



**UNITED STATES**  
**SECURITIES AND EXCHANGE COMMISSION**  
**Washington D.C. 20549**  
**FORM 10-Q**

(Mark One)

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

For the quarterly period ended March 31, 2004

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 1-3701

**AVISTA CORPORATION**

(Exact name of registrant as specified in its charter)

Washington

(State or other jurisdiction of  
incorporation or organization)

91-0462470

(I.R.S. Employer  
Identification No.)

1411 East Mission Avenue, Spokane, Washington

(Address of principal executive offices)

99202-2600

(Zip Code)

Registrant's telephone number, including area code: 509-489-0500

Web site: <http://www.avistacorp.com>

None

(Former name, former address and former fiscal year, if changed since last report)

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

Yes [X]      No [ ]

Indicate by check mark whether the Registrant is an accelerated filer (as defined in Rule 12b-2 of the Exchange Act):

Yes [X]      No [ ]

As of April 30, 2004, 48,378,373 shares of Registrant's Common Stock, no par value (the only class of common stock), were outstanding.

AVISTA CORPORATION

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Avista CorporationFor the Three Months Ended March 31  
Dollars in thousands, except per share amounts

	2004	2003
OPERATING REVENUES	\$343,732	\$338,892
OPERATING EXPENSES:		
Resource costs	198,954	185,916
Operations and maintenance	38,054	33,323
Administrative and general	25,496	27,863
Depreciation and amortization	17,682	18,942
Taxes other than income taxes	20,339	17,858
Total operating expenses	300,525	283,902
INCOME FROM OPERATIONS	43,207	54,990
OTHER INCOME (EXPENSE):		
Interest expense	(22,151)	(23,509)
Interest expense to affiliated trusts	(1,478)	—
Capitalized interest	580	172
Net interest expense	(23,049)	(23,337)
Other income — net	1,656	254
Total other income (expense)-net	(21,393)	(23,083)
INCOME FROM CONTINUING OPERATIONS BEFORE INCOME TAXES	21,814	31,907
INCOME TAXES	9,130	13,465
INCOME FROM CONTINUING OPERATIONS	12,684	18,442
DISCONTINUED OPERATIONS (Note 3):		
Loss before income tax benefit	—	(2,044)
Income tax benefit	—	924
LOSS FROM DISCONTINUED OPERATIONS	—	(1,120)
NET INCOME BEFORE CUMULATIVE EFFECT OF ACCOUNTING CHANGE	12,684	17,322
CUMULATIVE EFFECT OF ACCOUNTING CHANGE (net of tax)	(460)	(1,190)
NET INCOME	12,224	16,132
DEDUCT-Preferred stock dividend requirements	—	578
INCOME AVAILABLE FOR COMMON STOCK	\$ 12,224	\$ 15,554
Weighted-average common shares outstanding (thousands), Basic	48,352	48,100
Weighted-average common shares outstanding (thousands), Diluted	49,038	48,119
EARNINGS PER COMMON SHARE, BASIC AND DILUTED (Note 12):		
Earnings per common share from continuing operations	\$ 0.26	\$ 0.37
Loss per common share from discontinued operations	—	(0.02)
Earnings per common share before cumulative effect of accounting change	0.26	0.35
Loss per common share from cumulative effect of accounting change	(0.01)	(0.03)
Total earnings per common share, basic and diluted	\$ 0.25	\$ 0.32
Dividends paid per common share	\$ 0.125	\$ 0.120

*The Accompanying Notes are an Integral Part of These Statements.*

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Avista CorporationFor the Three Months Ended March 31  
Dollars in thousands

	<u>2004</u>	<u>2003</u>
NET INCOME	\$12,224	\$16,132
OTHER COMPREHENSIVE INCOME (LOSS):		
Foreign currency translation adjustment	(72)	291
Unrealized gains (losses) on interest rate swap agreements - net of taxes of \$102 and \$(9), respectively	189	(17)
Unfunded accumulated benefit obligation - net of taxes of \$6	—	12
Unrealized losses on derivative commodity instruments - net of taxes of \$(701)	(1,301)	—
Reclassification adjustment for realized gains on derivative commodity instruments included in net income — net of taxes of \$(32)	(59)	—
TOTAL OTHER COMPREHENSIVE INCOME (LOSS)	(1,243)	286
COMPREHENSIVE INCOME	<u>\$10,981</u>	<u>\$16,418</u>

*The Accompanying Notes are an Integral Part of These Statements.*

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Avista Corporation

Dollars in thousands

	March 31, 2004	December 31, 2003
<b>ASSETS:</b>		
<b>CURRENT ASSETS:</b>		
Cash and cash equivalents	\$ 160,986	\$ 128,126
Restricted cash	22,144	16,472
Securities held for trading	4,913	18,903
Accounts and notes receivable-less allowances of \$46,539 and \$46,382, respectively	238,478	318,848
Energy commodity assets	273,996	253,676
Materials and supplies, fuel stock and natural gas stored	14,023	22,428
Prepayments and other current assets	75,022	79,472
Deferred income taxes	11,201	11,455
Total current assets	<u>800,763</u>	<u>849,380</u>
<b>NET UTILITY PROPERTY:</b>		
Utility plant in service	2,620,964	2,606,012
Construction work in progress	47,589	49,615
Total	2,668,553	2,655,627
Less: Accumulated depreciation and amortization	745,601	741,626
Total net utility property	<u>1,922,952</u>	<u>1,914,001</u>
<b>OTHER PROPERTY AND INVESTMENTS:</b>		
Investment in exchange power-net	37,771	38,383
Non-utility properties and investments-net	92,770	89,133
Non-current energy commodity assets	245,960	242,359
Investment in affiliated trusts	13,403	13,403
Other property and investments-net	18,856	17,958
Total other property and investments	<u>408,760</u>	<u>401,236</u>
<b>DEFERRED CHARGES:</b>		
Regulatory assets for deferred income tax	131,957	131,763
Other regulatory assets	41,429	44,381
Utility energy commodity derivative assets	46,774	39,500
Power and natural gas deferrals	165,748	171,342
Unamortized debt expense	46,946	48,825
Other deferred charges	28,667	30,431
Total deferred charges	<u>461,521</u>	<u>466,242</u>
<b>TOTAL ASSETS</b>	<u><b>\$3,593,996</b></u>	<u><b>\$3,630,859</b></u>

*The Accompanying Notes are an Integral Part of These Statements.*

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Avista Corporation

Dollars in thousands

	March 31, 2004	December 31, 2003
<b>LIABILITIES AND STOCKHOLDERS' EQUITY:</b>		
<b>CURRENT LIABILITIES:</b>		
Accounts payable	\$ 219,946	\$ 298,285
Energy commodity liabilities	244,943	229,642
Deposits from counterparties	111,954	97,811
Current portion of long-term debt	29,899	29,711
Current portion of preferred stock-cumulative (17,500 shares outstanding)	1,750	1,750
Short-term borrowings	55,520	80,525
Interest accrued	22,785	18,504
Other current liabilities	90,066	82,125
Total current liabilities	<u>776,863</u>	<u>838,353</u>
LONG-TERM DEBT	<u>930,923</u>	<u>925,012</u>
LONG-TERM DEBT TO AFFILIATED TRUSTS	<u>113,403</u>	<u>113,403</u>
PREFERRED STOCK-CUMULATIVE (subject to mandatory redemption):		
10,000,000 shares authorized: \$6.95 Series K 297,500 shares outstanding (\$100 stated value)	<u>29,750</u>	<u>29,750</u>
<b>OTHER NON-CURRENT LIABILITIES AND DEFERRED CREDITS:</b>		
Non-current energy commodity liabilities	196,885	192,731
Regulatory liability for utility plant retirement costs	170,505	167,061
Utility energy commodity derivative liabilities	33,892	36,057
Deferred income taxes	492,088	492,799
Other non-current liabilities and deferred credits	92,410	84,441
Total other non-current liabilities and deferred credits	<u>985,780</u>	<u>973,089</u>
<b>TOTAL LIABILITIES</b>	<u><u>2,836,719</u></u>	<u><u>2,879,607</u></u>
<b>COMMITMENTS AND CONTINGENCIES (See Notes to Consolidated Financial Statements)</b>		
<b>STOCKHOLDERS' EQUITY:</b>		
Common stock, no par value; 200,000,000 shares authorized; 48,375,327 and 48,344,009 shares outstanding, respectively	627,368	626,788
Note receivable from employee stock ownership plan	(1,981)	(2,424)
Capital stock expense and other paid in capital	(10,753)	(10,950)
Accumulated other comprehensive loss	(9,283)	(8,040)
Retained earnings	151,926	145,878
<b>TOTAL STOCKHOLDERS' EQUITY</b>	<u>757,277</u>	<u>751,252</u>
<b>TOTAL LIABILITIES AND STOCKHOLDERS' EQUITY</b>	<u><u>\$3,593,996</u></u>	<u><u>\$3,630,859</u></u>

*The Accompanying Notes are an Integral Part of These Statements.*

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Increase (Decrease) in Cash and Cash Equivalents  
Avista CorporationFor the Three Months Ended March 31  
Dollars in thousands

	2004	2003
<b>CONTINUING OPERATING ACTIVITIES:</b>		
Net income	\$ 12,224	\$ 16,132
Loss from discontinued operations	—	1,120
Cumulative effect of accounting change	460	1,190
Purchases of securities held for trading	(1,994)	—
Sales of securities held for trading	15,973	—
Non-cash items included in net income:		
Depreciation and amortization	17,682	18,942
Provision for deferred income taxes	(31)	4,151
Power and natural gas cost amortizations, net of deferrals	5,194	8,271
Amortization of debt expense	2,036	2,002
Energy commodity assets and liabilities	(6,558)	(12,363)
Other	3,440	(123)
Changes in working capital components:		
Restricted cash	(5,672)	2,266
Sale of customer accounts receivable under revolving agreement-net	(4,000)	13,000
Accounts and notes receivable	84,195	(43,586)
Materials and supplies, fuel stock and natural gas stored	8,405	8,341
Other current assets	4,450	28,364
Accounts payable	(78,339)	62,896
Deposits from counterparties	14,143	(4,495)
Other current liabilities	12,222	7,265
<b>NET CASH PROVIDED BY CONTINUING OPERATING ACTIVITIES</b>	<b>83,830</b>	<b>113,373</b>
<b>CONTINUING INVESTING ACTIVITIES:</b>		
Utility property construction expenditures (excluding AFUDC)	(19,889)	(18,585)
Other capital expenditures	(636)	(2,472)
Changes in other property and investments	(477)	(155)
Repayments received on notes receivable	990	97
<b>NET CASH USED IN CONTINUING INVESTING ACTIVITIES</b>	<b>(20,012)</b>	<b>(21,115)</b>
<b>CONTINUING FINANCING ACTIVITIES:</b>		
Decrease in short-term borrowings	(25,005)	(30,000)
Redemption and maturity of long-term debt	(910)	(15,797)
Redemption of preferred stock	—	(1,575)
Issuance of common stock	1,868	1,745
Repurchase of common stock under equity compensation plans	(815)	—
Cash dividends paid	(6,043)	(6,349)
Cash received in interest rate swap agreement	125	—
Premiums paid for the redemption of long-term debt	(97)	(88)
Long-term debt and short-term borrowing issuance costs	(81)	(50)
<b>NET CASH USED IN CONTINUING FINANCING ACTIVITIES</b>	<b>(30,958)</b>	<b>(52,114)</b>
<b>NET CASH PROVIDED BY CONTINUING OPERATIONS</b>	<b>32,860</b>	<b>40,144</b>
<b>NET CASH USED IN DISCONTINUED OPERATIONS</b>	<b>—</b>	<b>(2,089)</b>
<b>NET INCREASE IN CASH AND CASH EQUIVALENTS</b>	<b>32,860</b>	<b>38,055</b>
<b>CASH AND CASH EQUIVALENTS AT BEGINNING OF PERIOD</b>	<b>128,126</b>	<b>173,286</b>
<b>CASH AND CASH EQUIVALENTS AT END OF PERIOD</b>	<b>\$160,986</b>	<b>\$211,341</b>
<b>SUPPLEMENTAL CASH FLOW INFORMATION:</b>		
Cash paid (received) during the period:		
Interest	\$ 17,077	\$ 18,185
Income taxes	(1,933)	3,502

*The Accompanying Notes are an Integral Part of These Statements.*



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## SCHEDULE OF INFORMATION BY BUSINESS SEGMENTS

Avista Corporation

For the Three Months Ended March 31

Dollars in thousands

	2004	2003
<b>OPERATING REVENUES:</b>		
Avista Utilities	\$ 290,005	\$ 259,740
Energy Marketing and Resource Management	103,718	122,877
Avista Advantage	5,286	4,763
Other	3,913	4,100
Intersegment eliminations	(59,190)	(52,588)
Total operating revenues	<u>\$ 343,732</u>	<u>\$ 338,892</u>
<b>RESOURCE COSTS:</b>		
Avista Utilities	\$ 164,333	\$ 144,528
Energy Marketing and Resource Management	93,811	93,976
Intersegment eliminations	(59,190)	(52,588)
Total resource costs	<u>\$ 198,954</u>	<u>\$ 185,916</u>
<b>GROSS MARGINS (operating revenues less resource costs):</b>		
Avista Utilities	\$ 125,672	\$ 115,212
Energy Marketing and Resource Management	9,907	28,901
Total gross margins (operating revenues less resource costs)	<u>\$ 135,579</u>	<u>\$ 144,113</u>
<b>OPERATIONS AND MAINTENANCE EXPENSES:</b>		
Avista Utilities	\$ 31,565	\$ 26,288
Energy Marketing and Resource Management	—	—
Avista Advantage	2,814	3,245
Other	3,675	3,790
Total operations and maintenance expenses	<u>\$ 38,054</u>	<u>\$ 33,323</u>
<b>ADMINISTRATIVE AND GENERAL EXPENSES:</b>		
Avista Utilities	\$ 18,046	\$ 16,996
Energy Marketing and Resource Management	4,661	8,594
Avista Advantage	1,785	1,628
Other	1,004	645
Total administrative and general expenses	<u>\$ 25,496</u>	<u>\$ 27,863</u>
<b>DEPRECIATION AND AMORTIZATION EXPENSES:</b>		
Avista Utilities	\$ 16,236	\$ 17,403
Energy Marketing and Resource Management	347	305
Avista Advantage	507	686
Other	592	548
Total depreciation and amortization expenses	<u>\$ 17,682</u>	<u>\$ 18,942</u>
<b>INCOME FROM OPERATIONS:</b>		
Avista Utilities	\$ 39,661	\$ 36,873
Energy Marketing and Resource Management	4,719	19,804
Avista Advantage	180	(795)
Other	(1,353)	(892)
Total income from operations	<u>\$ 43,207</u>	<u>\$ 54,990</u>
<b>INCOME FROM CONTINUING OPERATIONS:</b>		
Avista Utilities	\$ 10,816	\$ 8,326
Energy Marketing and Resource Management	3,530	13,065
Avista Advantage	(17)	(639)
Other	(1,645)	(2,310)
Total income from continuing operations	<u>\$ 12,684</u>	<u>\$ 18,442</u>
<b>ASSETS (2003 amounts as of December 31):</b>		
Avista Utilities	\$2,546,647	\$2,532,936
Energy Marketing and Resource Management	963,737	1,013,213
Avista Advantage	31,578	36,405
Other	52,034	48,305
Total assets	<u>\$3,593,996</u>	<u>\$3,630,859</u>
<b>CAPITAL EXPENDITURES:</b>		
Avista Utilities	\$ 19,889	\$ 18,585
Energy Marketing and Resource Management	289	1,988
Avista Advantage	53	74
Other	294	410
Total capital expenditures	<u>\$ 20,525</u>	<u>\$ 21,057</u>

*The Accompanying Notes are an Integral Part of These Statements.*

**AVISTA CORPORATION**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

The accompanying consolidated financial statements of Avista Corporation (Avista Corp. or the Company) for the interim periods ended March 31, 2004 and 2003 are unaudited; however, in the opinion of management, reflect all adjustments necessary for a fair statement of the results of operations for those interim periods. The consolidated financial statements have been prepared in accordance with accounting principles generally accepted in the United States of America for interim financial information and with the instructions to Form 10-Q and Rule 10-01 of Regulation S-X. The Consolidated Statements of Income for the interim periods are not necessarily indicative of the results to be expected for the full year. These consolidated financial statements do not contain the detail or footnote disclosure concerning accounting policies and other matters which would be included in full fiscal year consolidated financial statements; therefore, they should be read in conjunction with the Company's audited consolidated financial statements included in the Company's Annual Report on Form 10-K for the year ended December 31, 2003 (2003 Form 10-K).

Please refer to the section "Acronyms and Terms" in the 2003 Form 10-K for definitions of terms such as capacity, energy and therm.

**NOTE 1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES**

***Nature of Business***

Avista Corp. is an energy company engaged in the generation, transmission and distribution of energy as well as other energy-related businesses. Avista Utilities is an operating division of Avista Corp., comprising the regulated utility operations. Avista Utilities generates, transmits and distributes electricity in parts of eastern Washington and northern Idaho. Avista Utilities also provides natural gas distribution service in parts of eastern Washington, northern Idaho, northeast and southwest Oregon and in the South Lake Tahoe region of California. Avista Capital, a wholly owned subsidiary of Avista Corp., is the parent company of all of the subsidiary companies in the non-utility business segments.

The Company's operations are exposed to risks including, but not limited to, the price and supply of purchased power, fuel and natural gas, regulatory allowance of power and natural gas costs and capital investments, streamflow and weather conditions, the effects of changes in legislative and governmental regulations, changes in regulatory requirements, availability of generation facilities, competition, technology and availability of funding. Also, like other utilities, the Company's facilities and operations may be exposed to terrorism risks or other malicious acts. In addition, the energy business exposes the Company to the financial, liquidity, credit and commodity price risks associated with wholesale purchases and sales.

***Basis of Reporting***

The consolidated financial statements include the assets, liabilities, revenues and expenses of the Company and its subsidiaries. The accompanying financial statements include the Company's proportionate share of utility plant and related operations resulting from its interests in jointly owned plants.

***Use of Estimates***

The preparation of the consolidated financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect amounts reported in the consolidated financial statements. Significant estimates include determining unbilled revenues, the market value of energy commodity assets and liabilities, pension and other postretirement benefit plan liabilities, and contingent liabilities. Changes in these estimates and assumptions are considered reasonably possible and may have a material effect on the consolidated financial statements and thus actual results could differ from the amounts reported and disclosed herein.

***Business Segments***

Financial information for each of the Company's business segments is reported in the Schedule of Information by Business Segments. Such information is an integral part of these consolidated financial statements. The business segment presentation reflects the basis currently used by the Company's management to analyze performance and determine the allocation of resources. Avista Utilities' business is managed based on the total regulated utility operation. The Energy Marketing and Resource Management business segment primarily consists of electricity and natural gas marketing, trading and resource management including optimization of energy assets owned by other entities and derivative commodity instruments such as futures, options, swaps and other contractual arrangements.

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Avista Advantage is a provider of utility bill processing, payment and information services to multi-site customers throughout North America. The Other business segment includes other investments and operations of various subsidiaries as well as certain other operations of Avista Capital.

**Avista Utilities Operating Revenues**

Operating revenues for Avista Utilities related to the sale of energy are generally recorded when service is rendered or energy is delivered to customers. The determination of the energy sales to individual customers is based on the reading of their meters, which occurs on a systematic basis throughout the month. At the end of each calendar month, the amount of energy delivered to customers since the date of the last meter reading is estimated and the corresponding unbilled revenue is estimated and recorded.

**Avista Energy Operating Revenues**

Avista Energy follows Statement of Financial Accounting Standards (SFAS) No. 133, "Accounting for Derivative Instruments and Hedging Activities," as amended by SFAS No. 138 and SFAS No. 149, with respect to the majority of its contracts. Avista Energy reports the net margin on derivative commodity instruments held for trading as operating revenues. Revenues from contracts that are not accounted for as derivatives under SFAS No. 133, as well as derivative commodity instruments not held for trading, are reported on a gross basis in operating revenues.

Avista Energy accounted for energy commodity trading activities in compliance with Emerging Issues Task Force (EITF) Issue No. 98-10, "Accounting for Contracts Involved in Energy Trading and Risk Management Activities" through December 31, 2002 for contracts entered into on or prior to October 25, 2002. During the three months ended March 31, 2003, Avista Energy recorded as a cumulative effect of accounting change a charge of \$1.2 million (net of tax) related to EITF Issue No. 02-3, "Issues Involved in Accounting for Derivative Contracts Held for Trading Purposes and Contracts Involved in Energy Trading and Risk Management Activities," which effectively required the transition of accounting for energy trading activities from EITF Issue No. 98-10 to SFAS No. 133.

**Other Income-Net**

Other income-net consisted of the following items for the three months ended March 31 (dollars in thousands):

	2004	2003
Interest income	\$ 1,704	\$ 860
Interest on power and natural gas deferrals	2,015	1,935
Net gain (loss) on the disposition of assets	9	(18)
Net loss on subsidiary investments	(707)	(1,555)
Other expense	(1,946)	(1,652)
Other income	581	684
Total	<u>\$ 1,656</u>	<u>\$ 254</u>

**Stock-Based Compensation**

The Company follows the disclosure only provisions of SFAS No. 123, "Accounting for Stock-Based Compensation." Accordingly, employee stock options are accounted for under Accounting Principle Board Opinion (APB) No. 25, "Accounting for Stock Issued to Employees." Stock options are granted at exercise prices not less than the fair value of common stock on the date of grant. Under APB No. 25, no compensation expense is recognized pursuant to the Company's stock option plans. If compensation expense for the Company's stock option plans were determined consistent with SFAS No. 123, net income and earnings per common share would have been the following pro forma amounts for the three months ended March 31:

	2004	2003
Net income (dollars in thousands):		
As reported	\$12,224	\$16,132
Deduct: Total stock-based employee compensation expense determined under the fair value method for all awards, net of tax	555	719
Pro forma	<u>\$11,669</u>	<u>\$15,413</u>
Basic and diluted earnings per common share:		
As reported	\$ 0.25	\$ 0.32
Pro forma	\$ 0.24	\$ 0.31

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***Restricted Cash***

Restricted cash includes bank deposits of \$20.5 million and \$15.0 million as collateral for letters of credit issued under Avista Energy's credit agreement as of March 31, 2004 and December 31, 2003, respectively. See Note 10 for further information with respect to Avista Energy's credit agreement. Restricted cash also includes deposits held in trust of \$1.6 million and \$1.5 million for certain employees of Avista Energy as part of a bonus retention plan as of March 31, 2004 and December 31, 2003, respectively.

***Depreciation***

For utility operations, depreciation expense is estimated by a method of depreciation accounting utilizing unit rates for hydroelectric plants and composite rates for other utility plant. Such rates are designed to provide for retirements of properties at the expiration of their service lives.

The Company recovers certain utility plant retirement costs through rates charged to customers as a portion of its depreciation expense. During the three months ended March 31, 2004, the Company changed its estimate of utility plant retirement costs that are included as a component of depreciation expense, which resulted in a decrease in the regulatory liability for utility plant retirement costs and an increase in accumulated depreciation. The Company had estimated retirement costs of \$170.5 million and \$167.1 million included as a regulatory liability on the Consolidated Balance Sheet as of March 31, 2004 and December 31, 2003, respectively. These costs do not represent legal or contractual obligations.

***Goodwill***

Goodwill arising from acquisitions represents the excess of the purchase price over the estimated fair value of net assets acquired. The Company evaluates goodwill for impairment using a discounted cash flow model on at least an annual basis or more frequently if impairment indicators arise. The Company completed its annual evaluation of goodwill for potential impairment during the three months ended March 31, 2004 and determined that goodwill was not impaired. Goodwill is included in non-utility properties and investments-net on the Consolidated Balance Sheets and totaled \$7.5 million (\$6.6 million in the Other business segment and \$0.9 million in Energy Marketing and Resource Management) as of March 31, 2004 and December 31, 2003. The level of goodwill as of March 31, 2004 and December 31, 2003 was supported by the value attributed to the operations acquired.

***Regulatory Deferred Charges and Credits***

The Company prepares its consolidated financial statements in accordance with the provisions of SFAS No. 71, "Accounting for the Effects of Certain Types of Regulation." The Company prepares its financial statements in accordance with SFAS No. 71 because (i) the Company's rates for regulated services are established by or subject to approval by an independent third-party regulator; (ii) the regulated rates are designed to recover the Company's cost of providing the regulated services; and (iii) in view of demand for the regulated services and the level of competition, it is reasonable to assume that rates can be charged to and collected from customers at levels that will recover the Company's costs. SFAS No. 71 requires the Company to reflect the impact of regulatory decisions in its financial statements. SFAS No. 71 requires that certain costs and/or obligations (such as incurred power and natural gas costs not currently recovered through rates, but expected to be recovered in the future) are reflected as deferred charges on the balance sheet. These costs and/or obligations are not reflected in the statement of income until the period during which matching revenues are recognized. If at some point in the future the Company determines that it no longer meets the criteria for continued application of SFAS No. 71 with respect to all or a portion of the Company's regulated operations, the Company could be required to write off its regulatory assets. The Company could also be precluded from the future deferral of costs not recovered through rates at the time such costs were incurred, even if the Company expected to recover such costs in the future.

The Company's primary regulatory assets include power and natural gas deferrals (see "Power Cost Deferrals and Recovery Mechanisms" and "Natural Gas Cost Deferrals and Recovery Mechanisms" below for further information), investment in exchange power, regulatory assets for deferred income taxes, unamortized debt expense, regulatory asset for consolidation of variable interest entity (see Note 2 for further information), demand side management programs, conservation programs and the provision for postretirement benefits. Those items without a specific line on the Consolidated Balance Sheets are included in other regulatory assets.

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Other regulatory assets consisted of the following as of March 31, 2004 and December 31, 2003 (dollars in thousands):

	March 31, 2004	December 31, 2003
Regulatory asset for consolidation of variable interest entity	\$17,322	\$16,707
Regulatory asset for postretirement benefit obligation	4,137	4,255
Demand side management and conservation programs	16,673	19,683
Other	3,297	3,736
Total	<u>\$41,429</u>	<u>\$44,381</u>

Regulatory liabilities include utility plant retirement costs. Deferred credits include, among other items, regulatory liabilities created when the Centralia Power Plant (Centralia) was sold, regulatory liabilities offsetting net energy commodity derivative assets (see Note 5 for further information) and the gain on the general office building sale/leaseback, which is being amortized over the life of the lease, and are included on the Consolidated Balance Sheets as other non-current liabilities and deferred credits.

**Natural Gas Benchmark Mechanism**

The Idaho Public Utilities Commission (IPUC), Washington Utilities and Transportation Commission (WUTC) and Oregon Public Utility Commission (OPUC) approved Avista Utilities' Natural Gas Benchmark Mechanism in 1999. The mechanism eliminated the majority of natural gas procurement operations within Avista Utilities and placed responsibility for natural gas procurement operations with Avista Energy, the Company's non-regulated subsidiary. The ownership of the natural gas assets remains with Avista Utilities; however, the assets are managed by Avista Energy through an Agency Agreement. Avista Utilities has continued to manage natural gas procurement for its California operations, which currently represents approximately four percent of its total natural gas therm sales.

The Natural Gas Benchmark Mechanism provides benefits to retail customers and allows Avista Energy to retain a portion of the benefits associated with asset optimization and the efficiencies gained in purchasing natural gas for Avista Utilities as part of a larger portfolio. In the first quarter of 2002, the IPUC and the OPUC approved the continuation of the Natural Gas Benchmark Mechanism and related Agency Agreement through March 31, 2005. In January 2003, the WUTC approved the continuation of the Natural Gas Benchmark Mechanism and related Agency Agreement through January 29, 2004. In February 2004, the WUTC ordered that the Natural Gas Benchmark Mechanism and related Agency Agreement be terminated for Washington customers and ordered Avista Utilities to file a transition plan to move management of these functions back into Avista Utilities. In April 2004, the WUTC approved Avista Utilities' transition plan, which provides for the movement of these functions back into Avista Utilities to be completed by March 31, 2005. The Company is also planning to move these functions from Avista Energy to Avista Utilities for Idaho and Oregon natural gas customers with the expiration of the current agreements on March 31, 2005.

In accordance with SFAS No. 71, profits recognized by Avista Energy on natural gas sales to Avista Utilities, including gains and losses on natural gas contracts, are not eliminated in the consolidated financial statements. This is due to the fact that Avista Utilities expects to recover the costs of natural gas purchases to serve retail customers and for fuel for electric generation through future retail rates.

**Power Cost Deferrals and Recovery Mechanisms**

Avista Utilities defers the recognition in the income statement of certain power supply costs as approved by the WUTC. Deferred power supply costs are recorded as a deferred charge on the balance sheet for future review and the opportunity for recovery through retail rates. The power supply costs deferred include certain differences between actual power supply costs incurred by Avista Utilities and the costs included in base retail rates. This difference in power supply costs primarily results from changes in short-term wholesale market prices, changes in the level of hydroelectric generation and changes in the level of thermal generation (including changes in fuel prices). Avista Utilities accrues interest on deferred power costs in the Washington jurisdiction at a rate, which is adjusted semi-annually, of 8.5 percent as of March 31, 2004. Total deferred power costs for Washington customers were \$116.5 million and \$125.7 million as of March 31, 2004 and December 31, 2003, respectively.

The WUTC issued an order that became effective July 1, 2002 for restructuring of rate increases previously approved by the WUTC totaling 31.2 percent. The July 2002 rate change increased base retail rates 19.3 percent and provided an 11.9 percent continuing surcharge for the recovery of deferred power costs. The WUTC rate order

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also established an Energy Recovery Mechanism (ERM) effective July 1, 2002. The ERM replaced a series of temporary deferral mechanisms that had been in place in Washington since mid-2000. The ERM allows Avista Utilities to increase or decrease electric rates periodically with WUTC approval to reflect changes in power supply costs. The ERM provides for Avista Utilities to incur the cost of, or receive the benefit from, the first \$9.0 million in annual power supply costs above or below the amount included in base retail rates. Under the ERM, 90 percent of annual power supply costs exceeding or below the initial \$9.0 million are deferred for future surcharge or rebate to Avista Utilities' customers. The remaining 10 percent of power supply costs are an expense of, or benefit to, the Company.

Under the ERM, Avista Utilities makes an annual filing to provide the opportunity for the WUTC and other interested parties to review the prudence of and audit the ERM deferred power cost transactions for the prior calendar year. The settlement agreement establishing the ERM provides for a 90-day review period for the filing; however, the period may be extended by agreement of the parties or by WUTC order. Avista Utilities made its annual filing with the WUTC on April 1, 2004 related to \$22.8 million of deferred power costs incurred for 2003.

Avista Utilities has a power cost adjustment (PCA) mechanism in Idaho that allows it to modify electric rates periodically with IPUC approval. Under the PCA mechanism, Avista Utilities defers 90 percent of the difference between certain actual net power supply expenses and the authorized level of net power supply expenses approved in the last Idaho general rate case. Avista Utilities accrues interest on deferred power costs in the Idaho jurisdiction at a rate, which is adjusted annually, of 1.0 percent on current year deferrals and 3.0 percent on carryover balances as of March 31, 2004. The IPUC originally approved a 19.4 percent surcharge in October 2001, which has been extended through October 2004 for recovery of previously deferred power costs. Based on IPUC staff recommendations and IPUC orders, the prudence of \$11.9 million of deferred power costs will be reviewed in the electric general rate case that Avista Utilities filed in February 2004. Total deferred power costs for Idaho customers were \$28.5 million and \$30.3 million as of March 31, 2004 and December 31, 2003, respectively.

***Natural Gas Cost Deferrals and Recovery Mechanisms***

Under established regulatory practices in each respective state, Avista Utilities is allowed to adjust its natural gas rates periodically (with regulatory approval) to reflect increases or decreases in the cost of natural gas purchased. Differences between actual natural gas costs and the natural gas costs already included in retail rates are deferred and charged or credited to expense when regulators approve inclusion of the cost changes in rates. Total deferred natural gas costs were \$20.8 million and \$15.4 million as of March 31, 2004 and December 31, 2003, respectively.

***Intersegment Eliminations***

Intersegment eliminations represent the transactions between Avista Utilities and Avista Energy for energy commodities and services, primarily natural gas purchased by Avista Utilities under the Agency Agreement.

***Reclassifications***

Certain prior period amounts were reclassified to conform to current statement format. These reclassifications were made for comparative purposes and to conform to changes in accounting standards and have not affected previously reported total net income or stockholders' equity.

**NOTE 2. NEW ACCOUNTING STANDARDS**

In May 2003, the Financial Accounting Standards Board (FASB) issued SFAS No. 150, "Accounting for Certain Financial Instruments with Characteristics of Both Liabilities and Equity." This statement requires the Company to classify certain financial instruments as liabilities that have historically been classified as equity. This statement requires the Company to classify as a liability financial instruments that are subject to mandatory redemption at a specified or determinable date or upon an event that is certain to occur. This statement was effective for financial instruments entered into or modified after May 31, 2003, and otherwise was effective at the beginning of the first interim period beginning after June 15, 2003. The restatement of financial statements for prior periods was not permitted. The adoption of this statement required the Company to classify \$31.5 million of preferred stock subject to mandatory redemption as liabilities on the Consolidated Balance Sheet. The adoption of this statement also required the Company to classify preferred stock dividends subsequent to July 1, 2003 as interest expense in the Consolidated Statements of Income.

In December 2003, the FASB issued SFAS No. 132 (revised 2003), "Employers' Disclosures about Pensions and Other Postretirement Benefits." This statement requires expanded disclosures with respect to pension plan assets, benefit obligations, cash flows, benefit costs and other relevant information. However, this statement does not

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change the measurement and recognition provisions of previous FASB statements related to pensions and other postretirement benefits. The Company was required to adopt this statement as of December 31, 2003. The adoption of this statement did not have any effect on the Company's financial condition or results of operations. The expanded disclosures required by this statement are included in Note 7.

In July 2003, the EITF reached consensus on Issue No. 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. 02-3." This EITF Issue requires that revenues and resource costs from Avista Utilities' settled energy contracts that are "booked out" (not physically delivered) should be reported on a net basis as part of operating revenues effective October 1, 2003. Derivatives not held for trading purposes at Avista Energy are reported gross, unless they are "booked out" or the economic substance indicates that net reporting is appropriate. The adoption of this EITF Issue resulted in a reduction in operating revenues and resource costs of approximately \$2.7 million for 2004 as compared to 2003 for Avista Utilities.

In January 2003, the FASB issued Interpretation No. 46, "Consolidation of Variable Interest Entities," which was revised in December 2003 (collectively referred to as FIN 46). In general, a variable interest entity does not have equity investors with voting rights or it has equity investors that do not provide sufficient financial resources for the entity to support its activities. Variable interest entities are commonly referred to as special purpose entities or off-balance sheet structures; however, FIN 46 applies to a broader group of entities. FIN 46 requires a variable interest entity to be consolidated by the primary beneficiary of that entity. The primary beneficiary is subject to a majority of the risk of loss from the variable interest entity's activities or it is entitled to receive a majority of the entity's residual returns. FIN 46 also requires disclosure of variable interest entities that a company is not required to consolidate but in which it has a significant variable interest. The consolidation requirements of FIN 46 applied immediately to variable interest entities created after January 31, 2003 and applied to certain existing variable interest entities for the first fiscal year or interim period ending after December 15, 2003. Application for all other types of entities was required for periods ending after March 15, 2004.

FIN 46 required the Company to consolidate WP Funding LP effective for the period ended December 31, 2003. WP Funding LP is an entity that was formed in 1993 for the purpose of acquiring the natural gas-fired combustion turbine generating facility in Rathdrum, Idaho (Rathdrum CT). WP Funding LP purchased the Rathdrum CT from the Company with funds provided by unrelated investors of which 97 percent represented debt and 3 percent represented equity. The Company operates the Rathdrum CT and leases it from WP Funding LP. The total amount of WP Funding LP debt outstanding was \$54.6 million as of March 31, 2004 and December 31, 2003. The lease term expires in February 2020; however, the current debt matures in October 2005 and will need to be refinanced at that time. As of March 31, 2004, the book value of the debt and equity of WP Funding LP exceeded the book value of the Rathdrum CT by \$17.3 million. In accordance with regulatory accounting practices, the Company recorded this amount as a regulatory asset upon the consolidation of WP Funding LP. The addition of the Rathdrum CT, which entered commercial operation in 1995, to Avista Utilities' generation resource base was reviewed in previous state regulatory filings with the WUTC and IPUC.

FIN 46 also resulted in the Company no longer including Avista Capital I and Avista Capital II in its consolidated financial statements for the period ended December 31, 2003. Avista Capital I and Avista Capital II are business trusts formed in 1997 for the purpose of issuing a combined \$110.0 million of preferred trust securities to third parties and \$3.4 million of common trust securities to Avista Corp. The sole assets of Avista Capital I and Avista Capital II are \$113.4 million of junior subordinated deferrable interest debentures of Avista Corp. Avista Capital I and Avista Capital II are considered variable interest entities under the provisions of FIN 46. As Avista Corp. is not the primary beneficiary, these entities are no longer included in Avista Corp.'s consolidated financial statements. Interest expense to affiliated trusts of \$1.5 million in the Consolidated Statements of Income for the three months ended March 31, 2004 represents interest expense on the \$113.4 million of long-term debt to affiliated trusts for the first quarter of 2004.

Additionally, the implementation of FIN 46, as revised in December 2003, resulted in the Company including a partnership as well as several low-income housing project investments held in the Other business segment in its consolidated financial statements for the three months ended March 31, 2004. This resulted in an increase in assets of \$7.1 million, long-term debt of \$5.4 million and a charge of \$0.5 million recorded as a cumulative effect of accounting change for the three months ended March 31, 2004.

The Company has evaluated Avista Energy's contracts and relationship with Rathdrum Power, LLC (RP LLC), an entity that is 49 percent owned by Avista Power, and determined that RP LLC should not be consolidated pursuant to

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FIN 46. RP LLC operates a 270 MW natural gas-fired combined cycle combustion turbine plant in northern Idaho (Lancaster Project). All of the output from the Lancaster Project is contracted to Avista Energy through 2026 under a Power Purchase Agreement. As of March 31, 2004, RP LLC had \$117.2 million of debt outstanding that is not included in the consolidated financial statements of the Company. There is no recourse to the Company with respect to this debt.

The adoption of SFAS No. 150 and FIN 46 does not cause the Company to fail to meet any of the covenants of the Company's \$245.0 million committed line of credit, including covenants not to permit the ratio of "consolidated total debt" to "consolidated total capitalization" of Avista Corp. to be greater than 65 percent at the end of any fiscal quarter as the covenant calculations exclude the effect of changes in accounting standards.

**NOTE 3. DISCONTINUED OPERATIONS**

In 2003, total investments of \$12.2 million were made by private equity investors in a new entity, ReliOn, Inc. (formerly AVLB, Inc.), which acquired the assets previously held by Avista Corp.'s fuel cell manufacturing and development subsidiary, Avista Labs. As of March 31, 2004, Avista Corp., through Avista Labs, had an ownership interest of approximately 17.5 percent in ReliOn, Inc., with the opportunity but no further obligation to fund or invest in this business. Avista Corp.'s investment in ReliOn, Inc. is accounted for under the cost method.

**NOTE 4. ACCOUNTS RECEIVABLE SALE**

In 1997, Avista Receivables Corp. (ARC) was formed as a wholly owned, bankruptcy-remote subsidiary of the Company for the purpose of acquiring or purchasing interests in certain accounts receivable, both billed and unbilled, of the Company. On May 29, 2002, ARC, the Company and a third-party financial institution entered into a three-year agreement whereby ARC can sell without recourse, on a revolving basis, up to \$100.0 million of those receivables. In April 2004, the revolving amount available for sale was reduced to \$85.0 million. ARC is obligated to pay fees that approximate the purchaser's cost of issuing commercial paper equal in value to the interests in receivables sold. On a consolidated basis, the amount of such fees is included in operating expenses of the Company. As of March 31, 2004 and December 31, 2003, \$68.0 million and \$72.0 million, respectively, in accounts receivables were sold under this revolving agreement.

**NOTE 5. UTILITY ENERGY COMMODITY DERIVATIVE ASSETS AND LIABILITIES**

SFAS No. 133, as amended by SFAS No. 138 and SFAS No. 149, establishes accounting and reporting standards for derivative instruments, including certain derivative instruments embedded in other contracts, and for hedging activities. It requires the recording of all derivatives as either assets or liabilities on the balance sheet measured at estimated fair value and the recognition of the unrealized gains and losses. In certain defined conditions, a derivative may be specifically designated as a hedge for a particular exposure. The accounting for derivatives depends on the intended use of the derivatives and the resulting designation.

Avista Utilities enters into forward contracts to purchase or sell energy. Under these forward contracts, Avista Utilities commits to purchase or sell a specified amount of energy at a specified time, or during a specified period, in the future. Certain of these forward contracts are considered derivative instruments. Avista Utilities also records derivative commodity assets and liabilities for over-the-counter and exchange-traded derivative instruments as well as certain long-term contracts. These contracts are entered into as part of Avista Utilities' management of its loads and resources as discussed in Note 6. In conjunction with the issuance of SFAS No. 133, the WUTC and the IPUC issued accounting orders authorizing Avista Utilities to offset any derivative assets or liabilities with a regulatory asset or liability. This accounting treatment is intended to defer the recognition of mark-to-market gains and losses on energy commodity transactions until the period of settlement. The order provides for Avista Utilities to not recognize the unrealized gain or loss on utility derivative commodity instruments in the Consolidated Statements of Income. Realized gains or losses are recognized in the period of settlement subject to current or future recovery in retail rates. Realized gains and losses are reflected as adjustments through purchased gas cost adjustments, the ERM and the PCA mechanism.

Prior to the adoption of SFAS No. 149 on July 1, 2003, Avista Utilities elected the normal purchases and sales exception for substantially all of its contracts for both capacity and energy under SFAS No. 133. As such, Avista Utilities was not required to record these contracts as derivative commodity assets and liabilities. Under SFAS No. 149, substantially all new forward contracts to purchase or sell power and natural gas used for generation, which were entered into on or after July 1, 2003, are recorded as assets or liabilities at market value with an offsetting



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regulatory asset or liability. Contracts that are not considered derivatives under SFAS No. 133 are generally accounted for at cost until they are settled or realized, unless there is a decline in the fair value of the contract that is determined to be other than temporary.

As of March 31, 2004, the utility derivative commodity asset balance was \$46.8 million, the derivative commodity liability balance was \$33.9 million and the offsetting net regulatory liability was \$12.9 million. As of December 31, 2003, the utility derivative commodity asset balance was \$39.5 million, the derivative commodity liability balance was \$36.1 million and the offsetting net regulatory liability was \$3.4 million. Utility derivative assets and liabilities, as well as the offsetting net regulatory asset or liability, can change significantly from period to period due to the settlement of contracts, the entering of new contracts and changes in commodity prices. The offsetting net regulatory liability is included in other non-current liabilities and deferred credits on the Consolidated Balance Sheet.

**NOTE 6. ENERGY COMMODITY TRADING**

The Company's energy-related businesses are exposed to risks relating to, but not limited to, changes in certain commodity prices, interest rates, foreign currency and counterparty performance. In order to manage the various risks relating to these exposures, Avista Utilities utilizes derivative instruments, such as forwards, futures, swaps and options, and Avista Energy engages in the trading of such instruments. Avista Utilities and Avista Energy use a variety of techniques to manage risks for their energy resources and wholesale energy market activities. The Company has risk management policies and procedures to manage these risks, both qualitative and quantitative, for Avista Utilities and Avista Energy. The Company's Risk Management Committee, which is separate from the units tasked with managing this risk exposure and is overseen by the Audit Committee of the Company's Board of Directors, monitors compliance with the Company's risk management policies and procedures.

**Avista Utilities**

Avista Utilities engages in an ongoing process of resource optimization, which involves the pursuit of economic resources to serve load obligations and using existing resources to capture available economic value. Avista Utilities sells and purchases wholesale electric capacity and energy to and from utilities and other entities as part of the process of acquiring resources to serve its retail and wholesale load obligations. These transactions range from a term as short as one hour up to long-term contracts that extend beyond one year. Avista Utilities makes continuing projections of (1) future retail and wholesale loads based on, among other things, forward estimates of factors such as customer usage and weather as well as historical data and contract terms and (2) resource availability based on, among other things, estimates of streamflows, generating unit availability, historic and forward market information and experience. On the basis of these continuing projections, Avista Utilities makes purchases and sales of energy on an annual, quarterly, monthly, daily and hourly basis to match expected resources to expected energy requirements. Resource optimization also includes transactions such as purchasing fuel to run thermal generation and, when economic, selling fuel and substituting electric wholesale market purchases for the operation of Avista Utilities' own resources, as well as other wholesale transactions to capture the value of available generation and transmission resources. This optimization process includes entering into financial and physical hedging transactions as a means of managing risks.

Avista Utilities manages the impact of fluctuations in electric energy prices by establishing volume limits for the imbalance between projected loads and resources and through the use of derivative commodity instruments for hedging purposes. Any load/resource imbalances within a rolling 18-month planning horizon are managed within risk policy volumetric limits. Management also assesses available resource decisions and actions that are appropriate for longer-term planning periods. Avista Energy is responsible for the daily management of natural gas supplies to meet the requirements of Avista Utilities' customers in the states of Washington, Idaho and Oregon. In February 2004, the WUTC ordered that these functions be moved back to Avista Utilities for Washington customers, and in April 2004, the WUTC approved Avista Utilities' transition plan to move these functions back into Avista Utilities by March 31, 2005. Avista Utilities is also planning to move these functions for Idaho and Oregon customers with the expiration of current agreements on March 31, 2005. See description of Natural Gas Benchmark Mechanism in Note 1 for further information. Avista Utilities has continued to manage natural gas procurement for its California operations, which currently represents approximately four percent of its total natural gas therm sales.

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**Avista Energy**

Avista Energy is an electricity and natural gas marketing, trading and resource management business. Avista Energy focuses on optimization of combustion turbines and hydroelectric assets owned by other entities, long-term electric supply contracts, natural gas storage, and electric transmission and natural gas transportation arrangements. Avista Energy is also involved in trading electricity and natural gas, including derivative commodity instruments. Avista Energy purchases natural gas and electricity from producers and energy marketing and trading companies. Its customers include commercial and industrial end-users, electric utilities, natural gas distribution companies, and energy marketing and trading companies.

Avista Energy's marketing and energy risk management services are provided through the use of a variety of derivative commodity contracts to purchase or supply natural gas and electric energy at specified delivery points and at specified future dates. Avista Energy trades natural gas and electricity derivative commodity instruments on national exchanges and through other exchanges and brokers, and therefore can experience net open positions in terms of price, volume, and specified delivery point. The open positions expose Avista Energy to the risk that fluctuating market prices may adversely impact its financial condition or results of operations. However, the net open positions are actively managed with strict policies designed to limit the exposure to market risk and requiring daily reporting to management of potential financial exposure.

Avista Energy measures the risk in its electric and natural gas portfolio daily utilizing a Value-at-Risk (VAR) model, which monitors its risk in comparison to established thresholds. VAR measures the expected portfolio loss under hypothetical adverse price movements over a given time interval within a given confidence level. Avista Energy also measures its open positions in terms of volumes at each delivery location for each forward time period. The extent of open positions is included in the risk management policy and is measured with stress tests and VAR modeling.

Derivative commodity instruments sold and purchased by Avista Energy include: forward contracts, which involve physical delivery of an energy commodity; futures contracts, which involve the buying or selling of natural gas or electricity at a fixed price; over-the-counter swap agreements, which require Avista Energy to receive or make payments based on the difference between a specified price and the actual price of the underlying commodity; and options, which mitigate price risk by providing for the right, but not the requirement, to buy or sell energy-related commodities at a fixed price. Foreign currency risks are primarily related to Canadian exchange rates and are managed using standard instruments available in the foreign currency markets.

Avista Energy's derivative commodity instruments accounted for under SFAS No. 133 are subject to mark-to-market accounting, under which changes in the market value of outstanding electric, natural gas and related derivative commodity instruments are recognized as unrealized gains or losses in the period of change. Market prices are utilized in determining the value of the electric, natural gas and related derivative commodity instruments. For electric derivative commodity instruments, these market prices are generally available through two years. For natural gas derivative commodity instruments, these market prices are generally available through three years. For longer-term positions and certain short-term positions for which market prices are not available, a model to estimate forward price curves is utilized. Avista Energy reports the net margin on derivative commodity instruments held for trading as operating revenues. Revenues from contracts, which are not accounted for as derivatives under SFAS No. 133 and derivative commodity instruments not held for trading, are reported on a gross basis in operating revenues. Costs from contracts, which are not accounted for as derivatives under SFAS No. 133 and derivative instruments not held for trading, are reported on a gross basis in resource costs. Contracts in a receivable position, as well as the options held, are reported as assets. Similarly, contracts in a payable position, as well as options written, are reported as liabilities. Net cash flows are recognized in the period of settlement.

Avista Energy implemented hedge accounting in accordance with SFAS No. 133 during the third quarter of 2003. Specific natural gas and electric trading derivative contracts have been designated as hedging instruments in cash flow hedging relationships. The hedge strategies represent cash flow hedges of the variable price risk associated with expected purchases of natural gas and sales of electricity. These designated hedging instruments represent hedges of variable price exposures generated from certain contracts, which do not qualify as derivatives under SFAS No. 133. For all derivatives designated as cash flow hedges, Avista Energy documents the relationship between the hedging instrument and the hedged item (forecasted purchases and sales of power and natural gas), as well as the risk management objective and strategy for using the hedging instrument. Avista Energy assesses whether a change in the value of the designated derivative is highly effective in achieving offsetting cash flows attributable to the hedged item, both at the inception of the hedge and on an ongoing basis. Any changes in the fair value of the designated derivative that are effective are recorded in accumulated other comprehensive income or loss, while changes in fair

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value that are not effective are recognized currently in earnings as operating revenues. Amounts recorded in accumulated other comprehensive income or loss are recognized in earnings during the period that the hedged items are recognized in earnings.

During the three months ended March 31, 2004, a gain of \$0.4 million related to hedge ineffectiveness was recorded in earnings as operating revenues. As of March 31, 2004, there was a gain of \$0.5 million (net of tax) in accumulated other comprehensive income (loss) related to designated cash flow hedges, while a gain of \$0.1 million (net of tax) was reclassified from accumulated comprehensive income (loss) and recognized in earnings during the three months ended March 31, 2004. Of the amount in accumulated other comprehensive income (loss) as of March 31, 2004, Avista Energy expects to recognize a loss of \$0.4 million in earnings during the next 12 months. The actual amounts that will be recognized in earnings during the next 12 months will vary from the expected amounts as a result of changes in market prices. The maximum term of the designated hedging instruments was 33 months.

**Contract Amounts and Terms** Under Avista Energy's derivative instruments, Avista Energy either (i) as "fixed price payor," is obligated to pay a fixed price or a fixed amount and is entitled to receive the commodity or a fixed amount or (ii) as "fixed price receiver," is entitled to receive a fixed price or a fixed amount and is obligated to deliver the commodity or pay a fixed amount or (iii) as "index price payor," is obligated to pay an indexed price or an indexed amount and is entitled to receive the commodity or a variable amount or (iv) as "index price receiver," is entitled to receive an indexed price or amount and is obligated to deliver the commodity or pay a variable amount.

The contract or notional amounts and terms of Avista Energy's derivative commodity instruments outstanding as of March 31, 2004 are set forth below (in thousands of mMBTUs and MWhs):

	Fixed Price Payor	Fixed Price Receiver	Maximum Terms in Years	Index Price Payor	Index Price Receiver	Maximum Terms in Years
Energy commodities (volumes)						
Electric	41,074	41,622	13	205	452	1
Natural gas	193,537	188,186	2	1,217,327	1,212,361	3

The weighted average term of Avista Energy's electric derivative commodity instruments as of March 31, 2004 was approximately 8 months. The weighted average term of Avista Energy's natural gas derivative commodity instruments as of March 31, 2004 was approximately 5 months.

**Estimated Fair Value** The estimated fair value of Avista Energy's derivative commodity instruments outstanding as of March 31, 2004, and the average estimated fair value of those instruments held during the three months ended March 31, 2004, are set forth below (dollars in thousands):

	Estimated Fair Value as of March 31, 2004				Average Estimated Fair Value for the three months ended March 31, 2004			
	Current Assets	Long-term Assets	Current Liabilities	Long-term Liabilities	Current Assets	Long-term Assets	Current Liabilities	Long-term Liabilities
Electric	\$167,626	\$226,947	\$147,260	\$186,770	\$144,204	\$223,219	\$123,059	\$183,723
Natural gas	106,370	19,013	97,683	10,115	90,159	17,841	80,505	8,725
Total	\$273,996	\$245,960	\$244,943	\$196,885	\$234,363	\$241,060	\$203,564	\$192,448

The change in the estimated fair value position of Avista Energy's energy commodity portfolio, net of reserves for credit and market risk for three months ended March 31, 2004 was an unrealized gain of \$6.6 million and is included in the Consolidated Statements of Income in operating revenues. The change in the fair value position for the three months ended March 31, 2003 was an unrealized gain of \$12.4 million.

**NOTE 7. PENSION PLANS AND OTHER POSTRETIREMENT BENEFIT PLANS**

The Company has a defined benefit pension plan covering substantially all of its regular full-time employees. Employees of Avista Energy also participate in this plan. Individual benefits under this plan are based upon years of service and the employee's average compensation as specified in the plan. The Company's funding policy is to contribute amounts that are not less than the minimum amounts required to be funded under the Employee Retirement Income Security Act, nor more than the maximum amounts that are currently deductible for income tax purposes. The Company made \$12 million in cash contributions to the pension plan in 2003. The Company expects

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to contribute approximately \$15 million to the pension plan in 2004 (\$3.75 million was contributed during the three months ended March 31, 2004).

The Company provides certain health care and life insurance benefits for substantially all of its retired employees. The Company accrues the estimated cost of postretirement benefit obligations during the years that employees provide services.

The Company uses a December 31 measurement date for its pension and postretirement plans. The following table sets forth the components of net periodic benefit costs for the three months ended March 31 (dollars in thousands):

	Pension Benefits		Post-retirement Benefits	
	2004	2003	2004	2003
Service cost	\$ 2,025	\$ 1,951	\$ 125	\$ 121
Interest cost	4,162	3,926	620	619
Expected return on plan assets	(3,425)	(2,716)	(300)	(211)
Transition (asset)/obligation recognition	(275)	(271)	250	245
Amortization of prior service cost	100	164	—	—
Net (gain) loss recognition	1,138	974	205	(104)
Net periodic benefit cost	<u>\$ 3,725</u>	<u>\$ 4,028</u>	<u>\$ 900</u>	<u>\$ 670</u>

**NOTE 8. LONG-TERM DEBT**

The following details the interest rate and maturity dates of long-term debt outstanding as of March 31, 2004 and December 31, 2003 (dollars in thousands):

Maturity Year	Description	Interest Rate	March 31, 2004	December 31, 2003
2005	Secured Medium-Term Notes	6.39%-6.68%	\$ 29,500	\$ 29,500
2005	WP Funding LP Note	8.36%	54,572	54,572
2006	Secured Medium-Term Notes	7.89%-7.90%	30,000	30,000
2007	First Mortgage Bonds	7.75%	150,000	150,000
2008	Secured Medium-Term Notes	6.89%-6.95%	20,000	20,000
2010	Secured Medium-Term Notes	6.67%-6.90%	10,000	10,000
2012	Secured Medium-Term Notes	7.37%	7,000	7,000
2013	First Mortgage Bonds	6.13%	45,000	45,000
2018	Secured Medium-Term Notes	7.26%-7.45%	27,500	27,500
2023	Secured Medium-Term Notes	7.18%-7.54%	24,500	24,500
	Total secured long-term debt		<u>398,072</u>	<u>398,072</u>
2004	Unsecured Medium-Term Notes	7.42%	28,500	28,500
2006	Unsecured Medium-Term Notes	8.14%	8,000	8,000
2007	Unsecured Medium-Term Notes	5.99%-7.94%	25,850	25,850
2008	Senior Notes	9.75%	317,118	317,683
2008	Unsecured Medium-Term Notes	6.06%	25,000	25,000
2010	Unsecured Medium-Term Notes	8.02%	25,000	25,000
2022	Unsecured Medium-Term Notes	8.15%-8.23%	5,000	5,000
2023	Unsecured Medium-Term Notes	7.99%	5,000	5,000
2023	Pollution Control Bonds	6.00%	4,100	4,100
2028	Unsecured Medium-Term Notes	6.37%-6.88%	25,000	25,000
2032	Pollution Control Bonds	5.00%	66,700	66,700
2034	Pollution Control Bonds	5.13%	17,000	17,000
	Total unsecured long-term debt		<u>552,268</u>	<u>552,833</u>
	Other long-term debt and capital leases		<u>12,256</u>	<u>5,812</u>
	Unamortized debt discount		<u>(1,774)</u>	<u>(1,994)</u>
	Total		<u>960,822</u>	<u>954,723</u>
	Current portion of long-term debt		<u>(29,899)</u>	<u>(29,711)</u>
	Total long-term debt		<u>\$930,923</u>	<u>\$925,012</u>

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**NOTE 9. LONG-TERM DEBT TO AFFILIATED TRUSTS**

In April 2004, the Company issued Junior Subordinated Debt Securities, with a principal amount of \$61.9 million to AVA Capital Trust III, a business trust. Concurrently, AVA Capital Trust III issued \$60.0 million of Preferred Trust Securities to third parties and \$1.9 million of Common Trust Securities to the Company. All of these securities have a fixed interest rate of 6.50 percent for five years (through March 31, 2009). Subsequent to the initial five-year fixed rate period, the securities will either have a new fixed rate or an adjustable rate. These debt securities may be redeemed by the Company on or after March 31, 2009 and will mature on April 1, 2034.

The Company used the proceeds from the Junior Subordinated Debt Securities to redeem \$61.9 million of 7.875 percent Junior Subordinated Deferrable Interest Debentures, Series A, originally issued in 1997 to Avista Capital I, a business trust. Avista Capital I used these proceeds to redeem \$60.0 million of Preferred Trust Securities issued to third parties and \$1.9 million of Common Trust Securities issued to the Company.

In 1997, the Company issued Floating Rate Junior Subordinated Deferrable Interest Debentures, Series B, with a principal amount of \$51.5 million to Avista Capital II, a business trust. Avista Capital II issued \$50.0 million of Preferred Trust Securities with a floating distribution rate of LIBOR plus 0.875 percent, calculated and reset quarterly. Concurrent with the issuance of the Preferred Trust Securities, Avista Capital II issued \$1.5 million of Common Trust Securities to the Company. These debt securities may be redeemed at the option of Avista Capital II on or after June 1, 2007 and mature on June 1, 2037; however, this is limited by an agreement under the Company's 9.75 percent Senior Notes that mature in 2008. In December 2000, the Company purchased \$10.0 million of these Preferred Trust Securities.

The Company has guaranteed the payment of distributions on, and redemption price and liquidation amount with respect to, the Preferred Trust Securities to the extent that AVA Capital Trust III and Avista Capital II have funds available for such payments from the respective debt securities. Upon maturity or prior redemption of such debt securities, the Preferred Trust Securities will be mandatorily redeemed. As discussed in Note 2, FIN 46 results in the Company no longer including these capital trusts in its consolidated financial statements as of December 31, 2003.

**NOTE 10. SHORT-TERM BORROWINGS**

As of March 31, 2004, the Company maintained a committed line of credit with various banks in the amount of \$245.0 million with an expiration date of May 11, 2004. As of March 31, 2004, the Company could request the issuance of up to \$75.0 million in letters of credit under the committed line of credit. As of March 31, 2004 and December 31, 2003, the Company had \$55.0 million and \$80.0 million, respectively, of borrowings outstanding under this committed line of credit. As of March 31, 2004 and December 31, 2003, there were \$8.4 million and \$10.7 million in letters of credit outstanding, respectively. As of March 31, 2004, the committed line of credit was secured by \$245.0 million of non-transferable first mortgage bonds of the Company issued to the agent bank. Such first mortgage bonds would only become due and payable in the event, and then only to the extent, that the Company defaults on its obligations under the committed line of credit.

The committed line of credit agreement contains customary covenants and default provisions, including covenants not to permit the ratio of "consolidated total debt" (not including preferred stock, long-term debt to affiliated trusts, WP Funding LP debt or other long-term debt included in the consolidated financial statements as a result of the implementation of FIN 46) to "consolidated total capitalization" of Avista Corp. to be greater than 65 percent at the end of any fiscal quarter. As of March 31, 2004, the Company was in compliance with this covenant with a ratio of 52.5 percent. The committed line of credit also has a covenant requiring the ratio of "earnings before interest, taxes, depreciation and amortization" to "interest expense" of Avista Utilities for the twelve-month period ending March 31, 2004 to be greater than 1.6 to 1. As of March 31, 2004, the Company was in compliance with this covenant with a ratio of 2.3 to 1.

On May 6, 2004, the Company's committed line of credit was amended to increase the available amount to \$350.0 million (secured by non-transferable first mortgage bonds) and extend the expiration date to May 5, 2005. The amount available for the issuance of letters of credit was increased to \$125.0 million. The increase in the committed line of credit is necessary due to seasonal credit requirements anticipated as natural gas procurement functions are moved from Avista Energy to Avista Utilities. Also, the covenant requirement for the ratio of "consolidated total debt" to "consolidated total capitalization" was increased to 70 percent and includes all debt.

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On July 25, 2003, Avista Energy and its subsidiary, Avista Energy Canada, Ltd., as co-borrowers, entered into a committed credit agreement with a group of banks in the aggregate amount of \$110.0 million expiring July 23, 2004. This committed credit facility provides for the issuance of letters of credit to secure contractual obligations to counterparties. This facility is guaranteed by Avista Capital and secured by Avista Energy's assets. The maximum amount of credit extended by the banks for the issuance of letters of credit is the subscribed amount of the facility less the amount of outstanding cash advances, if any. The maximum amount of credit extended by the banks for cash advances is \$30.0 million. No cash advances were outstanding as of March 31, 2004 and December 31, 2003. Letters of credit in the aggregate amount of \$20.5 million and \$15.0 million were outstanding as of March 31, 2004 and December 31, 2003, respectively. The cash deposits of Avista Energy at the respective banks collateralize these letters of credit, which is reflected as restricted cash on the Consolidated Balance Sheet.

The Avista Energy credit agreement contains customary covenants and default provisions, including covenants to maintain "minimum net working capital" and "minimum net worth," as well as a covenant limiting the amount of indebtedness that the co-borrowers may incur. The credit agreement also contains covenants and other restrictions related to Avista Energy's trading limits and positions, including VAR limits, restrictions with respect to changes in risk management policies or volumetric limits, and limits on exposure related to hourly and daily trading of electricity. Also, a reduction in the credit rating of Avista Corp. would represent an event of default under Avista Energy's credit agreement. These covenants, certain counterparty agreements and current market liquidity conditions result in Avista Energy maintaining certain levels of cash and therefore effectively limit the amount of cash dividends that are available for distribution to Avista Capital and ultimately to Avista Corp. Avista Energy was in compliance with the covenants of its credit agreement as of March 31, 2004.

Avista Energy is currently negotiating a renewal of its credit facility and anticipates it will be in place by the July 23, 2004 expiration date of the current credit agreement.

**NOTE 11. INTEREST RATE SWAP AGREEMENTS**

RP LLC has entered into two interest rate swap agreements, maturing in 2006, to manage the risk that changes in interest rates may affect the amount of future interest payments. RP LLC agreed to pay fixed rates of interest with the differential paid or received under the interest rate swap agreements recognized as an adjustment to interest expense. These interest rate swap agreements are considered hedges against fluctuations in future cash flows associated with changes in interest rates in accordance with SFAS No. 133. The fair value of the interest rate swap agreements was determined by reference to market values obtained from various third party sources. Avista Power's 49 percent ownership interest in RP LLC is accounted for under the equity method of accounting. As of March 31, 2004, there was an unrealized loss of \$1.0 million included in accumulated other comprehensive loss on the Consolidated Balance Sheet.

**NOTE 12. EARNINGS PER COMMON SHARE**

The following table presents the computation of basic and diluted earnings per common share for the three months ended March 31 (in thousands, except per share amounts):

	<u>2004</u>	<u>2003</u>
<b>Numerator:</b>		
Income from continuing operations	\$12,684	\$18,442
Loss from discontinued operations	—	(1,120)
Net income before cumulative effect of accounting change	12,684	17,322
Cumulative effect of accounting change	(460)	(1,190)
Net income	12,224	16,132
Deduct: Preferred stock dividend requirements	—	578
Income available for common stock	<u>\$12,224</u>	<u>\$15,554</u>
<b>Denominator:</b>		
Weighted-average number of common shares outstanding-basic	48,352	48,100
Effect of dilutive securities:		
Contingent stock	386	—
Stock options	300	19
Weighted-average number of common shares outstanding-diluted	<u>49,038</u>	<u>48,119</u>

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	2004	2003
<b>Earnings per common share, basic and diluted:</b>		
Earnings per common share from continuing operations	\$ 0.26	\$ 0.37
Loss per common share from discontinued operations	—	(0.02)
Earnings per common share before cumulative effect of accounting change	0.26	0.35
Loss per common share from cumulative effect of accounting change	(0.01)	(0.03)
Total earnings per common share, basic and diluted	<u>\$ 0.25</u>	<u>\$ 0.32</u>

**NOTE 13. COMMITMENTS AND CONTINGENCIES**

The Company believes, based on the information presently known, that the ultimate liability for the matters discussed in this Note, individually or in the aggregate, taking into account established accruals for estimated liabilities, will not be material to the consolidated financial condition of the Company, but could be material to results of operations or cash flows for a particular quarter or annual period. No assurance can be given, however, as to the ultimate outcome with respect to any particular issue.

