institution of any such action or proceeding, (c) if the Indemnifying Party shall authorize the Indemnified Party to employ separate counsel at the Indemnifying Party's expense, or (d) such action shall seek relief other than monetary damages against the Indemnified Party.

Section 7.3.3 Real Property Title Claims. Purchaser shall join the title insurance company and the title insurance underwriter providing insurance with respect to the Purchased Assets in any claim, action or proceeding against the Sellers with respect to the Sellers' indemnification obligations arising in connection with Section 3.1.11(a) (Real Property); provided, however, that Purchaser, in its sole discretion, shall have a claim against said title insurance company and title insurance underwriter.

Section 7.4 Limitations of Liability.

Section 7.4.1 Claim Threshold. Notwithstanding anything to the contrary contained in this Agreement, (a) Sellers shall have no liability for their obligations under Section 4.2(d), Section 4.2(e), Section 4.11(b)(iii) or Section 7.1 until the aggregate amount of all Losses incurred by the Purchaser Indemnified Parties equals or exceeds \$500,000 (the "Claim Threshold"), in which event Sellers shall be liable for all such Losses in excess of the Claim Threshold; it being understood and agreed that the Claim Threshold shall not apply in the event of fraud, gross negligence or willful misconduct or to (i) claims for indemnification relating to Excluded Liabilities or Excluded Assets, or (ii) claims for indemnification relating to Section 3.1.1 (Existence), Section 3.1.2 (Authority), Section 3.1.3 (Binding Agreement), Section 3.1.4 (No Conflicts), Section 3.1.5 (Approvals and Filings), Section 3.1.10 (Title to Personal Property), Section 3.1.11(a) (Real Property), or Section 3.1.20 (Brokers), in each case for which Sellers shall be responsible from dollar one, whether or not the Claim Threshold has been reached, and (b) Purchaser shall have no liability for its obligations under Section 4.1(f)(C), Section 4.3(c), or Section 7.2 until the aggregate amount of all Losses incurred by the Sellers' Indemnified Parties equals or exceeds the Claim Threshold, in which event Purchaser shall be liable for all such Losses in excess of the Claim Threshold; it being understood and agreed that the foregoing Claim Threshold shall not apply in the event of fraud, gross negligence or willful

misconduct or to (i) claims for indemnification relating to Liabilities assumed by Purchaser under Section 2.1.2, or (ii) claims for indemnification relating to Section 3.2.1 (Existence), Section 3.2.2 (Authority), Section 3.2.3 (Binding Agreement), Section 3.2.4 (No Conflicts), Section 3.2.5 (Approvals and Filings) or Section 3.2.7 (Brokers), in each case for which Purchaser shall be responsible from dollar one, whether or not the Claim Threshold has been reached.

Section 7.4.2 Cap Amount. In no event shall (i) Sellers' aggregate liability arising out of their indemnification obligations under Section 4.2(d), Section 4.2(e), Section 4.11(b)(iii), Section 6.2(b), or Section 7.1 exceed 50% of the Purchase Price; it being understood and agreed that the foregoing limitation shall not apply in the event of fraud or willful misconduct, or to claims for indemnification relating to Excluded Liabilities or Excluded Assets or arising under any of Section 3.1.1 (Existence), Section 3.1.2 (Authority), Section 3.1.3 (Binding Agreement), Section 3.1.4 (No Conflicts), Section 3.1.5 (Approvals and Filings), Section 3.1.10 (Title to Personal Property), Section 3.1.11(a) (Real Property), or Section 3.1.20 (Brokers), and any such excluded indemnifiable Losses shall not be deemed to count against or otherwise reduce such limitation on Sellers' aggregate liability; and (ii) Purchaser's aggregate liability arising out of its indemnification obligations under Section 4.1(f)(C), Section 4.3(c), Section 6.2(b), or Section 7.2 exceed 50% of the Purchase Price; it being understood and agreed that the foregoing limitation shall not apply in the event of fraud or willful misconduct or to (a) claims for indemnification relating to Liabilities assumed by Purchaser under Section 2.1.2, or (b) claims for indemnification arising under any of Section 3.2.1 (Existence), Section 3.2.2 (Authority), Section 3.2.3 (Binding Agreement), Section 3.2.4 (No Conflicts), Section 3.2.5 (Approvals and Filings) or Section 3.2.7 (Brokers), and any such excluded indemnifiable Losses shall not be deemed to count against or otherwise reduce such limitation on Purchaser's aggregate liability. For the avoidance of doubt, Sellers aggregate obligations under Sections 4.1(g), 4.2(d), 4.2(e), 4.9, and 4.11(b)(iii) shall not exceed \$20,000,000.

Section 7.5 Indemnification in Case of Strict Liability or Indemnitee Negligence. THE INDEMNIFICATION PROVISIONS IN ARTICLE IV, ARTICLE VIII AND IN THIS ARTICLE VII SHALL BE ENFORCEABLE REGARDLESS OF WHETHER THE LIABILITY IS BASED ON PAST, PRESENT OR FUTURE ACTS, CLAIMS OR LAWS (INCLUDING ANY PAST, PRESENT OR FUTURE ENVIRONMENTAL LAW, FRAUDULENT TRANSFER ACT, OCCUPATIONAL SAFETY AND HEALTH LAW, OR PRODUCTS LIABILITY, SECURITIES OR OTHER LAW), AND REGARDLESS OF WHETHER ANY PERSON (INCLUDING THE PERSON FROM WHOM INDEMNIFICATION IS SOUGHT) ALLEGES OR PROVES THE SOLE, JOINT, CONCURRENT, CONTRIBUTORY OR COMPARATIVE NEGLIGENCE OF THE PERSON SEEKING INDEMNIFICATION, OR THE SOLE, JOINT, OR CONCURRENT STRICT LIABILITY IMPOSED ON THE PERSON SEEKING INDEMNIFICATION.

ARTICLE VIII

TAX MATTERS

Section 8.1 Representations and Warranties. Sellers represent and warrant to Purchaser, except as set forth in Section 8.1 of Sellers' Disclosure Schedule that:

(a) (i) GenWest has filed or will file when due all Tax Returns that are required to be filed on or before the Closing Date and paid or will pay in full all Taxes required to be paid; (ii) PWEC has filed or will file when due all Tax Returns that are required to be filed on or before the Closing Date, which filings, if not so made, could reasonably be expected to have an adverse effect on the Purchased Assets, and has paid or will pay in full all Taxes on such returns required to be paid; and (iii) such Tax Returns were prepared or will be prepared in the manner required by applicable Laws. Neither GenWest nor, with respect to the Purchased Assets, PWEC has received any notice that any Taxes relating to any period prior to Closing are owing that have not been paid.

(b) True and complete copies of all Tax Returns (other than Federal and State income and franchise tax returns) and all schedules thereto filed by, or on behalf of, GenWest and copies of all written communications to or from any Taxing Authority for all prior taxable years have been made available to Purchaser for inspection.

(c) Since the date of its inception, GenWest has qualified as and been treated as a disregarded entity for U.S. federal income Tax purposes.

(d) Neither GenWest nor PWEC has extended or waived the application of any statute of limitations of any jurisdiction regarding the assessment or collection of any Tax of GenWest or, with respect to the Purchased Assets, PWEC.

(e) There are no audits, claims, assessments, levies, administrative or judicial proceedings pending, or to Sellers' Knowledge, threatened, proposed or contemplated against GenWest or with respect to the Purchased Assets by any Taxing Authority.

(f) Each of GenWest and, with respect to the Purchased Assets, PWEC and PWCC has withheld and paid all Taxes required to have been withheld and paid in connection with amounts paid or owing to any employee, independent contractor, creditor, member or other third party.

(g) Neither GenWest nor, with respect to the Purchased Assets, PWEC is a party to any joint venture, partnership or other arrangement or contract which is or has been qualified as, and treated as, a partnership for United States federal and state income Tax purposes.

Section 8.2 Transfer Taxes. Other than the Tax on transfers of real property under chapter 375 of the Nevada Revenue and Taxation Code ("Real Property Transfer Taxes"), which shall be borne 50% by Purchaser and 50% by Sellers, Sellers shall bear all sales, use, transfer, and other similar taxes and fees ("Other Transfer Taxes"), if any, arising out of or in connection with the sale of the Purchased Assets by Sellers pursuant to this Agreement. GenWest shall file

all necessary documentation and Tax Returns with respect to the Other Transfer Taxes and the Real Property Transfer Taxes (collectively, the "Transfer Taxes") and cause such Taxes, if any, to be paid to the relevant Taxing Authorities on or prior to the Closing Date. The Parties shall cooperate to comply with all Tax Return requirements for any and all Transfer Taxes and shall provide such documentation and take such other reasonable actions as may be necessary to minimize the amount of any Transfer Taxes.

Section 8.3 Property Taxes. Real and personal property ad valorem taxes with respect to the Purchased Assets ("Property Taxes") for the taxable period that includes the Closing Date shall be prorated on a daily basis to the Closing Date. Sellers shall be liable only for the portion of such Property Taxes attributable to the portion of such taxable period ending on the Closing Date. Following the Closing, Sellers and Purchaser shall cooperate and consult with each other with respect to the determination of such Property Taxes and Sellers shall have the right to participate in any proceedings or disputes with the applicable Taxing Authority concerning the determination of the amount of such Property Taxes (including the determination of the value of the property with respect to which such Property Taxes are assessed).

Section 8.4 Sellers' Tax Indemnification. Sellers shall indemnify and hold harmless Purchaser from and against (a) any and all Taxes imposed on or incurred in respect of the income, business, assets and properties or operations of GenWest or PWEC with respect to the Purchased Assets, attributable to any taxable period ending on or prior to the Closing Date ("Pre-Closing Taxes"), (b) with respect to any taxable period beginning before and ending after the Closing Date (the "Overlap Period"), any and all Taxes imposed on or incurred in respect of the income, business, assets and properties or the operations of GenWest or PWEC with respect to the Purchased Assets, attributable to the period ending on the Closing Date ("Overlap Period Taxes"), (c) any and all Transfer Taxes for which Sellers are responsible pursuant to Section 8.2 of this Agreement, and (d) any Liabilities arising from a breach by Sellers of their covenants in this Article VIII. For purposes of the Overlap Period, Taxes shall be attributable to the period ending on the Closing Date: (A) in the case of Taxes imposed on a periodic basis or otherwise measured by the level of any item, deemed to be the amount of such Taxes for the entire period (or, in the case of such Taxes determined on an arrears basis, the amount of such Taxes for the immediately preceding period), multiplied by a fraction the numerator of which is the number of days in the Pre-Closing Tax Period and the denominator of which is the number of days in the entire taxable period; and (B) in the case of all other Taxes, to the extent of any Taxes that would be payable if the taxable year ended on the Closing Date. Notwithstanding anything to the contrary in this agreement, no claim for Taxes shall be permitted under this Section 8.4 unless such claim is first made not later than 30 days after the expiration of the applicable statute of limitations (including extensions) with respect to such Taxes.

Section 8.5 Purchaser Tax Indemnification. Purchaser shall indemnify and hold harmless Sellers from and against (a) any Taxes with respect to the Purchased Assets attributable to the time period after the Closing Date, (b) any and all Transfer Taxes for which Purchaser is responsible pursuant to Section 8.2 of this Agreement, and (c) any liability arising from a breach by Purchaser of its covenants set forth in this Article VIII.

Section 8.6 Refunds. If, after the Closing Date, Purchaser receives a refund or utilizes a credit of any Tax attributable to a Pre-Closing Tax Period or an Overlap Period, Purchaser shall

pay to GenWest within 15 Business Days after such receipt or utilization an amount equal to such refund received or credit utilized (or so much of such refund or credit as relates to the portion of the taxable period ending on or before Closing Date), together with any interest received or credited thereon. Purchaser shall take such action to obtain a refund or credit attributable to a Pre-Closing Tax Period or to mitigate, reduce or eliminate any Taxes that could be imposed for a Pre-Closing Tax Period (including with respect to the transactions contemplated hereby) as is reasonably requested by Sellers. Sellers shall reimburse Purchaser for any reasonable, out-of-pocket costs pre-approved by Sellers and demonstrated to Sellers' reasonable satisfaction that are incurred by Purchaser in providing such assistance.

Section 8.7 Contests. In the event Purchaser or Sellers receives written notice of any examination, claim, settlement, proposed adjustment, administrative or judicial proceeding, or other matter ("Tax Claim") related to any Pre-Closing Taxes, Transfer Taxes or Overlap Period Taxes, Purchaser or Sellers, as the case may be, shall notify the other Parties in writing as soon as reasonably practical (but in no event more than ten (10) Business Days) after receipt of such notice. If Sellers notify Purchaser in writing within thirty (30) Business Days following receipt of such written notice they intend to exercise their rights pursuant to this Section 8.7, they shall be entitled to control the defense, prosecution, settlement or compromise of such Tax Claim, at their own expense. Purchaser shall take such action in contesting such Tax Claim as Sellers shall reasonably request from time to time, including the selection of counsel and experts and execution of powers of attorney. Purchaser shall (a) not make any payments of such Tax Claim for at least thirty (30) days (or such shorter period as may be required by applicable Law) after giving the notice required by this Section 8.7, (b) give the Sellers any information requested relating to such Tax Claim, (c) give any Tax Authority any information requested by Sellers relating to such Tax Claim, and (d) otherwise cooperate with and make internal resources available to the Sellers in good faith in order to effectively contest any such Tax Claim. Sellers shall reimburse Purchaser for any reasonable, out-of-pocket costs pre-approved by Sellers and demonstrated to Sellers' reasonable satisfaction that are incurred by Purchaser in providing such assistance. Purchaser shall not settle or otherwise compromise any such Tax Claim with any Taxing Authority or prosecute such contest to a determination in court or other tribunal or initial or appellate jurisdiction unless instructed to do so by the Sellers. Any of the Sellers may settle or otherwise compromise any such Tax Claim without Purchaser's prior written consent, except that if as a result of such settlement or compromise the Taxes payable by Purchaser would be materially increased, none of Sellers may settle or compromise such matter without Purchaser's prior written consent, which consent shall not be unreasonably withheld. In connection with any proceeding taken with respect to such matters, (i) Sellers shall keep Purchaser informed of all material developments and events relating to such matters if involving a material liability for Taxes and (ii) Purchaser shall have the right, at its sole expense, to participate in any such proceedings. Purchaser shall cooperate with Sellers by giving them and their representatives, on prior reasonable notice, reasonable access and cooperation during normal business hours to all information, books and records pertaining to Transfer Taxes, Pre-Closing Taxes and Overlap Period Taxes. Sellers shall reimburse Purchaser for any reasonable, out-of-pocket costs pre-approved by Sellers and demonstrated to Sellers' reasonable satisfaction that are incurred by Purchaser in providing such assistance.

Section 8.8 Assistance and Cooperation. After the Closing Date, each of Sellers and Purchaser shall (and shall cause their respective Affiliates to) (i) assist the other Party in

preparing any Tax Returns which such other Party is responsible for preparing and filing in accordance with the terms of this Agreement, and (ii) cooperate fully in preparing for any audits of, or disputes with any Taxing Authority regarding, any Tax Returns of GenWest, PWEC or PWCC, or with respect to the Purchased Assets.

Section 8.9 Information. After the Closing, Sellers and Purchaser will make available to each other as reasonably requested, all information, records, or documents relating to liability or potential liability for Pre-Closing Taxes, Overlap Taxes and Transfer Taxes and will preserve such information, records or documents until 30 days after the expiration of the applicable statute of limitations (including extensions) with respect to such Taxes.

Section 8.10 Tax Returns. Sellers shall be responsible for preparing and filing all Tax Returns with respect to the Purchased Assets relating to Tax periods ending on or prior to the Closing Date. Purchaser shall be responsible for preparing and filing all Tax Returns with respect to the Purchased Assets relating to Tax periods ending after the Closing Date.

Section 8.11 Survival of Obligations. The obligations of the Parties set forth in this Article VIII shall be unconditional and absolute and shall remain in effect until 30 days after expiration of the applicable statutes of limitation (giving effect to any extensions or waivers thereof) relating to the Tax or Tax Return in question.

Section 8.12 Adjustments to Purchase Price. The Parties hereby agree that any and all indemnity payments made pursuant to this Agreement shall, to the maximum extent permitted by applicable Law, be treated for all Tax purposes as an adjustment to the Purchase Price.

ARTICLE IX

SURVIVAL; NO OTHER REPRESENTATIONS

Section 9.1 Survival of Representations, Warranties, Covenants and Agreements. The representations, warranties, covenants and agreements of Sellers and Purchaser contained in this Agreement shall survive the Closing and shall expire two (2) years from the Closing Date. Notwithstanding the preceding sentence, (i) the representations and warranties contained in Section 3.1.1 (Existence), Section 3.1.2 (Authority), Section 3.1.3 (Binding Agreement), Section 3.1.10 (Title to Personal Property), Section 3.1.11(a) (Real Property), Section 3.1.20 (Brokers), Section 3.2.1 (Existence), Section 3.2.2 (Authority), Section 3.2.3 (Binding Agreement), Section 3.2.4 (No Conflicts), Section 3.2.5 (Approvals and Filings) and Section 3.2.7 (Brokers), the covenants in Section 2.1.2 (Assignment and Assumption of Agreements), Section 2.1.4 (Excluded Liabilities), Section 2.5.2(a) (Pre-Closing Books and Records), Section 2.5.5 (Site Description Error), and Section 2.5.6 (Drainage Encroachment Indemnity) shall survive indefinitely after the Closing, (ii) the covenants in Section 2.5.2(b) (Pre-Closing Books and Records), with respect to Retained Information, shall survive for so long as Sellers retain the Retained Information, (iii) the covenants in Section 2.5.4, with respect to SCE RRSU Refunds, shall survive until all SCE RRSU Refunds have been paid, (iv) the representations, warranties, covenants and agreements contained in Article VIII (Tax Matters) and Section 12.6

(Confidentiality) shall be governed solely by the terms therein, (v) the representations and warranties contained in Section 3.1.17 (Environmental Matters) shall survive the Closing and shall expire on the date that is five (5) years after the Closing Date, and (vi) the representations and warranties contained in Section 3.1.21 (Intellectual Property) shall survive the Closing and shall expire on the date that is seven (7) years after the Closing Date.

Section 9.2 No Other Representations. NOTWITHSTANDING ANYTHING TO THE CONTRARY CONTAINED IN THIS AGREEMENT, IT IS THE EXPLICIT INTENT OF EACH PARTY HERETO THAT NONE OF THE PARTIES IS MAKING ANY REPRESENTATION OR WARRANTY WHATSOEVER, EXPRESS OR IMPLIED, INCLUDING BUT NOT LIMITED TO ANY IMPLIED REPRESENTATION OR WARRANTY AS TO CONDITION, MERCHANTABILITY, USAGE, SUITABILITY OR FITNESS FOR ANY PARTICULAR PURPOSE WITH RESPECT TO THE FACILITY, OR ANY PART THEREOF, EXCEPT THOSE REPRESENTATIONS AND WARRANTIES CONTAINED IN ARTICLE III AND ARTICLE VIII OF THIS AGREEMENT OR IN ANY CERTIFICATE, INSTRUMENT OR DOCUMENT EXECUTED AND DELIVERED PURSUANT TO THIS AGREEMENT.

ARTICLE X

DISPUTE RESOLUTION

Section 10.1 Dispute Resolution. Any dispute or claims arising under this Agreement which is not resolved in the ordinary course of business shall be referred to a panel consisting of a senior executive (President or a Vice President) of Purchaser and PWCC, with authority to decide or resolve the matter in dispute, for review and resolution. Such senior executives shall meet and in good faith attempt to resolve the dispute within 30 days. If the Parties are unable to resolve a dispute pursuant to this Section 10.1, either Party may enforce its rights at law or in equity subject to the provisions of this Agreement, including Section 10.2 below.

Section 10.2 Submission to Jurisdiction. Each Party hereto irrevocably submits to the exclusive jurisdiction of the federal court in the State of Nevada for the purposes of any action arising out of or based upon this Agreement or relating to the subject matter hereof. If, for any reason, the Parties fail to qualify for the jurisdiction of the federal court in the State of Nevada, then each Party hereto irrevocably submits to the exclusive jurisdiction of the state courts of the State of Nevada for the purposes of any action arising out of or based on this Agreement or relating to the subject matter hereof. Each Party hereto irrevocably and unconditionally waives any objection to the laying of venue of any action, suit or proceeding in the state or federal court in Nevada, and hereby further irrevocably and unconditionally waives and agrees not to plead or claim in any such court that any such action, suit or proceeding brought in any such court has been brought in an inconvenient forum. Each of GenWest and PWEC hereby appoints PWCC as its agent for service of process.

ARTICLE XI

LIMITED REMEDIES AND DAMAGES

Section 11.1 Exclusive Remedies. THE EXPRESS REMEDIES AND MEASURES OF DAMAGES PROVIDED FOR IN THIS AGREEMENT SHALL BE THE SOLE AND EXCLUSIVE REMEDIES FOR A PARTY HEREUNDER AND ALL OTHER REMEDIES OR DAMAGES AT LAW OR IN EQUITY ARE WAIVED. IF NO REMEDY OR MEASURE OF DAMAGES IS EXPRESSLY HEREIN PROVIDED, A PARTY MAY, SUBJECT TO THE LIMITATIONS OF SECTION 7.4 AND SECTION 11.2, PURSUE SUCH REMEDIES, INCLUDING DAMAGES AND FEES AND EXPENSES OF ATTORNEYS AS MAY BE AVAILABLE AT LAW OR IN EQUITY.

Section 11.2 Limitation of Liability. NOTWITHSTANDING THE FOREGOING, HOWEVER, NO PARTY SHALL, UNDER ANY CIRCUMSTANCES, BE LIABLE FOR SPECIAL, INDIRECT, CONSEQUENTIAL, INCIDENTAL, PUNITIVE OR EXEMPLARY DAMAGES, WHETHER BY STATUTE, IN TORT OR CONTRACT OR OTHERWISE. THE LIMITATIONS HEREIN IMPOSED ON REMEDIES AND THE MEASURE OF DAMAGES SHALL BE WITHOUT REGARD TO THE CAUSE OR CAUSES RELATED THERETO, INCLUDING THE NEGLIGENCE OF ANY PARTY. THIS PROVISION SHALL SURVIVE ANY TERMINATION, CANCELLATION OR SUSPENSION OF THIS AGREEMENT.

Section 11.3 Specific Performance. EACH PARTY AGREES THAT DAMAGE REMEDIES SET FORTH IN THIS AGREEMENT MAY BE DIFFICULT OR IMPOSSIBLE TO CALCULATE OR OTHERWISE INADEQUATE TO PROTECT ITS INTERESTS AND THAT IRREPARABLE DAMAGE MAY OCCUR IN THE EVENT THAT PROVISIONS OF THIS AGREEMENT ARE NOT PERFORMED BY THE PARTIES IN ACCORDANCE WITH THE SPECIFIC TERMS OF THIS AGREEMENT. ANY PARTY MAY SEEK TO REQUIRE THE PERFORMANCE OF ANY OTHER PARTY'S OBLIGATIONS UNDER THIS AGREEMENT THROUGH AN ORDER OF SPECIFIC PERFORMANCE RENDERED BY THE FEDERAL COURT IN THE STATE OF NEVADA OR THE STATE COURTS IN THE STATE OF NEVADA AS PROVIDED IN SECTION 10.2 OF THIS AGREEMENT.

ARTICLE XII

MISCELLANEOUS

Section 12.1 Notices.

Section 12.1.1 Notice Addresses. Unless this Agreement specifically requires otherwise, any notice, demand or request provided for in this Agreement, or served, given or made in connection with it, shall be in writing and shall be deemed properly served, given or made if delivered in person or sent by fax or sent by registered or certified mail, postage prepaid, or by a nationally recognized overnight courier service that provides a receipt of delivery, in each case, to a Party at its address specified below:

If to Purchaser, to:

Nevada Power
P.O. Box 98910, Las Vegas, NV 89151
Facsimile No.: (702) 367-5869
Attn: Corporate Senior Vice President,
Generation and Energy Supply

with a copy to:

Nevada Power
P.O. Box 98910, Las Vegas, NV 89151
Facsimile No.: (702) 367-5869
Attn: General Counsel

If to Sellers, to:

GenWest, LLC
400 North Fifth Street
Mail Station: 9068
Phoenix, Arizona 85004
Facsimile No.: (602) 250-3002
Attn: Secretary
Pinnacle West Capital Corporation
400 North Fifth Street
Mail Station: 9042
Phoenix, Arizona 85004
Facsimile No.: (602) 250-3002
Attn: Chief Financial Officer

Pinnacle West Energy Corporation
400 North Fifth Street
Mail Station: 9068
Phoenix, Arizona 85004
Facsimile No.: (602) 250-3002
Attn: Secretary

with a copy to:

Diane Wood, Senior Attorney
Pinnacle West Capital Corporation
Law & Business Practices Department
400 North Fifth Street
Mail Station: 8695
Phoenix, Arizona 85004
Facsimile No.: (602) 250-3393

with a copy to:

Snell & Wilmer L.L.P.
One Arizona Center
Phoenix, AZ 85004
Facsimile No.: (602) 382-6070
Attn: Matthew P. Feeney

Section 12.1.2 Effective Time. Notice given by personal delivery, mail or overnight courier pursuant to this Section 12.1 shall be effective upon physical receipt. Notice given by fax pursuant to this Section 12.1 shall be effective as of (i) the date of confirmed delivery if delivered before 5:00 p.m. local time on any Business Day, or (ii) the next succeeding Business Day if confirmed delivery is after 5:00 p.m. local time on any Business Day or during any non-Business Day.

Section 12.2 Payments. Except for Payments due at Closing, if either Party is required to make any payment under this Agreement on a day other than a Business Day, the date of payment shall be extended to the next Business Day. In the event a Party does not make any payment required or approved by the Parties under this Agreement on or before the due date, interest on the unpaid amount shall be due and paid at a rate that is the lesser of (a) the prime rate under "Money Rates" as reported in the Wall Street Journal on the first business day of the month during which interest is payable plus two percent (2%) or (b) the maximum rate of interest permitted to be charged by applicable Law (such lesser rate, the "Default Rate") from the date such payment is due until the date such payment is made in full. Any payment of such interest at the Default Rate pursuant to this Agreement shall not excuse or cure any default hereunder. All payments shall first be applied to the payment of accrued but unpaid interest.

Section 12.3 Entire Agreement. This Agreement and the Transaction Agreements supersede all prior discussions and agreements between the Parties with respect to the subject matter hereof and thereof, including, in each case, all schedules and exhibits thereto, and contain the sole and entire agreement between the Parties hereto with respect to the subject matter hereof and thereof.

Section 12.4 Expenses. Except as otherwise expressly provided in this Agreement, whether or not the transactions contemplated hereby are consummated, each Party will pay its own costs and expenses incurred in connection with the negotiation, execution and performance under this Agreement and the Transaction Agreements and the transactions contemplated hereby and thereby.

Section 12.5 Public Announcements. Prior to the Closing, Sellers and Purchaser will not issue or make any press releases or similar public announcements concerning the transactions contemplated hereby without the consent of the other. If either Party is unable to obtain the approval of its press release or similar public statement from the other Party and such press release or similar public statement is, in the opinion of legal counsel to such Party, required by Law in order to discharge such Party's disclosure obligations, then such Party may make or issue the legally required press release or similar public statement and promptly furnish the other Party

with a copy thereof. Sellers and Purchaser will also obtain the other Party's prior approval of any press release to be issued immediately following the execution of this Agreement or the Closing announcing either the execution of this Agreement or the consummation of the transactions contemplated by this Agreement.

Section 12.6 Confidentiality. Each Party hereto will hold, and will use commercially reasonable efforts to cause its Related Persons to hold, in strict confidence from any Person (other than any such Related Persons), unless (i) compelled to disclose by judicial or administrative process (including in connection with obtaining the necessary approvals of this Agreement and the transactions contemplated hereby of Governmental Authorities) or by other requirements of Law or necessary or desirable to disclose in order to obtain the PUCN Approval, the FERC Approval, or in connection with the HSR Act filing, or (ii) disclosed in an action or proceeding brought by a Party hereto in pursuit of its rights or in the exercise of its remedies hereunder, all documents and information concerning the other Party or any of its Related Persons furnished to it by the other Party or such other Party's Related Persons in connection with this Agreement or the transactions contemplated hereby and in the case of Purchaser, any information relating to the Purchased Assets, except to the extent that such documents or information can be shown to have been (a) previously known by the Party receiving such documents or information, (b) in the public domain (either prior to or after the furnishing of such documents or information hereunder) through no fault of such receiving Party or (c) later acquired by the receiving Party from another source if the receiving Party is not aware after reasonable inquiry that such source is under an obligation to another Party hereto to keep such documents and information confidential. In the event this Agreement is terminated, upon the request of the other Party, each Party hereto will, and will use commercially reasonable efforts to cause its Related Persons to, promptly (and in no event later than five (5) Business Days after such request) destroy or cause to be destroyed all copies of confidential documents and information furnished by the other Party in connection with this Agreement or the transactions contemplated hereby and destroy or cause to be destroyed all notes, memoranda, summaries, analyses, compilations and other writings related thereto or based thereon prepared by the Party furnished such documents and information or its Related Persons. The obligations contained in this Section 12.6 shall not survive Closing or, if this Agreement is terminated pursuant to ARTICLE VI, such obligations shall survive for one (1) year following the termination of this Agreement. The obligations in this Section 12.6 shall supersede the provisions of the Mutual Confidentiality Agreement, dated February 1, 2005, between Sierra Pacific Resources and Pinnacle West Energy, Inc (which party the Parties hereby acknowledge was intended to have been PWEC). Notwithstanding Section 12.10, this Section 12.6 is for the benefit of Sierra Pacific Resources.

Section 12.7 Waivers.

Section 12.7.1 Grant of Waivers. Any term or condition of this Agreement may be waived at any time by the Party that is entitled to the benefit thereof, but no such waiver shall be effective unless set forth in a written instrument duly executed by or on behalf of the Party waiving such term or condition. No waiver by any Party of any term or condition of this Agreement, in any one or more instances, shall be deemed to be or construed as a waiver of the same or any other term or condition of this Agreement on any future occasion. All remedies,

either under this Agreement or by Law or otherwise afforded, will be cumulative and not alternative.

Section 12.7.2 Exercise of Remedies. No failure or delay of any Party, in any one or more instances, (i) in exercising any power, right or remedy (other than failure or unreasonable delay in giving notice of default) under this Agreement or (ii) in insisting upon the strict performance by the other Party of such other Party's covenants, obligations or agreements under this Agreement, shall operate as a waiver, discharge or invalidation thereof, nor shall any single or partial exercise of any such right, power or remedy or insistence on strict performance, or any abandonment or discontinuance of steps to enforce such a right, power or remedy or to enforce strict performance, preclude any other or future exercise thereof or insistence thereupon or the exercise of any other right, power or remedy. The covenants, obligations, and agreements of a defaulting Party and the rights and remedies of the other Party upon a default shall continue and remain in full force and effect with respect to any subsequent breach, act or omission.

Section 12.8 Amendment. This Agreement may be amended, supplemented or modified only by a written instrument duly executed by or on behalf of each Party hereto.

Section 12.9 No Construction Against Drafting Party. The language used in this Agreement is the product of both Parties' efforts, and each Party hereby irrevocably waives the benefits of any rule of contract construction that disfavors the drafter of a contract or the drafter of specific words in a contract.

Section 12.10 No Third Party Beneficiary. Except as provided in Section 12.6, the terms and provisions of this Agreement are intended solely for the benefit of each Party hereto and their respective successors or permitted assigns, and it is not the intention of the Parties to confer third-party beneficiary rights upon any other Person.

Section 12.11 Headings. The headings used in this Agreement have been inserted for convenience of reference only and do not define or limit the provisions hereof.

Section 12.12 Invalid Provisions. If any provision of this Agreement is held to be illegal, invalid or unenforceable under any present or future Law, and if the rights or obligations of any Party hereto under this Agreement will not be materially and adversely affected thereby, (a) such provision will be fully severable, (b) this Agreement will be construed and enforced as if such illegal, invalid or unenforceable provision had never comprised a part hereof, (c) the remaining provisions of this Agreement will remain in full force and effect and will not be affected by the illegal, invalid or unenforceable provision or by its severance herefrom and (d) Purchaser and Sellers shall negotiate an equitable adjustment in the provisions of the Agreement with a view toward effecting the purposes of the Agreement, and the validity and enforceability of the remaining provisions, or portions or applications thereof, shall not be affected thereby.

Section 12.13 Governing Law. THIS AGREEMENT SHALL BE GOVERNED BY AND CONSTRUED IN ACCORDANCE WITH THE LAWS OF THE STATE OF NEVADA APPLICABLE TO A CONTRACT EXECUTED AND PERFORMED IN SUCH STATE, WITHOUT GIVING EFFECT TO THE CONFLICTS OF LAWS PRINCIPLES THEREOF.

Section 12.14 No Assignment; Binding Effect. Neither this Agreement nor any right, interest or obligation hereunder may be assigned by any Party hereto without the prior written consent of the other Party hereto and any attempt to do so will be void, except for assignments and transfers by operation of Law. This Agreement is binding upon, inures to the benefit of and is enforceable by the Parties and their respective successors and assigns.

Section 12.15 Counterparts. This Agreement may be executed in any number of counterparts, each of which will be deemed an original, but all of which together will constitute one and the same instrument.

Section 12.16 Time of Essence. Time is of the essence with respect to all obligations of the Parties hereunder.

[Signature Page Follows.]

IN WITNESS WHEREOF, this Purchase Agreement has been executed by the Parties as of the Effective Date.

PINNACLE WEST CAPITAL CORPORATION

By: /s/ Donald E. Brandt

Name: Donald E. Brandt
Title: Executive Vice President and Chief
Financial Officer

PINNACLE WEST ENERGY CORPORATION

By: /s/ James M. Levine

Name: James M. Levine
Title: President

GENWEST, LLC

By: /s/ Warren C. Kotzmann

Name: Warren C. Kotzmann
Title: Vice President

NEVADA POWER COMPANY

By: /s/ Roberto R. Denis

Name: Roberto R. Denis
Title: Corporate Senior Vice President,
Generation and Energy Supply

AMENDED AND RESTATED

REIMBURSEMENT AGREEMENT

among

ARIZONA PUBLIC SERVICE COMPANY

THE BANKS PARTY HERETO

JPMORGAN CHASE BANK, N.A.,
as Administrative Agent and Issuing Bank and

BARCLAYS BANK PLC,
as Syndication Agent

dated as of May 19, 2005

J.P. Morgan Securities Inc. and Barclays Capital,
Joint Lead Arrangers and Joint Bookrunners

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SCHEDULE I - Letter of Credit Commission Rates

SCHEDULE II - Participation Amounts and Participation Percentages

EXHIBIT A Form of Amended and Restated Letter of Credit

THE TABLE OF CONTENTS IS NOT A PART OF THIS AGREEMENT.

AMENDED AND RESTATED REIMBURSEMENT AGREEMENT

AMENDED AND RESTATED REIMBURSEMENT AGREEMENT among ARIZONA PUBLIC SERVICE COMPANY, JPMORGAN CHASE BANK, N.A. (successor to JPMORGAN CHASE BANK ("JPMC")), as Administrative Agent and as Issuing Bank, and the BANKS listed on the signature pages hereto, as amended and restated as of May 19, 2005. (Unless otherwise indicated, all capitalized terms used herein have the meanings referred to or set forth in Section 1.)

WHEREAS, the Company has entered into a Participation Agreement dated as of August 1, 1986 (as amended and in effect on May 19, 2005, the "PARTICIPATION AGREEMENT") among the Company, U.S. Bank National Association (as successor to State Street Bank and Trust Company, as successor to The First National Bank of Boston), for itself and as Owner Trustee (together with its successors in such capacity, the "OWNER TRUSTEE"), JPMorgan Chase Bank, N.A. (as successor to Chemical Bank), for itself and as Indenture Trustee (together with its successors in such capacity, the "INDENTURE TRUSTEE"), PVNGS Funding Corp., Inc., PVNGS II Funding Corp., Inc. and Emerson Finance LLC, as Equity Participant (together with its successors and assigns, the "EQUITY PARTICIPANT"), relating to the acquisition of an undivided interest in Unit 2 of the Palo Verde Nuclear Generating Station through a trust for the benefit of the Equity Participant which interest has been leased to the Company pursuant to a lease dated as of August 1, 1986 between the Owner Trustee and the Company (as amended and in effect on May 19, 2005, the "FACILITY LEASE");

WHEREAS, pursuant to Section 10(b)(3)(ix) of the Participation Agreement, the Company has agreed to maintain at all times during the Basic Lease Term (as defined in the Participation Agreement) an irrevocable letter of credit for the benefit of the Equity Participant;

WHEREAS, in order to comply with the requirements of Section 10(b)(3)(ix) of the Participation Agreement, the Company entered into a Reimbursement Agreement dated as of August 1, 1986 (as amended and restated thereafter from time to time prior to July 22, 2002, further amended and restated as of July 22, 2002 and in effect immediately prior to May 19, 2005, the "EXISTING REIMBURSEMENT AGREEMENT") between the Company and JPMC, pursuant to which JPMC issued to the Equity Participant its irrevocable transferable letter of credit (such letter of credit, as amended and restated and in effect from time to time before May 19, 2005, as further amended and restated as of May 19, 2005, and as the same may be amended in accordance with this Agreement and in effect from time to time thereafter, and any successor Letter of Credit as provided in such Letter of Credit, being referred to herein as the "LETTER OF CREDIT"), to secure the payment of Rent (as defined in the Participation

Agreement) by the Company under the Facility Lease to the extent of the amount available to be drawn from time to time under the Letter of Credit;

WHEREAS, the Letter of Credit will expire on July 22, 2005, if not extended; and

WHEREAS, pursuant to Section 17 of the Existing Reimbursement Agreement, the Company has requested that the Letter of Credit be amended and restated, that the term of the Letter of Credit be extended for five years, and that certain provisions of the Existing Reimbursement Agreement be amended, and the Banks are willing to comply with such requests on the terms and conditions set forth below;

NOW, THEREFORE, in consideration of the premises and in order to induce the Banks to agree to the amendment and restatement of the Letter of Credit, the extension of the term of the Letter of Credit and the amendment of certain provisions of the Existing Reimbursement Agreement, the parties hereto agree that, upon satisfaction of the conditions set forth in Section 3(b) below and subject to Section 3(c) below, the Existing Reimbursement Agreement will, without any further action by the parties hereto, be amended and restated to read in full as follows:

Section 1 Definitions; Accounting Terms. (a) Definitions. Capitalized terms used herein and not otherwise defined herein have the respective meanings assigned thereto in Appendix A to the Facility Lease. The following terms as used herein have the following respective meanings:

"ACC" means the Arizona Corporation Commission or any successor thereto.

"ADMINISTRATIVE AGENT" means JPMorgan Chase Bank, N.A., in its capacity as administrative agent for the Banks hereunder, and its successors in such capacity.

"ADMINISTRATIVE QUESTIONNAIRE" means, with respect to each Bank, an administrative questionnaire in the form prepared by the Administrative Agent and submitted to the Administrative Agent (with a copy to the Company) duly completed by such Bank.

"AFFILIATE" means, as to any Person, any other Person that, directly or indirectly, controls, is controlled by or is under common control with such Person or is a director or officer of such Person.

"AGENT PARTIES" has the meaning given in Section 11(d).

"AGREEMENT" means, when used with reference to this Agreement, this Reimbursement Agreement as originally executed as of August 1, 1986, as amended or amended and restated from time to time before May 19, 2005, as amended and restated as of May 19, 2005, and as the same may be amended in accordance with its terms from time to time thereafter.

"AMENDED AND RESTATED LETTER OF CREDIT" means the Amended and Restated Irrevocable Transferable Letter of Credit No. 010152 (formerly numbered as S-1002), dated as of May 19, 2005, amending the Existing Letter of Credit, substantially in the form of Exhibit A hereto.

"AMENDMENT AND RESTATEMENT" means the Amendment and Restatement dated as of May 19, 2005, amending and restating the Existing Reimbursement Agreement.

"APPLICABLE BOOKING OFFICE" means, as to each Bank, its office, branch or affiliate located at its address set forth in its Administrative Questionnaire (or identified in its Administrative Questionnaire as its Applicable Booking Office) or such other office, branch or affiliate of such Bank as it may hereafter designate as its Applicable Booking Office by notice to the Company and the Administrative Agent.

"ASSIGNEE" has the meaning set forth in Section 15(a).

"AUTHORIZED OFFICER" means the chairman of the board, chief executive officer, president, chief financial officer, chief operating officer, treasurer, controller, any vice president or any assistant treasurer of the Company.

"BANK" means (i) each bank or financial institution listed on the signature pages hereof, each Assignee that becomes a Bank pursuant to Section 15(a), and their respective successors, and (ii) the Issuing Bank with respect to its Participation.

"BASE RATE" means, for any day, a rate per annum equal to the higher of (i) the Prime Rate for such day and (ii) the sum of 1/2 of 1% plus the Federal Funds Rate for such day.

"BUSINESS DAY" means any day except a Saturday, Sunday or other day on which commercial banks in New York, New York, Chicago, Illinois or the State of California or, for purposes of Sections 2(a), 2(g) and 9(i) only, Phoenix, Arizona, are authorized by law to close.

"CAPITAL LEASE OBLIGATIONS" means as to any Person, the obligations of such Person to pay rent or other amounts under a lease of (or other agreement conveying the right to use) real and/or personal property, which obligations are

required to be classified and accounted for as a capital lease on the balance sheet of such Person under generally accepted accounting principles and, for the purposes of this Agreement, the amount of such obligations shall be the capitalized amount thereof, determined in accordance with generally accepted accounting principles.

"CODE" means the Internal Revenue Code of 1986, as amended, or any successor statute.

"COMPANY" means Arizona Public Service Company, an Arizona corporation, and its successors and permitted assigns.

"COMPANY MATERIALS" has the meaning given in Section 7(g).

"CONFIDENTIAL INFORMATION" means information that the Company furnishes to any other party hereto in a writing designated as confidential, or that such party obtains pursuant to its rights under Section 7(e), but does not include any such information that (a) is or becomes generally available to the public other than as a result of a breach by such party of its obligations hereunder, (b) was available to such party on a nonconfidential basis prior to its disclosure to such party by the Company or any of its Affiliates or (c) is or becomes available to such party from a source other than the Company that is not, to the knowledge of such party, acting in violation of a confidentiality agreement with the Company.

"CONSOLIDATED CAPITALIZATION" has the meaning set forth in Section 8(e).