**Federal Energy Regulatory Commission Inquiry**

On April 19, 2004, the Federal Energy Regulatory Commission (FERC) issued an order approving the contested Agreement in Resolution of Section 206 Proceeding (Agreement in Resolution) reached by Avista Corp. doing business as Avista Utilities, Avista Energy and the FERC's Trial Staff with respect to an investigation into the activities of Avista Utilities and Avista Energy in western energy markets during 2000 and 2001. In the Agreement in Resolution, the FERC Trial Staff stated that its investigation found: (1) no evidence that any executives or employees of Avista Utilities or Avista Energy knowingly engaged in or facilitated any improper trading strategy; (2) no evidence that Avista Utilities or Avista Energy engaged in any efforts to manipulate the western energy markets during 2000 and 2001; and (3) that Avista Utilities and Avista Energy did not withhold relevant information from the FERC's inquiry into the western energy markets for 2000 and 2001. As part of the Agreement in Resolution, Avista Utilities has agreed to improve its system of taping energy trading conversations and improve its account settlement process. Avista Utilities and Avista Energy have agreed to maintain an annual training program on the applicable FERC Code of Conduct for all employees engaged in the trading of electric energy and capacity. Under the Agreement in Resolution, no remedial measures were taken against Avista Utilities or Avista Energy and there was no imposition of monetary remedies or assessment of penalties, or relinquishment or modification of market-based rate authority. Parties have 30 days from the FERC order date (April 19, 2004) to file a request for rehearing. See the 2003 Form 10-K for a history of the FERC Inquiry.

**U.S. Commodity Futures Trading Commission (CFTC) Subpoena**

Beginning in June 2002, the CFTC issued several subpoenas directing Avista Corp. and Avista Energy to produce certain materials and make employees available to be interviewed. The inquiries related to whether electricity and natural gas trades by Avista Corp. and Avista Energy involved "round trip trades," "wash trades," or "sell/buyback trades" and whether Avista Corp. and Avista Energy properly reported trading prices to publishers of power and natural gas indices. While the CFTC always reserves the right to reopen its investigation, the CFTC provided written notification to Avista Corp. and Avista Energy on January 29, 2004 that it has determined to close the investigation.

**Class Action Securities Litigation**

On September 27, 2002, Ronald R. Wambolt filed a class action lawsuit in the United States District Court for the Eastern District of Washington against Avista Corp., Thomas M. Matthews, the former Chairman of the Board, President and Chief Executive Officer of the Company, Gary G. Ely, the current Chairman of the Board, President and Chief Executive Officer of the Company, and Jon E. Eliassen, the former Senior Vice President and Chief Financial Officer of the Company. In October and November 2002, Gail West, Michael Atlas and Peter Arnone filed similar class action lawsuits in the same court against the same parties. On February 3, 2003, the court issued an order consolidating the complaints under the name "In re Avista Corp. Securities Litigation," and on February 7, 2003 appointed the lead plaintiff and co-lead counsel. On August 19, 2003, the plaintiffs filed their consolidated amended class action complaint in the same court against the same parties. In their complaint, the plaintiffs continue to assert violations of the federal securities laws in connection with alleged misstatements and omissions of material fact pursuant to Sections 10(b) and 20(a) of the Securities Exchange Act of 1934. The plaintiffs allege that the

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Company did not have adequate risk management processes, procedures and controls. The plaintiffs further allege that the Company engaged in unlawful energy trading practices and allegedly manipulated western power markets. The plaintiffs assert that alleged misstatements and omissions have occurred in the Company's filings with the Securities and Exchange Commission and other information made publicly available by the Company, including press releases. The class action complaint asserts claims on behalf of all persons who purchased, converted, exchanged or otherwise acquired the Company's common stock during the period between November 23, 1999 and August 13, 2002. The Company filed a motion to dismiss this complaint in October 2003 and the plaintiffs filed an answer to this motion in January 2004. Arguments before the Court on the motion were held on March 19, 2004. On April 15, 2004, the Court called for additional briefing on what effect, if any, the FERC proceedings (see "Federal Energy Regulatory Commission Inquiry" above) have on this case. The Company intends to vigorously defend against this lawsuit.

### **California Energy Markets**

In April 2002, several subsidiaries of Reliant Energy, Inc. (Reliant) and Duke Energy Corporation (Duke) filed cross-complaints against Avista Energy and numerous other participants in the California energy markets. The cross-complaints seek indemnification for any liability that may arise from original complaints filed against Reliant and Duke with respect to charges of unlawful and unfair business practices in the California energy markets under California law. In June 2002, Avista Energy filed motions to dismiss the cross-complaints. In the meantime, the U.S. District Court remanded the case to California State Court, which remand is itself the subject of an appeal to the United States Court of Appeals for the Ninth Circuit.

In March 2002, the Attorney General of the State of California (California AG) filed a complaint with the FERC against certain specific companies (not including Avista Corp. or its subsidiaries) and "all other public utility sellers" in California. The complaint alleges that sellers with market-based rates have violated their tariffs by not filing with the FERC transaction-specific information about all of their sales and purchases at market-based rates. As a result, the California AG contends that all past sales should be subject to refund if found to be above just and reasonable levels. In May 2002, the FERC issued an order denying the claim to issue refunds. In July 2002, the California AG requested a rehearing on the FERC order, which request was denied in September 2002. The California AG filed a Petition for Review of the FERC's decision with the United States Court of Appeals for the Ninth Circuit and awaits decision.

### **Port of Seattle Complaint**

On May 21, 2003, the Port of Seattle filed a complaint in the United States District Court for the Western District of Washington against numerous companies, including Avista Corp., Avista Energy and Avista Power. The complaint seeks compensatory and treble damages for alleged violations of the Sherman Act and the Racketeer Influenced and Corrupt Organization Act by transmitting, via wire communications, false information intended to increase the price of power, knowing that others would rely upon such information. The complaint alleges that the defendants and others knowingly devised and attempted to devise a scheme to defraud and to obtain money and property from electricity customers throughout the WECC, by means of false and fraudulent pretenses, representations and promises. The alleged purpose of the scheme was to artificially increase the price that the defendants received for their electricity and ancillary services, to receive payments for services they did not provide and to manipulate the price of electricity throughout the WECC. In August 2003, the Company filed a motion to dismiss this complaint. A transfer order has been granted, which moves this case to the United States District Court for the Southern District of California to consolidate it with other pending actions. Arguments with respect to the motions to dismiss filed by the Company and other defendants were held on March 26, 2004.

### **Wah Chang Complaint**

On May 5, 2004, Wah Chang, a division of TDY Industries, Inc., filed a complaint in the United States District Court for the District of Oregon against numerous companies, including Avista Corp., Avista Energy and Avista Power. The complaint seeks compensatory and treble damages for alleged violations of the Sherman Act, the Racketeer Influenced and Corrupt Organization Act, as well as violations of Oregon state law. From September 1997 to September 2002, the plaintiff purchased electricity from PacifiCorp pursuant to a contract that was indexed to the spot wholesale market price of electricity. The plaintiff alleges that the defendants transmitted, via wire communications, false and fraudulent information in interstate commerce. The plaintiff also alleges that the defendants engaged in numerous practices involving the generation, purchase, sale, exchange, scheduling and/or transmission of electricity with the effect of artificially and illegally fixing and raising the price of electricity in California and throughout the Pacific Northwest. As a result of the defendants' alleged conduct, the plaintiff allegedly suffered damages of not less than \$30 million through the payment of higher electricity prices.

### **State of Montana Proceedings**

On June 30, 2003, the Attorney General of the State of Montana (Montana AG) filed a complaint in the Montana District Court on behalf of the people of Montana and the Flathead Electric Cooperative, Inc. against numerous companies, including Avista Corp. The complaint alleges that the companies illegally manipulated western electric and natural gas markets in 2000 and 2001. This case was subsequently moved to the United States District Court for the District of Montana; however, it has since been remanded back to the Montana District Court.

The Montana AG also petitioned the Montana Public Service Commission (MPSC) to fine public utilities \$1,000 a day for each day it finds they engaged in alleged "deceptive, fraudulent, anticompetitive or abusive practices" and order refunds when consumers were forced to pay more than just and reasonable rates. On February 12, 2004, the



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MPSC issued an order initiating investigation of the Montana retail electricity market for the purpose of determining whether there is evidence of unlawful manipulation of that market.

### **Montana Public School Trust Fund Lawsuit**

On October 20, 2003, Richard Dolan and Denise Hayman filed a lawsuit in the United States District Court for the District of Montana against all private owners of hydroelectric dams in Montana, including Avista Corp. The lawsuit alleges that the hydroelectric facilities are located on state-owned riverbeds and the owners have never paid compensation to the state's public school trust fund. The lawsuit requests lease payments dating back to the construction of the respective dams and also requests damages for trespassing and unjust enrichment. An Amended Complaint adding Great Falls Elementary School District No. 1 and Great Falls High School District 1A was filed on January 16, 2004. On February 2, 2004, the Company filed its motion to dismiss this lawsuit; PacifiCorp and PPL Montana, as the other named defendants also filed a motion to dismiss, or joined therein. The Montana AG has indicated that it intends to file a complaint on behalf of the state in the pending action to allegedly protect and preserve the state lands/school trust lands from use without compensation.

### **Montana Energy Security Act Initiative**

In April 2004, the Montana Secretary of State certified that it had approved the form of a proposed initiative to create a governor-appointed board that would have the power to purchase at fair market value, operate or sell electric and natural gas facilities encompassing all elements of generation, transmission, distribution and energy marketing, and to sell electricity and natural gas at retail and wholesale. In the November 2002 General Election, a similar initiative, which only included hydroelectric assets, was rejected with 68 percent of the vote. The Company's Noxon Rapids Hydroelectric Generating Station (Noxon Rapids) (527 MW) is located in Montana on the Clark Fork River. Avista Utilities also owns a 15 percent interest in a twin-unit, coal-fired generating facility, the Colstrip 3 & 4 Generating Project (Colstrip) (the Company's share is 222 MW) in southeastern Montana. Additionally, the Company owns electric transmission, both solely and through joint interests, located in Montana.

The proposal is being presented as a ballot initiative, which allows for the enactment of law through public vote without legislative approval. The supporters of the initiative need to gather the necessary signatures by June 18, 2004. If this is accomplished, the initiative will be presented to the public in the November 2004 General Election and will require a majority vote to become law. The Company is opposing this initiative and intends to legally defend itself against the acquisition of its Montana assets. The Company is unable to predict whether or not the proposed initiative will obtain the necessary signatures and if it does, whether or not the initiative would pass in the November 2004 election. Further, the Company is not able to predict whether any legal challenge would be successful.

### **State of Washington Business and Occupation Tax**

In December 2003, Avista Energy and the Washington Department of Revenue reached a settlement in principle with respect to a final resolution of a business and occupational tax matter within the amount that Avista Energy had previously accrued for this matter. The settlement in principle was finalized and completed in March 2004 with no impact on the results of operations for the three months ended March 31, 2004. See the 2003 Form 10-K for a history of this matter.

### **Colstrip Generating Project Complaint**

In May 2003, various parties (all of which are residents or businesses of Colstrip, Montana) filed a consolidated complaint against the owners of Colstrip in Montana District Court. Avista Corp. owns a 15 percent interest in Colstrip. The plaintiffs allege damages to buildings as a result of rising ground water, as well as damages from contaminated waters leaking from the lakes and ponds of Colstrip. The plaintiffs are seeking punitive damages, an order by the court to remove the lakes and ponds and the forfeiture of all profits earned from the generation of Colstrip. The Company intends to work with the other owners of Colstrip in defense of this complaint.

### **Hamilton Street Bridge Site**

A portion of the Hamilton Street Bridge Site in Spokane, Washington (including a former coal gasification plant site that operated for approximately 60 years until 1948) was acquired by the Company through a merger in 1958. The

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Company no longer owns the property. In January 1999, the Company received notice from the State of Washington's Department of Ecology (DOE) that it had been designated as a potentially liable party (PLP) with respect to any hazardous substances located on this site, stemming from the Company's past ownership of the former gas plant site. In its notice, the DOE stated that it intended to complete an on-going remedial investigation of this site, complete a feasibility study to determine the most effective means of halting or controlling future releases of substances from the site, and to implement appropriate remedial measures. The Company responded to the DOE acknowledging its listing as a PLP, but requested that additional parties also be listed as PLPs. In the spring of 1999, the DOE named two other parties as additional PLPs.

The DOE, the Company and another PLP, Burlington Northern & Santa Fe Railway Co. (BNSF) signed an Agreed Order in March 2000 that provided for the completion of a remedial investigation and a feasibility study. The work to be performed under the Agreed Order includes three major technical parts: completion of the remedial investigation; performance of a focused feasibility study; and implementation of an interim groundwater monitoring plan. During the second quarter of 2000, the Company received comments from the DOE on its initial remedial investigation, and then submitted another draft of the remedial investigation, which was accepted as final by the DOE. After responding to comments from the DOE, the feasibility study was accepted by the DOE during the fourth quarter of 2000. After receiving input from the Company and the other PLPs, the final Cleanup Action Plan (CAP) was issued by the DOE in August 2001. In September 2001, the DOE issued an initial draft Consent Decree for the PLPs to review. During the first quarter of 2002, the Company and BNSF signed a cost sharing agreement. In September 2002, the Company, BNSF and the DOE finalized the Consent Decree to implement the CAP. The third PLP has indicated it will not sign the Consent Decree. It is currently estimated that the Company's share of the costs will be less than \$1.0 million. The Engineering and Design Report for the CAP was submitted to the DOE in January 2003 and approved by the DOE in May 2003. Work under the CAP commenced during the second quarter of 2003. Negotiations are continuing with the third PLP with respect to the logistics of the CAP.

### **Spokane River**

In March 2001, the DOE informed Avista Development, a subsidiary of Avista Capital, of a health advisory concerning PCBs found in fish caught in a portion of the Spokane River. In June 2001, Avista Development received official notice that it had been designated as a PLP with respect to contaminated sites on the Spokane River. The DOE discovered PCBs in fish and sediments in the Spokane River in the 1970s and 1980s. In the 1990s, the DOE performed subsequent sampling of the river and identified potential sources of the PCBs, including the Spokane Industrial Park (SIP) and a number of other entities in the area. The SIP, renamed Pentzer Development Corporation (Pentzer Development) in 1990, operated a wastewater treatment plant at the site until it was closed in December 1993. The SIP's treatment plant discharged to the Spokane River under the terms of a National Pollutant Discharge Elimination System permit issued by the DOE. Pentzer Development sold the property in 1996 and merged with Avista Development in 1998. Avista Development filed a response to this notice in August 2001. In December 2001, the DOE confirmed Avista Development's status as a PLP and named at least two other PLPs in this matter. In April 2003, the DOE released its study of wastewater and sludge handling from facilities owned by a fourth PLP. The DOE study indicated that the fourth PLP continued to discharge PCBs into the Spokane River. The DOE issued the fourth PLP a final notice of participation as a PLP on April 30, 2003.

During the fourth quarter of 2002, Avista Development and one other PLP, Kaiser Aluminum & Chemical Corporation (Kaiser), finalized the Consent Decree and Scope of Work for the remedial investigation and feasibility study of the site, which was formally entered into Spokane County Superior Court in January 2003. The other PLPs have not been participating in the process. As directed by Avista Development and Kaiser, the field work for the remedial investigation began in April 2003 and was completed by the end of 2003 with a draft remedial investigation report and feasibility study technical memorandum submitted to the DOE in March 2004. Kaiser has filed for bankruptcy and is expected to file its reorganization plan in mid-2004. Kaiser has initiated negotiations with the DOE and Avista Development to settle its future financial liabilities associated with the site. The DOE has indicated that the actual cleanup of PCB sediments in the Spokane River will be coordinated to the extent possible with the EPA's separate plan to remove heavy metals from the Spokane River. The Company believes that the heavy metals contamination resulted from decades of mining upstream at locations in Idaho and is not related to the activities of Avista Development or Avista Corp.

### **Lake Coeur d'Alene**

In July 1998, the United States District Court for the District of Idaho issued its finding that the Coeur d'Alene Tribe of Idaho (Tribe) owns, among other things, portions of the bed and banks of Lake Coeur d'Alene (Lake) lying within

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the current boundaries of the Coeur d'Alene Reservation. This action had been brought by the United States on behalf of the Tribe against the State of Idaho. The Company was not a party to this action. The United States District Court decision was affirmed by the United States Court of Appeals for the Ninth Circuit. The United States Supreme Court affirmed this decision in June 2001. This will result in, among other things, the Company being liable to the Tribe for compensation for the use of reservation lands under Section 10(e) of the Federal Power Act.

The Company's Post Falls Hydroelectric Generating Station (Post Falls), a facility constructed in 1906 with a present capability of 18 MW, utilizes a dam on the Spokane River downstream of the Lake which controls the water level in the Lake for portions of the year (including portions of the lakebed owned by the Tribe). The Company has other hydroelectric facilities on the Spokane River downstream of Post Falls, but these facilities do not affect the water level in the Lake. The Company and the Tribe are engaged in discussions with respect to past and future compensation (which may include interest) for use of the portions of the bed and banks of the Lake, which are owned by the Tribe. If the parties cannot agree on the amount of compensation, the matter could result in litigation. The Company cannot predict the amount of compensation that it will ultimately pay or the terms of such payment. However, the Company intends to seek recovery of any amounts paid through the rate making process.

**Spokane River Relicensing**

The Company operates six hydroelectric plants on the Spokane River, and five of these (Long Lake, Nine Mile, Upper Falls, Monroe Street and Post Falls) are under one FERC license and referred to herein as the Spokane River Project. The sixth, Little Falls, is operated under separate Congressional authority and is not licensed by the FERC. The license for the Spokane River Project expires in August 2007; the Company filed a Notice of Intent to Relicense in July 2002. The formal consultation process involving planning and information gathering with stakeholder groups is underway. The Company's goal is to develop with the stakeholders a comprehensive and cost-effective settlement agreement to be filed as part of the Company's license application to the FERC in July 2005.

**Clark Fork Settlement Agreement**

Dissolved gas levels exceed Idaho and federal water quality standards downstream of the Cabinet Gorge Hydroelectric Generating Project (Cabinet Gorge) during periods when excess river flows must be diverted over the spillway. Mitigation of the dissolved gas levels continues to be studied as agreed to in the Clark Fork Settlement Agreement. Under the terms of the Clark Fork Settlement Agreement, the Company developed an abatement and mitigation strategy with the other signatories to the agreement and submitted the plan in December 2002 for review and approval to the Idaho Department of Environmental Quality (DEQ) and the U.S. Fish and Wildlife Service. In February 2004, the Idaho DEQ and the U.S. Fish and Wildlife Service approved the Company's plan. The structural alternative proposed by the Company provides for the modification of the two existing diversion tunnels built when Cabinet Gorge was originally constructed. The costs of modifications to the first tunnel are currently estimated to be \$37 million (including AFUDC and inflation) and would be incurred between 2004 and 2009. The second tunnel would be modified only after evaluation of the performance of the first tunnel and such modifications would commence no later than 10 years following the completion of the first tunnel. It is currently estimated that the costs to modify the second tunnel would be \$23 million (including AFUDC and inflation). As part of the plan, the Company will also provide \$0.5 million annually commencing as early as 2004, as mitigation for aquatic resources that might be adversely affected by high dissolved gas levels. Mitigation funds will continue until the modification of the second tunnel commences or if the second tunnel is not modified to an agreed upon point in time commensurate with the biological effects of high dissolved gas levels. The Company will seek regulatory recovery of the costs for the modification of Cabinet Gorge and the mitigation payments.

The operating license for the Clark Fork Project describes the approach to restore bull trout populations in the project areas. Using the concept of adaptive management and working closely with the U.S. Fish and Wildlife Service, the Company is evaluating the feasibility of fish passage. The results of these studies will help the Company and other parties determine the best use of funds toward continuing fish passage efforts or other population enhancement measures.

**Other Contingencies**

In the normal course of business, the Company has various other legal claims and contingent matters outstanding. The Company believes that any ultimate liability arising from these actions will not have a material adverse impact on the Company's financial condition, results of operations or cash flows.

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**Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations**

***Safe Harbor for Forward-Looking Statements***

This Report on Form 10-Q contains forward-looking statements within the meaning of Section 21E of the Securities Exchange Act of 1934. Avista Corp. is including the following cautionary statement to make applicable, and to take advantage of, the safe harbor provisions of the Private Securities Litigation Reform Act of 1995 for any forward-looking statements made by, or on behalf of, the Company. Forward-looking statements include statements concerning plans, objectives, goals, strategies, projections of future events or performance, and underlying assumptions (many of which are based, in turn, upon further assumptions). Forward-looking statements are all statements other than statements of historical fact including, without limitation, those that are identified by the use of words such as, but not limited to, "will," "anticipates," "seeks to," "estimates," "expects," "intends," "plans," "predicts," and similar expressions. From time to time, the Company may publish or otherwise make available forward-looking statements of this nature. All such subsequent forward-looking statements, whether written or oral and whether made by or on behalf of the Company, are also expressly qualified by these cautionary statements.

Such statements are inherently subject to a variety of risks and uncertainties that could cause actual results to differ materially from those expressed. Most of these risks and uncertainties are beyond the Company's control. Such risks and uncertainties include, among others:

- changes in the utility regulatory environment in the individual states and provinces in which the Company operates and the United States and Canada in general. This can impact allowed rates of return, financings, or industry and rate structures;
- the impact of regulatory and legislative decisions including FERC price controls, and including possible retroactive price caps and resulting refunds;
- the potential effects of any legislation or administrative rulemaking passed into law;
- the impact from the potential formation of a Regional Transmission Organization and/or an Independent Transmission Company;
- the impact from the implementation of the FERC's proposed wholesale power market rules;
- volatility and illiquidity in wholesale energy markets, including the availability and prices of purchased energy and demand for energy sales;
- wholesale and retail competition (including, but not limited to, electric retail wheeling and transmission costs);
- future streamflow conditions that affect the availability of hydroelectric resources;
- outages at any Company-owned generating facilities from any cause, including equipment failure;
- unanticipated delays or changes in construction costs with respect to present or prospective facilities;
- changes in weather conditions that can affect customer demand, result in natural disasters and/or disrupt energy delivery;
- changes in industrial, commercial and residential growth and demographic patterns in the Company's service territory;
- the loss of significant customers and/or suppliers;
- failure to deliver on the part of any parties from which the Company purchases and/or sells capacity or energy;
- changes in the creditworthiness of customers and energy trading counterparties;
- the Company's ability to obtain financing through the issuance of debt and/or equity securities, which can be affected by various factors including the Company's credit ratings, interest rate fluctuations and other capital market conditions;
- changes in future economic conditions in the Company's service territory and the United States in general, including inflation or deflation and monetary policy;
- the potential for future terrorist attacks, particularly with respect to utility plant assets;
- changes in tax rates and/or policies;
- changes in, and compliance with, environmental and endangered species laws, regulations, decisions and policies, including present and potential environmental remediation costs;
- the outcome of legal and regulatory proceedings concerning the Company or affecting directly or indirectly its operations, including the potential disallowance of previously deferred costs;
- employee issues, including changes in collective bargaining unit agreements, strikes, work stoppages or the loss of key executives, as well as the ability to recruit and retain employees;
- changes in actuarial assumptions and the return on assets with respect to the Company's pension plan, which can impact future funding obligations, costs and pension plan liabilities;
- increasing health care costs and the resulting effect on health insurance premiums paid for employees and on the

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obligation to provide postretirement health care benefits; and

- increasing costs of insurance, changes in coverage terms and the ability to obtain insurance.

The Company's expectations, beliefs and projections are expressed in good faith and are believed by the Company to have a reasonable basis including, without limitation, management's examination of historical operating trends, data contained in the Company's records and other data available from third parties. However, there can be no assurance that the Company's expectations, beliefs or projections will be achieved or accomplished. Furthermore, any forward-looking statement speaks only as of the date on which such statement is made. The Company undertakes no obligation to update any forward-looking statement or statements to reflect events or circumstances that occur after the date on which such statement is made or to reflect the occurrence of unanticipated events. New factors emerge from time to time, and it is not possible for management to predict all of such factors, nor can it assess the impact of each such factor on the Company's business or the extent to which any such factor, or combination of factors, may cause actual results to differ materially from those contained in any forward-looking statement.

The following discussion and analysis is provided for the consolidated financial condition and results of operations of Avista Corp., including its subsidiaries. This discussion focuses on significant factors concerning the Company's financial condition and results of operations and should be read along with the consolidated financial statements.

### Avista Corp. Business Segments

Avista Corp. is an energy company engaged in the generation, transmission and distribution of energy as well as other energy-related businesses. The Company has four business segments – Avista Utilities, Energy Marketing and Resource Management, Avista Advantage and Other. Avista Utilities is an operating division of Avista Corp. comprising the regulated utility operations. Avista Utilities generates, transmits and distributes electricity and distributes natural gas. Avista Capital, a wholly owned subsidiary of Avista Corp., is the parent company of all of the subsidiary companies in the non-utility business segments. As of March 31, 2004, the Company had common equity investments of \$499.7 million and \$257.6 million in Avista Utilities and Avista Capital, respectively.

The Energy Marketing and Resource Management business segment is comprised of Avista Energy, Inc. (Avista Energy) and Avista Power, LLC (Avista Power). Avista Energy is an electricity and natural gas marketing, trading and resource management business, operating primarily in the Western Electricity Coordinating Council (WECC) geographical area, which is comprised of eleven Western states and the provinces of British Columbia and Alberta, Canada. Avista Power is an investor in certain generation assets, primarily its 49 percent interest in a 270-megawatt (MW) natural gas-fired combined cycle combustion turbine plant in northern Idaho (Lancaster Project).

Avista Advantage, Inc. (Avista Advantage) is a provider of utility bill processing, payment and information services to multi-site customers throughout North America. Its primary product lines include consolidated billing, resource accounting, energy analysis and load profiling services.

The Other business segment includes Avista Ventures, Inc. (Avista Ventures), Pentzer Corporation (Pentzer), Avista Development and certain other operations of Avista Capital. Included in this business segment is Advanced Manufacturing and Development (AM&D) doing business as METALfx, a subsidiary of Avista Ventures that performs custom sheet metal manufacturing of electronic enclosures, parts and systems for the computer, telecom and medical industries. AM&D also has a wood products division that provides complete fabrication and turnkey assembly for arcade games, kiosks, store fixtures, and displays.

### Executive Level Summary

Avista Corp.'s net income and operating cash flows are derived primarily from Avista Utilities and Avista Energy (included in the Energy Marketing and Resource Management segment). Avista Corp. intends to focus on improving earnings and operating cash flows, controlling costs and reducing debt while working to restore an investment grade credit rating.

Avista Utilities will seek to continue to be among the industry leaders in performance, value and service in its electric and natural gas utility businesses. The utility business is expected to grow modestly, consistent with historical trends. Expansion is expected to result primarily from economic and population growth in its service territory. It is Avista Utilities' strategy to own or to have contracts that provide a sufficient amount of resources to meet its retail and wholesale energy requirements under a range of operating conditions. Available resources and the costs of those resources are significantly affected by Avista Utilities' hydroelectric production, which was 89 percent of normal in 2003. Based on forecasts and snowpack conditions as of April 2004, Avista Utilities expects

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hydroelectric production will be approximately 86 percent of normal in 2004. This forecast may change based upon precipitation, temperatures and other variables. The effects of below normal hydroelectric production are addressed through power cost deferral and recovery mechanisms. Customer loads and resulting revenues are significantly affected by weather. During the first quarter of 2004, the weather in Avista Utilities' service territory was warmer than normal, which reduced net income. However, the weather was colder as compared to the first quarter of 2003, which increased net income compared to the first quarter of 2003. Avista Utilities expects normal weather during the remainder of 2004. As is the case with most regulated entities, Avista Utilities generally has ongoing regulatory proceedings. Avista Utilities continues to make progress with respect to resolving its regulatory matters; however, significant issues remain unresolved (see "Avista Utilities – Regulatory Matters" and "Power Market Issues"). Avista Utilities will continue to file for rate adjustments to provide recovery of its costs and to more closely align earned returns with those allowed by regulatory agencies in each jurisdiction. The Company expects Avista Utilities' net income to increase for the remainder of 2004 as compared to 2003, assuming more normal weather, a decrease in interest expenses and the implementation of general rate increases.

Avista Utilities faces issues with respect to an aging workforce at all levels of its operations. Management succession plans have been implemented to work towards ensuring that executive officer positions are appropriately filled. Avista Utilities has taken similar steps in key technical and craft areas to work towards ensuring that these positions will be appropriately filled when retirements occur.

Avista Energy focuses on optimization of combustion turbines and hydroelectric assets owned by other entities, long-term electric supply contracts, natural gas storage, and electric transmission and natural gas transportation arrangements. Avista Energy is also involved in trading electricity and natural gas, including derivative commodity instruments. Avista Energy Canada, Ltd. (Avista Energy Canada) is a wholly owned subsidiary of Avista Energy that provides natural gas services to approximately 400 industrial customers in British Columbia, Canada. In addition to earnings and resulting cash flows from settled or realized transactions, Avista Energy records unrealized or mark-to-market adjustments for the change in the value of derivative commodity instruments. Avista Energy's marketing, trading and resource management activities are driven by its base of knowledge and experience in the operation of both electric energy and natural gas physical systems in the WECC, as well as its relationship-focused approach with its customers. Avista Energy is also subject to certain regulatory proceedings that remain unresolved (see "Power Market Issues"); however, Avista Energy believes that it has adequate reserves established for refunds that may be ordered. The wholesale power markets in which Avista Energy operates continue to change with respect to market participants involved, level of activity, volatility in market prices, liquidity, FERC-imposed price caps and counterparty credit issues. Net income for Avista Energy decreased for the first quarter of 2004 as compared to the first quarter of 2003. This was primarily due to the positive effects in the first quarter of 2003 of accounting for energy trading activities under SFAS No. 133 and the settlement of positions with certain Enron affiliates. Due to these factors, the Company expects that net income from Avista Energy will decrease for fiscal year 2004 as compared to 2003.

Avista Advantage remains focused on increasing revenues, improving margins, and continuously enhancing client satisfaction. In April 2004, the president of Avista Advantage left the Company. A replacement search is currently underway. The Company expects Avista Advantage will be break-even or generate slightly positive net income for the second half of 2004 based on improving revenues and stabilized operating expenses from processing efficiencies.

Over time as opportunities arise, the Company plans to dispose of assets and phase out operations in the Other business segment. The Company expects the net loss in the Other business segment to be less for fiscal year 2004 as compared to 2003 due to the resolution of prior legal matters, as well as decreased losses from current investments and the operations of AM&D.

During the remainder of 2004, the Company expects cash flows from operations and Avista Corp.'s committed line of credit to provide adequate resources to fund capital expenditures, maturing long-term debt and other contractual commitments. However, if market conditions warrant during 2004, the Company may issue securities to fund these obligations, refinance existing debt and repurchase long-term debt scheduled to mature in future years to reduce its overall debt service costs, as well as to reduce the impact of significant debt maturities scheduled for 2007 and 2008.

### **Avista Utilities – Resources and Resource Optimization**

Avista Utilities owns and operates eight hydroelectric projects, a wood-waste fueled generating station, a two-unit natural gas-fired combustion turbine (CT) generating facility and two small generating facilities. It also owns a 15 percent share in a two-unit coal-fired generating facility and leases and operates a two-unit natural gas-fired CT

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generating facility. WP Funding LP, an entity that is included in Avista Corp.'s consolidated financial statements and in the Avista Utilities business segment, owns the two-unit natural gas-fired CT generating facility that is leased by Avista Utilities. In July 2003, the combined cycle natural gas-fired Coyote Springs 2 Generation Project (Coyote Springs 2) was placed into operation. Avista Utilities has a 50 percent ownership interest (140 MW) in Coyote Springs 2. See "Avista Utilities-Developments with Coyote Springs 2" for information with respect to a transformer failure at Coyote Springs 2. In addition to company owned resources, Avista Utilities has a number of long-term power purchase and exchange contracts that increase its available resources.

Avista Utilities engages in an ongoing process of resource optimization, which involves the pursuit of economic resources to serve load obligations and using existing resources to capture available economic value. Avista Utilities sells and purchases wholesale electric capacity and energy to and from utilities and other entities as part of the process of acquiring resources to serve its retail and wholesale load obligations. These transactions range from a term as short as one hour up to long-term contracts that extend beyond one year. Avista Utilities makes continuing projections of (1) future retail and wholesale loads based on, among other things, forward estimates of factors such as customer usage and weather as well as historical data and contract terms and (2) resource availability based on, among other things, estimates of streamflows, generating unit availability, historic and forward market information and experience. On the basis of these continuing projections, Avista Utilities makes purchases and sales of energy on an annual, quarterly, monthly, daily and hourly basis to match expected resources to expected energy requirements. Resource optimization also includes transactions such as purchasing fuel to run thermal generation and, when economic, selling fuel and substituting electric wholesale market purchases for the operation of Avista Utilities' own resources, as well as other wholesale transactions to capture the value of available generation and transmission resources. This optimization process includes entering into financial and physical hedging transactions as a means of managing risks.

### **Avista Utilities – Regulatory Matters**

#### **General Rate Cases**

Avista Utilities regularly reviews the need for electric and natural gas rate changes in each state in which it provides service. In February 2004, Avista Utilities filed electric and natural gas general rate cases in Idaho. The request is designed to increase electric revenues by 11 percent, or \$18.9 million in annual revenues, over current rates. This would result from a 24 percent increase in base retail rates (an increase of \$35.2 million in annual revenues) offset by a \$16.3 million annual revenue decrease from the current Power Cost Adjustment (PCA) surcharge with the remaining balance being recovered over a two-year period at a reduced rate. Avista Utilities also requested a natural gas general rate increase of 9.2 percent, or \$4.8 million in annual revenues. Avista Utilities' requests are based on an overall rate of return of 9.82 percent and a return on equity of 11.5 percent. The IPUC has established a procedural schedule, which currently calls for an order on these requests to be released in September 2004.

In September 2003, the OPUC approved a general natural gas rate increase of \$6.3 million in annual revenues effective October 1, 2003 that authorizes, among other things, an overall rate of return of 8.88 percent and a return on equity of 10.25 percent.

#### **Power Cost Deferrals and Recovery Mechanisms**

Avista Utilities defers the recognition in the income statement of certain power supply costs that are in excess of the level currently recovered from retail customers as authorized by the WUTC and the IPUC. A portion of power supply costs are recorded as a deferred charge on the balance sheet for future review and the opportunity for recovery through retail rates.

The June 2002 WUTC rate order established an Energy Recovery Mechanism (ERM) effective July 1, 2002. The ERM replaced a series of temporary deferral mechanisms that had been in place in Washington since mid-2000. The ERM allows Avista Utilities to increase or decrease electric rates periodically with WUTC approval to reflect changes in power supply costs. The ERM provides for Avista Utilities to incur the cost of, or receive the benefit from, the first \$9.0 million in annual power supply costs above or below the amount included in base retail rates. Under the ERM, 90 percent of the power supply costs exceeding or below the initial \$9.0 million are deferred for future surcharge or rebate to Avista Utilities' customers. The remaining 10 percent of power supply costs are an expense of, or benefit to, the Company. The Company expensed \$6.3 million of power supply costs above the amount included in base retail rates during the first quarter of 2004 and expects to expense the full \$9.0 million during 2004.

Under the ERM, Avista Utilities agreed to make an annual filing on or before April 1st of each year to provide the opportunity for the WUTC and other interested parties to review the prudence of and audit the ERM deferred power

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cost transactions for the prior calendar year. The settlement agreement establishing the ERM provides for a 90-day review period for the filing; however, the period may be extended by agreement of the parties or by WUTC order. Avista Utilities made its annual filing with the WUTC on April 1, 2004 related to \$22.8 million of deferred power costs incurred for 2003.

Avista Utilities has a PCA mechanism in Idaho that allows it to modify electric rates periodically with IPUC approval. Under the PCA mechanism, Avista Utilities defers 90 percent of the difference between certain actual net power supply expenses and the authorized level of net power supply expense approved in the last Idaho general rate case. The IPUC originally approved a 19.4 percent surcharge in October 2001, which has been extended through October 2004 for recovery of previously deferred power costs. Based on IPUC staff recommendations and IPUC orders, the prudence of \$11.9 million of deferred power costs will be reviewed in the electric general rate case that Avista Utilities filed in February 2004. Avista Utilities believes that such costs for long-term fuel supply contracts were prudently incurred. The IPUC has also directed Avista Utilities to work with the IPUC staff and interested customers to address concerns with respect to risk management policies as it pertains to long-term fuel supply contracts. As directed by the IPUC, Avista Utilities addressed this issue in its February 2004 electric general rate case filing.

The following table shows activity in deferred power costs for Washington and Idaho during 2003 and the three months ended March 31, 2004 (dollars in thousands):

	Washington	Idaho	Total
Deferred power costs as of December 31, 2002	\$123,749	\$ 31,518	\$155,267
Activity from January 1 – December 31, 2003:			
Power costs deferred	22,217	23,341	45,558
Unrealized loss on fuel contracts (1)	1,975	1,004	2,979
Interest and other net additions	6,002	1,037	7,039
Write-off deferred power costs	(2,461)	—	(2,461)
Recovery of deferred power costs through retail rates	(25,777)	(26,615)	(52,392)
Deferred power costs as of December 31, 2003	125,705	30,285	155,990
Activity from January 1 – March 31, 2004:			
Power costs deferred	—	6,825	6,825
Unrealized gain on fuel contracts (1)	(3,139)	(738)	(3,877)
Interest and other net additions	1,628	202	1,830
Recovery of deferred power costs through retail rates	(7,669)	(8,117)	(15,786)
Deferred power costs as of March 31, 2004	<u>\$116,525</u>	<u>\$ 28,457</u>	<u>\$144,982</u>

(1) Unrealized gains and losses on fuel contracts are not included in the ERM and PCA mechanism until the contracts are settled or realized.

**Purchased Gas Adjustments**

Natural gas commodity prices increased towards the end of 2002 and into the first half of 2003 before declining somewhat in the middle of 2003 and increasing at the end of 2003 and into the first quarter of 2004. The continued tight balance between supply and demand for natural gas is a major contributor to the ongoing price volatility in natural gas, and this is expected to continue through 2004. The Company is well connected to multiple supply basins in the western United States and western Canada and believes there will be sufficient supplies of natural gas to meet its customers' needs. However, natural gas prices in the Pacific Northwest are increasingly affected by supply and demand factors in other regions of the United States and Canada. Natural gas commodity costs in excess of the amount recovered in current rates are deferred and recovered in future periods with applicable regulatory approval through adjustments to rates. Market prices for natural gas continue to be competitive compared to alternative fuel sources for residential, commercial and industrial customers. Avista Utilities believes that natural gas should sustain its market advantage over competing energy sources based on the levels of existing reserves and potential natural gas development in the future.

During the second half of 2002, Avista Utilities adjusted its natural gas rates in response to a decrease in current and projected natural gas costs at that time. During the fourth quarter of 2002, natural gas rate decreases of 17.4 percent, 15.5 percent, 7.1 percent and 16.2 percent were approved and implemented in Washington, Idaho, Oregon and California, respectively. As discussed above, current and projected natural gas prices increased towards the end of 2002 and into 2003. During September and October of 2003, natural gas rate increases of 8.7 percent, 2.4 percent, 12.4 percent and 15.0 percent were approved and implemented in Washington, Idaho, Oregon and California, respectively. In March 2004, the WUTC removed a refund stipulation with respect to the Washington natural gas



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rate increase and approved full recovery. On April 1, 2004, a 7.3 percent increase in Oregon was approved and implemented. In March 2004, a 6.3 percent increase was requested in California to become effective in May 2004. These natural gas rate increases and decreases are designed to pass through changes in purchased natural gas costs to customers with no change in Avista Utilities' gross margin or net income. Total deferred natural gas costs were \$20.8 million and \$15.4 million as of March 31, 2004 and December 31, 2003, respectively.

### ***Natural Gas Benchmark Mechanism***

The IPUC, WUTC and OPUC approved Avista Utilities' Natural Gas Benchmark Mechanism in 1999. The mechanism eliminated the majority of natural gas procurement operations within Avista Utilities and placed responsibility for natural gas procurement operations with Avista Energy, the Company's non-regulated subsidiary. The ownership of the natural gas assets remains with Avista Utilities; however, the assets are managed by Avista Energy through an Agency Agreement. In early 2002, the IPUC and the OPUC approved the continuation of the Natural Gas Benchmark Mechanism and related Agency Agreement through March 31, 2005. In February 2004, the WUTC ordered that the Natural Gas Benchmark Mechanism and related Agency Agreement be terminated for Washington customers and ordered Avista Utilities to file a transition plan to move management of these functions back into Avista Utilities. In April 2004, the WUTC approved Avista Utilities' transition plan, which provides for the movement of these functions back into Avista Utilities to be completed by March 31, 2005. The Company is also planning to move these functions from Avista Energy to Avista Utilities for Idaho and Oregon natural gas customers with the expiration of the current agreements on March 31, 2005. It is estimated that the termination of the Natural Gas Benchmark Mechanism and related Agency Agreement will result in a reduction of approximately \$1.0 million in Avista Energy's pre-tax earnings and an increase in costs of approximately \$1.0 million for Avista Utilities. Avista Utilities would seek recovery of any increased costs in future general rate case proceedings. This transition of Avista Utilities' natural gas procurement operations will also impact the level of counterparty credit requirements at both Avista Utilities and Avista Energy.

### **Power Market Issues**

#### ***Counterparty Defaults***

In early 2001, California's two largest utilities defaulted on payment obligations owed to various energy sellers, including Avista Energy, resulting in defaults by the California Power Exchange (CalPX) and the California Independent System Operator (CalISO). In April 2004, Pacific Gas & Electric Company (PG&E) paid its defaulted obligations into an escrow fund in accordance with its bankruptcy reorganization. The FERC has ordered that the settlement of defaulted obligations held in the PG&E escrow fund and by the CalPX will depend on a determination of the California refund claims (see further information under "California Refund Proceeding"). As of March 31, 2004, Avista Energy's accounts receivable outstanding related to defaulting parties in California were fully offset by reserves for uncollected amounts and refunds. Avista Energy is pursuing recovery of the defaulted obligations.

#### ***California Refund Proceeding***

In July 2001, the FERC initiated a proceeding to determine if refunds should be owed and, if so, the amounts of such refunds for sales during the period from October 2, 2000 to June 20, 2001 in the California power market. The order provides that any refunds owed could be offset against unpaid energy debts due to the same party. Interested parties have contested pricing determinants and other matters since the proceeding started. The CalISO and the CalPX prepared revised values for the affected power transactions and they are preparing additional iterations of revised prices and terms as directed by the FERC. The results of these calculations are likely to be appealed to the FERC and federal courts. In March 2003, the FERC issued an order that addressed issues related to the California refund proceedings, setting forth proposed retroactive pricing standards. In June 2003, the FERC issued an order to review bids above \$250 per MW made by participants in the short-term energy markets operated by the CalISO and the CalPX from May 1, 2000 to October 2, 2000. Market participants with bids above \$250 per MW during the period described above will be required to demonstrate why their bidding behavior and practices did not violate applicable market rules. If violations were found to exist, the FERC would require the refund of any unjust profits and could also enforce other non-monetary penalties, such as the revocation of market-based rate authority. Avista Energy is subject to this review. Avista Energy maintains that it has engaged in sound business practices in accordance with established market rules. Based on current information, the Company believes that it has sufficient reserves in place for potential California refunds.

#### ***Pacific Northwest Refund Proceeding***

In July 2001, the FERC initiated a proceeding to determine if refunds should be owed and, if so, the amounts of such refunds for sales during the period from December 25, 2000 to June 20, 2001 in the Pacific Northwest power market. Various parties including aggrieved parties, FERC staff, and alleged beneficiaries of excess prices filed pleadings, analyses, and motions related to the requested refunds in the two years following the initiation of this proceeding. In

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June 2003, the FERC denied the request for retroactive refunds for spot market sales in the Pacific Northwest power market. In July 2003, a group, which includes Avista Utilities and Avista Energy, filed a request for rehearing supporting the FERC's decision to deny retroactive refund claims in the Pacific Northwest spot market but raising argument on certain procedural issues only in the event that the FERC entertains additional arguments in the case. Also in July 2003, several other parties filed requests for rehearing on the FERC's June 2003 order. The requests for rehearing were denied by the FERC in November 2003. A petition for review of the FERC's decision was filed by the City of Tacoma on December 24, 2003, with the United States Court of Appeals for the Ninth Circuit. Final closure of the Pacific Northwest refund proceeding will await appellate court review and the Company cannot predict its ultimate conclusion.

**Market Conduct Investigations**

As a result of certain revelations about alleged improper practices engaged in by Enron and certain of its affiliates, the FERC initiated investigations in February 2002 of Avista Utilities, Avista Energy and other unrelated parties. Avista Utilities and Avista Energy cooperated with the FERC investigation by providing requested documents and other information. Several parties filed documents with the FERC in March 2003 alleging improper market conduct by various parties, including Avista Utilities and Avista Energy, and requesting refunds and other relief. Based upon review of the filings, there were no new allegations or information not known to and addressed by the FERC Trial Staff in its investigations of Avista Corp. and Avista Energy. Avista Corp. and Avista Energy filed replies in response to the allegations of the parties.

In March 2003, the FERC policy staff issued its final report on their investigation of western energy markets. In the report, the FERC policy staff recommended the issuance of "show cause" orders to dozens of companies to respond to allegations of possible misconduct in the western energy markets during 2000 and 2001. Of the companies named in the March 2003 FERC policy staff report, Avista Corp. and Avista Energy were among the few that had already been subjects of a FERC investigation. As explained at "Federal Energy Regulatory Commission Inquiry" in "Note 13 of the Notes to Consolidated Financial Statements" regarding the investigation of Avista Corp. and Avista Energy, on April 19, 2004 the FERC approved the Agreement in Resolution reached between Avista Corp. doing business as Avista Utilities, Avista Energy and the FERC's Trial Staff with respect to an investigation into the activities of Avista Utilities and Avista Energy in western energy markets during 2000 and 2001. In the Agreement in Resolution, the FERC Trial Staff stated that its investigation found: (1) no evidence that any executives or employees of Avista Utilities or Avista Energy knowingly engaged in or facilitated any improper trading strategy; (2) no evidence that Avista Utilities or Avista Energy engaged in any efforts to manipulate the western energy markets during 2000 and 2001; and (3) that Avista Utilities and Avista Energy did not withhold relevant information from the FERC's inquiry into the western energy markets for 2000 and 2001. As part of the Agreement in Resolution, Avista Utilities has agreed to improve its system of taping energy trading conversations and improve its account settlement process. Avista Utilities and Avista Energy have agreed to maintain an annual training program on the applicable FERC Code of Conduct for all employees engaged in the trading of electric energy and capacity. Under the Agreement in Resolution, no remedial measures were taken against Avista Utilities or Avista Energy and there was no imposition of monetary remedies or assessment of penalties, or relinquishment or modification of market-based rate authority. Parties have 30 days from the FERC order date (April 19, 2004) to file a request for rehearing.

See further information under "Federal Energy Regulatory Commission Inquiry," "U.S. Commodity Futures Trading Commission (CFTC) Subpoena," "California Energy Markets," "Port of Seattle Complaint," and "State of Montana Proceedings" in "Note 13 of the Notes to Consolidated Financial Statements."

**Regional Transmission Organizations**

FERC Order No. 2000 required all utilities subject to FERC regulation to file a proposal to form a Regional Transmission Organization (RTO), or a description of efforts to participate in an RTO, and any existing obstacles to RTO participation. FERC Order No. 2000 is a follow-up to FERC Orders No. 888 and No. 889 issued in 1996, which required transmission owners to provide non-discriminatory transmission service to third parties.

Avista Corp. is in continuing discussions with utilities and others in the Pacific Northwest region to define how such an RTO might work. For example, the Company has negotiated with nine other utilities in the western United States on the possible formation of an RTO, RTO West, a non-profit organization. The Company and two other western utilities have also taken steps toward the formation of a for-profit Independent Transmission Company, TransConnect, which could be a member of a future RTO.

The final proposal for any RTO or TransConnect must be approved by the FERC, the boards of directors of the filing companies and regulators in various states. The Company's decision to move forward with the formation of TransConnect or any RTO serving the Pacific Northwest region, as well as the legal, financial and operating

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implications of such decisions, will ultimately depend on the terms and conditions related to the formation of the entities and conditions established in the regulatory approval processes. The Company cannot predict these implications.

In September 2003, a new organization called Western Interconnection L.L.C. (WI) filed an application with the FERC for certification as an RTO to provide transmission service in the western United States. As part of its application, WI requested that FERC order each jurisdictional utility in the western United States (including Avista Corp.) to provide escrow funding to WI in the amount of \$4.0 million per year. Several parties (including Avista Corp.) have filed motions with the FERC requesting that WI's application be denied.

**Wholesale Power Market Design**

In April 2003, the FERC issued a White Paper presenting a revised version of proposed wholesale power market rules. The White Paper emphasizes a focus on the formation of RTOs and on ensuring that all independent transmission organizations have sound market rules. The White Paper further indicates that the implementation schedule will vary depending on regional needs and will also allow for regional differences. This White Paper was developed based on input from numerous state regulatory agencies, utility companies, industry and consumer groups, as well as the public. The White Paper reflects significant concerns raised with respect to the FERC's initial proposal of a Standard Market Design in July 2002. The FERC's stated goals with respect to wholesale power markets include: reliable and reasonably priced electric service for all customers; sufficient electric infrastructure; transparent markets with fair rules for all market participants; stability and regulatory certainty for customers, the electric power industry, and investors; technological innovation; and efficient use of the nation's resources. The White Paper proposes a significant role being played by regional authorities in setting up regional power markets. At this time, the Company cannot predict the ultimate impact the changes may have on its operations as well as how the changes may impact the RTO West, TransConnect and WI proposals.

**Results of Operations****Diluted Earnings (Loss) per Common Share by Business Segments**

The following table presents diluted earnings (loss) per common share by business segments for the three months ended March 31:

	2004	2003
Avista Utilities	\$ 0.22	\$ 0.16
Energy Marketing and Resource Management	0.07	0.27
Avista Advantage	—	(0.01)
Other	(0.03)	(0.05)
Earnings per common share from continuing operations	0.26	0.37
Loss per common share from discontinued operations	—	(0.02)
Earnings per common share before cumulative effect of accounting change	0.26	0.35
Loss per common share from cumulative effect of accounting change	(0.01)	(0.03)
Total earnings per common share, diluted	<u>\$ 0.25</u>	<u>\$ 0.32</u>

**Overall Operations**

Income from continuing operations was \$12.7 million for the three months ended March 31, 2004 compared to \$18.4 million for the three months ended March 31, 2003. The decrease was primarily due to decreased net income for Energy Marketing and Resource Management, partially offset by increased net income for Avista Utilities and decreased net losses for Avista Advantage and the Other business segment.

Net income for Energy Marketing and Resource Management was \$3.5 million for the three months ended March 31, 2004 compared to \$13.1 million (excluding the cumulative effect of accounting change) for the three months ended March 31, 2003. During the three months ended March 31, 2003, Avista Energy's earnings were positively impacted by the effects of accounting for energy contracts under SFAS No. 133 and a settlement with certain Enron affiliates. The combined effect of these two items on net income for the three months ended March 31, 2003 was approximately \$9.6 million, or \$0.20 per diluted share.

Net income for Avista Utilities was \$10.8 million for the three months ended March 31, 2004, compared to \$8.3 million for the three months ended March 31, 2003. The increase for Avista Utilities was primarily due to an

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increase in gross margin and a decrease in depreciation and amortization, partially offset by an increase in other operating expenses (operations and maintenance, administrative and general, and taxes other than income taxes).

Avista Advantage incurred a net loss of less than \$0.1 million for the three months ended March 31, 2004 compared to a net loss of \$0.6 million for the three months ended March 31, 2003. The decrease in the net loss was primarily due to an increase in operating revenues and a decrease in operating expenses.

The Other business segment incurred a net loss of \$1.6 million (excluding the cumulative effect of accounting change) for the three months ended March 31, 2004 compared to \$2.3 million for the three months ended March 31, 2003. The decrease in the net loss was primarily due to a decrease in the losses on certain investments of Avista Ventures, partially offset by an increase in the loss from operations.

Total revenues increased \$4.8 million for the three months ended March 31, 2004 compared to the three months ended March 31, 2003. Avista Utilities' revenues increased \$30.3 million, or 12 percent, due to both increased electric and natural gas revenues. The increase in natural gas revenues was primarily due to natural gas rate increases implemented during the fourth quarter of 2003 and partially due to increased therms sold as a result of colder weather during the first quarter of 2004 as compared to the first quarter of 2003. The increase in electric revenues reflects an increase in retail revenues and sales of fuel, partially offset by a decrease in wholesale revenues. Revenues from Energy Marketing and Resource Management decreased \$19.2 million, or 16 percent, primarily due to decreased net trading margin on contracts accounted for under SFAS No. 133 and a settlement with Enron affiliates during the three months ended March 31, 2003, partially offset by increased revenues on contracts that are not considered derivatives under SFAS No. 133 (primarily the Agency Agreement with Avista Utilities). Revenues from Avista Advantage increased 11 percent to \$5.3 million primarily as a result of customer growth. Revenues from the Other business segment decreased \$0.2 million primarily due to decreased revenues from AM&D.

Total resource costs increased \$13.0 million for the three months ended March 31, 2004 compared to the three months ended March 31, 2003. Resource costs for Avista Utilities increased \$19.8 million primarily due to an increase in the expense for natural gas purchased. This increase was due to both an increase in prices and the volume purchased due to colder weather. Resource costs for Energy Marketing and Resource Management decreased \$0.2 million.

Intersegment eliminations, which decreases both operating revenues and resource costs, increased to \$59.2 million for the three months ended March 31, 2004 from \$52.6 million for the three months ended March 31, 2003, representing increased purchases of natural gas under the Agency Agreement between Avista Utilities and Avista Energy.

Operations and maintenance expenses increased \$4.7 million for the three months ended March 31, 2004 compared to the three months ended March 31, 2003 primarily due to increased expenses for Avista Utilities, partially offset by decreased expenses for Avista Advantage and the Other business segment. The increase for Avista Utilities primarily reflects an increase in labor costs and was also due to expenses for Coyote Springs 2, which commenced operations in mid-2003.

Administrative and general expenses decreased \$2.4 million for the three months ended March 31, 2004 compared to the three months ended March 31, 2003 primarily due to decreased expenses for Energy Marketing and Resource Management, partially offset by increased expenses from Avista Utilities, Avista Advantage and the Other business segment. The decrease for Energy Marketing and Resource Management was primarily a result of decreased compensation expenses and professional fees. The increase for Avista Utilities was primarily due to increased employee benefit costs, insurance costs and professional services.

Depreciation and amortization decreased \$1.3 million for the three months ended March 31, 2004 compared to the three months ended March 31, 2003 primarily due to a correction at Avista Utilities for overstated depreciation expense in prior periods, partially offset by utility plant additions at Avista Utilities and the resulting increase in depreciation expense. Coyote Springs 2 was placed into service in mid-2003 and increased depreciation expense by \$0.6 million.

Taxes other than income taxes increased \$2.5 million for the three months ended March 31, 2004 compared to the three months ended March 31, 2003 primarily due to increased retail revenues and related taxes for Avista Utilities.

Interest expense (including interest expense to affiliated trusts) increased \$0.1 million for the three months ended March 31, 2004 compared to the three months ended March 31, 2003 primarily due to the inclusion of \$0.5 million

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of preferred stock dividends as interest expense for the first quarter of 2004 in accordance with SFAS No. 150, "Accounting for Certain Financial Instruments with Characteristics of Both Liabilities and Equity" (see Note 2 of the Notes to Consolidated Financial Statements), partially offset by a decrease in interest expense other than preferred stock dividends due to the repurchase of higher cost debt. Preferred stock dividends of \$0.6 million were classified as a separate line item on the Consolidated Statement of Income for the three months ended March 31, 2003. During 2003, the Company repurchased \$52.5 million of long-term debt. Excluding the effect of preferred stock dividends, the Company expects interest expense to continue to decline in 2004 due to the effect of previous debt repurchases. The Company also expects interest expense to continue to decline due to the April 2004 issuance of \$61.9 million of Junior Subordinated Debt Securities to AVA Capital Trust III, a business trust. Concurrently, AVA Capital Trust III issued \$60.0 million of Preferred Trust Securities to third parties and \$1.9 million of Common Trust Securities to the Company. All of these securities have a fixed interest rate of 6.50 percent for five years (through March 31, 2009). The Company used the proceeds from the Junior Subordinated Debt Securities to redeem \$61.9 million of 7.875 percent Junior Subordinated Deferrable Interest Debentures, Series A, originally issued in 1997 to Avista Capital I, a business trust. Avista Capital I used these proceeds to redeem \$60.0 million of Preferred Trust Securities issued to third parties and \$1.9 million of Common Trust Securities issued to the Company.

Capitalized interest increased \$0.4 million for the three months ended March 31, 2004 compared to the three months ended March 31, 2003. This was primarily due to increased construction activity at Avista Utilities and higher average construction work in progress balances.

Other income-net increased \$1.4 million for the three months ended March 31, 2004 compared to the three months ended March 31, 2003 primarily due to increased interest income and decreased losses in 2004 on certain investments in the Other business segment.

Income taxes decreased \$4.3 million for three months ended March 31, 2004 compared to the three months ended March 31, 2003, primarily due to decreased income before income taxes. The effective tax rate was 41.9 percent for the three months ended March 31, 2004 compared to 42.2 percent for the three months ended March 31, 2003.

During the three months ended March 31, 2004, the Other business segment recorded as a cumulative effect of accounting change a charge of \$0.5 million related to the implementation of FIN 46, which required Avista Ventures to consolidate several minor entities.

During the three months ended March 31, 2003, Avista Energy recorded as a cumulative effect of accounting change a charge of \$1.2 million (net of tax) related to Emerging Issues Task Force (EITF) Issue No. 02-3, "Issues Involved in Accounting for Derivative Contracts Held for Trading Purposes and Contracts Involved in Energy Trading and Risk Management Activities," which effectively required the transition of accounting for energy trading activities from EITF Issue No. 98-10, "Accounting for Contracts Involved in Energy Trading and Risk Management Activities" to SFAS No. 133.

**Avista Utilities**

Net income for Avista Utilities was \$10.8 million for the three months ended March 31, 2004 compared to \$8.3 million for the three months ended March 31, 2003. Avista Utilities' income from operations was \$39.7 million for the three months ended March 31, 2004 compared to \$36.9 million for the three months ended March 31, 2003. This increase was primarily due to an increase in gross margin and a decrease in depreciation and amortization, partially offset by an increase in operations and maintenance, administrative and general, and taxes other than income taxes.

The following table presents Avista Utilities' gross margin for the three months ended March 31 (dollars in thousands):

	Electric		Natural Gas		Total	
	2004	2003	2004	2003	2004	2003
Operating revenues	\$171,966	\$162,593	\$118,039	\$97,147	\$290,005	\$259,740
Resource costs	83,068	79,334	81,265	65,194	164,333	144,528
Gross margin	\$ 88,898	\$ 83,259	\$ 36,774	\$31,953	\$125,672	\$115,212

Avista Utilities' operating revenues increased \$30.3 million and resource costs increased \$19.8 million, which resulted in an increase of \$10.5 million in gross margin for the three months ended March 31, 2004 as compared to the three months ended March 31, 2003. The gross margin on natural gas sales increased \$4.8 million and the gross margin on electric sales increased \$5.7 million. The increase in the gross margin on natural gas sales was primarily

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due to an increase in retail customer usage. Primarily due to colder weather and partially due to customer growth during the first three months of 2004, total retail therm sales increased by 9 percent. The increase in electric gross margin was partially due to the expense of the initial \$6.3 million of power supply costs in Washington exceeding the amount included in base retail rates during the first quarter of 2004, compared to \$9.0 million for the first quarter of 2003. The remaining increase in electric gross margin primarily reflects increased customer usage due to colder weather and customer growth.

The following table presents Avista Utilities' electric operating revenues and megawatt-hour (MWh) sales for the three months ended March 31 (dollars and MWhs in thousands):

	Electric Operating Revenues		Electric Energy MWh sales	
	2004	2003	2004	2003
Residential	\$ 62,733	\$ 57,767	994	921
Commercial	49,708	48,842	716	693
Industrial	21,217	16,475	498	360
Public street and highway lighting	1,204	1,184	6	6
Total retail	134,862	124,268	2,214	1,980
Wholesale	10,114	16,007	220	424
Sales of fuel	23,029	18,547	—	—
Other	3,961	3,771	—	—
Total	<u>\$171,966</u>	<u>\$162,593</u>	<u>2,434</u>	<u>2,404</u>

Retail electric revenues increased \$10.6 million for the three months ended March 31, 2004 from the three months ended March 31, 2003. This increase was primarily due to an increase in total MWhs sold (increased revenues \$14.3 million), partially offset by a decrease in revenue per MWh (decreased revenues \$3.7 million). The weather was generally colder than 2003 during the first quarter of 2004 which increased MWh sales. The decrease in revenue per MWh was primarily due to a slight change in revenue mix with a greater percentage of revenues from industrial sales. The increase in industrial revenues was primarily due to the new Potlatch Corporation contract.

Wholesale electric revenues decreased \$5.9 million reflecting a decrease in wholesale sales volumes partially offset by higher average sales prices. The decrease in wholesale revenues was also due to the implementation of EITF Issue No. 03-11, which requires that wholesale revenues and resource costs from Avista Utilities' settled energy contracts that are "booked out" (not physically delivered) should be reported on a net basis as part of operating revenues effective October 1, 2003. The adoption of this EITF Issue resulted in a reduction in wholesale revenues of approximately \$2.7 million for 2004 as compared to 2003 for Avista Utilities.

Sales of fuel increased \$4.5 million as a result of natural gas that was not used for generation because electric wholesale market prices were generally below the cost of operating the gas-fired thermal generating units.

The following table presents Avista Utilities' natural gas operating revenues and therm sales for the three months ended March 31 (dollars and therms in thousands):

	Natural Gas Operating Revenues		Natural Gas Therm Sales	
	2004	2003	2004	2003
Residential	\$ 73,908	\$59,715	84,034	76,011
Commercial	38,899	32,303	48,933	45,829
Industrial	2,311	1,796	3,478	3,025
Total retail	115,118	93,814	136,445	124,865
Wholesale	98	—	210	—
Transportation	1,999	2,393	41,215	43,096
Other	824	940	424	659
Total	<u>\$118,039</u>	<u>\$97,147</u>	<u>178,294</u>	<u>168,620</u>

Natural gas revenues increased \$20.9 million for the three months ended March 31, 2004 from the three months ended March 31, 2003 primarily due to an increase in retail natural gas rates and sales volumes. The \$21.3 million increase in retail natural gas revenues was due to an increase in retail rates (increased revenues \$11.5 million) and an increase in volumes (increased revenues \$9.8 million). During the fourth quarter of 2003, retail rates for natural gas were increased in response to an increase in current and projected natural gas costs. The increase in total therms sold was a result of colder weather during the first quarter of 2004 as compared to the first quarter of 2003, as well as customer growth.

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The following table presents Avista Utilities' average number of electric and natural gas customers as well as heating degree days for the three months ended March 31:

	Electric Customers		Natural Gas Customers	
	2004	2003	2004	2003
Residential	287,542	282,408	267,648	259,926
Commercial	36,566	36,146	31,850	31,268
Industrial	1,413	1,408	310	306
Public street and highway lighting	426	412	—	—
Total retail	325,947	320,374	299,808	291,500
Wholesale	38	49	1	—
Transportation	—	—	77	90
Total customers	325,985	320,423	299,886	291,590
Heating degree days (1):				
Spokane, Washington				
Actual			2,803	2,584
30 year average (2)			2,875	2,875
Medford, Oregon				
Actual			1,671	1,751
30 year average (2)			1,964	1,964

(1) Heating degree days are the measure of the coldness of weather experienced, based on the extent to which the average of the high and low temperatures for a day falls below 65 degrees Fahrenheit (annual degree days below historic indicate warmer than average temperatures).

(2) Computed for the period from 1971 through 2000.

The following table presents Avista Utilities' resource costs for the three months ended March 31 (dollars in thousands):

	2004	2003
Electric resource costs:		
Power purchased	\$ 42,187	\$ 39,491
Power cost amortizations, net	10,406	7,685
Fuel for generation	6,958	4,826
Other fuel costs	24,315	26,745
Other regulatory amortizations, net	(2,733)	(2,788)
Other electric resource costs	1,935	3,375
Total electric resource costs	83,068	79,334
Natural gas resource costs:		
Natural gas purchased	86,420	64,554
Natural gas cost amortizations (deferrals), net	(5,212)	586
Other regulatory amortizations, net	57	54
Total natural gas resource costs	81,265	65,194
Total resource costs	\$164,333	\$144,528

Power purchased for the three months ended March 31, 2004 increased \$2.7 million, or 7 percent, compared to the three months ended March 31, 2003, due to an increase in the price of power purchases (increased costs \$4.4 million) and an increase in the volume of power purchases (increased costs \$1.0 million), partially offset by the effects of EITF Issue No. 03-11 (decreased costs by \$2.7 million).

Net amortization of deferred power costs was \$10.4 million for the three months ended March 31, 2004 compared to \$7.7 million for the three months ended March 31, 2003. During the three months ended March 31, 2004, Avista Utilities recovered (collected as revenue) \$7.7 million of previously deferred power costs in Washington and \$8.1 million in Idaho. During the three months ended March 31, 2004, Avista Utilities deferred \$6.8 million of power costs in Idaho. Avista Utilities did not defer any power costs in Washington during the three months ended March 31, 2004 as the initial \$9.0 million in power costs above the amount included in rates was not expensed under the ERM.

Fuel for generation for the three months ended March 31, 2004 increased \$2.1 million compared to the three months ended March 31, 2003. This was due to both an increase in thermal generation and an increase in fuel prices.

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Other fuel costs for the three months ended March 31, 2004 decreased \$2.4 million compared to the three months ended March 31, 2003. This natural gas was sold with the associated revenues reflected as sales of fuel. Other fuel costs exceeded the revenues from selling the natural gas. This excess cost is accounted for under the ERM in Washington and the PCA in Idaho.

The expense for natural gas purchased for the three months ended March 31, 2004 increased \$21.9 million compared to the three months ended March 31, 2003 due to an increase in the cost of natural gas (increased costs \$14.5 million) and an increase in total therms purchased (increased costs \$7.4 million) consistent with an increase in natural gas sales. During the three months ended March 31, 2004, Avista Utilities had \$5.2 million of net deferrals of natural gas costs compared to \$0.6 million of net amortization for the three months ended March 31, 2003.