"CONSOLIDATED CASH COVERAGE RATIO" means, with respect to the Company and its Consolidated Subsidiaries, for each twelve-month period ending on the last day of each fiscal quarter (determined as of the last day of such fiscal quarter), the ratio of:

(a) an amount equal to:

(i) consolidated net income of the Company and its Consolidated Subsidiaries for such period, plus

(ii) all material non-recurring items which decreased said net income for such period, minus

(iii) all material non-recurring items which increased said net income for such period, plus

(iv) income taxes deducted in determining said net income for such period, plus

(v) total "Interest Charges", as defined in clause (b) below, of the Company and its Consolidated Subsidiaries for such period, plus

(vi) depreciation and amortization, and nuclear fuel amortization for such period, minus

(vii) allowance for equity and borrowed funds used during construction for such period, minus

(viii) deferrals as described in Financial Accounting Standards Board Statement No. 71 for such period, plus or minus

(ix) other significant noncash items for such period as may be specified under Financial Accounting Standards Board Statements or other accounting guidelines, to

(b) without duplication of any item, an amount equal to the sum (such amount being the "INTEREST CHARGES") of:

(i) interest on long-term debt for such period as reported in the consolidated income statement for such period, plus

(ii) interest on short-term debt for such period as reported in the consolidated income statement for such period, plus

(iii) imputed interest on the Sale Leaseback Obligation Bonds for such period, such amount being equal to the product of (A) the principal amount of Sale Leaseback Obligation Bonds outstanding during such period and (B) the rate of interest applicable to such Sale Leaseback Obligation Bonds during such period, plus

(iv) all rental payments in respect of operating leases (excluding any portion of such rental payments attributable to operating expenses and excluding any payments in respect of Sale Leaseback Obligation Bonds) with respect to which the payment obligations of the Company or a Consolidated Subsidiary of the Company have a present value of at least \$25,000,000.

"CONSOLIDATED INDEBTEDNESS" has the meaning set forth in Section 8(e).

"CONSOLIDATED NET WORTH" has the meaning set forth in Section 8(e).

"CONSOLIDATED SUBSIDIARY" means at any date any Subsidiary or other entity the accounts of which would be consolidated with those of the Company in its consolidated financial statements if such statements were prepared as of such date.

"DATE OF EARLY TERMINATION" has the meaning set forth in the Letter of Credit.

"ELIGIBLE INSTITUTION" means (i) a commercial bank or a savings and loan association having a net worth in excess of \$250,000,000 (or the equivalent in any other currency), (ii) a Bank or an affiliate of a Bank or (iii) any other Person which the Company designates as an Eligible Institution with the consent of the Administrative Agent.

"EQUITY PARTICIPANT" has the meaning set forth in the first recital hereto.

"ERISA" means the Employee Retirement Income Security Act of 1974, as amended from time to time, and the regulations promulgated and rulings issued thereunder.

"ERISA AFFILIATE" means any corporation or trade or business which is a member of the same controlled group of corporations (within the meaning of Section 414(b) of the Code) as the Company or is under common control (within the meaning of Section 414(c) of the Code) with the Company.

"EXISTING LETTER OF CREDIT" means the Letter of Credit, as amended and in effect immediately prior to May 19, 2005.

"EXISTING REIMBURSEMENT AGREEMENT" has the meaning set forth in the third recital hereto.

"FACILITY LEASE" has the meaning set forth in the first recital hereto.

"FEDERAL FUNDS RATE" means, for any day, the rate per annum (rounded upward, if necessary, to the nearest 1/100th of 1%) equal to the weighted average of the rates on overnight Federal funds transactions with members of the Federal Reserve System arranged by Federal funds brokers on such day, as published by the Federal Reserve Bank of New York on the Business Day next succeeding such day, provided that (i) if such day is not a Business Day, the Federal Funds Rate for such day shall be such rate on such transactions on the next preceding Business Day as so published on the next succeeding Business Day, and (ii) if no such rate is so published on such next succeeding Business Day, the Federal Funds Rate for such day shall be the average rate quoted to JPMorgan Chase Bank, N.A. on such day as determined by the Administrative Agent.

"FEE LETTER" means the Fee Letter dated as of April 14, 2005, among the Company, JPMorgan Chase Bank, N.A., J.P. Morgan Securities Inc., Barclays Bank PLC and Barclays Capital, the investment banking division of Barclays Bank PLC.

"FINANCIAL INFORMATION" means (i) the annual report of the Company on Form 10-K for the year ended December 31, 2004, as filed with the Securities and Exchange Commission pursuant to the Securities Exchange Act of 1934, as amended, (ii) the Company's quarterly report on Form 10-Q for the fiscal quarter of the Company ended March 31, 2005, as so filed, and (iii) the Company's current reports on Form 8-K filed January 28, 2005, March 1, 2005, March 29, 2005, April 13, 2005, April 26, 2005 and May 19, 2005, as so filed.

"GUARANTEE" means as to any Person, any obligation, contingent or otherwise, of such Person directly or indirectly guaranteeing any Indebtedness of any other Person or in any manner providing for the payment of any Indebtedness of any other Person or otherwise protecting the holder of such Indebtedness against loss (whether by virtue of partnership arrangements, agreements to keep well, to purchase assets, goods, securities or services, or to take-or-pay or otherwise), provided that the term "Guarantee" shall not include endorsements for collection or deposit in the ordinary course of business. The term "GUARANTEE" used as a verb has a corresponding meaning.

"INDEBTEDNESS" means as to any Person at any date (without duplication): (a) indebtedness created, issued, incurred or assumed by such Person for borrowed money or evidenced by bonds, debentures, notes or similar instruments; (b) all obligations of such Person to pay the deferred purchase price of property or services, excluding, however, trade accounts payable (other than for borrowed money) arising in, and accrued expenses incurred in, the ordinary course of business of such Person so long as such trade accounts payable are paid within 180 days of the date incurred; (c) all Indebtedness secured by a lien on any asset of such Person, to the extent such Indebtedness has been assumed by, or is a recourse obligation of, such Person; (d) all Guarantees by such Person; (e) all Capital Lease Obligations of such Person; and (f) the amount of all reimbursement obligations of such Person (whether contingent or otherwise) in respect of letters of credit, bankers' acceptances, surety or other bonds and similar instruments in support of Indebtedness.

"INDENTURE TRUSTEE" has the meaning set forth in the first recital hereto.

"ISSUING BANK" means JPMorgan Chase Bank, N.A. and its successors in their capacity as issuer of the Letter of Credit.

"LETTER OF CREDIT" has the meaning set forth in the third recital hereto.

"LETTER OF CREDIT COMMISSION RATE" means a rate per annum determined in accordance with Schedule I hereto.

"LIEN" means any lien, security interest or other charge or encumbrance of any kind, including, without limitation, the lien or retained security title of a

conditional vendor and any easement, right of way or other encumbrance on title to real property.

"MATERIAL SUBSIDIARY" means, at any time, a Subsidiary of the Company which as of such time meets the definition of a "significant subsidiary" included as of May 19, 2005 in Regulation S-X of the Securities and Exchange Commission or whose assets at such time exceed 10% of the assets of the Company and the Subsidiaries (on a consolidated basis).

"MAXIMUM CREDIT AMOUNT" means, at any date, the Maximum Credit Amount, as defined in the Letter of Credit.

"MAXIMUM DRAWING AMOUNT" means, at any date, the Maximum Drawing Amount, as defined in the Letter of Credit.

"MULTIEMPLOYER PLAN" means a plan defined as such in Section 3(37) of ERISA to which contributions have been made by the Company or any ERISA Affiliate within any of the preceding five plan years and which is covered by Title IV of ERISA.

"1986 ORDER" means Decision No. 55120, dated July 24, 1986, of the ACC.

"OTHER TAXES" has the meaning set forth in Section 2(e).

"OWNER TRUSTEE" has the meaning set forth in the first recital hereto.

"PARENT" means, as to any Bank, any Person controlling such Bank.

"PARTICIPANT" has the meaning set forth in Section 15(b).

"PARTICIPATION" means a participating interest of a Bank in the credit represented by the Letter of Credit including, without limitation, the interest therein retained by the Issuing Bank after giving effect to all participating interests therein granted by it pursuant to Section 14(a), but prior to giving effect to any interest therein granted to any Participant pursuant to Section 15(b).

"PARTICIPATION AGREEMENT" has the meaning set forth in the first recital hereto.

"PARTICIPATION AMOUNT" means, with respect to any Bank, the amount set forth in Schedule II hereto opposite the name of such Bank therein, as such amount may be changed by reason of an assignment by or to such Bank in accordance with Section 15(a). Such amount shall be reduced from time to time by such Bank's ratable share of each reduction of the Maximum Credit Amount.

"PARTICIPATION PERCENTAGE" means, with respect to any Bank at any time, the percentage equivalent of a fraction (i) the numerator of which is the Participation Amount of such Bank at such time and (ii) the denominator of which is the Maximum Credit Amount at such time.

"PBGC" means the Pension Benefit Guaranty Corporation or any entity succeeding to any or all of its functions under ERISA.

"PERMITTED LIEN" of the Company or any Material Subsidiary means any of the following:

(i) Liens for taxes, assessments or other governmental charges or levies not at the time delinquent or thereafter payable without penalty or being contested in good faith by appropriate proceedings and for which adequate reserves in accordance with generally accepted accounting principles shall have been made;

(ii) Liens of carriers, warehousemen, mechanics, materialmen and landlords incurred in the ordinary course of business, including, without limitation, landlord's liens arising under Arizona law under leases entered into by the Company in the 1986 sale and leaseback transactions with respect to Unit 2, including without limitation the Facility Lease, and securing the payment of rent under such leases, to the extent such leases are properly treated as operating leases, in each case, for sums not overdue or being contested in good faith by appropriate proceedings and for which adequate reserves in accordance with generally accepted accounting principles shall have been made;

(iii) Liens incurred in the ordinary course of business in connection with worker's compensation, unemployment insurance or other forms of governmental insurance or benefits or other similar statutory obligations;

(iv) Liens to secure obligations on surety or appeal bonds;

(v) rights of setoff and banker's Liens with respect to funds on deposit in a financial institution in the ordinary course of business;

(vi) easements, restrictions and other minor defects of title that are not, in the aggregate, material to the use of such property;

(vii) Liens securing claims against any Person other than the Company or any Subsidiary of the Company neither assumed nor guaranteed by the Company or any Subsidiary of the Company nor on which the Company or any Subsidiary of the Company customarily pays

interest, existing upon real estate or rights in or relating to real estate acquired by the Company or any Subsidiary of the Company for substation, transmission line, transportation line, distribution line or right of way purposes;

(viii) rights reserved to or vested in any municipality or public authority by the terms of any right, power, franchise, grant, license or permit or by any provision of law, to terminate such right, power, franchise, grant, license or permit, or to purchase or recapture or to designate a purchaser of any of the property of the Company;

(ix) rights reserved to or vested in others to take or receive any part of the power pursuant to firm power commitment contracts, purchased power contracts and similar agreements, gas, oil or other minerals or timber generated, developed, manufactured or produced by, or grown on, or acquired with, any property of the Company;

(x) rights reserved to or vested in any municipality or public authority to control or regulate any property of the Company, or to use such property in a manner that does not materially impair the use of such property for the purposes for which it is held by the Company;

(xi) security interests granted in favor of the Unit 2 sale leaseback transaction lessors in the Company's Decommissioning Trust Agreement (PVNGS Unit 2) dated as of January 31, 1992 (such agreement, as amended or otherwise modified from time to time, being the "Unit 2 Trust Agreement") to secure the Company's obligations in respect of the decommissioning of Unit 2 or related facilities;

(xii) Liens that may exist with respect to the Unit 2 Trust Agreement (other than as described in clause (xi) above), or with respect to either of the Company's Decommissioning Trust Agreement (PVNGS Unit 1) or Decommissioning Trust Agreement (PVNGS Unit 3), each dated as of July 1, 1991, as amended or otherwise modified from time to time, relating to the Company's obligation to set aside funds for the decommissioning and retirement from service of such Units;

(xiii) pledges of pollution control bonds and related rights to secure the Company's reimbursement obligations in respect of letters of credit and bond insurance supporting pollution control bond transactions, provided that such pollution control bonds are not secured by any other assets of the Company or any Material Subsidiary;

(xiv) Liens established on specified bank accounts of the Company to secure the Company's reimbursement obligations in respect

of letters of credit supporting commercial paper issued by the Company and similar arrangements for collateral security with respect to refinancings or replacements of the same;

(xv) interests of other participants under agreements governing jointly-owned electric generating facilities and transmission facilities and transfers of operational or other control of facilities to a regional transmission organization or other similar body and Liens on such facilities to cover expenses, fees and other costs of such an organization or body;

(xvi) rights of transmission users or any regional transmission organizations or similar entities in transmission facilities;

(xvii) Liens on property of the Company sold in a transaction permitted by Section 8(a) hereof to another Person pursuant to a conditional sales agreement where the Company retains title; and

(xviii) any Liens securing a claim (other than in respect of Indebtedness) in an amount less than \$10,000,000;

provided, however, that no Lien in favor of the PBGC shall, in any event, be a Permitted Lien.

"PERSON" means an individual, a corporation, a partnership, an association, a trust or any other entity or organization, including a government or political subdivision or an agency or instrumentality thereof.

"PLAN" means an employee benefit plan within the meaning of Section 3(3) of ERISA established or maintained by the Company or any ERISA Affiliate which is covered by Title IV of ERISA, other than a Multiemployer Plan.

"PLATFORM" has the meaning given in Section 7(g).

"PRIME RATE" means the rate of interest publicly announced by JPMorgan Chase Bank, N.A. in New York City from time to time as its Prime Rate.

"PVNGS" means the Palo Verde Nuclear Generating Station.

"PWCC" means Pinnacle West Capital Corporation, an Arizona corporation and its successors.

"REIMBURSEMENT DEFAULT" means any event or condition which constitutes a Reimbursement Event of Default or which with the giving of notice or the lapse of time or both would, unless cured or waived, become a Reimbursement Event of Default.

"REIMBURSEMENT EVENT OF DEFAULT" has the meaning set forth in Section 9.

"REQUIRED BANKS" means, at any time, Banks with Participation Percentages aggregating more than 50% at such time.

"RESTATEMENT EFFECTIVE DATE" has the meaning set forth in Section 3(b).

"SALE LEASEBACK OBLIGATION BONDS" means PVNGS II Funding Corp. Inc.'s (i) 7.39% Secured Lease Obligation Bonds, Series 1993, due 2005; (ii) 8.00% Secured Lease Obligation Bonds, Series 1993, due 2015; (iii) any other bonds issued by the Company in connection with a sale/leaseback transaction; and (iv) any refinancing or refunding of the obligations specified in clauses (i) through (iii) above.

"STATED TERMINATION DATE" means May 19, 2010 or such later date to which such Stated Termination Date shall have been extended pursuant to Section 17.

"SUBSEQUENT ORDER" means any decision, order or ruling of the ACC issued after May 19, 2005 that amends, supersedes or otherwise modifies the 1986 Order or any successor decision, order or ruling.

"SUBSIDIARY" of any Person means any corporation of which more than 50% of the issued and outstanding capital stock having ordinary voting power to elect a majority of the Board of Directors of such corporation (irrespective of whether at the time capital stock of any other class or classes of such corporation shall or might have voting power upon the occurrence of any contingency) is at the time directly or indirectly owned or controlled by such Person, such Person and one or more of its other Subsidiaries, or one or more of such Person's other Subsidiaries.

"TAXES" has the meaning set forth in Section 2(e).

"TERMINATION DATE" means the earliest of (i) the date on which the Issuing Bank pays a drawing under the Letter of Credit for the lesser of the Maximum Drawing Amount and the Maximum Credit Amount, (ii) if a drawing is not requested by the Equity Participant after a notice of termination is given under the Letter of Credit, the Date of Early Termination, (iii) if a drawing is requested by the Equity Participant after a notice of termination is given under the Letter of Credit, the date on which the Issuing Bank pays such drawing, (iv) the date on which the Company delivers a certificate to the Issuing Bank certifying that the Company has paid the amounts due under Section 9(c) of the Facility Lease (so long as the Equity Participant shall have acknowledged such payment by its express confirmation thereof in, and its countersignature to, such certificate),

(v) the date on which the Company delivers a certificate to the Issuing Bank certifying that the Company has paid the amounts due under Section 9(d) of the Facility Lease (so long as the Equity Participant shall have acknowledged such payment by its express confirmation thereof in, and its countersignature to, such certificate), and (vi) the latest of (x) the Stated Termination Date, (y) if a draft and certificate all in strict conformity with the terms and conditions of the Letter of Credit are presented on the Stated Termination Date at such time and at such office as specified in the fifth paragraph of the Letter of Credit, the date on which the Issuing Bank is required to honor the draft in accordance with the provisions of such paragraph pursuant to such presentation, and (z) if a corrected draft and certificate all in strict conformity with the terms and conditions of the Letter of Credit are presented on the date specified in, and in accordance with, the provisions of the sixth paragraph of the Letter of Credit, the date on which the Issuing Bank is required to honor the draft in accordance with the provisions of such paragraph pursuant to such presentation.

"TOTAL ASSETS" means the aggregate of all assets properly appearing on the most recent balance sheet of the Company and its Consolidated Subsidiaries furnished pursuant to Section 6(f) or Section 7(g).

"UNITED STATES" means the United States of America, including the States and the District of Columbia, but excluding its territories and possessions.

"WHOLLY-OWNED SUBSIDIARY" of any Person means any corporation of which all shares of the issued and outstanding capital stock (other than any director's qualifying shares) having ordinary voting power to elect a majority of the Board of Directors of such corporation (irrespective of whether at the time capital stock of any other class or classes of such corporation shall or might have voting power upon the occurrence of any contingency) is at the time directly or indirectly owned or controlled by such Person, such Person and one or more of its other Subsidiaries, or one or more of such Person's other Subsidiaries.

(b) Accounting Terms. Unless otherwise specified herein, all accounting terms used herein shall be interpreted, all accounting determinations hereunder shall be made, and all financial statements required to be delivered hereunder shall be prepared, in accordance with generally accepted accounting principles as in effect from time to time, applied on a basis consistent (except for changes concurred in by the Company's independent public accountants) with the most recent audited consolidated financial statements of the Company delivered to the Agent.

Section 2 Reimbursement. (a) The Company agrees to pay to the Administrative Agent for the account of the Issuing Bank (i) not later than 2:00 p.m., New York City time, on the fifth Business Day after the Issuing Bank shall have paid any draft under the Letter of Credit a sum equal to the amount so paid

under the Letter of Credit, (ii) interest on each amount paid by the Issuing Bank under the Letter of Credit from and including the date such amount is paid by the Issuing Bank under the Letter of Credit until but excluding the earlier of (x) the date the Issuing Bank shall have received from the Company the amounts due under clause (i) above and this clause (ii) and (y) the fifth Business Day after the Issuing Bank shall have paid the relevant draft, payable on demand, at a rate per annum equal to the Base Rate, and (iii) interest on any amount not paid by the Company when due under clauses (i) and (ii) above from and including the fifth Business Day after the relevant draft is paid by the Issuing Bank under the Letter of Credit until such overdue amount is paid in full, payable on demand, at a rate per annum equal to 2% per annum above the Base Rate; provided that such interest rate shall in no event be higher (with respect to each amount due and payable hereunder, from the date such amount is due and payable until the date such amount is paid in full) than the maximum rate permitted by applicable law.

(b) The Company agrees to pay to the Administrative Agent for the account of the Banks ratably in proportion to their Participation Percentages a letter of credit commission computed at the Letter of Credit Commission Rate on the Maximum Credit Amount of the Letter of Credit from and including the Restatement Effective Date to, but excluding, the Termination Date. Such commission accrued through and including the last day of March, June, September and December of each year shall be payable in arrears on the third Business Day following such last day, commencing on the first such date to occur after the Restatement Effective Date.

(c) The Company agrees to pay to the Administrative Agent for the account of the Issuing Bank a fronting fee at the rate per annum heretofore mutually agreed by the Company and the Issuing Bank pursuant to the Fee Letter, on the Maximum Credit Amount of the Letter of Credit from and including the Restatement Effective Date to, but excluding, the Termination Date. Such fronting fee accrued through and including the last day of March, June, September and December of each year shall be payable in arrears on the third Business Day following such last day, commencing on the first such date to occur after the Restatement Effective Date.

(d) (i) If after May 19, 2005 the adoption of any applicable law, rule or regulation, or any change therein, or any change in the interpretation or administration thereof by any governmental authority, central bank or comparable agency charged with the interpretation or administration thereof, or compliance by any Bank with any request or directive (whether or not having the force of law) of any such authority, central bank or comparable agency shall impose, modify or deem applicable any reserve, special deposit or similar requirement (including, without limitation, any such requirement imposed by the Board of Governors of the Federal Reserve System) against letters of credit issued by or assets held by, deposits with or for the account of, or credit extended by, any Bank or shall

impose on any Bank any other condition regarding this Agreement or the Letter of Credit or its Participation therein, and the result of any of the foregoing is to increase the cost to such Bank of the issuance or maintenance of the Letter of Credit or its Participation therein, or to reduce the amount of any sum received or receivable by such Bank under this Agreement with respect thereto, by an amount deemed by such Bank to be material, then within 15 days after demand by such Bank (with a copy to the Administrative Agent), the Company shall pay to the Administrative Agent for the account of such Bank such additional amount or amounts as will compensate such Bank for such increased cost or reduction.

(ii) If any Bank shall have determined that, after May 19, 2005, the adoption of any applicable law, rule or regulation regarding capital adequacy, or any change in any such law, rule or regulation, or any change in the interpretation or administration thereof by any governmental authority, central bank or comparable agency charged with the interpretation or administration thereof, or any request or directive regarding capital adequacy (whether or not having the force of law) of any such authority, central bank or comparable agency, has or would have the effect of reducing the rate of return on capital of such Bank (or its Parent) as a consequence of such Bank's obligations hereunder to a level below that which such Bank (or its Parent) could have achieved but for such adoption, change, request or directive (taking into consideration its policies with respect to capital adequacy) by an amount deemed by such Bank to be material, then from time to time, within 15 days after demand by such Bank (with a copy to the Administrative Agent), the Company shall pay to such Bank such additional amount or amounts as will compensate such Bank (or its Parent) for such reduction.

(iii) Each Bank will notify the Company and the Administrative Agent of any event of which it has knowledge, occurring after May 19, 2005 which will entitle such Bank to compensation pursuant to clause (i) or (ii) of this Section 2(d) as promptly as practicable, but in any event within 90 days after such Bank obtains knowledge thereof; provided that, if such Bank fails to give such notice within 90 days after it obtains knowledge of such an event, such Bank shall, with respect to compensation payable in respect of any costs resulting from such event, only be entitled to payment for costs incurred on and after the date that such Bank does give such notice. A certificate of any Bank claiming compensation under this Section 2(d) and setting forth the additional amount or amounts to be paid to it hereunder shall be conclusive in the absence of demonstrable error. In determining such amount, such Bank may use any reasonable averaging and attribution methods.

(e) (i) For the purposes of this Section 2(e), the following terms have the following meanings:

"TAXES" means any and all present or future taxes, duties, levies, imposts, deductions, charges or withholdings with respect to any payment by the Company pursuant to this Agreement, and all liabilities with respect thereto, excluding (i) in the case of each Bank and the Administrative Agent, taxes imposed on its net income, and franchise or similar taxes imposed on it, by the United States, or by the jurisdiction under the laws of which such Bank or the Administrative Agent (as the case may be) is organized or in which its principal executive office is located or, in the case of each Bank, in which its Applicable Booking Office is located and (ii) in the case of each Bank, any United States withholding tax imposed with respect to any payment by the Company pursuant to this Agreement, but only up to the rate (if any) at which United States withholding tax would apply to such payments to such Bank at the time such Bank first becomes a party to this Agreement.

"OTHER TAXES" means any present or future stamp or documentary taxes and any other excise or property taxes, or similar charges or levies, which arise from any payment made pursuant to this Agreement or from the execution or delivery of, or otherwise with respect to, this Agreement or the Letter of Credit.

(ii) Any and all payments by the Company to or for the account of any Bank or the Administrative Agent hereunder shall be made without deduction for any Taxes or Other Taxes; provided that, if the Company shall be required by law to deduct any Taxes or Other Taxes from any such payments, (A) the sum payable shall be increased as necessary so that after making all required deductions for any Taxes or Other Taxes (including deductions applicable to additional sums payable under this Section) such Bank or the Administrative Agent (as the case may be) receives an amount equal to the sum it would have received had no such deductions been made, (B) the Company shall make such deductions, (C) the Company shall pay the full amount deducted to the relevant taxation authority or other authority in accordance with applicable law and (D) the Company shall furnish to the Administrative Agent the original or a certified copy of a receipt evidencing payment thereof.

(iii) The Company agrees to indemnify each Bank and the Administrative Agent for the full amount of Taxes or Other Taxes (including, without limitation, any Taxes or Other Taxes imposed or asserted by any jurisdiction on amounts payable under this Section) paid by such Bank or the Administrative Agent (as the case may be) and any liability (including penalties, interest and expenses) arising therefrom or with respect thereto. This indemnification shall be paid within 30 days after such Bank or the Administrative Agent (as the case may be) makes demand therefor. Such demand shall be made as promptly as practicable, but in any event within 90 days after such Bank obtains actual knowledge of such event; provided, however, that if any Bank fails to make such

demand within 90 days after such Bank obtains knowledge of such event, such Bank shall, with respect to compensation payable in respect of such event, not be entitled to compensation in respect of the costs and losses incurred between the 90th day after such Bank obtains actual knowledge of such event and the date such Bank makes such demand.

(iv) Each Bank organized under the laws of a jurisdiction outside the United States shall provide the Company and the Administrative Agent with Internal Revenue Service Form W-8BEN, W-8ECI, or other type of W-8, as appropriate, or any successor form prescribed by the Internal Revenue Service: (i) on or prior to the date of its execution and delivery of this Agreement in the case of each Bank listed on the signature pages hereof and on or prior to the date on which it becomes a Bank in the case of each other Bank, (ii) before the end of each third calendar year thereafter, and (iii) at any time that a change of circumstances occurs that makes any information on the form so provided incorrect, certifying that such Bank is entitled to benefits under an income tax treaty to which the United States is a party which exempts such Bank from United States withholding tax or reduces the rate of withholding tax on payments under this Agreement or certifying that the income receivable pursuant to this Agreement is effectively connected with the conduct of a trade or business in the United States. Further, each such Bank that is not an exempt recipient listed in Section 6049(b)(4) of the Code shall provide the Company and the Administrative Agent with Internal Revenue Service Form W-8 or W-9, as appropriate, or other successor form prescribed by the Internal Revenue Service, certifying that it is exempt from United States back-up withholding.

(v) For any period with respect to which a Bank has failed to provide the Company or the Administrative Agent with the appropriate forms pursuant to Section 2(e)(iv) (unless such failure is due to a change in treaty, law or regulation occurring subsequent to the date on which such form originally was required to be provided), such Bank shall not be entitled to indemnification under Section 2(e)(ii) or (iii) with respect to Taxes imposed by the United States; provided that if a Bank, which is otherwise exempt from or subject to a reduced rate of withholding tax, becomes subject to Taxes because of its failure to deliver a form required hereunder, the Company shall take such steps as such Bank shall reasonably request to assist such Bank to recover such Taxes.

(vi) If the Company is required to pay additional amounts to or for the account of any Bank pursuant to this Section, then such Bank will change the jurisdiction of its Applicable Booking Office if, in the judgment of such Bank, such change (A) will eliminate or reduce any such

additional payment which may thereafter accrue and (B) is not otherwise disadvantageous to such Bank.

(f) If the payments claimed by any such Bank pursuant to Section 2(d) or Section 2(e) are substantially in excess, as reasonably determined by the Company, relative to the amount of such Bank's Participation, of the payments claimed by the other Banks pursuant to such Sections, the Company shall have the right, with the assistance of the Administrative Agent, to seek one or more mutually satisfactory substitute Eligible Institutions to assume all of the rights and obligations of such Bank in respect of its Participation pursuant to an assignment and assumption agreement in form and substance satisfactory to the Administrative Agent; provided that the aggregate amount of the Participation so assigned to each such Eligible Institution (together with any Participation then held by such Eligible Institution) shall not be less than \$5,000,000.

(g) The Company shall make each payment hereunder to the Administrative Agent at 270 Park Avenue, New York, New York 10017, not later than 2:00 p.m. (New York City time) on the date when due in lawful money of the United States of America and in Federal or other funds immediately available in New York City. Whenever any payment under this Section 2 shall be due on a day which is not a Business Day, the date for payment thereof shall be extended to the next succeeding day that is a Business Day. If the date for any payment of principal is extended by operation of law or otherwise, interest thereon shall be payable for such extended time.

(h) Computations of the letter of credit commission, the fee referred to in Section 2(c), and interest based on the Prime Rate shall be made by the Administrative Agent on the basis of a year of 365 or 366 days, as the case may be, for the actual number of days (including the first day but excluding the last day) elapsed. Computations of all other interest hereunder shall be made by the Administrative Agent on the basis of a year of 360 days for the actual number of days (including the first day but excluding the last day) elapsed.

Section 3. Amendment and Restatement of Letter of Credit; Conditions to Effectiveness; Transitional Provisions. (a) On the terms and conditions herein set forth, the Issuing Bank agrees to execute and deliver to the Equity Participant on the Restatement Effective Date, or, if all of the conditions precedent to the effectiveness of this Amendment and Restatement shall not have been satisfied by 3:00 p.m., New York City time, on the Restatement Effective Date, on the next succeeding Business Day, the Amended and Restated Letter of Credit substantially in the form of Exhibit A hereto, amending and restating the Existing Letter of Credit.

(b) This Amendment and Restatement shall become effective on the date (the "RESTATEMENT EFFECTIVE DATE") on which all of the following conditions shall have been satisfied (or waived in accordance with Section 10):

(i) receipt by the Administrative Agent of a counterpart of this Amendment and Restatement signed by each party hereto;

(ii) receipt by the Administrative Agent of fees payable by the Company on or before the Restatement Effective Date in such amounts and for the accounts of such parties as heretofore mutually agreed pursuant to the Fee Letter;

(iii) receipt by the Administrative Agent of evidence to its satisfaction that all amounts accrued and unpaid under the Existing Reimbursement Agreement to (but not including) the Restatement Effective Date payable by any party thereto have been paid;

(iv) receipt by the Administrative Agent of an opinion of Snell & Wilmer L.L.P., special counsel for the Company, dated the Restatement Effective Date, in form and substance satisfactory to the Administrative Agent;

(v) receipt by the Administrative Agent of an opinion of Davis Polk & Wardwell, special counsel for the Administrative Agent, dated the Restatement Effective Date, in form and substance satisfactory to the Administrative Agent;

(vi) receipt by the Administrative Agent of copies, certified by the Secretary, an Associate Secretary or an Assistant Secretary of the Company, of the resolutions of the Board of Directors of the Company authorizing the execution, delivery and performance of this Amendment and Restatement and the transactions contemplated hereby;

(vii) receipt by the Administrative Agent of a certificate of the Secretary, an Associate Secretary or an Assistant Secretary of the Company, dated the Restatement Effective Date, certifying the names and true signatures of the officers of the Company authorized to sign this Amendment and Restatement;

(viii) receipt by the Administrative Agent of a certificate, dated the Restatement Effective Date, signed by the chief financial officer, vice president, finance, or treasurer of the Company to the effect that (x) (A) no Default or Event of Default; (B) no Reimbursement Default (as defined in the Existing Reimbursement Agreement) and (C) no Reimbursement Default (as defined in this Amendment and Restatement) shall have

occurred and be continuing on the Restatement Effective Date or would result from the amendment and restatement of the Letter of Credit pursuant to subsection (a) of this Section 3; and (y) that the representations and warranties of the Company set forth in Section 6 of this Amendment and Restatement shall be true and correct on and as of the Restatement Effective Date as though made on and as of such date;

(ix) receipt by the Administrative Agent of certified copies of all approvals, authorizations, orders or consents of, or notices to or registrations with, any governmental body or agency, if any, required for the Company to enter into this Amendment and Restatement;

(x) receipt by the Administrative Agent of such other approvals, opinions or documents as the Administrative Agent may reasonably request; and

(xi) receipt by the Administrative Agent of all documents the Administrative Agent may reasonably request relating to the existence of the Company, the corporate authority for and the validity of this Amendment and Restatement and any other matters relevant hereto;

provided that all documents (or copies thereof) to be delivered to the Administrative Agent on or before the Restatement Effective Date shall be provided to each Bank and shall be in form and substance satisfactory to the Required Banks.

(c) Promptly after this Amendment and Restatement becomes effective, the Administrative Agent shall give notice thereof and of the Restatement Effective Date to each party hereto. Immediately upon the effectiveness of this Amendment and Restatement, the Issuing Bank will be obligated to extend the Letter of Credit as provided in subsection (a) of this Section 3 and each party hereto will be bound by the provisions of this subsection (c). The rights and obligations of the parties hereto on and after the Restatement Effective Date shall be governed by the provisions of this Amendment and Restatement and as the same may be further amended and in effect from time to time thereafter. The rights and obligations of the parties hereto with respect to the period prior to the Restatement Effective Date will continue to be governed by the provisions of this Agreement as in effect prior to the Restatement Effective Date.

(d) Each of the parties hereto (other than Citibank, N.A. and KBC Bank NV), together comprising all of the parties to the Existing Reimbursement Agreement and their successors in such capacity, hereby agrees that by its execution hereof, it is deemed to have provided each written consent or agreement required on its part under Sections 10 and 17 of the Existing Reimbursement Agreement to the extension and amendment of the Existing Letter of Credit and

the amendment and restatement of the Existing Reimbursement Agreement on the terms provided herein.

Section 4. Adjustment of Maximum Drawing Amount; Terms of Drawing. The Maximum Drawing Amount shall be modified as specified in the third paragraph of the Letter of Credit and drawings under the Letter of Credit shall be subject to the other terms and conditions set forth in the Letter of Credit.

Section 5. Obligations Absolute. The payment obligations of the Company under this Agreement shall be absolute, unconditional and irrevocable, and shall be performed strictly in accordance with the terms of this Agreement under all circumstances whatsoever, including, without limitation, the following circumstances:

(i) any lack of validity or enforceability of the Letter of Credit or any of the Transaction Documents or Financing Documents;

(ii) any amendment or waiver of or any consent to departure from all or any of the Transaction Documents or Financing Documents;

(iii) the existence of any claim, set-off, defense or other rights which the Company may have at any time against the Equity Participant, the Owner Trustee or any transferee of the Letter of Credit (or any persons or entities for whom any of the foregoing may be acting), the Administrative Agent, any Bank, any Participant or any other person or entity, whether in connection with this Agreement, the Transaction Documents or Financing Documents, the transactions contemplated hereby or thereby or any unrelated transaction; provided that nothing herein shall prevent the assertion of such claim by separate suit or compulsory counterclaim;

(iv) any statement or any other document presented under the Letter of Credit proving to be forged, fraudulent, invalid or insufficient in any respect or any statement therein being untrue or inaccurate in any respect whatsoever;

(v) payment by the Issuing Bank under the Letter of Credit against presentation of a draft or certificate which does not comply with the terms of the Letter of Credit; or

(vi) any other circumstance or happening whatsoever, whether or not similar to any of the foregoing.

Section 6. Representations and Warranties of the Company. The Company represents and warrants as of the Restatement Effective Date as follows:

(a) Corporate Existence. Each of the Company and each Material Subsidiary: (i) is a corporation duly organized and validly existing under the laws of the jurisdiction of its incorporation; (ii) has all requisite corporate power necessary to own its assets and carry on its business as presently conducted; (iii) has all governmental licenses, authorizations, consents and approvals necessary to own its assets and carry on its business as presently conducted, unless the failure to have any such license, authorization, consent or approval would not have a material adverse effect on the financial condition or financial prospects of the Company and its Consolidated Subsidiaries, taken as a whole, and except as disclosed in the Financial Information or by written notice delivered to the Banks more than five Business Days prior to the execution and delivery of this Amendment and Restatement; and (iv) is qualified to do business in all jurisdictions in which the nature of the business conducted by it makes such qualification necessary and where failure so to qualify would have a material adverse effect on the financial condition or financial prospects of the Company and its Consolidated Subsidiaries, taken as a whole. All of the issued and outstanding common stock of the Company is owned by PWCC.

(b) Noncontravention, Etc. The execution, delivery, and performance by the Company of this Agreement are within the Company's corporate powers, have been duly authorized by all necessary corporate action, and do not (i) contravene the Company's charter or by-laws or (ii) contravene any Applicable Law or any contractual restriction binding on or affecting the Company. The execution, delivery, and performance by the Company of this Agreement do not cause the creation or imposition of any Lien upon the assets of the Company or any Material Subsidiary, except as it may be necessary for the Company to grant a Lien to the Administrative Agent for the benefit of the Banks pursuant to Section 8(c).

(c) Approvals. No authorization or approval or other action by, and no notice to or filing or registration with, any governmental authority or regulatory body is required for the due execution, delivery and performance by the Company of this Agreement, except for (w) the 1986 Order which has been duly issued by the ACC and is in full force and effect in the form originally issued, (x) such other Governmental Actions as have been duly obtained, given or accomplished, (y) the filing with the ACC of a copy of this Agreement within five days of the execution hereof, in accordance with the 1986 Order and (z) as may be required under Applicable Law not now in effect. The execution, delivery, and performance by the Company of this Agreement do not require the consent or approval of the Equity Participant or the Owner Trustee (except as specified in this Agreement) or PWCC or any trustee or holder of any indebtedness or other obligation of the Company, other than such consents and approvals as have been duly obtained, given or accomplished. No Governmental Action by any Federal, Arizona or New York Governmental Authority relating to the Securities Act, the Securities Exchange Act, the Trust Indenture Act, the Federal Power Act, the Atomic

Energy Act, the Nuclear Waste Act, the Holding Company Act, the Arizona Public Utility Act, energy or nuclear matters, public utilities, the environment, health and safety or Unit 2 is or will be required in connection with the participation by the Administrative Agent, any Bank or any Participant in the consummation of the transactions contemplated by this Agreement, except such Governmental Actions (A) as have been, duly obtained, given or accomplished or (B) as may be required by Applicable Law not now in effect.

(d) Binding Agreement. This Agreement is a legal, valid and binding obligation of the Company enforceable against the Company in accordance with its terms, subject, however, to the application by a court of general principles of equity and to the effect of any applicable bankruptcy, insolvency, reorganization, moratorium or similar laws affecting creditors' rights generally.

(e) Litigation. There is no pending or (to the knowledge of the Company) threatened action or proceeding affecting the Company or any of its Subsidiaries before any court, governmental agency or arbitrator, that, if adversely determined, could have a material adverse effect on the financial condition or financial prospects of the Company and its Consolidated Subsidiaries, taken as a whole, except as disclosed in the Financial Information or by written notice delivered to the Banks more than five Business Days prior to the execution and delivery of this Amendment and Restatement.

(f) Financial Statements. The balance sheet of the Company and its Consolidated Subsidiaries as of December 31, 2004 and the related statements of income and cash flows of the Company and its Consolidated Subsidiaries for the fiscal year then ended, copies of which have been furnished to the Banks, fairly present in all material respects the financial condition of the Company and its Consolidated Subsidiaries as of such date and the results of operations and cash flows of the Company and its Consolidated Subsidiaries for such fiscal year, all in accordance with generally accepted accounting principles consistently applied (except as disclosed therein). The balance sheet of the Company and its Consolidated Subsidiaries as of March 31, 2005 and the related statements of income and cash flows of the Company and its Consolidated Subsidiaries for the quarter then ended, copies of which have been furnished to the Banks, fairly present in all material respects the financial condition of the Company and its Consolidated Subsidiaries as of such date and the results of operations and cash flows of the Company and its Consolidated Subsidiaries for the quarter then ended, all in accordance with generally accepted accounting principles consistently applied (except as disclosed therein and subject to normal year-end audit adjustments). Since March 31, 2005, there has been no material adverse change in the financial condition or financial prospects of the Company and its Consolidated Subsidiaries, taken as a whole.

(g) ERISA. The Company and the ERISA Affiliates have fulfilled their respective obligations under the minimum funding standards of ERISA and the Code with respect to each Plan and are in compliance in all material respects with the presently applicable provisions of ERISA and the Code, and have not incurred any liability to the PBGC or any Plan or Multiemployer Plan, other than liability to the PBGC for premiums prior to the due date for such premiums and liability to any Plan maintained by the Company or an ERISA Affiliate or to any Multiemployer Plan for contributions prior to the due date for such contributions which shall be paid in accordance with the provisions of the minimum funding standards of ERISA and the Code.

(h) Taxes. The Company and its Subsidiaries have filed all United States Federal income tax returns and all other material tax returns which are required to be filed by them and have paid all taxes due pursuant to such returns or pursuant to any assessment received by the Company or any of its Subsidiaries, except to the extent that (i) such taxes are being contested in good faith and by appropriate proceedings and appropriate reserves for the payment thereof have been maintained by the Company and its Subsidiaries in accordance with generally accepted accounting principles or (ii) the failure to make such filings or such payments is not likely to have a material adverse effect on the financial condition or the financial prospects of the Company and its Consolidated Subsidiaries, taken as a whole. The charges, accruals and reserves on the books of the Company and its Material Subsidiaries as set forth in the most recent financial statements of the Company delivered to the Banks pursuant to Section 6(f) or Section 7(g)(i) or Section 7(g)(ii) hereof in respect of taxes and other governmental charges are, in the opinion of the Company, adequate.

(i) Environmental. The operations and properties of the Company and its Subsidiaries comply in all material respects with all environmental laws, the noncompliance with which would have a material adverse effect on the financial condition or financial prospects of the Company and its Consolidated Subsidiaries taken as a whole, except as disclosed in the Financial Information or by written notice delivered to the Banks more than five Business Days prior to the execution and delivery of this Amendment and Restatement.

(j) Investment Company. The Company is not an "investment company", or a company "controlled" by an "investment company", within the meaning of the Investment Company Act of 1940, as amended.

(k) No Material Misstatements or Omissions. The Financial Information did not, and any documents to be filed with the Securities and Exchange Commission and delivered to the Banks pursuant to Section 7(g)(i) or Section 7(g)(ii) after December 31, 2004 will not, as of the date furnished, contain any untrue statement of a material fact or omit to state any material fact necessary

to make the statements made therein, in the light of the circumstances under which they were or shall be made, not misleading.

(1) No Amendments. Except as provided to the Banks prior to the Restatement Effective Date, there has been no amendment or waiver of, or consent with respect to, the payment obligations of the Company under any Transaction Document or Financing Document since March 17, 1993.

Section 7. Affirmative Covenants. So long as a drawing is available under the Letter of Credit or the Company shall have any obligation to pay any amount hereunder to or for the account of the Administrative Agent or any Bank, the Company will, unless the Required Banks shall otherwise consent in writing:

(a) Preservation of Corporate Existence, Business, Etc. (i) Preserve and maintain its corporate existence and all rights and privileges (other than "franchises" as described in Arizona Revised Statutes, Section 40-283 or any successor provision) reasonably necessary in the normal conduct of its business, unless the failure to maintain such rights and privileges would not have a material adverse effect on the financial condition or financial prospects of the Company and its Consolidated Subsidiaries taken as a whole, and use its best efforts to preserve and maintain such franchises reasonably necessary in the normal conduct of its business, except that (A) the Company from time to time may make minor extensions of its lines, plants, services or systems prior to the time a related franchise, certificate of convenience and necessity, license or permit is procured, (B) from time to time communities served by the Company may become incorporated and considerable time may elapse before such a franchise is procured, (C) certain such franchises may have expired prior to the renegotiation thereof, (D) certain minor defects and exceptions may exist which, individually and in the aggregate, are not material and (E) certain franchises, certificates, licenses and permits may not be specific as to their geographical scope.