**Developments with Coyote Springs 2**

In January 2004, Avista Utilities determined there was a problem with the transformer at Coyote Springs 2. The plant was taken off-line and the transformer has been returned to the manufacturer for repairs covered by warranty. Avista Utilities expects that Coyote Springs 2 will be returned to operations in the third quarter of 2004. Based on current forward power price curves and assuming that the transformer is returned when expected, Avista Utilities does not expect that the absence of Coyote Springs 2 will have a material effect on its resource costs for 2004. If Coyote Springs 2 is not placed back into operation during the third quarter of 2004, it could have an effect on the Company's resource costs for 2004 depending on the level of wholesale market prices. The Company has ordered a backup transformer for Coyote Springs 2 that is scheduled for delivery in the fourth quarter of 2004.

On May 5, 2004, Coyote Springs 2, LLC (CS2, LLC) filed a complaint in Circuit Court for the State of Oregon in the County of Morrow against Alstom USA, Inc., Alston T&D, Inc. and Areva T&D, Inc., as the manufacturer (and its successors) of the transformer that originally failed in May of 2002. Additionally, on May 5, 2004, CS2, LLC filed an arbitration demand with the American Arbitration Association, at their location in Seattle, Washington, naming those same parties. Both actions seek damages related to the failure of the original transformer and the delays in delivering a serviceable replacement to Coyote Springs 2. CS2, LLC is jointly owned by Avista Corp. and Mirant Oregon, LLC (Mirant Oregon), and was the owner of Coyote Springs 2 prior to its transfer to Avista Corp. and Mirant Oregon on January 1, 2003.

**Energy Marketing and Resource Management**

Energy Marketing and Resource Management includes the results of Avista Energy and Avista Power.

Avista Energy's earnings are primarily derived from the following activities:

- Marketing and managing the output and availability of combustion turbines and hydroelectric assets owned by other entities.
- Capturing price differences between commodities (spark spread) by converting natural gas into electricity through the power generation process.
- Purchasing and storing natural gas for later sales to seek gains from seasonal price variations and demand peaks.
- Transmitting electricity and transporting natural gas between locations, including moving energy from lower priced/demand regions to higher priced/demand markets and hub locations within the WECC.
- Taking speculative positions on future price movements within established risk management policies.

Avista Energy reports the net margin on derivative commodity instruments held for trading as operating revenues. Revenues from contracts, which are not accounted for as derivatives under SFAS No. 133 and derivative commodity instruments not held for trading, are reported on a gross basis in operating revenues. Costs from contracts, which are not accounted for as derivatives under SFAS No. 133 and derivative commodity instruments not held for trading, are reported on a gross basis in resource costs.

The following table presents Avista Energy's realized and unrealized gains for the three months ended March 31 (dollars in thousands):

	<u>2004</u>	<u>2003</u>
Realized gains	\$3,349	\$16,537
Unrealized gains	6,558	12,364
Total gross margin (operating revenues less resource costs)	<u>\$9,907</u>	<u>\$28,901</u>



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Energy Marketing and Resource Management's net income was \$3.5 million for the three months ended March 31, 2004, compared to net income before the cumulative effect of accounting change of \$13.1 million for the three months ended March 31, 2003. Operating revenues decreased \$19.2 million and resource costs decreased \$0.2 million for the three months ended March 31, 2004 as compared to the three months ended March 31, 2003 resulting in a decrease in gross margin of \$19.0 million.

Avista Energy's gross margin (operating revenues less resource costs) was \$9.9 million for the three months ended March 31, 2004 compared to \$28.9 million for the three months ended March 31, 2003. The decrease in gross margin was primarily due to the transition to SFAS No. 133 and the settlement with Enron affiliates in the first quarter of 2003. The transition to SFAS No. 133 resulted in certain contracts with net estimated unrecognized losses of \$12.3 million for the three months ended March 31, 2003 not being accounted for at market value. These contracts that are not accounted for at market value were economically hedged by certain other contracts with unrealized gains for the three months ended March 31, 2003 that are considered derivatives under SFAS No. 133, and as such were recorded at market value with a positive effect on gross margin. The positive effect of the transition to SFAS No. 133 is reversed in future periods as market values change or the contracts are settled and realized. During September 2003, Avista Energy implemented hedge accounting for certain transactions. This should partially mitigate the effects from the transition to SFAS No. 133 and reduce the volatility of reporting earnings on a prospective basis. Avista Energy's settlement of various positions with Enron affiliates and the resulting release by Avista Energy of amounts, which had been reserved against such positions, also had a positive effect of \$8.4 million on gross margin for the three months ended March 31, 2003.

Realized gains decreased to \$3.3 million for the three months ended March 31, 2004 from \$16.5 million for the three months ended March 31, 2003. Realized gains represent the net gain on contracts that have settled. The decrease in realized gains was due to a decrease in the gains on physical natural gas transactions, the settlement with Enron affiliates in the prior year and decreased gains on settled financial transactions, partially offset by increased gains on physical electric transactions. The total mark-to-market adjustment for Energy Marketing and Resource Management was an unrealized gain of \$6.6 million for the three months ended March 31, 2004 compared to an unrealized gain of \$12.4 million for the three months ended March 31, 2003. The change in the unrealized gain was primarily due to the transition to SFAS No. 133 described above. During the three months ended March 31, 2004, the change in the total unrealized gain attributable to market prices and other market changes was \$7.8 million, a decrease from \$28.9 million for the three months ended March 31, 2003.

**Energy trading activities and positions**

The following table summarizes information with respect to Avista Energy's trading activities during the three months ended March 31, 2004 (dollars in thousands):

	Electric Assets net of Liabilities	Natural Gas Assets net of Liabilities	Total Unrealized Gain (Loss)
Fair value of contracts as of December 31, 2003	\$ 63,573	\$10,089	\$73,662
Less contracts settled during 2004 (1)	(16,223)	12,874	(3,349)
Fair value of new contracts when entered into during 2004 (2)	—	—	—
Change in fair value due to changes in valuation techniques (3)	—	—	—
Change in fair value attributable to market prices and other market changes	13,193	(5,378)	7,815
Fair value of contracts as of March 31, 2004	<u>\$ 60,543</u>	<u>\$17,585</u>	<u>\$78,128</u>

- (1) Contracts settled during the three months ended March 31, 2004 include those contracts that were open in 2003 but settled during the three months ended March 31, 2004 as well as new contracts entered into and settled during the three months ended March 31, 2004. Amount represents realized gains associated with these settled transactions.
- (2) Avista Energy has not entered into any origination transactions during the three months ended March 31, 2004 in which dealer profit or mark-to-market gain or loss was recorded at inception.
- (3) During the three months ended March 31, 2004, Avista Energy did not experience a change in fair value as a result of changes in valuation techniques.

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The following table discloses summarized information with respect to valuation techniques and contractual maturities of Avista Energy's energy commodity contracts outstanding as of March 31, 2004 (dollars in thousands):

	Less than one year	Greater than one and less than three years	Greater than three and less than five years	Greater than five years	Total
<b>Electric assets (liabilities), net</b>					
Prices from other external sources (1)	\$22,049	\$26,165	\$ —	\$ —	\$48,214
Fair value based on valuation models (2)	(1,684)	9,881	11,415	(7,283)	12,329
Total electric assets (liabilities), net	<u>\$20,365</u>	<u>\$36,046</u>	<u>\$11,415</u>	<u>\$(7,283)</u>	<u>\$60,543</u>
<b>Natural gas assets (liabilities), net</b>					
Prices from other external sources (1)	\$ 2,172	\$ 7,132	\$ —	\$ —	\$ 9,304
Fair value based on valuation models (3)	6,515	(54)	1,458	362	8,281
Total natural gas assets (liabilities), net	<u>\$ 8,687</u>	<u>\$ 7,078</u>	<u>\$ 1,458</u>	<u>\$ 362</u>	<u>\$17,585</u>

- (1) Fair value is determined based upon actively traded, "over-the-counter" market quotes received from third party brokers. For electric assets and liabilities, these market quotes are generally available through two years. For natural gas assets and liabilities, these market quotes are generally available through three years.
- (2) Represents contracts for delivery at basis locations not actively traded in the "over-the-counter" markets. In addition, this includes all contracts with a delivery period greater than two years, for which active quotes are not available. These internally developed market curves are determined using a production cost model with inputs for assumptions related to power prices (including, without limitation, natural gas prices, generation on-line, transmission constraints, future demand and weather). Avista Energy performs frequent stress tests on the valuation of the portfolio. While consistent valuation methodologies and updates to the assumptions are used to capture current market information, changes in these methodologies or underlying assumptions could result in significantly different fair values and income recognition. These same pricing techniques and stress tests are used to evaluate a contract prior to taking a position.
- (3) Represents contracts for delivery at basis locations not actively traded in the "over-the-counter" markets. In addition, this includes all contracts with a delivery period greater than three years, for which active quotes are not available. These internally developed market curves are based upon published New York Mercantile Exchange prices through seven years, as well as basis spreads using historical and broker estimates. After seven years, an escalation is used to estimate the valuation.

**Avista Advantage**

Avista Advantage had a net loss of less than \$0.1 million for the three months ended March 31, 2004 compared to a net loss of \$0.6 million for the three months ended March 31, 2003. Operating revenues for Avista Advantage increased \$0.5 million and operating expenses decreased \$0.5 million, as compared to the three months ended March 31, 2003. The increase in operating revenues was primarily due to the expansion of Avista Advantage's customer base. Avista Advantage had an 11 percent increase in the number of billed sites as of March 31, 2004 as compared to March 31, 2003. The decrease in operating expenses reflects improved efficiencies and a focus on reducing operating expenses.

**Other**

The Other business segment includes Avista Ventures (including AM&D), Pentzer, Avista Development and certain other operations of Avista Capital. The net loss from this business segment was \$1.6 million (excluding the cumulative effect of accounting change) for the three months ended March 31, 2004, compared to \$2.3 million for the three months ended March 31, 2003. The decrease in the net loss was primarily due to a decrease in losses from certain investments of Avista Ventures not related to AM&D, partially offset by an increase in the loss from operations. Operating revenues from this business segment decreased \$0.2 million and operating expenses increased \$0.3 million, respectively, for the three months ended March 31, 2004 as compared to the three months ended March 31, 2003. The loss from AM&D decreased to \$0.2 million for the three months ended March 31, 2004 from \$0.8 million for the three months ended March 31, 2003.

**AVISTA CORPORATION**

**Discontinued Operations**

In 2003, total investments of \$12.2 million were made by private equity investors in a new entity, ReliOn, Inc. (formerly AVLB, Inc.), which acquired the assets previously held by Avista Corp.'s fuel cell manufacturing and development subsidiary, Avista Labs. As such, these operations are reported as a discontinued operation. As of March 31, 2004, Avista Corp., through Avista Labs, had an ownership interest of approximately 17.5 percent in ReliOn, Inc., with the opportunity but no further obligation to fund or invest in this business. The loss from discontinued operations of \$1.1 million for the three months ended March 31, 2003 represents the operations of Avista Labs for that period.

**Transactions with Mirant Corporation**

In July 2003, Mirant Corporation and substantially all its subsidiaries in the United States filed for bankruptcy protection under chapter 11 of the bankruptcy code for protection from creditors. The Company does not expect the bankruptcy filing by Mirant Corporation, which did not include Mirant Oregon, the owner of 50 percent of Coyote Springs 2, to have any material effect on the joint ownership and operation of the plant. Avista Corp. and Mirant Oregon are both current with respect to their obligations to share equally in the costs of the plant. Avista Corp. and Mirant Oregon are sharing equally in the costs of operation and rights to the output from Coyote Springs 2. Each owner is separately responsible for arranging for the purchase and delivery of natural gas in order to fuel its respective interest in the plant. Each owner is also separately responsible for the sale and delivery of electric energy generated with respect to its interest in the plant. While physical limitations prevent the operation of the plant at less than approximately seventy percent of its base load capacity, the joint operating agreement provides mechanisms to allow a single owner to dispatch and direct the operation of more than its interest in the plant in order to achieve operation at or above the plant's minimum dispatch level in the event that the other owner is unable or unwilling to dispatch its portion of the plant. Additionally, provisions in the joint operating agreement provide that if either party fails to fund its portion of the operating costs or otherwise meet its obligations under the joint operating agreement, that the non-defaulting owner may elect a variety of remedies. Such remedies include the right, after notice and a cure period, (i) to convert a payment default into an adjustment of the ownership interests in the plant, resulting in a reduction of the defaulting owner's interest and a corresponding increase in the non-defaulting owner's interest, (ii) to declare a default and pursue recovery of unpaid amounts or other equitable remedies against the defaulting party, (iii) to exercise a purchase option to acquire the defaulting owner's interest in the plant, or (iv) to trigger a retirement of the plant. The Company will continue to assess the ability of Mirant Oregon to perform its obligations under the joint operating agreement and the need to exercise remedies in the event the impact of the Mirant Corporation bankruptcy prevents Mirant Oregon from performing its obligations with respect to Coyote Springs 2.

**AVISTA CORPORATION**

**Liquidity and Capital Resources**

**Review of Cash Flow Statement**

**Continuing Operating Activities** Net cash provided by continuing operating activities was \$83.8 million for the three months ended March 31, 2004 compared to \$113.4 million for the three months ended March 31, 2003. The primary reason for the decrease in net cash provided by continuing operating activities was a decrease in net cash provided by working capital components. Net cash provided by working capital components was \$35.4 million for the three months ended March 31, 2004, compared to \$74.1 million for the three months ended March 31, 2003. The net cash provided for the three months ended March 31, 2004 primarily reflects a net decrease in accounts receivable (represents cash collected from customers), a net increase in deposits from counterparties and other current liabilities, and a seasonal net decrease in natural gas stored as the natural gas was sold during the first quarter of 2004. This was partially offset by a net decrease in accounts payable (represents cash paid to vendors). The net cash provided for the three months ended March 31, 2003 primarily reflects an increase in accounts payable and a net decrease in other current assets (primarily a decrease in deposits with counterparties at Avista Energy). Significant changes in non-cash items also included a \$5.8 million change in energy commodity assets and liabilities, representing the change from an unrealized gain of \$12.4 million on energy trading activities for Avista Energy for the three months ended March 31, 2003 to an unrealized gain of \$6.6 million for the three months ended March 31, 2004. This decrease reflects a decrease in realized gains and cash receipts on settled trading transactions at Avista Energy. The net sales of securities held for trading of \$14.0 million (sales of \$16.0 million and purchases of \$2.0 million) represents the investment of cash held at Avista Energy in short-term instruments.

**Continuing Investing Activities** Net cash used in continuing investing activities was \$20.0 million for the three months ended March 31, 2004, a decrease compared to \$21.1 million for the three months ended March 31, 2003. The decrease was primarily due to a decrease in other capital expenditures and an increase in repayments received on notes receivable.

**Continuing Financing Activities** Net cash used in continuing financing activities was \$31.0 million for the three months ended March 31, 2004 compared to \$52.1 million for the three months ended March 31, 2003. During the three months ended March 31, 2004, short-term borrowings decreased \$25.0 million, which primarily reflects a decrease in the amount of debt outstanding under Avista Corp.'s line of credit. The decrease in the amount of short-term borrowings reflects cash flows from operations in excess of funding requirements for investing and financing activities.

During the three months ended March 31, 2003, short-term borrowings decreased \$30.0 million and the Company repurchased \$15.5 million of long-term debt scheduled to mature in future years. The decrease in short-term borrowings reflected a decrease in the amount outstanding under Avista Corp.'s line of credit. The overall decrease in borrowings during the three months ended March 31, 2003 reflected positive cash flows from operations.

**Overall Liquidity**

The Company's consolidated operating cash flows are primarily derived from the operations of Avista Utilities and Avista Energy. The primary source of operating cash flows for Avista Utilities is revenues (including the recovery of previously deferred power and natural gas costs) from sales of electricity and natural gas. Significant uses of cash flows from operations include the purchase of electricity and natural gas, other operating expenses, taxes and interest. The primary source and use of operating cash flows for Avista Energy is revenues and costs from realized energy commodity transactions. Significant operating cash outflows for Avista Energy also include other operating expenses and taxes.

Over time, operating cash flows do not always fully support the capital expenditure needs of Avista Utilities. As such, from time to time, the Company may need to access capital markets in order to fund these needs as well as fund maturing debt. See further discussion at "Capital Resources."

During 2002, 2003 and the three months ended March 31, 2004, the Company's overall liquidity improved compared to 2001. The general electric rate case order issued by the WUTC in June 2002 is allowing the Company to continue to improve its liquidity. The general electric rate case order provided for the restructuring and continuation of previously approved rate increases totaling 31.2 percent. In 2003, the Company received a general rate increase of \$6.3 million in Oregon. Additionally, the Company has a PCA surcharge of 19.4 percent in place in Idaho and has filed for general rate increases for both electric and natural gas customers in Idaho. See further details in the section "Avista Utilities — Regulatory Matters."

**AVISTA CORPORATION**

The Company designs operating budgets to control operating costs and capital expenditures. In addition to operating expenses, the Company has continuing commitments for capital expenditures for construction, improvement and maintenance of facilities. In 2001, the Company incurred substantial levels of indebtedness, both short and long-term, to fund high power and natural gas costs in addition to these continuing requirements and to otherwise maintain adequate levels of working capital. As a result of improved operating cash flow, during 2002, 2003 and the three months ended March 31, 2004, the Company repurchased \$256.6 million of long-term debt.

If Avista Utilities' power and natural gas costs were to significantly exceed the levels currently recovered from retail customers, its cash flows would be negatively affected. Factors that could cause purchased power costs to exceed the levels currently recovered from customers include, but are not limited to, higher prices in wholesale markets combined with an increased need to purchase power in the wholesale markets. Current FERC imposed price caps limit wholesale market prices to \$250 per MWh. Factors beyond the Company's control that could result in an increased need to purchase power in the wholesale markets include, but are not limited to, increases in demand (either due to weather or customer growth), low availability of hydroelectric resources, outages at generating facilities and failure of third parties to deliver on energy or capacity contracts. Forecasts as of April 2004 indicate that hydroelectric generation will be approximately 86 percent of normal in 2004. This will result in increased cash requirements to purchase power to serve Avista Utilities' loads. However, Avista Utilities believes that it has adequate liquidity through cash flows generated from operations and funds available under its committed line of credit to meet increased cash requirements for purchased power due to below normal hydroelectric conditions.

On May 6, 2004, the Company's committed line of credit was amended to increase the amount from \$245.0 million to \$350.0 million and increase the amount available for the issuance of letters of credit from \$75.0 million to \$125.0 million. The increase in the committed line of credit is necessary due to seasonal credit requirements anticipated as natural gas procurement functions are moved from Avista Energy to Avista Utilities.

**Capital Resources**

The Company's consolidated capital structure, including the current portion of long-term debt and short-term borrowings consisted of the following as of March 31, 2004 and December 31, 2003 (dollars in thousands):

	March 31, 2004		December 31, 2003	
	Amount	Percent of total	Amount	Percent of total
Current portion of long-term debt	\$ 29,899	1.6%	\$ 29,711	1.5%
Short-term borrowings	55,520	2.9	80,525	4.2
Long-term debt to affiliated trusts	113,403	5.9	113,403	5.9
Long-term debt	930,923	48.5	925,012	47.9
Total debt	1,129,745	58.9	1,148,651	59.5
Preferred stock-cumulative (including current portion)	31,500	1.6	31,500	1.6
Total liabilities	1,161,245	60.5	1,180,151	61.1
Common equity	757,277	39.5	751,252	38.9
Total	\$1,918,522	100.0%	\$1,931,403	100.0%

The Company's total debt decreased from December 31, 2003 to March 31, 2004 due to a decrease in short-term borrowings, partially offset by the adoption of FIN 46 (see Note 2 of the Notes to Consolidated Financial Statements), which increased long-term debt due to the consolidation of several minor entities. The Company needs to finance capital expenditures and obtain additional working capital from time to time. The cash requirements needed to service indebtedness, both short-term and long-term, reduces the amount of cash flow available to fund working capital, purchased power and natural gas costs, capital expenditures, dividends and other corporate requirements. The Company's consolidated common equity increased \$6.0 million during the three months ended March 31, 2004 primarily due to net income and the issuance of common stock through the Dividend Reinvestment Plan and employee benefit plans, partially offset by dividends and other comprehensive loss.

The Company generally funds capital expenditures with a combination of internally generated cash and external financing. The level of cash generated internally and the amount that is available for capital expenditures fluctuates depending on a variety of factors. Cash provided by utility operating activities and cash generated by Avista Energy are expected to be the Company's primary sources of funds for operating needs, dividends and capital expenditures for the remainder of 2004.

## **AVISTA CORPORATION**

In April 2004, the Company issued Junior Subordinated Debt Securities, with a principal amount of \$61.9 million to AVA Capital Trust III, a business trust. Concurrently, AVA Capital Trust III issued \$60.0 million of Preferred Trust Securities to third parties and \$1.9 million of Common Trust Securities to the Company. All of these securities have a fixed interest rate of 6.50 percent for five years (through March 31, 2009). Subsequent to the initial five-year fixed rate period, the securities will either have a new fixed rate or an adjustable rate. These debt securities may be redeemed by the Company on or after March 31, 2009 and will mature on April 1, 2034.

The Company used the proceeds from the Junior Subordinated Debt Securities to redeem \$61.9 million of 7.875 percent Junior Subordinated Deferrable Interest Debentures, Series A, originally issued in 1997 to Avista Capital I, a business trust. Avista Capital I used these proceeds to redeem \$60.0 million of Preferred Trust Securities issued to third parties and \$1.9 million of Common Trust Securities issued to the Company.

As of March 31, 2004, the Company maintained a committed line of credit with various banks in the amount of \$245.0 million with an expiration date of May 11, 2004. As of March 31, 2004, the Company could request the issuance of up to \$75.0 million in letters of credit under the committed line of credit. As of March 31, 2004 and December 31, 2003, the Company had \$55.0 million and \$80.0 million, respectively, of borrowings outstanding under this committed line of credit. As of March 31, 2004 and December 31, 2003, there were \$8.4 million and \$10.7 million in letters of credit outstanding, respectively. As of March 31, 2004, the committed line of credit was secured by \$245.0 million of non-transferable first mortgage bonds of the Company issued to the agent bank. Such first mortgage bonds would only become due and payable in the event, and then only to the extent, that the Company defaults on its obligations under the committed line of credit.

The committed line of credit agreement contains customary covenants and default provisions, including covenants not to permit the ratio of "consolidated total debt" (not including preferred stock, long-term debt to affiliated trusts, WP Funding LP debt or other long-term debt included in the consolidated financial statements as a result of the implementation of FIN 46) to "consolidated total capitalization" of Avista Corp. to be greater than 65 percent at the end of any fiscal quarter. As of March 31, 2004, the Company was in compliance with this covenant with a ratio of 52.5 percent. The committed line of credit also has a covenant requiring the ratio of "earnings before interest, taxes, depreciation and amortization" to "interest expense" of Avista Utilities for the twelve-month period ending March 31, 2004 to be greater than 1.6 to 1. As of March 31, 2004, the Company was in compliance with this covenant with a ratio of 2.3 to 1.

On May 6, 2004, the Company's committed line of credit was amended to increase the available amount to \$350.0 million (secured by non-transferable first mortgage bonds) and extend the expiration date to May 5, 2005. The amount available for the issuance of letters of credit was increased to \$125.0 million. The increase in the committed line of credit is necessary due to seasonal credit requirements anticipated as natural gas procurement functions are moved from Avista Energy to Avista Utilities. Also, the covenant requirement for the ratio of "consolidated total debt" to "consolidated total capitalization" was increased to 70 percent and includes all debt.

Any default on its committed line of credit or other financing arrangements could result in cross-defaults to other agreements and could induce vendors and other counterparties to demand collateral. In the event of default, it would be difficult for the Company to obtain financing on reasonable terms to pay creditors or fund operations, and the Company would likely be prohibited from paying dividends on its common stock. As of March 31, 2004, Avista Corp. was in compliance with the covenants of all of its financing agreements.

The Mortgage and Deed of Trust securing the Company's First Mortgage Bonds contains limitations on the amount of First Mortgage Bonds that may be issued based on, among other things, a 70 percent debt-to-collateral ratio, and/or retired First Mortgage Bonds, and a 2.00 to 1 net earnings to First Mortgage Bond interest ratio. Under various financing agreements, the Company is also restricted as to the amount of additional First Mortgage Bonds that it can issue. As of March 31, 2004, the Company could issue \$93.1 million of additional First Mortgage Bonds under the most restrictive of these financing agreements.

In April 2004, the Company filed an amended registration statement on Form S-3 with the Securities and Exchange Commission, which would allow for the issuance of up to \$349.6 million of securities (either debt or common stock). This filing amended and combined three previous registration statement filed by the Company.

### **Inter-Company Debt**

As part of its on-going cash management practices and operations, Avista Corp. from time to time makes unsecured short-term loans to, and borrowings from, Avista Capital. In turn, Avista Capital from time to time makes unsecured

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short-term loans to, and borrowings from, its subsidiaries. As of March 31, 2004, Avista Corp. held short-term notes receivable from Avista Capital in the principal amount of \$40.1 million.

In addition, Avista Capital from time to time guarantees the indebtedness and other obligations of its subsidiaries. See "Energy Marketing and Resource Management Operations" for further information.

#### Pension Plan

As of March 31, 2004, the Company's pension plan had assets with a fair value that was less than the present value of the accumulated benefit obligation under the plan. The Company does not expect the current pension plan funding deficit to have a material adverse impact on its financial condition, results of operations or cash flows. The Company made \$12 million in cash contributions to the pension plan in 2003 and expects to make \$15 million in cash contributions during 2004 (\$3.75 million was contributed during the three months ended March 31, 2004). The Company's goal is to have the pension plan's current obligations fully funded by the end of 2006.

#### Off-Balance Sheet Arrangements

Avista Receivables Corp. (ARC) is a wholly owned, bankruptcy-remote subsidiary of the Company formed in 1997 for the purpose of acquiring or purchasing interests in certain accounts receivable, both billed and unbilled, of the Company. On May 29, 2002, ARC, the Company and a third-party financial institution entered into a three-year agreement whereby ARC can sell without recourse, on a revolving basis, up to \$100.0 million of those receivables. In April 2004, the revolving amount available for sale was reduced to \$85.0 million. ARC is obligated to pay fees that approximate the purchaser's cost of issuing commercial paper equal in value to the interests in receivables sold. As of March 31, 2004 and December 31, 2003, \$68.0 million and \$72.0 million in receivables were sold pursuant to the revolving agreement, respectively. This agreement provides the Company with cost-effective funds for working capital requirements, capital expenditures and other general corporate needs.

#### Credit Ratings

The Company's credit ratings were downgraded during the fourth quarter of 2001 resulting in an overall corporate credit rating that is below investment grade. The downgrade was due to liquidity concerns primarily related to the significant amount of purchased power and natural gas costs incurred and the resulting increase in debt levels and debt service costs.

The following table summarizes the Company's credit ratings as of May 3, 2004:

	<u>Standard &amp; Poor's</u>	<u>Moody's</u>	<u>Fitch, Inc.</u>
Avista Corporation			
Corporate/Issuer rating	BB+	Ba1	BB+
Senior secured debt	BBB-	Baa3	BBB-
Senior unsecured debt	BB+	Ba1	BB+
Preferred stock	BB-	Ba3	BB
Avista Capital I* (1)			
Preferred Trust Securities	BB-	Ba2	BB
Avista Capital II*			
Preferred Trust Securities	BB-	Ba2	BB
AVA Capital Trust III*			
Preferred Trust Securities	BB-	Ba2	BB
Rating outlook	Stable	Stable (2)	Stable

\* Only assets are subordinated debentures of Avista Corporation.

(1) All securities issued by Avista Capital I were redeemed in April 2004.

(2) Changed to stable from negative in March 2004.

These security ratings are not recommendations to buy, sell or hold securities. The ratings are subject to change or withdrawal at any time by the respective credit rating agencies. Each credit rating should be evaluated independently of any other ratings.

## **AVISTA CORPORATION**

### **Avista Utilities Operations**

Avista Utilities held cash deposits from other parties in the amount of \$27.9 million as of March 31, 2004, which is included in cash and cash equivalents with a corresponding amount in deposits from counterparties on the Consolidated Balance Sheet. These amounts are subject to return if conditions warrant because of continuing portfolio value fluctuations with those parties or substitution of collateral.

The transition of the natural gas procurement operations from Avista Energy to Avista Utilities will impact the level of counterparty credit requirements with respect to natural gas purchase contracts.

As of March 31, 2004, Avista Utilities had \$36.7 million in cash and temporary investments, including the \$27.9 million of cash deposits from other parties.

See “Notes 4, 8, 9 and 10 of Notes to Consolidated Financial Statements” for additional details related to financing activities.

### **Energy Marketing and Resource Management Operations**

On July 25, 2003, Avista Energy and its subsidiary, Avista Energy Canada, Ltd., as co-borrowers, entered into a committed credit agreement with a group of banks in the aggregate amount of \$110.0 million expiring July 23, 2004. This committed credit facility provides for the issuance of letters of credit to secure contractual obligations to counterparties. This facility is guaranteed by Avista Capital and secured by Avista Energy’s assets. The maximum amount of credit extended by the banks for the issuance of letters of credit is the subscribed amount of the facility less the amount of outstanding cash advances, if any. The maximum amount of credit extended by the banks for cash advances is \$30.0 million. No cash advances were outstanding as of March 31, 2004. Letters of credit in the aggregate amount of \$20.5 million were outstanding as of March 31, 2004. The cash deposits of Avista Energy at the respective banks collateralize these letters of credit, which are reflected as restricted cash on the Consolidated Balance Sheet.

The Avista Energy credit agreement contains customary covenants and default provisions, including covenants to maintain “minimum net working capital” and “minimum net worth,” as well as a covenant limiting the amount of indebtedness that the co-borrowers may incur. The credit agreement also contains covenants and other restrictions related to Avista Energy’s trading limits and positions, including VAR limits, restrictions with respect to changes in risk management policies or volumetric limits, and limits on exposure related to hourly and daily trading of electricity. Also, a reduction in the credit rating of Avista Corp. would represent an event of default under Avista Energy’s credit agreement. These covenants, certain counterparty agreements and current market liquidity conditions result in Avista Energy maintaining certain levels of cash and therefore effectively limit the amount of cash dividends that are available for distribution to Avista Capital and ultimately to Avista Corp. Avista Energy was in compliance with the covenants of its credit agreement as of March 31, 2004.

Avista Energy is currently negotiating a renewal of its credit facility and anticipates it will be in place by the July 23, 2004 expiration date of the current credit agreement.

Avista Capital provides guarantees for Avista Energy’s credit agreement (see discussion above) and, in the course of business, may provide performance guarantees to other parties with whom Avista Energy may be doing business. At any point in time, Avista Capital is only liable for the outstanding portion of the performance guarantee, which was \$38.8 million as of March 31, 2004. The face value of all performance guarantees issued by Avista Capital for energy trading contracts at Avista Energy was \$406.7 million as of March 31, 2004.

As part of its on-going cash management practices and operations, Avista Energy from time to time makes unsecured short-term loans to its parent, Avista Capital. Avista Capital’s Board of Directors has limited the total outstanding indebtedness to no more than \$45.0 million. Further, as required under Avista Energy’s credit facility, such loans cannot be outstanding longer than 90 days without being repaid. During the three months ended March 31, 2004, Avista Energy’s maximum total outstanding short-term loan to Avista Capital was \$40.1 million including accrued interest. As of March 31, 2004, all outstanding loans including accrued interest had been repaid.

Avista Energy manages collateral requirements with counterparties by providing letters of credit, providing guarantees from Avista Capital, depositing cash with counterparties and offsetting transactions with counterparties. Cash deposited with counterparties totaled \$25.6 million as of March 31, 2004, which is included in prepayments and other current assets on the Consolidated Balance Sheet. Avista Energy held cash deposits from other parties in the amount



**AVISTA CORPORATION**

of \$84.1 million as of March 31, 2004, which is included in cash and cash equivalents with a corresponding amount in deposits from counterparties on the Consolidated Balance Sheet. These amounts are subject to return if conditions warrant because of continuing portfolio value fluctuations with those parties or substitution of collateral.

As of March 31, 2004, Avista Energy had \$145.5 million in cash, including \$22.1 million of restricted cash and \$84.1 million of cash deposits from other parties. In addition, Avista Energy had \$4.9 million of short-term investments held for trading as of March 31, 2004. Covenants in Avista Energy's credit agreement, certain counterparty agreements and current market liquidity conditions result in Avista Energy maintaining certain levels of cash and therefore effectively limit the amount of cash dividends that are available for distribution to Avista Capital and ultimately to Avista Corp. Absent default, these covenants allow for the payment of dividends from Avista Energy to Avista Capital up to current earnings levels. During the three months ended March 31, 2004, Avista Energy did not pay any dividends to Avista Capital.

**Contractual Obligations**

During the three months ended March 31, 2004, the Company's future contractual obligations have not changed materially from the amounts disclosed in the 2003 Form 10-K with the following exceptions:

Short-term debt of Avista Utilities decreased from \$80.0 million as of December 31, 2003 to \$55.0 million as of March 31, 2004.

The amount outstanding under Avista Utilities' \$100.0 million revolving accounts receivable sales financing facility decreased from \$72.0 million as of December 31, 2003 to \$68.0 million as of March 31, 2004. In April 2004, the revolving amount available for sale was reduced to \$85.0 million.

In April 2004, Avista Utilities entered into a new energy purchase contract for wind power generation. The 10-year contract is currently estimated to result in an obligation of approximately \$34.2 million, within a range of \$3 million to \$4 million per year.

Avista Energy's contractual commitments to purchase energy commodities in future periods were as follows as of March 31, 2004 (dollars in millions):

<u>Year ended March 31,</u>	<u>2005</u>	<u>2006</u>	<u>2007</u>	<u>2008</u>	<u>2009</u>	<u>Thereafter</u>
Energy purchase contracts	\$820	\$314	\$218	\$178	\$186	\$623

Avista Energy also has sales commitments related to energy commodities in future periods.

As of March 31, 2004, Avista Corp. did not have any commitments outstanding with equity triggers. Avista Corp. does not expect any material impact from rating triggers; although there are certain rating triggers for Avista Corp. primarily related to changes in pricing under certain financing agreements. A reduction in the credit rating of Avista Corp. would represent an event of default under Avista Energy's credit agreement.

**Business Risk**

The Company's operations are exposed to risks including, but not limited to, the price and supply of purchased power, fuel and natural gas, regulatory allowance of the recovery of power and natural gas costs, operating costs and capital investments, streamflow and weather conditions, the effects of changes in legislative and governmental regulations, changes in regulatory requirements, availability of generation facilities, competition, technology and availability of funding. Also, like other utilities, the Company's facilities and operations may be exposed to terrorism risks or other malicious acts. See further reference to risks and uncertainties under "Safe Harbor for Forward-Looking Statements."

Avista Utilities has mechanisms in each regulatory jurisdiction, which provide for the recovery of the majority of the changes in its power and natural gas costs. The majority of power and natural gas costs that exceed the amount currently recovered through retail rates are deferred on the balance sheet for the opportunity for recovery through future retail rates. These deferred power and natural gas costs are subject to review for prudence and recoverability and as such certain deferred costs may be disallowed by the respective regulatory agencies.

Hydroelectric generation was 89 percent of normal in 2003. Forecasts as of April 2004 indicate that hydroelectric generation will be approximately 86 percent of normal in 2004. This forecast may change based upon precipitation, temperatures and other variables. The earnings impact of these factors is mitigated by regulatory mechanisms that are

## AVISTA CORPORATION

intended to defer increased power supply costs for recovery in future periods. Avista Utilities is not able to predict how the combination of energy resources, energy loads, prices, rate recovery and other factors will ultimately drive deferred power costs and the timing of recovery of these costs in future periods. See further information at “Avista Utilities — Regulatory Matters.”

Challenges facing Avista Utilities’ electric operations include, among other things, the timing and approval of the recovery of deferred power costs, changes in the availability of and volatility in the prices of power and fuel, generating unit availability, legislative and governmental regulations, potential tax law changes, customer response to price increases and surcharges, streamflows and weather conditions.

Challenges facing Avista Utilities’ natural gas operations include, among other things, volatility in the price of natural gas, changes in the availability of natural gas, legislative and governmental regulations, weather conditions and the timing and approval of recovery for increased commodity costs. Avista Utilities’ natural gas business also faces the potential for certain natural gas customers to by-pass its natural gas system. To reduce the potential for such by-pass, Avista Utilities prices its natural gas services, including transportation contracts, competitively and has varying degrees of flexibility to price its transportation and delivery rates by means of individual contracts, subject to state regulatory review and approval. Avista Utilities has long-term transportation contracts with several of its largest industrial customers, which reduces the risk of these customers by-passing the system in the foreseeable future.

In addition to its asset management activities, Avista Energy trades electricity and natural gas, along with derivative commodity instruments, including futures, options, swaps and other contractual arrangements. As a result of these trading activities, Avista Energy is subject to various risks including commodity price risk and credit risk, as well as possible risks resulting from the imposition of market controls by federal and state agencies. The FERC is conducting proceedings and investigations related to market controls within the western United States that include proposals by certain parties to impose refunds. As a result, certain parties have asserted claims for significant refunds from Avista Energy and lesser refunds from Avista Utilities, which could result in liabilities for refunding revenues recognized in prior periods. Avista Energy and Avista Utilities have joined other parties in opposing these proposals. The refund proceedings provide that any refunds owed could be offset against unpaid energy debts due to the same party. As of March 31, 2004, Avista Energy’s accounts receivable outstanding related to defaulting parties in California are fully offset by reserves for uncollected amounts and refunds. Avista Energy is pursuing recovery of the defaulted obligations. The FERC denied the request of certain parties for retroactive refunds for spot market sales in the Pacific Northwest during the period from December 25, 2000 to June 20, 2001. See “Power Market Issues” for further information with respect to the refund proceedings.

In connection with matching loads to available resources and optimizing the use of its assets, Avista Utilities engages in wholesale sales and purchases of electric capacity and energy and, accordingly, is also subject to commodity price risk, credit risk and other risks associated with these activities. Please refer the 2003 Form 10-K for a description and analysis of commodity price, credit, other operating, interest rate and foreign currency risks.

### Risk Management

*Risk Policies and Oversight.* Avista Utilities and Avista Energy use a variety of techniques to manage risks for their energy resources and wholesale energy market activities. See the 2003 Form 10-K for discussion of risk management policies and procedures.

*Quantitative Risk Measurements.* Avista Energy measures the risk in its electric and natural gas portfolio daily utilizing a Value-at-Risk (VAR) model, which monitors its risk in comparison to established thresholds. See the 2003 Form 10-K for further discussion of the VAR model. Avista Energy’s estimated potential one-day unfavorable impact on gross margin as measured by VAR was \$0.7 million as of March 31, 2004 and December 31, 2003. The average daily VAR for the three months ended March 31, 2004 was \$0.5 million. The high daily VAR was \$0.7 million and the low daily VAR was \$0.4 million during the three months ended March 31, 2004. Avista Energy was in compliance with its one-day VAR limits during the three months ended March 31, 2004. Changes in markets inconsistent with historical trends or assumptions used could cause actual results to exceed predicted limits.

Other quantitative risk measurement disclosures have not changed materially from the 2003 Form 10-K.

### Environmental Issues and Other Contingencies

See “Note 13 of the Notes to Consolidated Financial Statements.”

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**Dividends**

The Board of Directors considers the level of dividends on the Company's common stock on a regular basis, taking into account numerous factors including, without limitation, the Company's results of operations, cash flows and financial condition, as well as the success of the Company's strategies and general economic and competitive conditions. The Company's net income available for dividends is derived primarily from the operations of Avista Utilities and Avista Energy.

Avista Energy holds a significant portion of cash and cash equivalents reflected on the Consolidated Balance Sheet. Covenants in Avista Energy's credit agreement, certain counterparty agreements and current market liquidity conditions result in Avista Energy maintaining certain levels of cash and therefore effectively limit the amount of cash dividends that are available for distribution to Avista Capital and ultimately to Avista Corp. Absent default, these covenants allow for the payment of dividends from Avista Energy to Avista Capital up to current earnings levels. During the three months ended March 31, 2004, Avista Energy did not pay any dividends to Avista Capital.

**Item 3. Quantitative and Qualitative Disclosures About Market Risk**

See "Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations: Business Risk and Risk Management," and "Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations – Energy Marketing and Resource Management-Energy trading activities and positions."

**Item 4. Controls and Procedures**

The Company has disclosure controls and procedures (as defined in Rules 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934, as amended) to ensure that material information contained in its filings with the Securities and Exchange Commission is recorded, processed, summarized and reported on a timely and accurate basis. The Company's principal executive officer and principal financial officer have reviewed and evaluated the Company's disclosure controls and procedures as of the end of the period covered by this report. Based on such evaluation, the Company's principal executive officer and principal financial officer have concluded that the Company's disclosure controls and procedures are effective at ensuring that material information is recorded, processed, summarized and reported on a timely and accurate basis in the Company's filings with the Securities and Exchange Commission. Since such evaluation there have not been any significant changes in the Company's internal controls, or in other factors that could significantly affect these controls.

There have been no changes in the Company's internal control over financial reporting identified in connection with the evaluation required by the Securities Exchange Act rules 13a-15(d) and 15d-15(d) that occurred during the Company's last fiscal quarter (the Company's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the Company's internal control over financial reporting.

**Part II. Other Information**

**Item 1. Legal Proceedings**

See “Note 13 of the Notes to Consolidated Financial Statements” which is incorporated by reference.

**Item 6. Exhibits and Reports on Form 8-K**

(a) Exhibits.

Exhibits Filed:

- 4(a) Indenture dated as of April 1, 2004 between Avista Corporation and Union Bank of California, N.A., as Trustee.
- 4(b) Avista Corporation Officer’s Certificate (Under Section 301 of the Indenture, dated as of April 1, 2004).
- 4(c) AVA Capital Trust III Amended and Restated Declaration of Trust, dated as of April 5, 2004, among Avista Corporation, Union Bank of California, N.A., as Institutional Trustee, SunTrust Delaware Trust Company, as Delaware Trustee, and Malyn K. Malquist and Diane C. Thoren, as Regular Trustees.
- 12 Computation of ratio of earnings to fixed charges and preferred dividend requirements.
- 31(a) Certification of Chief Executive Officer
- 31(b) Certification of Chief Financial Officer

Exhibits Furnished:

- 32 Certification of Corporate Officers (Furnished Pursuant to 18 U.S.C. Section 1350, as Adopted Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002)

(b) Reports on Form 8-K.

Furnished under items 7 and 12, dated January 28, 2004, with respect to 2003 fourth quarter and year-end earnings.

An amendment to the 8-K furnished above, furnished under items 7 and 12, dated January 28, 2004.

Filed under items 5 and 7, dated February 6, 2004, with respect to a request with the Idaho Public Utilities Commission to change Avista Corp.’s electric and natural gas rates.

Filed under item 5, dated March 12, 2004, with respect to Moody’s Investors Service affirming the debt ratings of Avista Corp. and changing the rating outlook to stable from negative.

*AVISTA CORPORATION*

SIGNATURE

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

AVISTA CORPORATION

\_\_\_\_\_  
(Registrant)

/s/ Malyn K. Malquist

\_\_\_\_\_  
Malyn K. Malquist  
Senior Vice President, Chief  
Financial Officer and Treasurer  
(Principal Accounting and  
Financial Officer)

Date: May 7, 2004

AVISTA CORPORATION  
TO  
UNION BANK OF CALIFORNIA, N.A.,  
Trustee

-----  
Indenture  
DATED AS OF APRIL 1, 2004  
-----

AVISTA CORPORATION  
 RECONCILIATION AND TIE BETWEEN TRUST INDENTURE ACT OF 1939 AND  
 INDENTURE, DATED AS OF APRIL 1, 2004

TRUST INDENTURE ACT SECTION -----	INDENTURE SECTION(S) -----
Section 310(a)(1)	809
(a)(2)	809
(a)(3)	Not Applicable
(a)(4)	Not Applicable
(b)	808, 810
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(b)	813
(c)	813
Section 312(a)	901
(b)	901
(c)	901
Section 313(a)	902
(b)	902
(c)	902
(d)	902
Section 314(a)	902, 507
(b)	Not Applicable
(c)(1)	102
(c)(2)	102
(c)(3)	Not Applicable
(d)	Not Applicable
(e)	102
Section 315(a)	801, 803
(b)	802
(c)	801
(d)	801
(e)	714
Section 316(a)	712, 713
(a)(1)(A)	702, 712
(a)(1)(B)	713
(a)(2)	Not Applicable
(b)	708
Section 317(a)(1)	703
(a)(2)	705
(b)	503
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INDENTURE, dated as of April 1, 2004 between AVISTA CORPORATION, a corporation duly organized and existing under the laws of the State of Washington (hereinafter sometimes called the "Company"), and UNION BANK OF CALIFORNIA, N.A., a national banking association duly organized and existing under the laws of the United States of America, as trustee (hereinafter sometimes called the "Trustee").

#### RECITALS OF THE COMPANY

The Company has duly authorized the execution and delivery of this Indenture to provide for the issuance from time to time of its unsecured subordinated debentures, notes or other evidences of indebtedness (herein called the "Securities"), to be issued in one or more series as contemplated herein; and all acts necessary to make this Indenture a valid agreement of the Company have been performed.

NOW, THEREFORE, THIS INDENTURE WITNESSETH that in consideration of the premises and of the purchase of the Securities by the Holders thereof, it is hereby covenanted and agreed, for the equal and ratable benefit of all Holders of the Securities or of series thereof (except as otherwise contemplated herein), as follows:

#### ARTICLE ONE

##### DEFINITIONS AND OTHER PROVISIONS OF GENERAL APPLICATION

##### SECTION 101. GENERAL DEFINITIONS.

For all purposes of this Indenture, except as otherwise expressly provided or unless the context otherwise requires:

(a) the terms defined in this Article have the meanings assigned to them in this Article and include the plural as well as the singular;

(b) all terms used herein without definition which are defined in the Trust Indenture Act, either directly or by reference therein, have the meanings assigned to them therein;

(c) all accounting terms not otherwise defined herein have the meanings assigned to them in accordance with generally accepted accounting principles in the United States, and, except as otherwise herein expressly provided, the term "generally accepted accounting principles" with respect to any computation required or permitted hereunder shall mean such accounting principles as are generally accepted in the United States at the date of such computation or, at the election of the Company, at the date of the execution and delivery of this Indenture;

(d) any reference to an "Article" or a "Section" refers to an Article or a Section, as the case may be, of this Indenture; and

(e) the words "herein", "hereof" and "hereunder" and other words of similar import refer to this Indenture as a whole and not to any particular Article, Section or other subdivision.

"ACT", when used with respect to any Holder of a Security, has the meaning specified in Section 104.

"AFFILIATE" of any specified Person means any other Person directly or indirectly controlling or controlled by or under direct or indirect common control with such specified Person. For the purposes of this definition, "CONTROL" when used with respect to any specified Person means the power to direct generally the management and policies of such Person, directly or indirectly, whether through the ownership of voting securities, by contract or otherwise; and the terms "CONTROLLING" and "CONTROLLED" have meanings correlative to the foregoing.

"AUTHENTICATING AGENT" means any Person (other than the Company or any Affiliate thereof) authorized by the Trustee to act on behalf of the Trustee to authenticate the Securities of one or more series.

"AUTHORIZED OFFICER" means the Chairman of the Board, the President, any Vice President, the Treasurer, any Assistant Treasurer or the Corporate Secretary or any other duly authorized officer, agent or attorney-in-fact of the Company named in an Officer's Certificate of the Company signed by any of the aforesaid corporate officers.

"BOARD OF DIRECTORS" means either the board of directors of the Company or any committee thereof duly authorized to act in respect of matters relating to this Indenture.

"BOARD RESOLUTION" means a copy of a resolution certified by the Corporate Secretary or an Assistant Corporate Secretary of the Company to have been duly adopted by the Board of Directors of the Company and to be in full force and effect on the date of such certification, and delivered to the Trustee.

"BUSINESS DAY", when used with respect to a Place of Payment or any other particular location specified in the Securities or this Indenture, means any day, other than a Saturday or Sunday, which is not a day on which banking institutions or trust companies in such Place of Payment or other location are generally authorized or required by law, regulation or executive order to remain closed, except as may be otherwise specified as contemplated by Section 301.

"COMMISSION" means the Securities and Exchange Commission, as from time to time constituted, created under the Securities Exchange Act of 1934, as amended, or, if at any time after the date of the execution and delivery of this Indenture such Commission is not existing and performing the duties now assigned to it under the Trust Indenture Act, then the body, if any, performing such duties at such time.

"COMMON SECURITIES" means any common trust interests issued by a Trust or similar securities issued by permitted successors to such Trust in accordance with the Declaration pertaining to such Trust.

"COMPANY" means the Person named as the "Company" in the first paragraph of this Indenture until a successor Person shall have become such pursuant to the applicable provisions of this Indenture, and thereafter "Company" shall mean such successor Person.

"COMPANY ORDER" or "COMPANY REQUEST" means, respectively, a written order or request, as the case may be, signed in the name of the Company by an Authorized Officer and delivered to the Trustee.

"CORPORATE TRUST OFFICE" means the office of the Trustee at which at any particular time its corporate trust business shall be principally administered, which office at the date of the execution and delivery of this Indenture is located at 475 Sansome Street, 12th Floor, San Francisco, California 94111.

"CORPORATION" means a corporation, association, company, joint stock company or business trust.

"DECLARATION", with respect to a Trust, means the Declaration of Trust establishing such Trust, as the same shall be amended and restated from time to time.

"DISCOUNT SECURITY" means any Security which provides for an amount less than the principal amount thereof to be due and payable upon a declaration of acceleration of the Maturity thereof pursuant to Section 702. "INTEREST" with respect to a Discount Security means interest, if any, borne by such Security at a Stated Interest Rate.

"DOLLAR" or "\$" means a dollar or other equivalent unit in such coin or currency of the United States as at the time shall be legal tender for the payment of public and private debts.

"ELIGIBLE OBLIGATIONS" means:

(a) with respect to Securities denominated in Dollars, Government Obligations; or

(b) with respect to Securities denominated in a currency other than Dollars or in a composite currency, such other obligations or instruments as shall be specified with respect to such Securities as contemplated by Section 301.

"EVENT OF DEFAULT" has the meaning specified in Section 701.

"FAIR VALUE" has the meaning specified in Section 1005.

"GOVERNMENTAL AUTHORITY" means the government of the United States or of any State or Territory thereof or of the District of Columbia or of any county, municipality or other political subdivision of any thereof, or any department, agency, authority or other instrumentality of any of the foregoing.

"GOVERNMENT OBLIGATIONS" means:

(a) direct obligations of, or obligations the principal of and interest on which are unconditionally guaranteed by, the United States entitled to the benefit of the full faith and credit thereof; and

(b) certificates, depositary receipts or other instruments which evidence a direct ownership interest in obligations described in clause (a) above or in any specific interest or principal payments due in respect thereof; provided, however, that the custodian of such obligations or specific interest or principal payments shall be a bank or trust company (which may include the Trustee or any Paying Agent) subject to Federal or State supervision or examination with a combined capital and surplus of at least Fifty Million Dollars (\$50,000,000); and provided, further, that except as may be otherwise required by law, such custodian shall be obligated to pay to the holders of such certificates, depositary receipts or other instruments the full amount received by such custodian in respect of such obligations or specific payments and shall not be permitted to make any deduction therefrom.

"HOLDER" means a Person in whose name a Security is registered in the Security Register.

"INDENTURE" means this instrument as originally executed and delivered and as it may from time to time be amended and/or supplemented by one or more indentures or other instruments supplemental thereto or hereto entered into pursuant to the applicable provisions hereof and shall include the terms of particular series of Securities established as contemplated by Section 301.

"INDEPENDENT EXPERT'S CERTIFICATE" has the meaning specified in Section 1005.

"INSTITUTIONAL TRUSTEE", with respect to a Trust, has the meaning set forth in the Declaration establishing such Trust.

"INTEREST PAYMENT DATE", when used with respect to any Security, means the Stated Maturity of an installment of interest on such Security.

"MATURITY", when used with respect to any Security, means the date on which the principal of such Security or an installment of principal becomes due and payable as provided in



such Security or in this Indenture, whether at the Stated Maturity, by declaration of acceleration, upon call for redemption or otherwise.

"NOTICE OF DEFAULT" has the meaning specified in Section 701.

"OFFICER'S CERTIFICATE" means a certificate signed by an Authorized Officer of the Company and delivered to the Trustee.

"OPINION OF COUNSEL" means a written opinion of counsel, who may be counsel for the Company or other counsel acceptable to the Trustee and who may be an employee or Affiliate of the Company.

"OUTSTANDING", when used with respect to Securities, means, as of the date of determination, all Securities theretofore authenticated and delivered under this Indenture, except:

(a) Securities theretofore canceled or delivered to the Trustee for cancellation;

(b) Securities deemed to have been paid for all purposes of this Indenture in accordance with Section 601 (whether or not the Company's indebtedness in respect thereof shall be satisfied and discharged for any other purpose); and

(c) Securities which have been paid pursuant to Section 306 or in exchange for or in lieu of which other Securities have been authenticated and delivered pursuant to this Indenture, other than any such Securities in respect of which there shall have been presented to the Trustee proof satisfactory to it and the Company that such Securities are held by a bona fide purchaser or purchasers in whose hands such Securities are valid obligations of the Company;

provided, however, that in determining whether or not the Holders of the requisite principal amount of the Securities Outstanding under this Indenture, or the Outstanding Securities of any series or Tranche, have given any request, demand, authorization, direction, notice, consent or waiver hereunder or whether or not a quorum is present at a meeting of Holders of Securities,

(x) Securities owned by the Company or any other obligor upon the Securities or any Affiliate of the Company or of such other obligor (unless the Company, such obligor or such Affiliate owns all Securities Outstanding under this Indenture, or all Outstanding Securities of each such series and each such Tranche, as the case may be, determined without regard to this clause (x)) shall be disregarded and deemed not to be Outstanding, except that, in determining whether the Trustee shall be protected in relying upon any such request, demand, authorization, direction, notice, consent or waiver or upon any such determination as to the presence of a quorum, only Securities which the Trustee knows to be so owned shall be so

disregarded; provided, however, that Securities so owned which have been pledged in good faith may be regarded as Outstanding if it is established to the reasonable satisfaction of the Trustee that the pledgee, and not the Company, any such other obligor or Affiliate of either thereof, has the right so to act with respect to such Securities and that the pledgee is not the Company or any other obligor upon the Securities or any Affiliate of the Company or of such other obligor; and

(y) the principal amount of a Discount Security that shall be deemed to be Outstanding for such purposes shall be the amount of the principal thereof that would be due and payable as of the date of such determination upon a declaration of acceleration of the Maturity thereof pursuant to Section 702; and

provided, further, that, in the case of any Security the principal of which is payable from time to time without presentment or surrender, the principal amount of such Security that shall be deemed to be Outstanding at any time for all purposes of this Indenture shall be the original principal amount thereof less the aggregate amount of principal thereof theretofore paid.

"PAYING AGENT" means any Person, including the Company, authorized by the Company to pay the principal of and premium, if any, or interest, if any, on any Securities on behalf of the Company.

"PERIODIC OFFERING" means an offering of Securities of a series from time to time any or all of the specific terms of which Securities, including without limitation the rate or rates of interest, if any, thereon, the Stated Maturity or Maturities thereof and the redemption provisions, if any, with respect thereto, are to be determined by the Company or its agents from time to time subsequent to the initial request for the authentication and delivery of such Securities by the Trustee, all as contemplated in Section 301 and clause (b) of Section 303.

"PERSON" means any individual, corporation, partnership, limited liability partnership, limited liability company, joint venture, trust or unincorporated organization or any Governmental Authority.

"PLACE OF PAYMENT", when used with respect to the Securities of any series, or any Tranche thereof, means the place or places, specified as contemplated by Section 301, at which, subject to Section 502, principal of and premium, if any, and interest, if any, on the Securities of such series or Tranche are payable.

"PREDECESSOR SECURITY" of any particular Security means every previous Security evidencing all or a portion of the same debt as that evidenced by such particular Security; and, for the purposes of this definition, any Security authenticated and delivered under Section 306 in exchange for or in lieu of a mutilated, destroyed, lost or stolen Security shall be deemed (to the extent lawful) to evidence the same debt as the mutilated, destroyed, lost or stolen Security.

"PREFERRED SECURITIES" means any preferred trust interests issued by a Trust or similar securities issued by permitted successors to such Trust in accordance with the Declaration pertaining to such Trust.

"REDEMPTION DATE", when used with respect to any Security to be redeemed, means the date fixed for such redemption by or pursuant to this Indenture.

"REDEMPTION PRICE", when used with respect to any Security to be redeemed, means the price at which it is to be redeemed pursuant to this Indenture.

"REGULAR RECORD DATE" for the interest payable on any Interest Payment Date on the Securities of any series means the date specified for that purpose as contemplated by Section 301.

"REQUIRED CURRENCY" has the meaning specified in Section 311.

"RESPONSIBLE OFFICER", when used with respect to the Trustee, means any officer of the Trustee assigned by the Trustee to administer its corporate trust matters.

"SECURITIES" means any bonds, notes and other evidences of indebtedness authenticated and delivered under this Indenture.

"SECURITY REGISTER" and "SECURITY REGISTRAR" have the respective meanings specified in Section 305.

"SENIOR INDEBTEDNESS" means, with respect to any Person (a) indebtedness (including premium, if any, and interest, if any, thereon) of such Person for money borrowed or for the deferred purchase price of property or services in transactions not in the ordinary course of business; (b) all other indebtedness (including premium, if any, and interest, if any, thereon) evidenced by bonds, debentures, notes or other similar instruments (other than Securities) issued by such Person; (c) all obligations of such Person under lease agreements designating such Person as lessee, irrespective of the treatment of any such lease agreement for accounting, tax or other purposes; (d) all obligations of such Person for reimbursement (including premium, if any, and interest, if any thereon) in respect of any letter of credit, banker's acceptance, security purchase facility or similar credit transaction; (e) all obligations of the character referred to in clauses (a) through (d) above of other Persons for the payment of which such Person is responsible or liable as obligor, guarantor or otherwise; and (f) all obligations of the character referred to in clauses (a) through (d) above of other Persons secured by any lien on any property or asset of such Person (whether or not such obligation is assumed by such Person); provided, however, that Senior Indebtedness shall not include (x) any such indebtedness that is by its terms subordinated to or *pari passu* with the Securities; (y) any indebtedness between or among such Person and its Affiliates, including all other debt securities and guarantees in respect of such debt securities, issued to (i) any Trust or (ii) any other trust, or a trustee of such trust, partnership or other entity which is a financing

vehicle of such Person in connection with the issuance by such financing vehicle of preferred securities or (z) indebtedness for goods or materials purchased in the ordinary course of business or for services obtained in the ordinary course of business or indebtedness consisting of trade payables.

"SPECIAL RECORD DATE" for the payment of any Unpaid Interest on the Securities of any series means a date fixed by the Trustee pursuant to Section 307.

"STATED INTEREST RATE" means a rate (whether fixed or variable) at which an obligation by its terms is stated to bear simple interest. Any calculation or other determination to be made under this Indenture by reference to the Stated Interest Rate on an obligation shall be made (a) if the Company's obligations in respect of any other indebtedness shall be evidenced or secured in whole or in part by such obligation, by reference to the lower of the Stated Interest Rate on such obligation and the Stated Interest Rate on such other indebtedness and (b) without regard to the effective interest cost to the Company of such obligation or of any such other indebtedness.

"STATED MATURITY", when used with respect to any obligation or any installment of principal thereof or interest thereon, means the date on which the principal of such obligation or such installment of principal or interest is stated to be due and payable (without regard to any provisions for redemption, prepayment, acceleration, purchase or extension).

"SUCCESSOR" has the meaning set forth in Section 1001.

"TRANCHE" means a group of Securities which (a) are of the same series and (b) have identical terms except as to principal amount and/or date of issuance.

"TRUST" means AVA Capital Trust III, a statutory trust established under the laws of the State of Delaware, and any other Trust established for the purpose of issuing securities upon the issuance and delivery to it of Securities.

"TRUSTEE" means the Person named as the "Trustee" in the first paragraph of this Indenture until a successor trustee shall have become such with respect to one or more series of Securities pursuant to the applicable provisions of this Indenture, and thereafter "Trustee" shall mean or include each Person who is then a Trustee hereunder, and, if at any time there is more than one such Person, acting as trustee hereunder, "Trustee" shall mean each such Person so acting.

"TRUST INDENTURE ACT" means, as of any time, the Trust Indenture Act of 1939, or any successor statute, as in effect at such time.

"TRUST SECURITIES", with respect to a Trust, means the securities issued by such Trust, as established in the Declaration of such Trust.

"TRUST SECURITIES GUARANTEE" means the Guarantee Agreement between the Company, as Trust Securities Guarantor, and a guarantee trustee for the benefit of the holders of Preferred Securities and Common Securities issued by the Trust.

"UNITED STATES" means the United States of America, its territories, its possessions and other areas subject to its political jurisdiction.

"UNPAID INTEREST" has the meaning specified in Section 307.

#### SECTION 102. COMPLIANCE CERTIFICATES AND OPINIONS.

Except as otherwise expressly provided in this Indenture, upon any application or request by the Company to the Trustee to take any action under any provision of this Indenture, the Company shall furnish to the Trustee an Officer's Certificate stating that all conditions precedent, if any, provided for in this Indenture relating to the proposed action have been complied with and an Opinion of Counsel stating that in the opinion of such counsel all such conditions precedent, if any, have been complied with, it being understood that in the case of any such application or request as to which the furnishing of such documents is specifically required by any provision of this Indenture relating to such particular application or request, no additional certificate or opinion need be furnished.

Every certificate or opinion with respect to compliance with a condition or covenant provided for in this Indenture shall include:

(a) a statement that each individual signing such certificate or opinion has read such covenant or condition and the definitions herein relating thereto;

(b) a brief statement as to the nature and scope of the examination or investigation upon which the statements or opinions contained in such certificate or opinion are based;

(c) a statement that, in the opinion of each such individual, such individual has made such examination or investigation as is necessary to enable such individual to express an informed opinion as to whether or not such covenant or condition has been complied with; and

(d) a statement as to whether, in the opinion of each such individual, such condition or covenant has been complied with.

#### SECTION 103. CONTENT AND FORM OF DOCUMENTS DELIVERED TO TRUSTEE.

(a) Any Officer's Certificate may be based (without further examination or investigation), insofar as it relates to or is dependent upon legal matters, upon an opinion of, or representations by, counsel, unless, in any case, such officer has actual knowledge that the certificate or opinion or representations with respect to the matters upon which such Officer's Certificate may be based as aforesaid are erroneous.

Any Opinion of Counsel may be based (without further examination or investigation), insofar as it relates to or is dependent upon factual matters, information with respect to which is in the possession of the Company, upon a certificate of, or representations by, an officer or officers of the Company, unless such counsel has actual knowledge that the certificate or opinion or representations with respect to the matters upon which his opinion may be based as aforesaid are erroneous. In addition, any Opinion of Counsel may be based (without further examination or investigation), insofar as it relates to or is dependent upon matters covered in an Opinion of Counsel rendered by other counsel, upon such other Opinion of Counsel, unless such counsel has actual knowledge that the Opinion of Counsel rendered by such other counsel with respect to the matters upon which his Opinion of Counsel may be based as aforesaid are erroneous. If, in order to render any Opinion of Counsel provided for herein, the signer thereof shall deem it necessary that additional facts or matters be stated in any Officer's Certificate provided for herein, then such certificate may state all such additional facts or matters as the signer of such Opinion of Counsel may request.

(b) In any case where several matters are required to be certified by, or covered by an opinion of, any specified Person, it is not necessary that all such matters be certified by, or covered by the opinion of, only one such Person, or that they be so certified or covered by only one document, but one such Person may certify or give an opinion with respect to some matters and one or more other such Persons as to other matters, and any such Person may certify or give an opinion as to such matters in one or several documents. Where (i) any Person is required to make, give or execute two or more applications, requests, consents, certificates, statements, opinions or other instruments under this Indenture, or (ii) two or more Persons are each required to make, give or execute any such application, request, consent, certificate, statement, opinion or other instrument, any such applications, requests, consents, certificates, statements, opinions or other instruments may, but need not, be consolidated and form one instrument.

(c) Whenever, subsequent to the receipt by the Trustee of any Board Resolution, Officer's Certificate, Opinion of Counsel or other document or instrument, a clerical, typographical or other inadvertent or unintentional error or omission shall be discovered therein, a new document or instrument may be substituted therefor in corrected form with the same force and effect as if originally filed in the corrected form and, irrespective of the date or dates of the actual execution and/or delivery thereof, such substitute document or instrument shall be deemed to have been executed and/or delivered as of the date or dates required with respect to the document or instrument for which it is substituted. Anything in this Indenture to the contrary notwithstanding, if any such corrective document or instrument indicates that action has been taken by or at the request of the Company which could not have been taken had the original document or instrument not contained such error or omission, the action so taken shall not be invalidated or otherwise rendered ineffective but shall be and remain in full force and effect, except to the extent that such action was a result of willful misconduct or bad faith. Without limiting the generality of the foregoing, any Securities issued under the authority of such defective document or instrument shall nevertheless be

the valid obligations of the Company entitled to the benefits provided by this Indenture equally and ratably with all other Outstanding Securities, except as aforesaid.

#### SECTION 104. ACTS OF HOLDERS.

(a) Any request, demand, authorization, direction, notice, consent, election, waiver or other action provided by this Indenture to be made, given or taken by Holders may be embodied in and evidenced by one or more instruments of substantially similar tenor signed by such Holders in person or by an agent duly appointed in writing or, alternatively, may be embodied in and evidenced by the record of Holders voting in favor thereof, either in person or by proxies duly appointed in writing, at any meeting of Holders duly called and held in accordance with the provisions of Article Twelve, or a combination of such instruments and any such record. Except as herein otherwise expressly provided, such action shall become effective when such instrument or instruments or record or both are delivered to the Trustee and, where it is hereby expressly required, to the Company. Such instrument or instruments and any such record (and the action embodied therein and evidenced thereby) are herein sometimes referred to as the "ACT" of the Holders signing such instrument or instruments and so voting at any such meeting. Proof of execution of any such instrument or of a writing appointing any such agent, or of the holding by any Person of a Security, shall be sufficient for any purpose of this Indenture and (subject to Section 801) conclusive in favor of the Trustee and the Company, if made in the manner provided in this Section. The record of any meeting of Holders shall be proved in the manner provided in Section 1206.