(ii) Continue to conduct the same general type of business conducted on May 19, 2005.

(b) Compliance with Laws, Etc. (i) Comply, and cause each Material Subsidiary to comply, in all material respects with all applicable laws, rules, regulations and orders of governmental or regulatory authorities if the failure to comply would have a material adverse effect on the financial condition or financial prospects of the Company and its Consolidated Subsidiaries, taken as a whole.

(ii) Comply at all times with the 1986 Order and any Subsequent Order, unless the failure to so comply could not affect the validity or enforceability of the indebtedness of the Company pursuant to this Agreement.

(c) Payment of Taxes and Claims. Pay and discharge, and cause each of its Subsidiaries to pay and discharge, before the same shall become delinquent, all taxes, assessments and governmental charges or levies imposed on it or its property; provided that neither the Company nor any of its Subsidiaries shall be required to pay or discharge any such tax, assessment, charge or levy (i) that is being contested in good faith and by proper proceedings and as to which adequate reserves are being maintained in accordance with generally accepted accounting principles or (ii) if the failure to pay such tax, assessment, charge or levy is not likely to have a material adverse effect on the financial condition or financial prospects of the Company and its Consolidated Subsidiaries, taken as a whole.

(d) Maintenance of Insurance. Maintain, and cause each Material Subsidiary to maintain, insurance, either with responsible and reputable insurance companies or associations, or through its own program of self-insurance, in such amounts and covering such risks as is usually carried by companies engaged in similar businesses and owning similar properties in the same general areas in which the Company or such Material Subsidiary operates.

(e) Visitation Rights. Permit, and cause each of its Subsidiaries to permit, at any reasonable time and from time to time, any Bank or any of its agents or representatives to examine and make copies of and abstracts from the records and books of account of, and visit the properties of, the Company and any of its Subsidiaries, and to discuss the affairs, finances and accounts of the Company and any of its Subsidiaries with any of their respective officers or directors; provided that the Company and its Subsidiaries reserve the right to restrict access to any of its properties in accordance with reasonably adopted procedures relating to safety and security; and provided further that the costs and expenses incurred by any Bank or its agents or representatives in connection with any such examinations, copies, abstracts, visits or discussions shall be, upon the occurrence and during the continuation of a Reimbursement Default, for the account of the Company and, in all other circumstances, for the account of such Bank.

(f) Maintenance of Property. Keep, and cause each Material Subsidiary to keep, all property useful and necessary in its business in good working order and condition (ordinary wear and tear excepted), it being understood that this covenant relates only to the working order and condition of such properties and shall not be construed as a covenant not to dispose of properties.

(g) Reporting Requirements. Furnish to each of the Banks:

(i) as soon as available and in any event within 60 days after the end of each of the first three fiscal quarters of each fiscal year of the Company, (A) for each such fiscal quarter of the Company, statements of income and cash flows of the Company and its Consolidated Subsidiaries

for such fiscal quarter and the related balance sheet of the Company and its Consolidated Subsidiaries as at the end of such fiscal quarter, setting forth in each case in comparative form the corresponding figures for the corresponding fiscal quarter in the preceding fiscal year and (B) for the period commencing at the end of the previous fiscal year and ending with the end of such fiscal quarter, statements of income and cash flows of the Company and its Consolidated Subsidiaries for such period setting forth in each case in comparative form the corresponding figures for the corresponding period in the preceding fiscal year; provided that so long as the Company remains subject to the reporting requirements of the Securities Exchange Act of 1934, as amended, the Company may provide, in satisfaction of the requirements of this first sentence of this Section 7(g)(i), its report on Form 10-Q for such fiscal quarter. Each set of financial statements provided under this Section 7(g)(i) shall be accompanied by a certificate of an Authorized Officer, which certificate shall state that said financial statements fairly present in all material respects the financial condition and results of operations and cash flows of the Company and its Consolidated Subsidiaries in accordance with generally accepted accounting principles, consistently applied (except as disclosed therein), as at the end of, and for, such period (subject to normal year-end audit adjustments);

(ii) as soon as available and in any event within 90 days after the end of each fiscal year of the Company, statements of income, changes in common stock equity and cash flows of the Company and its Consolidated Subsidiaries for such year and the related balance sheets of the Company and its Consolidated Subsidiaries as at the end of such year, setting forth in each case in comparative form the corresponding figures for the preceding fiscal year; provided that, so long as the Company remains subject to the reporting requirements of the Securities Exchange Act of 1934, as amended, the Company may provide, in satisfaction of the requirements of this first sentence of this Section 7(g)(ii), its report on Form 10-K for such fiscal year. Each set of financial statements provided pursuant to this Section 7(g)(ii) shall be accompanied by an opinion thereon of independent certified public accountants of recognized national standing, which opinion shall state that said financial statements fairly present in all material respects the financial condition and results of operations and cash flows of the Company and its Consolidated Subsidiaries as at the end of, and for, such fiscal year, in accordance with generally accepted accounting principles consistently applied (except as disclosed therein);

(iii) as soon as possible and in any event within ten days after an Authorized Officer knows of the occurrence of any Reimbursement Default continuing on the date of such statement, a statement of an

Authorized Officer setting forth details of such Reimbursement Default and the action which the Company has taken and proposes to take with respect thereto;

(iv) as soon as possible, and in any event within ten days after an Authorized Officer knows that any of the events or conditions specified below with respect to any Plan or Multiemployer Plan have occurred or exist, a statement signed by an Authorized Officer setting forth details respecting such event or condition and the action, if any, which the Company or its ERISA Affiliate proposes to take with respect thereto (and a copy of any report or notice required to be filed with or given to the PBGC by the Company or an ERISA Affiliate with respect to such event or condition):

(A) any reportable event, as defined in Section 4043 of ERISA and the regulations issued thereunder, with respect to a Plan, as to which the PBGC has not by regulation or other ruling or notice of general applicability waived the requirement of Section 4043(a) of ERISA that it be notified within 30 days of the occurrence of such event; provided that a failure to meet the minimum funding standard of Section 412 of the Code or Section 302 of ERISA shall be a reportable event regardless of the issuance of any waivers in accordance with Section 412(d) of the Code;

(B) the filing under Section 4041(c) of ERISA of a notice of intent to terminate any Plan in a distress termination or the termination of any Plan in a distress termination;

(C) the institution by the PBGC of proceedings under Section 4042 of ERISA for the termination of, or the appointment of a trustee to administer, any Plan, or the receipt by the Company or any ERISA Affiliate of a notice from a Multiemployer Plan that such action has been taken by the PBGC with respect to such Multiemployer Plan;

(D) the complete or partial withdrawal by the Company or any ERISA Affiliate under Part 1 of Subtitle E of Title IV of ERISA from a Multiemployer Plan, or the receipt by the Company or any ERISA Affiliate of notice from a Multiemployer Plan that it is in reorganization or insolvency pursuant to Section 4241 or 4245 of ERISA or that it intends to terminate or has terminated under Section 4041A of ERISA; and

(E) the institution of a proceeding by a fiduciary of any Multiemployer Plan against the Company or any ERISA Affiliate to enforce Section 515 of ERISA, which proceeding is not dismissed within 45 days;

(v) promptly after (A) any amendment or modification of the 1986 Order or (B) the promulgation, amendment or modification of any Subsequent Order by the ACC, a copy thereof;

(vi) promptly after the sending or filing thereof, copies of all reports which the Company sends to its public security holders as a group, and copies of all reports and registration statements which the Company or any of its Subsidiaries files with the Securities and Exchange Commission or any national securities exchange;

(vii) as soon as practicable and in any event within 30 days after the execution thereof, a copy of each amendment, waiver or consent relating to the payment obligations of the Company under any Transaction Document or Financing Document; and

(viii) such other information respecting the condition or operations, financial or otherwise, of the Company or any of its Subsidiaries as the Administrative Agent at the request of any Bank may from time to time reasonably request.

The Company will furnish to the Banks, at the time it furnishes each set of financial statements pursuant to Section 7(g)(i) or 7(g)(ii) above, a certificate of an Authorized Officer (x) to the effect that no Reimbursement Default has occurred and is continuing (or, if any Reimbursement Default has occurred and is continuing, describing the same in reasonable detail and describing the action that the Company has taken and proposes to take with respect thereto) and (y) setting forth in reasonable detail the computations necessary to determine whether the Company is in compliance with Sections 7(h) and 8(e) as of the end of the relevant fiscal quarter or fiscal year.

Financial statements required to be delivered pursuant to clause (i) or (ii) of Section 7(g) or reports and registration statements required to be delivered pursuant to clause (vi) of Section 7(g) (to the extent any such documents are included in materials otherwise filed with the Securities and Exchange Commission) may be delivered electronically and if so delivered, shall be deemed to have been delivered on the date (i) on which the Company posts such documents, or provides a link thereto on the Company's website on the Internet at the website address at <http://www.pinnaclewest.com/main/pnw/investors/financials/filings/default.html>; or (ii) on which such documents are posted on the Company's behalf on an

Internet or intranet website, if any, to which each Bank and the Administrative Agent have access (whether a commercial, third-party website or whether sponsored by the Administrative Agent)); provided that: (x) the Company shall deliver paper copies of such documents to any Bank that requests the Company to deliver such paper copies until a written request to cease delivering paper copies is given by such Bank and (y) the Company shall notify each Bank (which notice may be given by telecopier or electronic mail) of the posting of any such documents and provide to each Bank by electronic mail electronic versions (i.e., soft copies) of such documents. Notwithstanding anything contained herein, in every instance the Company shall be required to provide to the Banks paper copies of certificates of Authorized Officers required under Section 7(g). The Company hereby acknowledges that the Administrative Agent may make available to the Banks materials and/or information provided by or on behalf of the Company hereunder (collectively, "COMPANY MATERIALS") by posting the Company Materials on IntraLinks or another similar electronic system (the "PLATFORM"); provided, however, that to the extent such Company Materials constitute Confidential Information, they shall be treated as set forth in Section 22.

(h) Consolidated Cash Coverage Ratio. Maintain for each twelve-month period ending on the last day of each fiscal quarter (determined as of the last day of such fiscal quarter) a Consolidated Cash Coverage Ratio of no less than 2.0:1.0.

(i) Filing with ACC. File a copy of this Amendment and Restatement, as executed by each of the parties hereto, with the ACC within five days of the execution hereof.

Section 8 . Negative Covenants. So long as a drawing is available under the Letter of Credit or the Company shall have any obligation to pay any amount hereunder to or for the account of the Administrative Agent or any Bank, the Company will not, without the written consent of the Required Banks:

(a) Sale of Assets. Permit the Company nor any Material Subsidiary to, in one or a series of transactions after December 31, 2004, sell, lease, transfer or otherwise dispose of assets to any Person other than the Company or any Subsidiary of the Company (excluding individual dispositions occurring in the ordinary course of business which involve assets with a book value not exceeding \$5,000,000) if, immediately after giving effect to such transaction, the aggregate book value of the assets disposed of in all such transactions after December 31, 2004, would equal or exceed 30% of the total of all assets properly appearing on the December 31, 2004 balance sheet of the Company and its Consolidated Subsidiaries included in its annual report on Form 10-K for the year ended December 31, 2004. No Lien on any asset will be considered a sale, lease, transfer or disposition under this provision, but will be governed exclusively under Section 8(c).

(b) Mergers, Etc. Merge or consolidate with or into any Person, or permit any Material Subsidiary to do so, except that:

(i) any Material Subsidiary may merge with any Wholly-Owned Subsidiary of the Company;

(ii) any Material Subsidiary may merge into the Company; and

(iii) the Company may merge with, and any Material Subsidiary may merge with, any other Person;

provided that, in each case, immediately after giving effect to such proposed transaction, no Reimbursement Default would exist; and provided further that, in the case of any such merger to which the Company is a party, the Company is the surviving corporation and in the case of any such merger to which any Material Subsidiary and any other Person are the parties, such Material Subsidiary is the surviving corporation.

(c) Negative Pledge. Permit the aggregate amount of all claims secured by Liens (other than Permitted Liens) upon or with respect to any of its assets or the assets of any of its Material Subsidiaries, whether now owned or hereafter acquired, to exceed 55% of Total Assets, unless the Company shall simultaneously (i) grant to the Administrative Agent, for the benefit of the Banks, Liens on its assets as collateral for its obligations under this Agreement in a form and on terms satisfactory to the Administrative Agent and the Required Banks in their sole and absolute discretion and (ii) obtain the consent of the Equity Participant thereto.

(d) Assignment of Transaction Documents or Financing Documents. Enter into any assignment of the Company's obligations under any of the Transaction Documents or Financing Documents.

(e) Indebtedness. Permit Consolidated Indebtedness to exceed 65% of Consolidated Capitalization at any time.

"CONSOLIDATED CAPITALIZATION" means, at any date, the sum as of such date of Consolidated Indebtedness and Consolidated Net Worth.

"CONSOLIDATED INDEBTEDNESS" means, at any date, the Indebtedness of the Company and its Consolidated Subsidiaries determined on a consolidated basis as of such date.

"CONSOLIDATED NET WORTH" means, at any date, the sum as of such date of (a) the par value (or value stated on the books of the Company) of all classes of capital stock of the Company and its Subsidiaries, excluding the Company's capital stock owned by the Company and/or its Subsidiaries, plus (or minus in the

case of a surplus deficit) (b) the amount of the consolidated surplus, whether capital or earned, of the Company, determined in accordance with generally accepted accounting principles as of the end of the most recent calendar month (excluding (x) cumulative charges of up to \$300 million to consolidated surplus resulting from, or in anticipation of, discontinuation of Financial Accounting Standards Board Statement No. 71, accounting for all or part of the business and (y) the effect on the Company's accumulated other comprehensive income/loss of the ongoing application of Financial Accounting Standards Board Statement No. 133).

Section 9 . Reimbursement Events of Default. If any of the following events ("REIMBURSEMENT EVENTS OF DEFAULT") shall occur and be continuing:

(i) The Company shall fail to pay when due any amount payable under Section 2(a) or fail to pay any other amount payable under Section 2 within five Business Days after the same becomes due and payable; or

(ii) The Company shall fail to perform or observe (A) any term, covenant or agreement contained in Section 7(a)(ii), 7(g)(iv), 7(h), 8(a), 8(b), 8(c), 8(e), or (B) any term, covenant or agreement contained in this Agreement (other than those covered by clause (i) above or subclause (A) of this clause (ii) or Section 7(e) or Section 19) on its part to be performed or observed if the failure to perform or observe such term, covenant or agreement shall remain unremedied for 30 days after written notice thereof shall have been given to the Company by the Administrative Agent; or

(iii) Any representation or warranty made by the Company herein or by the Company (or any of its officers) in any certificate delivered in connection with this Agreement shall prove to have been false or misleading in any material respect when made; or

(iv) Any material provision of this Agreement shall at any time for any reason cease to be valid and binding upon the Company, or shall be declared to be null and void, or the validity or enforceability thereof shall be contested by the Company or any governmental agency or authority, or the Company shall deny that it has any or further liability or obligation under this Agreement; or

(v) The Company shall fail to pay any principal of or premium or interest on any Indebtedness which is outstanding in a principal amount of at least \$5,000,000 (but excluding Indebtedness owing hereunder) of the Company, when the same becomes due and payable (whether by scheduled maturity, required prepayment, acceleration, demand or

otherwise), and such failure shall continue after the applicable grace period, if any, specified in the agreement or instrument relating to such Indebtedness; or the Company shall fail to perform or comply with any other term or covenant in any agreement or instrument relating to any such Indebtedness and such failure shall continue after the applicable grace period, if any, specified in such agreement or instrument, if the effect of such failure is to accelerate, or to permit the acceleration of, the maturity of such Indebtedness; or

(vi) The Company shall fail to pay any principal of or premium or interest in respect of any operating lease in respect of which the payment obligations of the Company have a present value of at least \$25,000,000, when the same becomes due and payable (whether by scheduled maturity, required prepayment, acceleration, demand or otherwise), and such failure shall continue after the applicable grace period, if any, specified in such operating lease, if the effect of such failure is to terminate, or to permit the termination of, such operating lease; or

(vii) The Company shall generally not pay its debts as such debts become due, or shall admit in writing its inability to pay its debts generally, or shall make a general assignment for the benefit of creditors; or any proceeding shall be instituted by or against the Company seeking to adjudicate it a bankrupt or insolvent, or seeking liquidation, winding up, reorganization, arrangement, adjustment, protection, relief, or composition of it or its debts under any law relating to bankruptcy, insolvency or reorganization or relief of debtors, or seeking the entry of an order for relief or the appointment of a receiver, trustee, custodian or other similar official for it or for any substantial part of its property and, in the case of any such proceeding instituted against it (but not instituted by it), either such proceeding shall remain undismissed or unstayed for a period of 60 days, or any of the actions sought in such proceeding (including, without limitation, the entry of an order for relief against, or the appointment of a receiver, trustee, custodian or other similar official for, it or for any substantial part of its property) shall occur; or the Company shall take any corporate action to authorize any of the actions set forth above in this clause (vii); or

(viii) Any Material Subsidiary shall generally not pay its debts as such debts become due, or shall admit in writing its inability to pay its debts generally, or shall make a general assignment for the benefit of creditors; or any proceeding shall be instituted by or against any Material Subsidiary seeking to adjudicate it a bankrupt or insolvent, or seeking liquidation, winding up, reorganization, arrangement, adjustment, protection, relief, or composition of it or its debts under any law relating to bankruptcy, insolvency or reorganization or relief of debtors, or seeking

the entry of an order for relief or the appointment of a receiver, trustee, custodian or other similar official for it or for any substantial part of its property and, in the case of any such proceeding instituted against it (but not instituted by it), either such proceeding shall remain undismissed or unstayed for a period of 60 days, or any of the actions sought in such proceeding (including, without limitation, the entry of an order for relief against, or the appointment of a receiver, trustee, custodian or other similar official for it or for any substantial part of its property) shall occur; or any Material Subsidiary shall take any corporate action to authorize any of the actions set forth above in this clause (viii) and, in each case, the Required Banks determine that such circumstances could have a material adverse effect on the financial condition or financial prospects of the Company and its Consolidated Subsidiaries, taken as a whole; or

(ix) Any judgment or order for the payment of money that exceeds any applicable insurance coverage by more than \$5,000,000 shall be rendered against the Company and such judgment or order shall remain unsatisfied or unstayed for a period of 30 days; or

(x) Any judgment or order for the payment of money that exceeds any applicable insurance coverage by more than \$25,000,000 shall be rendered against any Material Subsidiary; such judgment or order shall remain unsatisfied or unstayed for 30 days; and the Required Banks determine that such judgment or order could have a material adverse effect on the financial condition or financial prospects of the Company and its Consolidated Subsidiaries, taken as a whole; or

(xi) An event or condition specified in Section 7(g)(iv) shall occur or exist with respect to any Plan or Multiemployer Plan and, as a result of such event or condition, together with all other such events or conditions, the Company or any ERISA Affiliate shall incur or in the opinion of the Required Banks shall be reasonably likely to incur a liability to a Plan, a Multiemployer Plan or the PBGC (or any combination of the foregoing) which is, in the determination of the Required Banks, material in relation to the financial condition or the financial prospects of the Company and its Consolidated Subsidiaries, taken as a whole; or

(xii) any change in Applicable Law or any Governmental Action shall occur which has the effect of making the transactions contemplated by the Transaction Documents unauthorized, illegal or otherwise contrary to Applicable Law; or

(xiii) any event specified in subsection (vii), (viii) or (x) of Section 15 of the Facility Lease shall occur; or

(xiv) the Company shall fail to make, or cause to be made, any payment specified in Section 15(i) of the Facility Lease equal to or exceeding \$1,000,000 within the periods specified in that Section.

then, in every such event the Issuing Bank may, and if instructed to do so by the Required Banks the Issuing Bank shall, by notice to the Company and the Equity Participant, terminate the Letter of Credit as provided therein. The Administrative Agent shall give notice to the Company under Section 9(ii) promptly upon being requested to do so by the Required Banks and will promptly notify each Bank of any such notice given at the request of the Required Banks.

Section 10 . Amendments and Waivers. No modification, amendment or waiver of any provision of this Agreement or the Letter of Credit or any consent to the assignment of the Company's obligations under any of the Transaction Documents or the Financing Documents shall be effective unless the same shall be in writing and signed by (or with the written consent of) the Company and the Required Banks (and, if the rights or duties of the Issuing Bank or the Administrative Agent are affected thereby, by it); provided that no such modification, amendment, waiver or consent shall, unless signed by (or with the written consent of) each Bank affected thereby, (i) increase the Maximum Credit Amount or Maximum Drawing Amount or subject any Bank to any additional obligation under this Agreement or the Letter of Credit, (ii) reduce the principal of or rate of interest on any reimbursement obligation or reduce the letter of credit commission payable under Section 2(b), (iii) postpone the date fixed for any payment of principal of or interest on any reimbursement obligation or any payment of such letter of credit commission, (iv) extend the Stated Termination Date or the Termination Date or (v) change the definition of Required Banks or the provisions of this Section 10 or any provision of this Agreement that requires action by all the Banks. Any waiver of any provision of this Agreement or the Letter of Credit shall be effective only in the specific instance and for the specific purpose for which given.

Section 11 . Notices. (a) All notices, requests, demands and other communications provided for hereunder shall, unless otherwise stated herein, be in writing (including facsimile transmission, electronic transmission (subject to Section 11(c) below), or similar transmission) and mailed, sent or delivered:

(i) if to the Company, in the case of deliveries, to its street address at 400 North Fifth Street, Phoenix, Arizona 85004; in the case of mailings, to its mailing address at P.O. Box 53999, Phoenix, Arizona 85072-3999, and in the case of facsimile transmission, to telecopy no. (602) 250-5640, in each case to the attention of the Treasurer; and in the case of electronic mail, to Barbara.Gomez@pinnaclewest.com;

(ii) if to the Administrative Agent, in the case of deliveries or mailings, to its address at 1111 Fannin Street, 10th Floor, Houston, Texas 77002, and in the case of facsimile transmission, to telecopy no. 713-427-6307, in each case to the attention of Kelly Collins, Loan and Agency Services; and in the case of electronic mail, to kelly.collins@jpmchase.com;

(iii) if to the Issuing Bank, in the case of deliveries or mailings, to its address at JPMorgan Chase Bank, N.A., c/o JPMorgan Treasury Services, 10420 Highland Manor Drive, 4th Floor, Tampa, Florida 33610, and in the case of facsimile transmission, to telecopy no. 813-432-5161, in each case to the attention of James Alonzo, Standby Letter of Credit Manager - Immediate Action Required; and in the case of electronic mail, to james.alonzo@chase.com;

(iv) if to any other Bank, at such address, electronic mail address, or telecopy number as shall be designated by it in its Administrative Questionnaire;

or, as to each party, to such other person and/or to such other address or number as shall be designated by such party in a written notice to each other party. All such notices, requests, demands and other communications shall be effective when mailed or sent, addressed as aforesaid (subject to Section 11(c) below in the case of electronic communications), except that notices to the Administrative Agent shall not be effective until received by the Administrative Agent and any notice to the Equity Participant pursuant to Section 9 shall not be effective until received by the Equity Participant. Notices of any Reimbursement Default shall be sent by the Company to the Administrative Agent by facsimile transmission.

(b) As promptly as practicable after receipt by the Administrative Agent of any notice or other communication delivered hereunder by the Company, the Administrative Agent shall furnish a copy thereof to each Bank, to the extent such notice or other communication is not otherwise required by the terms thereof to be delivered by the Company to each Bank.

(c) Notices and other communications to the Banks hereunder may be delivered or furnished by electronic communications pursuant to procedures approved by the Administrative Agent (including electronic mail and Internet websites); provided that the foregoing shall not apply to notices pursuant to Sections 2, 14 or 17 unless otherwise agreed by the Administrative Agent and the applicable Bank. The Administrative Agent and the Company may, each in its discretion, agree to accept notices and other communications to it hereunder by electronic communications pursuant to procedures approved by it; provided that approval of such procedures may be limited to particular notices or communications. Notices and other communications sent to an electronic mail

address shall be deemed received upon the sender's receipt of an acknowledgement from the intended recipient (such as by the "return receipt requested" function, as available, return electronic mail or other written acknowledgement); provided that (x) if such notice or other communication is not sent during the normal business hours of the recipient, such notice or communication shall be deemed to have been sent at the opening of business on the next business day for the recipient, and (y) notices or communications posted to an Internet website shall be deemed received upon the deemed receipt by the intended recipient at its electronic mail address as described in immediately foregoing clause (x) of notification that such notice or communication is available and identifying the website address therefor.

(d) The Platform is provided "as is" and "as available." The Agent Parties (as defined below) do not warrant the accuracy or completeness of the Company Materials or the adequacy of the Platform, and expressly disclaim any liability for errors in or omissions from the Company Materials. No warranty of any kind, express or implied or statutory, is made by any Agent Party in connection with the Company Materials or the Platform. In no event shall the Administrative Agent, its Affiliates, or any partners, directors, officers, employees, agents and advisors of the Administrative Agent or of its Affiliates (collectively, the "AGENT PARTIES") have any liability to the Company, any Bank or any other Person for losses, claims, damages, liabilities or expenses of any kind (whether in tort, contract or otherwise) arising out of the Company's or the Administrative Agent's transmission of Company Materials through the Internet, except to the extent that such losses, claims, damages, liabilities or expenses are determined by a court of competent jurisdiction by a final and nonappealable judgment to have resulted from the gross negligence or willful misconduct of such Agent Party; provided, however, that in no event shall any Agent Party have any liability to the Company, any Bank, or any other Person for indirect, special, incidental, consequential or punitive damages (as opposed to direct or actual damages).

Section 12 . No Waiver; Remedies. No failure on the part of the Administrative Agent or any Bank to exercise, and no delay in exercising, any right, power, or privilege hereunder shall operate as a waiver thereof; nor shall any single or partial exercise of any right hereunder preclude any other or further exercise thereof or the exercise of any other right. The remedies herein provided are cumulative and not exclusive of any remedies provided by law.

Section 13 . Waiver of Right of Setoff. The Administrative Agent and each Bank hereby waive any right to set off and apply any and all deposits (general or special, time or demand, provisional or final) and collateral at any time held and other indebtedness at any time owing by it to or for the credit or the account of the Company if there shall be a drawing under the Letter of Credit at any time during the pendency of any proceeding by or against the Company seeking to adjudicate it a bankrupt or insolvent, or seeking liquidation, winding up, reorganization,

arrangement, adjustment, protection, relief or composition of it or its debts under any law relating to bankruptcy, insolvency or reorganization or relief of debtors, or seeking the entry of an order for relief or the appointment of a receiver, custodian, trustee or other similar official for it or for any substantial part of its property (collectively the "BANKRUPTCY EVENTS"), against any and all of the obligations of the Company now or hereafter existing in respect of any reimbursement obligation of the Company set forth in Section 2(a), provided that any such waiver shall be deemed ineffective as and to the extent that the Administrative Agent and each Bank receive, after any of the bankruptcy events occur, an unqualified opinion of nationally-recognized counsel with bankruptcy law experience (which counsel shall be mutually satisfactory to the Administrative Agent and the Equity Participant, each of which shall use its best efforts to agree on such counsel), that non-waiver would not, as a result of the application of bankruptcy or similar laws as then in effect, lead to the Administrative Agent or any Bank being refused, prevented, permanently enjoined or restrained from or delayed in fulfilling its obligation under the Letter of Credit. This Section 13 shall not constitute a waiver of any right of setoff if there shall be a drawing under the Letter of Credit at any time other than that described in this Section 13.

Section 14 . Participations of the Banks. (a) The Issuing Bank hereby sells to each other Bank, and each Bank hereby severally purchases from the Issuing Bank, as of the Restatement Effective Date, a Participation in an amount equal to such Bank's Participation Percentage of the Letter of Credit and in each drawing thereunder, all on the terms and conditions set forth herein.

(b) If at any time on or after the Restatement Effective Date the Company shall fail to reimburse a drawing under the Letter of Credit in accordance with Section 2(a), the Administrative Agent shall promptly (but in any event no later than 1:00 p.m., New York City time, on the date payment is due from the Banks under this Section 14(b)) advise each Bank thereof and of the amount due from the Company and the amount of such Bank's Participation therein, and each Bank shall pay, no later than 4:00 p.m. (New York City time) on such date such Bank's Participation Percentage of such amount by transferring the same in immediately available funds to the Administrative Agent for the account of the Issuing Bank at the Administrative Agent's address specified in Section 11. With respect to any such drawing, each Bank agrees that the Issuing Bank shall have no responsibility to the Banks other than obtaining the draft and certificates referred to in the Letter of Credit and notifying each Bank thereof. The Administrative Agent shall promptly credit each Bank's account with such Bank's Participation Percentage of (i) all amounts representing principal of, or interest on, any reimbursement obligations, in each case in respect of drawings under the Letter of Credit of which such Bank has funded its Participation Percentage in accordance with the foregoing provisions of this Section 14(b) and (ii) letter of credit commissions payable to each Bank pursuant to Section 2(b) of this

Agreement and accruing on and after the Restatement Effective Date, but, in the case of both clause (i) and clause (ii), only if, when and to the extent received by the Administrative Agent from the Company. All such payments shall be made if, when and to the extent the Administrative Agent receives payment from the Company in respect of reimbursement for drawings under the Letter of Credit and of the letter of credit commission pursuant to Section 2(b) of this Agreement, and in the same funds in which such amounts are received, by credit to an account at a bank located in the United States of America as each Bank shall designate in writing to the Administrative Agent.

(c) If the Administrative Agent should for any reason make any payment to any Bank in anticipation of the receipt of funds from the Company and such funds are not received by the Administrative Agent from the Company on the date payment is due, then such Bank shall, on demand by the Administrative Agent, forthwith return to the Administrative Agent any such amounts transferred to such Bank by the Administrative Agent in respect of such Bank's Participation plus interest thereon from the day such amounts were transferred by the Administrative Agent to such Bank to but not including the day such amounts are returned by such Bank at a rate per annum equal to the Federal Funds Rate. If the Administrative Agent is required at any time to return to the Company or to a trustee, receiver, liquidator, custodian or other similar official any portion of the payments made by the Company to the Administrative Agent for the account of any Bank, then such Bank shall, on demand by the Administrative Agent, forthwith return to the Administrative Agent any such payments transferred to such Bank by the Administrative Agent in respect of such Bank's Participation, but without interest on such payments (unless the Administrative Agent is required to pay interest on such amounts to the Person recovering such payments).

(d) Each Bank agrees that if it should receive any amount due to it under this Agreement in respect of its Participation other than from the Administrative Agent, such Bank will remit all of the same to the Administrative Agent to distribute to the Banks pursuant to this Agreement, and such Bank's Participation shall be adjusted to reflect such remittance. Each Bank further agrees to send the Administrative Agent a copy of any notice sent by such Bank to the Company hereunder.

(e) Each Bank acknowledges and represents that it has made its own independent appraisal of the Company, and the business, affairs and financial condition of the Company, based on such documents and information as such Bank has deemed appropriate, and each Bank will continue to be responsible for making its own independent appraisal of such matters, based on such documents and information as such Bank shall deem appropriate at the time, and has not relied upon and will not hereafter rely upon the Administrative Agent or any other Bank or any information prepared, distributed or otherwise made available by the

Administrative Agent for such appraisal or other assessment or review of the Company. Each Bank represents, and in granting a Participation to such Bank it is specifically understood and agreed, that such Bank is acquiring its Participation in the Letter of Credit for its own account in the ordinary course of its commercial banking business and not with a view to, or for sale in connection with, any distribution thereof.

Section 15 . Assignees; Participants. (a) Each Bank shall have the right, with the prior written consent of the Company (which shall not be unreasonably withheld, and shall not be required if a Reimbursement Event of Default has occurred and is continuing) and the prior written consent of the Administrative Agent, to assign all or a pro rata portion of all of its rights and obligations under its Participation at any time and from time to time to one or more Eligible Institutions (each an "ASSIGNEE"); provided that (i) each such Assignee shall assume such rights and obligations and agree, for the benefit of each other party hereto, to be bound by the provisions of, and perform the obligations of a Bank under, this Agreement, pursuant to an assignment and assumption agreement in form and substance satisfactory to the Administrative Agent and (ii) the aggregate amount of the Participation or Participations assigned to each such Assignee pursuant to this Section 15(a) shall not be less than \$5,000,000. Each Bank shall give prompt notice to the Administrative Agent and the Company of each such assignment made by it.

(b) (i) Each Bank shall also have the right, without the consent of the Company, to grant participating interests in its Participation at any time and from time to time to one or more other financial institutions or other entities (each a "PARTICIPANT"); provided that (A) such Bank's obligations under this Agreement shall remain unchanged, (B) such Bank shall remain solely responsible to the other parties hereto for the performance of such obligations and (C) the Company, the Administrative Agent and the other Banks shall continue to deal solely and directly with such Bank in connection with such Bank's rights and obligations under this Agreement. Each such participation granted by a Bank shall be evidenced by a participation agreement in form acceptable to such Bank. Each such participation agreement shall provide that such Bank shall retain the sole right to exercise its rights under this Agreement and to enforce the obligations owed to it hereunder pursuant to its Participation including, without limitation, the right to consent to any modification, amendment or waiver of any provision of this Agreement or the Letter of Credit or any assignment of the Company's obligations under any of the Transaction Documents or the Financing Documents; provided that any such participation agreement may provide that such Bank will not, without the consent of the Participant, consent to any modification, amendment or waiver of this Agreement or the Letter of Credit that (w) increases the Maximum Credit Amount or Maximum Drawing Amount or subjects such Bank to any additional obligation under this Agreement or the Letter of Credit, (x) reduces the principal of or rate of interest on any reimbursement obligation or

reduces the letter of credit commission payable under Section 2(b), (y) postpones the date fixed for any payment of principal of or interest on any reimbursement obligation or any payment of such letter of credit commission or (z) extends the Stated Termination Date or the Termination Date.

(i) Subject to clause (iii) below, the Company agrees that each Participant shall be entitled to the benefits of Sections 2(d) and 2(e) to the same extent as if it were a Bank and had acquired its interest by assignment pursuant to Section 15(a).

(ii) A Participant shall not be entitled to receive any greater payment under Section 2(d) or 2(e) than the applicable Bank would have been entitled to receive with respect to the participating interest granted to such Participant, unless the granting of such interest to such Participant is made with the Company's prior written consent. A Participant organized under the laws of a jurisdiction outside the United States shall not be entitled to the benefits of Section 2(d) or 2(e) unless the Company is notified of the participating interest granted to such Participant and such Participant agrees, for the benefit of the Company, to comply with Section 2(d) or 2(e) as though it were a Bank.

Section 16 . Continuing Obligation; Binding Effect. The obligations of the Company under this Agreement shall continue until the later of (i) the Termination Date and (ii) the date upon which all amounts due and owing to the Administrative Agent or any Bank hereunder shall have been paid in full. This Agreement shall be binding upon and inure to the benefit of each of the parties hereto and their respective successors. The Company shall not have the right to assign its rights hereunder or any interest herein to any Person without the prior written consent of the Issuing Bank and each Bank. The Issuing Bank shall not have the right to assign its rights as the Issuing Bank hereunder without the prior written consent of the Company (which shall not be unreasonably withheld) and each Bank.

Section 17 . Extension of the Letter of Credit. At least 105 days but not more than 180 days before the Stated Termination Date, the Company may request the Administrative Agent in writing (each such request being irrevocable and binding), with a copy to each Bank, to extend for not less than three years, nor more than eight years, the Stated Termination Date, specifying the terms and conditions, including fees, to be applicable to such extension. Within 45 days after receiving such extension request (or such later date as the Company may authorize in writing, but in no event later than 60 days before the Stated Termination Date), each Bank shall notify the Company of its consent or nonconsent to such extension request, and if any Bank shall give no such notice, it shall be deemed not to have consented to such extension request. No such requested extension shall be effective without the consent of all the Banks. The

consent of any Bank shall be in its sole discretion and shall be conditional upon the preparation, execution and delivery of legal documentation in form and substance satisfactory to such Bank and its counsel, incorporating substantially the terms and conditions contained in the extension request as the same may be modified by agreement among the Company, and the Banks, and evidence satisfactory to it of the due authorization and validity thereof.

Section 18 . Limited Liability of the Banks. The Company assumes all risks of the acts or omissions of the Equity Participant and any beneficiary or transferee of the Letter of Credit with respect to its use of the Letter of Credit. None of the Administrative Agent and the Banks, nor their respective Affiliates nor any officer or director of any of the foregoing shall be liable or responsible for: (a) the use which may be made of the Letter of Credit or any acts or omissions of the Equity Participant or any beneficiary or transferee in connection therewith; (b) the validity, sufficiency or genuineness of documents, or of any endorsement thereon, even if such documents shall prove to be in any or all respects invalid, insufficient, fraudulent or forged; (c) payment by the Issuing Bank against presentation of documents which do not comply with the terms of the Letter of Credit, including failure of any documents to bear any reference or adequate reference to the Letter of Credit; or (d) any other circumstances whatsoever in making or failing to make payment under the Letter of Credit, except that the Company shall have a claim against the Issuing Bank, and the Issuing Bank shall be liable to the Company, to the extent, but only to the extent, of any direct, as opposed to consequential, damages suffered by the Company which the Company proves were caused by (i) the willful misconduct or gross negligence of the Issuing Bank in determining whether a draft or certificate presented under the Letter of Credit complied with the terms of the Letter of Credit or (ii) the Issuing Bank's willful failure to make lawful payment under the Letter of Credit after the presentation to it by the Equity Participant of a draft and certificate strictly complying with the terms and conditions of the Letter of Credit. In furtherance and not in limitation of the foregoing, the Issuing Bank may accept documents that appear on their face to be in order, without responsibility for further investigation, regardless of any notice or information to the contrary unless the Equity Participant and the Company have notified the Issuing Bank in writing prior to a drawing under the Letter of Credit that such documents do not comply with the Letter of Credit.

Section 19 . Cost, Expenses and Taxes. The Company agrees to pay not later than 30 days after demand therefor all reasonable costs and expenses in connection with the preparation, execution, delivery, filing, recording and administration of this Agreement and any other documents which may be delivered in connection with this Agreement and any waiver or consent under, or amendment of, this Agreement or any of the Transaction Documents or Financing Documents, including, without limitation, the reasonable fees and out-of-pocket expenses of counsel for the Administrative Agent, and local counsel who may be

retained by said counsel, with respect thereto and with respect to advising the Administrative Agent as to its rights and responsibilities under this Agreement; all costs and expenses (including counsel fees and expenses) in connection with (i) the enforcement of this Agreement and such other documents which may be delivered in connection with this Agreement or (ii) any action or proceeding relating to a court order, injunction or other process or decree restraining or seeking to restrain the Issuing Bank from paying any amount under the Letter of Credit; and all costs and expenses (including reasonable counsel fees and expenses) in connection with each transfer of the Letter of Credit in accordance with its terms. In addition, the Company shall pay any and all stamp, documentary, filing, recording or other similar taxes and fees payable or determined to be payable in connection with the execution, delivery, filing and recording of this Agreement and such other documents, and agrees to save the Administrative Agent and each Bank harmless from and against any and all liabilities with respect to or resulting from any delay in paying or omission to pay such taxes and fees, provided that the Administrative Agent and each Bank agree promptly to notify the Company of any such taxes and fees which are incurred by the Administrative Agent or such Bank.

Section 20 . Administrative Agent; Issuing Bank. (a) Each Bank irrevocably appoints and authorizes the Administrative Agent to take such action as agent on its behalf and to exercise such powers under this Agreement as are delegated to the Administrative Agent by the terms hereof, together with all such powers as are reasonably incidental thereto.

(b) The Administrative Agent and its Affiliates may accept deposits from, make loans or otherwise extend credit to, and generally engage in any kind of business with, the Company, the Equity Participant and their respective Subsidiaries and Affiliates and receive payment on such loans or extensions of credit and otherwise act with respect thereto freely and without accountability in the same manner as if this Agreement and the transactions contemplated hereby were not in effect.

(c) The Administrative Agent may consult with legal counsel (who may be counsel for the Company), independent public accountants and other experts as it may select and shall not be liable for any action taken or omitted to be taken by it in good faith in accordance with the advice of such counsel, accountants or experts.

(d) It is understood that the Issuing Bank will exercise and give the same care and attention to the Letter of Credit as it gives to its other letters of credit and loans for its own account and that the Issuing Bank shall have no obligation to the Company or any other Bank and no duty or responsibility with respect to this Agreement or the Letter of Credit, except as expressly provided herein and in the Letter of Credit. Without limiting the generality of the

foregoing, neither the Administrative Agent nor the Issuing Bank shall be required to take any action with respect to any Reimbursement Default, except as expressly provided in Section 9 hereof. Neither the Administrative Agent nor the Issuing Bank shall be liable for any action taken or not taken at the request or with the approval of the Required Banks (or all the Banks, as applicable) or for the performance or non-performance of the obligations of any other party under this Agreement or any Transaction Document or Financing Document or any other document contemplated thereby. It is further understood that: (i) except as expressly limited by the provisions of this Agreement, the Issuing Bank retains the sole right to exercise its rights and enforce the obligations of the Company under this Agreement, and the Issuing Bank may use its sole discretion with respect to exercising or refraining from exercising any rights or taking or refraining from taking any actions which may be vested in it or which it may be entitled to take or assert under this Agreement or any of the Transaction Documents or Financing Documents (including, without limitation, the giving of any notice to any Person of any Reimbursement Event of Default under this Agreement except as provided in Section 9); and (ii) the Issuing Bank shall not, in the absence of gross negligence or willful misconduct, be under any liability to any other Bank with respect to anything which the Issuing Bank may do or refrain from doing in the exercise of its best judgment or which it may deem to be necessary or desirable. Neither the Administrative Agent nor the Issuing Bank shall incur any liability by acting in reliance upon any written communication or any telephone conversation which it reasonably believes to be genuine and correct or to have been signed, sent or made by the proper Person. Neither the Administrative Agent nor the Issuing Bank shall have any obligation to make any claim on, or assert any lien upon, or assert any setoff against, any property held by it and, if it elects to do so, it may in its discretion apply the same against indebtedness of the Company other than the Company's obligations under this Agreement; provided that, to the extent any funds received pursuant to any of the foregoing are applied to the obligations of the Company under Section 2(a) or 2(b) hereof, each Bank shall be entitled to receive its pro rata share thereof in accordance with Section 14(b) above. Any such setoff or other action in respect of any reimbursement obligation of the Company set forth in Section 2(a) will be subject to Section 13.