(b) The fact and date of the execution by any Person of any such instrument or writing may be proved by the affidavit of a witness of such execution or by a certificate of a notary public or other officer authorized by law to take acknowledgments of deeds, certifying that the individual signing such instrument or writing acknowledged to him the execution thereof or may be proved in any other manner which the Trustee and the Company deem sufficient. Where such execution is by a signer acting in a capacity other than his individual capacity, such certificate or affidavit shall also constitute sufficient proof of his authority.

(c) The ownership, principal amount (except as otherwise contemplated in clause (y) of the first proviso to the definition of Outstanding) and serial numbers of Securities held by any Person, and the date of holding the same, shall be proved by the Security Register.

(d) Any request, demand, authorization, direction, notice, consent, election, waiver or other Act of a Holder shall bind every future Holder of the same Security and the Holder of every Security issued upon the registration of transfer thereof or in exchange therefor or in lieu thereof in respect of anything done, omitted or suffered to be done by the Trustee or the Company in reliance thereon, whether or not notation of such action is made upon such Security.

(e) Until such time as written instruments shall have been delivered to the Trustee with respect to the requisite percentage of principal amount of Securities for the action contemplated by such instruments, any such instrument executed and delivered by or on behalf of a

Holder may be revoked with respect to any or all of such Securities by written notice by such Holder or any subsequent Holder, proven in the manner in which such instrument was proven.

(f) Securities of any series, or any Tranche thereof, authenticated and delivered after any Act of Holders may, and shall if required by the Trustee, bear a notation in form approved by the Trustee as to any action taken by such Act of Holders. If the Company shall so determine, new Securities of any series, or any Tranche thereof, so modified as to conform, in the opinion of the Trustee and the Company, to such action may be prepared and executed by the Company and authenticated and delivered by the Trustee in exchange for Outstanding Securities of such series or Tranche.

(g) The Company may, at its option, by Company Order, fix in advance a record date for the determination of Holders entitled to give any request, demand, authorization, direction, notice, consent, waiver or other Act solicited by the Company, but the Company shall have no obligation to do so; provided, however, that the Company may not fix a record date for the giving or making of any notice, declaration, request or direction referred to in the next sentence. In addition, the Trustee may, at its option, fix in advance a record date for the determination of Holders of Securities of any series entitled to join in the giving or making of any Notice of Default, any declaration of acceleration referred to in Section 702, any request to institute proceedings referred to in Section 707 or any direction referred to in Section 712, in each case with respect to Securities of such series. If any such record date is fixed, such request, demand, authorization, direction, notice, consent, waiver or other Act, or such notice, declaration, request or direction, may be given before or after such record date, but only the Holders of record at the close of business on the record date shall be deemed to be Holders for the purposes of determining (i) whether Holders of the requisite proportion of the Outstanding Securities have authorized or agreed or consented to such Act (and for that purpose the Outstanding Securities shall be computed as of the record date) and/or (ii) which Holders may revoke any such Act (notwithstanding subsection (e) of this Section); and any such Act, given as aforesaid, shall be effective whether or not the Holders which authorized or agreed or consented to such Act remain Holders after such record date and whether or not the Securities held by such Holders remain Outstanding after such record date.

#### SECTION 105. NOTICES, ETC. TO TRUSTEE OR COMPANY.

Any request, demand, authorization, direction, notice, consent, election, waiver or Act of Holders or other document provided or permitted by this Indenture to be made upon, given or furnished to, or filed with, the Trustee by any Holder or by the Company, or the Company by the Trustee or by any Holder, shall be sufficient for every purpose hereunder (unless otherwise expressly provided herein) if in writing and delivered personally to an officer or other responsible employee of the addressee, or transmitted by facsimile transmission, telex or other direct written electronic means to the telephone number or other electronic communications address set forth for such party below or otherwise as such party shall from time to time designate, or transmitted by registered mail, charges prepaid, to the applicable address set forth for such party below or to such other address as such party may from time to time designate:



If to the Trustee, to:

Union Bank of California, N.A.  
475 Sansome Street, 12th Floor  
San Francisco, California 94111  
Attention: Corporate Trust Department  
Facsimile: (415) 296-6757

If to the Company, to:

Avista Corporation  
1411 East Mission Avenue  
Spokane, Washington 99202  
Attention: Assistant Treasurer  
Facsimile: (509) 482-4879

Any communication contemplated herein shall be deemed to have been made, given, furnished and filed if personally delivered, on the date of delivery, if transmitted by facsimile transmission, telex or other direct written electronic means, on the date of transmission, and if transmitted by registered mail, on the date of receipt.

SECTION 106. NOTICE TO HOLDERS OF SECURITIES; WAIVER.

Except as otherwise expressly provided herein, where this Indenture provides for notice to Holders of any event, such notice shall be sufficiently given, and shall be deemed given, to Holders if in writing and mailed, first-class postage prepaid, to each Holder affected by such event, at the address of such Holder as it appears in the Security Register, not later than the latest date, and not earlier than the earliest date, prescribed for the giving of such notice.

In case by reason of the suspension of regular mail service or by reason of any other cause it shall be impracticable to give such notice to Holders by mail, then such notification as shall be made with the approval of the Trustee shall constitute a sufficient notification for every purpose hereunder. In any case where notice to Holders is given by mail, neither the failure to mail such notice, nor any defect in any notice so mailed, to any particular Holder shall affect the sufficiency of such notice with respect to other Holders.

Any notice required by this Indenture may be waived in writing by the Person entitled to receive such notice, either before or after the event otherwise to be specified therein, and such waiver shall be the equivalent of such notice. Waivers of notice by Holders shall be filed with the Trustee, but such filing shall not be a condition precedent to the validity of any action taken in reliance upon such waiver.

SECTION 107. CONFLICT WITH TRUST INDENTURE ACT.

If any provision of this Indenture limits, qualifies or conflicts with another provision hereof which is required or deemed to be included in this Indenture by, or is otherwise governed by, any provision of the Trust Indenture Act, such other provision shall control; and if any provision hereof otherwise conflicts with the Trust Indenture Act, the Trust Indenture Act shall control.

SECTION 108. EFFECT OF HEADINGS AND TABLE OF CONTENTS.

The Article and Section headings in this Indenture and the Table of Contents are for convenience only and shall not affect the construction hereof.

SECTION 109. SUCCESSORS AND ASSIGNS.

All covenants and agreements in this Indenture by the Company shall bind its successors and assigns, whether so expressed or not.

SECTION 110. SEPARABILITY CLAUSE.

In case any provision in this Indenture or the Securities shall be held to be invalid, illegal or unenforceable, the validity, legality and enforceability of the remaining provisions shall not in any way be affected or impaired thereby.

SECTION 111. BENEFITS OF INDENTURE.

Nothing in this Indenture or the Securities, express or implied, shall give to any Person, other than the parties hereto, their successors hereunder and the Holders and, to the extent provided in Sections 104(a) and 716, registered holders of Trust Securities (other than Trust Securities initially issued and sold to the Company) and, so long as the notice described in Section 1413 shall not have been given, holders of Senior Indebtedness, any benefit or any legal or equitable right, remedy or claim under this Indenture, provided, however, that so long as any Preferred Securities remain outstanding, the holders of such Preferred Securities, subject to certain limitations set forth in this Indenture, may enforce the Company's obligations hereunder, directly against the Company, as third party beneficiaries of this Indenture without proceeding against the Trust issuing such Preferred Securities.

SECTION 112. GOVERNING LAW.

This Indenture and the Securities shall be governed by and construed in accordance with the law of the State of New York (including without limitation Section 5-1401 of the New York General Obligations Law or any successor to such statute), except to the extent that the Trust Indenture Act shall be applicable.

SECTION 113. LEGAL HOLIDAYS.

In any case where any Interest Payment Date, Redemption Date or Stated Maturity of any Security shall not be a Business Day at any Place of Payment, then (notwithstanding any other provision of this Indenture or of the Securities other than a contrary provision in the Securities of any series, or any Tranche thereof, or in the indenture supplemental hereto, Board Resolution or Officer's Certificate which establishes the terms of the Securities of such series or Tranche) payment of interest or principal and premium, if any, need not be made at such Place of Payment on such date, but may be made on the next succeeding Business Day at such Place of Payment with the same force and effect as if made on the Interest Payment Date or Redemption Date, or at the Stated Maturity, and, if such payment is made or duly provided for on such Business Day, no interest shall accrue on the amount so payable for the period from and after such Interest Payment Date, Redemption Date or Stated Maturity, as the case may be, to such Business Day.

## ARTICLE TWO

### SECURITY FORMS

#### SECTION 201. FORMS GENERALLY.

The definitive Securities of each series shall be in substantially the form or forms established in the Officer's Certificate, the indenture supplemental hereto or the Board Resolution establishing such series, in any case with such appropriate insertions, omissions, substitutions and other variations as are required or permitted by this Indenture, and may have such letters, numbers or other marks of identification and such legends or endorsements placed thereon as may be required to comply with the rules of any securities exchange or as may, consistently herewith, be determined by the officers executing such Securities, as evidenced by their execution thereof. If the form or forms of Securities of any series are established in an Officer's Certificate or a Board Resolution, such Officer's Certificate or Board Resolution shall be delivered to the Trustee at or prior to the delivery of the Company Order contemplated by Section 303 for the authentication and delivery of such Securities.

Unless otherwise specified as contemplated by Section 301 or 1101(f), the Securities of each series shall be issuable in registered form without coupons. The definitive Securities shall be produced in such manner as shall be determined by the officers executing such Securities, as evidenced by their execution thereof.

#### SECTION 202. FORM OF TRUSTEE'S CERTIFICATE OF AUTHENTICATION.

The Trustee's certificate of authentication shall be in substantially the form set forth below:

This is one of the Securities of the series designated therein referred to in the within-mentioned Indenture.

\_\_\_\_\_ as Trustee

By: \_\_\_\_\_  
Authorized Officer

ARTICLE THREE

THE SECURITIES

SECTION 301. AMOUNT UNLIMITED; ISSUABLE IN SERIES.

The aggregate principal amount of Securities which may be authenticated and delivered under this Indenture is unlimited.

The Securities may be issued from time to time in one or more series. Subject to the last paragraph of this Section, prior to the authentication and delivery of Securities of any series there shall be established by specification in an Officer's Certificate, a supplemental indenture or in a Board Resolution:

(a) the title of the Securities of such series (which shall distinguish the Securities of such series from Securities of all other series);

(b) any limit upon the aggregate principal amount of the Securities of such series which may be authenticated and delivered under this Indenture (except for Securities authenticated and delivered upon registration of transfer of, or in exchange for, or in lieu of, other Securities of such series pursuant to Section 304, 305, 306, 406 or 1106 and except for any Securities which, pursuant to Section 303, are deemed never to have been authenticated and delivered hereunder);

(c) the Persons (without specific identification) to whom interest, if any, on Securities of such series, or any Tranche thereof, shall be payable, if other than the Persons in whose names such Securities (or one or more Predecessor Securities) are registered at the close of business on the Regular Record Date for such interest;

(d) the date or dates on which the principal of the Securities of such series, or any Tranche thereof, is payable or any formulary or other method or other means by which such date or dates shall be determined, by reference to an index or

other fact or event ascertainable outside of this Indenture or otherwise (without regard to any provisions for redemption, prepayment, acceleration, purchase or extension); and the right, if any, to extend the Maturity of the Securities of such series, or any Tranche thereof, and the duration of any such extension;

(e) the rate or rates at which the Securities of such series, or any Tranche thereof, shall bear interest, if any (including the rate or rates at which overdue principal shall bear interest, and the right, if any, to extend the interest payment periods and the duration of any such extension; if different from the rate or rates at which such Securities shall bear interest prior to Maturity, and, if applicable, the rate or rates at which overdue premium or interest shall bear interest, if any), or any formula or other method or other means by which such rate or rates shall be determined by reference to an index or other fact or event ascertainable outside of this Indenture or otherwise; the date or dates from which such interest shall accrue; the Interest Payment Dates on which such interest shall be payable and the Regular Record Date, if any, for the interest payable on such Securities on any Interest Payment Date; the basis of computation of interest, if other than as provided in Section 310; and the right, if any, to extend the interest payment periods and the duration of any such extension;

(f) the place or places at which and/or the methods (if other than as provided elsewhere in this Indenture) by which (i) the principal of and premium, if any, and interest, if any, on Securities of such series, or any Tranche thereof, shall be payable, (ii) registration of transfer of Securities of such series, or any Tranche thereof, may be effected, (iii) exchanges of Securities of such series, or any Tranche thereof, may be effected and (iv) notices and demands to or upon the Company in respect of the Securities of such series, or any Tranche thereof, and this Indenture may be served; the Security Registrar and any Paying Agent or Agents for such series or Tranche; and, if such is the case, that the principal of such Securities shall be payable without the presentment or surrender thereof;

(g) the period or periods within which or the date or dates on which, the price or prices at which and the terms and conditions upon which the Securities of such series, or any Tranche thereof, may be redeemed, in whole or in part, at the option of the Company and any restrictions on such redemptions;

(h) the obligation or obligations, if any, of the Company to redeem or purchase the Securities of such series, or any Tranche thereof, pursuant to any sinking fund or other mandatory redemption provisions or at the option of a Holder thereof and the period or periods within which or the date or dates on which, the price or prices at which and the terms and conditions upon which such Securities shall be redeemed or purchased, in whole or in part, pursuant to such obligation, and

applicable exceptions to the requirements of Section 404 in the case of mandatory redemption or redemption at the option of the Holder;

(i) the denominations in which Securities of such series, or any Tranche thereof, shall be issuable if other than denominations of One Thousand Dollars (\$1,000) and any integral multiple thereof (in the case of Securities issued to a Trust or a trustee of such trust in connection with the issuance of Trust Securities by such Trust, the denomination in which such Securities shall be issuable if other than denominations of Twenty-Five Dollars (\$25) and any integral multiple thereof);

(j) the currency or currencies, including composite currencies, in which payment of the principal of or premium, if any, or interest, if any, on the Securities of such series, or any Tranche thereof, shall be payable (if other than in Dollars) and the formulary or other method or other means by which the equivalent of any such amount in Dollars is to be determined for any purpose, including for the purpose of determining the principal amount of such Securities deemed to be outstanding at any time;

(k) if the principal of or premium, if any, or interest, if any, on the Securities of such series, or any Tranche thereof, are to be payable, at the election of the Company or a Holder thereof, in a coin or currency other than that in which the Securities are stated to be payable, the period or periods within which, and the terms and conditions upon which, such election may be made;

(l) if the principal of or premium, if any, or interest, if any, on the Securities of such series, or any Tranche thereof, are to be payable, or are to be payable at the election of the Company or a Holder thereof, in securities or other property, the type and amount of such securities or other property, or the formulary or other method or other means by which such amount shall be determined, and the period or periods within which, and the terms and conditions upon which, any such election may be made;

(m) if the amount payable in respect of the principal of or premium, if any, or interest, if any, on the Securities of such series, or any Tranche thereof, may be determined with reference to an index or other fact or event ascertainable outside of this Indenture, the manner in which such amounts shall be determined (to the extent not established pursuant to clause (e) of this paragraph);

(n) if other than the entire principal amount thereof, the portion of the principal amount of Securities of such series, or any Tranche thereof, which shall be payable upon declaration of acceleration of the Maturity thereof pursuant to Section 702;

(o) the terms, if any, pursuant to which the Securities of such series, or any Tranche thereof, may be converted into or exchanged for shares of capital stock or other securities of the Company or any other Person;

(p) the obligations or instruments, if any, which shall be considered to be Eligible Obligations in respect of the Securities of such series, or any Tranche thereof, denominated in a currency other than Dollars or in a composite currency, and any additional or alternative provisions for the reinstatement of the Company's indebtedness in respect of such Securities after the satisfaction and discharge thereof as provided in Section 601;

(q) if the Securities of such series, or any Tranche thereof, are to be issued in global form, (i) any limitations on the rights of the Holder or Holders of such Securities to transfer or exchange the same or to obtain the registration of transfer thereof, (ii) any limitations on the rights of the Holder or Holders thereof to obtain certificates therefor in definitive form in lieu of temporary form and (iii) any and all other matters incidental to such Securities;

(r) if the Securities of such series, or any Tranche thereof, are to be issuable as bearer securities, any and all matters incidental thereto which are not specifically addressed in a supplemental indenture as contemplated by clause (f) of Section 1101;

(s) to the extent not established pursuant to clause (q) of this paragraph, any limitations on the rights of the Holders of the Securities of such Series, or any Tranche thereof, to transfer or exchange such Securities or to obtain the registration of transfer thereof; and if a service charge will be made for the registration of transfer or exchange of Securities of such series, or any Tranche thereof, the amount or terms thereof;

(t) any exceptions to Section 113, or variation in the definition of Business Day, with respect to the Securities of such series, or any Tranche thereof; and

(u) the designation of the Trust to which Securities of such series are to be issued;

(v) any other terms of the Securities of such series, or any Tranche thereof.

With respect to Securities of a series subject to a Periodic Offering, the Officer's Certificate, the indenture supplemental hereto or the Board Resolution which establishes such series, as the case may be, may provide general terms or parameters for Securities of such series and

provide either that the specific terms of Securities of such series, or any Tranche thereof, shall be specified in a Company Order or that such terms shall be determined by the Company or its agents in accordance with procedures specified in a Company Order as contemplated by clause (b) of Section 303.

Unless otherwise specified with respect to a series of Securities as contemplated by Section 301(b), any limit upon the aggregate principal amount of a series of Securities may be increased without the consent of any Holders and additional Securities of such series may be authenticated and delivered up to the limit upon the aggregate principal amount authorized with respect to such series as so increased.

Anything herein to the contrary notwithstanding, the Trustee shall be under no obligation to authenticate and deliver Securities of any series the terms of which, established as contemplated by this Section, would affect the rights, duties, obligations, liabilities or immunities of the Trustee under this Indenture or otherwise.

#### SECTION 302. DENOMINATIONS.

Unless otherwise provided as contemplated by Section 301 with respect to any series of Securities, or any Tranche thereof, the Securities of each series shall be issuable in denominations of One Thousand Dollars (\$1,000) and any integral multiple thereof (in the case of securities issued to a Trust or a trustee of such trust in connection with the issuance of Trust Securities by such Trust, the Securities of each series shall be issuable in denominations of Twenty-Five Dollars (\$25) and any integral multiple thereof).

#### SECTION 303. EXECUTION, DATING, AUTHENTICATION.

Unless otherwise specified as contemplated by Section 301 with respect to any series of Securities, or any Tranche thereof, the Securities shall be executed on behalf of the Company by an Authorized Officer, and may have the corporate seal of the Company affixed thereto or reproduced thereon and attested by its Secretary, one of its Assistant Secretaries or any other Authorized Officer. The signature of any or all of these officers on the Securities may be manual or facsimile.

Securities bearing the manual or facsimile signatures of individuals who were at the time of execution Authorized Officers shall bind the Company, notwithstanding that such individuals, or any of them, have ceased to be such Authorized Officers prior to the authentication and delivery of such Securities or were not such Authorized Officers at the date of such Securities.

The Trustee shall authenticate and deliver Securities of a series, for original issue, at one time or from time to time in accordance with the Company Order referred to below, upon receipt by the Trustee of:



(a) the instrument or instruments establishing the form or forms and terms of the Securities of such series, as provided in Sections 201 and 301;

(b) a Company Order requesting the authentication and delivery of such Securities and, to the extent that the terms of such Securities shall not have been established in an Officer's Certificate, an indenture supplemental hereto or in a Board Resolution, all as contemplated by Sections 201 and 301, either (i) establishing such terms or (ii) in the case of Securities of a series subject to a Periodic Offering, specifying procedures, acceptable to the Trustee, by which such terms are to be established (which procedures may provide, to the extent acceptable to the Trustee, for authentication and delivery pursuant to oral or electronic instructions from the Company or any agent or agents thereof, which oral instructions are to be promptly confirmed electronically or in writing), in either case in accordance with the instrument or instruments delivered pursuant to clause (a) above;

(c) the Securities of such series, each executed on behalf of the Company by an Authorized Officer;

(d) an Opinion of Counsel to the effect that:

(i) (A) the form or forms of such Securities have been duly authorized by the Company and (B) the forms of such Securities have been established in conformity with the provisions of this Indenture;

(ii) (A) the terms of such Securities have been duly authorized by the Company and (B) the terms of such Securities have been established in conformity with the provisions of this Indenture; and

(iii) when such Securities shall have been authenticated and delivered by the Trustee and issued and delivered by the Company in the manner and subject to any conditions specified in such Opinion of Counsel, such Securities will constitute valid obligations of the Company, entitled to the benefits provided by this Indenture equally and ratably with all other Securities then Outstanding;

provided, however, that, with respect to the Securities of a series subject to a Periodic Offering, the Trustee shall be entitled to receive such Opinion of Counsel only once at or prior to the time of the first authentication and delivery of the Securities of such series (provided that such Opinion of Counsel addresses the authentication and delivery of all Securities of such series) and that, in lieu of the opinions described in clauses (ii) and (iii) above, such Counsel may opine that:

(x) when the terms of such Securities shall have been established pursuant to a Company Order or Orders or pursuant to such procedures as may be specified from time to time by a Company Order or Orders, all as contemplated by and in accordance with the instrument or instruments delivered pursuant to clause (a) above, such terms will have been duly authorized by the Company and will have been established in conformity with the provisions of this Indenture; and

(y) when such Securities shall have been (1) authenticated and delivered by the Trustee in accordance with this Indenture and the Company Order or Orders or the specified procedures referred to in clause (x) above and (2) issued and delivered by the Company in the manner and subject to any conditions specified in such Opinion of Counsel, such Securities will constitute valid obligations of the Company, entitled to the benefits provided by this Indenture equally and ratably with all other Securities then Outstanding.

With respect to Securities of a series subject to a Periodic Offering, the Trustee may conclusively rely, as to the authorization by the Company of any of such Securities, the forms and terms thereof, the validity thereof and the compliance of the authentication and delivery thereof with the terms and conditions of this Indenture, upon the Opinion or Opinions of Counsel and the certificates and other documents delivered pursuant to this Article at or prior to the time of the first authentication and delivery of Securities of such series until any of such opinions, certificates or other documents have been superseded or revoked or expire by their terms. In connection with the authentication and delivery of Securities of a series subject to a Periodic Offering, the Trustee shall be entitled to assume that the Company's instructions to authenticate and deliver such Securities do not violate any applicable law or any applicable rule, regulation or order of any Governmental Authority having jurisdiction over the Company.

If the form or terms of the Securities of any series have been established by or pursuant to an Officer's Certificate or Board Resolution as permitted by Sections 201 or 301, the Trustee shall not be required to authenticate such Securities if the issuance of such Securities pursuant to this Indenture will adversely affect the Trustee's own rights, duties or immunities under the Securities and this Indenture or otherwise in a manner which is not reasonably acceptable to the Trustee.

Unless otherwise specified as contemplated by Section 301 with respect to any series of Securities, or any Tranche thereof, each Security shall be dated the date of the authentication of such Security.

Unless otherwise specified as contemplated by Section 301 with respect to any series of Securities, or any Tranche thereof, no Security shall be entitled to any benefit under this Indenture or be valid or obligatory for any purpose unless there appears on such Security a

certificate of authentication substantially in the form provided for herein executed by the Trustee or an Authenticating Agent by manual signature of an authorized officer thereof, and such certificate upon any Security shall be conclusive evidence, and the only evidence, that such Security has been duly authenticated and delivered hereunder and is entitled to the benefits of this Indenture. Notwithstanding the foregoing, if (a) any Security shall have been authenticated and delivered hereunder to the Company, or any Person acting on its behalf, but shall never have been issued and sold by the Company, (b) the Company shall deliver such Security to the Security Registrar for cancellation or shall cancel such Security and deliver evidence of such cancellation to the Trustee, in each case as provided in Section 309, and (c) the Company, at its election, shall deliver to the Trustee a written statement (which need not comply with Section 102 and need not be accompanied by an Officer's Certificate or an Opinion of Counsel) stating that such Security has never been issued and sold by the Company, then, for all purposes of this Indenture, such Security shall be deemed never to have been authenticated and delivered hereunder and shall never be entitled to the benefits hereof.

#### SECTION 304. TEMPORARY SECURITIES.

Pending the preparation of definitive Securities of any series, or any Tranche thereof, the Company may execute, and upon Company Order the Trustee shall authenticate and deliver, temporary Securities which are printed, lithographed, typewritten, mimeographed, photocopied or otherwise produced, in any authorized denomination, substantially of the tenor of the definitive Securities in lieu of which they are issued, with such appropriate insertions, omissions, substitutions and other variations as the officers executing such Securities may determine, as evidenced by their execution of such Securities; provided, however, that temporary Securities need not recite specific redemption, sinking fund, conversion or exchange provisions.

Except as otherwise specified as contemplated by Section 301 with respect to the Securities of any series, or any Tranche thereof, after the preparation of definitive Securities of such series or Tranche, the temporary Securities of such series or Tranche shall be exchangeable, without charge to the Holder thereof, for definitive Securities of such series or Tranche upon surrender of such temporary Securities at the office or agency of the Company maintained pursuant to Section 502 in a Place of Payment for such Securities. Upon such surrender of temporary Securities, the Company shall, except as aforesaid, execute and the Trustee shall authenticate and deliver in exchange therefor definitive Securities of the same series and Tranche, of authorized denominations and of like tenor and aggregate principal amount.

Until exchanged in full as hereinabove provided, temporary Securities shall in all respects be entitled to the same benefits under this Indenture as definitive Securities of the same series and Tranche and of like tenor authenticated and delivered hereunder.

#### SECTION 305. REGISTRATION, REGISTRATION OF TRANSFER AND EXCHANGE.

The Company shall cause to be kept in one of the offices designated pursuant to Section 502, with respect to the Securities of each series, or any Tranche thereof, a register (the "SECURITY REGISTER") in which, subject to such reasonable regulations as it may prescribe, the Company shall provide for the registration of Securities of such series or Tranche and the registration of transfer thereof. The Company shall designate one Person to maintain the Security Register for the Securities of each series and such Person is referred to herein, with respect to such series, as the "SECURITY REGISTRAR". Anything herein to the contrary notwithstanding, the Company may designate one or more of its offices or an office of any Affiliate as an office in which a register with respect to the Securities of one or more series, or any Tranche or Tranches thereof, shall be maintained, and the Company may designate itself or any Affiliate as the Security Registrar with respect to one or more of such series. The Security Register shall be open for inspection by the Trustee and the Company at all reasonable times.

Except as otherwise specified as contemplated by Section 301 with respect to the Securities of any series, or any Tranche thereof, upon presentment for registration of transfer of any Security of such series or Tranche at the office or agency of the Company maintained pursuant to Section 502 in a Place of Payment for such series or Tranche, and further upon satisfaction of any conditions prescribed by applicable law, the Company shall execute, and the Trustee shall authenticate and deliver, in the name of the designated transferee or transferees, one or more new Securities of the same series and Tranche, of authorized denominations and of like tenor and aggregate principal amount.

Except as otherwise specified as contemplated by Section 301 with respect to the Securities of any series, or any Tranche thereof, any Security of such series or Tranche may be exchanged at the option of the Holder, for one or more new Securities of the same series and Tranche, of authorized denominations and of like tenor and aggregate principal amount, upon presentment of the Securities to be exchanged at any such office or agency. Whenever any Securities are so presented for exchange and upon satisfaction of any conditions prescribed by applicable law, the Company shall execute, and the Trustee shall authenticate and deliver, the Securities which the Holder making the exchange is entitled to receive.

All Securities delivered upon any registration of transfer or exchange of Securities shall be valid obligations of the Company, evidencing the same respective obligations, and being entitled to the same benefits under this Indenture, as the Securities presented upon such registration of transfer or exchange.

Every Security presented for registration of transfer or for exchange shall (if so required by the Company, the Trustee or the Security Registrar) be duly endorsed or shall be accompanied by a written instrument of transfer in form satisfactory to the Company, and the Trustee or the Security Registrar, as the case may be, duly executed by the Holder thereof or his attorney duly authorized in writing.

Unless otherwise specified as contemplated by Section 301 with respect to Securities of any series, or any Tranche thereof, no service charge shall be made for any registration of transfer or exchange of Securities, but the Company may require payment of a sum sufficient to cover any tax or other governmental charge that may be imposed in connection with any registration of transfer or exchange of Securities, other than exchanges pursuant to Section 304, 406 or 1106 not involving any transfer.

The Company shall not be required to execute or to provide for the registration of transfer of or the exchange of (a) Securities of any series, or any Tranche thereof, during a period of fifteen (15) days immediately preceding the date notice is to be given identifying the serial numbers of the Securities of such series or Tranche called for redemption or (b) any Security so selected for redemption in whole or in part, except the unredeemed portion of any Security being redeemed in part.

#### SECTION 306. MUTILATED, DESTROYED, LOST AND STOLEN SECURITIES.

If any mutilated Security is presented to the Trustee, the Company shall execute and the Trustee shall authenticate and deliver in exchange therefor a new Security of the same series and Tranche, and of like tenor and principal amount and bearing a number not contemporaneously outstanding.

If there shall be delivered to the Company and the Trustee (a) evidence to their satisfaction of the ownership of and the destruction, loss or theft of any Security and (b) such security or indemnity as may be reasonably required by them to save each of them and any agent of any of them harmless, then, in the absence of notice to the Company or the Trustee that such Security is held by a Person deemed to be a protected purchaser under applicable law, the Company shall execute and the Trustee shall authenticate and deliver, in lieu of any such destroyed, lost or stolen Security, a new Security of the same series and Tranche, and of like tenor and principal amount and bearing a number not contemporaneously outstanding.

Notwithstanding the foregoing, in case any such mutilated, destroyed, lost or stolen Security has become or is about to become due and payable, the Company in its discretion may, but subject to compliance with the conditions set forth in the next preceding paragraph, instead of issuing a new Security, pay such Security.

Upon the issuance of any new Security under this Section, the Company may require the payment of a sum sufficient to cover any tax or other governmental charge that may be imposed in relation thereto and any other reasonable expenses (including the fees and expenses of the Trustee) in connection therewith.

Every new Security of any series issued pursuant to this Section in lieu of any destroyed, lost or stolen Security shall constitute an original additional contractual obligation of the Company, whether or not the destroyed, lost or stolen Security shall be at any time enforceable by

anyone other than the Holder of such new Security, and any such new Security shall be entitled to all the benefits of this Indenture equally and ratably with any and all other Securities of such series duly issued hereunder.

The provisions of this Section are exclusive and shall preclude (to the extent lawful) all other rights and remedies with respect to the replacement or payment of mutilated, destroyed, lost or stolen Securities.

SECTION 307. PAYMENT OF INTEREST; INTEREST RIGHTS PRESERVED.

Unless otherwise specified as contemplated by Section 301 with respect to the Securities of any series, or any Tranche thereof, interest on any Security which is payable, and is punctually paid or duly provided for, on any Interest Payment Date shall be paid to the Person in whose name that Security (or one or more Predecessor Securities) is registered at the close of business on the Regular Record Date for such interest.

Any interest on any Security of any series which is payable, but is not punctually paid or duly provided for, on any Interest Payment Date, including without limitation interest the payment period for which has been extended as specified with respect to such series as contemplated by Section 301 (herein called "UNPAID INTEREST"), shall forthwith cease to be payable to the Holder on the related Regular Record Date by virtue of having been such Holder, and such Unpaid Interest may be paid by the Company, at its election in each case, as provided in clause (a) or (b) below:

(a) The Company may elect to make payment of any Unpaid Interest to the Persons in whose names the Securities of such series (or their respective Predecessor Securities) are registered at the close of business on a date (herein called a "SPECIAL RECORD DATE") for the payment of such Unpaid Interest, which shall be fixed in the following manner. The Company shall notify the Trustee in writing of the amount of Unpaid Interest proposed to be paid on each Security of such series and the date of the proposed payment, and at the same time the Company shall deposit with the Trustee an amount of money equal to the aggregate amount proposed to be paid in respect of such Unpaid Interest or shall make arrangements satisfactory to the Trustee for such deposit prior to the date of the proposed payment, such money when deposited to be held in trust for the benefit of the Persons entitled to such Unpaid Interest as in this clause provided. Thereupon the Trustee shall fix a Special Record Date for the payment of such Unpaid Interest which shall be not more than thirty (30) days and not less than ten (10) days prior to the date of the proposed payment and not less than twenty-five (25) days after the receipt by the Trustee of the notice of the proposed payment. The Trustee shall promptly notify the Company of such Special Record Date and, in the name and at the expense of the Company, shall, not less than fifteen (15) days prior to such Special Record Date, cause notice of the proposed payment of such Unpaid Interest and the Special Record

Date therefor to be mailed, first-class postage prepaid, to each Holder of Securities of such series at the address of such Holder as it appears in the Security Register. Notice of the proposed payment of such Unpaid Interest and the Special Record Date therefor having been so mailed, such Unpaid Interest shall be paid to the Persons in whose names the Securities of such series (or their respective Predecessor Securities) are registered at the close of business on such Special Record Date.

(b) The Company may make payment of any Unpaid Interest on the Securities of any series in any other lawful manner not inconsistent with the requirements of any securities exchange on which such Securities may be listed, and upon such notice as may be required by such exchange, if, after notice given by the Company to the Trustee of the proposed payment pursuant to this clause, such manner of payment shall be deemed practicable by the Trustee.

Subject to the foregoing provisions of this Section and Section 305, each Security delivered under this Indenture upon registration of transfer of or in exchange for or in lieu of any other Security shall carry the rights to interest accrued and unpaid, and to accrue, which were carried by such other Security.

#### SECTION 308. PERSONS DEEMED OWNERS.

Prior to the due presentation of any Security for registration of transfer, the Company, the Trustee and any agent of the Company or the Trustee may treat the Person in whose name such Security is registered as the absolute owner of such Security (subject to Sections 305 and 307) for the purpose of receiving payment of principal of and premium, if any, and interest, if any, on such Security and for all other purposes whatsoever, whether or not such Security be overdue, and neither the Company, nor the Trustee, or any agent of the Company or the Trustee shall be affected by notice to the contrary.

#### SECTION 309. CANCELLATION BY SECURITY REGISTRAR.

All Securities presented for payment, redemption, registration of transfer or exchange shall, if presented to any Person other than the Security Registrar, be delivered to the Security Registrar and, if not theretofore canceled, shall be promptly canceled by the Security Registrar. The Company may at any time deliver to the Security Registrar for cancellation any Securities previously authenticated and delivered hereunder which the Company may have acquired in any manner whatsoever or which the Company shall not have issued and sold, and all Securities so delivered shall be promptly canceled by the Security Registrar. Unless by a Company Order the Company shall direct that canceled Securities be returned to it, all canceled Securities held by the Security Registrar shall be disposed of in accordance with the Security Registrar's customary procedures. The Security Registrar shall promptly deliver to the Company and the Trustee evidence of any cancellation by it of a Security, and of any disposition by it of a canceled Security, in accordance with this Section 309 to the Trustee and the Company.

SECTION 310. COMPUTATION OF INTEREST.

Except as otherwise specified as contemplated by Section 301 for Securities of any series, or any Tranche thereof, interest on the Securities of each series shall be computed on the basis of a three hundred sixty (360) day year consisting of twelve (12) thirty (30) day months and, with respect to any period less than a full calendar month, on the basis of the actual number of days elapsed during such period.

SECTION 311. PAYMENT TO BE IN PROPER CURRENCY.

In the case of the Securities of any series, or any Tranche thereof, denominated in any currency other than Dollars or in a composite currency (the "REQUIRED CURRENCY"), except as otherwise specified with respect to such Securities as contemplated by Section 301, the obligation of the Company to make any payment of the principal thereof, or the premium, if any, or interest, if any, thereon, shall not be discharged or satisfied by any tender by the Company, or recovery by the Trustee, in any currency other than the Required Currency, except to the extent that such tender or recovery shall result in the Trustee timely holding the full amount of the Required Currency then due and payable. If any such tender or recovery is in a currency other than the Required Currency, the Trustee may take such actions as it considers appropriate to exchange such currency for the Required Currency. The costs and risks of any such exchange, including without limitation the risks of delay and exchange rate fluctuation, shall be borne by the Company and the Company shall remain fully liable for any shortfall or delinquency in the full amount of Required Currency then due and payable, and in no circumstances shall the Trustee be liable therefor except in the case of its negligence or willful misconduct.

ARTICLE FOUR

REDEMPTION OF SECURITIES

SECTION 401. APPLICABILITY OF ARTICLE.

Securities of any series, or any Tranche thereof, which are redeemable before their Stated Maturity shall be redeemable in accordance with their terms and (except as otherwise specified as contemplated by Section 301 for Securities of such series or Tranche) in accordance with this Article.

SECTION 402. ELECTION TO REDEEM; NOTICE TO TRUSTEE.

The election of the Company to redeem any Securities shall be evidenced by a Board Resolution or an Officer's Certificate. The Company shall, at least forty-five (45) days prior to the Redemption Date fixed by the Company (unless a shorter notice shall be satisfactory to the Trustee), notify the Trustee and in the case of Securities of a Series held by a Trust, the Institutional Trustee under the related Declaration establishing such Trust in writing of such Redemption Date



and of the principal amount of such Securities to be redeemed. In the case of any redemption of Securities (a) prior to the expiration of any restriction on such redemption provided in the terms of such Securities or elsewhere in this Indenture or (b) pursuant to an election of the Company which is subject to a condition specified in the terms of such Securities, the Company shall furnish the Trustee with an Officer's Certificate evidencing compliance with such restriction or condition.

#### SECTION 403. SELECTION OF SECURITIES TO BE REDEEMED.

If less than all the Securities of any series, or any Tranche thereof, are to be redeemed, the particular Securities to be redeemed shall be selected by the Security Registrar from the Outstanding Securities of such series or Tranche not previously called for redemption, by such method as shall be provided for such series or Tranche, or, in the absence of any such provision, by such method of random selection as the Security Registrar shall deem fair and appropriate and which may, in any case, provide for the selection for redemption of portions (in any authorized denomination for Securities of such series or Tranche) of the principal amount of Securities of such series or Tranche having a denomination larger than the minimum authorized denomination for Securities of such series or Tranche; provided, however, that if, as indicated in an Officer's Certificate, the Company shall have offered to purchase all or any principal amount of the Securities then Outstanding of any series, or any Tranche thereof, and less than all of such Securities as to which such offer was made shall have been tendered to the Company for such purchase, the Security Registrar, if so directed by Company Order, shall select for redemption all or any principal amount of such Securities which have not been so tendered.

The Security Registrar shall promptly notify the Company and the Trustee in writing of the Securities selected for redemption and, in the case of any Securities selected to be redeemed in part, the principal amount thereof to be redeemed.

For all purposes of this Indenture, unless the context otherwise requires, all provisions relating to the redemption of Securities shall relate, in the case of any Securities redeemed or to be redeemed only in part, to the portion of the principal amount of such Securities which has been or is to be redeemed.

#### SECTION 404. NOTICE OF REDEMPTION.

Notice of redemption shall be given in the manner provided in Section 106 to the Holders of the Securities to be redeemed not less than thirty (30) nor more than sixty (60) days prior to the Redemption Date.

All notices of redemption shall state:

- (a) the Redemption Date,
- (b) the Redemption Price,

(c) if less than all the Securities of any series or Tranche are to be redeemed, the identification of the particular Securities to be redeemed and the portion of the principal amount of any Security to be redeemed in part,

(d) that on the Redemption Date the Redemption Price, together with accrued interest, if any, to the Redemption Date, will become due and payable upon each such Security to be redeemed and, if applicable, that interest thereon will cease to accrue on and after said date,

(e) the place or places where such Securities are to be surrendered for payment of the Redemption Price and accrued interest, if any, unless it shall have been specified as contemplated by Section 301 with respect to such Securities that such surrender shall not be required,

(f) that the redemption is for a sinking or other fund, if such is the case, and

(g) such other matters as the Company shall deem desirable or appropriate.

With respect to any notice of redemption of Securities at the election of the Company, unless, upon the giving of such notice, such Securities shall be deemed to have been paid in accordance with Section 601, such notice may state that such redemption shall be conditional upon the receipt by the Paying Agent or Agents for such Securities, on or prior to the date fixed for such redemption, of money sufficient to pay the principal of and premium, if any, and interest, if any, on such Securities and that if such money shall not have been so received such notice shall be of no force or effect and the Company shall not be required to redeem such Securities. In the event that such notice of redemption contains such a condition and such money is not so received, the redemption shall not be made and within a reasonable time thereafter notice shall be given, in the manner in which the notice of redemption was given, that such money was not so received and such redemption was not required to be made, and the Paying Agent or Agents for the Securities otherwise to have been redeemed shall promptly return to the Holders thereof any of such Securities which had been surrendered for payment upon such redemption.

Notice of redemption of Securities to be redeemed at the election of the Company, and any notice of non-satisfaction of a condition for redemption as aforesaid, shall be given by the Company or, at the Company's Request, by the Security Registrar in the name and at the expense of the Company. Notice of mandatory redemption of Securities shall be given by the Security Registrar in the name and at the expense of the Company.

SECTION 405. SECURITIES PAYABLE ON REDEMPTION DATE.

Notice of redemption having been given as aforesaid, and the conditions, if any, set forth in such notice having been satisfied, the Securities or portions thereof so to be redeemed shall, on the Redemption Date, become due and payable at the Redemption Price therein specified, and from and after such date (unless, in the case of an unconditional notice of redemption, the Company shall default in the payment of the Redemption Price and accrued interest, if any) such Securities or portions thereof, if interest-bearing, shall cease to bear interest. Upon surrender of any such Security for redemption in accordance with such notice, such Security or portion thereof shall be paid by the Company at the Redemption Price, together with accrued interest, if any, to the Redemption Date; provided, however, that no such surrender shall be a condition to such payment if so specified as contemplated by Section 301 with respect to such Security; and provided, further, that, except as otherwise specified as contemplated by Section 301 with respect to such Security, any installment of interest on any Security the Stated Maturity of which installment is on or prior to the Redemption Date shall be payable to the Holder of such Security, or one or more Predecessor Securities, registered as such at the close of business on the related Regular Record Date according to the terms of such Security and subject to the provisions of Sections 305 and 307.

#### SECTION 406. SECURITIES REDEEMED IN PART.

Upon the surrender of any Security which is to be redeemed only in part at a Place of Payment therefor (with, if the Company or the Trustee so requires, due endorsement by, or a written instrument of transfer in form satisfactory to the Company or the Trustee, as the case may be, duly executed by, the Holder thereof or his attorney duly authorized in writing), the Company shall execute, and the Trustee shall authenticate and deliver to the Holder of such Security, without service charge, a new Security or Securities of the same series and Tranche, of any authorized denomination requested by such Holder and of like tenor and in aggregate principal amount equal to and in exchange for the unredeemed portion of the principal of the Security so surrendered.

### ARTICLE FIVE

#### COVENANTS

#### SECTION 501. PAYMENT OF SECURITIES.

The Company shall pay the principal of and premium, if any, and interest, if any, on the Securities of each series in accordance with the terms of such Securities and this Indenture.

#### SECTION 502. MAINTENANCE OF OFFICE OR AGENCY.

The Company shall maintain in each Place of Payment for the Securities of each series, or any Tranche thereof, an office or agency where payment of such Securities shall be made, where the registration of transfer or exchange of such Securities may be effected and where notices and demands to or upon the Company in respect of such Securities and this Indenture may be served. The Company shall give prompt written notice to the Trustee of the location, and any

change in the location, of each such office or agency and prompt notice to the Holders of any such change in the manner specified in Section 106. If at any time the Company shall fail to maintain any such required office or agency in respect of Securities of any series, or any Tranche thereof, or shall fail to furnish the Trustee with the address thereof, payment of such Securities shall be made, registration of transfer or exchange thereof may be effected and notices and demands in respect thereof may be served at the Corporate Trust Office of the Trustee, and the Company hereby appoints the Trustee as its agent for all such purposes in any such event.

The Company may also from time to time designate one or more other offices or agencies with respect to the Securities of one or more series, or any Tranche thereof, for any or all of the foregoing purposes and may from time to time rescind such designations; provided, however, that, unless otherwise specified as contemplated by Section 301 with respect to the Securities of such series or Tranche, no such designation or rescission shall in any manner relieve the Company of its obligation to maintain an office or agency for such purposes in each Place of Payment for such Securities in accordance with the requirements set forth above. The Company shall give prompt written notice to the Trustee, and prompt notice to the Holders in the manner specified in Section 106, of any such designation or rescission and of any change in the location of any such other office or agency.

Anything herein to the contrary notwithstanding, any office or agency required by this Section may be maintained at an office of the Company or any Affiliate thereof, in which event the Company or such Affiliate, as the case may be, shall perform all functions to be performed at such office or agency.

#### SECTION 503. MONEY FOR SECURITIES PAYMENTS TO BE HELD IN TRUST.

If the Company shall at any time act as its own Paying Agent with respect to the Securities of any series, or any Tranche thereof, it shall, on or before each due date of the principal of and premium, if any, and interest, if any, on any of such Securities, segregate and hold in trust for the benefit of the Persons entitled thereto a sum sufficient to pay the principal and premium or interest so becoming due until such sums shall be paid to such Persons or otherwise disposed of as herein provided. The Company shall promptly notify the Trustee of any failure by the Company (or any other obligor on such Securities) to make any payment of principal of or premium, if any, or interest, if any, on such Securities.

Whenever the Company shall have one or more Paying Agents for the Securities of any series, or any Tranche thereof, it shall, on or before each due date of the principal of and premium, if any, and interest, if any, on such Securities, deposit with such Paying Agents sums sufficient (without duplication) to pay the principal and premium or interest so becoming due, such sums to be held in trust for the benefit of the Persons entitled to such principal, premium or interest, and (unless such Paying Agent is the Trustee) the Company shall promptly notify the Trustee of any failure by it so to act.

The Company shall cause each Paying Agent for the Securities of any series, or any Tranche thereof, other than the Company or the Trustee, to execute and deliver to the Trustee an instrument in which such Paying Agent shall agree with the Trustee, subject to the provisions of this Section, that such Paying Agent shall:

(a) hold all sums held by it for the payment of the principal of and premium, if any, or interest, if any, on such Securities in trust for the benefit of the Persons entitled thereto until such sums shall be paid to such Persons or otherwise disposed of as herein provided;

(b) give the Trustee notice of any failure by the Company (or any other obligor upon such Securities) to make any payment of principal of or premium, if any, or interest, if any, on such Securities; and

(c) at any time during the continuance of any such failure, upon the written request of the Trustee, forthwith pay to the Trustee all sums so held in trust by such Paying Agent and furnish to the Trustee such information as it possesses regarding the names and addresses of the Persons entitled to such sums.

The Company may at any time pay, or by Company Order direct any Paying Agent to pay, to the Trustee all sums held in trust by the Company or such Paying Agent, such sums to be held by the Trustee upon the same trusts as those upon which such sums were held by the Company or such Paying Agent and, if so stated in a Company Order delivered to the Trustee, in accordance with the provisions of Article Six; and, upon such payment by any Paying Agent to the Trustee, such Paying Agent shall be released from all further liability with respect to such money.

Any money deposited with the Trustee or any Paying Agent, or then held by the Company, in trust for the payment of the principal of and premium, if any, or interest, if any, on any Security and remaining unclaimed for two years after such principal and premium, if any, or interest, if any, has become due and payable shall be paid to the Company on Company Request, or, if then held by the Company, shall be discharged from such trust; and, upon such payment or discharge, the Holder of such Security shall, as an unsecured general creditor and not as the Holder of an Outstanding Security, look only to the Company for payment of the amount so due and payable and remaining unpaid (subject, however, to the provisions of Article Fourteen), and all liability of the Trustee or such Paying Agent with respect to such trust money, and all liability of the Company as trustee thereof, shall thereupon cease; provided, however, that the Trustee or such Paying Agent, before being required to make any such payment to the Company, may at the expense of the Company cause to be mailed, on one occasion only, notice to such Holder that such money remains unclaimed and that, after a date specified therein, which shall not be less than thirty (30) days from the date of such mailing, any unclaimed balance of such money then remaining will be paid to the Company.

SECTION 504. CORPORATE EXISTENCE.

Subject to the rights of the Company under Article Ten, the Company shall do or cause to be done all things necessary to preserve and keep its corporate existence in full force and effect.

SECTION 505. MAINTENANCE OF PROPERTIES .

The Company shall cause (or, with respect to property owned in common with others, make reasonable efforts to cause) all its properties used or useful in the conduct of its businesses, considered as a whole, to be maintained and kept in good condition, repair and working order and shall cause (or, with respect to property owned in common with others, make reasonable effort to cause) to be made such repairs, renewals, replacement, betterments and improvements thereof, as, in the judgment of the Company, may be necessary in order that the operation of such properties, considered as a whole, may be conducted in accordance with common industry practice; provided, however, that nothing in this section shall prevent the Company from discontinuing, or causing the discontinuance of, the operation and maintenance of any of its properties; and provided, further, that nothing in this Section shall prevent the Company from selling, transferring or otherwise disposing of, or causing the sale, transfer or other disposition of any of its properties.

SECTION 506. WAIVER OF CERTAIN COVENANTS.

The Company may omit in any particular instance to comply with any term, provision or condition set forth in

(a) any covenant or restriction specified with respect to the Securities of any one or more series, or any Tranche or Tranches thereof, as contemplated by Section 301, or by Section 1201(b) if before the time for such compliance the Holders of a majority in aggregate principal amount of the Outstanding Securities of all series and Tranches with respect to which compliance with such covenant or restriction is to be omitted, considered as one class, shall, by Act of such Holders, either waive such compliance in such instance or generally waive compliance with such term, provision or condition; provided, however, that no such waiver shall be effective as to any matters contemplated in clause (a), (b) or (c) in Section 1102 without consent of the Holders specified in such Section; and

(b) Section 504 or Article Ten if before the time for such compliance the Holders of a majority in principal amount of Securities Outstanding under this Indenture shall, by Act of such Holders, either waive such compliance in such instance or generally waive compliance with such term, provision or condition;

but, in either case, no such waiver shall extend to or affect such term, provision or condition except to the extent so expressly waived, and, until such waiver shall become effective, the obligations of the Company and the duties of the Trustee in respect of any such term, provision or condition shall remain in full force and effect; provided, however, so long as a Trust holds Securities of any series,

such Trust may not waive compliance or waive any default in compliance by the Company with any covenant or other term contained in this Indenture or the Securities of such series without the approval of the holders of at least a majority in aggregate liquidation preference of the outstanding Trust Securities issued by such Trust, obtained as provided in the Declaration pertaining to such Trust.

#### SECTION 507. ANNUAL OFFICER'S CERTIFICATE AS TO COMPLIANCE.

Not later than December 1 in each year, commencing December 1, 2004, the Company shall deliver to the Trustee an Officer's Certificate which need not comply with Section 102, executed by the principal executive officer, the principal financial officer or the principal accounting officer of the Company, as to such officer's knowledge of the Company's compliance with all conditions and covenants under this Indenture, such compliance to be determined without regard to any period of grace or requirement of notice under this Indenture.

#### SECTION 508. RESTRICTION ON PAYMENT OF DIVIDENDS, ETC.

So long as any preferred securities of any series remain outstanding, if, at any time (a) there shall have occurred and be continuing an Event of Default described in clause (a) or (b) of Section 701 with respect to the Securities of any series, (b) the Company shall have elected to extend any interest payment period as specified with respect to the Securities of any series, or any Tranche thereof, as contemplated by Section 301 and any such period, as so extended, shall be continuing, or (c) the Company shall be in default in respect of its payment or other obligations under the Trust Securities Guarantee relating to any Trust Securities (other than Trust Securities initially issued and sold to the Company), then the Company shall not (x) declare or pay any dividend on, make any distribution or liquidation payment with respect to, or redeem, purchase or exchange any of its capital stock, (y) make any payment of principal, premium, if any, or interest, if any, on or repay, repurchase or redeem any debt securities (including other Securities) that rank pari passu with or junior in right of payment to the Securities and (z) make any guarantee payments with respect to any of the foregoing (other than payments under the Trust Securities Guarantee); provided, however, that nothing in this Section shall be deemed to prohibit (i) dividends or distributions payable in shares of the Company's capital stock, or in the form of warrants, options or other rights, where the dividend or distributed stock issuable upon exercise of the warrants, options or other rights are the same stock as that on which the dividend is being paid or is pari passu or junior to the stock, (ii) reclassification of the Company's capital stock or exchange or conversion of shares of one class or series of the Company's capital stock into shares of another class or series of the Company's capital stock, (iii) purchases or other acquisitions of fractional interests in shares of the Company's capital stock pursuant to the conversion or exchange provisions of the capital stock or the security being converted or exchanged; (iv) redemption, purchases or other acquisitions of the Company's capital stock in connection with the satisfaction by the Company of its obligations under provisions of the Company's Restated Articles of Incorporation, as amended, under any direct purchase, dividend reinvestment, customer purchase or employee benefit plans or under any contract or security requiring the Company to purchase shares of its capital stock; and (v) payments

under any Trust Securities Guarantee executed and delivered by the Company concurrently with the issuance of any Preferred Securities.

#### SECTION 509. AVA CAPITAL TRUST III.

If Securities of any series are issued and delivered to a Trust (or a trustee thereof) in connection with the issuance by such trust of Trust Securities, so long as such Trust Securities remain outstanding the Company shall (a) maintain 100% direct ownership, by the Company or any Affiliate thereof, of the Common Securities initially issued and sold to the Company by such Trust, except as otherwise provided in Section 1005, and (b) use all reasonable efforts to cause such Trust (i) to maintain its existence as a business trust, except in connection with a distribution of Securities, with the redemption, purchase or other acquisition and retirement of all Trust Securities of such trust or with certain mergers, consolidations or other business combinations, in each case as permitted by the Declaration establishing such Trust, and (ii) to otherwise continue not to be treated as an association taxable as a corporation for United States federal income tax purposes.

#### SECTION 510. HOLDERS OF PREFERRED SECURITIES

The Company agrees that, for so long as any Preferred Securities remain outstanding, its obligations under this Indenture will also be for the benefit of the holders from time to time of Preferred Securities, and the Company acknowledges and agrees that such holders will be entitled to enforce this Indenture, as third party beneficiaries, directly against the Company to the same extent as if such holders of Preferred Securities held a principal amount of Securities equal to the stated liquidation preference of the Preferred Securities held by such holders.

### ARTICLE SIX

#### SATISFACTION AND DISCHARGE

#### SECTION 601. SATISFACTION AND DISCHARGE OF SECURITIES.

Any Security or Securities, or any portion of the principal amount thereof, shall be deemed to have been paid for all purposes of this Indenture, and the entire indebtedness of the Company in respect thereof shall be satisfied and discharged, if there shall have been irrevocably deposited with the Trustee or any Paying Agent (other than the Company), in trust:

(a) money in an amount which shall be sufficient, or

(b) in the case of a deposit made prior to the Maturity of such Securities or portions thereof, Eligible Obligations, which shall not contain provisions permitting the redemption or other prepayment thereof at the option of the issuer thereof, the principal of and the interest on which when due, without any regard to



reinvestment thereof, will provide moneys which, together with the money, if any, deposited with or held by the Trustee or such Paying Agent, shall be sufficient, or

(c) a combination of (a) or (b) which shall be sufficient,

to pay when due the principal of and premium, if any, and interest, if any, due and to become due on such Securities or portions thereof; provided, however, that in the case of the provision for payment or redemption of less than all the Securities of any series or Tranche, such Securities or portions thereof shall have been selected by the Security Registrar as provided herein and, in the case of a redemption, the notice requisite to the validity of such redemption shall have been given or irrevocable authority shall have been given by the Company to the Trustee to give such notice, under arrangements satisfactory to the Trustee; and provided, further, that the Company shall have delivered to the Trustee and such Paying Agent:

(x) if such deposit shall have been made prior to the Maturity of such Securities, a Company Order stating that the money and Eligible Obligations deposited in accordance with this Section shall be held in trust, as provided in Section 603;

(y) if Eligible Obligations shall have been deposited, an Opinion of Counsel to the effect that such obligations constitute Eligible Obligations and do not contain provisions permitting the redemption or other prepayment thereof at the option of the issuer thereof, and an opinion of an independent public accountant of nationally recognized standing, selected by the Company, to the effect that the other requirements set forth in clause (b) and, if applicable, (c) above have been satisfied; and

(z) if such deposit shall have been made prior to the Maturity of such Securities, an Officer's Certificate stating the Company's intention that, upon delivery of such Officer's Certificate, its indebtedness in respect of such Securities or portions thereof will have been satisfied and discharged as contemplated in this Section.

Upon the deposit of money or Eligible Obligations, or both, in accordance with this Section, together with the documents required by clauses (x), (y) and (z) above, the Trustee shall, upon Company Request, acknowledge in writing that such Securities or portions thereof are deemed to have been paid for all purposes of this Indenture and that the entire indebtedness of the Company in respect thereof has been satisfied and discharged as contemplated in this Section. In the event that all of the conditions set forth in the preceding paragraph shall have been satisfied in respect of any Securities or portions thereof except that, for any reason, the Officer's Certificate specified in clause (z) (if otherwise required) shall not have been delivered, such Securities or portions thereof shall nevertheless be deemed to have been paid for all purposes of this Indenture, and the Holders of such Securities or portions thereof shall nevertheless be no longer entitled to the benefits provided

by this Indenture or of any of the covenants of the Company under Article Five (except the covenants contained in Sections 502 and 503) or any other covenants made in respect of such Securities or portions thereof as contemplated by Section 301 or Section 1201(b), but the indebtedness of the Company in respect of such Securities or portions thereof shall not be deemed to have been satisfied and discharged prior to Maturity for any other purpose; and, upon Company Request, the Trustee shall acknowledge in writing that such Securities or portions thereof are deemed to have been paid for all purposes of this Indenture.

If payment at Stated Maturity of less than all of the Securities of any series, or any Tranche thereof, is to be provided for in the manner and with the effect provided in this Section, the Security Registrar shall select such Securities, or portions of principal amount thereof, in the manner specified by Section 403 for selection for redemption of less than all the Securities of a series or Tranche.

In the event that Securities which shall be deemed to have been paid for purposes of this Indenture, and, if such is the case, in respect of which the Company's indebtedness shall have been satisfied and discharged, all as provided in this Section, do not mature and are not to be redeemed within the sixty (60) day period commencing with the date of the deposit of moneys or Eligible Obligations, as aforesaid, the Company shall, as promptly as practicable, give a notice, in the same manner as a notice of redemption with respect to such Securities, to the Holders of such Securities to the effect that such deposit has been made and the effect thereof.

Notwithstanding that any Securities shall be deemed to have been paid for purposes of this Indenture, as aforesaid, the obligations of the Company and the Trustee in respect of such Securities under Sections 304, 305, 306, 404, 502, 503, 807 and 814 and this Article shall survive.

The Company shall pay, and shall indemnify the Trustee or any Paying Agent with which Eligible Obligations shall have been deposited as provided in this Section against, any tax, fee or other charge imposed on or assessed against such Eligible Obligations or the principal or interest received in respect of such Eligible Obligations, including, but not limited to, any such tax payable by any entity deemed, for tax purposes, to have been created as a result of such deposit.

Anything herein to the contrary notwithstanding, (a) if, at any time after a Security would be deemed to have been paid for purposes of this Indenture, and, if such is the case, the Company's indebtedness in respect thereof would be deemed to have been satisfied and discharged, pursuant to this Section (without regard to the provisions of this paragraph), the Trustee or any Paying Agent, as the case may be, (i) shall be required to return the money or Eligible Obligations, or combination thereof, deposited with it as aforesaid to the Company or any representative thereof, under any applicable Federal or State bankruptcy, insolvency or other similar law or (ii) are unable to apply any money held by the Trustee as provided in this Section with respect to such Security by reason of any order or judgment of any court or governmental authority enjoining, restraining or otherwise prohibiting such application, such Security shall thereupon be deemed retroactively not to have been paid and any satisfaction and discharge of the Company's indebtedness in respect thereof

shall retroactively be deemed not to have been effected, and such Security shall be deemed to remain Outstanding and (b) any satisfaction and discharge of the Company's indebtedness in respect of any Security shall be subject to the provisions of the last paragraph of Section 503.

SECTION 602. SATISFACTION AND DISCHARGE OF INDENTURE.

This Indenture shall upon Company Request cease to be of further effect (except as hereinafter expressly provided), and the Trustee, at the expense of the Company, shall execute such instruments as the Company shall reasonably request to evidence and acknowledge the satisfaction and discharge of this Indenture, when:

- (a) no Securities remain Outstanding hereunder; and
- (b) the Company has paid or caused to be paid all other sums payable hereunder by the Company;

provided, however, that if, in accordance with the last paragraph of Section 601, any Security, previously deemed to have been paid for purposes of this Indenture, shall be deemed retroactively not to have been so paid, this Indenture shall thereupon be deemed retroactively not to have been satisfied and discharged, as aforesaid, and to remain in full force and effect, and the Company shall execute and deliver such instruments as the Trustee shall reasonably request to evidence and acknowledge the same.

Notwithstanding the satisfaction and discharge of this Indenture as aforesaid, the obligations of the Company and the Trustee under Sections 304, 305, 306, 404, 502, 503, 807 and 814 and this Article shall survive.

Upon satisfaction and discharge of this Indenture as provided in this Section, the Trustee shall turn over to the Company any and all money, securities and other property then held by the Trustee for the benefit of the Holders of the Securities (other than money and Eligible Obligations held by the Trustee pursuant to Section 603) and shall execute and deliver to the Company such instruments as, in the judgment of the Company, shall be necessary, desirable or appropriate to effect or evidence the satisfaction and discharge of this Indenture.

SECTION 603. APPLICATION OF TRUST MONEY.

Neither the Eligible Obligations nor the money deposited pursuant to Section 601, nor the principal or interest payments on any such Eligible Obligations, shall be withdrawn or used for any purpose other than, and shall be held in trust for, the payment of the principal of and premium, if any, and interest, if any, on the Securities or portions of principal amount thereof in respect of which such deposit was made, all subject, however, to the provisions of Section 503; provided, however, that any cash received from such principal or interest payments on such Eligible Obligations, if not then needed for such purpose, shall, to the extent practicable and upon Company

Request and delivery to the Trustee of the documents referred to in clause (y) in the first paragraph of Section 601, be invested in Eligible Obligations of the type described in clause (b) in the first paragraph of Section 601 maturing at such times and in such amounts as shall be sufficient, together with any other moneys and the proceeds of any other Eligible Obligations then held by the Trustee, to pay when due the principal of and premium, if any, and interest, if any, due and to become due on such Securities or portions thereof on and prior to the Maturity thereof, and interest earned from such reinvestment shall be paid over to the Company as received, free and clear of any trust, lien or pledge under this Indenture (except the lien provided by Section 807); and provided, further, that any moneys held in accordance with this Section on the Maturity of all such Securities in excess of the amount required to pay the principal of and premium, if any, and interest, if any, then due on such Securities shall be paid over to the Company free and clear of any trust, lien or pledge under this Indenture (except the lien provided by Section 807); and provided, further, that if an Event of Default shall have occurred and be continuing, moneys to be paid over to the Company pursuant to this Section shall be held until such Event of Default shall have been waived or cured.

#### ARTICLE SEVEN

##### EVENTS OF DEFAULT; REMEDIES

##### SECTION 701. EVENTS OF DEFAULT.

"EVENT OF DEFAULT", wherever used herein with respect to the Securities of any series, means any of the following events which shall have occurred and be continuing:

(a) failure to pay interest, if any, on any Security of such series within sixty (60) days after the same becomes due and payable (whether or not payment is prohibited by the provisions of Article Fourteen); provided, however, that no such failure shall constitute an "Event of Default" if the Company shall have made a valid extension of the interest payment period with respect to the Securities of such series if so provided with respect to such series as contemplated by Section 301; or

(b) failure to pay the principal of or premium, if any, on any Security of such series within three (3) Business Days after its Maturity (whether or not payment is prohibited by the provisions of Article Fourteen); provided, however, that no such failure shall constitute an "Event of Default" if the Company shall have made a valid extension of the Maturity of the Securities of such series if so provided with respect to such series as contemplated by Section 301; or

(c) failure to perform or breach of any covenant or warranty of the Company in this Indenture (other than a covenant or warranty a default in the performance of which or breach of which is elsewhere in this Section specifically dealt with or which has expressly been included in this Indenture solely for the benefit of one or more series of Securities

other than such series) for a period of ninety (90) days after there has been given, by registered or certified mail, to the Company by the Trustee, or to the Company and the Trustee by the Holders of at least thirty-three per centum (33%) in principal amount of the Outstanding Securities of such series, a written notice specifying such default or breach and requiring it to be remedied and stating that such notice is a "NOTICE OF DEFAULT" hereunder, unless the Trustee, or the Trustee and the Holders of a principal amount of Securities of such series not less than the principal amount of Securities the Holders of which gave such notice, as the case may be, shall agree in writing to an extension of such period prior to its expiration; provided, however, that the Trustee, or the Trustee and the Holders of such principal amount of Securities of such series, as the case may be, shall be deemed to have agreed to an extension of such period if corrective action is initiated by the Company within such period and is being diligently pursued; or

(d) the entry by a court having jurisdiction in the premises of (i) a decree or order for relief in respect of the Company in an involuntary case or proceeding under any applicable Federal or State bankruptcy, insolvency, reorganization or other similar law or (ii) a decree or order adjudging the Company a bankrupt or insolvent, or approving as properly filed a petition by one or more Persons other than the Company seeking reorganization, arrangement, adjustment or composition of or in respect of the Company under any applicable Federal or State law, or appointing a custodian, receiver, liquidator, assignee, trustee, sequestrator or other similar official for the Company or for any substantial part of its property, or ordering the winding-up or liquidation of its affairs, and any such decree or order for relief or any such other decree or order shall have remained unstayed and in effect for a period of ninety (90) consecutive days; or

(e) the commencement by the Company of a voluntary case or proceeding under any applicable Federal or State bankruptcy, insolvency, reorganization or other similar law or of any other case or proceeding to be adjudicated a bankrupt or insolvent, or the consent by the Company to the entry of a decree or order for relief in respect of the Company in a case or proceeding under any applicable Federal or State bankruptcy, insolvency, reorganization or other similar law or to the commencement of any bankruptcy or insolvency case or proceeding against the Company, or the filing by the Company of a petition or answer or consent seeking reorganization or relief under any applicable Federal or State law, or the consent by the Company to the filing of such petition or to the appointment of or taking possession by a custodian, receiver, liquidator, assignee, trustee, sequestrator or similar official of the Company or of any substantial part of its property, or the making by the Company of an assignment for the benefit of creditors, or the admission by the Company in writing of its inability to pay its debts generally as they become due, or the authorization of such action by the Board of Directors of the Company; or

(f) if such Securities shall have been issued and delivered to a Trust (or trustee thereof) in connection with the issuance by such Trust of Trust Securities and so long as such Trust Securities remain outstanding, such Trust shall have voluntarily or involuntarily

dissolved, wound up its business or otherwise terminated its existence except in connection with (i) the distribution of Securities to holders of Trust Securities in liquidation of their interests in such Trust; (ii) the redemption of all or the outstanding Trust Securities of such Trust or (iii) certain mergers, consolidations or other business combinations, each as permitted by the Declaration establishing such Trust, or

(g) any other Event of Default specified with respect to Securities of such series.