Section 21 . Indemnification. (a) The Company indemnifies and holds harmless the Administrative Agent, each Bank, and their respective officers, directors, agents, affiliates and employees from and against any and all claims, damages, losses, liabilities, costs or expenses whatsoever which the Administrative Agent or such Bank may incur (or which may be claimed against the Administrative Agent or such Bank by any Person whatsoever):

(i) by reason of any inaccuracy in any material respect, or any untrue statement or alleged untrue statement of any material fact contained or incorporated by reference in any offering document distributed by or on

behalf of the Company in connection with obtaining purchasers of the Company's undivided interest in Unit 2 of the Palo Verde Nuclear Generating Station, or in any supplement or amendment to either thereof, or by reason of the omission or alleged omission to state therein a material fact necessary to make such statements, in the light of the circumstances under which they are or were made, not misleading;

(ii) by reason of or in connection with the execution, delivery and performance of the Transaction Documents and Financing Documents, or any transaction contemplated by the Transaction Documents or the Financing Documents; or

(iii) by reason of or in connection with the execution and delivery or transfer of, or payment or failure to make lawful payment under, the Letter of Credit; provided that the Company shall not be required to indemnify the Administrative Agent or any Bank pursuant to this Section 21 for any claims, damages, losses, liabilities, costs or expenses to the extent, but only to the extent, caused by (A) the willful misconduct or gross negligence of the Issuing Bank in determining whether a draft or certificate presented under the Letter of Credit complied with the terms of the Letter of Credit or (B) the Issuing Bank's willful failure to make lawful payment under the Letter of Credit after the presentation to it by the Equity Participant of a draft and certificate strictly complying with the terms and conditions of the Letter of Credit.

Nothing in this Section 21(a) is intended to limit the Company's obligations contained in Section 2. Without prejudice to the survival of any other obligation of the Company hereunder, the indemnities and obligations of the Company contained in this Section 21(a) shall survive the payment in full of all amounts payable pursuant to Section 2 and the termination of the Letter of Credit.

(b) To the extent that the Administrative Agent or the Issuing Bank is not reimbursed and indemnified by the Company under this Agreement, each Bank will reimburse and indemnify the Administrative Agent and the Issuing Bank on demand for and against such Bank's Participation Percentage of any and all claims, demands, liabilities, obligations, losses, damages, penalties, actions, judgments, suits, costs, expenses or disbursements (including fees and disbursements of counsel) of any kind or nature whatsoever which may be imposed on, incurred by, or asserted against the Administrative Agent or the Issuing Bank in any way relating to or arising out of this Agreement, the Letter of Credit, or any of the Transaction Documents or Financing Documents or any action taken or omitted to be taken by the Administrative Agent or the Issuing Bank hereunder or thereunder, or the transactions contemplated hereby and thereby or the enforcement of any of the terms hereof and thereof; provided that such Bank shall not be liable for any portion of such claims, demands, liabilities,

obligations, losses, damages, penalties, actions, judgments, suits, costs, out-of-pocket expenses or disbursements resulting from the gross negligence or willful misconduct of the Administrative Agent or the Issuing Bank or which are expressly excluded from the indemnification by the Company by the proviso to Section 21(a)(iii) of this Agreement. Each Bank's obligations under this Section 21(b) shall survive the termination of this Agreement and the Letter of Credit. If the Administrative Agent or the Issuing Bank is reimbursed by the Company for any amounts previously received from any Bank pursuant to this Section 21(b), it will promptly pay to such Bank its proportionate share of any amounts so received.

Section 22 . Confidentiality. Neither the Administrative Agent nor any Bank shall disclose any Confidential Information to any Person without the consent of the Company, other than (a) to the Administrative Agent's or such Bank's respective Affiliates or any officer, director, employee, accountant and advisor of any of the foregoing, and to actual or prospective Assignees and Participants, and then only on a confidential basis, (b) as required by any law, rule or regulation or judicial process and (c) as requested or required by any state, federal or foreign authority or examiner regulating banks or banking or otherwise regulating the business of the Administrative Agent or such Bank, as the case may be.

Section 23 . Severability. Any provision of this Agreement which is prohibited, unenforceable or not authorized in any jurisdiction shall, as to such jurisdiction, be ineffective to the extent of such prohibition, unenforceability or non-authorization without invalidating the remaining provisions hereof or affecting the validity, enforceability or legality of such provision in any other jurisdiction.

Section 24 . Governing Law; Consent to Jurisdiction. (a) This Agreement shall be governed by, and construed in accordance with, the laws of the State of New York.

(b) Each party hereto submits, for itself and its property, to the non-exclusive jurisdiction of the Supreme Court of the State of New York sitting in New York County and of the United States District Court of the Southern District of New York, and any appellate court from any thereof, in any action or proceeding arising out of or relating to this Agreement or for recognition or enforcement of any judgment, and each party hereto hereby agrees, to the fullest extent permitted by law, that all claims in respect of any such action or proceeding may be heard and determined in such New York State or, to the extent permitted by law, in such Federal court. Each of the parties hereto agrees that a final judgment in any such action or proceeding shall be conclusive and may be enforced in other jurisdictions by suit on the judgment or in any other manner provided by law. Nothing in this Agreement shall affect any right that any party

hereto may otherwise have to bring action or proceeding relating to this Agreement in the courts of any jurisdiction.

Section 25 . Headings. Section headings in this Agreement are included herein for convenience of reference only and shall not constitute a part of this Agreement for any other purpose.

Section 26 . Counterparts; Integration. This Amendment and Restatement may be signed in any number of counterparts, each of which shall be an original, with the same effect as if the signatures thereto and hereto were upon the same instrument. This Agreement and that certain Letter Agreement dated as of July 22, 2002 between the Issuing Bank and the Company constitute the entire agreement and understanding among the parties hereto and, subject to Section 3(c), supersede any and all prior agreements and understandings, oral or written, relating to the subject matter hereof.

Section 27 . WAIVER OF JURY TRIAL. EACH OF THE COMPANY, THE BANKS AND THE ADMINISTRATIVE AGENT HEREBY IRREVOCABLY WAIVES ANY AND ALL RIGHT TO TRIAL BY JURY IN ANY LEGAL PROCEEDING ARISING OUT OF OR RELATING TO THIS AGREEMENT OR THE TRANSACTIONS CONTEMPLATED HEREBY.

Signature Pages Follow

IN WITNESS WHEREOF, the parties hereto have caused this Amendment and Restatement to be duly executed and delivered by their respective officers thereunto duly authorized as of the date first above written.

ARIZONA PUBLIC SERVICE COMPANY

By: /s/ Barbara M. Gomez

Name: Barbara M. Gomez

Title: Vice President and Treasurer

IN WITNESS WHEREOF, the parties hereto have caused this Amendment and Restatement to be duly executed and delivered by their respective officers thereunto duly authorized as of the date first above written.

JPMORGAN CHASE BANK, N.A.,
as Administrative Agent and Issuing Bank

By: /s/ Peter M. Ling

Name: Peter M. Ling
Title: Managing Director

IN WITNESS WHEREOF, the parties hereto have caused this Amendment and Restatement to be duly executed and delivered by their respective officers thereunto duly authorized as of the date first above written.

BARCLAYS BANK PLC

By: /s/ Gary B. Wenslow

Name: Gary B. Wenslow

Title: Associate Director

IN WITNESS WHEREOF, the parties hereto have caused this Amendment and Restatement to be duly executed and delivered by their respective officers thereunto duly authorized as of the date first above written.

BANK HAPOLIM B.M.

By: /s/ Marc Bosc

Name: Marc Bosc
Title: Vice President

By: /s/ Lenroy Hackett

Name: Lenroy Hackett
Title: First Vice President

IN WITNESS WHEREOF, the parties hereto have caused this Amendment and Restatement to be duly executed and delivered by their respective officers thereunto duly authorized as of the date first above written.

CITIBANK, N.A.

By: /s/ Dhaya Ranganathan

Name: Dhaya Ranganathan
Title: Director

IN WITNESS WHEREOF, the parties hereto have caused this Amendment and Restatement to be duly executed and delivered by their respective officers thereunto duly authorized as of the date first above written.

UNION BANK OF CALIFORNIA, N.A.

By: /s/ Efrain Soto

Name: Efrain Soto

Title: Vice President

IN WITNESS WHEREOF, the parties hereto have caused this Amendment and Restatement to be duly executed and delivered by their respective officers thereunto duly authorized as of the date first above written.

KBC BANK NV

By: /s/ Rik Scheerlinck

Name: Rik Scheerlinck
Title: Sr. Vice President &
General Manager

By: /s/ Eric Raskin

Name: Eric Raskin
Title: Vice President

SCHEDULE I

The "LETTER OF CREDIT COMMISSION RATE" for any day is the rate set forth below (in basis points per annum) under the column corresponding to the Status that exists on such day:

Status	Level I	Level II	Level III	Level IV	Level V	Level VI
Letter of Credit Commission Rate	50.0	60.0	70.0	87.5	112.5	137.5

For purposes of this Schedule, the following terms have the following meanings:

"LEVEL I STATUS" exists at any date if, at such date, the higher of the two Ratings is:

A- or higher by S&P or A3 or higher by Moody's.

"LEVEL II STATUS" exists at any date if, at such date, (i) Level I Status does not exist and (ii) the higher of the two Ratings is:

BBB+ or higher by S&P or Baa1 or higher by Moody's.

"LEVEL III STATUS" exists at any date if, at such date, (i) neither Level I Status nor Level II Status exists and (ii) the higher of the two Ratings is:

BBB or higher by S&P or Baa2 or higher by Moody's.

"LEVEL IV STATUS" exists at any date if, at such date, (i) none of Level I Status, Level II Status and Level III Status exists and (ii) the higher of the two Ratings is:

BBB- or higher by S&P or Baa3 or higher by Moody's.

"LEVEL V STATUS" exists at any date if, at such date, (i) none of Level I Status, Level II Status, Level III Status or Level IV Status exists, and (ii) the higher of the two Ratings is:

BB+ or higher by S&P or Ba1 or higher by Moody's.

"LEVEL VI STATUS" exists at any date if, at such date, no other Status exists.

"MOODY'S" means Moody's Investors Service, Inc.

"RATING AGENCIES" means Moody's and S&P.

"RATINGS" means the credit ratings assigned to the senior unsecured long-term debt securities of the Company without third-party credit enhancement by the Rating Agencies. If there is no rating assigned to debt securities, the corporate credit rating will be used. Any rating assigned to any other debt security of the Company shall be disregarded. The rating in effect at any date is that in effect at the close of business on such date. In the case of split ratings from S&P or Moody's, the rating to be used to determine which pricing level applies is the higher of the two (e.g., BBB+/Baa2 results in Level II Status); provided that if the split is more than one full rating category, the rating category immediately above the lower of the two rating categories will be used (e.g., BBB+/Baa3 results in Level III Status, as does A-/Baa3).

"S&P" means Standard & Poor's Ratings Services, a division of the McGraw-Hill Companies, Inc.

"STATUS" refers to the determination of which of Level I Status, Level II Status, Level III Status, Level IV Status, Level V Status or Level VI Status exists at any date.

Schedule I-2

SCHEDULE II

BANK	PARTICIPATION PERCENTAGE	PARTICIPATION AMOUNT
JPMorgan Chase Bank, N.A.	18.9256646%	\$ 10,448,412.70
Barclays Bank PLC	18.9256646%	\$ 10,448,412.70
Bank Hapoalim B.M.	17.3247282%	\$ 9,564,573.47
Citibank, N.A.	14.9413142%	\$ 8,248,746.86
Union Bank of California, N.A.	14.9413142%	\$ 8,248,746.86
KBC Bank NV	14.9413142%	\$ 8,248,746.86

Schedule II

[Form of Amended and Restated Letter of Credit]

[SEE ATTACHED]

AMENDED AND RESTATED
IRREVOCABLE TRANSFERABLE LETTER OF CREDIT
No. P-010152
(formerly numbered as S-1002)

Originally Issued August 18, 1986
Reissued May 19, 2005

Emerson Finance LLC
8000 W. Florissant Avenue
P.O. Box 4100
St. Louis, Missouri 63136

Attention: President

Dear Sirs:

We hereby establish, at the request of Arizona Public Service Company (the "COMPANY"), in your favor, our Irrevocable Transferable Letter of Credit No. P-010152 (formerly numbered as S-1002) (the "LETTER OF CREDIT"), in a maximum amount at any date (the "MAXIMUM CREDIT AMOUNT") equal to the amount shown opposite the period including such date in the Table of Maximum Credit Amounts attached hereto as Schedule II-A, effective immediately and expiring at 5:00 p.m. (New York City time) on the Termination Date. Capitalized terms used herein and in Schedules II-A, II-B and III and Exhibits 1, 2, 3 and 4 hereto shall have the meanings set forth in Schedule I hereto. This Letter of Credit is issued in connection with the leasing of an undivided interest in Unit 2 of the Palo Verde Nuclear Generating Station to the Company pursuant to a Facility Lease dated as of August 1, 1986 (the "FACILITY LEASE") as amended and in effect on the date hereof, between the Company and State Street Bank and Trust Company (as successor to The First National Bank of Boston), as Owner Trustee under a trust agreement with you.

We hereby irrevocably authorize you to draw on us, in accordance with the terms and conditions hereinafter set forth, an amount not in excess of the amount shown opposite the period including the date of such drawing (the "DATE OF DRAWING") in the Table of Maximum Drawing Amounts attached hereto as Schedule II-B as such amounts are modified from time to time in accordance with the next paragraph. Such amounts, as modified in accordance with the next

paragraph, are hereinafter referred to collectively as the "MAXIMUM DRAWING AMOUNTS" and individually as the "MAXIMUM DRAWING AMOUNT". A drawing in respect of a payment hereunder honored by us shall not exceed the lesser of the Maximum Drawing Amount applicable on the Date of Drawing and the Maximum Credit Amount applicable on the Date of Drawing. All payments hereunder shall be made from our own general funds.

The Maximum Drawing Amounts shall be modified from time to time as follows:

(a) upon payment by the Issuing Bank of each drawing under the Letter of Credit, the Maximum Drawing Amounts applicable to each Date of Drawing subsequent to such payment shall be automatically reduced by an amount equal to the amount of the drawing so paid and shall not be reinstated; and

(b) if adjustments are made to Modified Special Casualty Values, corresponding adjustments shall be made to the Maximum Drawing Amounts shown in Schedule II-B, (as theretofore reduced pursuant to clause (a) above), provided that if any such adjustment of Modified Special Casualty Values would cause the Maximum Drawing Amount for any period to exceed the Maximum Credit Amount for such period (minus the amount of any drawing theretofore honored by us hereunder), such Maximum Credit Amount (as so reduced) shall apply for such period and provided further that adjustments pursuant to this clause (b) shall be effective automatically upon receipt by us of a notice from you in the form of Exhibit 1 hereto.

Upon surrender of this Letter of Credit together with a notice in the form of Exhibit 1 hereto, we will promptly issue an irrevocable transferable letter of credit containing a revised Schedule II-B reflecting the adjustments contained in such notice and in all other respects identical to this Letter of Credit.

Funds under this Letter of Credit are available to you against presentation on or prior to the Termination Date of (a) your draft in the form of Exhibit 2 attached hereto and (b) a completed certificate signed by you in the form of Exhibit 3 attached hereto. Such draft and certificate shall be dated the date of its presentation and shall be presented at our Tampa, Florida office specified below, or at our Brooklyn, New York office specified below (or at any other office in New York City which may be designated by us by written notice (given in the manner set forth in the next paragraph) delivered to you at least 15 days prior to the applicable Date of Drawing). If we receive such draft and certificate at our Tampa, Florida office specified below, all in strict conformity with the terms and conditions of this Letter of Credit, prior to 10:00 a.m. (New York City time) on any Business Day, we will honor the draft on the same Business Day. If we receive such draft and certificate at our Tampa, Florida office specified below on

or after 10:00 a.m. and prior to 5:00 p.m. (New York City time) on any Business Day, or if we receive such draft and certificate at our Brooklyn, New York office specified below prior to 5:00 p.m. (New York City time) on any Business Day, in each case all in strict conformity with the terms and conditions of this Letter of Credit, we will honor the draft on the next Business Day. If requested by you, payment under this Letter of Credit may be made by wire transfer of federal funds to your account with any bank located in the United States of America or by deposit of immediately available funds into a designated account that you maintain with us.

Notwithstanding any provisions of Articles 13(b) and 14(d)(i) of the Uniform Customs and of Section 5-108(b) of the New York Uniform Commercial Code to the contrary, which provisions are hereby expressly waived, if the presentation of such draft and certificate are not in strict conformity with the terms and conditions of this Letter of Credit, we will give you prompt notice prior to the time we would have been obliged to make payment as set forth in the preceding paragraph by facsimile transmission addressed to you at the fax number set forth in the next succeeding paragraph, effective upon confirmation, that we have refused such non-conforming draft and certificate, and stating all discrepancies in respect of which the Issuing Bank refuses such non-conforming draft and certificate. If you correct such non-conforming demand by presentation of the draft and certificate corrected to be in strict conformity with the terms and conditions of the Letter of Credit within two Business Days of your receipt of our notice of refusal, then we will honor the draft and make payment in accordance with the terms provided herein based upon the time such corrected draft and certificate are presented, provided that you may make only one such corrected demand with respect to any such non-conforming demand, and provided further that for purposes of determining whether the draft and certificate have been timely presented, the corrected draft and certificate shall be deemed to have been presented on the date the non-conforming draft and certificate were presented.

Notwithstanding any other provision of this Letter of Credit, we shall have the right, upon the occurrence of any of the events listed in Schedule III hereto, to terminate this Letter of Credit by delivering to you a written notice indicating the date of such termination (the "DATE OF EARLY TERMINATION"), provided that on or before the Date of Early Termination you will have the right to draw once an amount not in excess of the lesser of the Maximum Credit Amount and the Maximum Drawing Amount in accordance with the procedures described herein. The written notice referred to in the preceding sentence shall be given by facsimile transmission addressed to you at Emerson Finance LLC, 8000 W. Florissant Avenue, P.O. Box 4100, St. Louis, Missouri 63136; Attention: President; Fax: 314-553-2463 (or to such other address or facsimile number designated by you by written notice delivered to us at least 15 days prior to the notice of early termination) and shall be effective upon receipt of the appropriate confirmation of the facsimile transmission. We will also forward a copy of such

notice by overnight delivery service to the address set forth above. The Date of Early Termination specified in such written notice shall be:

(a) in the case of events specified in paragraphs A and G of Schedule III, not earlier than ten days after such notice is given, and

(b) in the case of all other events specified in Schedule III, not earlier than 30 days after such notice is given.

Except as set forth herein, this Letter of Credit shall be governed by the Uniform Customs and Practice for Documentary Credits (1993 Revision) International Chamber of Commerce Publication No. 500, other than the provisions of Article 48 thereof. This Letter of Credit shall be deemed to be a contract made under the laws of the State of New York and shall, as to matters not governed by the Uniform Customs, be governed by and construed in accordance with the laws of such State.

All demands for payment, notices and other communications to us in respect of this Letter of Credit shall be in writing, specifically referring to the number of this Letter of Credit, and addressed and presented to us (and all courier or physical deliveries should be addressed to us) at JPMorgan Chase Bank, N.A., c/o JP Morgan Treasury Services, Standby Letter of Credit Manager - Immediate Action Required, 4th Floor, 10240 Highland Manor Drive, Tampa, Florida 33610. Although we prefer physical presentations be made to our Tampa, Florida location, our location at 4 Chase Metrotech Center, 10th Floor, Brooklyn, New York 11245 is also available for your physical presentations. Should you use our 4 Chase Metrotech Center location for physical presentations, documents must be directed to: Governmental Agency Unit, Attention: Global Trade.

Notwithstanding Article 48 of the Uniform Customs and Practice for Documentary Credits referred to above, this Letter of Credit may be transferred in its entirety more than once, but in each case only to the successor Equity Participant under the Trust Agreement dated as of August 1, 1986 between yourself and State Street Bank and Trust Company as successor to The First National Bank of Boston. Upon receipt by us at the address for presentation of documents set forth above of a copy of the instrument effecting such transfer, signed by the transferor and by the transferee, in the form of Exhibit 4 hereto (which shall be conclusive evidence of such transferee's authority without any inquiry by us into the terms of the Trust Agreement) then, in such case, we will, upon surrender of this Letter of Credit (and amendments thereto, if any), issue an irrevocable transferable letter of credit in the name of the transferee and providing for notices to be sent to the transferee at the address set forth therein and in all other respects identical to this Letter of Credit and the transferee, instead of the transferor, shall, without necessity of further act, be entitled to all the benefits of, and rights under, this Letter of Credit in the transferor's place.

We hereby notify you of our agreement to the terms and conditions of Section 13 of the Reimbursement Agreement.

This Letter of Credit sets forth in full our undertaking, and such undertaking shall not in any way be modified, amended, amplified or limited by reference to any document, instrument or agreement referred to herein, except only Schedules I, II-A, II-B and III and Exhibits 1, 2, 3 and 4 hereto and the notices referred to herein; and any such reference shall not be deemed to incorporate herein by reference any document, instrument or agreement except as set forth above.

This Letter of Credit No. P-010152 (formerly numbered as S-1002) amends and restates our Letter of Credit No. S-1002 dated as of August 15, 1986, as heretofore amended.

JPMORGAN CHASE BANK, N.A.

By: _____
Name:
Title:

LETTER OF CREDIT NO. P-010152 (FORMERLY NUMBERED AS S-1002)
ISSUED BY JPMORGAN CHASE BANK, N.A.
SIGNATURE PAGE

EXHIBIT 1
TO LETTER OF CREDIT

JPMorgan Chase Bank, N.A.
[c/o JP Morgan Treasury Services
Standby Letter of Credit Manager -
Immediate Action Required
4th Floor
10240 Highland Manor Drive
Tampa, Florida 33610]

[Governmental Agency Unit
4 Chase Metrotech Center
10th Floor
Brooklyn, New York 11245
Attention: Global Trade]

Dear Sirs:

Reference is made to that certain amended and restated irrevocable transferable Letter of Credit bearing Letter of Credit No. P-010152 (formerly numbered as S-1002) dated May 19, 2005, which has been established by you in favor of Emerson Finance LLC (the "EQUITY PARTICIPANT").