#### SECTION 702. ACCELERATION OF MATURITY; RESCISSION AND ANNULMENT.

If an Event of Default shall have occurred and be continuing with respect to Securities of any series at the time Outstanding, then in every such case the Trustee or the Holders of not less than thirty-three per centum (33%) in principal amount of the Outstanding Securities of such series may declare the principal amount (or, if any of the Securities of such series are Discount Securities, such portion of the principal amount of such Securities as may be specified in the terms thereof as contemplated by Section 301) of all of the Outstanding Securities of such series to be due and payable immediately (provided that the payment of principal and interest on such Securities shall remain subordinated to the extent provided in this Indenture), by a notice in writing to the Company (and to the Trustee if given by Holders), and upon receipt by the Company of notice of such declaration such principal amount (or specified amount), together with premium, if any, and accrued interest, if any, thereon, shall become immediately due and payable; provided, however, that if an Event of Default shall have occurred and be continuing with respect to more than one series of Securities, the Trustee or the Holders of not less than thirty-three per centum (33%) in aggregate principal amount of the Outstanding Securities of all such series, considered as one class, may make such declaration of acceleration, and not the Holders of the Securities of any one of such series (provided that the payment of principal and interest on such Securities shall remain subordinated to the extent provided in this Indenture).

At any time after such a declaration of acceleration of the maturity of the Securities of any series shall have been made, but before a judgment or decree for payment of the money due shall have been obtained by the Trustee as provided in this Article, the Event or Events of Default giving rise to such declaration of acceleration shall, without further act, be deemed to have been cured, and such declaration and its consequences shall, without further act, be deemed to have been rescinded and annulled, if

(a) the Company shall have paid or deposited with the Trustee a sum sufficient to pay

(i) all overdue interest, if any, on all Securities of such series then Outstanding;

(ii) the principal of and premium, if any, on any Securities of such series then Outstanding which have become due otherwise than by such

declaration of acceleration and interest, if any, thereon at the rate or rates prescribed therefor in such Securities;

(iii) interest, if any, upon overdue interest, if any, at the rate or rates prescribed therefor in such Securities, to the extent that payment of such interest is lawful; and

(iv) all amounts due to the Trustee under Section 807; and

(b) all Event or Events of Default with respect to Securities of such series, other than the non-payment of the principal of Securities of such series which shall have become due solely by such declaration of acceleration, shall have been cured or waived as provided in Section 713.

No such rescission shall affect any subsequent Event of Default or impair any right consequent thereon.

#### SECTION 703. COLLECTION OF INDEBTEDNESS AND SUITS FOR ENFORCEMENT BY TRUSTEE.

If an Event of Default described in clause (a) or (b) of Section 701 shall have occurred and be continuing, the Company shall, upon demand of the Trustee, pay to it, for the benefit of the Holders of the Securities of the series with respect to which such Event of Default shall have occurred, the whole amount then due and payable on such Securities for principal and premium, if any, and interest, if any, and, in addition thereto, such further amount as shall be sufficient to cover any amounts due to the Trustee under Section 807.

If the Company shall fail to pay such amounts forthwith upon such demand, the Trustee, in its own name and as trustee of an express trust, may institute a judicial proceeding for the collection of the sums so due and unpaid, may prosecute such proceeding to judgment or final decree and may enforce the same against the Company or any other obligor upon such Securities and collect the moneys adjudged or decreed to be payable in the manner provided by law out of the property of the Company or any other obligor upon such Securities, wherever situated.

If an Event of Default with respect to Securities of any series shall have occurred and be continuing, the Trustee may in its discretion proceed to protect and enforce its rights and the rights of the Holders of the Securities of such series then outstanding by such appropriate judicial proceedings as the Trustee shall deem most effectual to protect and enforce any such rights, whether for the specific enforcement of any covenant or agreement in this Indenture or in aid of the exercise of any power granted herein, or to enforce any other proper remedy.

#### SECTION 704. APPLICATION OF MONEY COLLECTED.

Any money collected by the Trustee pursuant to this Article shall be applied in the following order, to the extent permitted by law, at the date or dates fixed by the Trustee and, in case

of the distribution of such money on account of principal or premium, if any, or interest, if any, upon presentation of the Securities in respect of which or for the benefit of which such money shall have been collected and the notation thereon of the payment if only partially paid and upon surrender thereof if fully paid:

FIRST: To the payment of all amounts due the Trustee under Section 807;

SECOND: To the payment of the whole amount then due and unpaid upon the Outstanding Securities for principal and premium, if any, and interest, if any, in respect of which or for the benefit of which such money has been collected; and in case such proceeds shall be insufficient to pay in full the whole amount so due and unpaid upon such Securities, then to the payment of such principal and interest, if any, thereon without any preference or priority, ratably according to the aggregate amount so due and unpaid, with any balance then remaining to the payment of premium, if any, and, if so specified as contemplated by Section 301 with respect to the Securities of any series, or any Tranche thereof, interest, if any, on overdue premium, if any, and overdue interest, if any, ratably as aforesaid, all to the extent permitted by applicable law;

THIRD: To the payment of the remainder, if any, to the Company or to whomsoever may be lawfully entitled to receive the same or as a court of competent jurisdiction may direct.

SECTION 705. TRUSTEE MAY FILE PROOFS OF CLAIM.

In case of the pendency of any receivership, insolvency, liquidation, bankruptcy, reorganization, arrangement, adjustment, composition or other judicial proceeding relative to the Company or any other obligor upon the Securities or the property of the Company or of such other obligor or their creditors, the Trustee (irrespective of whether the principal of the Securities shall then be due and payable as therein expressed or by declaration or otherwise and irrespective of whether the Trustee shall have made any demand on the Company for the payment of overdue principal or interest) shall be entitled and empowered, by intervention in such proceeding or otherwise,

(a) to file and prove a claim for the whole amount of principal, premium, if any, and interest, if any, owing and unpaid in respect of the Securities and to file such other papers or documents as may be necessary or advisable in order to have the claims of the Trustee (including any claim for amounts due to the Trustee under Section 807) and of the Holders allowed in such judicial proceeding, and

(b) to collect and receive any moneys or other property payable or deliverable on any such claims and to distribute the same;



and any custodian, receiver, assignee, trustee, liquidator, sequestrator or other similar official in any such judicial proceeding is hereby authorized by each Holder to make such payments to the Trustee and, in the event that the Trustee shall consent to the making of such payments directly to the Holders, to pay to the Trustee any amounts due it under Section 807.

Nothing herein contained shall be deemed to authorize the Trustee to authorize or consent to or accept or adopt on behalf of any Holder any plan of reorganization, arrangement, adjustment or composition affecting the Securities or the rights of any Holder thereof or to authorize the Trustee to vote in respect of the claim of any Holder in any such proceeding.

SECTION 706. TRUSTEE MAY ENFORCE CLAIMS WITHOUT POSSESSION OF SECURITIES.

All rights of action and claims under this Indenture or on the Securities may be prosecuted and enforced by the Trustee without the possession of any of the Securities or the production thereof in any proceeding relating thereto, and any such proceeding instituted by the Trustee shall be brought in its own name as trustee of an express trust, and any recovery of judgment shall, after provision for the payment of the reasonable compensation, expenses, disbursements and advances of the Trustee, its agents and counsel, be for the ratable benefit of the Holders in respect of which such judgment has been recovered.

SECTION 707. LIMITATION ON SUITS.

No Holder shall have any right to institute any proceeding, judicial or otherwise, with respect to this Indenture, or for the appointment of a receiver or trustee, or for any other remedy hereunder, unless:

(a) such Holder shall have previously given written notice to the Trustee of a continuing Event of Default with respect to the Securities of such series;

(b) the Holders of a majority in aggregate principal amount of the Outstanding Securities of all series in respect of which an Event of Default shall have occurred and be continuing, considered as one class, shall have made written request to the Trustee to institute proceedings in respect of such Event of Default in its own name as Trustee hereunder;

(c) such Holder or Holders shall have offered to the Trustee reasonable indemnity against the costs, expenses and liabilities to be incurred in compliance with such request;

(d) the Trustee for sixty (60) days after its receipt of such notice, request and offer of indemnity shall have failed to institute any such proceeding; and

(e) no direction inconsistent with such written request shall have been given to the Trustee during such sixty (60) day period by the Holders of a majority in aggregate

principal amount of the Outstanding Securities of all series in respect of which an Event of Default shall have occurred and be continuing, considered as one class.

it being understood and intended that no one or more of such Holders shall have any right in any manner whatever by virtue of, or by availing of, any provision of this Indenture to affect, disturb or prejudice the rights of any other of such Holders or to obtain or to seek to obtain priority or preference over any other of such Holders or to enforce any right under this Indenture, except in the manner herein provided and for the equal and ratable benefit of all of such Holders.

SECTION 708. UNCONDITIONAL RIGHT OF HOLDERS TO RECEIVE PRINCIPAL, PREMIUM AND INTEREST.

Notwithstanding any other provision in this Indenture, the Holder of any Security shall have the right, which is absolute and unconditional, to receive payment of the principal of and premium, if any, and (subject to Sections 307) interest, if any, on such Security on the Stated Maturity or Maturities expressed in such Security (or, in the case of redemption, on the Redemption Date) and to institute suit for the enforcement of any such payment, and such rights shall not be impaired without the consent of such Holder. In addition, in the case of Securities of a series held by a Trust, a holder of Preferred Securities may directly institute a proceeding against the Company for enforcement of payment to such holder of principal of or interest on the Securities having a principal amount equal to the aggregate liquidation preference amount of the Preferred Securities of such holder on or after the due dates specified or provided for in the Securities.

SECTION 709. RESTORATION OF RIGHTS AND REMEDIES.

If the Trustee or any Holder has instituted any proceeding to enforce any right or remedy under this Indenture and such proceeding shall have been discontinued or abandoned for any reason, or shall have been determined adversely to the Trustee or to such Holder, then and in every such case, subject to any determination in such proceeding, the Company, the Trustee and such Holder shall be restored severally and respectively to their former positions hereunder and thereafter all rights and remedies of the Trustee and such Holder shall continue as though no such proceeding had been instituted.

SECTION 710. RIGHTS AND REMEDIES CUMULATIVE.

Except as otherwise provided in the last paragraph of Section 306, no right or remedy herein conferred upon or reserved to the Trustee or to the Holders is intended to be exclusive of any other right or remedy, and every right and remedy shall, to the extent permitted by law, be cumulative and in addition to every other right and remedy given hereunder or now or hereafter existing at law or in equity or otherwise. The assertion or employment of any right or remedy hereunder, or otherwise, shall not prevent the concurrent assertion or employment of any other appropriate right or remedy.

SECTION 711. DELAY OR OMISSION NOT WAIVER.

No delay or omission of the Trustee or of any Holder to exercise any right or remedy accruing upon any Event of Default shall impair any such right or remedy or constitute a waiver of any such Event of Default or an acquiescence therein. Every right and remedy given by this Article or by law to the Trustee or to the Holders may be exercised from time to time, and as often as may be deemed expedient, by the Trustee or by the Holders, as the case may be.

SECTION 712. CONTROL BY HOLDERS OF SECURITIES.

If an Event of Default shall have occurred and be continuing in respect of a series of Securities, the Holders of a majority in principal amount of the Outstanding Securities of such series shall have the right to direct the time, method and place of conducting any proceeding for any remedy available to the Trustee, or exercising any trust or power conferred on the Trustee with respect to the Securities of such series; provided, however, that if an Event of Default shall have occurred and be continuing with respect to more than one series of Securities, the Holders of a majority in aggregate principal amount of the Outstanding Securities of all such series, considered as one class, shall have the right to make such direction, and not the Holders of the Securities of any one of such series; and provided, further, that

(a) such direction shall not be in conflict with any rule of law or with this Indenture, and could not involve the Trustee in personal liability in circumstances where indemnity would not, in the Trustee's sole discretion, be adequate,

(b) the Trustee may take any other action deemed proper by the Trustee which is not inconsistent with such direction.

SECTION 713. WAIVER OF PAST DEFAULTS.

The Holders of not less than a majority in aggregate principal amount of the Outstanding Securities of any series may on behalf of the Holders of all the Securities of such series then outstanding waive any past default with respect to such series hereunder and its consequences, except a default

(a) in the payment of the principal of or premium, if any, or interest, if any, on any Security of such series then outstanding, or

(b) in respect of a covenant or provision hereof which under Section 1102 cannot be modified or amended without the consent of the Holder of each Outstanding Security of such series affected; provided, however, that so long as a Trust holds the Securities of any series, such trust may not waive any past default without the consent of at least a majority in aggregate liquidation preference of the outstanding Trust Securities issued by such Trust, obtained as provided in the Declaration pertaining to such Trust. Any such waiver by

holders of a majority in aggregate liquidation preference of outstanding Preferred Securities issued by any such Trust shall be deemed to be on behalf of all holders of Preferred Securities issued by any such Trust.

Upon any such waiver, such default shall cease to exist, and any and all Events of Default arising therefrom shall be deemed to have been cured, for every purpose of this Indenture; but no such waiver shall extend to any subsequent or other default or impair any right consequent thereon.

#### SECTION 714. UNDERTAKING FOR COSTS.

The Company and the Trustee agree, and each Holder by its acceptance of a Security shall be deemed to have agreed, that any court may in its discretion require, in any suit for the enforcement of any right or remedy under this Indenture, or in any suit against the Trustee for any action taken, suffered or omitted by it as Trustee, the filing by any party litigant in such suit of an undertaking to pay the costs of such suit, and that such court may in its discretion assess reasonable costs, including reasonable attorneys' fees, against any party litigant in such suit, having due regard to the merits and good faith of the claims or defenses made by such party litigant all in the manner, to the extent and except as provided in the Trust Indenture Act; but the provisions of this Section shall not apply to any suit instituted by the Company, to any suit instituted by the Trustee, to any suit instituted by any Holder, or group of Holders, holding in the aggregate more than ten per centum (10%) in aggregate principal amount of the Outstanding Securities of all series in respect of which such suit may be brought, considered as one class, or to any suit instituted by any Holder for the enforcement of the payment of the principal of or premium, if any, or interest, if any, on any Security on or after the Stated Maturity or Maturities expressed in such Security (or, in the case of redemption, on or after the Redemption Date).

#### SECTION 715. WAIVER OF STAY OR EXTENSION LAWS.

To the full extent that it may lawfully so agree, the Company shall not at any time set up, claim or otherwise seek to take the benefit or advantage of any stay or extension law, now or hereafter in effect, in order to prevent or hinder the enforcement of this Indenture; and the Company, for itself and all who may claim under it, so far as it or they now or hereafter may lawfully do so, hereby waives the benefit of all such laws.

#### SECTION 716. ACTION BY HOLDERS OF CERTAIN TRUST SECURITIES.

If the Securities of any series shall be held by the Institutional Trustee of a Trust and if such Institutional Trustee, as such Holder, shall have failed to exercise any of the rights and remedies available under this Indenture to the Holders of such Securities, the holders of the Trust Securities issued by such Trust (other than Trust Securities initially issued and sold to the Company) shall have and may exercise all such rights and remedies, to the same extent as if such holders of such Trust Securities held a principal amount of Securities of such series equal to the

liquidation preference of such Trust Securities, without first proceeding against such trustee or trust. Notwithstanding the foregoing, in the case of an Event of Default described in clause (a) or (b) of Section 701, each holder of such Trust Securities shall have and may exercise all rights available to the Institutional Trustee under Section 708 as the Holder of the Securities of such series.

If action shall have been taken by both the Holders and the holders of Trust Securities (other than Trust Securities initially issued and sold to the Company) to exercise such rights as contemplated in the preceding paragraph, the action taken by holders of Trust Securities shall control. Any such action taken by registered holders of Trust Securities shall be evidenced to the Trustee in the same manner as an Act of Holders, as provided in Section 104(a). The Trustee shall be entitled to rely on the books and records of the related Trust in determining the identities of the holders of Trust Securities (and, upon the reasonable request of the Trustee, the Company, as the sponsor of such Trust, shall, at its own expense, promptly provide copies of applicable portions of such books and records to the Trustee to the extent reasonably necessary to enable the Trustee to make such determination).

#### ARTICLE EIGHT

#### THE TRUSTEE

#### SECTION 801. CERTAIN DUTIES AND RESPONSIBILITIES.

(a) Except during the continuance of an Event of Default with respect to Securities of any series,

(i) the Trustee undertakes to perform, with respect to Securities of such series, such duties and only such duties as are specifically set forth in this Indenture, and no implied covenants or obligations shall be read into this Indenture against the Trustee; and

(ii) in the absence of bad faith on its part, the Trustee may, with respect to Securities of such series, conclusively rely, as to the truth of the statements and the correctness of the opinions expressed therein, upon certificates or opinions furnished to the Trustee and conforming to the requirements of this Indenture; but in the case of any such certificates or opinions which by any provisions hereof are specifically required to be furnished to the Trustee, the Trustee shall be under a duty to examine the same to determine whether or not they conform to the requirements of this Indenture.

(b) In case an Event of Default with respect to Securities of any series shall have occurred and be continuing, the Trustee shall exercise, with respect to Securities of such series, such of the rights and powers vested in it by this Indenture, and use the same degree of care and skill in

their exercise, as a prudent man would exercise or use under the circumstances in the conduct of his own affairs.

(c) No provision of this Indenture shall be construed to relieve the Trustee from liability for its own negligent action, its own negligent failure to act, or its own willful misconduct, except that:

(i) this subsection shall not be construed to limit the effect of subsection (a) of this Section;

(ii) the Trustee shall not be liable for any error of judgment made in good faith by a Responsible Officer, unless it shall be proved that the Trustee was negligent in ascertaining the pertinent facts;

(iii) the Trustee shall not be liable with respect to any action taken or omitted to be taken by it in good faith in accordance with the direction of the Holders of a majority in principal amount of the Outstanding Securities of any one or more series, as provided herein, relating to the time, method and place of conducting any proceeding for any remedy available to the Trustee, or exercising any trust or power conferred upon the Trustee, under this Indenture with respect to the Securities of such series; and

(iv) no provision of this Indenture shall require the Trustee to expend or risk its own funds or otherwise incur any financial liability in the performance of any of its duties hereunder, or in the exercise of any of its rights or powers, if it shall have reasonable grounds for believing that repayment of such funds or adequate indemnity against such risk or liability is not reasonably assured to it.

(d) Whether or not therein expressly so provided, every provision of this Indenture relating to the conduct or affecting the liability of or affording protection to the Trustee shall be subject to the provisions of this Section.

#### SECTION 802. NOTICE OF DEFAULTS.

The Trustee shall give notice of any default hereunder known to the Trustee with respect to the Securities of any series to the Holders of Securities of such series in the manner and to the extent required to do so by the Trust Indenture Act, unless such default shall have been cured or waived; provided, however, that in the case of any default of the character specified in Section 701(c), no such notice to Holders shall be given until at least seventy-five (75) days after the occurrence thereof; and provided, further, that, subject to the provisions of Section 801, the Trustee shall not be deemed to have knowledge of such default unless either (i) a Responsible Officer of the Trustee shall have actual knowledge of such default or (ii) the Trustee shall have received written notice thereof from the Company or any Holder or, in the case of a default described in Section

701(d), from the holder of any indebtedness or from the trustee under any mortgage, indenture or other instrument referred to in such Section. For the purpose of this Section, the term "DEFAULT" means any event which is, or after notice or lapse of time, or both, would become, an Event of Default with respect to the Securities of such series.

#### SECTION 803. CERTAIN RIGHTS OF TRUSTEE.

Subject to the provisions of Section 801 and to the applicable provisions of the Trust Indenture Act:

(a) the Trustee may rely and shall be protected in acting or refraining from acting upon any resolution, certificate, statement, instrument, opinion, report, notice, request, direction, consent, order, bond, debenture, note, other evidence of indebtedness or other paper or document believed by it to be genuine and to have been signed, sent or presented by the proper party or parties;

(b) any request, direction or act of the Company mentioned herein shall be sufficiently evidenced by a Company Request or Company Order, or as otherwise expressly provided herein, and any resolution of the Board of Directors of the Company may be sufficiently evidenced by a Board Resolution;

(c) whenever in the administration of this Indenture the Trustee shall deem it desirable that a matter be proved or established prior to taking, suffering or omitting any action hereunder, the Trustee (unless other evidence is specifically prescribed herein) may, in the absence of bad faith on its part, rely upon an Officer's Certificate of the Company;

(d) the Trustee may consult with counsel and the written advice of such counsel or any Opinion of Counsel shall be full and complete authorization and protection in respect of any action taken, suffered or omitted by it hereunder in good faith and in reliance thereon;

(e) the Trustee shall be under no obligation to exercise any of the rights or powers vested in it by this Indenture at the request or direction of any Holder pursuant to this Indenture, unless such Holder shall have offered to the Trustee reasonable security or indemnity against the costs, expenses and liabilities which might be incurred by it complying with such request or direction;

(f) the Trustee shall not be bound to make any investigation into the facts or matters stated in any resolution, certificate, statement, instrument, opinion, report, notice, request, direction, consent, order, bond, debenture, note, other evidence of indebtedness or other paper or document, but the Trustee, in its discretion, may make such further inquiry or investigation into such facts or matters as it may see fit, and, if the Trustee shall determine to make such further inquiry or investigation, it shall (subject to applicable legal requirements)

be entitled to examine, during normal business hours, the books, records and premises of the Company, personally or by agent or attorney;

(g) the Trustee may execute any of the trusts or powers hereunder or perform any duties hereunder either directly or by or through agents or attorneys and the Trustee shall not be responsible for any misconduct or negligence on the part of any agent or attorney appointed with due care by it hereunder; and

(h) the Trustee shall not be charged with knowledge of any Event of Default with respect to the Securities of any series for which it is acting as Trustee unless either (i) a Responsible Officer of the Trustee shall have actual knowledge of the Event of Default or (ii) written notice of such Event of Default shall have been given to the Trustee by the Company, any other obligor on such Securities or by any Holder of such Securities.

#### SECTION 804. NOT RESPONSIBLE FOR RECITALS OR ISSUANCE OF SECURITIES.

The recitals contained herein and in the Securities (except the Trustee's certificates of authentication) shall be taken as the statements of the Company, and neither the Trustee nor any Authenticating Agent assumes any responsibility for their correctness. The Trustee makes no representations as to the validity or sufficiency of this Indenture or of the Securities. Neither the Trustee nor any Authenticating Agent shall be accountable for the use or application by the Company of Securities or the proceeds thereof.

#### SECTION 805. MAY HOLD SECURITIES.

Each of the Trustee, any Authenticating Agent, any Paying Agent, any Security Registrar or any other agent of the Company or the Trustee, in its individual or any other capacity, may become the owner or pledgee of Securities and/or Preferred Securities, subject to Sections 808 and 813, may otherwise deal with the Company with the same rights it would have if it were not such Trustee, Authenticating Agent, Paying Agent, Security Registrar or other agent.

#### SECTION 806. MONEY HELD IN TRUST.

Money held by the Trustee in trust hereunder need not be segregated from other funds, except to the extent required by law. The Trustee shall be under no liability for interest on or investment of any money received by it hereunder except as expressly provided herein or otherwise agreed with, and for the sole benefit of, the Company.

#### SECTION 807. COMPENSATION AND REIMBURSEMENT.

The Company agrees



(a) to pay to the Trustee from time to time reasonable compensation for all services rendered by it hereunder (which compensation shall not be limited by any provision of law in regard to the compensation of a trustee of an express trust);

(b) except as otherwise expressly provided herein, to reimburse the Trustee upon its request for all reasonable expenses, disbursements and advances reasonably incurred or made by the Trustee in accordance with any provision of this Indenture (including the reasonable compensation and the expenses and disbursements of its agents and counsel), except to the extent that any such expense, disbursement or advance as may be attributable to its negligence, willful misconduct or bad faith; and

(c) to indemnify the Trustee and hold it harmless from and against any loss, liability or expense reasonably incurred by it arising out of or in connection with the acceptance or administration of the trust or trusts hereunder or the performance of its duties hereunder, including the reasonable costs and expenses of defending itself against any claim or liability in connection with the exercise or performance of any of its powers or duties hereunder, except to the extent that any such loss, liability or expense may be attributable to its negligence, willful misconduct or bad faith.

As security for the performance of the obligations of the Company under this Section, the Trustee shall have a lien prior to the Securities upon all property and funds held or collected by the Trustee as such other than property and funds held in trust under Section 603 (except moneys payable to the Company as provided in Section 603). "TRUSTEE" for purposes of this Section shall include any predecessor Trustee; provided, however, that the negligence, willful misconduct or bad faith of any Trustee hereunder shall not affect the rights of any other Trustee hereunder.

**SECTION 808. DISQUALIFICATION; CONFLICTING INTERESTS.**

If the Trustee shall have or acquire any conflicting interest within the meaning of the Trust Indenture Act, it shall either eliminate such conflicting interest or resign to the extent, in the manner and with the effect, and subject to the conditions, provided in the Trust Indenture Act and this Indenture. For purposes of Section 310(b)(1) of the Trust Indenture Act and to the extent permitted thereby, the Trustee, in its capacity as trustee in respect of the Securities of any series, shall not be deemed to have a conflicting interest arising from its capacity as trustee in respect of (i) the Securities of any other series and (ii) the Declaration and the Trust Securities Guarantee Agreement pertaining to each Trust.

**SECTION 809. CORPORATE TRUSTEE REQUIRED; ELIGIBILITY.**

There shall at all times be a Trustee hereunder which shall be

(a) a corporation organized and doing business under the laws of the United States, any State or Territory thereof or the District of Columbia, authorized under such laws to exercise corporate trust powers, having a combined capital and surplus of at least Fifty Million Dollars (\$50,000,000) and subject to supervision or examination by Federal, State, Territorial or District of Columbia authority, or

(b) if and to the extent permitted by the Commission by rule, regulation or order upon application, a corporation or other Person organized and doing business under the laws of a foreign government, authorized under such laws to exercise corporate trust powers, having a combined capital and surplus of at least Fifty Million Dollars (\$50,000,000) or the Dollar equivalent of the applicable foreign currency and subject to supervision or examination by authority of such foreign government or a political subdivision thereof substantially equivalent to supervision or examination applicable to United States institutional trustees,

and, in either case, qualified and eligible under this Article and the Trust Indenture Act. If such corporation publishes reports of condition at least annually, pursuant to law or to the requirements of such supervising or examining authority, then for the purposes of this Section, the combined capital and surplus of such corporation shall be deemed to be its combined capital and surplus as set forth in its most recent report of condition so published. If at any time the Trustee shall cease to be eligible in accordance with the provisions of this Section or the Trust Indenture Act, it shall resign immediately in the manner and with the effect hereinafter specified in this Article.

#### SECTION 810. RESIGNATION AND REMOVAL; APPOINTMENT OF SUCCESSOR.

(a) No resignation or removal of the Trustee and no appointment of a successor Trustee pursuant to this Article shall become effective until the acceptance of appointment by the successor Trustee in accordance with the applicable requirements of Section 811.

(b) The Trustee may resign at any time with respect to the Securities of one or more series by giving written notice thereof to the Company. If the instrument of acceptance by a successor Trustee required by Section 811 shall not have been delivered to the Trustee within thirty (30) days after the giving of such notice of resignation, the resigning Trustee may petition any court of competent jurisdiction for the appointment of a successor Trustee with respect to the Securities of such series.

(c) The Trustee may be removed at any time with respect to the Securities of any series by Act of the Holders of a majority in principal amount of the Outstanding Securities of such series delivered to the Trustee and to the Company; provided that so long as any Preferred Securities remain outstanding, the Trust which issued such Preferred Securities shall not execute any Act to remove the Trustee without the consent of the holders of a majority in aggregate liquidation preference of Preferred Securities issued by such Trust outstanding, obtained as provided in the Declaration pertaining to such Trust.

(d) If at any time:

(i) the Trustee shall fail to comply with Section 808 after written request therefor by the Company or by any Holder who has been a bona fide Holder for at least six months, or

(ii) the Trustee shall cease to be eligible under Section 809 or Section 310(a) of the Trust Indenture Act and shall fail to resign after written request therefor by the Company or by any such Holder, or

(iii) the Trustee shall become incapable of acting or shall be adjudged a bankrupt or insolvent or a receiver of the Trustee or of its property shall be appointed or any public officer shall take charge or control of the Trustee or of its property or affairs for the purpose of rehabilitation, conservation or liquidation,

then, in any such case, (x) the Company may remove the Trustee with respect to all Securities or (y) subject to Section 714, any Holder who has been a bona fide Holder for at least six (6) months may, on behalf of itself and all others similarly situated, petition any court of competent jurisdiction for the removal of the Trustee with respect to all Securities and the appointment of a successor Trustee or Trustees.

(e) If the Trustee shall resign, be removed or become incapable of acting, or if a vacancy shall occur in the office of Trustee for any cause (other than as contemplated in clause (y) in subsection (d) of this Section), with respect to the Securities of one or more series, the Company shall take prompt steps to appoint a successor Trustee or Trustees with respect to the Securities of that or those series (it being understood that any such successor Trustee may be appointed with respect to the Securities of one or more or all of such series and that at any time there shall be only one Trustee with respect to the Securities of any particular series) and shall comply with the applicable requirements of Section 811. If, within one (1) year after such resignation, removal or incapability, or the occurrence of such vacancy, a successor Trustee with respect to the Securities of any series shall be appointed by Act of the Holders of a majority in principal amount of the Outstanding Securities of such series delivered to the Company and the retiring Trustee, the successor Trustee so appointed shall, forthwith upon its acceptance of such appointment in accordance with the applicable requirements of Section 811, become the successor Trustee with respect to the Securities of such series and to that extent supersede the successor Trustee appointed by the Company. If no successor Trustee with respect to the Securities of any series shall have been so appointed by the Company or the Holders and accepted appointment in the manner required by Section 811, any Holder who has been a bona fide Holder of a Security of such series for at least six (6) months may, on behalf of itself and all others similarly situated, petition any court of competent jurisdiction for the appointment of a successor Trustee with respect to the Securities of such series.

(f) So long as no event which is, or after notice or lapse of time, or both, would become, an Event of Default shall have occurred and be continuing, if the Company shall have

delivered to the Trustee or Trustees with respect to the Securities of one or more series (i) an instrument executed by an Authorized Officer of the Company appointing a successor Trustee or Trustees with respect to such series, effective as of a date specified therein, and (ii) an instrument of acceptance of such appointment, effective as of such date, by such successor Trustee or Trustees in accordance with Section 811, the Trustee or Trustees with respect to such series shall be deemed to have resigned as contemplated in subsection (b) of this Section, the successor Trustee or Trustees shall be deemed to have been appointed by the Company pursuant to subsection (e) of this Section and such appointment shall be deemed to have been accepted as contemplated in Section 811, all as of such date, and all other provisions of this Section and Section 811 shall be applicable to such resignation, appointment and acceptance except to the extent inconsistent with this subsection (f).

(g) The Company shall give notice of each resignation and each removal of the Trustee with respect to the Securities of any series and each appointment of a successor Trustee with respect to the Securities of any series to all Holders of Securities of such series. Each notice shall include the name of the successor Trustee with respect to the Securities of such series and the address of its corporate trust office.

#### SECTION 811. ACCEPTANCE OF APPOINTMENT BY SUCCESSOR.

(a) In case of the appointment hereunder of a successor Trustee with respect to the Securities of all series, every such successor Trustee so appointed shall execute, acknowledge and deliver to the Company and to the retiring Trustee an instrument accepting such appointment, and thereupon the resignation or removal of the retiring Trustee shall become effective and such successor Trustee, without any further act, shall become vested with all the rights, powers, trusts and duties of the retiring Trustee; but, on the request of the Company or the successor Trustee, such retiring Trustee shall, upon payment of all sums owed to it, execute and deliver an instrument transferring to such successor Trustee all the rights, powers and trusts of the retiring Trustee and shall duly assign, transfer and deliver to such successor Trustee all property and money held by such retiring Trustee hereunder.

(b) In case of the appointment hereunder of a successor Trustee with respect to the Securities of one or more (but not all) series, the Company, the retiring Trustee and each successor Trustee with respect to the Securities of such series shall execute and deliver an indenture supplemental hereto wherein each successor Trustee shall accept such appointment and which (1) shall contain such provisions as shall be necessary or desirable to transfer and confirm to, and to vest in, each successor Trustee all the rights, powers, trusts and duties of the retiring Trustee with respect to the Securities of that or those series to which the appointment of such successor Trustee relates, (2) if the retiring Trustee is not retiring with respect to all Securities, shall contain such provisions as shall be deemed necessary or desirable to confirm that all the rights, powers, trusts and duties of the retiring Trustee with respect to the Securities of that or those series as to which the retiring Trustee is not retiring shall continue to be vested in the retiring Trustee and (3) shall add to or change any of the provisions of this Indenture as shall be necessary to provide for or facilitate the administration of the trusts hereunder by more than one Trustee, it being understood that nothing

herein or in such supplemental indenture shall constitute such Trustees co-trustees of the same trust and that each such Trustee shall be trustee of a trust or trusts hereunder separate and apart from any trust or trusts hereunder administered by any other such Trustee; and upon the execution and delivery of such supplemental indenture the resignation or removal of the retiring Trustee shall become effective to the extent provided therein and each such successor Trustee, without any further act, shall become vested with all the rights, powers, trusts and duties of the retiring Trustee with respect to the Securities of that or those series to which the appointment of such successor Trustee relates; but, on request of the Company or any successor Trustee, such retiring Trustee, upon payment of all sums owed to it, shall duly assign, transfer and deliver to such successor Trustee all property and money held by such retiring Trustee hereunder with respect to the Securities of that or those series to which the appointment of such successor Trustee relates.

(c) Upon reasonable request of any such successor Trustee, the Company shall execute instruments to more fully and certainly vest in and confirm to such successor Trustee all rights, powers and trusts referred to in subsection (a) or (b) of this Section, as the case may be.

(d) No successor Trustee shall accept its appointment unless at the time of such acceptance such successor Trustee shall be qualified and eligible under this Article.

#### SECTION 812. MERGER, CONVERSION, CONSOLIDATION OR SUCCESSION TO BUSINESS.

Any corporation into which the Trustee may be merged or converted or with which it may be consolidated, or any corporation resulting from any merger, conversion or consolidation to which the Trustee shall be a party, or any corporation succeeding to all or substantially all the corporate trust business of the Trustee, shall be the successor of the Trustee hereunder, provided such corporation shall be otherwise qualified and eligible under this Article, without the execution or filing of any paper or any further act on the part of any of the parties hereto. In case any Securities shall have been authenticated, but not delivered, by the Trustee then in office, any successor by merger, conversion or consolidation to such authenticating Trustee may adopt such authentication and deliver the Securities so authenticated with the same effect as if such successor Trustee had itself authenticated such Securities.

#### SECTION 813. PREFERENTIAL COLLECTION OF CLAIMS AGAINST COMPANY.

If the Trustee shall be or become a creditor of the Company or any other obligor upon the Securities (other than by reason of a relationship described in Section 311(b) of the Trust Indenture Act), the Trustee shall be subject to any and all applicable provisions of the Trust Indenture Act regarding the collection of claims against the Company or such other obligor. For purposes of Section 311(b) of the Trust Indenture Act:

(a) the term "CASH TRANSACTION" means any transaction in which full payment for goods or securities sold is made within seven days after delivery of the goods or securities in currency or in

checks or other orders drawn upon banks or bankers and payable upon demand; and

(b) the term "SELF-LIQUIDATING PAPER" means any draft, bill of exchange, acceptance or obligation which is made, drawn, negotiated or incurred by the Company or such obligor for the purpose of financing the purchase, processing, manufacturing, shipment, storage or sale of goods, wares or merchandise and which is secured by documents evidencing title to, possession of, or a lien upon, the goods, wares or merchandise or the receivables or proceeds arising from the sale of the goods, wares or merchandise previously constituting the security, provided the security is received by the Trustee simultaneously with the creation of the creditor relationship with the Company or such obligor arising from the making, drawing, negotiating or incurring of the draft, bill of exchange, acceptance or obligation.

#### SECTION 814. APPOINTMENT OF AUTHENTICATING AGENT.

The Trustee may appoint an Authenticating Agent or Agents with respect to the Securities of one or more series, or any Tranche thereof, which shall be authorized to act on behalf of the Trustee to authenticate Securities of such series or Tranche issued upon original issuance, exchange, registration of transfer or partial redemption thereof or pursuant to Section 306, and Securities so authenticated shall be entitled to the benefits of this Indenture and shall be valid and obligatory for all purposes as if authenticated by the Trustee hereunder. Wherever reference is made in this Indenture to the authentication and delivery of Securities by the Trustee or the Trustee's certificate of authentication, such reference shall be deemed to include authentication and delivery on behalf of the Trustee by an Authenticating Agent and a certificate of authentication executed on behalf of the Trustee by an Authenticating Agent. Each Authenticating Agent shall be acceptable to the Company and shall at all times be a corporation organized and doing business under the laws of the United States, any State or Territory thereof or the District of Columbia or the Commonwealth of Puerto Rico, authorized under such laws to act as Authenticating Agent, having a combined capital and surplus of not less than Fifty Million Dollars (\$50,000,000) and subject to supervision or examination by Federal or State authority. If such Authenticating Agent publishes reports of condition at least annually, pursuant to law or to the requirements of said supervising or examining authority, then for the purposes of this Section, the combined capital and surplus of such Authenticating Agent shall be deemed to be its combined capital and surplus as set forth in its most recent report of condition so published. If at any time an Authenticating Agent shall cease to be eligible in accordance with the provisions of this Section, such Authenticating Agent shall resign immediately in the manner and with the effect specified in this Section.

Any corporation into which an Authenticating Agent may be merged or converted or with which it may be consolidated, or any corporation resulting from any merger, conversion or consolidation to which such Authenticating Agent shall be a party, or any corporation succeeding to all or substantially all of the corporate agency or corporate trust business of an Authenticating Agent, shall continue to be an Authenticating Agent, provided such corporation shall be otherwise

eligible under this Section, without the execution or filing of any paper or any further act on the part of the Trustee or the Authenticating Agent.

An Authenticating Agent may resign at any time by giving written notice thereof to the Trustee and to the Company. The Trustee may at any time terminate the agency of an Authenticating Agent by giving written notice thereof to such Authenticating Agent and to the Company. Upon receiving such a notice of resignation or upon such a termination, or in case at any time such Authenticating Agent shall cease to be eligible in accordance with the provisions of this Section, the Trustee may appoint a successor Authenticating Agent which shall be acceptable to the Company. Any successor Authenticating Agent upon acceptance of its appointment hereunder shall become vested with all the rights, powers and duties of its predecessor hereunder, with like effect as if originally named as an Authenticating Agent. No successor Authenticating Agent shall be appointed unless eligible under the provisions of this Section.

The Company agrees to pay to each Authenticating Agent from time to time reasonable compensation for its services under this Section.

The provisions of Sections 308, 804 and 805 shall be applicable to each Authenticating Agent.

If an appointment with respect to the Securities of one or more series, or any Tranche thereof, shall be made pursuant to this Section, the Securities of such series or Tranche may have endorsed thereon, in addition to the Trustee's certificate of authentication, an alternate certificate of authentication substantially in the following form:

This is one of the Securities of the series designated therein referred to in the within-mentioned Indenture.

\_\_\_\_\_  
As Trustee

By \_\_\_\_\_  
As Authenticating Agent

By \_\_\_\_\_  
Authorized Officer

If all of the Securities of a series may not be originally issued at one time, and if the Trustee does not have an office capable of authenticating Securities upon original issuance located in a Place of Payment where the Company wishes to have Securities of such series authenticated upon original issuance, the Trustee, if so requested by the Company in writing (which writing need

not comply with Section 102 and need not be accompanied by an Opinion of Counsel), shall appoint, in accordance with this Section and in accordance with such procedures as shall be acceptable to the Trustee, an Authenticating Agent having an office in a Place of Payment designated by the Company with respect to such series of Securities.

#### ARTICLE NINE

##### LISTS OF HOLDERS; REPORTS BY TRUSTEE AND COMPANY

###### SECTION 901. LISTS OF HOLDERS.

Semiannually, not later than June 1 and December 1 in each year, commencing June 1, 2004, and within thirty (30) days of such other times as the Trustee may request in writing, the Company shall furnish or cause to be furnished to the Trustee information as to the names and addresses of the Holders, as of a date no more than fifteen (15) days prior to the date such information is so furnished, and the Trustee shall preserve such information and similar information received by it in any other capacity and afford to the Holders access to information so preserved by it, all to such extent, if any, and in such manner as shall be required by the Trust Indenture Act; provided, however, that no such list need be furnished so long as the Trustee shall be the Security Registrar.

###### SECTION 902. REPORTS BY TRUSTEE AND COMPANY.

Not later than May 15 in each year, commencing May 15, 2004, the Trustee shall transmit to the Holders, the Commission and each securities exchange upon which any Securities are listed, a report, dated as of the next preceding May 15, with respect to any events and other matters described in Section 313(a) of the Trust Indenture Act, in such manner and to the extent required by the Trust Indenture Act. The Trustee shall transmit to the Holders, the Commission and each securities exchange upon which any Securities are listed, and the Company shall file with the Trustee (within thirty (30) days after filing with the Commission in the case of reports which pursuant to the Trust Indenture Act must be filed with the Commission and furnished to the Trustee) and transmit to the Holders, such other information, reports and other documents, if any, at such times and in such manner, as shall be required by the Trust Indenture Act. The Company shall notify the Trustee of the listing of any Securities on any securities exchange.



ARTICLE TEN

CONSOLIDATION, MERGER, CONVEYANCE  
OR OTHER TRANSFER

SECTION 1001. COMPANY MAY CONSOLIDATE, ETC., ONLY ON CERTAIN TERMS.

The Company shall not consolidate with or merge into any other Person, or convey or otherwise transfer, or lease, all of its properties, as or substantially as an entirety, to any Person, unless:

(a) the Person formed by such consolidation or into which the Company is merged or the Person which acquires by conveyance or other transfer, or which leases (for a term extending beyond the last Stated Maturity of the Securities then Outstanding), all of the properties of the Company, as or substantially as an entirety, shall be a Person organized and existing under the laws of the United States, any State or Territory thereof or the District of Columbia or under the laws of Canada or any Province thereof (such Person being hereinafter sometimes called the "SUCCESSOR") and shall expressly assume, by an indenture supplemental hereto, executed and delivered to the Trustee, in form reasonably satisfactory to the Trustee, the due and punctual payment of the principal of and premium, if any, and interest, if any, on all the Securities then Outstanding and the performance and observance of every other covenant and condition of this Indenture to be performed or observed by the Company; and

(b) the Company shall have delivered to the Trustee an Officer's Certificate and an Opinion of Counsel, each of which shall state that such consolidation, merger, conveyance or other transfer or lease, and such supplemental indenture, comply with this Article and that all conditions precedent herein provided for relating to such transaction have been complied with.

Anything in this Indenture to the contrary notwithstanding, the conveyance or other transfer by the Company of all of its facilities (a) for the generation of electric energy, (b) for the transmission of electric energy or (c) for the distribution of electric energy and/or natural gas, in each case considered alone, or all of its facilities described in clauses (a) and (b), considered together, or all of its facilities described in clauses (b) and (c), considered together, shall in no event be deemed to constitute a conveyance or other transfer of all the properties of the Company, as or substantially as an entirety, unless, immediately following such conveyance or other transfer, the Company shall own no properties in the other such categories of property not so conveyed or otherwise transferred. The character of particular facilities shall be determined by reference to the Uniform System of Accounts prescribed for public utilities and licensees subject to the Federal Power Act, as amended, to the extent applicable.

SECTION 1002. SUCCESSOR SUBSTITUTED.

Upon any consolidation or merger or any conveyance or other transfer of all the properties of the Company, as or substantially as an entirety, in accordance with Section 1001, the Successor shall succeed to, and be substituted for, and may exercise every power and right of, the Company under this Indenture with the same effect as if such Successor had been named as the "Company" herein. Without limiting the generality of the foregoing, the Successor may execute and deliver to the Trustee, and thereupon the Trustee shall, subject to the provisions of Article Three, authenticate and deliver, Securities. All Securities so executed by the Successor, and authenticated and delivered by the Trustee, shall in all respects be entitled to the benefits provided by this Indenture equally and ratably with all Securities executed, authenticated and delivered prior to the time such consolidation, merger, conveyance or other transfer became effective.

SECTION 1003. RELEASE OF COMPANY UPON CONVEYANCE OR OTHER TRANSFER.

In the case of a conveyance or other transfer to any Person or Persons as contemplated in Section 1001, upon the satisfaction of all the conditions specified in Section 1001 the Company (such term being used in this Section without giving effect to such transaction) shall be released and discharged from all obligations and covenants under this Indenture and on and under all Securities then Outstanding (unless the Company shall have delivered to the Trustee an instrument in which it shall waive such release and discharge) and the Trustee shall acknowledge in writing that the Company has been so released and discharged.

SECTION 1004. MERGER INTO COMPANY.

Nothing in this Indenture shall be deemed to prevent or restrict any consolidation or merger after the consummation of which the Company would be the surviving or resulting corporation or any conveyance or other transfer, or lease of any part of the properties of the Company which does not constitute the entirety, or substantially the entirety, thereof.

SECTION 1005. TRANSFER OF LESS THAN THE ENTIRETY.

(a) If the Company shall have conveyed or otherwise transferred any part of its properties which does not constitute the entirety, or substantially the entirety, thereof to another corporation meeting the requirements set forth in clause (a) of the first paragraph of Section 1001 and if:

(i) the transferee of such part of the properties of the Company shall have executed and delivered to the Trustee an indenture supplemental hereto, in form reasonably satisfactory to the Trustee, which contains an assumption by such transferee of the due and punctual payment of the principal of and premium, if any, and interest, if any, on all the Securities then Outstanding and the performance and observance of every covenant and condition of this Indenture to be performed or observed by the Company;

(ii) there shall have been delivered to the Trustee an Independent Expert's Certificate

(A) describing the property so conveyed or otherwise transferred (such description of property to be made by reference either to specific items, units and/or elements of property or portions thereof, on a percentage or Dollar basis, or to properties reflected in specified accounts in the Company's books of account or portions thereof, on a Dollar basis); provided, however, that such property shall be identified in such certificate as facilities for the generation, transmission or distribution of electric energy or for the storage, transportation or distribution of natural gas;

(B) stating, in the judgment of the signers, the Fair Value to the transferee of the property so conveyed or otherwise transferred;

(C) stating an amount equal to seventy percent (70%) of the amount stated pursuant to clause (B) above; provided, however, that there shall be excluded from the property so evaluated any property subject to any mortgage, deed of trust, security interest or other lien which secures indebtedness for borrowed money or for the deferred purchase price of property;

(D) stating an amount equal to the aggregate principal amount of the Securities then Outstanding; and

(E) stating that the amount stated pursuant to clause (D) above does not exceed the amount stated pursuant to clause (C) above;

(iii) the Company shall have assigned or otherwise transferred to such transferee all Trust Securities (initially issued and sold to the Company) then outstanding, and such transferee shall have expressly assumed all obligations under all Trust Securities Guarantees; and

(iv) the Company shall have delivered to the Trustee an Officer's Certificate and an Opinion of Counsel each of which shall state that such conveyance or other transfer and such supplemental indenture comply with this Section and that all conditions precedent relating to such transactions provided for in this Section and otherwise in this Indenture have been complied with;

then, upon the satisfaction of all such conditions,

(x) the Company shall be released and discharged from all obligations and covenants under this Indenture and on and under all Securities then Outstanding (unless the Company shall have delivered to the Trustee an instrument in which it shall waive such

release and discharge), and the Trustee shall acknowledge in writing that the Company has been so released and discharged; and

(y) if the Company shall have been released and discharged as contemplated in clause (x) above, such transferee shall succeed to, and be substituted for, and may exercise every right and power of, the Company under this Indenture with the same effect as if such transferee had been named the "Company" herein; and without limiting the generality of the foregoing, such transferee shall be deemed a "Successor" for purposes of Section 1002 and for all other purposes of this Indenture.

(b) For purposes of this Section:

"FAIR VALUE" means the fair value of such property so conveyed or otherwise transferred as may be determined by reference to (a) the amount which would be likely to be obtained in an arm's-length transaction with respect to such property between an informed and willing buyer and an informed and willing seller, under no compulsion, respectively, to buy or sell, (b) the amount of investment with respect to such property which, together with a reasonable return thereon, would be likely to be recovered through ordinary business operations or otherwise, (c) the cost, accumulated depreciation and replacement cost with respect to such property and/or (d) any other relevant factors; provided, however, that (x) the Fair Value of property shall be determined without deduction for any mortgage, deed of trust, pledge, security interest, encumbrance, lease, reservation, restriction, servitude, charge or similar right or any other lien of any kind on such property and (y) the Fair Value to the transferee of any property shall not reflect any reduction relating to the fact that such property may be of less value to a Person which is not the owner or operator of the property or any portion thereof than to a Person which is such owner or operator. Fair Value may be determined, without physical inspection, by the use of accounting and engineering records and other data maintained by the Company or the transferee or otherwise available to the Expert certifying the same.

"INDEPENDENT EXPERT'S CERTIFICATE" means a certificate signed by an authorized officer of the transferee and by an Independent Expert (which Independent Expert shall be selected either by the board of directors or by an authorized officer of the transferee, the execution of such certificate by such authorized officer to be conclusive evidence of such selection) and delivered to the Trustee. For purposes of this definition, (a) "EXPERT" means a Person which is an engineer, appraiser or other expert and which, with respect to any certificate to be signed by such Person and delivered to the Trustee, is qualified to pass upon the matter set forth in such certificate; (b) "ENGINEER" means a Person engaged in the engineering profession or otherwise qualified to pass upon engineering matters (including, but not limited to, a Person licensed as a professional engineer, whether

or not then engaged in the engineering profession) and (c) "APPRAISER" means a Person engaged in the business of appraising property or otherwise qualified to pass upon the Fair Value or fair market value of property. "INDEPENDENT", when applied to any Expert, means such a Person who (a) is in fact independent, (b) does not have any direct material financial interest in the transferee or in any obligor upon the Securities or in any Affiliate of the transferee, (c) is not connected with the transferee or such other obligor as an officer, employee, promoter, underwriter, trustee, partner, director or any person performing similar functions and (d) is approved by the Trustee in the exercise of reasonable care.

#### ARTICLE ELEVEN

#### SUPPLEMENTAL INDENTURES

#### SECTION 1101. SUPPLEMENTAL INDENTURES WITHOUT CONSENT OF HOLDERS.

Without the consent of any Holders, the Company and the Trustee, at any time and from time to time, may enter into one or more indentures supplemental hereto, in form reasonably satisfactory to the Trustee, for any of the following purposes:

(a) to evidence the succession of another Person to the Company and the assumption by any such successor of the covenants of the Company herein and in the Securities, all as provided in Article Ten; or

(b) to add one or more covenants of the Company or other provisions for the benefit of all Holders or for the benefit of the Holders of, or to remain in effect only so long as there shall be Outstanding, Securities of one or more specified series, or one or more specified Tranches thereof, or to surrender any right or power herein conferred upon the Company; or

(c) to change or eliminate any provision of this Indenture or to add any new provision to this Indenture; provided, however, that if such change, elimination or addition shall adversely affect the interests of the Holders of Outstanding Securities of any series or Tranche in any material respect, such change, elimination or addition shall become effective with respect to such series or Tranche only in accordance with the provisions of Section 1102 or when no Security of such series or Tranche remains Outstanding; or

(d) to provide collateral security for the Securities or any series thereof; or

(e) to establish the form or terms of Securities of any series or Tranche as contemplated by Sections 201 and 301; or

(f) to provide for the authentication and delivery of bearer securities and coupons appertaining thereto representing interest, if any, thereon and for the procedures for the registration, exchange and replacement thereof and for the giving of notice to, and the solicitation of the vote or consent of, the holders thereof, and for any and all other matters incidental thereto; or

(g) to evidence and provide for the acceptance of appointment hereunder by a successor Trustee with respect to the Securities of one or more series and to add to or change any of the provisions of this Indenture as shall be necessary to provide for or facilitate the administration of the trusts hereunder by more than one Trustee, pursuant to the requirements of Section 811(b); or

(h) to provide for the procedures required to permit the Company to utilize, at its option, a non-certificated system of registration for all, or any series or Tranche of, the Securities; or

(i) to change any place or places where (1) the principal of and premium, if any, and interest, if any, on all or any series of Securities, or any Tranche thereof, shall be payable, (2) all or any series of Securities, or any Tranche thereof, may be surrendered for registration of transfer, (3) all or any series of Securities, or any Tranche thereof, may be surrendered for exchange and (4) notices and demands to or upon the Company in respect of all or any series of Securities, or any Tranche thereof, and this Indenture may be served; or

(j) to cure any ambiguity, to correct or supplement any provision herein which may be defective or inconsistent with any other provision herein; or to make any other changes to the provisions hereof or to add other provisions with respect to matters or questions arising under this Indenture, provided that such other changes or additions shall not adversely affect the interests of the Holders of Securities of any series or Tranche in any material respect.

Without limiting the generality of the foregoing, if the Trust Indenture Act as in effect at the date of the execution and delivery of this Indenture or at any time thereafter shall be amended and

(x) if any such amendment shall require one or more changes to any provisions hereof or the inclusion herein of any additional provisions, or shall by operation of law be deemed to effect such changes or incorporate such provisions by reference or otherwise, this Indenture shall be deemed to have been amended so as to conform to such amendment to the Trust Indenture Act, and the Company and the Trustee may, without the consent of any Holders, enter into an indenture supplemental hereto to evidence such amendment hereof; or

(y) if any such amendment shall permit one or more changes to, or the elimination of, any provisions hereof which, at the date of the execution and delivery hereof or at any time thereafter, are required by the Trust Indenture Act to be contained herein or are contained herein to reflect any provisions of the Trust Indenture Act as in effect at such date, this Indenture shall be deemed to have been amended to effect such changes or elimination, and the Company and the Trustee may, without the consent of any Holders, enter into an indenture supplemental hereto to evidence such amendment.

#### SECTION 1102. SUPPLEMENTAL INDENTURES WITH CONSENT OF HOLDERS.

Subject to the provisions of Section 1101, with the consent of the Holders of a majority in aggregate principal amount of the Securities of all series then Outstanding under this Indenture, considered as one class, by Act of said Holders delivered to the Company and the Trustee, the Company and the Trustee may enter into an indenture or indentures supplemental hereto for the purpose of adding any provisions to, or changing in any manner or eliminating any of the provisions of, this Indenture; provided, however, that if there shall be Securities of more than one series Outstanding hereunder and if a proposed supplemental indenture shall directly affect the rights of the Holders of Securities of one or more, but less than all, of such series, then the consent only of the Holders of a majority in aggregate principal amount of the Outstanding Securities of all series so directly affected, considered as one class, shall be required; and provided, further, that if the Securities of any series shall have been issued in more than one Tranche and if the proposed supplemental indenture shall directly affect the rights of the Holders of Securities of one or more, but less than all, of such Tranches, then the consent only of the Holders of a majority in aggregate principal amount of the Outstanding Securities of all Tranches so directly affected, considered as one class, shall be required; and provided, further, that no such supplemental indenture shall:

(a) change the Stated Maturity of the principal of, or any installment of principal of or interest on, any Security other than pursuant to the terms thereof, or reduce the principal amount thereof or the rate of interest thereon (or the amount of any installment of interest thereon) or change the method of calculating such rate or reduce any premium payable thereon, or reduce the amount of the principal of any Discount Security that would be due and payable upon a declaration of acceleration of the Maturity thereof pursuant to Section 702, or change the coin or currency (or other property), in which any Security or premium, if any, or interest, if any, thereon is payable, or impair the right to institute suit for the enforcement of any such payment on or after the Maturity of any Security, without, in any such case, the consent of the Holder of such Security; or

(b) reduce the percentage in principal amount of the Outstanding Securities of any series (or, if applicable, in liquidation preference of any series of Trust Securities), or any Tranche thereof, the consent of the Holders of which is required for any such supplemental indenture, or the consent of the Holders of which

is required for any waiver of compliance with any provision of this Indenture or of any default hereunder and its consequences, or reduce the requirements of Section 1204 for quorum or voting, without, in any such case, the consent of the Holder of each Outstanding Security of such series or Tranche; or

(c) modify any of the provisions of this Section, Section 506 or Section 713 with respect to the Securities of any series or any Tranche thereof (except to increase the percentages in principal amount referred to in this Section or such other Sections or to provide that other provisions of this Indenture cannot be modified or waived) without, in any such case, the consent of the Holder of each Outstanding Security of such series or Tranche; provided, however, that this clause shall not be deemed to require the consent of any Holder with respect to changes in the references to "the Trustee" and concomitant changes in this Section, or the deletion of this proviso, in accordance with the requirements of Sections 811(b) and 1101(g).

A supplemental indenture which (x) changes or eliminates any covenant or other provision of this Indenture which has expressly been included solely for the benefit of the Holders of, or which is to remain in effect only so long as there shall be Outstanding, Securities of one or more specified series, or one or more Tranches thereof, or (y) modifies the rights of the Holders of Securities of such series or Tranches with respect to such covenant or other provision, shall be deemed not to affect the rights under this Indenture of the Holders of Securities of any other series or Tranche.

Notwithstanding the foregoing, so long as any of the Preferred Securities remain outstanding, the Trustee may not consent to a supplemental indenture under this Section 1102 without the prior consent, obtained as provided in a Declaration pertaining to a Trust which issued such Preferred Securities of the holders of not less than a majority in aggregate liquidation preference of all Trust Securities issued by such Trust affected, considered as one class, or, in the case of changes described in clauses (a), (b) and (c) above, 100% in aggregate liquidation preference of all such Preferred Securities then outstanding which would be affected thereby, considered as one class.

It shall not be necessary for any Act of Holders under this Section to approve the particular form of any proposed supplemental indenture, but it shall be sufficient if such Act shall approve the substance thereof.

Anything in this Indenture to the contrary notwithstanding, if the Officer's Certificate, supplemental indenture or Board Resolution, as the case may be, establishing the Securities of any series or Tranche shall so provide, (a) the Holders of such Securities shall be deemed to have consented to a supplemental indenture containing the additions, changes or eliminations to or from the Indenture which shall be specified in such Officer's Certificate, supplemental indenture or Board Resolution establishing such series or Tranche, (b) no Act of such Holders shall be required to evidence such consent and (c) such consent may be counted in the



determination of whether or not the Holders of the requisite principal amount of Securities shall have consented to such supplemental indenture.

SECTION 1103. EXECUTION OF SUPPLEMENTAL INDENTURES.

In executing, or accepting the additional trusts created by, any supplemental indenture permitted by this Article or the modifications thereby of the trusts created by this Indenture, the Trustee shall be entitled to receive, and (subject to Section 801) shall be fully protected in relying upon, an Opinion of Counsel stating that the execution of such supplemental indenture is authorized or permitted by this Indenture. The Trustee may, but shall not be obligated to, enter into any such supplemental indenture which affects the Trustee's own rights, duties, immunities or liabilities under this Indenture or otherwise.

SECTION 1104. EFFECT OF SUPPLEMENTAL INDENTURES.

Upon the execution and delivery of any supplemental indenture under this Article this Indenture shall be modified in accordance therewith, and such supplemental indenture shall form a part of this Indenture for all purposes; and every Holder of Securities theretofore or thereafter authenticated and delivered hereunder shall be bound thereby. Any supplemental indenture permitted by this Article may restate this Indenture in its entirety, and, upon the execution and delivery thereof, any such restatement shall supersede this Indenture as theretofore in effect for all purposes.

SECTION 1105. CONFORMITY WITH TRUST INDENTURE ACT.

Every supplemental indenture executed pursuant to this Article shall conform to the requirements of the Trust Indenture Act.

SECTION 1106. REFERENCE IN SECURITIES TO SUPPLEMENTAL INDENTURES.

Securities of any series, or any Tranche thereof, authenticated and delivered after the execution of any supplemental indenture pursuant to this Article may, and shall if required by the Trustee, bear a notation in form approved by the Trustee as to any matter provided for in such supplemental indenture. If the Company shall so determine, new Securities of any series, or any Tranche thereof, so modified as to conform, in the opinion of the Trustee and the Company, to any such supplemental indenture may be prepared and executed by the Company and authenticated and delivered by the Trustee in exchange for Outstanding Securities of such series or Tranche.

SECTION 1107. MODIFICATION WITHOUT SUPPLEMENTAL INDENTURE.

To the extent, if any, that the terms of any particular series of Securities shall have been established in or pursuant to an Officer's Certificate or a Board Resolution as contemplated by Section 301, and not in a supplemental indenture hereto, additions to, changes in or the elimination of any of such terms may be effected by means of a supplemental Officer's Certificate or a

supplemental Board Resolution, as the case may be, delivered to, and accepted by, the Trustee; provided, however, that such supplemental Officer's Certificate or supplemental Board Resolution shall not be accepted by the Trustee or otherwise be effective unless all conditions set forth in this Indenture which would be required to be satisfied if such additions, changes or elimination were contained in a supplemental indenture shall have been appropriately satisfied. Upon the acceptance thereof by the Trustee, any supplemental Officer's Certificate or supplemental Board Resolution shall be deemed to be a "supplemental indenture" for purposes of Section 1104 and 1106.

## ARTICLE TWELVE

### MEETINGS OF HOLDERS; ACTION WITHOUT MEETING

#### SECTION 1201. PURPOSES FOR WHICH MEETINGS MAY BE CALLED.

A meeting of Holders of Securities of one or more, or all, series, or any Tranche or Tranches thereof, may be called at any time and from time to time pursuant to this Article to make, give or take any request, demand, authorization, direction, notice, consent, waiver or other action provided by this Indenture to be made, given or taken by Holders of Securities of such series or Tranches.

#### SECTION 1202. CALL, NOTICE AND PLACE OF MEETINGS.

(a) The Trustee may at any time call a meeting of Holders of Securities of one or more, or all, series, or any Tranche or Tranches thereof, for any purpose specified in Section 1201, to be held at such time and (except as provided in subsection (b) of this Section) at such place in the Borough of Manhattan, The City of New York, as the Trustee shall determine, or, with the approval of the Company, at any other place. Notice of every such meeting, setting forth the time and the place of such meeting and in general terms the action proposed to be taken at such meeting, shall be given, in the manner provided in Section 106, not less than twenty-one (21) nor more than one hundred eighty (180) days prior to the date fixed for the meeting.

(b) The Trustee may be asked to call a meeting of the Holders of Securities of one or more, or all, series, or any Tranche or Tranches thereof, by the Company or by the Holders of thirty-three per centum (33%) in aggregate principal amount of all of such series and Tranches, considered as one class, for any purpose specified in Section 1201, by written request setting forth in reasonable detail the action proposed to be taken at the meeting. If the Trustee shall have been asked by the Company to call such a meeting, the Company shall determine the time and place for such meeting and may call such meeting by giving notice thereof in the manner provided in subsection (a) of this Section, or shall direct the Trustee, in the name and at the expense of the Company, to give such notice. If the Trustee shall have been asked to call such a meeting by Holders in accordance with this subsection (b), and the Trustee shall not have given the notice of such meeting within twenty-one (21) days after receipt of such request or shall not thereafter proceed to cause the meeting to be held as provided herein, then the Holders of Securities of such

series and Tranches, in the principal amount above specified, may determine the time and the place in the Borough of Manhattan, The City of New York, or in such other place as shall be determined or approved by the Company for such meeting and may call such meeting for such purposes by giving notice thereof as provided in subsection (a) of this Section.

(c) Any meeting of Holders of Securities of one or more, or all, series, or any Tranche or Tranches thereof, shall be valid without notice if the Holders of all Outstanding Securities of such series or Tranches are present in person or by proxy and if representatives of the Company and the Trustee are present, or if notice is waived in writing before or after the meeting by the Holders of all Outstanding Securities of such series, or any Tranche or Tranches thereof, or by such of them as are not present at the meeting in person or by proxy, and by the Company and the Trustee.

#### SECTION 1203. PERSONS ENTITLED TO VOTE AT MEETINGS.

To be entitled to vote at any meeting of Holders of Securities of one or more, or all, series, or any Tranche or Tranches thereof, a Person shall be (a) a Holder of one or more Outstanding Securities of such series or Tranches, or (b) a Person appointed by an instrument in writing as proxy for a Holder or Holders of one or more Outstanding Securities of such series or Tranches by such Holder or Holders. The only Persons who shall be entitled to attend any meeting of Holders of Securities of any series or Tranche shall be the Persons entitled to vote at such meeting and their counsel, any representatives of the Trustee and its counsel and any representatives of the Company and its counsel.