The undersigned, a duly authorized representative of the Equity Participant, hereby certifies that Modified Special Casualty Values have been adjusted and the amounts shown on Schedule II-B to the Letter of Credit should be modified, in accordance with the terms of clauses (a) and (b) of the third paragraph of the Letter of Credit, to the amounts shown in Appendix A hereto.

The Letter of Credit is returned herewith and we request that you issue an irrevocable transferable letter of credit with the revised Schedule II-B attached and in all other respects identical to the Letter of Credit.

Capitalized terms used herein and not otherwise defined herein shall have the meanings given to them in the Letter of Credit.

[Name of Equity Participant]

[Name and Title of Authorized
Representative of Equity Participant]

Letter of Credit - Exhibit 1

EXHIBIT 2
TO LETTER OF CREDIT

[Place]

[Date], 20__

ON [Business Day on which payment is required in accordance with the provisions of the fifth paragraph of the Letter of Credit]

PAY TO [Name of beneficiary] U.S.\$ [not to exceed the lesser of the Maximum Drawing Amount or the Maximum Credit Amount] DOLLARS

FOR VALUE RECEIVED AND CHARGE TO ACCOUNT OF LETTER OF

CREDIT NO. P-010152 (formerly numbered as S-1002)

OF

JPMorgan Chase Bank, N.A.
[c/o JP Morgan Treasury Services
Standby Letter of Credit Manager -
Immediate Action Required
4th Floor
10240 Highland Manor Drive
Tampa, Florida 33610]

[Governmental Agency Unit
4 Chase Metrotech Center
10th Floor
Brooklyn, New York 11245
Attention: Global Trade]

[Name and address of Equity Participant]

By: _____
[Authorized Representative]

Letter of Credit - Exhibit 2

CERTIFICATE

The undersigned, a duly authorized representative of Emerson Finance LLC (the "EQUITY PARTICIPANT"), as beneficiary under that certain amended and restated irrevocable transferable Letter of Credit No. P-010152 (formerly numbered as S-1002) dated May 19, 2005, established by JPMorgan Chase Bank, N.A. (the "ISSUING BANK") and issued pursuant to that certain Amended and Restated Reimbursement Agreement dated as of May 19, 2005 between Arizona Public Service Company (the "COMPANY"), the Issuing Bank and the other Banks named therein, hereby certifies as follows:

1. An Event of Default under the Facility Lease has occurred and is continuing.

2. The amount of the accompanying draft does not exceed the Maximum Drawing Amount available under the Letter of Credit on the date hereof, as determined in accordance with the terms of the Letter of Credit.

Capitalized terms used herein and not otherwise defined herein shall have the meanings given to them in the Letter of Credit.

IN WITNESS WHEREOF, the undersigned has executed this Certificate as of ,
20__ .

[Name of Equity Participant]

[Name and Title of Authorized
Representative of Equity Participant]

Letter of Credit - Exhibit 3

EXHIBIT 4
TO LETTER OF CREDIT

JPMorgan Chase Bank, N.A.
[c/o JP Morgan Treasury Services
Standby Letter of Credit Manager -
Immediate Action Required
4th Floor
10240 Highland Manor Drive
Tampa, Florida 33610]

[Governmental Agency Unit
4 Chase Metrotech Center
10th Floor
Brooklyn, New York 11245
Attention: Global Trade]

Dear Sirs:

Reference is made to the certain amended and restated irrevocable transferable Letter of Credit bearing Letter of Credit No. P-010152 (formerly numbered as S-1002) dated May 19, 2005 (the "LETTER OF CREDIT"), which has been established by you in favor of [name of Equity Participant (the "TRANSFEROR")].

The Transferor has transferred (and hereby confirms to you said transfer) all of its rights in and under said Letter of Credit to [name of Transferee (the "TRANSFEREE")] and confirms that the Transferor no longer has any rights under or interest in said Letter of Credit.

The Letter of Credit is returned herewith and we request that you issue an irrevocable transferable letter of credit in the name of the Transferee and providing for notices to be sent to the Transferee at the address set forth below and in all other respects identical to the Letter of Credit.

Transferee hereby certifies that it is a duly authorized transferee under the terms of said Letter of Credit and is accordingly entitled, upon presentation of the drafts and certificates called for therein, to receive payments thereunder. Notices under the Letter of Credit should be sent to the Transferee as follows: [Name], [Address], [Facsimile Number], Attention: -.

[Name of Transferor]

[Name and Title of Authorized
Representative of Transferor]

[Name of Transferee]

[Name and Title of Authorized
Representative of Transferee]

SCHEDULE I
TO LETTER OF CREDIT

The following terms have the following meanings for purposes of the Letter of Credit and the Schedules and Exhibits thereto. Terms defined in the Letter of Credit have the meanings given to them therein. Terms defined by reference to the Facility Lease have the meanings assigned to them therein from time to time.

"ADMINISTRATIVE AGENT" means JPMorgan Chase Bank, N.A., in its capacity as administrative agent for the Banks under the Reimbursement Agreement, and its successors in such capacity.

"APPLICABLE LAW" has the meaning assigned to it in the Facility Lease.

"BANK" means (i) each bank or financial institution listed on the signature pages of the Reimbursement Agreement, each Assignee that becomes a Bank pursuant to Section 15(a) of the Reimbursement Agreement, and their respective successors, and (ii) the Issuing Bank with respect to its Participation.

"BUSINESS DAY" means any day except a Saturday, Sunday or other day on which commercial banks in New York, New York, Chicago, Illinois or the State of California are authorized by law to close.

"CAPITAL LEASE OBLIGATIONS" means as to any Person, the obligations of such Person to pay rent or other amounts under a lease of (or other agreement conveying the right to use) real and/or personal property, which obligations are required to be classified and accounted for as a capital lease on the balance sheet of such Person under generally accepted accounting principles and, for the purposes of this Agreement, the amount of such obligations shall be the capitalized amount thereof, determined in accordance with generally accepted accounting principles.

"CODE" means the Internal Revenue Code of 1986, as amended, or any successor statute.

"EQUITY PARTICIPANT" means Emerson Finance LLC, as Equity Participant, and its successors and assigns.

"ERISA" means the Employee Retirement Income Security Act of 1974, as amended from time to time, and the regulations promulgated and rulings issued thereunder.

"ERISA AFFILIATE" means any corporation or trade or business which is a member of the same controlled group of corporations (within the meaning of

Section 414(b) of the Code) as the Company or is under common control (within the meaning of Section 414(c) of the Code) with the Company.

"GOVERNMENTAL ACTION" has the meaning assigned to it in the Facility Lease.

"GUARANTEE" means as to any Person, any obligation, contingent or otherwise, of such Person directly or indirectly guaranteeing any Indebtedness of any other Person or in any manner providing for the payment of any Indebtedness of any other Person or otherwise protecting the holder of such Indebtedness against loss (whether by virtue of partnership arrangements, agreements to keep well, to purchase assets, goods, securities or services, or to take-or-pay or otherwise), provided that the term "Guarantee" shall not include endorsements for collection or deposit in the ordinary course of business. The term "Guarantee" used as a verb has a corresponding meaning.

"INDEBTEDNESS" means as to any Person at any date (without duplication): (a) indebtedness created, issued, incurred or assumed by such Person for borrowed money or evidenced by bonds, debentures, notes or similar instruments; (b) all obligations of such Person to pay the deferred purchase price of property or services, excluding, however, trade accounts payable (other than for borrowed money) arising in, and accrued expenses incurred in, the ordinary course of business of such Person so long as such trade accounts payable are paid within 180 days of the date incurred; (c) all Indebtedness secured by a lien on any asset of such Person, to the extent such Indebtedness has been assumed by, or is a recourse obligation of, such Person; (d) all Guarantees by such Person; (e) all Capital Lease Obligations of such Person; and (f) the amount of all reimbursement obligations of such Person (whether contingent or otherwise) in respect of letters of credit, bankers' acceptances, surety or other bonds and similar instruments in support of Indebtedness.

"ISSUING BANK" means JPMorgan Chase Bank, N.A., and its successors in their capacity as issuer of the Letter of Credit.

"MATERIAL SUBSIDIARY" means, at any time, a Subsidiary of the Company which as of such time meets the definition of a "significant subsidiary" included as of May 19, 2005 in Regulation S-X of the Securities and Exchange Commission or whose assets at such time exceed 10% of the assets of the Company and the Subsidiaries (on a consolidated basis).

"MODIFIED SPECIAL CASUALTY VALUE" has the meaning assigned to it in the Facility Lease.

"MULTIEMPLOYER PLAN" means a plan defined as such in Section 3(37) of ERISA to which contributions have been made by the Company or any ERISA

Affiliate within any of the preceding five plan years and which is covered by Title IV of ERISA.

"PARTICIPANT" has the meaning set forth in Section 15(b) of the Reimbursement Agreement.

"PARTICIPATION" means a participating interest in the credit represented by the Letter of Credit including, without limitation, the interest therein retained by the Issuing Bank after giving effect to all participating interests therein granted by it pursuant to Section 14(a) of the Reimbursement Agreement, but prior to giving effect to any interest therein granted to any Participant pursuant to Section 15(b) of the Reimbursement Agreement.

"PARTICIPATION AMOUNT" means, with respect to any Bank, the amount set forth in Schedule II to the Reimbursement Agreement opposite the name of such Bank therein, as such amount may be changed by reason of an assignment by or to such Bank in accordance with Section 15(a). Such amount shall be reduced from time to time by such Bank's ratable share of each reduction of the Maximum Credit Amount.

"PARTICIPATION PERCENTAGE" means, with respect to any Bank at any time, the percentage equivalent of a fraction (i) the numerator of which is the Participation Amount of such Bank at such time and (ii) the denominator of which is the Maximum Credit Amount at such time.

"PBGC" means the Pension Benefit Guaranty Corporation or any entity succeeding to any or all of its functions under ERISA.

"PERSON" means an individual, a corporation, a partnership, an association, a trust or any other entity or organization, including a government or political subdivision or an agency or instrumentality thereof.

"PLAN" means an employee benefit plan within the meaning of Section 3(3) of ERISA established or maintained by the Company or any ERISA Affiliate which is covered by Title IV of ERISA, other than a Multiemployer Plan.

"REIMBURSEMENT AGREEMENT" means the Reimbursement Agreement as originally executed as of August 1, 1986, as amended or amended and restated from time to time before May 19, 2005, as amended and restated as of May 19, 2005 among Arizona Public Service Company, the Banks party thereto, and JPMorgan Chase Bank, N.A., as Administrative Agent and Issuing Bank, and as the same may be amended and restated from time to time thereafter.

"REQUIRED BANKS" means, at any time, Banks holding Participation Percentages aggregating more than 50% at such time.

"STATED TERMINATION DATE" means May 19, 2010 or such later date to which such Stated Termination Date shall have been extended pursuant to Section 17 of the Reimbursement Agreement.

"SUBSIDIARY" of any Person means any corporation of which more than 50% of the issued and outstanding capital stock having ordinary voting power to elect a majority of the Board of Directors of such corporation (irrespective of whether at the time capital stock of any other class or classes of such corporation shall or might have voting power upon the occurrence of any contingency) is at the time directly or indirectly owned or controlled by such Person and one or more of its other Subsidiaries or by one or more of such Person's other Subsidiaries.

"TERMINATION DATE" means the earliest of (i) the date on which the Issuing Bank pays a drawing under the Letter of Credit for the lesser of the Maximum Drawing Amount and the Maximum Credit Amount, (ii) if a drawing is not requested by the Equity Participant after a notice of termination is given under the Letter of Credit, the Date of Early Termination, (iii) if a drawing is requested by the Equity Participant after a notice of termination is given under the Letter of Credit, the date on which the Issuing Bank pays such drawing, (iv) the date on which the Company delivers a certificate to the Issuing Bank certifying that the Company has paid the amounts due under Section 9(c) of the Facility Lease (so long as the Equity Participant shall have acknowledged such payment by its express confirmation thereof in, and its countersignature to, such certificate), (v) the date on which the Company delivers a certificate to the Issuing Bank certifying that the Company has paid the amounts due under Section 9(d) of the Facility Lease (so long as the Equity Participant shall have acknowledged such payment by its express confirmation thereof in, and its countersignature to, such certificate), and (vi) the latest of (x) the Stated Termination Date, (y) if a draft and certificate all in strict conformity with the terms and conditions of the Letter of Credit are presented on the Stated Termination Date at such time and at such office as specified in the fifth paragraph of the Letter of Credit, the date on which the Issuing Bank is required to honor the draft in accordance with the provisions of such paragraph pursuant to such presentation, and (z) if a corrected draft and certificate all in strict conformity with the terms and conditions of the Letter of Credit are presented on such date as specified in, and in accordance with the provisions of, the sixth paragraph of the Letter of Credit, the date on which the Issuing Bank is required to honor the draft in accordance with the provisions of such paragraph pursuant to such presentation.

"TRANSACTION DOCUMENTS" means the Participation Agreement, the Refinancing Agreement, the Indemnity Agreement, the Escrow Deposit Agreement, the Facility Lease, the Trust Agreement, the Indenture, the Decommissioning Trust Agreement, the Tax Indemnification Agreement, the Mortgage Release, the Assignment and Assumption, the Purchase Documents,

any ground lease contemplated by Section 10(b)(3)(xvii) of the Participation Agreement and the Notes, each as defined in the Facility Lease.

SCHEDULE II-A
TO LETTER OF CREDIT

TABLE OF MAXIMUM CREDIT AMOUNTS
EMERSON FINANCE LLC

APPLICABLE PERIOD

MAXIMUM CREDIT AMOUNT

From May 19, 2005 through July 10, 2005	\$ 55,207,639.45
From July 11, 2005 through January 10, 2006	\$ 54,073,073.44
From January 11, 2006 through July 10, 2006	\$ 51,520,058.76
From July 11, 2006 through January 10, 2007	\$ 50,939,589.19
From January 11, 2007 through July 10, 2007	\$ 47,820,443.92
From July 11, 2007 through January 10, 2008	\$ 47,088,800.23
From January 11, 2008 through July 10, 2008	\$ 43,631,504.04
From July 11, 2008 through January 10, 2009	\$ 42,847,098.46
From January 11, 2009 through July 10, 2009	\$ 39,198,185.36
From July 11, 2009 through January 10, 2010	\$ 38,352,436.54
From January 11, 2010 through May 19, 2010	\$ 34,494,359.44

Letter of Credit - Schedule II-A

SCHEDULE II-B
TO LETTER OF CREDIT

TABLE OF MAXIMUM DRAWING AMOUNTS
EMERSON FINANCE LLC

APPLICABLE PERIOD	MAXIMUM DRAWING AMOUNT
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From May 19, 2005 through July 10, 2005	\$ 55,207,639.45
From July 11, 2005 through January 10, 2006	\$ 54,073,073.44
From January 11, 2006 through July 10, 2006	\$ 51,520,058.76
From July 11, 2006 through January 10, 2007	\$ 50,939,589.19
From January 11, 2007 through July 10, 2007	\$ 47,820,443.92
From July 11, 2007 through January 10, 2008	\$ 47,088,800.23
From January 11, 2008 through July 10, 2008	\$ 43,631,504.04
From July 11, 2008 through January 10, 2009	\$ 42,847,098.46
From January 11, 2009 through July 10, 2009	\$ 39,198,185.36
From July 11, 2009 through January 10, 2010	\$ 38,352,436.54
From January 11, 2010 through May 19, 2010	\$ 34,494,359.44

Letter of Credit - Schedule II-B

SCHEDULE III
TO LETTER OF CREDIT

The Issuing Bank shall have the right upon the occurrence of any of the events listed below to terminate the Letter of Credit in accordance with the terms of the Letter of Credit:

(A) The Company shall fail to pay when due any amount payable under Section 2(a) of the Reimbursement Agreement or fail to pay any other amount payable under Section 2 of the Reimbursement Agreement within five Business Days after the same becomes due and payable; or

(B) The Company shall fail to perform or observe (i) any term, covenant or agreement contained in Section 7(a)(ii), 7(g)(iv), 7(h), 8(a), 8(b), 8(c) or 8(e) of the Reimbursement Agreement, or (ii) any term, covenant or agreement contained in the Reimbursement Agreement (other than those covered by clause (A) above or subclause (i) of this clause (B) or Section 7(e) or Section 19 of the Reimbursement Agreement) on its part to be performed or observed if the failure to perform or observe such term, covenant or agreement shall remain unremedied for 30 days after written notice thereof shall have been given to the Company by the Administrative Agent; or

(C) Any representation or warranty made by the Company in the Reimbursement Agreement or by the Company (or any of its officers) in any certificate delivered in connection with the Reimbursement Agreement shall prove to have been false or misleading in any material respect when made; or

(D) Any material provision of the Reimbursement Agreement shall at any time for any reason cease to be valid and binding upon the Company, or shall be declared to be null and void, or the validity or enforceability thereof shall be contested by the Company or any governmental agency or authority, or the Company shall deny that it has any or further liability or obligation under the Reimbursement Agreement; or

(E) The Company shall fail to pay any principal of or premium or interest on any Indebtedness which is outstanding in a principal amount of at least \$5,000,000 (but excluding Indebtedness owing under the Reimbursement Agreement) of the Company, when the same becomes due and payable (whether by scheduled maturity, required prepayment, acceleration, demand or otherwise), and such failure shall continue after the applicable grace period, if any, specified in the agreement or instrument relating to such Indebtedness; or the Company shall fail to perform or comply with any other term or covenant in any agreement or instrument relating to any such Indebtedness and such failure shall continue after the applicable grace period, if any, specified in such agreement or instrument,

if the effect of such failure is to accelerate, or to permit the acceleration of, the maturity of such Indebtedness; or

(F) The Company shall fail to pay any principal of or premium or interest in respect of any operating lease in respect of which the payment obligations of the Company have a present value of at least \$25,000,000, when the same becomes due and payable (whether by scheduled maturity, required prepayment, acceleration, demand or otherwise), and such failure shall continue after the applicable grace period, if any, specified in such operating lease, if the effect of such failure is to terminate, or to permit the termination of, such operating lease; or

(G) The Company shall generally not pay its debts as such debts become due, or shall admit in writing its inability to pay its debts generally, or shall make a general assignment for the benefit of creditors; or any proceeding shall be instituted by or against the Company seeking to adjudicate it a bankrupt or insolvent, or seeking liquidation, winding up, reorganization, arrangement, adjustment, protection, relief, or composition of it or its debts under any law relating to bankruptcy, insolvency or reorganization or relief of debtors, or seeking the entry of an order for relief or the appointment of a receiver, trustee, custodian or other similar official for it or for any substantial part of its property and, in the case of any such proceeding instituted against it (but not instituted by it), either such proceeding shall remain undismissed or unstayed for a period of 60 days, or any of the actions sought in such proceeding (including, without limitation, the entry of an order for relief against, or the appointment of a receiver, trustee, custodian or other similar official for, it or for any substantial part of its property) shall occur; or the Company shall take any corporate action to authorize any of the actions set forth above in this clause (G) or

(H) Any Material Subsidiary shall generally not pay its debts as such debts become due, or shall admit in writing its inability to pay its debts generally, or shall make a general assignment for the benefit of creditors; or any proceeding shall be instituted by or against any Material Subsidiary seeking to adjudicate it a bankrupt or insolvent, or seeking liquidation, winding up, reorganization, arrangement, adjustment, protection, relief, or composition of it or its debts under any law relating to bankruptcy, insolvency or reorganization or relief of debtors, or seeking the entry of an order for relief or the appointment of a receiver, trustee, custodian or other similar official for it or for any substantial part of its property and, in the case of any such proceeding instituted against it (but not instituted by it), either such proceeding shall remain undismissed or unstayed for a period of 60 days, or any of the actions sought in such proceeding (including, without limitation, the entry of an order for relief against, or the appointment of a receiver, trustee, custodian or other similar official for it or for any substantial part of its property) shall occur; or any Material Subsidiary shall take any corporate action to authorize any of the actions set forth above in this clause (H) and, in each case,

the Required Banks determine that such circumstances could have a material adverse effect on the financial condition or financial prospects of the Company and its consolidated Subsidiaries, taken as a whole; or

(I) Any judgment or order for the payment of money that exceeds any applicable insurance coverage by more than \$5,000,000 shall be rendered against the Company and such judgment or order shall remain unsatisfied or unstayed for a period of 30 days; or

(J) Any judgment or order for the payment of money that exceeds any applicable insurance coverage by more than \$25,000,000 shall be rendered against any Material Subsidiary; such judgment or order shall remain unsatisfied or unstayed for 30 days; and the Required Banks determine that such judgment or order could have a material adverse effect on the financial condition or financial prospects of the Company and its consolidated Subsidiaries, taken as a whole; or

(K) An event or condition specified in Section 7(g)(iv) of the Reimbursement Agreement shall occur or exist with respect to any Plan or Multiemployer Plan and, as a result of such event or condition, together with all other such events or conditions, the Company or any ERISA Affiliate shall incur or in the opinion of the Required Banks shall be reasonably likely to incur a liability to a Plan, a Multiemployer Plan or the PBGC (or any combination of the foregoing) which is, in the determination of the Required Banks, material in relation to the financial condition or the financial prospects of the Company and its consolidated Subsidiaries, taken as a whole; or

(L) any change in Applicable Law or any Governmental Action shall occur which has the effect of making the transactions contemplated by the Transaction Documents unauthorized, illegal or otherwise contrary to Applicable Law; or

(M) any event specified in Sections 15(vii), (viii) or (x) of the Facility Lease shall occur; or

(N) the Company shall fail to make, or cause to be made, any payment specified in Section 15(i) of the Facility Lease equal to or exceeding \$1,000,000 within the periods specified in that Section.

Capitalized terms used herein and not otherwise defined herein shall have the meanings given to them in the Letter of Credit.