#### SECTION 1204. QUORUM; ACTION.

The Persons entitled to vote a majority in aggregate principal amount of the Outstanding Securities of the series and Tranches with respect to which a meeting shall have been called as hereinbefore provided, considered as one class, shall constitute a quorum for a meeting of Holders of Securities of such series and Tranches; provided, however, that if any action is to be taken at such meeting which this Indenture expressly provides may be taken by the Holders of a specified percentage, which is less than a majority, in principal amount of the Outstanding Securities of such series and Tranches, considered as one class, the Persons entitled to vote such specified percentage in principal amount of the Outstanding Securities of such series and Tranches, considered as one class, shall constitute a quorum. In the absence of a quorum within one hour of the time appointed for any such meeting, the meeting shall, if convened at the request of Holders of Securities of such series and Tranches, be dissolved. In any other case the meeting may be adjourned for such period as may be determined by the chairman of the meeting prior to the adjournment of such meeting. In the absence of a quorum at any such adjourned meeting, such adjourned meeting may be further adjourned for such period as may be determined by the chairman of the meeting prior to the adjournment of such adjourned meeting. Except as provided by Section 1205(e), notice of the reconvening of any meeting adjourned for more than thirty (30) days shall be given as provided in Section 106 not less than ten (10) days prior to the date on which the meeting

is scheduled to be reconvened. Notice of the reconvening of an adjourned meeting shall state expressly the percentage, as provided above, of the principal amount of the Outstanding Securities of such series and Tranches which shall constitute a quorum.

Except as limited by Section 1102, any resolution presented to a meeting or adjourned meeting duly reconvened at which a quorum is present as aforesaid may be adopted only by the affirmative vote of the Holders of a majority in aggregate principal amount of the Outstanding Securities of the series and Tranches with respect to which such meeting shall have been called, considered as one class; provided, however, that, except as so limited, any resolution with respect to any action which this Indenture expressly provides may be taken by the Holders of a specified percentage, which is less than a majority, in principal amount of the Outstanding Securities of such series and Tranches, considered as one class, may be adopted at a meeting or an adjourned meeting duly reconvened and at which a quorum is present as aforesaid by the affirmative vote of the Holders of such specified percentage in principal amount of the Outstanding Securities of such series and Tranches, considered as one class.

Any resolution passed or decision taken at any meeting of Holders of Securities duly held in accordance with this Section shall be binding on all the Holders of Securities of the series and Tranches with respect to which such meeting shall have been held, whether or not present or represented at the meeting.

SECTION 1205. ATTENDANCE AT MEETINGS; DETERMINATION OF VOTING RIGHTS; CONDUCT AND ADJOURNMENT OF MEETINGS.

(a) Attendance at meetings of Holders of Securities may be in person or by proxy; and, to the extent permitted by law, any such proxy shall remain in effect and be binding upon any future Holder of the Securities with respect to which it was given unless and until specifically revoked by the Holder or future Holder (except as provided in Section 104(g)) of such Securities before being voted.

(b) Notwithstanding any other provisions of this Indenture, the Trustee may make such reasonable regulations as it may deem advisable for any meeting of Holders of Securities in regard to proof of the holding of such Securities and of the appointment of proxies and in regard to the appointment and duties of inspectors of votes, the submission and examination of proxies, certificates and other evidence of the right to vote, and such other matters concerning the conduct of the meeting as it shall deem appropriate. Except as otherwise permitted or required by any such regulations and approved by the Company, the holding of Securities shall be proved in the manner specified in Section 104 and the appointment of any proxy shall be proved in the manner specified in Section 104. Such regulations may provide that written instruments appointing proxies, regular on their face, may be presumed valid and genuine without the proof specified in Section 104 or other proof.

(c) The Trustee shall, by an instrument in writing, appoint a temporary chairman of the meeting, unless the meeting shall have been called by the Company or by Holders as provided in Section 1202(b), in which case the Company or the Holders of Securities of the series and Tranches calling the meeting, as the case may be, shall in like manner appoint a temporary chairman. A permanent chairman and a permanent secretary of the meeting shall be elected by vote of the Persons entitled to vote a majority in aggregate principal amount of the Outstanding Securities of all series and Tranches represented at the meeting, considered as one class.

(d) At any meeting each Holder or proxy shall be entitled to one vote for each One Thousand Dollars (\$1,000) principal amount of Outstanding Securities held or represented by such Holder; provided, however, that no vote shall be cast or counted at any meeting in respect of any Security challenged as not Outstanding and ruled by the chairman of the meeting to be not Outstanding. The chairman of the meeting shall have no right to vote, except as a Holder of a Security or proxy.

(e) Any meeting duly called pursuant to Section 1202 at which a quorum is present may be adjourned from time to time by Persons entitled to vote a majority in aggregate principal amount of the Outstanding Securities of all series and Tranches represented at the meeting, considered as one class; and the meeting may be held as so adjourned without further notice.

#### SECTION 1206. COUNTING VOTES AND RECORDING ACTION OF MEETINGS.

The vote upon any resolution submitted to any meeting of Holders shall be by written ballots on which shall be subscribed the signatures of the Holders or of their representatives by proxy and the principal amounts and serial numbers of the Outstanding Securities, of the series and Tranches with respect to which the meeting shall have been called, held or represented by them. The permanent chairman of the meeting shall appoint two inspectors of votes who shall count all votes cast at the meeting for or against any resolution and who shall make and file with the secretary of the meeting their verified written reports of all votes cast at the meeting. A record in duplicate of the proceedings of each meeting of Holders shall be prepared by the secretary of the meeting and there shall be attached to such record the original reports of the inspectors of votes on any vote by ballot taken thereat and affidavits by one or more persons having knowledge of the facts setting forth a copy of the notice of the meeting and showing that such notice was given as provided in Section 1202 and, if applicable, Section 1204. Each copy shall be signed and verified by the affidavits of the permanent chairman and secretary of the meeting and one such copy shall be delivered to the Company, and another to the Trustee to be preserved by the Trustee, the latter to have attached thereto the ballots voted at the meeting. Any record so signed and verified shall be conclusive evidence of the matters therein stated.

#### SECTION 1207. ACTION WITHOUT MEETING.

In lieu of a vote of Holders at a meeting as hereinbefore contemplated in this Article, any request, demand, authorization, direction, notice, consent, waiver or other action may be made, given or taken by Holders by written instruments as provided in Section 104.

#### ARTICLE THIRTEEN

##### IMMUNITY OF INCORPORATORS, STOCKHOLDERS, OFFICERS AND DIRECTORS

###### SECTION 1301. LIABILITY SOLELY CORPORATE.

No recourse shall be had for the payment of the principal of or premium, if any, or interest, if any, on any Securities, or any part thereof, or for any claim based thereon or otherwise in respect thereof, or of the indebtedness represented thereby, or upon any obligation, covenant or agreement under this Indenture, against any incorporator, stockholder, officer or director, as such, past, present or future, of the Company or of any predecessor or successor of either of them (either directly or through the Company or a predecessor or successor of either of them), whether by virtue of any constitutional provision, statute or rule of law or by the enforcement of any assessment or penalty or otherwise; it being expressly agreed and understood that this Indenture and all the Securities are solely corporate obligations and that no personal liability whatsoever shall attach to, or be incurred by, any incorporator, stockholder, officer or director, past, present or future, of the Company or of any predecessor or successor, either directly or indirectly through the Company or any predecessor or successor, because of the indebtedness hereby authorized or under or by reason of any of the obligations, covenants or agreements contained in this Indenture or in any of the Securities or to be implied herefrom or therefrom; and such personal liability, if any, is hereby expressly waived and released as a condition of, and as part of the consideration for, the execution and delivery of this Indenture and the issuance of the Securities.

#### ARTICLE FOURTEEN

##### SUBORDINATION OF SECURITIES

###### SECTION 1401. SECURITIES SUBORDINATE TO SENIOR INDEBTEDNESS.

The Company, for itself, its successors and assigns, covenants and agrees, and each Holder of the Securities of each series, by its acceptance thereof, likewise covenants and agrees, that the payment of the principal of and premium, if any, and interest, if any, on each and all of the Securities is hereby expressly subordinated and subject to the extent and in the manner set forth in this Article, in right of payment to the prior payment in full of all Senior Indebtedness of the Company.

Each Holder of the Securities of each series, by its acceptance thereof, authorizes and directs the Trustee on its behalf to take such action as may be necessary or appropriate to effectuate the subordination as provided in this Article, and appoints the Trustee its attorney-in-fact for any and all such purposes.

#### SECTION 1402. PAYMENT OVER OF PROCEEDS OF SECURITIES.

In the event (a) of any insolvency or bankruptcy proceedings or any receivership, liquidation, reorganization or other similar proceedings in respect of the Company or a substantial part of its property, or of any proceedings for liquidation, dissolution or other winding-up of the Company, whether or not involving insolvency or bankruptcy, or (b) subject to the provisions of Section 1403, that (i) a default shall have occurred with respect to the payment of principal of or interest on or other monetary amounts due and payable on any Senior Indebtedness of the Company, or (ii) there shall have occurred a default (other than a default in the payment of principal or interest or other monetary amounts due and payable) in respect of any Senior Indebtedness, as defined therein or in the instrument under which the same is outstanding, permitting the holder or holders thereof to accelerate the maturity thereof (with notice or lapse of time, or both), and such default shall have continued beyond the period of grace, if any, in respect thereof, and, in the case of subclauses (i) and (ii) of this clause (b), such default shall not have been cured or waived or shall not have ceased to exist, or (c) that the principal of and accrued interest on the Securities of any Series shall have been declared due and payable pursuant to Section 701 and such declaration shall not have been rescinded and annulled as provided in Section 702, then:

(1) the holders of all Senior Indebtedness of the Company shall first be entitled to receive payment of the full amount due thereon, or provision shall be made for such payment in money or money's worth, before the Holders of any of the Securities are entitled to receive a payment on account of the principal of or interest on the indebtedness evidenced by the Securities, including, without limitation, any payments made pursuant to Article Four;

(2) any payment by, or distribution of assets of, the Company of any kind or character, whether in cash, property or securities, to which any Holder or the Trustee would be entitled except for the provisions of this Article, shall be paid or delivered by the Person making such payment or distribution, whether a trustee in bankruptcy, a receiver or liquidating trustee or otherwise, directly to the holders of such Senior Indebtedness of the Company or their representative or representatives or to the trustee or trustees under any indenture under which any instruments evidencing any of such Senior Indebtedness of the Company may have been issued, ratably according to the aggregate amounts remaining unpaid on account of such Senior Indebtedness of the Company held or represented by each, to the extent necessary to make payment in full of all Senior Indebtedness of the Company remaining unpaid after giving effect to any concurrent payment or

distribution (or provision therefor) to the holders of such Senior Indebtedness of the Company, before any payment or distribution is made to the Holders of the indebtedness evidenced by the Securities or to the Trustee under this Indenture; and

(3) in the event that, notwithstanding the foregoing, any payment by, or distribution of assets of, the Company of any kind or character, whether in cash, property or securities, in respect of principal of or interest on the Securities or in connection with any repurchase by the Company of the Securities, shall be received by the Trustee or any Holder before all Senior Indebtedness of the Company is paid in full, or provision is made for such payment in money or money's worth, such payment or distribution in respect of principal of or interest on the Securities or in connection with any repurchase by the Company of the Securities shall be paid over to the holders of such Senior Indebtedness of the Company or their representative or representatives or to the trustee or trustees under any indenture under which any instruments evidencing any such Senior Indebtedness of the Company may have been issued, ratably as aforesaid, for application to the payment of all Senior Indebtedness of the Company remaining unpaid until all such Senior Indebtedness of the Company shall have been paid in full, after giving effect to any concurrent payment or distribution (or provision therefor) to the holders of such Senior Indebtedness of the Company.

Notwithstanding the foregoing, at any time after the 123rd day following the date of deposit of cash or Eligible Obligations pursuant to Section 601 (provided all conditions set out in such Section shall have been satisfied), the funds so deposited and any interest thereon will not be subject to any rights of holders of Senior Indebtedness of the Company including, without limitation, those arising under this Article Fourteen; provided that no event described in clause (e) of Section 701 with respect to the Company has occurred during such 123-day period.

For purposes of this Article only, the words "cash, property or securities" shall not be deemed to include shares of stock of the Company as reorganized or readjusted, or securities of the Company or any other corporation provided for by a plan or reorganization or readjustment which are subordinate in right of payment to all Senior Indebtedness of the Company which may at the time be outstanding to the same extent as, or to a greater extent than, the Securities are so subordinated as provided in this Article. The consolidation of the Company with, or the merger of the Company into, another corporation or the liquidation or dissolution of the Company following the conveyance or transfer of its property as an entirety, or substantially as an entirety, to another corporation upon the terms and conditions provided for in Article Ten hereof shall not be deemed a dissolution, winding-up, liquidation or reorganization for the purposes of this Section 1402 if such other corporation shall, as a part of such consolidation, merger, conveyance or transfer, comply with the conditions stated in Article Ten hereof. Nothing in Section 1401 or in this Section 1402 shall apply to claims of, or payments to, the Trustee under or pursuant to Section 807.



SECTION 1403. DISPUTES WITH HOLDERS OF CERTAIN SENIOR INDEBTEDNESS.

Any failure by the Company to make any payment on or perform any other obligation in respect of Senior Indebtedness of the Company, other than any indebtedness incurred by the Company or assumed or guaranteed, directly or indirectly, by the Company for money borrowed (or any deferral, renewal, extension or refunding thereof) or any other obligation as to which the provisions of this Section shall have been waived by the Company in the instrument or instruments by which the Company incurred, assumed, guaranteed or otherwise created such indebtedness or obligation, shall not be deemed a default under clause (b) of Section 1402 if (i) the Company shall be disputing its obligation to make such payment or perform such obligation and (ii) either (A) no final judgment relating to such dispute shall have been issued against the Company which is in full force and effect and is not subject to further review, including a judgment that has become final by reason of the expiration of the time within which a party may seek further appeal or review, or (B) in the event that a judgment that is subject to further review or appeal has been issued, the Company shall in good faith be prosecuting an appeal or other proceeding for review and a stay or execution shall have been obtained pending such appeal or review.

SECTION 1404. SUBROGATION.

Senior Indebtedness of the Company shall not be deemed to have been paid in full unless the holders thereof shall have received cash (or securities or other property satisfactory to such holders) in full payment of such Senior Indebtedness of the Company then outstanding. Subject to the prior payment in full of all Senior Indebtedness of the Company, the rights of the Holders of the Securities shall be subrogated to the rights of the holders of Senior Indebtedness of the Company to receive any further payments or distributions of cash, property or securities of the Company applicable to the holders of the Senior Indebtedness of the Company until all amounts owing on the Securities shall be paid in full; and such payments or distributions of cash, property or securities received by the Holders of the Securities, by reason of such subrogation, which otherwise would be paid or distributed to the holders of such Senior Indebtedness of the Company shall, as between the Company, its creditors other than the holders of Senior Indebtedness of the Company, and the Holders, be deemed to be a payment by the Company to or on account of Senior Indebtedness of the Company, it being understood that the provisions of this Article are and are intended solely for the purpose of defining the relative rights of the Holders, on the one hand, and the holders of the Senior Indebtedness of the Company, on the other hand.

SECTION 1405. OBLIGATION OF THE COMPANY UNCONDITIONAL.

Nothing contained in this Article or elsewhere in this Indenture or in the Securities is intended to or shall impair, as among the Company, its creditors other than the holders of Senior Indebtedness of the Company and the Holders, the obligation of the Company, which is absolute and unconditional, to pay to the Holders the principal of and interest on the Securities as and when the same shall become due and payable in accordance with their terms, or is intended to or shall affect the relative rights of the Holders and creditors of the Company other than the holders of

Senior Indebtedness of the Company, nor shall anything herein or therein prevent the Trustee or any Holder from exercising all remedies otherwise permitted by applicable law upon default under this Indenture, subject to the rights, if any, under this Article of the holders of Senior Indebtedness of the Company in respect of cash, property or securities of the Company received upon the exercise of any such remedy.

Upon any payment or distribution of assets or securities of the Company referred to in this Article, the Trustee and the Holders shall be entitled to rely upon any order or decree of a court of competent jurisdiction in which such dissolution, winding-up, liquidation or reorganization proceedings are pending for the purpose of ascertaining the Persons entitled to participate in such distribution, the holders of the Senior Indebtedness of the Company and other indebtedness of the Company, the amount thereof or payable thereon, the amount or amounts paid or distributed thereon, and all other facts pertinent thereto or to this Article.

SECTION 1406. PRIORITY OF SENIOR INDEBTEDNESS UPON MATURITY.

Upon the maturity of the principal of any Senior Indebtedness of the Company by lapse of time, acceleration or otherwise, all matured principal of Senior Indebtedness of the Company and interest and premium, if any, thereon shall first be paid in full before any payment of principal or premium, if any, or interest, if any, is made upon the Securities or before any Securities can be acquired by the Company or any sinking fund payment is made with respect to the Securities (except that required sinking fund payments may be reduced by Securities acquired before such maturity of such Senior Indebtedness of the Company).

SECTION 1407. TRUSTEE AS HOLDER OF SENIOR INDEBTEDNESS.

The Trustee shall be entitled to all rights set forth in this Article with respect to any Senior Indebtedness of the Company at any time held by it, to the same extent as any other holder of Senior Indebtedness of the Company. Nothing in this Article shall deprive the Trustee of any of its rights as such holder.

SECTION 1408. NOTICE TO TRUSTEE TO EFFECTUATE SUBORDINATION.

Notwithstanding the provisions of this Article or any other provision of the Indenture, the Trustee shall not be charged with knowledge of the existence of any facts which would prohibit the making of any payment of moneys to or by the Trustee unless and until a Responsible Officer of the Trustee shall have received written notice thereof from the Company, from a Holder or from a holder of any Senior Indebtedness of the Company or from any representative or representatives of such holder or any trustee or trustees under any indenture under which any instruments evidencing any such Senior Indebtedness of the Company may have been issued and, prior to the receipt of any such written notice, the Trustee shall be entitled, subject to Section 801, in all respects to assume that no such facts exist; provided, however, that, if prior to the fifth Business Day preceding the date upon which by the terms hereof any such moneys may

become payable for any purpose, or in the event of the execution of an instrument pursuant to Section 602 acknowledging that Securities or portions thereof are deemed to have been paid for all purposes of this Indenture, acknowledging that the entire indebtedness of the Company in respect thereof has been satisfied and discharged or acknowledging satisfaction and discharge of this Indenture, then if prior to the second Business Day preceding the date of such execution, the Trustee shall not have received with respect to such moneys the notice provided for in this Section, then, anything herein contained to the contrary notwithstanding, the Trustee may, in its discretion, receive such moneys and/or apply the same to the purpose for which they were received, and shall not be affected by any notice to the contrary, which may be received by it on or after such date; provided, however, that no such application shall affect the obligations under this Article of the persons receiving such moneys from the Trustee.

SECTION 1409. MODIFICATION, EXTENSION, ETC. OF SENIOR INDEBTEDNESS OF THE COMPANY.

The holders of Senior Indebtedness of the Company may, without affecting in any manner the subordination of the payment of the principal of and premium, if any, and interest, if any, on the Securities, at any time or from time to time and in their absolute discretion, agree with the Company to change the manner, place or terms of payment, change or extend the time of payment of, or renew or alter, any Senior Indebtedness of the Company, or amend or supplement any instrument pursuant to which any Senior Indebtedness of the Company is issued, or exercise or refrain from exercising any other of their rights under the Senior Indebtedness of the Company including, without limitation, the waiver of default thereunder, all without notice to or assent from the Holders or the Trustee.

SECTION 1410. TRUSTEE HAS NO FIDUCIARY DUTY TO HOLDERS OF SENIOR INDEBTEDNESS OF THE COMPANY.

With respect to the holders of Senior Indebtedness of the Company, the Trustee undertakes to perform or to observe only such of its covenants and objectives as are specifically set forth in this Indenture, and no implied covenants or obligations with respect to the holders of Senior Indebtedness of the Company shall be read into this Indenture against the Trustee. The Trustee shall not be deemed to owe any fiduciary duty to the holders of Senior Indebtedness of the Company, and shall not be liable to any such holders if it shall mistakenly pay over or deliver to the Holders or the Company or any other Person, money or assets to which any holders of Senior Indebtedness of the Company shall be entitled by virtue of this Article or otherwise.

SECTION 1411. PAYING AGENTS OTHER THAN THE TRUSTEE.

In case at any time any Paying Agent other than the Trustee shall have been appointed by the Company and be then acting hereunder, the term "Trustee" as used in this Article shall in such case (unless the context shall otherwise require) be construed as extending to and including such Paying Agent within its meaning as fully for all intents and purposes as if such Paying Agent were named in this Article in addition to or in place of the Trustee; provided,

however, that Sections 1407, 1408 and 1410 shall not apply to the Company if it acts as Paying Agent.

SECTION 1412. RIGHTS OF HOLDERS OF SENIOR INDEBTEDNESS NOT IMPAIRED.

No right of any present or future holder of Senior Indebtedness of the Company to enforce the subordination herein shall at any time or in any way be prejudiced or impaired by any act or failure to act on the part of the Company or by any noncompliance by the Company with the terms, provisions and covenants of this Indenture, regardless of any knowledge thereof any such holder may have or be otherwise charged with.

SECTION 1413. EFFECT OF SUBORDINATION PROVISIONS; TERMINATION.

Notwithstanding anything contained herein to the contrary, other than as provided in the immediately succeeding sentence, all the provisions of this Indenture shall be subject to the provisions of this Article, so far as the same may be applicable thereto.

Notwithstanding anything contained herein to the contrary, the provisions of this Article Fourteen shall be of no further effect and the Securities shall no longer be subordinated in right of payment to the prior payment of such Senior Indebtedness of the Company if the Company shall have delivered to the Trustee a notice to such effect. Any such notice delivered by the Company shall not be deemed to be a supplemental indenture for purposes of Article Twelve hereof.

ARTICLE FIFTEEN

EXCHANGE OF PREFERRED SECURITIES FOR SECURITIES

SECTION 1501. EXCHANGE OF PREFERRED SECURITIES FOR SECURITIES.

(a) If at any time the Company or any of its Affiliates (in either case, a "Company Affiliated Owner/Holder") is the owner or Holder of any Preferred Securities of a Trust, such Company Affiliated Owner/Holder shall have the right to deliver to the Institutional Trustee of such Trust all or such portion of its Preferred Securities as it elects and receive, in exchange therefore, a like amount of Securities. Such election (i) shall be exercisable effective on any Interest Payment Date by such Sponsor Affiliated Owner/Holder delivering to the Institutional Trustee a written notice of such election specifying the liquidation amount of Preferred Securities with respect to which such election is being made and the Interest Payment Date on which such exchange shall occur, which Interest Payment Date shall be not less than ten Business Days after the date of receipt by the Institutional Trustee or its designee the Preferred Securities which are the subject of such election by 10:00 A.M. New York time, on the Interest Payment Date on which such exchange is to occur. After the exchange, such Preferred Securities will be canceled and will no

longer be deemed to be outstanding and all rights of the Company or its Affiliate(s) with respect to such Preferred Securities will cease.

(b) In the case of an exchange described in Section 1501(a), the Trust will, on the date of such exchange, exchange Securities having a principal amount equal to the aggregate liquidation amount of the outstanding Common Securities of such Trust, multiplied by the ratio of the aggregate liquidation amount of the Preferred Securities exchanged pursuant to Section 1501(a) divided by the aggregate liquidation amount of the Preferred Securities outstanding immediately prior to such exchange, for such proportional amount of Common Securities held by the Sponsor (which contemporaneously shall be canceled and no longer be deemed to be outstanding); provided, that the Sponsor delivers or caused to be delivered to the Institutional Trustee or its designee the required amount of Common Securities to be exchanged by 10:00 A.M. New York time, on the Interest Payment Date on which such exchange is to occur.

This instrument may be executed in any number of counterparts, each of which so executed shall be deemed to be an original, but all such counterparts shall together constitute one and the same instrument.

IN WITNESS WHEREOF, the parties hereto have caused this Indenture to be duly executed as of the day and year first above written.

AVISTA CORPORATION

By: /s/ Malyn K. Malquist

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Name: Malyn K. Malquist  
Title: Senior Vice President,  
Chief Financial Officer and  
Treasurer

UNION BANK OF CALIFORNIA, N.A., Trustee

By: /s/ Sonia N. Flores

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Name: Sonia N. Flores  
Title: Vice President

AVISTA CORPORATION

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OFFICER'S CERTIFICATE

(Under Section 301 of the Indenture,  
dated as of April 1, 2004)

Establishing Series of Securities Designated  
Subordinated Debt Securities, Series due 2034

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April 5, 2004

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AVISTA CORPORATION

OFFICER'S CERTIFICATE  
(Under Section 301 of the Indenture,  
dated as of April 1, 2004)

I, Diane C. Thoren, Assistant Treasurer of AVISTA CORPORATION (the "Company"), in accordance with Section 301 of the Indenture, dated as of April 1, 2004 (the "Indenture", capitalized terms used herein and not defined herein having the meanings specified in the Indenture), of the Company to Union Bank of California, N.A., trustee (the "Trustee"), do hereby establish a series of Securities having the terms and characteristics set forth in this Officer's Certificate.

PART I

Set forth below in this Part I are the terms and characteristics of the series of Securities established hereby referred to in clauses (a) through (u) in the second paragraph of Section 301 of the Indenture (the lettered clauses set forth herein corresponding to such clauses in said Section 301).

(a) the title of the Securities of such series, being Series No. 1 under the Indenture, shall be "Subordinated Debt Securities, Series due 2034" (the Securities of such series, for purposes of this Officer's Certificate, being sometimes hereinafter called the "Notes"); the Notes are to be issued and sold to AVA Capital Trust III; and all references herein to the Declaration, the Institutional Trustee and the Trust Securities relate to the Trust;

(b) the aggregate principal amount of Notes which may be authenticated and delivered under the Indenture shall be limited to \$61,856,000, except as contemplated in Section 301(b) of the Indenture;

(c) interest on the Notes shall be payable to the Person or Persons in whose names the Notes are registered at the close of business on the Regular Record Date for such interest, except as otherwise expressly provided in the form of Note attached hereto and hereby authorized and approved;

(d) the principal of the Notes shall be payable on April 1, 2034;

(e) Article 4 of the Declaration sets forth the procedures to determine the Distribution Rate, Distribution Periods and Distribution Payment Dates for the Preferred Securities. While the Preferred Securities are outstanding, the Interest Rate, Interest Periods, Interest Payment Dates and associated terms relating to the Notes shall be the same as the Distribution Rate, Distribution Periods and Distribution Payment Dates and associated terms relating to the Preferred Securities, respectively. If the Trust is dissolved and the Notes are distributed to the holders of the Preferred Securities, the interest payable, Interest Rate, Interest Periods, Interest Payment Dates and the redemption provisions with respect to Fixed Rate Periods for the Preferred Securities and the Remarketing Procedures shall remain the same with respect to the Notes distributed to the holders of Preferred Securities except: (i) the effects of the



Declaration Events of Default will only be occasioned by the Events of Default and (ii) the cure and waiver provisions relating to the Declaration Events of Default will be superceded by the cure and waiver provisions relating to the Events of Default. In addition, if the Trust is dissolved and the Notes are distributed to the holders of the Preferred Securities, the below described procedures will be applicable to the Notes.

(i) interest payments shall accrue from the date of original issuance until Maturity or the Redemption Date. During the Initial Fixed Rate Period, interest will be payable semiannually in arrears on April 1 and October 1 of each year, commencing on October 1, 2004. During any Fixed Rate Period, other than the Initial Fixed Rate Period, interest will be payable semiannually in arrears on Interest Payment Dates determined based on the Remarketing Date (if the Notes are remarketed for a new Fixed Rate Period that begins on April 1 or October 1, interest will be payable on April 1 and October 1 of each year, and if the Notes are remarketed for a new Fixed Rate Period that begins on January 1 or July 1, interest will be payable on January 1 and July 1 of each year). During any Floating Rate Period, interest will be payable quarterly in arrears on January 1, April 1, July 1 and October 1 of each year;

(ii) if any Interest Payment Date with respect to a Fixed Rate Period is not a Business Day, interest will be payable, without additional interest, on the immediately succeeding Business Day, with the same force and effect as if payment was made on the date such payment was originally payable (and without the accrual of any additional amount of interest). If any Interest Payment Date with respect to a Floating Rate Period is not a Business Day, then interest will be payable on the immediately succeeding Business Day and interest shall accrue to the actual payment date (except for an Interest Payment Date that coincides with Maturity or the Redemption Date);

(iii) the amount of interest payable on each Interest Payment Date relating to a Fixed Rate Period will be computed on the basis of a 360-day year of twelve 30-day months. The amount of interest payable on each Interest Payment Date in respect of a Floating Rate Period will be computed by multiplying the per annum Interest Rate in effect for such Interest Period by a fraction, the numerator of which will be the actual number of days in such Interest Period (or portion thereof) (determined by including the first day thereof and excluding the last thereof) and the denominator of which will be 360, and multiplying the rate so obtained by \$1,000;

(iv) interest on the Notes will be deferred during any Extension Period (as defined below) but will continue to accrue. The payment of such interest, together with any interest thereon, will be distributed to the holders of Notes at the end of any Extension Period;

(v) each Note upon registration of transfer or in exchange for or in lieu of any other Note shall carry the rights of interest accrued and unpaid, and to accrue, which were carried by such other Note;

(vi) during the Initial Fixed Rate Period, the Interest Rate shall be the Initial Interest Rate;

(vii) prior to the expiration of the Initial Fixed Rate Period and any subsequent Fixed Rate Period or an Interest Period with respect to a Floating Rate Period or an Interest Period in a Fixed Rate Period during a time in which the Notes are redeemable in such Fixed Rate Period, the Company will have the option to remarket the Notes to establish a new Fixed Rate for a new Fixed Rate Period (to be in effect after the expiration of the then current Interest Period). If the Company elects to conduct a Remarketing of the Notes for the purpose of establishing a new Fixed Rate for a new Fixed Rate Period, the Company shall not less than 20 nor more than 35 Business Days prior to the related Election Date, notify the Clearing Agency, the Calculation Agent, the Trustee and the Remarketing Agent. If the Notes are not issued in global, fully registered form to the Clearing Agency, such notice shall be delivered to the holders of the Notes instead of the Clearing Agency. Such notice shall indicate the length of the proposed new Fixed Rate Period, the proposed Remarketing Date and any redemption provisions that apply during such new Fixed Rate Period. The Company shall have the right to terminate a Remarketing at any time prior to the Election Date by notice of such termination to the Clearing Agency, the Remarketing Agent, the Trustee and the Calculation Agent;

(viii) if the Remarketing Agent has determined that it will be able to remarket all Notes tendered or deemed tendered for purchase in the Remarketing at a Fixed Rate and at a price of \$1,000 per Note, on such Remarketing Date, the Interest Rate for the new Fixed Rate Period will be the Fixed Rate determined by the Remarketing Agent, which will be the rate per annum (rounded to the nearest one-thousandth (0.001) of one percent per annum) which the Remarketing Agent determines, in its sole judgment, to be the lowest Fixed Rate per annum that will enable it to remarket all Notes tendered or deemed tendered for Remarketing at a price of \$1,000 per Note. By approximately 4:30 P.M., New York City time, on a Remarketing Date, the Remarketing Agent shall advise, by telephone: (i) the Clearing Agency, the Institutional Trustee, the Trustee, the Trust, the Company and the Calculation Agent of any new Fixed Rate established pursuant to the Remarketing, (ii) each purchaser of Remarketed Securities (or the Clearing Agency Participant thereof) of such new Fixed Rate and the number of Remarketed Securities such purchaser is to purchase and (iii) each purchaser to give instructions to its Clearing Agency Participant to pay the purchase price on the Remarketing Settlement Date in same day funds against delivery of the Remarketed Securities purchased through the facilities of the Clearing Agency;

(ix) if the Company does not elect to remarket the Notes or has terminated a Remarketing or if the Remarketing Agent is unable to remarket all of the Notes tendered or deemed tendered for a purchase price of \$1,000 per Note, the Interest Rate for the next Interest Period shall be the Floating Rate and the new Interest Period shall be a Floating Rate Period;

(x) the Calculation Agent shall calculate the Floating Rate on the Floating Rate Determination Date as follows:

(A) Except as provided below, the Floating Rate for any Floating Rate Period for the Notes will be equal to the Adjustable Rate (as defined

below) plus 3.66%. The "Adjustable Rate" for any Interest Period will be equal to the highest of the 3-month LIBOR Rate, the 10-year Treasury CMT and the 30-year Treasury CMT (each as defined below and collectively referred to as the "Benchmark Rates") for such Interest Period during the Floating Rate Period. In the event that the Calculation Agent determines in good faith that for any reason:

(1) any one of the Benchmark Rates cannot be determined for any Interest Period, the Adjustable Rate for such Interest Period will be equal to the higher of whichever two of such rates can be so determined;

(2) only one of the Benchmark Rates can be determined for any Interest Period, the Adjustable Rate for such Interest Period will be equal to whichever such rate can be so determined; or

(3) none of the Benchmark Rates can be determined for any Interest Period, the Adjustable Rate for the preceding Interest Period will be continued for such Interest Period.

(B) The "3-month LIBOR Rate" means, for each Interest Period, the arithmetic average of the two most recent weekly quotes for deposits for U.S. Dollars having a term of three months, as published on the first Business Day of each week immediately preceding the Interest Period for which the Floating Rate is being determined. Such quotes will be taken from Telerate Page 3750 at approximately 11:00 a.m. London time on the Floating Rate Determination Date. If such rate does not appear on Telerate Page 3750 on the Floating Rate Determination Date, the 3-month LIBOR Rate will be the arithmetic mean of the rates quoted by three major banks in New York City selected by the Calculation Agent, at approximately 11:00 a.m., New York City time, on the relevant date for loans in U.S. Dollars to leading European banks for a period of three months.

(C) The "10-year Treasury CMT" means the rate determined in accordance with the following provisions:

(1) With respect to any Floating Rate Determination Date and the Interest Period that begins immediately thereafter, the 10-year Treasury CMT means the rate displayed on Telerate Page 7051 under the caption "...Treasury Constant Maturities...Federal Reserve Board Release H.15...Mondays Approximately 3:45 P.M.", under the column for the Designated CMT Maturity Index (as defined below).

(2) If such rate is no longer displayed on the relevant page, or is not so displayed by 3:00 P.M., New York City time, on the applicable Floating Rate Determination Date, then the 10-year Treasury CMT for such Floating Rate Determination Date will be

such treasury constant maturity rate for the Designated CMT Maturity Index as is published in H.15(519).

(3) If such rate is no longer displayed on the relevant page, or if not published by 3:00 P.M., New York City time, on the applicable Floating Rate Determination Date, then the 10-year Treasury CMT for such Floating Rate Determination Date will be such constant maturity treasury rate for the Designated CMT Maturity Index (or other United States Treasury rate for the Designated CMT Maturity Index) for the applicable Floating Rate Determination Date with respect to such interest reset date as may then be published by either the Board of Governors of the Federal Reserve System or the United States Department of the Treasury that the Calculation Agent determines to be comparable to the rate formerly displayed on the Telerate Page 7051 and published in H.15(519).

(4) If such information is not provided by 3:00 P.M., New York City time, on the applicable Floating Rate Determination Date, then the 10-year Treasury CMT for such Floating Rate Determination Date will be calculated by the Calculation Agent and will be a yield to maturity, based on the arithmetic mean of the secondary market offered rates as of approximately 3:30 P.M., New York City time, on the Floating Rate Determination Date reported, according to their written records, by three leading primary United States government securities dealers in The City of New York (each, a "Reference Dealer") selected by the Calculation Agent (from five such Reference Dealers selected by the Calculation Agent and eliminating the highest quotation (or, in the event of equality, one of the highest) and the lowest quotation (or, in the event of equality, one of the lowest)), for the most recently issued direct noncallable fixed rate obligations of the United States ("Treasury Debentures") with an original maturity of approximately the Designated CMT Maturity Index and a remaining term to maturity of not less than such Designated CMT Maturity Index minus one year.

(5) If the Calculation Agent is unable to obtain three such Treasury Debentures quotations, the 10-year Treasury CMT for the applicable Floating Rate Determination Date will be calculated by the Calculation Agent and will be a yield to maturity based on the arithmetic mean of the secondary market offered rates as of approximately 3:30 P.M., New York City time, on the applicable Floating Rate Determination Date of three Reference Dealers in The City of New York (from five such Reference Dealers selected by the Calculation Agent and eliminating the highest quotation (or, in the event of equality, one of the highest) and the lowest

quotation (or, in the event of equality, one of the lowest)), for Treasury Debentures with an original maturity of the number of years that is the next highest to the Designated CMT Maturity Index and a remaining term to maturity closest to the Designated CMT Maturity Index and in an amount of at least \$100 million.

(6) If three or four (and not five) of such Reference Dealers are quoting as set forth above, then the 10-year Treasury CMT will be based on the arithmetic mean of the offered rates obtained and neither the highest nor lowest of such quotes will be eliminated; provided, however, that if fewer than three Reference Dealers selected by the Calculation Agent are quoting as set forth above, the 10-year Treasury CMT with respect to the applicable interest determination date will remain the 10-year Treasury CMT for the immediately preceding Interest Period. If two Treasury Debentures with an original maturity as described in the second preceding sentence have remaining terms to maturity equally close to the Designated CMT Maturity Index, then the quotes for the Treasury Debentures with the shorter remaining term to maturity will be used.

(7) "Designated CMT Maturity Index" means the original period to maturity of the U.S. Treasury securities (10 years) with respect to which the 10-year Treasury CMT will be calculated.

(8) "Telerate Page 3750" means the display designated on page 3750 on MoneyLine Telerate (or such other page as may replace the 3750 page on the service or such other service as may be nominated by the British Bankers' Association for the purpose of displaying London interbank offered rates for U.S. Dollars deposits).

(9) "Telerate Page 7051" means the display on MoneyLine Telerate (or any successor service), on such page (or any other page as may replace such page on that service), for the purpose of displaying Treasury Constant Maturities as reported in H.15(519).

(10) "30-year Treasury CMT" has the meaning specified under the definition of 10-year Treasury CMT, except that the Designated CMT Maturity Index for the 30-year Treasury CMT shall be 30 years.

(D) The 3-month LIBOR Rate, the 10-year Treasury CMT and the 30-year Treasury CMT shall each be rounded to the nearest hundredth of a percent.

(E) The Floating Rate with respect to each Floating Rate Period will be calculated as promptly as practicable by the Calculation Agent according

to the appropriate method described above.

(xi) if the Company elects to defer interest during a Fixed Rate Period, interest will continue to accrue and be compounded semiannually at the Fixed Rate until the expiration of the Fixed Rate Period. Prior to the expiration of such Fixed Rate Period and any subsequent Fixed Rate Period during the Extension Period, the Company will have the option to remarket the Notes for a new Fixed Rate Period (to take effect upon expiration of such Fixed Rate Period). If the Company does not remarket the Notes, the Floating Rate during the Extension Period shall be determined as provided herein, but shall not be less than the Fixed Rate for the Fixed Rate Period just ended. If the Company elects to defer interest during a Floating Rate Period, interest will continue to accrue and be compounded quarterly at the applicable Floating Rate, reset quarterly, subject to the right of the Company to remarket the Notes prior to any Interest Payment Date in order to establish a new Fixed Rate for a new Fixed Rate Period in accordance with the Remarketing Procedures;

(xii) in accordance with Part II, clause (b) of this Officer's Certificate and the Remarketing Procedures, the Company may, prior to the expiration of the Initial Fixed Rate Period and any subsequent Fixed Rate Period, prior to any Interest Payment Date during a time in which the Notes are redeemable in any Fixed Rate Period or prior to any Interest Payment Date with respect to a Floating Rate Period, elect to remarket the Notes to establish a new Fixed Rate for a new Fixed Rate Period (to be in effect after the then current Interest Period). A Fixed Rate Period must be for a duration of at least six months, may not extend beyond the Maturity of the Notes and may not end on a day other than a day immediately preceding an Interest Payment Date. If a new Fixed Rate for a new Fixed Rate Period is set in a Remarketing, a new Fixed Rate Period shall commence following the expiration of the then current Interest Period. If a new Fixed Rate for a new Fixed Rate Period is not set, for any reason, including after the expiration of the Initial Fixed Rate Period, a Floating Rate Period, and the Floating Rate reset quarterly shall be in effect until the Company remarkets the Notes and sets a new Fixed Rate for a new Fixed Rate Period in accordance with the Remarketing Procedures;

(xiii) so long as no Event of Default has occurred and is continuing, the Company has the right at any time, and from time to time, to defer payments of interest on the Notes by extending the interest payment period (an "Extension Period"). During an Extension Period, interest will continue to accrue on the Notes. If the Company decides to defer interest payments on the Notes, the Extension Period shall not exceed five consecutive years. An Extension Period shall not extend beyond the Maturity of the Notes. Prior to the termination of any Extension Period, the Company may further defer payments of interest provided that the Extension Period, together with all previous and further extensions thereof, may not exceed five consecutive years. There could be multiple Extension Periods of varying lengths throughout the term of the Notes. Upon the termination of any such Extension Period and upon the payment of all accrued and unpaid interest then due, the Company may select a new Extension Period, subject to the above limitations and requirements. Upon the termination of any Extension Period, which termination shall be on an Interest Payment Date, the Company shall pay all Deferred Interest on the next succeeding Interest Payment Date to the Person in whose

name the Notes are registered on the Regular Record Date for such Interest Payment Date, provided that Deferred Interest payable at Maturity or on any Redemption Date will be paid to the Person to whom principal is payable. The Company shall give the Holder or Holders of the Notes, the Trustee, the Remarketing Agent and the Calculation Agent, notice as provided in Sections 105 and 106, respectively, of the Indenture of its selection or extension of an Extension Period at least one Business Day prior to the earlier of (i) the Regular Record Date relating to the Interest Payment Date on which the Extension Period is to commence or relating to the Interest Payment Date on which an Extension Period that is being extended would otherwise terminate, or (ii) the date the Company or the Trust is required to give notice to any applicable self-regulatory organization of the record date or the date such distributions are payable. The Company shall cause the Trust to give notice of the Company's selection of such Extension Period to Holders of the Trust Securities, the Calculation Agent and the Remarketing Agent.

(f) the corporate trust office of Union Bank of California, N.A. in Los Angeles, California shall be the place at which (i) the principal of, premium, if any, and interest, if any, on the Notes at Maturity shall be payable upon presentment and interest prior to Maturity shall be payable as specified in the form of Note attached hereto, (ii) registration of transfer of the Notes may be effected, (iii) exchanges of Notes may be effected and (iv) notices and demands to or upon the Company in respect of the Notes and the Indenture may be served; and Union Bank of California, N.A. shall be the Security Registrar and a Paying Agent for the Notes; provided, however, that the Company reserves the right to change, by one or more Officer's Certificates supplemental to this Officer's Certificate, any such place or the Security Registrar or such Paying Agent; and provided, further, that the Company reserves the right to designate, by one or more Officer's Certificates supplemental to this Officer's Certificate, its principal corporate office in Spokane, Washington as any such place or itself as the Security Registrar;

(g) (i) the Notes shall be subject to redemption, in whole but not in part, at the election of the Company on the last Interest Payment Date relating to the Initial Fixed Rate Period, on such dates with respect to any other Fixed Rate Period as the Company and the Trust may determine prior to the remarketing establishing such Fixed Rate Period or on any Interest Payment Date relating to a Floating Rate Period, at a Redemption Price equal to 100% of the principal amount to be redeemed plus accrued but unpaid interest to the Redemption Date;

(ii) the Notes shall be subject to redemption, in whole but not in part, at the election of the Company, on any date within 90 days of the occurrence, and during the continuation of, a Special Event (as defined herein) at a redemption price equal to 100% of the principal amount thereof plus accrued interest, if any to the date fixed for redemption;

"Special Event" means an "Investment Company Act Event" or "Tax Event";

"Investment Company Act Event" means the receipt by the Company and the Regular Trustees of an Opinion of Counsel to the Company experienced in these matters to the effect that, as a result of the occurrence of a change in law or regulation or

a written change (including any announced prospective change) in interpretation or application of law or regulation by any legislative body, court, governmental agency or regulatory authority, there is more than an insubstantial risk that the Trust is or will be considered an "investment company" that is required to be registered under the Investment Company Act of 1940, as amended, which change or prospective change becomes effective or would become effective, as the case may be, after the date of the issuance by the Trust of the Preferred Securities.

"Tax Event" means the receipt by the Company and the Regular Trustees of an opinion from independent tax counsel experienced in such matters (which may be counsel to the Company) to the effect that, as a result of (a) any amendment to, or change (including any announced proposed change) in, the laws (or any regulations thereunder) of the United States or any political subdivision or taxing authority thereof or therein or (b) any amendment to, or change in, an interpretation or application of such laws or regulations, there is more than an insubstantial risk that (i) the Trust would be subject to United States federal income tax with respect to income accrued or received on the Notes; (ii) interest payable on the Notes would not be deductible, in whole or in part, by the Company for United States federal income tax purposes; or (iii) the Trust would be subject to more than a de minimis amount of other taxes, duties or other governmental charges, which change or amendment becomes effective on or after the date of issuance by the Trust of the Preferred Securities.

(h) inapplicable;

(i) the Notes shall be issued in denominations of \$1,000 and any integral multiple thereof;

(j) inapplicable;

(k) inapplicable;

(l) inapplicable;

(m) inapplicable;

(n) inapplicable;

(o) inapplicable;

(p) inapplicable;

(q) inapplicable;

(r) inapplicable;

(s) (i) the Notes are to be initially registered in the name of Union Bank of California, N.A., as Institutional Trustee of the Trust. The Notes shall not be transferable, nor shall any purported transfer be registered, except (A) to a nominee of such Institutional Trustee,



to such Institutional Trustee by such nominee, by such Institutional Trustee to another nominee, by any such nominee to a successor nominee or by such Institutional Trustee or any nominee thereof to a successor Institutional Trustee or a nominee thereof or (B) to the holders of Trust Securities in the event of the dissolution of the Trust in accordance with the provisions of the Declaration;

(ii) no service charge shall be made for the registration of transfer or exchange of the Notes; provided, however, that, after the distribution of the Notes contemplated in clause (i)(B) above, the Company may require payment of a sum sufficient to cover any tax or other governmental charge payable in connection with the exchange and transfer;

(t) reference is made to clause (e)(ii) above; and

(u) the notes are to be issued and sold to the Trust.

## PART II

Set forth below in this Part II are additional terms of the series of Notes established hereby, as contemplated by clause (v) in the second paragraph of Section 301 of the Indenture.

(a) the Notes shall have such further terms as are set forth in the form of Note attached hereto; provided, however, that if the Trust is dissolved and the Notes are distributed to the holders of the Preferred Securities, the form of Note may, at the election of the Company, be revised to specifically include the provisions of the determination of the interest rate thereon, as set forth in this Officer's Certificate;

(b) Article 10 of the Declaration sets forth the Remarketing Procedures to determine the applicable Fixed Rate from time to time for the Preferred Securities. If the Trust is dissolved and the Notes are distributed to the holders of the Preferred Securities, the below described Remarketing Procedures will be applicable to the Notes;

(i) if the Company elects to conduct a Remarketing, the Company, not less than 20 nor more than 35 Business Days prior to the related Election Date, is required to give the written notice of proposed Remarketing of the Notes to the Clearing Agency, the Trustee, the Calculation Agent and the Remarketing Agent. If the Notes are not issued in global, fully registered form, such notice shall be delivered to the holders of the Notes instead of the Clearing Agency. Such notice will describe the Remarketing and will indicate the length of the proposed new Fixed Rate Period, the proposed Remarketing Date and any redemption provisions that apply during such new Fixed Rate Period. At any time prior to the Election Date, the Company may elect to terminate a Remarketing by giving the Clearing Agency (or the Holders as applicable), the Remarketing Agent, the Trustee and the Calculation Agent written notice of such termination;

(ii) not later than 4:00 p.m., New York City time, on an Election Date, each Holder of Notes may give a written notice to the Trustee of its election ("Notice of Election") (i) to retain and not to have all or any portion of the Notes owned by it remarketed in the Remarketing, or (ii) to tender all or any portion of such Notes for purchase in the Remarketing (such portion, in either case, is required to be in the Liquidation Amount of \$1,000 or any integral multiple thereof). Any Notice of Election given to the Trustee will be irrevocable and may not be conditioned upon the level at which the Fixed Rate is established in the Remarketing. Promptly after 4:30 p.m., New York City time, on such Election Date, the Trustee, based on the Notices of Election received by it through the Clearing Agency prior to such time, will notify the Company and the Remarketing Agent of the number of Notes to be retained by holders of Notes and the number of Notes tendered for purchase in the Remarketing;

(iii) if any holder of Notes gives a Notice of Election to tender Notes as described above, the Notes so subject to such Notice of Election will be deemed tendered for purchase in the Remarketing, notwithstanding any failure by such holder to deliver or properly deliver such Notes to the Remarketing Agent for purchase. If any holder of Notes fails timely to deliver a Notice of Election, as described above, such Notes will be deemed tendered for purchase in such Remarketing, notwithstanding such failure or the failure by such holder to deliver or properly deliver such Notes to the Remarketing Agent for purchase;

(iv) the right of each holder of Notes to have Notes tendered for purchase in the Remarketing shall be limited to the extent that (i) the Remarketing Agent conducts a Remarketing pursuant to the terms of the Remarketing Agreement; (ii) the Notes tendered have not been called for redemption; (iii) the Remarketing Agent is able to find a purchaser or purchasers for tendered Notes at a Fixed Rate; and (iv) such purchaser or purchasers deliver the purchase price therefor to the Remarketing Agent;

(v) any holder of Notes that desires to continue to retain a number of Notes, but only if the Fixed Rate is not less than a specified rate per annum, shall submit a Notice of Election pursuant to this clause (b) to tender such Notes and separately notify the Remarketing Agent of its interest at the telephone number set forth in the notice of Remarketing. If such holder so notifies the Remarketing Agent, the Remarketing Agent will give priority to such holder's purchase of such number of Notes in the Remarketing, providing that the Fixed Rate is not less than such specified rate;

(vi) if holders submit Notices of Election to retain all of the Notes then outstanding, the Fixed Rate will be the rate determined by the Remarketing Agent, in its sole discretion, as the rate that would have been established had a Remarketing been held on the related Remarketing Date;

(vii) on any Remarketing Date on which the Remarketing is to be conducted, the Remarketing Agent will use commercially reasonable efforts to remarket, at a price equal to 100% of the principal amount thereof, Notes tendered or deemed tendered for purchase. Except as provided in the previous paragraph of this clause (b), if, as a result of such efforts, on any Remarketing Date, the Remarketing Agent has

determined that it will be able to remarket all Notes tendered or deemed tendered for purchase in the Remarketing at a Fixed Rate and at a price of \$1,000 per Note, prior to 4:00 p.m., New York City time, on such Remarketing Date, the Remarketing Agent will determine the Fixed Rate, which will be the rate per annum (rounded to the nearest one-thousandth (0.001) of one percent per annum) which the Remarketing Agent determines, in its sole judgment, to be the lowest Fixed Rate per annum that will enable it to remarket all Notes tendered or deemed tendered for Remarketing at a price of \$1,000 per Note. By approximately 4:30 P.M., New York City time, on a Remarketing Date, the Remarketing Agent shall advise, by telephone: (i) the Clearing Agency, the Institutional Trustee, the Trustee, the Trust, the Company and the Calculation Agent of any new Fixed Rate established pursuant to the Remarketing, (ii) each purchaser of Remarketed Securities (or the Clearing Agency Participant thereof) of such new Fixed Rate and the number of Remarketed Securities such purchaser is to purchase and (iii) each purchaser to give instructions to its Clearing Agency Participant to pay the purchase price on the Remarketing Settlement Date in same day funds against delivery of the Remarketed Securities purchased through the facilities of the Clearing Agency;

(viii) if the Remarketing Agent is unable to remarket by 4:00 p.m., New York City time on the third Business Day prior to the Remarketing Settlement Date, all Notes tendered or deemed tendered for a purchase at a price of \$1,000 per Note, the Interest Rate for the next Interest Period shall be the Floating Rate and the new Interest Period shall be a Floating Rate Period. In such case, no Notes will be sold in the Remarketing and each holder will continue to hold its Notes at the Floating Rate during such Floating Rate Period;

(ix) all Notes tendered or deemed tendered in the Remarketing will be automatically delivered to the account of the Remarketing Agent through the facilities of the Clearing Agency against payment of the purchase price therefor on the Remarketing Settlement Date. The Remarketing Agent will make payment to the Clearing Agency Participant of each tendering holder of Notes in the Remarketing through the facilities of the Clearing Agency by the close of business on the Remarketing Settlement Date;

(x) in accordance with the Clearing Agency's normal procedures, on the Remarketing Settlement Date, the transaction described above with respect to each Note tendered for purchase and sold in the Remarketing, will be executed through the Clearing Agency Participants, will be debited and credited and such Notes delivered by book entry as necessary to effect purchases and sales of such Notes. The Clearing Agency is expected to make payment in accordance with its normal procedures;

(xi) if any holder selling Notes in the Remarketing fails to deliver such Notes, the Clearing Agency Participant of such selling holder and of any other person that was to have purchased Notes in the Remarketing may deliver to any such other person a number of Notes that is less than the number of Notes that otherwise was to be purchased by such person. In such event, the number of Notes to be so delivered will be determined by such Clearing Agency Participant and delivery of such lesser number of Notes will constitute good delivery;

(xii) the Remarketing Agent is not obligated to purchase any Notes that would otherwise remain unsold in a Remarketing. Neither the Trustee, the Company nor the Remarketing Agent shall be obligated in any case to provide funds to make payment upon tender of Notes for Remarketing;

(xiii) prior to the issuance of the Notes, the Company and the Trust will enter into the Remarketing Agreement with the Remarketing Agent, providing, among other things, that the Remarketing Agent will follow the Remarketing Procedures for the purposes of determining the applicable Fixed Rate. The Company will pay the Remarketing Agent compensation for its services under the Remarketing Agreement;

(c) if the Company shall make any deposit of money and/or Government Obligations with respect to any Notes, or any portion of the principal amount thereof, as contemplated by Section 601 of the Indenture, the Company shall not deliver an Officer's Certificate described in clause (z) in the first paragraph of said Section 601 unless the Company shall also deliver to the Trustee, together with such Officer's Certificate, either:

(i) an instrument wherein the Company, notwithstanding the satisfaction and discharge of its indebtedness in respect of the Notes, shall assume the obligation (which shall be absolute and unconditional) to irrevocably deposit with the Trustee or Paying Agent such additional sums of money, if any, or additional Government Obligations (meeting the requirements of Section 601), if any, or any combination thereof, at such time or times, as shall be necessary, together with the money and/or Government Obligations theretofore so deposited, to pay when due the principal of and premium, if any, and interest due and to become due on such Notes or portions thereof, all in accordance with and subject to the provisions of said Section 601; provided, however, that such instrument may state that the obligation of the Company to make additional deposits as aforesaid shall be subject to the delivery to the Company by the Trustee of a notice asserting the deficiency accompanied by an opinion of an independent public accountant of nationally recognized standing showing the calculation thereof (which opinion shall be obtained at the expense of the Company); or

(ii) an Opinion of Counsel to the effect that the Holders of such Notes, or portions of the principal amount thereof, will not recognize income, gain or loss for United States federal income tax purposes as a result of the satisfaction and discharge of the Company's indebtedness in respect thereof and will be subject to United States federal income tax on the same amounts, at the same times and in the same manner as if such satisfaction and discharge had not been effected;

(d) if the Company engages in a conveyance or transfer of property as contemplated in Section 1005 of the Indenture, the Company will not be released and discharged from all obligations under the Indenture and the Notes unless the Company shall deliver to the Trustee an Opinion of Counsel to the effect that the Holders of such Notes, or portions of the principal amount thereof, will not recognize income, gain or loss for United States federal income tax purposes as a result of conveyance or transfer and will be subject to United States federal income tax on the same amounts, at the same times and in the same manner as if such conveyance or transfer had not been effected;

(e) for so long as the Notes are outstanding, the Company shall not consolidate with or merge into any other Person, or convey or otherwise transfer, or lease, all of its properties, as or substantially as an entirety, as contemplated by Section 1001 of the Indenture, to any Person if such person is organized and existing under the laws of Canada or any Province thereof.

(f) if at any time the Notes are to be held by a securities depository, the Company may at such time establish the matters contemplated in clause (q) in the second paragraph of Section 301 of the Indenture in an Officer's Certificate supplemental to this Officer's Certificate; and

(g) For all purposes of this Officer's Certificate, except as otherwise expressly provided or unless the context otherwise requires:

"Calculation Agent" means Union Bank of California, N.A., or its successor appointed by the Company, acting as calculation agent.

"Clearing Agency" means an organization registered as a "clearing agency" pursuant to Section 17A of the Securities Exchange Act of 1934, as amended.

"Clearing Agency Participant" means a broker, dealer, bank, other financial institution or other Person for whom from time to time a Clearing Agency effects book-entry transfers and pledges of securities deposited with the Clearing Agency.

"Declaration" means the AVA Capital Trust III Amended and Restated Declaration of Trust dated as of April 5, 2004 among the Company, the trustees named therein, and the holders of undivided beneficial interests in the assets of the Trust.

"Declaration Event of Default" means an "Event of Default" under the Declaration.

"Deferred Interest" means each installment of interest not paid during any Extension Period, and interest thereon. Deferred installments of interest shall bear interest at the rate of the prevailing Interest Rate per annum from the applicable Interest Payment Date to the date of payment, compounded on each Interest Payment Date.

"Definitive Preferred Securities Certificates" means Preferred Securities Certificates issued in certificated, fully registered form as provided in the Declaration.

"Distribution Payment Date" means each day on which Distributions are payable on the Trust Securities determined based on the prevailing Distribution Rate.

"Distribution Period" means each semiannual period in a Fixed Rate Period and each quarterly period in a Floating Rate Period for which Distributions are payable on the Trust Securities.

"Distribution Rate" means the rate at which Distributions will accrue on the Trust Securities.

"Distributions" means amounts payable in respect of the Trust Securities pursuant to Section 4.01 of the Declaration.

"Election Date" means a date that is no later than the fifth Business Day prior to the proposed Remarketing Date.

"Extension Period" means any period during which the Company has elected to defer payments of interest on the Notes, which deferral may be for a period of up to five years.

"Fixed Rate" means the Distribution Rate (or Interest Rate with respect to the Notes) during a Fixed Rate Period.

"Fixed Rate Period" means the Initial Fixed Rate Period and each period set by the Company and, if applicable, the Regular Trustees during a Remarketing for which the Fixed Rate determined in such Remarketing will apply; provided, however, that a Fixed Rate Period must be for a duration of at least six months, may not extend beyond the Maturity of the Notes and may not end on a day other than a day immediately preceding a Distribution Payment Date (or Interest Payment Date with respect to the Notes).

"Floating Rate" has the meaning set forth in Part I, clause (e).

"Floating Rate Determination Date" means the second London Business Day immediately preceding the first day of the relevant Distribution Period (or Interest Period with respect to the Notes) in the Floating Rate Period.

"Floating Rate Period" means any period during which a Floating Rate is in effect.

"Initial Distribution Rate" means 6.50% per annum.

"Initial Fixed Rate Period" means the period from the date of original issuance through March 31, 2009.

"Initial Interest Rate" means 6.50% per annum.

"Institutional Trustee" means the commercial bank or trust company identified as the "Institutional Trustee" in the Declaration solely in its capacity as Institutional Trustee of the Trust.

"Interest Payment Dates" means the dates on which interest on the Notes is payable.

"Interest Period" means the period for which interest on the Notes is payable.

"Interest Rate" means the rate, in effect from time to time, at which interest shall accrue on the Notes.

"Liquidation Amount" means the stated amount of \$1,000 per Trust Security or the principal amount of the Notes.

"Liquidation Distribution" has the meaning specified in Section 9.05 of the Declaration.

"London Business Day" means a day that is a Business Day and a day on which dealings in deposits in U.S. dollars are transacted, or with respect to any future date are expected to be transacted, in the London interbank market.

"Preferred Security" means an undivided beneficial ownership interest in the assets of the Trust having a Liquidation Amount of \$1,000 and having rights provided therefor in the Declaration, including the right to receive Distributions and a Liquidation Distribution as provided in the Declaration.

"Preferred Securities Certificate" means a certificate evidencing ownership of a Preferred Security or Securities, substantially in the form attached as Exhibit A to the Declaration.

"Regular Trustee" means each of the individuals identified as a "Regular Trustee" in the Declaration.

"Remarketing" means the conduct by which a Fixed Rate shall be determined in accordance with the Remarketing Procedures.

"Remarketing Agent" means Lehman Brothers Inc., its successors or assigns, or such other remarketing agent appointed to such capacity by the Company and, if applicable, the Administrative Trustees.

"Remarketing Agreement" means the agreement among the Company, the Trust and Lehman Brothers Inc., as remarketing agent, dated as of April 5, 2004.

"Remarketing Date" means any Business Day no later than the third Business Day prior to any Remarketing Settlement Date.

"Remarketing Procedures" means those procedures set forth in Article 10 of the Declaration and Part II, clause (b) of this Officer's Certificate.

"Remarketing Settlement Date" means, to the extent applicable, (i) the first Business Day of the next Distribution Period (or Interest Period with respect to the Notes) following the expiration of the Initial Fixed Rate Period and any subsequent Fixed Rate Period, (ii) any Distribution Payment Date (or Interest Payment Date with respect to the Notes) during a Floating Rate Period or (iii) any Distribution Payment Date (or Interest Payment Date with respect to the Notes) during a time in which Preferred

Securities or Notes are redeemable in a Fixed Rate Period subsequent to the Initial Fixed Rate Period.

"Trust" means AVA Capital Trust III, a statutory trust formed by the Company under Delaware law to issue Trust Securities, the proceeds of which will be used to purchase the Notes.

"Trust Indenture Act" means the Trust Indenture Act of 1939 as in force at the date as of which this instrument was executed; provided, however, that in the event the Trust Indenture Act of 1939 is amended after such date, "Trust Indenture Act" means, to the extent required by any such amendment, the Trust Indenture Act of 1939 as so amended.

"Trust Security" means any one of the Common Securities (as defined in the Declaration) or the Preferred Securities.



IN WITNESS WHEREOF, I have executed this Officer's Certificate  
this 5th day of April, 2004.

/s/ Diane C. Thoren

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Name: Diane C. Thoren  
Title: Assistant Treasurer

(See legend at the end of this Security for restrictions on transfer and change of form)

AVISTA CORPORATION  
Subordinated Debt Securities, Series due 2034

ORIGINAL INTEREST ACCRUAL DATE: APRIL 5, 2004 REDEEMABLE: YES [X] NO [ ]  
STATED MATURITY: APRIL 1, 2034 INITIAL REDEMPTION DATE:  
INTEREST RATE: DETERMINED BY PROCEDURES MARCH 31, 2009  
SET FORTH IN THE INDENTURE INITIAL REDEMPTION PRICE: 100%  
INTEREST PAYMENT DATES: AS DESCRIBED BELOW  
REGULAR RECORD DATES: THE OPENING OF BUSINESS  
ON THE BUSINESS DAY IMMEDIATELY PRECEDING  
THE RELEVANT INTEREST PAYMENT DATE

OID: YES [ ] NO [ ]  
TOTAL AMOUNT OF OID (%):  
YIELD TO MATURITY (%):  
INITIAL ACCRUAL  
PERIOD OID (%):  
(CONSTANT - YIELD METHOD)

This Security is not a Discount Security within the meaning of the within-mentioned Indenture.

Principal Amount Registered No.  
\$ CUSIP

AVISTA CORPORATION, a corporation organized and existing under the laws of the State of Washington (herein called the "Company", which term includes any successor corporation under the Indenture referred to below), for value received, hereby promises to pay to

or registered assigns, the principal sum of

DOLLARS

on the Stated Maturity specified above (or upon earlier redemption), and to pay interest thereon from the Original Interest Accrual Date specified above or from the most recent Interest Payment Date to which interest has been paid or duly provided for, on each Interest Payment Date, commencing with the Interest Payment Date next succeeding the Original Interest Accrual Date specified above, and at Maturity (or upon earlier redemption), at the Interest Rate then in effect, until the principal hereof and any overdue interest is paid or duly provided for. The interest so payable, and paid or duly provided for, on any Interest Payment Date shall, as provided in such Indenture, be paid to the Person in whose name this Security (or one or more Predecessor Securities) is registered at the close of business on the Regular Record Date specified above next preceding such Interest Payment Date. Notwithstanding the foregoing,

(a) if the Original Interest Accrual Date of this Security is after a Regular Record Date and before the corresponding Interest Payment Date, interest so payable for the period from and including the Original Interest Accrual Date to but excluding such Interest Payment Date shall be paid on the next succeeding Interest Payment Date to the Holder hereof on the related Regular Record Date; and (b) interest payable at Maturity shall be paid to the Person to whom principal shall be paid. Except as otherwise provided in said Indenture, any such interest not so paid or duly provided for shall forthwith cease to be payable to the Holder on such Regular Record Date and may either be paid to the Person in whose name this Security (or one or more Predecessor Securities) is registered at the close of business on a Special Record Date for the payment of such Unpaid Interest to be fixed by the Trustee, notice of which shall be given to Holders of Securities of this series not less than 15 days prior to such Special Record Date, or be paid at any time in any other lawful manner not inconsistent with the requirements of any securities exchange on which the Securities of this series may be listed, and upon such notice as may be required by such exchange, all as more fully provided in said Indenture.

So long as no Event of Default shall have occurred and be continuing, the Company has the right to defer payments of interest on this Security by extending the interest payment period from time to time on this Security (an "Extension Period"). If the Company decides to defer interest payments on this Security, the Extension Period shall not exceed five consecutive years. An Extension Period shall not extend beyond the Stated Maturity of this Security. Prior to the termination of any Extension Period, the Company may further defer payments of interest provided that the Extension Period, together with all such previous and further extensions thereof, may not exceed five consecutive years. Upon termination of any Extension Period and the payments of all amounts then due, the Company may select a new Extension Period, subject to the above requirements. There could be multiple Extension Periods of varying lengths throughout the term of this Security. During an Extension Period, Unpaid Interest (together with interest thereon) will compound on each Interest Payment Date at the prevailing Interest Rate ("Deferred Interest"). Upon the termination of each Extension Period, which shall be an Interest Payment Date, the Company shall pay all Deferred Interest on the next succeeding Interest Payment Date to the Person in whose name this Security is registered at the close of business on the Regular Record Date for such Interest Payment Date, provided that any Deferred Interest payable at Stated Maturity or on any Redemption Date will be paid to the Person to whom principal is payable.

The Company shall give the Holder of this Security, the Trustee, the Remarketing Agent and the Calculation Agent notice of its selection or extension of an Extension Period at least one Business Day prior to the earlier of (i) the Regular Record Date relating to the Interest Payment Date on which the Extension Period is to commence or relating to the Interest Payment Date on which an Extension Period that is being extended would otherwise terminate or (ii) the date the Company or Trust is required to give notice to any applicable self-regulatory organization of the record date or the date distributions are payable.

Payment of the principal of and premium, if any, on this Security and interest hereon at Maturity shall be made upon presentation of this Security at the Corporate Trust Office of Union Bank of California, N.A. in Los Angeles, California, or at such other office or agency as may be designated for such purpose by the Company from time to time. Payment of interest

on this Security (other than interest at Maturity) shall be made by check mailed to the address of the Person entitled thereto as such address shall appear in the Security Register, except that if such Person shall be a Trust or securities depository, such payment may be made by such other means in lieu of check, as shall be agreed upon by the Company, the Trustee and such Person. Payment of the principal of and premium, if any, and interest on this Security, as aforesaid, shall be made in such coin or currency of the United States of America as at the time of payment shall be legal tender for the payment of public and private debts.

This Security is one of a duly authorized issue of securities of the Company (herein called the "Securities"), issued and issuable in one or more series under and equally secured by an Indenture, dated as of April 1, 2004 (such Indenture as originally executed and delivered and as supplemented or amended from time to time thereafter, together with any constituent instruments establishing the terms of particular Securities, being herein called the "Indenture"), between the Company and Union Bank of California, N.A., trustee (herein called the "Trustee," which term includes any successor trustee under the Indenture), to which Indenture and all indentures supplemental thereto reference is hereby made for a description of the respective rights, limitations of rights, duties and immunities of the Company, the Trustee and the Holders of the Securities thereunder and of the terms and conditions upon which the Securities are, and are to be, authenticated and delivered and secured. The acceptance of this Security shall be deemed to constitute the consent and agreement by the Holder hereof to all terms and provisions of the Indenture. This Security is one of the series designated above.

The Securities of this series are subject to redemption, in whole but not in part, at the election of the Company on the last Interest Payment Date relating to the Initial Fixed Rate Period, on such dates with respect to any other Fixed Rate Period as the Company and the Trust may determine prior to the remarketing establishing such Fixed Rate Period or on any Interest Payment Date relating to a Floating Rate Period, at a Redemption Price equal to 100% of the principal amount to be redeemed plus accrued but unpaid interest to the Redemption Date

The Securities of this series are subject to redemption, in whole but not in part, at the election of the Company, on any date within 90 days of the occurrence, and during the continuation of, a Special Event (as defined herein) at a redemption price equal to 100% of the principal amount thereof plus accrued interest, if any to the date fixed for redemption.

"Special Event" means an "Investment Company Act Event" or "Tax Event".

"Investment Company Act Event" means the receipt by the Company and the Regular Trustees of an Opinion of Counsel to the Company experienced in these matters to the effect that, as a result of the occurrence of a change in law or regulation or a written change (including any announced prospective change) in interpretation or application of law or regulation by any legislative body, court, governmental agency or regulatory authority, there is more than an insubstantial risk that the Trust is or will be considered an "investment company" that is required to be registered under the 1940 Act, which change or prospective change becomes effective or would become effective, as the case may be, after the date of the issuance by the Trust of the Preferred Securities.

"Tax Event" means receipt by the Company and the Regular Trustees of an

opinion from independent tax counsel experienced in such matters (which may be counsel to the Company) to the effect that, as a result of (a) any amendment to, or change (including any announced proposed change) in, the laws (or any regulations thereunder) of the United States or any political subdivision or taxing authority thereof or therein or (b) any amendment to, or change in, an interpretation or application of such laws or regulations, there is more than an insubstantial risk that (i) the Trust would be subject to United States federal income tax with respect to income accrued or received on the Securities; (ii) interest payable on the Securities would not be deductible, in whole or in part, by the Company for United States federal income tax purposes; or (iii) the Trust would be subject to more than a de minimis amount of other taxes, duties or other governmental charges, which change or amendment becomes effective on or after the date of issuance by the Trust of the Preferred Securities.

Notice of redemption shall be given by mail to Holders of Securities, not less than 30 days nor more than 60 days prior the date fixed for redemption, all as provided in the Indenture. As provided in the Indenture, notice of redemption at the election of the Company as aforesaid may state that such redemption shall be conditional upon the receipt by the Trustee of money sufficient to pay the principal of and premium, if any and interest, if any, on this Security on or prior the date fixed for such redemption; a notice of redemption so conditioned shall be of no force or effect if such money is not so received and, in such event, the Company shall not be required to redeem this Security.

The Company also shall be obligated to pay when due and without extension all additional amounts as may be required so that the net amount received and retained by the Holder of this Security (if the Holder is a Trust) after paying taxes, duties, assessments or governmental charges of any nature (other than withholding taxes) imposed by the United States or any other taxing authority will not be less than the amounts such Holder would have received had no such taxes, duties, assessments or other governmental charges been imposed.

If an Event of Default shall occur and be continuing, the principal of this Security may be declared due and payable in the manner and with the effect provided in the Indenture.

The indebtedness evidenced by this Security is, to the extent provided in the Indenture, subordinated and subject in right of payment to the prior payment in full of all Senior Indebtedness, and this Security is issued subject to the provisions of the Indenture with respect thereto. Each Holder of this Security, by accepting the same, (a) agrees to and shall be bound by such provisions, (b) authorizes and directs the Trustee on his behalf to take such action as may be necessary or appropriate to acknowledge or effectuate the subordination so provided and (c) appoints the Trustee his attorney-in-fact for any and all such purposes. Each Holder hereof, by his acceptance hereof, hereby waives all notice of the acceptance of the subordination provisions contained herein and in the Indenture by each holder of Senior Indebtedness, whether now outstanding or hereafter incurred, and waives reliance by each such Holder upon said provisions.

Each Holder hereof, by his acceptance hereof, agrees to treat this Security as indebtedness for all United States tax purposes.

The Indenture permits, with certain exceptions as therein provided, the Trustee to enter into one or more supplemental indentures for the purpose of adding any provisions to, or

changing in any manner or eliminating any of the provisions of, the Indenture with the consent of the Holders of not less than a majority in aggregate principal amount of the Securities of all series then Outstanding under the Indenture, considered as one class; provided, however, that if there shall be Securities of more than one series Outstanding under the Indenture and if a proposed supplemental indenture shall directly affect the rights of the Holders of Securities of one or more, but less than all, of such series, then the consent only of the Holders of a majority in aggregate principal amount of the Outstanding Securities of all series so directly affected, considered as one class, shall be required; and provided, further, that if the Securities of any series shall have been issued in more than one Tranche and if the proposed supplemental indenture shall directly affect the rights of the Holders of Securities of one or more, but less than all, of such Tranches, then the consent only of the Holders of a majority in aggregate principal amount of the Outstanding Securities of all Tranches so directly affected, considered as one class, shall be required; and provided, further, that the Indenture permits the Trustee to enter into one or more supplemental indentures for limited purposes without the consent of any Holders of Securities. The Indenture also contains provisions permitting the Holders of a majority in principal amount of the Securities then Outstanding, on behalf of the Holders of all Securities, to waive compliance by the Company with certain provisions of the Indenture and certain past defaults under the Indenture and their consequences. Any such consent or waiver by the Holder of this Security shall be conclusive and binding upon such Holder and upon all future Holders of this Security and of any Security issued upon the registration of transfer hereof or in exchange thereof or in lieu hereof, whether or not notation of such consent or waiver is made upon this Security.

As provided in the Indenture and subject to certain limitations therein set forth, this Security or any portion of the principal amount hereof will be deemed to have been paid for all purposes of the Indenture and to be no longer Outstanding thereunder, and, at the election of the Company, the Company's entire indebtedness in respect thereof will be satisfied and discharged, if there has been irrevocably deposited with the Trustee or any Paying Agent (other than the Company), in trust, money in an amount which will be sufficient and/or Eligible Obligations, the principal of and interest on which when due, without regard to any reinvestment thereof, will provide moneys which, together with moneys so deposited, will be sufficient to pay when due the principal of and interest on this Security when due.

The Indenture contains terms, provisions and conditions relating to the consolidation or merger of the Company with or into, and the conveyance or other transfer, or lease, of assets to, another Person, to the assumption by such other Person, in certain circumstances, of all of the obligations of the Company under the Indenture and on the Securities and to the release and discharge of the Company, in certain circumstances, from such obligation.

As provided in the Indenture and subject to certain limitations therein set forth, the transfer of this Security is registrable in the Security Register, upon surrender of this Security for registration of transfer at the corporate trust office of Union Bank of California, N.A. in Los Angeles, California, or such other office or agency as may be designated by the Company from time to time, duly endorsed by, or accompanied by a written instrument of transfer in form satisfactory to the Company and the Security Registrar duly executed by, the Holder hereof or his attorney duly authorized in writing, and thereupon one or more new Securities of this series of authorized denominations and of like tenor and aggregate principal amount, will be issued to the designated transferee or transferees.

If any Interest Payment Date with respect to a Fixed Rate Period is not a Business Day, interest will be payable, without additional interest, on the immediately succeeding Business Day, with the same force and effect as if payment was made on the date such payment was originally payable (and without the accrual of any additional amount of interest). If any Interest Payment Date with respect to a Floating Rate Period is not a Business Day, then interest will be payable on the immediately succeeding Business Day and interest shall accrue to the actual payment date (except for an Interest Payment Date that coincides with Maturity or the Redemption Date).

The Securities of this series are issuable only as registered Securities, without coupons, and in denominations of \$1,000 or any amount in excess thereof that is an integral multiple of \$1,000. As provided in the Indenture and subject to certain limitations therein set forth, Securities of this Series are exchangeable for a like aggregate principal amount of Securities of the same series and Tranche, of any authorized denominations, as requested by the Holder surrendering the same, and of like tenor upon surrender of the Security or Securities to be exchanged at the corporate trust office of Union Bank of California, N.A. in Los Angeles, California, or such other office or agency as may be designated by the Company from time to time.

No service charge shall be made for any such registration of transfer or exchange, but the Company may require payment of a sum sufficient to cover any tax or other governmental charge payable in connection therewith.

Prior to due surrender of this Security for registration of transfer, the Company, the Trustee and any agent of the Company or the Trustee may treat the Person in whose name this Security is registered as the absolute owner hereof for all purposes (subject to Section 307 of the Indenture), whether or not this Security be overdue, and neither the Company, the Trustee nor any such agent shall be affected by notice to the contrary.

The Indenture and the Securities shall be governed by and construed in accordance with the laws of the State of New York, except to the extent that the Trust Indenture Act shall be applicable .

As used herein, "Business Day" means any day, other than an Saturday or Sunday, which is not a day on which banking institutions or trust companies in the City of New York, New York or other city in which is located any office or agency maintained for the payment of principal, premium, if any, or interest on this Security, are authorized or required by law, regulation or executive order to remain closed. All other terms used in this Security which are defined in the Indenture shall have the meanings assigned to them in the Indenture, any supplemental indenture, Officer's Certificate or Board Resolution hereto.

As provided in the Indenture, no recourse shall be had for the payment of the principal of or premium, if any, or interest on any Securities, or any part thereof, or for any claim based thereon or otherwise in respect thereof, or of the indebtedness represented thereby, or upon any obligation, covenant or agreement under the Indenture, against, and no personal liability whatsoever shall attach to, or be incurred by, any incorporator, shareholder, officer or director, as such, past, present or future of the Company or of any predecessor or successor corporation

(either directly or through the Company or a predecessor or successor corporation), whether by virtue of any constitutional provision, statute or rule of law, or by the enforcement of any assessment or penalty or otherwise; it being expressly agreed and understood that the Indenture and all the Securities are solely corporate obligations and that any such personal liability is hereby expressly waived and released as a condition of, and as part of the consideration for, the execution of the Indenture and the issuance of the Securities.

Unless the certificate of authentication hereon has been executed by the Trustee or an Authenticating Agent by manual signature, this Security shall not be entitled to any benefit under the Indenture or be valid or obligatory for any purpose.



IN WITNESS WHEREOF, the Company has caused this instrument to be duly executed.

AVISTA CORPORATION

By: \_\_\_\_\_  
[Title]

CERTIFICATE OF AUTHENTICATION

This is one of the Securities of the series designated therein referred to in the within-mentioned Indenture.

Dated: \_\_\_\_\_

\_\_\_\_\_ OR \_\_\_\_\_  
\_\_\_\_\_

as Trustee  
By: \_\_\_\_\_  
Authorized Officer

as Trustee  
By: [ \_\_\_\_\_ ],

AS AUTHENTICATING AGENT

By: \_\_\_\_\_  
Authorized Officer

THIS SECURITY SHALL NOT BE TRANSFERABLE, NOR SHALL ANY PURPORTED TRANSFER BE REGISTERED, EXCEPT (a) TO A NOMINEE OF UNION BANK OF CALIFORNIA, N.A., AS INSTITUTIONAL TRUSTEE, TO SUCH INSTITUTIONAL TRUSTEE BY SUCH NOMINEE, BY SUCH INSTITUTIONAL TRUSTEE TO ANOTHER NOMINEE, BY ANY SUCH NOMINEE TO A SUCCESSOR NOMINEE OR BY SUCH INSTITUTIONAL TRUSTEE OR ANY NOMINEE THEREOF TO A SUCCESSOR INSTITUTIONAL TRUSTEE OR A NOMINEE THEREOF OR (b) TO THE HOLDERS OF TRUST SECURITIES IN THE EVENT OF THE DISSOLUTION OF THE TRUST IN ACCORDANCE WITH THE PROVISIONS OF THE DECLARATION.

FOR VALUE RECEIVED the undersigned hereby sells, assigns and transfers unto

\_\_\_\_\_ [please insert social security or other identifying number of assignee]

\_\_\_\_\_ [please print or typewrite name and address of assignee]

\_\_\_\_\_ the within Security of AVISTA CORPORATION and does hereby irrevocably constitute and appoint \_\_\_\_\_, Attorney, to transfer said Security on the books of the within-mentioned Company, with full power of substitution in the premises.

Dated: \_\_\_\_\_

Notice: The signature to this assignment must correspond with the name as written upon the face of the Security in every particular without alteration or enlargement or any change whatsoever.

AVA CAPITAL TRUST III

AMENDED AND RESTATED

DECLARATION OF TRUST

AMONG

AVISTA CORPORATION, AS SPONSOR,

UNION BANK OF CALIFORNIA, N.A., AS INSTITUTIONAL TRUSTEE,

SUNTRUST DELAWARE TRUST COMPANY, AS DELAWARE TRUSTEE,

AND

MALYN K. MALQUIST AND DIANE C. THOREN,

AS REGULAR TRUSTEES

DATED AS OF APRIL 5, 2004

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AVA CAPITAL TRUST III

Certain Sections of this Declaration of Trust relating to  
 Sections 310 through 318 of the  
 Trust Indenture Act of 1939:

Trust Indenture Act Section -----	Declaration of Trust Section -----
Section 310(a)(1) .....	8.07
(a)(2) .....	8.07
(a)(3) .....	8.09
(a)(4) .....	Not Applicable
(b) .....	8.08
Section 311(a) .....	8.13
(b) .....	8.13
Section 312(a) .....	5.07
(b) .....	5.07
(c) .....	5.07
Section 313(a) .....	8.14(a)
(a)(4) .....	8.14(b)
(b) .....	8.14(b)
(c) .....	8.14(a)
(d) .....	8.14(a), 8.14(b)
Section 314(a) .....	8.15
(b) .....	Not Applicable
(c)(1) .....	8.15, 8.16
(c)(2) .....	8.16
(c)(3) .....	8.16
(d) .....	Not Applicable
(e) .....	8.16
Section 315(a) .....	8.01
(b) .....	8.02, 8.14(b)
(c) .....	8.01(a)
(d) .....	8.01, 8.03
(e) .....	Not Applicable
Section 316(a) .....	Not Applicable
(a)(1)(A) .....	8.19
(a)(1)(B) .....	8.19
(a)(2) .....	Not Applicable
(b) .....	Not Applicable
(c) .....	Not Applicable
Section 317(a)(1) .....	Not Applicable
(a)(2) .....	Not Applicable
(b) .....	5.09
Section 318(a) .....	11.10

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 Note: This Cross Reference Table does not constitute part of the Declaration and shall not affect the interpretation of any of its terms and provisions.



AMENDED AND RESTATED DECLARATION OF TRUST

THIS AMENDED AND RESTATED DECLARATION OF TRUST ("Declaration") is made as of April 5, 2004, by and among (i) Avista Corporation, a Washington corporation (the "Sponsor" or the "Company"); (ii) Union Bank of California, N.A., a national banking association duly organized and existing under the laws of the United States of America, as trustee (the "Institutional Trustee" and, in its separate corporate capacity and not in its capacity as Trustee, the "Bank"); (iii) SunTrust Delaware Trust Company, a Delaware limited purpose trust company duly organized and existing under the laws of the State of Delaware, as Delaware trustee (the "Delaware Trustee" and, in its separate corporate capacity and not in its capacity as Delaware Trustee, the "Delaware Bank"); (iv) Malyn K. Malquist, an individual, and Diane C. Thoren, an individual, as regular trustees (each a "Regular Trustee" and together the "Regular Trustees") (the Institutional Trustee, the Delaware Trustee and the Regular Trustees referred to collectively as the "Trustees"); and (v) the several Holders, as hereinafter defined.

W I T N E S S E T H :

WHEREAS, a statutory trust has been declared and established pursuant to the Delaware Statutory Trust Act by entering into that certain Declaration of Trust, dated as of November 4, 1996 (the "1996 Declaration"), and by the execution and filing by the Trustees with the Secretary of State of the State of Delaware of the Certificate of Trust, dated November 4, 1996;

WHEREAS, pursuant to the Removal and Appointment of Trustee and Amendment of the Declaration of Trust of the Trust, entered into by the Sponsor, the Bank, the Delaware Bank and a Regular Trustee, dated as of March 9, 2004, (i) the Sponsor removed Wilmington Trust Company as a trustee of the Trust and appointed the Bank and the Delaware Bank as trustees of the Trust; (ii) the Sponsor removed Lawrence J. Pierce as a trustee of the Trust and appointed Malyn K. Malquist and Diane C. Thoren as trustees of the Trust; and (iii) the 1996 Declaration was amended by changing the name of the Trust from Washington Water Power Capital III to AVA Capital Trust III. The 1996 Declaration, as amended by the Removal and Appointment of Trustee and Amendment of the Declaration of Trust is referred to as the "Original Declaration."

WHEREAS, Malyn K. Malquist executed and filed the Amended and Restated Certificate of Trust of the Trust with the Secretary of State of the State of Delaware on March 9, 2004;

WHEREAS, the parties hereto desire to amend and restate the Original Declaration in its entirety as set forth herein to provide for, among other things, (i) the acquisition by the Trust from the Sponsor of all of the right, title and interest in the Subordinated Debt Securities; (ii) the issuance of the Common Securities by the Trust to the Sponsor; and (iii) the issuance and sale of the Preferred Securities by the Trust pursuant to the Underwriting Agreement.

NOW THEREFORE, in consideration of the agreements and obligations set forth herein and for other good and valuable consideration, the sufficiency of which is hereby acknowledged, each party, for the benefit of the other parties and for the benefit of the Securityholders, hereby amends and restates the Original Declaration in its entirety and agrees as follows:

ARTICLE I  
DEFINED TERMS

SECTION 1.01 Definitions

For all purposes of this Declaration, except as otherwise expressly provided or unless the context otherwise requires:

(a) the terms defined in this Article have the meanings assigned to them in this Article and include the plural as well as the singular;

(b) all other terms used herein that are defined in the Trust Indenture Act, either directly or by reference therein, have the meanings assigned to them therein;

(c) unless the context otherwise requires, any reference to an "Article" or a "Section" refers to an Article or a Section, as the case may be, of this Declaration; and

(d) the words "herein," "hereof" and "hereunder" and other words of similar import refer to this Declaration as a whole and not to any particular Article, Section or other subdivision.

"Act" has the meaning specified in Section 6.08.

"Affiliate" of any specified Person means any other Person directly or indirectly controlling or controlled by or under direct or indirect common control with such specified Person. For the purposes of this definition, "control" when used with respect to any specified Person means the power to direct the management and policies of such Person, directly or indirectly, whether through the ownership of voting securities, by contract or otherwise; and the terms "controlling" and "controlled" have meanings correlative to the foregoing.

"Bank" has the meaning specified in the preamble to this Declaration.

"Bankruptcy Event" means, with respect to any Person:

(i) the entry of a decree or order by a court having jurisdiction in the premises judging such Person a bankrupt or insolvent, or approving as properly filed a petition seeking reorganization, arrangement, adjudication or composition of or in respect of such Person under federal bankruptcy law or any other applicable federal or state law, or appointing a receiver, liquidator, assignee, trustee, sequestrator or other similar official of such Person or of any substantial part of its property, or ordering the winding up or liquidation of its affairs, and the continuance of such decree or order unstayed and in effect for a period of 60 consecutive days; or

(ii) the institution by such Person of proceedings to be adjudicated a bankrupt or insolvent, or the consent by it to the institution of bankruptcy or insolvency proceedings against it, or the filing by it of a petition or answer or

consent seeking reorganization or relief under federal bankruptcy law or any other applicable federal or state law, or the consent by it to the filing of such petition or to the appointment of a receiver, liquidator, assignee, trustee, sequestrator or similar official of such Person or of any substantial part of its property, or the making by it of an assignment for the benefit of creditors, or the admission by it in writing of its inability to pay its debts generally as they become due, or the taking of action by such Person in furtherance of any such action.

"Bankruptcy Laws" has the meaning specified in Section 11.09.

"Board Resolution" means a copy of a resolution certified by the Secretary or an Assistant Secretary of the Sponsor to have been duly adopted by the Sponsor's Board of Directors or a duly authorized committee thereof and to be in full force and effect on the date of such certification, and delivered to the Trustees.

"Book-Entry Preferred Securities Certificates" means certificates representing Preferred Securities issued in global, fully registered form to the Clearing Agency as described in Section 5.11.

"Business Day" means a day other than (i) a Saturday or a Sunday; (ii) a day on which banks in New York, New York are authorized or obligated by law or executive order to remain closed; or (iii) a day on which the Indenture Trustee's corporate trust office is closed for business.

"Calculation Agent" means Union Bank of California, N.A., acting as calculation agent, or its successor appointed by the Company and the Trust.

"Calculation Agent Agreement" means the agreement among the Company, the Trust and Union Bank of California, N.A., as calculation agent, dated as of April 5, 2004.

"Certificate Depository Agreement" means the agreement among the Trust, the Institutional Trustee and The Depository Trust Company, as the initial Clearing Agency, dated March 31, 2004, relating to the Preferred Securities Certificates.

"Clearing Agency" means an organization registered as a "clearing agency" pursuant to Section 17A of the Exchange Act. The Depository Trust Company will be the initial Clearing Agency.

"Clearing Agency Participant" means a broker, dealer, bank, other financial institution or other Person for whom from time to time a Clearing Agency effects book-entry transfers and pledges of securities deposited with the Clearing Agency.

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

"Commission" means the Securities and Exchange Commission, as from time to time constituted, created under the Exchange Act, or, if at any time after the execution of this instrument such Commission is not existing and performing the duties now assigned to it under the Trust Indenture Act, then the body performing such duties at such time.

"Common Security" means an undivided beneficial interest in the assets of the Trust having a Liquidation Amount of \$1,000 and having the rights provided therefor in this Declaration, including the right to receive Distributions and a Liquidation Distribution as provided herein.

"Common Securities Certificate" means a certificate evidencing ownership of a Common Security or Securities, substantially in the form attached as Exhibit C.

"Company" means Avista Corporation.

"Declaration" means this Amended and Restated Declaration of Trust, as the same may be modified, amended or supplemented in accordance with the applicable provisions hereof, including all exhibits hereto, including, for all purposes of this Amended and Restated Declaration of Trust and any modification, amendment or supplement, the provisions of the Trust Indenture Act that are deemed to be a part of and govern this Amended and Restated Declaration of Trust and any such modification, amendment or supplement, respectively.

"Definitive Preferred Securities Certificates" means either or both (as the context requires) of (i) Preferred Securities Certificates issued in certificated, fully registered form as provided in Section 5.11(a) and (ii) Preferred Securities Certificates issued in certificated, fully registered form as provided in Section 5.13.

"Delaware Bank" has the meaning specified in the preamble to this Declaration.

"Delaware Statutory Trust Act" means Chapter 38 of Title 12 of the Delaware Code, 12 Del. Code Section 3801 et seq., as it may be amended from time to time.

"Delaware Trustee" means the commercial bank or trust company or any other Person identified as the "Delaware Trustee" and has the meaning specified in the preamble to this Declaration solely in its capacity as Delaware Trustee of the Trust and not in its individual capacity, or its successor in interest in such capacity, or any successor Delaware Trustee appointed as herein provided.

"Designated CMT Maturity Index" means the original period to maturity of the U.S. Treasury securities (10 years) with respect to which the 10-year Treasury CMT will be calculated.

"Distribution Payment Date" means each day on which Distributions are payable determined based on the prevailing Distribution Rate.

"Distribution Period" means each semiannual period in a Fixed Rate Period and each quarterly period in a Floating Rate Period for which Distributions are payable.

"Distribution Rate" means the rate at which Distributions will accrue in respect of any Distribution Period, as determined pursuant to the terms of this Declaration, whether by Remarketing or otherwise.

"Distributions" means amounts payable in respect of the Trust Securities as provided in Section 4.01.

"Election Date" means a date that is no later than the fifth Business Day prior to the proposed Remarketing Date.

"Event of Default" means any one of the following events (whatever the reason for such Event of Default and whether it shall be voluntary or involuntary or be effected by operation of law or pursuant to any judgment, decree or order of any court or any order, rule or regulation of any administrative or governmental body):

- (a) the occurrence of an Indenture Event of Default;
- (b) default by the Trust in the payment of any Distribution when it becomes due and payable, and continuation of such default for a period of 60 days;
- (c) default by the Trust in the payment of any Redemption Price of any Trust Security when it becomes due and payable;
- (d) default in the performance, or breach, in any material respect, of any covenant or warranty of the Institutional Trustee and the Delaware Trustee in this Declaration (other than a covenant or warranty a default in the performance of which or the breach of which is dealt with in clause (b) or (c) above) and continuation of such default or breach for a period of 60 days after there has been give, by registered or certified mail, to the appropriate trustees and the Sponsor by the Holders of at least 33% in aggregate Liquidation Amount of the Outstanding Preferred Securities, a written notice specifying such default or breach and requiring it to be remedied and stating that such notice is a "Notice of Default" hereunder;
- (e) the occurrence of any Bankruptcy Event with respect to the Institutional Trustee or all or substantially all of its property if a successor Institutional Trustee has not been appointed within a period of 90 days thereof; or
- (f) the occurrence of any Bankruptcy Event with respect to the Trust.

"Exchange Act" means the Securities Exchange Act of 1934, as amended.

"Expense Agreement" means the Agreement as to Expenses and Liabilities between the Company and the Trust, substantially in the form attached as Exhibit B, as amended from time to time.

"Extension Period" has the meaning specified in Section 4.01(d).

"Federal Reserve Board" means the Board of Governors of the Federal Reserve System.

"Fixed Rate" means the Distribution Rate during a Fixed Rate Period as determined by a Remarketing.

"Fixed Rate Period" means the Initial Fixed Rate Period and each period set by the Company and the Regular Trustees during a Remarketing for which the Fixed Rate determined in such Remarketing will apply; provided, however, that a Fixed Rate Period must be for a duration of at least six months, may not extend beyond the stated maturity of the Subordinated Debt Securities and may not end on a day other than a day immediately preceding a Distribution Payment Date.

"Floating Rate" means the Distribution Rate during a Floating Rate Period calculated pursuant to Section 4.02(e).

"Floating Rate Determination Date" means the second London Business Day immediately preceding the first day of the relevant Distribution Period in the Floating Rate Period.

"Floating Rate Period" means any period during which a Floating Rate is in effect.

"Guarantee" means the Guarantee Agreement executed and delivered by the Company and Union Bank of California, N.A., as Guarantee Trustee, contemporaneously with the execution and delivery of this Declaration, for the benefit of the Holders of the Trust Securities, as amended from time to time.

"Indenture Event of Default" means an "Event of Default" as defined in the Subordinated Indenture.

"Indenture Redemption Date" means "Redemption Date," as defined in the Subordinated Indenture.

"Indenture Trustee" means the trustee under the Subordinated Indenture.

"Initial Distribution Rate" means 6.50% per annum.

"Initial Fixed Rate Period" means the Issue Date through March 31, 2009.

"Institutional Trustee" means the commercial bank or trust company identified as the "Institutional Trustee" in the preamble to this Declaration solely in its capacity as Institutional Trustee of the Trust and not in its individual capacity, or its successor in interest in such capacity, or any successor "Institutional Trustee" as herein provided.

"Investment Company Act" means the Investment Company Act of 1940, as amended.

"Issue Date" means the date of the delivery of the Trust Securities.

"Lien" means any lien, pledge, charge, encumbrance, mortgage, deed of trust, adverse ownership interest, hypothecation, assignment, security interest or preference, priority or other security agreement or preferential arrangement of any kind or nature whatsoever.

"Like Amount" means (i) Trust Securities having a Liquidation Amount equal to the principal amount of Subordinated Debt Securities to be contemporaneously redeemed or repaid

in accordance with the Subordinated Indenture and the proceeds of which will be used to pay the Redemption Price of such Trust Securities and (ii) Subordinated Debt Securities having a principal amount equal to the Liquidation Amount of the Trust Securities of the Holder to whom such Subordinated Debt Securities are distributed.

"Liquidation Amount" means the stated amount of \$1,000 per Trust Security.

"Liquidation Date" means the date on which Subordinated Debt Securities are to be distributed to Holders of Trust Securities in connection with a dissolution and liquidation of the Trust pursuant to Section 9.04.

"Liquidation Distribution" has the meaning specified in Section 9.05.

"London Business Day" means a day that is a Business Day and a day on which dealings in deposits in U.S. dollars are transacted, or with respect to any future date are expected to be transacted, in the London interbank market.

"Maturity Date of the Subordinated Debt Securities" means "Stated Maturity" as defined in the Subordinated Indenture.

"Majority in Liquidation Amount of the Preferred Securities" or "Majority in Liquidation Amount of the Common Securities" means, except as provided by the Trust Indenture Act, Preferred Securities or Common Securities, as the case may be, representing more than 50% of the aggregate Liquidation Amount of all then Outstanding Preferred Securities or Common Securities, as the case may be.

"Officers' Certificate" means a certificate signed by the Chairman of the Board, the President or a Vice President, and by the Treasurer, an Assistant Treasurer, the Secretary or an Assistant Secretary, of the Sponsor, and delivered to the appropriate Trustee. One of the officers signing an Officers' Certificate given pursuant to Section 8.16 shall be the principal executive, financial or accounting officer of the Sponsor. An Officers' Certificate delivered with respect to compliance with a condition or covenant provided for in this Declaration shall include:

(a) a statement that each officer signing the Officers' Certificate has read the covenant or condition and the definitions relating thereto;

(b) a brief statement of the nature and scope of the examination or investigation undertaken by each officer in rendering the Officers' Certificate;

(c) a statement that each such officer has made such examination or investigation as is necessary, in such officer's opinion, to express an informed opinion as to whether or not such covenant or condition has been complied with; and

(d) a statement as to whether, in the opinion of each such officer, such condition or covenant has been complied with.

"Opinion of Counsel" means a written opinion of counsel, who may be counsel for the Trust, the Trustees or the Sponsor, but not an employee of the Trust or the Trustees, and who

shall be reasonably acceptable to the Institutional Trustee. Any Opinion of Counsel pertaining to federal income tax matters may rely on published rulings of the Internal Revenue Service.

"Original Declaration of Trust" has the meaning specified in the recitals to this Declaration.

"Outstanding", when used with respect to Preferred Securities, means, as of the date of determination, all Preferred Securities theretofore authenticated and delivered under this Declaration, except:

(i) Preferred Securities theretofore canceled by the Regular Trustees or delivered to the Regular Trustees for cancellation;

(ii) Preferred Securities for whose payment or redemption money in the necessary amount has been theretofore deposited with the Institutional Trustee or any Paying Agent for the Holders of such Preferred Securities; provided that if such Preferred Securities are to be redeemed, notice of such redemption has been duly given pursuant to this Declaration; and

(iii) Preferred Securities in exchange for or in lieu of which other Preferred Securities have been authenticated and delivered pursuant to this Declaration;

provided, however, that in determining whether the Holders of the requisite Liquidation Amount of the Outstanding Preferred Securities have given any request, demand, authorization, direction, notice, consent or waiver hereunder, Preferred Securities owned by the Sponsor, the Holder of the Common Securities, any Trustee or any Affiliate of the Sponsor or any Trustee shall be disregarded and deemed not to be Outstanding, except that (a) in determining whether any Trustee shall be protected in relying upon any such request, demand, authorization, direction, notice, consent or waiver, only Preferred Securities which such Trustee knows to be so owned shall be so disregarded and (b) the foregoing shall not apply at any time when all of the outstanding Preferred Securities are owned by the Sponsor, the Holder of the Common Securities, one or more Trustees and/or any such Affiliate. Preferred Securities so owned which have been pledged in good faith may be regarded as Outstanding if the pledgee establishes to the satisfaction of the Regular Trustees the pledgee's right so to act with respect to such Preferred Securities and that the pledgee is not the Sponsor or any Affiliate of the Sponsor.

"Owner" means each Person who is the beneficial owner of a Book-Entry Preferred Securities Certificate as reflected in the records of the Clearing Agency or, if a Clearing Agency Participant is not the Owner, then as reflected in the records of a Person maintaining an account with such Clearing Agency (directly or indirectly, in accordance with the rules of such Clearing Agency).

"Paying Agent" means any paying agent or co-paying agent appointed pursuant to Section 5.09 and shall initially be the Institutional Trustee.

"Payment Account" means a segregated non-interest-bearing corporate trust account maintained by the Institutional Trustee for the benefit of the Securityholders in which all



amounts paid in respect of the Subordinated Debt Securities will be held and from which the Institutional Trustee shall make payments to the Securityholders in accordance with Section 4.01.

"Person" means an individual, corporation, partnership, joint venture, trust, limited liability company or corporation, unincorporated organization or government or any agency or political subdivision thereof.

"Preferred Securities Certificate" means a certificate evidencing ownership of a Preferred Security or Securities, substantially in the form attached as Exhibit A.

"Preferred Security" means an undivided beneficial interest in the assets of the Trust having a Liquidation Amount of \$1,000 and having rights provided therefor in this Declaration, including the right to receive Distributions and a Liquidation Distribution as provided herein.

"Record Date" means the opening of business on the Business Day immediately preceding the relevant Distribution Payment Date.

"Redemption Date" means, with respect to any Trust Security to be redeemed, the date fixed for such redemption by or pursuant to this Declaration; provided that each Indenture Redemption Date and the Maturity Date of the Subordinated Debt Securities shall be a Redemption Date for a Like Amount of Trust Securities.

"Redemption Price" means, with respect to any date fixed for redemption of any Trust Security, the Liquidation Amount of such Trust Security, plus accrued and unpaid Distributions to such date.

"Relevant Trustee" shall have the meaning specified in Section 8.10.

"Remarketing" means the conduct by which a Fixed Rate shall be determined in accordance with the Remarketing Procedures.

"Remarketing Agent" means Lehman Brothers Inc., its successors or assigns, or such other remarketing agent appointed to such capacity by the Company and the Regular Trustees.

"Remarketing Agreement" means the agreement among the Company, the Trust and Lehman Brothers Inc., as remarketing agent, dated as of April 5, 2004.

"Remarketing Date" means any Business Day no later than the third Business Day prior to any Remarketing Settlement Date.

"Remarketing Procedures" means those procedures set forth in Article X.

"Remarketing Settlement Date" means, to the extent applicable, (i) the first Business Day of the next Distribution Period following the expiration of the Initial Fixed Rate Period and any subsequent Fixed Rate Period; (ii) any Distribution Payment Date during a Floating Rate Period; or (iii) any Distribution Payment Date during a time in which Preferred Securities are redeemable in a Fixed Rate Period subsequent to the Initial Fixed Rate Period.

"Regular Trustee" means each of the individuals identified as a "Regular Trustee" in the preamble to this Declaration solely in their capacities as Regular Trustees of the Trust formed and continued hereunder and not in their individual capacities, or such trustee's successor(s) in interest in such capacity, or any successor "Regular Trustee" appointed as herein provided.

"Securities Register" and "Securities Registrar" are described in Section 5.04.

"Securityholder" or "Holder" means a Person in whose name a Trust Security or Securities is registered in the Securities Register; and any such Person who is a beneficial owner within the meaning of the Delaware Statutory Trust Act.

"Sponsor" means Avista Corporation, in its capacity as "Sponsor" under this Declaration.

"Subordinated Debt Securities" means the \$61,856,000 aggregate principal amount of the Sponsor's Subordinated Debt Securities, Series due 2034, issued pursuant to the Subordinated Indenture.

"Subordinated Indenture" means the Indenture, dated as of April 1, 2004, between the Sponsor and the Indenture Trustee, as the same may be modified, amended or supplemented in accordance with the applicable provisions thereof.

"Telerate Page 3750" means the display designated on page 3750 on MoneyLine Telerate (or such other page as may replace the 3750 page on the service or such other service as may be nominated by the British Bankers' Association for the purpose of displaying London interbank offered rates for U.S. dollar deposits).

"Telerate Page 7051" means the display on MoneyLine Telerate (or any successor service), on such page (or any other page as may replace such page on that service), for the purpose of displaying Treasury Constant Maturities as reported in H.15(519).

"10-year Treasury CMT" has the meaning set forth in Section 4.02(e).

"30-year Treasury CMT" has the meaning set forth in Section 4.02(e).

"3-month LIBOR Rate" has the meaning set forth in Section 4.02(e).

"Trust" means the Delaware statutory trust continued hereby and identified on the cover page to this Declaration.

"Trustees" means the Persons identified as "Trustees" in the preamble to this Declaration solely in their capacities as Trustees of the Trust and not in their individual capacities, or their successor in interest in such capacity, or any successor trustee appointed as herein provided.

"Trust Indenture Act" means the Trust Indenture Act of 1939 as in force at the date as of which this instrument was executed; provided, however, that in the event the Trust Indenture Act of 1939 is amended after such date, "Trust Indenture Act" means, to the extent required by any such amendment, the Trust Indenture Act of 1939 as so amended.

"Trust Property" means (i) the Subordinated Debt Securities; (ii) any cash on deposit in, or owing to, the Payment Account; and (iii) all proceeds and rights in respect of the foregoing and any other property and assets for the time being held or deemed to be held by the Institutional Trustee pursuant to this Declaration.

"Trust Securities Certificate" means any one of the Common Securities Certificates or the Preferred Securities Certificates.

"Trust Security" means any one of the Common Securities or the Preferred Securities.

"Underwriting Agreement" means the Underwriting Agreement, dated March 29, 2004, among the Trust, the Sponsor and the underwriters named therein.

## ARTICLE II

### ESTABLISHMENT OF THE TRUST

#### SECTION 2.01 Name

The Trust continued hereby shall be known as "AVA Capital Trust III", in which name the Trustees may conduct the business of the Trust, make and execute contracts and other instruments on behalf of the Trust and sue and be sued. The Regular Trustees may change the name of the Trust from time to time following written notice to the Holders.

#### SECTION 2.02 Offices of the Trustees; Principal Place of Business

The address of the Institutional Trustee is 475 Sansome Street, 12th Floor, San Francisco, California 94111, or at such other address as the Institutional Trustee may designate by written notice to the Securityholders and the Sponsor. The principal place of business of the Delaware Trustee is c/o SunTrust Delaware Trust Company, 1011 Centre Road, Suite 108, Wilmington, Delaware 19805, or at such other address in Delaware as the Delaware Trustee may designate by notice to the Sponsor. The address of the Regular Trustees is c/o Avista Corporation, 1411 East Mission Avenue, Spokane, Washington 99202, Attention: Treasurer. The principal place of business of the Trust is c/o Avista Corporation, 1411 East Mission Avenue, Spokane, Washington 99202. The Sponsor may change the principal place of business of the Trust at any time by giving notice thereof to the Trustees.

#### SECTION 2.03 Initial Contribution of Trust Property; Organizational Expenses

The Trust received from the Sponsor in connection with the Original Declaration of the sum of \$10, which constituted the initial Trust Property. The Sponsor, as obligor of the Subordinated Debt Securities, shall pay all costs and expenses of the Trust as they arise (including, but not limited to, costs and expenses relating to the organization of the Trust, issuance and sale of the Preferred Securities, the fees and expenses (including reasonable counsel fees and expenses) of the Trustees) or shall, upon request of the Trustees, promptly reimburse the Trustees for any such expenses paid by the Trustees. The Sponsor shall make no claim upon the Trust Property for the payment of such expenses.

#### SECTION 2.04 Issuance of the Preferred Securities

The Regular Trustees, on behalf of the Trust, shall execute and deliver to the underwriters named in the Underwriting Agreement Preferred Securities Certificates, registered in the name of the nominee of the initial Clearing Agency, in an aggregate amount of 60,000 Preferred Securities having an aggregate Liquidation Amount of \$60,000,000, against receipt of the aggregate purchase price of such Preferred Securities of \$60,000,000, which amount the Regular Trustees shall promptly deliver to the Institutional Trustee.

#### SECTION 2.05 Subscription and Purchase of Subordinated Debt Securities; Issuance of the Common Securities

The Regular Trustees, on behalf of the Trust, shall execute and deliver to the Sponsor Common Securities Certificates, registered in the name of the Sponsor, in an aggregate amount of 1,856 Common Securities having an aggregate Liquidation Amount of \$1,856,000 against payment by the Sponsor of such amount, which amount shall be promptly delivered to the Institutional Trustee. Contemporaneously therewith, the Regular Trustees, on behalf of the Trust, shall subscribe to and purchase from the Sponsor Subordinated Debt Securities, registered in the name of the Institutional Trustee, on behalf of the Trust and the Holders, and having an aggregate principal amount equal to \$61,856,000, and, in satisfaction of the purchase price for such Subordinated Debt Securities, the Institutional Trustee, on behalf of the Trust, shall deliver to the Sponsor the sum of \$61,856,000.

#### SECTION 2.06 Declaration of Trust

The exclusive purposes and functions of the Trust are (i) to issue and sell the Trust Securities and use the proceeds from such sale to acquire the Subordinated Debt Securities, (ii) to maintain its status as a grantor trust for federal income tax purposes; (iii) to make Distributions, and (iv) to engage in those activities necessary, incidental, appropriate or convenient thereto. The Sponsor hereby confirms each of the Bank, the Delaware Bank, Malyn K. Malquist and Diane C. Thoren as trustees of the Trust, to have all the rights, powers and duties to the extent set forth herein. The Institutional Trustee hereby declares that it will hold the Trust Property in trust upon and subject to the conditions set forth herein for the benefit of the Trust and the Securityholders. The Trustees shall have all rights, powers and duties set forth herein and in accordance with applicable law with respect to accomplishing the purposes of the Trust. The Delaware Trustee shall not be entitled to exercise any powers, nor shall the Delaware Trustee have any of the duties and responsibilities, of the Institutional Trustee or the Regular Trustees set forth herein. The Delaware Trustee shall be one of the Trustees for the sole and limited purpose of fulfilling the requirements of the Delaware Statutory Trust Act.

#### SECTION 2.07 Authorization to Enter into Certain Transactions

The Trustees shall conduct the affairs of the Trust in accordance with the terms of this Declaration. Subject to the limitations set forth in paragraph (c) of this Section, and in accordance with the following paragraphs (a) and (b), the Trustees shall have the authority to enter into all transactions and agreements determined by the Trustees to be appropriate in exercising the authority, express or implied, otherwise granted to the Trustees under this

Declaration, and to perform all acts in furtherance thereof, including without limitation, the following:

(a) As among the Trustees, the Regular Trustees, acting singly or jointly, shall have the exclusive power, duty and authority to act on behalf of the Trust with respect to the following matters:

(i) to acquire the Subordinated Debt Securities with the proceeds of the sale of the Trust Securities; provided, however, the Regular Trustees shall cause legal title to all of the Subordinated Debt Securities to be vested in, and the Subordinated Debt Securities to be held of record in the name of, the Institutional Trustee for the benefit of the Trust and Holders of the Trust Securities;

(ii) to give the Sponsor and the Institutional Trustee prompt written notice of the occurrence of any Special Event (as defined in the Subordinated Indenture) and to take any ministerial actions in connection therewith; provided, that the Regular Trustees shall consult with the Sponsor and the Institutional Trustee before taking or refraining to take any ministerial action in relation to a Special Event;

(iii) to establish a record date with respect to all actions to be taken hereunder that require a record date be established, including for the purposes of Section 316(c) of the Trust Indenture Act and with respect to Distributions, voting rights, redemptions, and exchanges, and to issue relevant notices to Holders of the Trust Securities as to such actions and applicable record dates;

(iv) to bring or defend, pay, collect, compromise, arbitrate, resort to legal action, or otherwise adjust claims or demands of or against the Trust ("Legal Action"), unless pursuant to Section 2.07(b)(v), the Institutional Trustee has the power to bring such Legal Action;

(v) to employ or otherwise engage employees and agents (who may be designated as officers with titles) and managers, contractors, advisors, and consultants and pay reasonable compensation for such services;

(vi) to cause the Trust to comply with the Trust's obligations under the Trust Indenture Act;

(vii) to give the certificate to the Institutional Trustee required by Section 314(a)(4) of the Trust Indenture Act, which certificate may be executed by any Regular Trustee;

(viii) to take all actions and perform such duties as may be required of the Regular Trustees pursuant to the terms of this Declaration, the Remarketing Agreement and the Calculation Agent Agreement;

(ix) to take all action that may be necessary or appropriate for the preservation and the continuation of the Trust's valid existence, rights, franchises

and privileges as a statutory trust under the laws of the State of Delaware and of each other jurisdiction in which such existence is necessary to protect the limited liability of the Holders of the Trust Securities or to enable the Trust to effect the purposes for which the Trust has been created;

(x) to take all action necessary to cause all applicable tax returns and tax information reports that are required to be filed with respect to the Trust to be duly prepared and filed by the Regular Trustees, on behalf of the Trust;

(xi) to execute and deliver the Trust Securities on behalf of the Trust;

(xii) to cause the Trust to enter into, and to execute, deliver and perform on behalf of the Trust, the Remarketing Agreement, the Calculation Agent Agreement, the Expense Agreement and the Certificate Depository Agreement and such other agreements as may be necessary or desirable in connection with the consummation hereof;

(xiii) to assist in the registration of the Preferred Securities under the Securities Act of 1933, as amended, and under state securities or blue sky laws, and the qualification of this Declaration as a trust indenture under the Trust Indenture Act;

(xiv) to assist in the listing of the Preferred Securities upon such securities exchange or exchanges, if necessary and as shall be determined by the Sponsor, and the registration of the Preferred Securities under the Exchange Act, and the preparation and filing of all periodic and other reports and other documents pursuant to the foregoing;

(xv) to send notices (other than notices of default) and other information regarding the Trust Securities and the Subordinated Debt Securities to the Securityholders in accordance with this Declaration, the Remarketing Agreement and the Calculation Agent Agreement;

(xvi) to appoint a Paying Agent (subject to Section 5.09), authenticating agent, Remarketing Agent, Calculation Agent and Securities Registrar in accordance with this Declaration;

(xvii) to elect to remarket the Preferred Securities and determine the length of any Fixed Rate Period in accordance with this Declaration, including redemption dates applicable to any Fixed Rate Period;

(xviii) to register transfers of the Trust Securities in accordance with this Declaration;

(xix) to assist in, to the extent provided in this Declaration, the winding up of the affairs of and termination of the Trust and the preparation, execution and filing of the certificate of cancellation with the Secretary of State of the State of Delaware; and

(xx) to take any action incidental to the foregoing as the Regular Trustees may from time to time determine is necessary, appropriate, convenient or advisable to protect and conserve the Trust Property for the benefit of the Securityholders (without consideration of the effect of any such action on any particular Securityholder).

(b) As among the Trustees, the Institutional Trustee shall have the exclusive power, duty and authority to act on behalf of the Trust with respect to the following matters:

(i) engage in such ministerial activities as shall be necessary or appropriate to effect promptly the redemption of the Trust Securities to the extent the Subordinated Debt Securities are redeemed, mature or otherwise repaid;

(ii) upon a distribution of Subordinated Debt Securities in accordance with the terms of this Declaration, engage in such ministerial activities as shall be necessary or appropriate to effect promptly the distribution of Subordinated Debt Securities to Holders of Trust Securities pursuant to the terms of this Declaration;

(iii) subject to the terms hereof, exercise all of the rights, powers and privileges of a holder of the Subordinated Debt Securities under the Subordinated Indenture and, if an Event of Default occurs and is continuing, shall enforce for the benefit of, and subject to the rights of, the Holders of the Trust Securities, its rights as holder of the Subordinated Debt Securities under the Subordinated Indenture;

(iv) take all actions and perform such duties as may be specifically required of the Institutional Trustee pursuant to the terms of this Declaration;

(v) take any Legal Action specifically required of the Institutional Trustee pursuant to the terms of this Declaration which arises out of or in connection with an Event of Default or the Institutional Trustee's duties and obligations under this Declaration, the Delaware Statutory Trust Act or the Trust Indenture Act;

(vi) the establishment and maintenance of the Payment Account;

(vii) the receipt of and holding of legal title to the Subordinated Debt Securities as described herein;

(viii) the collection of interest, principal and any other payments made in respect of the Subordinated Debt Securities in the Payment Account;

(ix) the distribution of amounts owed to the Securityholders in respect of the Trust Securities;

(x) the sending of notices of default and other information regarding the Trust Securities and the Subordinated Debt Securities to the Securityholders in accordance with this Declaration;

(xi) the distribution of the Trust Property in accordance with the terms of this Declaration;

(xii) as provided in this Declaration, the winding up of the affairs of and termination of the Trust; and

(xiii) the taking of any action incidental to the foregoing as the Institutional Trustee may from time to time determine is necessary, appropriate, convenient or advisable to protect and conserve the Trust Property for the benefit of the Securityholders (without consideration of the effect of any such action on any particular Securityholder).

(c) So long as this Declaration remains in effect, the Trust (or the Trustees acting on behalf of the Trust) shall not undertake any business, activities or transaction except as expressly provided herein or contemplated hereby. In particular, the Trustees shall not (i) acquire any investments or engage in any activities not authorized by this Declaration; (ii) sell, assign, transfer, exchange, pledge, set-off or otherwise dispose of any of the Trust Property or interests therein, including to Securityholders, except as expressly provided herein; (iii) take any action that would cause the Trust to fail or cease to qualify as a grantor trust for United States federal income tax purposes; (iv) incur any indebtedness for borrowed money; (v) take or consent to any action that would result in the placement of a Lien on any of the Trust Property; (vi) issue any securities other than the Trust Securities; or (vii) have any power to, or agree to any action by the Sponsor that would, vary the investment (within the meaning of Treasury Regulation Section 301.7701-4(c)) of the Trust or of the Securityholders. The Trustees shall defend all claims and demands of all Persons at any time claiming any Lien on any of the Trust Property adverse to the interest of the Trust or the Securityholders in their capacity as Securityholders.

(d) In connection with the issue and sale of the Preferred Securities, the Sponsor, as obligor of the Subordinated Debt Securities, shall have the right and responsibility to assist the Trust with respect to, or effect on behalf of the Trust, the following (and any actions taken by the Sponsor in furtherance of the following prior to the date of this Declaration are hereby ratified and confirmed in all respects):

(i) to prepare for filing by the Trust with the Commission, and execute on behalf of the Trust, a registration statement on Form S-3 under the Securities Act of 1933, as amended, in relation to the Preferred Securities, including any amendments thereto;

(ii) to determine the states in which to take appropriate action to qualify or register for sale all or part of the Preferred Securities and to do any and all such acts, other than actions which must be taken by or on behalf of the Trust, and advise the Trustees of actions they must take on behalf of the Trust, and prepare for execution and filing any documents to be executed and filed by the Trust or on behalf of the Trust, as the Sponsor deems necessary or advisable in order to comply with the applicable laws of any such States;



(iii) to prepare for filing by the Trust, and execute on behalf of the Trust, an application to the New York Stock Exchange or any other national stock exchange or the Nasdaq National Market for listing upon notice of issuance of any Preferred Securities, if applicable;

(iv) to prepare for filing by the Trust, and execute on behalf of the Trust, with the Commission a registration statement on Form 8-A relating to the registration of the Preferred Securities under Section 12(g) of the Exchange Act, including any amendments thereto, if applicable;

(v) to negotiate the terms of, and execute on behalf of the Trust, the Underwriting Agreement providing for the sale of the Preferred Securities and to execute, deliver and perform the Underwriting Agreement on behalf of the Trust;

(vi) to negotiate the terms of, on behalf of the Trust, the Remarketing Agreement providing for the retention of the Remarketing Agent and the establishment of certain procedures relating to Remarketings;

(vii) to negotiate the terms of, on behalf of the Trust, the Calculation Agent Agreement providing for the retention of the Calculation Agent;

(viii) to elect to remarket the Preferred Securities and determine the length of any Fixed Rate Period in accordance with this Declaration, including redemption dates applicable to any Fixed Rate Period; and

(ix) to take any other actions necessary, incidental, appropriate or convenient to carry out any of the foregoing activities.

(e) Notwithstanding anything herein to the contrary, the Regular Trustees are authorized and directed to conduct the affairs of the Trust and to operate the Trust so that the Trust will not be deemed to be an "investment company" required to be registered under the Investment Company Act of 1940, as amended, or taxed as other than a grantor trust for United States federal income tax purposes and so that the Subordinated Debt Securities will be treated as indebtedness of the Sponsor for United States federal income tax purposes. In this connection, the Sponsor and the Regular Trustees are authorized to take any action, not inconsistent with applicable law, the Certificate of Trust or this Declaration, that each of the Sponsor and the Regular Trustees determines in its discretion to be necessary or desirable for such purposes, as long as such action does not materially and adversely affect the interests of the Holders of the Preferred Securities.

#### SECTION 2.08. Assets of Trust

The assets of the Trust shall consist of the Trust Property.

#### SECTION 2.09. Title to Trust Property

Legal title to all Trust Property shall be vested at all times in the Institutional Trustee (in its capacity as such) and shall be held and administered by the Institutional Trustee for the

benefit of the Securityholders and the Trust in accordance with this Declaration. The right, title and interest of the Institutional Trustee to the Subordinated Debt Securities shall vest automatically in each Person who may thereafter be appointed as Institutional Trustee in accordance with the terms hereof. Such vesting and cessation of title shall be effective whether or not conveyancing documents have been executed and delivered.

#### SECTION 2.10. Mergers and Consolidations of the Trust

The Trust may not merge with or into, consolidate, amalgamate, or be replaced by, or convey, transfer or lease its properties and assets substantially as an entirety to, any entity, except pursuant to this Section 2.10 or Section 9.04. Upon the approval of the Holders of the Common Securities, and without the consent of the Holders of the Preferred Securities or the Trustees, the Trust may merge with or into, consolidate, amalgamate, or be replaced by or convey, transfer or lease its properties and assets substantially as an entirety to a trust organized as such under the laws of any state; provided, however, that (i) such successor entity either (a) expressly assumes all of the obligations of the Trust with respect to the Preferred Securities or (b) substitutes for the Preferred Securities other securities having substantially the same terms as the Preferred Securities (the "Successor Preferred Securities") so long as the Successor Preferred Securities have the same priority as the Preferred Securities with respect to distributions and payments upon liquidation, redemption and otherwise; (ii) a trustee of such successor entity possessing the same powers and duties as the Institutional Trustee is appointed to hold the Subordinated Debt Securities; (iii) such merger, consolidation, amalgamation, replacement, conveyance, transfer or lease does not cause the Preferred Securities (including any Successor Preferred Securities) to be downgraded by any nationally recognized statistical rating organization; (iv) the Preferred Securities or any Successor Preferred Securities are listed or quoted, or any Successor Preferred Securities will be listed or quoted upon notification of issuance, on any national securities exchange or with another organization on which Preferred Securities are then listed or quoted; (v) such merger, consolidation, amalgamation, replacement, conveyance, transfer or lease does not adversely affect the rights, preferences and privileges of the holders of the Preferred Securities (including any Successor Preferred Securities) in any material respect; (vi) such successor entity has a purpose substantially identical to that of the Trust; (vii) prior to such merger, consolidation, amalgamation, replacement, conveyance, transfer or lease, the Institutional Trustee has received an Opinion of Counsel from independent counsel experienced in such matters to the effect that (a) such merger, consolidation, amalgamation, replacement, conveyance, transfer or lease does not adversely affect the rights, preferences and privileges of the holders of the Preferred Securities (including any Successor Preferred Securities) in any material respect, and (b) following such merger, consolidation, amalgamation, replacement, conveyance, transfer or lease, neither the Trust nor such successor entity will be required to register as an "investment company" under the Investment Company Act; and (viii) the Sponsor or any permitted transferee to whom it has transferred the Common Securities hereunder owns all of the common securities of such successor entity and guarantees the obligations of such successor entity under the Successor Preferred Securities at least to the extent provided by the Guarantee. Notwithstanding the foregoing, the Trust shall not, except with the consent of Holders of 100% in aggregate Liquidation Amount of the Preferred Securities, consolidate, amalgamate, merge with or into, or be replaced by or convey, transfer or lease its properties and assets substantially as an entirety to, any other entity or permit any other entity to consolidate, amalgamate, merge with or into, or replace it if such consolidation, amalgamation, merger,

replacement, conveyance, transfer or lease would cause the Trust or the successor entity to be taxable other than as a grantor trust for United States federal income tax purposes. Any merger or similar agreement shall be executed by the Regular Trustees on behalf of the Trust.

### ARTICLE III

#### PAYMENT ACCOUNT

##### SECTION 3.01. Payment Account

(a) On or prior to the Issue Date, the Institutional Trustee shall establish the Payment Account. The Institutional Trustee and an agent of the Institutional Trustee shall have exclusive control and sole right of withdrawal with respect to the Payment Account for the purpose of making deposits in and withdrawals from the Payment Account in accordance with this Declaration. All monies and other property deposited or held from time to time in the Payment Account shall be held by the Institutional Trustee in the Payment Account for the exclusive benefit of the Securityholders and for distribution as herein provided, including (and subject to) any priority of payments provided for herein.

(b) The Institutional Trustee shall deposit in the Payment Account, promptly upon receipt, all payments of principal or interest on, and any other payments or proceeds with respect to, the Subordinated Debt Securities and any amounts paid to the Institutional Trustee pursuant to the Guarantee. Amounts held in the Payment Account shall not be invested by the Institutional Trustee pending distribution thereof.

### ARTICLE IV

#### DISTRIBUTIONS; REDEMPTION

##### SECTION 4.01. Distributions

(a) Distributions shall accrue from the Issue Date until the Redemption Date. During the Initial Fixed Rate Period, Distributions will be payable semiannually in arrears on April 1 and October 1 of each year, commencing on October 1, 2004. During any Fixed Rate Period, other than the Initial Fixed Rate Period, Distributions will be payable semiannually in arrears on the first day of the first month that begins at least six months after the first day of the Fixed Rate Period and on the first day of each six month period thereafter during such Fixed Rate Period. Any Fixed Rate Period may not end on a day other than a day immediately preceding a Distribution Payment Date. During any Floating Rate Period, Distributions will be payable quarterly in arrears on January 1, April 1, July 1 and October 1 of each year.

(b) If any Distribution Payment Date with respect to a Fixed Rate Period is not a Business Day, Distributions will be payable, without interest, on the immediately succeeding Business Day, with the same force and effect as if payment was made on the date such payment was originally payable (and without the accrual of any additional amount of Distributions). If any Distribution Payment Date with respect to a Floating Rate Period is not a Business Day, then Distributions will be payable on the immediately succeeding Business Day

and Distributions shall accrue to the actual payment date (except for a Distribution Payment Date that coincides with the Redemption Date).

(c) The amount of Distributions payable on each Distribution Payment Date relating to a Fixed Rate Period will be computed on the basis of a 360-day year of twelve 30-day months. The amount of Distributions payable on each Distribution Payment Date relating to a Floating Rate Period will be computed by multiplying the per annum Distribution Rate in effect for such Distribution Period by a fraction, the numerator of which will be the actual number of days in such Distribution Period (or portion thereof) (determined by including the first day thereof and excluding the last thereof) and the denominator of which will be 360, and multiplying the rate so obtained by \$1,000.

(d) The Company has the right under the Subordinated Indenture to defer payments of interest on the Subordinated Debt Securities by extending the interest period from time to time on the Subordinated Debt Securities (an "Extension Period") which, if exercised, would defer Distributions on the Trust Securities during any Extension Period. The payment of such Distributions, together with any interest thereon, will be distributed to the Holders of Trust Securities as received at the end of any Extension Period.

(e) Distributions on the Trust Securities shall be made and shall be deemed payable on each Distribution Payment Date only to the extent that the Trust has available funds on hand in the Payment Account for the payment of such Distributions.

(f) Distributions on the Trust Securities on each Distribution Date shall be payable to the Holders thereof as they appear on the Securities Register for the Trust Securities on the relevant Record Date.

Each Trust Security upon registration of transfer of or in exchange for or in lieu of any other Trust Security shall carry the rights of Distributions accrued and unpaid, and to accrue, which were carried by such other Trust Security.

#### SECTION 4.02. Distribution Rate

(a) During the Initial Fixed Rate Period, the Distribution Rate shall be the Initial Distribution Rate.

(b) Prior to the expiration of the Initial Fixed Rate Period and any subsequent Fixed Rate Period, prior to any Distribution Payment Date with respect to a Floating Rate Period or prior to any Distribution Payment Date in a Fixed Rate Period during a time in which the Preferred Securities are redeemable in such Fixed Rate Period, the Company and the Regular Trustees will have the option to remarket the Preferred Securities to establish a new Fixed Rate for a new Fixed Rate Period (to be in effect after the expiration of the then current Distribution Period). If the Company and the Regular Trustees elect to conduct a Remarketing of the Preferred Securities for the purpose of establishing a new Fixed Rate for a new Fixed Rate Period, the Trust shall, not less than 20 nor more than 35 Business Days prior to the related Election Date, notify in writing the Clearing Agency, the Institutional Trustee, the Indenture Trustee, the Calculation Agent and the Remarketing Agent. If the Preferred Securities are not

issued in global, fully registered form to the Clearing Agency or its nominee, such notice shall be delivered to the Owners instead of the Clearing Agency. Such notice shall describe the Remarketing and shall indicate the length of the proposed new Fixed Rate Period, the proposed Remarketing Date and any redemption provisions that will apply during such new Fixed Rate Period. The Company and the Regular Trustees shall have the right to terminate a Remarketing at any time prior to the Election Date by written notice of such termination to the Clearing Agency (or the Owners, as applicable), the Remarketing Agent, the Institutional Trustee, the Indenture Trustee and the Calculation Agent.

(c) If the Remarketing Agent has determined that it will be able to remarket all Preferred Securities tendered or deemed tendered for purchase in the Remarketing at a Fixed Rate and at a price of \$1,000 per Preferred Security, on any Remarketing Date, the Distribution Rate for the new Fixed Rate Period will be the Fixed Rate determined by the Remarketing Agent, which will be the rate per annum (rounded to the nearest one-thousandth (0.001) of one percent per annum) which the Remarketing Agent determines, in its sole judgment, to be the lowest Fixed Rate per annum that will enable it to remarket all Preferred Securities tendered or deemed tendered for Remarketing at a price of \$1,000 per Preferred Security.

(d) If the Company and the Regular Trustees do not elect to remarket the Preferred Securities pursuant to Section 4.02(b) or have terminated a Remarketing or if the Remarketing Agent is unable to remarket all of the Preferred Securities tendered or deemed tendered for a purchase price of \$1,000 per Preferred Security pursuant to the Remarketing Procedures, the Distribution Rate for the next Distribution Period shall be the Floating Rate and the new Distribution Period shall be a Floating Rate Period.

(e) The Calculation Agent shall calculate the Floating Rate on the Floating Rate Determination Date as follows:

Except as provided below, the Floating Rate for any Floating Rate Period for the Preferred Securities will be equal to the Adjustable Rate (as defined below) plus 3.66%. The "Adjustable Rate" for any Distribution Period will be equal to the highest of the 3-month LIBOR Rate, the 10-year Treasury CMT and the 30-year Treasury CMT (each as defined below and collectively referred to as the "Benchmark Rates") for such Distribution Period during the Floating Rate Period. In the event that the Calculation Agent determines in good faith that for any reason:

- (1) any one of the Benchmark Rates cannot be determined for any Distribution Period, the Adjustable Rate for such Distribution Period will be equal to the higher of whichever two of such rates can be so determined;
- (2) only one of the Benchmark Rates can be determined for any Distribution Period, the Adjustable Rate for such Distribution Period will be equal to whichever such rate can be so determined; or

- (3) none of the Benchmark Rates can be determined for any Distribution Period, the Adjustable Rate for the preceding Distribution Period will be continued for such Distribution Period.

The "3-month LIBOR Rate" means, for each Distribution Period, the arithmetic average of the two most recent weekly quotes for deposits for U.S. Dollars having a term of three months, as published on the first Business Day of each week immediately preceding the Distribution Period for which the Floating Rate is being determined. Such quotes will be taken from Telerate Page 3750 at approximately 11:00 a.m. London time on the relevant date. If such rate does not appear on Telerate Page 3750 on the Floating Rate Determination Date, the 3-month LIBOR Rate will be the arithmetic mean of the rates quoted by three major banks in New York City selected by the Calculation Agent, at approximately 11:00 a.m., New York City time, on the Floating Rate Determination Date for loans in U.S. Dollars to leading European banks for a period of three months.

"The 10-year Treasury CMT" means the rate determined in accordance with the following provisions:

- (1) With respect to any Floating Rate Determination Date and the Distribution Period that begins immediately thereafter, the 10-year Treasury CMT means the rate displayed on Telerate Page 7051 under the caption "...Treasury Constant Maturities... Federal Reserve Board Release H.15...Mondays Approximately 3:45 P.M.", under the column for the Designated CMT Maturity Index (as defined below).
- (2) If such rate is no longer displayed on the relevant page, or is not so displayed by 3:00 P.M., New York City time, on the applicable Floating Rate Determination Date, then the 10-year Treasury CMT for such Floating Rate Determination Date will be such treasury constant maturity rate for the Designated CMT Maturity Index as is published in H.15(519).
- (3) If such rate is no longer displayed on the relevant page, or if not published by 3:00 P.M., New York City time, on the applicable Floating Rate Determination Date, then the 10-year Treasury CMT for such Floating Rate Determination Date will be such constant maturity treasury rate for the Designated CMT Maturity Index (or other United States Treasury rate for the Designated CMT Maturity Index) for the applicable Floating Rate Determination Date with respect to such Distribution reset date as may then be published by either the Board of Governors of the Federal Reserve System or the United States Department of the Treasury that the Calculation Agent determines to be comparable to the rate formerly displayed on the Telerate Page 7051 and published in H.15(519).

- (4) If such information is not provided by 3:00 P.M., New York City time, on the applicable Floating Rate Determination Date, then the 10-year Treasury CMT for such Floating Rate Determination Date will be calculated by the Calculation Agent and will be a yield to maturity, based on the arithmetic mean of the secondary market offered rates as of approximately 3:30 P.M., New York City time, on such Floating Rate Determination Date reported, according to their written records, by three leading primary United States government securities dealers in The City of New York (each, a "Reference Dealer") selected by the Calculation Agent (from five such Reference Dealers selected by the Calculation Agent and eliminating the highest quotation (or, in the event of equality, one of the highest) and the lowest quotation (or, in the event of equality, one of the lowest)), for the most recently issued direct noncallable fixed rate obligations of the United States ("Treasury Debentures") with an original maturity of approximately the Designated CMT Maturity Index and a remaining term to maturity of not less than such Designated CMT Maturity Index minus one year.
- (5) If the Calculation Agent is unable to obtain three such Treasury Debentures quotations, the 10-year Treasury CMT for the applicable Floating Rate Determination Date will be calculated by the Calculation Agent and will be a yield to maturity based on the arithmetic mean of the secondary market offered rates as of approximately 3:30 P.M., New York City time, on the applicable Floating Rate Determination Date of three Reference Dealers in The City of New York (from five such Reference Dealers selected by the Calculation Agent and eliminating the highest quotation (or, in the event of equality, one of the highest) and the lowest quotation (or, in the event of equality, one of the lowest)), for Treasury Debentures with an original maturity of the number of years that is the next highest to the Designated CMT Maturity Index and a remaining term to maturity closest to the Designated CMT Maturity Index and in an amount of at least \$100 million.
- (6) If three or four (and not five) of such Reference Dealers are quoting as set forth above, then the 10-year Treasury CMT will be based on the arithmetic mean of the offered rates obtained and neither the highest nor lowest of such quotes will be eliminated; provided, however, that if fewer than three Reference Dealers selected by the Calculation Agent are quoting as set forth above, the 10-year Treasury CMT

with respect to the applicable Floating Rate Determination Date will remain the 10-year Treasury CMT for the immediately preceding interest period. If two Treasury Debentures with an original maturity as described in the second preceding sentence have remaining terms to maturity equally close to the Designated CMT Maturity Index, then the quotes for the Treasury Debentures with the shorter remaining term to maturity will be used.

The "30-year Treasury CMT" has the meaning specified under the definition of 10-year Treasury CMT, except that the Designated CMT Maturity Index for the 30-year Treasury CMT shall be 30 years.

The 3-month LIBOR Rate, the 10-year Treasury CMT and the 30-year Treasury CMT shall each be rounded to the nearest hundredth of a percent.

The Floating Rate with respect to each Floating Rate Period will be calculated as promptly as practicable by the Calculation Agent according to the appropriate method described above.

(f) If the Company elects to defer interest during a Fixed Rate Period, Distributions will continue to accrue and be compounded semiannually at the Fixed Rate until the expiration of the Fixed Rate Period. Prior to the expiration of such Fixed Rate Period and any subsequent Fixed Rate Period during the Extension Period, the Company and the Regular Trustees will have the option to remarket the Preferred Securities for a new Fixed Rate Period (to take effect upon expiration of such Fixed Rate Period). If the Company and the Trust do not remarket the Preferred Securities, the Floating Rate during the Extension Period shall be determined as provided herein, but shall not be less than the Fixed Rate for the Fixed Rate Period just ended. If the Company elects to defer interest during a Floating Rate Period, Distributions will continue to accrue and be compounded quarterly at the applicable Floating Rate, reset quarterly, subject to the right of the Company and the Regular Trustees to remarket the Preferred Securities prior to any Distribution Payment Date in order to establish a new Fixed Rate for a new Fixed Rate Period in accordance with this Section 4.02 and the Remarketing Procedures.

#### SECTION 4.03. Distribution Periods

In accordance with Section 4.02 and the Remarketing Procedures, the Company and the Regular Trustees, on behalf of the Trust may, prior to the expiration of the Initial Fixed Rate Period and any subsequent Fixed Rate Period, prior to any Distribution Payment Date in a Fixed Rate Period during a time in which the Preferred Securities are redeemable in such Fixed Rate Period or prior to any Distribution Payment Date with respect to a Floating Rate Period, elect to remarket the Preferred Securities to establish a new Fixed Rate for a new Fixed Rate Period (to be in effect after the then current Distribution Period). A Fixed Rate Period must be for a duration of at least six months, may not extend beyond the stated maturity of the Subordinated Debt Securities and may not end on a day other than a day immediately preceding a Distribution Payment Date. If a new Fixed Rate for a new Fixed Rate Period is set in a Remarketing, a new Fixed Rate Period shall commence following the expiration of the then current Distribution



Period. If a new Fixed Rate for a new Fixed Rate Period is not set, for any reason, including after the expiration of the Initial Fixed Rate Period, in accordance with the terms of this Declaration, a Floating Rate Period and the Floating Rate reset quarterly shall be in effect if and until the Company and the Regular Trustees remarket the Preferred Securities and set a new Fixed Rate for a new Fixed Rate Period in accordance with Section 4.02 and the Remarketing Procedures.

#### SECTION 4.04. Redemption

(a) On each Indenture Redemption Date and the Maturity Date of the Subordinated Debt Securities, the Trust will be required to redeem a Like Amount of Trust Securities at the Redemption Price.

(b) Notice of redemption shall be given by the Institutional Trustee by first class mail, postage prepaid, mailed not less than 30 nor more than 60 days prior to the Redemption Date to each Holder of Trust Securities to be redeemed, at such Holder's address appearing in the Securities Register. All notices of redemption shall state:

(i) the Redemption Date;

(ii) the Redemption Price;

(iii) the CUSIP number or CUSIP numbers of the Preferred Securities affected;

(iv) that on the Redemption Date the Redemption Price will become due and payable, to the extent set forth in Section 4.04(d) below, upon each such Trust Security to be redeemed and that Distributions thereon will cease to accumulate on and after said date, except as provided in Section 4.04(e) below; and

(v) the place or places where Trust Securities are to be surrendered for the payment of the Redemption Price.

If the notice of the related redemption of Subordinated Debt Securities states that such redemption of Subordinated Debt Securities is conditional upon the receipt by the paying agent or agents of money sufficient to pay the redemption price on such Subordinated Debt Securities as provided in Section 4.04 of the Subordinated Indenture, then the notice of redemption of the Trust Securities shall refer to such condition and the effect thereof.

(c) The Trust in issuing the Trust Securities may use "CUSIP" or "private placement" numbers (if then generally in use), and, if so, the Institutional Trustee shall indicate the "CUSIP" or "private placement" numbers of the Trust Securities in notices of redemption and related materials as a convenience to Holders; provided, that any such notice may state that no representation is made as to the correctness of such numbers either as printed on the Trust Securities or as contained in any notice of redemption and related material.

(d) The Trust Securities redeemed on each Redemption Date shall be redeemed at the Redemption Price with the applicable proceeds from the contemporaneous redemption or repayment of Subordinated Debt Securities. Redemptions of the Trust Securities shall be made and the Redemption Price shall be due and payable on each Redemption Date to the extent, but only to the extent, that the Trust has funds then on hand and available in the Payment Account for the payment of such Redemption Price.

(e) If the Trust gives a notice of redemption in respect of any Preferred Securities, then by 2:00 P.M., New York City time, on the Redemption Date, subject to Section 4.04(d) above and this Section 4.04(e), the Institutional Trustee will, with respect to Preferred Securities held in global form, irrevocably deposit with the Clearing Agency for such Preferred Securities, to the extent available therefor, funds sufficient to pay the applicable Redemption Price and will give such Clearing Agency irrevocable instructions and authority to pay the Redemption Price to the Holders of the Preferred Securities. With respect to Preferred Securities that are not held in global form, the Institutional Trustee, subject to Section 4.04(d) above and this Section 4.04(e), will irrevocably deposit with the Paying Agent, to the extent available therefor, funds sufficient to pay the applicable Redemption Price and will give the Paying Agent irrevocable instructions and authority to pay the Redemption Price to the Holders of the Preferred Securities upon surrender of their Preferred Securities Certificates. Notwithstanding the foregoing, Distributions payable on or prior to the Redemption Date for any Trust Securities called for redemption shall be payable to the Holders of such Trust Securities as they appear on the Securities Register for the Trust Securities on the relevant Record Dates for the related Distribution Dates. If notice of redemption shall have been given (or if the Sponsor has given irrevocable instructions to the Institutional Trustee to give notice of redemption) and funds deposited as required, then, upon the date of such deposit, all rights of Holders holding Trust Securities so called for redemption will cease, except the right of such Holders to receive the Redemption Price and any Distribution payable in respect of the Trust Securities on or prior to the Redemption Date, but without interest, and such Trust Securities will cease to be Outstanding. In the event that any date on which any applicable Redemption Price is payable is not a Business Day, then payment of the applicable Redemption Price payable on such date will be made on the next succeeding day that is a Business Day (and without any interest or other payment in respect of any such delay), except that, if such Business Day falls in the next calendar year, such payment will be made on the immediately preceding Business Day, in each case, with the same force and effect as if made on such date. In the event that payment of the Redemption Price in respect of any Trust Securities called for redemption is improperly withheld or refused and not paid either by the Trust or by the Sponsor pursuant to the Guarantee, Distributions on such Trust Securities will continue to accumulate, as set forth in Section 4.01 and in accordance with the continued accrual of interest on the Subordinated Debt Securities, from the Redemption Date originally established by the Trust for such Trust Securities to the date such applicable Redemption Price is actually paid, in which case the actual payment date will be the date fixed for redemption for purposes of calculating the applicable Redemption Price.

#### SECTION 4.05. Subordination of Common Securities and Distributions

(a) Payment of Distributions on, and the Redemption Price of, the Trust Securities, as applicable, shall be made pro rata based on the Liquidation Amount of the Trust

Securities; provided, however, that if on any Distribution Payment Date or Redemption Date an Indenture Event of Default shall have occurred and be continuing, no payment of any Distribution on, or Redemption Price of, any Common Security, and no other payment on account of the redemption, liquidation or other acquisition of Common Securities, shall be made unless payment in full in cash of all accumulated and unpaid Distributions on all Outstanding Preferred Securities for all Distribution Periods terminating on or prior thereto, or in the case of payment of the Redemption Price the full amount of such Redemption Price on all Outstanding Preferred Securities, shall have been made or provided for, and all funds immediately available to the Institutional Trustee shall first be applied to the payment in full in cash of all Distributions on, or Redemption Price of, Preferred Securities then due and payable.

(b) In the case of the occurrence of any Indenture Event of Default, the Holder of Common Securities will be deemed to have waived any right to act with respect to such Event of Default under this Declaration until the effect of all such Events of Default with respect to the Preferred Securities have been cured, waived or otherwise eliminated. Until any such Events of Default under this Declaration with respect to the Preferred Securities have been so cured, waived or otherwise eliminated, the Institutional Trustee shall act solely on behalf of the Holders of the Preferred Securities and not the Holder of the Common Securities, and only the Holders of the Preferred Securities will have the right to direct the Institutional Trustee to act on their behalf.

(c) Distributions on the Common Securities shall be payable at the same Distribution Rates, on the same Distribution Payment Dates and for the same Distribution Periods and to holders as of the same Record Date as for the Preferred Securities.

#### SECTION 4.06. Payment Procedures

Payments of Distributions in respect of the Preferred Securities shall be made by check mailed to the address of the Person entitled thereto as such address shall appear on the Securities Register or, if the Preferred Securities are held by a Clearing Agency, such Distributions shall be made to the Clearing Agency, which shall credit the relevant Persons' accounts at such Clearing Agency on the applicable Distribution Payment Dates. Payment of the Redemption Price of or Liquidation Distribution on the Preferred Securities shall be made in immediately available funds upon surrender of the Preferred Securities Certificates representing such Preferred Securities at the corporate trust office of the Institutional Trustee in Los Angeles, California, or, if the Preferred Securities are held by the Clearing Agency or its nominee, such Redemption Price or Liquidation Distribution shall be made to the Clearing Agency by wire transfer in immediately available funds. Payments in respect of the Common Securities shall be made in such manner as shall be mutually agreed between the Institutional Trustee and the Holder of the Common Securities.

#### SECTION 4.07. Tax Returns and Reports

The Regular Trustee(s) shall prepare (or cause to be prepared), at the Sponsor's expense, and file all United States federal, state and local tax and information returns and reports required to be filed by or in respect of the Trust. The Regular Trustee(s) shall provide or cause to be

provided on a timely basis to each Holder any Internal Revenue Service form required to be so provided in respect of the Trust Securities.

#### SECTION 4.08. Exchange

(a) If at any time the Sponsor or any of its Affiliates (in either case, a "Sponsor Affiliated Owner/Holder") is the Owner or Holder of any Preferred Securities, such Sponsor Affiliated Owner/Holder shall have the right to deliver to the Institutional Trustee all or such portion of its Preferred Securities as it elects and receive, in exchange therefore, a like amount of Subordinated Debt Securities. Such election (i) shall be exercisable effective on any Distribution Payment Date by such Sponsor Affiliated Owner/Holder delivering to the Institutional Trustee a written notice of such election specifying the liquidation amount of Preferred Securities with respect to which such election is being made and the Distribution Payment Date on which such exchange shall occur, which Distribution Payment Date shall be not less than ten Business Days after the date of receipt by the Institutional Trustee or its designee the Preferred Securities which are the subject of such election by 1:00 P.M. New York time, on the Distribution Payment Date on which such exchange is to occur. After the exchange, such Preferred Securities will be canceled and will no longer be deemed to be outstanding and all rights of the Sponsor or its Affiliate(s) with respect to such Preferred Securities will cease.

(b) In the case of an exchange described in Section 4.08(a), the Trust will, on the date of such exchange, exchange Subordinated Debt Securities having a principal amount equal to the aggregate liquidation amount of the outstanding Common Securities, multiplied by the ratio of the aggregate liquidation amount of the Preferred Securities exchanged pursuant to Section 4.08(a) divided by the aggregate liquidation amount of the Preferred Securities outstanding immediately prior to such exchange, for such proportional amount of Common Securities held by the Sponsor (which contemporaneously shall be canceled and no longer be deemed to be outstanding); provided, that the Sponsor delivers or caused to be delivered to the Institutional Trustee or its designee the required amount of Common Securities to be exchanged by 1:00 P.M. New York time, on the Distribution Payment Date on which such exchange is to occur.

### ARTICLE V

#### TRUST SECURITIES CERTIFICATES

##### SECTION 5.01. Initial Ownership

Upon the creation of the Trust by the contribution by the Sponsor pursuant to Section 2.03 and until the issuance of the Trust Securities, and at any time during which no Trust Securities are outstanding, the Sponsor shall be the sole beneficial owner of the Trust.

#### SECTION 5.02. The Trust Securities Certificates

Each of the Preferred and Common Securities Certificates shall be issued in minimum denominations of \$1,000 and integral multiples in excess thereof. The Trust Securities Certificates shall be executed on behalf of the Trust by manual or facsimile signature of at least one Regular Trustee. Trust Securities Certificates bearing the manual or facsimile signatures of individuals who were, at the time when such signatures shall have been affixed, authorized to sign on behalf of the Trust, shall be validly issued and entitled to the benefits of this Declaration, notwithstanding that such individuals or any of them shall have ceased to be so authorized prior to the authentication and delivery of such Trust Securities Certificates or did not hold such offices at the date of authentication and delivery of such Trust Securities Certificates. A transferee of a Trust Securities Certificate shall become a Securityholder, and shall be entitled to the rights and subject to the obligations of a Securityholder hereunder, upon due registration of such Trust Securities Certificate in such transferee's name pursuant to Section 5.04.

#### SECTION 5.03. Authentication of Trust Securities Certificates

On the Issue Date, the Regular Trustees shall cause Trust Securities Certificates, in an aggregate Liquidation Amount as provided in Sections 2.04 and 2.05, to be executed on behalf of the Trust, authenticated and delivered to or upon the written order of the Sponsor signed by its Chairman of the Board, its President or any Vice President, without further corporate action by the Sponsor, in authorized denominations. No Trust Securities Certificate shall entitle its holder to any benefit under this Declaration, or shall be valid for any purpose, unless there shall appear on such Trust Securities Certificate a certificate of authentication substantially in the form set forth in Exhibit A or Exhibit C, as applicable, executed by the Institutional Trustee by manual signature; such authentication shall constitute conclusive evidence that such Trust Securities Certificate shall have been duly authenticated and delivered hereunder. All Trust Securities Certificates shall be dated the date of their authentication.

#### SECTION 5.04. Registration of Transfer and Exchange of Preferred Securities Certificates

The Securities Registrar shall keep or cause to be kept, at the office or agency maintained pursuant to Section 5.08, a Securities Register in which, subject to such reasonable regulations as it may prescribe, the Securities Registrar shall provide for the registration of Preferred Securities Certificates and the Common Securities Certificates (subject to Section 5.10 in the case of the Common Securities Certificates) and registration of transfers and exchanges of Preferred Securities Certificates as herein provided. The Institutional Trustee shall be the initial Securities Registrar.

Upon surrender for registration of transfer of any Preferred Securities Certificate at the office or agency maintained pursuant to Section 5.08, one or more of the Regular Trustees shall execute, and the Institutional Trustee shall authenticate and deliver in the name of the designated transferee or transferees one or more new Preferred Securities Certificates in authorized denominations of a like aggregate Liquidation Amount dated the date of authentication by the Institutional Trustee. The Securities Registrar shall not be required to register the transfer of any Preferred Securities that have been called for redemption. At the option of a Holder, Preferred

Securities Certificates may be exchanged for other Preferred Securities Certificates in authorized denominations of the same class and of a like aggregate Liquidation Amount upon surrender of the Preferred Securities Certificates to be exchanged at the office or agency maintained pursuant to Section 5.08.

Every Preferred Securities Certificate presented or surrendered for registration of transfer or exchange shall be accompanied by a written instrument of transfer in form satisfactory to the Trustees and the Securities Registrar duly executed by the Holder or his attorney duly authorized in writing. Each Preferred Securities Certificate surrendered for registration of transfer or exchange shall be canceled and subsequently disposed of by the Securities Registrar in accordance with its customary practice.

No service charge shall be made for any registration of transfer or exchange of Preferred Securities Certificates, but the Securities Registrar or the Regular Trustees may require payment of a sum sufficient to cover any tax or governmental charge that may be imposed in connection with any transfer or exchange of Preferred Securities Certificates.

#### SECTION 5.05. Mutilated, Destroyed, Lost or Stolen Trust Securities Certificates

If (a) any mutilated Trust Securities Certificate shall be surrendered to the Securities Registrar, or if the Securities Registrar shall receive evidence to its satisfaction of the destruction, loss or theft of any Trust Securities Certificate and (b) there shall be delivered to the Securities Registrar and the Regular Trustees such security or indemnity as may be required by them to save each of them harmless, then in the absence of notice that such Trust Securities Certificate shall have been acquired by a bona fide purchaser, the Regular Trustees or any one of them on behalf of the Trust shall execute, and the Institutional Trustee shall authenticate and make available for delivery, in exchange for or in lieu of any such mutilated, destroyed, lost or stolen Trust Securities Certificate, a new Trust Securities Certificate of like class, tenor and denomination. In connection with the issuance of any new Trust Securities Certificate under this Section, the Regular Trustees or the Securities Registrar may require the payment of a sum sufficient to cover any tax or other governmental charge that may be imposed in connection therewith. Any duplicate Trust Securities Certificate issued pursuant to this Section shall constitute conclusive evidence of an ownership interest in the Trust, as if originally issued, whether or not the lost, stolen or destroyed Trust Securities Certificate shall be found at any time.

#### SECTION 5.06. Persons Deemed Securityholders

Prior to due presentation of a Trust Securities Certificate for registration of transfer, the Trustees or the Securities Registrar shall treat the Person in whose name any Trust Securities Certificate shall be registered in the Securities Register as the owner of such Trust Securities Certificate for the purpose of receiving Distributions (subject to Section 4.01(d)) and for all other purposes whatsoever, and neither the Trustees nor the Securities Registrar shall be bound by any notice to the contrary.

#### SECTION 5.07. Access to List of Securityholders' Names and Addresses

In the event that the Institutional Trustee is no longer the Securities Registrar, the Regular Trustees shall furnish or cause to be furnished to (i) the Sponsor and the Institutional Trustee semi-annually, not later than June 1 and December 1 in each year, and (ii) the Sponsor or the Institutional Trustee, as the case may be, within 15 days after receipt by any Regular Trustee of a request therefor from the Sponsor or the Institutional Trustee, as the case may be, in writing, a list, in such form as the Sponsor or the Institutional Trustee, as the case may be, may reasonably require, of the names and addresses of the Securityholders as of a date not more than 15 days prior to the time such list is furnished. If three or more Securityholders or one or more Holders of Trust Securities Certificates evidencing not less than 25% of the outstanding Liquidation Amount apply in writing to the Regular Trustees, and such application states that the applicants desire to communicate with other Securityholders with respect to their rights under this Declaration or under the Trust Securities Certificates and such application is accompanied by a copy of the communication that such applicants propose to transmit, then the Regular Trustees shall, within five Business Days after the receipt of such application, afford such applicants access during normal business hours to the current list of Securityholders. Each Holder, by receiving and holding a Trust Securities Certificate, shall be deemed to have agreed not to hold the Sponsor, the Institutional Trustee or the Regular Trustees accountable by reason of the disclosure of its name and address, regardless of the source from which such information was derived.

#### SECTION 5.08. Maintenance of Office or Agency

The Regular Trustees shall maintain an office or offices or agency or agencies where Preferred Securities Certificates may be surrendered for registration of transfer or exchange and where notices and demands to or upon the Trustees in respect of the Trust Securities Certificates may be served. The Regular Trustees initially designate Union Bank of California, N.A., 475 Sansome Street, 12th Floor, San Francisco, California 94111, or such other address as may be designated by the Institutional Trustee to the Regular Trustee, as its principal agency for such purposes. The Regular Trustees shall give prompt written notice to the Sponsor and to the Securityholders of any change in the location of the Securities Register or any such office or agency.

#### SECTION 5.09. Appointment of Paying Agent

The Paying Agent shall make Distributions and other payments provided hereby to Securityholders from the Payment Account and shall report the amounts of such Distributions and payments to the Institutional Trustee and the Regular Trustees. Any Paying Agent shall have the revocable power to withdraw funds from the Payment Account for the purpose of making the Distributions and payments provided hereby. The Regular Trustees may revoke such power and remove the Paying Agent if such Trustees determine in their sole discretion that the Paying Agent shall have failed to perform its obligations under this Agreement in any material respect, provided that such revocation and removal shall not become effective until the appointment of a successor. The Paying Agent shall initially be the Institutional Trustee, and it may choose any co-paying agent that is acceptable to the Regular Trustees and the Sponsor. Any Person acting as Paying Agent shall be permitted to resign as Paying Agent upon 30 days'

written notice to the Regular Trustees and the Institutional Trustee, provided that such resignation shall not become effective until the appointment of a successor. In the event that a Paying Agent shall resign or be removed, the Institutional Trustee shall appoint a successor that is acceptable to the Regular Trustees to act as Paying Agent (which shall be a bank or trust company). The Institutional Trustee shall cause such successor Paying Agent or any additional Paying Agent appointed by the Institutional Trustee to execute and deliver to the Trustees an instrument in which such successor Paying Agent or additional Paying Agent shall agree with the Trustees that as Paying Agent, such successor Paying Agent or additional Paying Agent will hold all sums, if any, held by it for payment to the Securityholders in trust for the benefit of the Securityholders entitled thereto until such sums shall be paid to such Securityholders. The Paying Agent shall return all unclaimed funds to the Institutional Trustee and upon removal of a Paying Agent such Paying Agent shall also return all funds in its possession to the Institutional Trustee. The provisions of Sections 8.01, 8.03 and 8.06 shall apply to the Institutional Trustee also in its role as Paying Agent, for so long as the Institutional Trustee shall act as Paying Agent and, to the extent applicable, to any other paying agent appointed hereunder. Any reference in this Agreement to the Paying Agent shall include any co-paying agent unless the context requires otherwise.

#### SECTION 5.10. Ownership of Common Securities by Sponsor

On the Issue Date, the Sponsor shall acquire, and thereafter retain, beneficial and record ownership of the Common Securities. To the fullest extent permitted by law, any attempted transfer of the Common Securities, except for transfers by operation of law or to an Affiliate of the Sponsor or a permitted successor under Article Ten of the Subordinated Indenture, shall be void. The Regular Trustees shall cause each Common Securities Certificate issued to the Sponsor to contain a legend stating "THIS CERTIFICATE IS NOT TRANSFERABLE EXCEPT AS PROVIDED IN THE DECLARATION OF TRUST REFERRED TO HEREIN".

#### SECTION 5.11. Book-Entry Preferred Securities Certificates; Common Securities Certificate

(a) The Preferred Securities Certificates, upon original issuance, will be issued in the form of a typewritten global Preferred Securities Certificate or Certificates representing Book-Entry Preferred Securities Certificates, to be delivered to The Depository Trust Company, the initial Clearing Agency, or its custodian, by or on behalf of, the Trust. Such Preferred Securities Certificate or Certificates shall initially be registered on the Securities Register in the name of Cede & Co., the nominee of the initial Clearing Agency, and no Owner will receive a definitive Preferred Securities Certificate representing such beneficial owner's interest in such Preferred Securities, except as provided in Section 5.13. Unless and until Definitive Preferred Securities Certificates have been issued to Owners pursuant to Section 5.13:

(i) the provisions of this Section 5.11(a) shall be in full force and effect;

(ii) the Securities Registrar and the Trustees shall be entitled to deal with the Clearing Agency for all purposes of this Declaration relating to the Book-Entry Preferred Securities Certificates (including the payment of principal



of and Distributions on the Book-Entry Preferred Securities and the giving of instructions or directions to Owners of Book-Entry Preferred Securities) as the sole Holder of Book-Entry Preferred Securities and shall have no obligations to the Owners thereof;

(iii) to the extent that the provisions of this Section conflict with any other provisions of this Declaration, the provisions of this Section shall control; and

(iv) the rights of the Owners of the Book-Entry Preferred Securities Certificates shall be exercised only through the Clearing Agency and shall be limited to those established by law and agreements between such Owners and the Clearing Agency and/or the Clearing Agency Participants. Pursuant to the Certificate Depository Agreement, unless and until Definitive Preferred Securities Certificates are issued pursuant to Section 5.13, the Clearing Agency will make book-entry transfers among the Clearing Agency Participants and receive and transmit payments on the Preferred Securities to such Clearing Agency Participants.

(v) The Clearing Agency will make book-entry transfers among the Clearing Agency Participants; provided, that solely for the purposes of determining whether the Holders of the requisite amount of Preferred Securities have voted on any matter provided for in this Declaration, so long as Definitive Preferred Securities Certificates have not been issued, the Trustees may conclusively rely on, and shall be fully protected in relying on, any written instrument (including a proxy) delivered to the Trustees by the Clearing Agency setting forth the Owners' votes or assigning the right to vote on any matter to any other Person either in whole or in part.

(b) A single Common Securities Certificate representing the Common Securities shall be issued to the Sponsor in the form of a definitive Common Securities Certificate.

#### SECTION 5.12. Notices to Clearing Agency

To the extent a notice or other communication to the Owners is required under this Declaration, unless and until Definitive Preferred Securities Certificates shall have been issued to Owners pursuant to Section 5.13, the Trustees shall give all such notices and communications specified herein to be given to Owners to the Clearing Agency, and shall have no obligations to the Owners.

#### SECTION 5.13. Definitive Preferred Securities Certificates

If (i) the Sponsor advises the Trustees in writing that the Clearing Agency is no longer willing or able to properly discharge its responsibilities with respect to the Preferred Securities Certificates, and the Sponsor is unable to locate a qualified successor within 90 days, or (ii) the Sponsor at its option advises the Trustees in writing that it elects to terminate the book-entry

system through the Clearing Agency, then the Regular Trustees shall notify the Clearing Agency and Holders of the Preferred Securities. Upon surrender to the Regular Trustees of the typewritten Preferred Securities Certificate or Certificates representing the Book-Entry Preferred Securities Certificates by the Clearing Agency, accompanied by registration instructions, the Regular Trustees or any one of them shall execute, and the Institutional Trustee shall authenticate, the Definitive Preferred Securities Certificates in accordance with the instructions of the Clearing Agency. Neither the Securities Registrar nor the Trustees shall be liable for any delay in delivery of such instructions and may conclusively rely on, and shall be protected in relying on, such instructions. Upon the issuance of Definitive Preferred Securities Certificates, the Trustees shall recognize the Holders of the Definitive Preferred Securities Certificates as Securityholders. The Definitive Preferred Securities Certificates shall be printed, lithographed or engraved or may be produced in any other manner as is reasonably acceptable to the Regular Trustees, as evidenced by the execution thereof by the Regular Trustees or any one of them.

#### SECTION 5.14. Rights of Securityholders

The legal title to the Trust Property is vested exclusively in the Institutional Trustee (in its capacity as such) in accordance with Section 2.09, and the Securityholders shall not have any right or title therein other than an undivided beneficial interest in the assets of the Trust conferred by their Trust Securities, and they shall have no right to call for any partition or division of property, profits or rights of the Trust except as described below. The Trust Securities shall be personal property giving only the rights specifically set forth therein and in this Declaration. The Trust Securities shall have no preemptive or other similar rights and when issued and delivered to Securityholders against payment of the purchase price therefor, except as otherwise provided in the Expense Agreement and Section 11.01 hereof, will be fully paid and nonassessable by the Trust. Except as otherwise provided in the Expense Agreement and Section 11.01 hereof, the Holders of the Trust Securities shall be entitled to the same limitation of personal liability extended to stockholders of private corporations for profit organized under the General Corporation Law of the State of Delaware.

### ARTICLE VI

#### ACTS OF SECURITYHOLDERS; MEETINGS; VOTING

##### SECTION 6.01. Limitations on Voting Rights

(a) Except as provided in this Section, in Section 2.10, in Section 8.10 or in Section 11.03 of this Declaration, in the Subordinated Indenture, and as otherwise required by law, no Holder of Preferred Securities shall have any right to vote or in any manner otherwise control the administration, operation and management of the Trust or the obligations of the parties hereto, nor shall anything herein set forth, or contained in the terms of the Trust Securities Certificates, be construed so as to constitute the Securityholders from time to time as partners or members of an association.

(b) So long as any Subordinated Debt Securities are held by the Institutional Trustee on behalf of the Trust, the Institutional Trustee shall not (i) direct the time, method and place of conducting any proceeding for any remedy available to the Indenture Trustee, or execute

any trust or power conferred on the Institutional Trustee with respect to such Subordinated Debt Securities; (ii) waive any past default that may be waived under Section 713 of the Subordinated Indenture; (iii) exercise any right to rescind or annul a declaration that the principal of all the Subordinated Debt Securities shall be due and payable; or (iv) consent to any amendment, modification or termination of the Subordinated Indenture or the Subordinated Debt Securities, where such consent shall be required, without, in each case, obtaining the prior approval of the Holders of at least a Majority in Liquidation Amount of the Preferred Securities; provided, however, that where a consent under the Subordinated Indenture would require the consent of each holder of Subordinated Debt Securities affected thereby, no such consent shall be given by the Institutional Trustee without the prior written consent of each Holder of Preferred Securities. The Institutional Trustee shall not revoke any action previously authorized or approved by a vote of the Holders of Preferred Securities, except by a subsequent vote of the Holders of Preferred Securities. Subject to Section 8.02, the Institutional Trustee shall notify all Holders of the Preferred Securities of any notice of default received with respect to the Subordinated Debt Securities. In addition to obtaining the foregoing approvals of the Holders of the Preferred Securities, prior to taking any of the foregoing actions, the Institutional Trustee shall, at the expense of the Sponsor, obtain an Opinion of Counsel experienced in such matters to the effect that such action will not cause the Trust to be taxable other than as a grantor trust for United States federal income tax purposes.

(c) If any proposed amendment to the Declaration provides for, or the Trust otherwise proposes to effect, (i) any action that would adversely affect in any material respect the interests, powers, preferences or special rights of the Preferred Securities, whether by way of amendment to the Declaration or otherwise, or (ii) the dissolution, winding-up or termination of the Trust, other than pursuant to the terms of this Declaration, then the Holders of Outstanding Trust Securities as a class will be entitled to vote on such amendment or proposal and such amendment or proposal shall not be effective except with the approval of the Holders of at least a Majority in Liquidation Amount of the Preferred Securities; except as otherwise provided in Section 11.03(c). Notwithstanding any other provision of this Declaration, no amendment to this Declaration may be made if, as a result of such amendment, it would cause the Trust to be taxable other than as a grantor trust for United States federal income tax purposes.

(d) Holders of a Majority in Liquidation Amount of the Preferred Securities may, on behalf of the Holders of all the Preferred Securities, waive any past Event of Default and its consequences, except a default described in clause (b) or (c) of the definition of "Event of Default" contained in Section 1.01, a default in respect of a covenant or provision which under this Declaration cannot be modified or amended without the consent of the Holder of each Outstanding Preferred Security or an Indenture Event of Default that the Holders of a Majority in Liquidation Amount of the Preferred Securities would not be entitled to waive pursuant to Section 6.01(e).

Upon any such waiver, any such Event of Default shall cease to exist, and any Event of Default arising therefrom shall be deemed to have been cured for every purpose of this Declaration; but no such waiver shall extend to any subsequent or other default or Event of Default or impair any right consequent thereon. Any waiver by the Holders of the Preferred Securities of an Event of Default with respect to Preferred Securities shall also be deemed to

constitute a waiver by the Holders of Common Securities for all purposes of the Declaration without any further act, vote or consent of the Holders of Common Securities.

(e) For so long as any Preferred Securities remain Outstanding, if, upon an Indenture Event of Default, the Indenture Trustee and the holders of the outstanding Subordinated Debt Securities have failed to declare the principal of all of the Subordinated Debt Securities to be immediately due and payable, the Holders of at least 33% in aggregate Liquidation Amount of the Preferred Securities then Outstanding shall have such right to make such declaration by a notice in writing to the Institutional Trustee, the Sponsor and the Indenture Trustee.

At any time after such a declaration of acceleration with respect to the Subordinated Debt Securities has been made and before a judgment or decree for payment of the money due has been obtained by the Indenture Trustee as provided in the Subordinated Indenture, the Holders of a Majority in Liquidation Amount of the Preferred Securities, by written notice to the Institutional Trustee, the Sponsor and the Indenture Trustee, may rescind and annul such declaration and its consequences if:

(i) the Sponsor has paid or deposited with the Indenture Trustee a sum sufficient to pay

(1) all overdue installments of interest on all of the Subordinated Debt Securities,

(2) the principal of any Subordinated Debt Securities which have become due otherwise than by such declaration of acceleration and interest thereon at the rate borne by the Subordinated Debt Securities, and

(3) all sums paid or advanced by the Indenture Trustee under the Subordinated Indenture and the reasonable compensation, expenses, disbursements and advances of the Indenture Trustee and the Institutional Trustee, their agents and counsel; and

(ii) all Indenture Events of Default, other than the non-payment of the principal of the Subordinated Debt Securities which has become due solely by such acceleration, have been cured or waived as provided in Section 713 of the Subordinated Indenture.

The Holders of at least a Majority in Liquidation Amount of the Preferred Securities may, on behalf of the Holders of all the Preferred Securities, waive any past default under the Subordinated Indenture, except a default in the payment of principal or interest (unless such default has been cured and a sum sufficient to pay all matured installments of interest and principal due otherwise than by acceleration has been deposited with the Indenture Trustee) or a default in respect of a covenant or provision which under the Subordinated Indenture cannot be modified or amended without the consent of the holder of each outstanding Subordinated Debt Securities. No such rescission shall affect any subsequent default or impair any right consequent thereon.

Upon receipt by the Institutional Trustee of written notice declaring such an acceleration, or rescission and annulment thereof, by Holders of the Preferred Securities all or part of which is represented by Book-Entry Preferred Securities Certificates, a record date shall be established for determining Holders of Outstanding Preferred Securities entitled to join in such notice, which record date shall be at the close of business on the day the Institutional Trustee receives such notice. The Holders on such record date, or their duly designated proxies, and only such Persons, shall be entitled to join in such notice, whether or not such Holders remain Holders after such record date; provided, that, unless such declaration of acceleration, or rescission and annulment, as the case may be, shall have become effective by virtue of the requisite percentage having joined in such notice prior to the day which is 90 days after such record date, such notice of declaration of acceleration, or rescission and annulment, as the case may be, shall automatically and without further action by any Holder be canceled and of no further effect. Nothing in this paragraph shall prevent a Holder, or a proxy of a Holder, from giving, after expiration of such 90-day period, a new written notice of declaration of acceleration, or rescission and annulment thereof, as the case may be, that is identical to a written notice which has been canceled pursuant to the proviso to the preceding sentence, in which event a new record date shall be established pursuant to the provisions of this Section 6.01(e).

(f) Except as set forth in Section 6.01(e) and Section 8.19, the Holders of Preferred Securities shall have no right to exercise directly any right or remedy available to the holders of, or in respect of, the Subordinated Debt Securities.

The Holders of a Majority in Liquidation Amount of the Preferred Securities at the time Outstanding shall have the right to direct the time, method and place of conducting any proceeding for any remedy available to the Institutional Trustee, or exercising any trust or power conferred on the Institutional Trustee with respect to the Preferred Securities; provided, however, that, the Institutional Trustee shall have the right to decline to follow any such direction if the Institutional Trustee being advised by counsel determines that the action so directed may not lawfully be taken, or if the Institutional Trustee in good faith shall determine that the proceedings so directed would be illegal or involve it in personal liability or be unduly prejudicial to the rights of Holders of Preferred Securities not parties to such direction, and provided further that nothing in this Declaration shall impair the right of the Institutional Trustee to take any action deemed proper by the Institutional Trustee and which is not inconsistent with such direction by such Holders.

#### SECTION 6.02. Notice of Meetings

Notice of all meetings of the Holders of Preferred Securities, stating the time, place and purpose of the meeting, shall be given by the Regular Trustees pursuant to Section 11.08 to each Holder of Preferred Securities of record, at his registered address, at least 15 days and not more than 90 days before the meeting. At any such meeting, any business properly before the meeting may be so considered whether or not stated in the notice of the meeting. Any adjourned meeting may be held as adjourned without further notice.

#### SECTION 6.03. Meetings of Holders of Preferred Securities

No annual meeting of Securityholders is required to be held. The Regular Trustees, however, shall call a meeting of Securityholders to vote on any matter upon the written request of the Holders of Preferred Securities of record of at least 33% of the Preferred Securities (based upon their Liquidation Amount) and the Regular Trustees or the Institutional Trustee may, at any time in their discretion, call a meeting of Holders of Preferred Securities to vote on any matters as to which Holders of Preferred Securities are entitled to vote.

Holders of Preferred Securities of record of at least 50% of the Preferred Securities (based upon their Liquidation Amount), present in person or by proxy, shall constitute a quorum at any meeting of Holders of Preferred Securities.

If a quorum is present at a meeting, an affirmative vote by the Holders of Preferred Securities of record present, in person or by proxy, holding more than 66-2/3% of the Preferred Securities (based upon their Liquidation Amount) held by the Holders of Preferred Securities of record present, either in person or by proxy, at such meeting shall constitute the action of the Securityholders, unless this Declaration requires a greater number of affirmative votes.

#### SECTION 6.04. Voting Rights

Securityholders shall be entitled to one vote for each \$1,000 of Liquidation Amount represented by their Trust Securities in respect of any matter as to which such Securityholders are entitled to vote; provided, however, any Preferred Securities that are owned by the Company, the Institutional Trustee or the Delaware Trustee will, for purposes of any vote or consent, be treated as if they were not outstanding.

#### SECTION 6.05. Proxies, etc.

At any meeting of Securityholders, any Securityholder entitled to vote may vote by proxy, provided that no proxy shall be voted at any meeting unless it shall have been placed on file with the Regular Trustees, or with such other officer or agent of the Trust as the Regular Trustees may direct, for verification prior to the time at which such vote shall be taken. Pursuant to a resolution of the Institutional Trustee, proxies may be solicited in the name of the Institutional Trustee or one or more officers of the Institutional Trustee. Only Securityholders of record shall be entitled to vote. When Trust Securities are held jointly by several Persons, any one of them may vote at any meeting in person or by proxy in respect of such Trust Securities, but if more than one of them shall be present at such meeting in person or by proxy, and such joint owners or their proxies so present disagree as to any vote to be cast, such vote shall not be received in respect of such Trust Securities. A proxy purporting to be executed by or on behalf of a Securityholder shall be deemed valid unless challenged at or prior to its exercise, and the burden of proving invalidity shall rest on the challenger. No proxy shall be valid more than three years after its date of execution.

#### SECTION 6.06. Securityholder Action by Written Consent

Any action which may be taken by Securityholders at a meeting may be taken without a meeting and without prior notice if Securityholders holding at least 66-2/3% of all outstanding

Trust Securities entitled to vote in respect of such action (or such other proportion thereof as shall be required by any express provision of this Declaration) shall consent to the action in writing (based upon their Liquidation Amount).

#### SECTION 6.07. Record Date for Voting and Other Purposes

For the purposes of determining the Securityholders who are entitled to notice of and to vote at any meeting or by written consent, or to participate in any Distribution on the Trust Securities in respect of which a record date is not otherwise provided for in this Declaration, or for the purpose of any other action, the Regular Trustees may from time to time fix a date, not more than 90 days prior to the date of any meeting of Securityholders or the payment of Distribution or other action, as the case may be, as a record date for the determination of the identity of the Securityholders of record for such purposes.

#### SECTION 6.08. Acts of Securityholders

Any request, demand, authorization, direction, notice, consent, waiver or other action provided or permitted by this Declaration to be given, made or taken by Securityholders may be embodied in and evidenced by one or more instruments of substantially similar tenor signed by such Securityholders in person or by an agent appointed in writing; and, except as otherwise expressly provided herein, such action shall become effective when such instrument or instruments are delivered to the Regular Trustees. Such instrument or instruments (and the action embodied therein and evidenced thereby) are herein sometimes referred to as the "Act" of the Securityholders signing such instrument or instruments. Proof of execution of any such instrument or of a writing appointing any such agent shall be sufficient for any purpose of this Declaration and (subject to Section 8.01) conclusive in favor of the Trustees, if made in the manner provided in this Section.

The fact and date of the execution by any Person of any such instrument or writing may be proved by the affidavit of a witness of such execution or by a certificate of a notary public or other officer authorized by law to take acknowledgments of deeds, certifying that the individual signing such instrument or writing acknowledged to him the execution thereof. Where such execution is by a signer acting in a capacity other than his individual capacity, such certificate or affidavit shall also constitute sufficient proof of his authority. The fact and date of the execution of any such instrument or writing, or the authority of the Person executing the same, may also be proved in any other manner which the Trustees deem sufficient.

The ownership of Preferred Securities shall be proved by the Securities Register. Any request, demand, authorization, direction, notice, consent, waiver or other Act of the Securityholder of any Trust Security shall bind every future Securityholder of the same Trust Security and the Securityholder of every Trust Security issued upon the registration of transfer thereof or in exchange therefor or in lieu thereof in respect of anything done, omitted or suffered to be done by the Trustees or the Trust in reliance thereon, whether or not notation of such action is made upon such Trust Security.

Without limiting the foregoing, a Securityholder entitled hereunder to take any action hereunder with regard to any particular Trust Security may do so with regard to all or any part of

the Liquidation Amount of such Trust Security or by one or more duly appointed agents each of which may do so pursuant to such appointment with regard to all or any part of such Liquidation Amount.

If any dispute shall arise between the Securityholders and the Trustees with respect to the authenticity, validity or binding nature of any request, demand, authorization, direction, consent, waiver or other Act of such Securityholder or Trustee under this Article VI, then the determination of such matter by the Institutional Trustee shall be conclusive with respect to such matter.

#### SECTION 6.09. Inspection of Records

Upon reasonable notice to the Trustees, the records of the Trust shall be open to inspection by Securityholders during normal business hours for any purpose reasonably related to such Securityholder's interest as a Securityholder.

### ARTICLE VII

#### REPRESENTATIONS AND WARRANTIES OF THE TRUSTEES

##### SECTION 7.01. Representations and Warranties of the Trustees

The Bank, the Delaware Bank, the Institutional Trustee and the Delaware Trustee, each on behalf of and as to itself, hereby represents and warrants for the benefit of the Sponsor and the Securityholders that:

(a) the Bank is a national banking association or trust company duly organized, validly existing and in good standing under the laws of the United States of America, and the Delaware Bank is a banking corporation or trust company, duly organized, validly existing and in good standing under the laws of the State of Delaware;

(b) each of the Bank and the Delaware Bank has full corporate power, authority and legal right to execute, deliver and perform their obligations under this Declaration and has taken all necessary action to authorize the execution, delivery and performance by it of this Declaration;

(c) this Declaration has been duly authorized, executed and delivered by each of the Bank and the Delaware Bank and constitutes the valid and legally binding agreement of each of the Bank and the Delaware Bank, enforceable against it in accordance with its terms, subject to bankruptcy, insolvency, fraudulent transfer, reorganization, moratorium and similar laws of general applicability relating to or affecting creditors' rights and to general equity principles;

(d) the execution, delivery and performance by each of the Bank and the Delaware Bank of this Declaration have been duly authorized by all necessary corporate action on the part of the Bank, the Institutional Trustee, the Delaware Bank and the Delaware Trustee and do not require any approval of stockholders of the Bank or the Delaware Bank and such execution, delivery and performance will not (i) violate the Bank's or the Delaware Bank's



Charter or By-laws, or (ii) violate any law, governmental rule or regulation of the United States or the State of New York or Delaware, as the case may be, governing the banking or trust powers of the Bank and the Institutional Trustee or the Delaware Bank and the Delaware Trustee, or any order, judgment or decree applicable to the Bank, the Institutional Trustee, the Delaware Bank or the Delaware Trustee; and

(e) neither the authorization, execution or delivery by the Bank or the Delaware Bank of this Declaration, nor the consummation of any of the transactions by the Bank, the Institutional Trustee, the Delaware Bank or the Delaware Trustee (as appropriate in context) contemplated herein or therein, require the consent or approval of, the giving of notice to, the registration with or the taking of any other action with respect to any governmental authority or agency under any existing federal, New York or Delaware law governing the banking or trust powers of the Bank or the Delaware Bank.

#### ARTICLE VIII

#### THE TRUSTEES

#### SECTION 8.01. Certain Duties and Responsibilities

(a) The rights, duties and responsibilities of the Trustees shall be as provided by this Declaration and, in the case of the Institutional Trustee, the Trust Indenture Act. The Institutional Trustee, other than during the occurrence and continuation of an Event of Default, undertakes to perform only such duties as are specifically set forth in this Declaration and, upon an Event of Default, must exercise the same degree of care and skill as a prudent person would exercise or use in the conduct of his/her own affairs. The Trustees shall have all the privileges, rights and immunities provided by the Delaware Statutory Trust Act. Notwithstanding the foregoing, no provision of this Declaration shall require the Trustees to expend or risk their own funds or otherwise incur any financial liability in the performance of any of their duties hereunder, or in the exercise of any of their rights or powers, if they shall have reasonable grounds for believing that repayment of such funds or adequate indemnity against such risk or liability is not reasonably assured to them. Whether or not therein expressly so provided, every provision of this Declaration relating to the conduct or affecting the liability of or affording protection to the Trustees shall be subject to the provisions of this Section. To the extent that, at law or in equity, each Trustee has duties (including fiduciary duties) and liabilities relating thereto to the Trust or to the Securityholders, each Trustee shall not be liable to the Trust or to any Securityholder for such Trustee's good faith reliance on the provisions of this Declaration. The provisions of this Declaration, to the extent that they restrict the duties and liabilities of each Trustee otherwise existing at law or in equity, are agreed by the Sponsor and the Securityholders to replace such other duties and liabilities of such Trustee.

(b) All payments made by the Institutional Trustee in respect of the Trust Securities shall be made only from the income and proceeds from the Trust Property and only to the extent that there shall be sufficient income or proceeds from the Trust Property to enable the Institutional Trustee to make payments in accordance with the terms hereof. Each Securityholder, by its acceptance of a Trust Security, agrees that it will look solely to the income and proceeds from the Trust Property to the extent available for distribution to it as herein

provided and that the Trustees are not personally liable to it for any amount distributable in respect of any Trust Security or for any other liability in respect of any Trust Security. This Section 8.01(b) does not limit the liability of the Trustees expressly set forth elsewhere in this Declaration or, in the case of the Institutional Trustee, in the Trust Indenture Act.

#### SECTION 8.02. Notice of Defaults

Within 90 days after the occurrence of any default known to the Institutional Trustee, the Institutional Trustee shall transmit, in the manner and to the extent provided in Section 11.08, notice of default to the Securityholders, the Regular Trustees and the Sponsor, unless such default shall have been cured or waived before the giving of such notice, provided that the Institutional Trustee shall be protected in withholding such notice if and so long as the board of directors, the executive committee, or a trust committee of directors and/or responsible officers of the Institutional Trustee in good faith determines that the withholding of such notice is in the interests of the Securityholders. For the purpose of this Section, the term "default" means any event which is, or after notice or lapse of time or both would become, an Event of Default.

#### SECTION 8.03. Certain Rights of Institutional Trustee

Subject to the provisions of Section 8.01 and except as provided by law:

(a) the Institutional Trustee may rely and shall be protected in acting or refraining from acting in good faith upon any resolution, Opinion of Counsel, certificate, written representation of a Holder or transferee, certificate of auditors or any other certificate, statement, instrument, opinion, report, notice, request, consent, order, appraisal, bond or other paper or document believed by it to be genuine and to have been signed or presented by the proper party or parties;

(b) if (i) in performing its duties under this Declaration the Institutional Trustee is required to decide between alternative courses of action, or (ii) in construing any of the provisions in this Declaration the Institutional Trustee finds the same ambiguous or inconsistent with any other provisions contained herein, or (iii) the Institutional Trustee is unsure of the application of any provision of this Declaration, then, except as to any matter as to which the Holders of Preferred Securities are entitled to vote under the terms of this Declaration, the Institutional Trustee shall deliver a notice to the Sponsor requesting written instructions of the Sponsor as to the course of action to be taken. The Institutional Trustee shall take such action, or refrain from taking such action, as the Institutional Trustee shall be instructed in writing to take, or to refrain from taking, by the Sponsor; provided, however, that if the Institutional Trustee does not receive such instructions of the Sponsor within ten Business Days after it has delivered such notice, or such reasonably shorter period of time set forth in such notice (which to the extent practicable shall not be less than two Business Days), it may, but shall be under no duty to, take or refrain from taking such action not inconsistent with this Declaration as it shall deem advisable and in the best interests of the Securityholders, in which event the Institutional Trustee shall have no liability except for its own bad faith, negligence or willful misconduct;

(c) the Institutional Trustee may consult with counsel or other experts of its selection and the written advice of such counsel or other experts or any Opinion of Counsel shall

be full and complete authorization and protection in respect of any action taken, suffered or omitted by it hereunder in good faith and in reliance thereon;

(d) the Institutional Trustee shall be under no obligation to exercise any of the rights or powers vested in it by this Declaration at the request or direction of any of the Securityholders pursuant to this Declaration, unless such Securityholders shall have offered to the Institutional Trustee reasonable security or indemnity against the costs, expenses and liabilities which might be incurred by it in compliance with such request or direction;

(e) the Institutional Trustee shall not be bound to make any investigation into the facts or matters stated in any resolution, certificate, statement, instrument, opinion, report, notice, request, consent, order, approval, bond or other document, but the Institutional Trustee, in its discretion, may make such further inquiry or investigation into such facts or matters as it may see fit;

(f) the Institutional Trustee may execute any of the trusts or powers hereunder or perform any duties hereunder either directly or by or through its agents or attorneys; provided that the Institutional Trustee shall be responsible for its own negligence or recklessness with respect to selection of any agent or attorney appointed by it hereunder;

(g) the Institutional Trustee shall not be liable for any action taken, suffered, or omitted to be taken by it in good faith and reasonably believed by it to be authorized or within the discretion or rights or powers conferred upon it by this Declaration;

(h) the Institutional Trustee shall not be deemed to have notice of any default or Event of Default unless an officer of the Institutional Trustee assigned to its Corporate Trust Division has actual knowledge thereof or unless written notice of any event which is in fact such a default is received by the Institutional Trustee at its corporate trust office, and such notice references the Trust Securities and this Declaration; and

(i) the rights, privileges, protections, immunities and benefits given to the Institutional Trustee, including, without limitation, its right to be indemnified, are extended to, and shall be enforceable by, the Institutional Trustee in each of its respective capacities hereunder, and to each agent, custodian and other Person employed to act hereunder.

#### SECTION 8.04. Not Responsible for Recitals or Issuance of Securities

The recitals contained herein and in the Trust Securities Certificates shall be taken as the statements of the Trust, and the Trustees do not assume any responsibility for their correctness. The Trustees shall not be accountable for the use or application by the Trust of the proceeds of the Trust Securities in accordance with Section 2.05.

The Institutional Trustee may conclusively assume that any funds held by it hereunder are legally available unless an officer of the Institutional Trustee assigned to its Institutional Trust Services Department shall have received written notice from the Company, any Holder or any other Trustee that such funds are not legally available.

The Institutional Trustee makes no representations as to the value or condition of the property of the Trust or any part thereof. The Institutional Trustee makes no representations as to the validity or sufficiency of this Declaration or the Trust Securities.

#### SECTION 8.05. May Hold Securities

Any Trustee or any other agent of the Trustees or the Trust, in its individual or any other capacity, and except as provided in the definition of the term "Outstanding" in Article I, may become the owner or pledgee of Trust Securities and may otherwise deal with the Trust with the same rights it would have if it were not a Trustee or such other agent.

#### SECTION 8.06. Compensation; Fees; Indemnity

The Sponsor, as obligor of the Subordinated Debt Securities, agrees:

(a) to pay to the Trustees from time to time reasonable compensation for all services rendered by the Trustees hereunder (which compensation shall not be limited by any provision of law in regard to the compensation of a trustee of an express trust);

(b) except as otherwise expressly provided herein, to reimburse the Trustees upon request for all reasonable expenses, disbursements and advances incurred or made by the Trustees in accordance with any provision of this Declaration (including the reasonable compensation and the expenses and disbursements of their agents and counsel), except any such expense, disbursement or advance as may be attributable to their willful misconduct, negligence or bad faith (or, in the case of the Delaware Trustee, any such expense, disbursement or advance as shall have been caused by his/her own gross negligence); and

(c) to indemnify each of the Trustees for, and to hold each of the Trustees harmless against, any and all loss, damage, claims, liability or expense incurred without willful misconduct, negligence (gross negligence, in the case of the Delaware Trustee) or bad faith on their part, arising out of or in connection with the acceptance or administration of this Declaration, including the costs and expenses of defending themselves against any claim (whether by the Sponsor, any Securityholder or any other person) or liability in connection with the exercise or performance of any of their powers or duties hereunder.

The provisions of this Section 8.06 shall survive the termination of this Declaration.

#### SECTION 8.07. Trustees Required; Eligibility

(a) There shall at all times be an Institutional Trustee hereunder with respect to the Trust Securities. The Institutional Trustee shall be a Person that has a combined capital and surplus of at least \$50,000,000. If any such Person publishes reports of condition at least annually, pursuant to law or to the requirements of its supervising or examining authority, then for the purposes of this Section, the combined capital and surplus of such Person shall be deemed to be its combined capital and surplus as set forth in its most recent report of condition so published. If at any time the Institutional Trustee with respect to the Trust Securities shall cease to be eligible in accordance with the provisions of this Section, it shall resign immediately in the manner and with the effect hereinafter specified in this Article.

(b) There shall at all times be one or more Regular Trustees hereunder with respect to the Trust Securities. Each Regular Trustee shall be either a natural person who is at least 21 years of age or a legal entity that shall act through one or more persons authorized to bind such entity.

(c) There shall at all times be a Delaware Trustee with respect to the Trust Securities. The Delaware Trustee shall either be (i) a natural person who is at least 21 years of age and a resident of the State of Delaware or (ii) a legal entity authorized to conduct a trust business and with its principal place of business in the State of Delaware that shall act through one or more persons authorized to bind such entity.

#### SECTION 8.08. Conflicting Interests

If the Institutional Trustee has or shall acquire a conflicting interest within the meaning of the Trust Indenture Act, the Institutional Trustee shall either eliminate such interest or resign, to the extent and in the manner provided by, and subject to the provisions of, the Trust Indenture Act and this Declaration. To the extent permitted by the Trust Indenture Act, the Institutional Trustee shall not be deemed to have a conflicting interest by virtue of being trustee under the Guarantee.

#### SECTION 8.09. Co-Trustees and Separate Trustee

At any time or times, for the purpose of meeting the legal requirements of the Trust Indenture Act or of any jurisdiction in which any part of the Trust Property may at the time be located, the Holder of the Common Securities and the Institutional Trustee shall have power to appoint, and upon the written request of the Institutional Trustee, the Sponsor shall for such purpose join with the Institutional Trustee in the execution, delivery and performance of all instruments and agreements necessary or proper to appoint, one or more Persons approved by the Institutional Trustee either to act as co-trustee, jointly with the Institutional Trustee, of all or any part of such Trust Property, or to act as separate trustee of any such Trust Property, in either case with such powers as may be provided in the instrument of appointment, and to vest in such Person or Persons in the capacity aforesaid, any property, title, right or power deemed necessary or desirable, subject to the other provisions of this Section. If the Sponsor does not join in such appointment within 15 days after the receipt by it of a request so to do, or in case an Indenture Event of Default has occurred and is continuing, the Institutional Trustee alone shall have power to make such appointment. Any co-trustee or separate trustee appointed pursuant to this Section shall satisfy the requirements of Section 8.07.

Should any written instrument from the Sponsor be required by any co-trustee or separate trustee so appointed for more fully confirming to such co-trustee or separate trustee such property, title, right, or power, any and all such instruments shall, on request, be executed, acknowledged, and delivered by the Sponsor.

Every co-trustee or separate trustee shall, to the extent permitted by law, but to such extent only, be appointed subject to the following terms, namely:

(i) The Trust Securities shall be executed, authenticated and delivered and all rights, powers, duties, and obligations hereunder in respect of the custody of securities, cash and other personal property held by, or required to be deposited or pledged with, the Trustees hereunder, shall be exercised, solely by the Trustees.

(ii) The rights, powers, duties, and obligations hereby conferred or imposed upon the Institutional Trustee in respect of any property covered by such appointment shall be conferred or imposed upon and exercised or performed by the Institutional Trustee or by the Institutional Trustee and such co-trustee or separate trustee jointly, as shall be provided in the instrument appointing such co-trustee or separate trustee, except to the extent that under any law of any jurisdiction in which any particular act is to be performed, the Institutional Trustee shall be incompetent or unqualified to perform such act, in which event such rights, powers, duties, and obligations shall be exercised and performed by such co-trustee or separate trustee.

(iii) The Institutional Trustee, at any time, by an instrument in writing executed by it, with the written concurrence of the Sponsor, may accept the resignation of or remove any co-trustee or separate trustee appointed under this Section, and, in case an Indenture Event of Default has occurred and is continuing, the Institutional Trustee shall have power to accept the resignation of, or remove, any such co-trustee or separate trustee without the concurrence of the Sponsor. Upon the written request of the Institutional Trustee, the Sponsor shall join with the Institutional Trustee in the execution, delivery, and performance of all instruments and agreements necessary or proper to effectuate such resignation or removal. A successor to any co-trustee or separate trustee so resigned or removed may be appointed in the manner provided in this Section.

(iv) No co-trustee or separate trustee hereunder shall be personally liable by reason of any act or omission of the Institutional Trustee, or any other such trustee hereunder.

(v) The Trustees shall not be liable by reason of any act of a co-trustee or separate trustee.

(vi) Any Act of Holders delivered to the Institutional Trustee shall be deemed to have been delivered to each such co-trustee and separate trustee.

#### SECTION 8.10. Resignation and Removal; Appointment of Successor

No resignation or removal of any Trustee (the "Relevant Trustee") and no appointment of a successor Relevant Trustee pursuant to this Article shall become effective until the acceptance of appointment by the successor Relevant Trustee in accordance with the applicable requirements of Section 8.11.

The Relevant Trustee may resign at any time by giving written notice thereof to the Securityholders, the Sponsor and the other Trustees, except that notice is only required to be

delivered to the Securityholders in the event that the Institutional Trustee or the Delaware Trustee is the resigning Relevant Trustee. If the instrument of acceptance by a successor Relevant Trustee required by Section 8.11 shall not have been delivered to the resigning Relevant Trustee within 30 days after the giving of such notice of resignation, the resigning Relevant Trustee may petition any court of competent jurisdiction for the appointment of a successor Relevant Trustee.

Unless an Indenture Event of Default shall have occurred and be continuing, the Relevant Trustee may be removed at any time by Act of the Holder of the Common Securities. If an Indenture Event of Default shall have occurred and be continuing, the Relevant Trustee may be removed at such time by Act of the Securityholders of a Majority in Liquidation Amount of the Preferred Securities, delivered to the Relevant Trustee (in its individual capacity and on behalf of the Trust).

If the Relevant Trustee shall resign, be removed or become incapable of continuing to act as Trustee at a time when no Indenture Event of Default shall have occurred and be continuing, the Holder of the Common Securities, by Act of the Holder of the Common Securities delivered to the retiring and successor Relevant Trustees, shall promptly appoint a successor Relevant Trustee or Trustees, and the retiring Relevant Trustee shall comply with the applicable requirements of Section 8.11. If the Relevant Trustee shall resign, be removed or become incapable of continuing to act as the Relevant Trustee at a time when an Indenture Event of Default shall have occurred and be continuing, the Holders of Preferred Securities, by Act of the Securityholders of a Majority in Liquidation Amount of the Preferred Securities then outstanding delivered to the retiring and successor Relevant Trustee, shall promptly appoint a successor Relevant Trustee or Trustees, and the Relevant Trustee shall comply with the applicable requirements of Section 8.11. If no successor Relevant Trustee shall have been so appointed in accordance with this Section 8.10 and accepted appointment in the manner required by Section 8.11, any Securityholder who has been a Securityholder of Trust Securities for at least six months may, on behalf of himself and all others similarly situated, petition any court of competent jurisdiction for the appointment of a successor Relevant Trustee.

The Institutional Trustee shall give notice of each resignation and each removal of the Relevant Trustee, and each appointment of a successor Trustee to all Securityholders in the manner provided in Section 11.08 and shall give notice to the Sponsor, except that notice is only required to be delivered to the Securityholders in the event that the Institutional Trustee or the Delaware Trustee is the resigning or removed Relevant Trustee. Each notice shall include the name of the successor Relevant Trustee and the address of its corporate trust office if it is the Institutional Trustee.

Notwithstanding the foregoing or any other provision of this Declaration, in the event any Regular Trustee or a Delaware Trustee who is a natural person dies or becomes incompetent or incapacitated, the vacancy created by such death, incompetence or incapacity may be filled by (i) the act of the remaining Regular Trustee or (ii) otherwise by the Sponsor (with the successor in each case being an individual who satisfies the eligibility requirement for Regular Trustees set forth in Section 8.07). Additionally, notwithstanding the foregoing or any other provision of this Declaration, in the event the Sponsor believes that any Regular Trustee has become incompetent or incapacitated, the Sponsor, by notice to the remaining Trustees, may terminate the status of

such Person as an Regular Trustee (in which case the vacancy so created will be filled in accordance with the preceding sentence).

#### SECTION 8.11. Acceptance of Appointment by Successor

In case of the appointment hereunder of a successor Relevant Trustee, every such successor Relevant Trustee so appointed shall execute, acknowledge and deliver to the Trust and to the retiring Relevant Trustee an instrument accepting such appointment, and thereupon the resignation or removal of the retiring Relevant Trustee shall become effective and such successor Relevant Trustee, without any further act, deed or conveyance, shall become vested with all the rights, powers, trusts and duties of the retiring Relevant Trustee; but, on the request of the Sponsor or the successor Relevant Trustee, such retiring Relevant Trustee shall, upon payment of its charges, execute and deliver an instrument transferring to such successor Relevant Trustee all the rights, powers and trusts of the retiring Relevant Trustee and shall duly assign, transfer and deliver to such successor Relevant Trustee all property and money held by such retiring Relevant Trustee hereunder.

Upon request of any such successor Relevant Trustee, the retiring Relevant Trustee shall execute any and all instruments for more fully and certainly vesting in and confirming to such successor Relevant Trustee all such rights, powers and trusts referred to in the preceding paragraph.

No successor Relevant Trustee shall accept its appointment unless at the time of such acceptance such successor Relevant Trustee shall be qualified and eligible under this Article.

#### SECTION 8.12. Merger, Conversion, Consolidation or Succession to Business

Any Person into which the Institutional Trustee, Delaware Trustee or any Regular Trustee which is not a natural person may be merged or converted or with which it may be consolidated, or any Person resulting from any merger, conversion or consolidation to which such Relevant Trustee shall be a party, or any Person succeeding to all or substantially all the corporate trust business of such Relevant Trustee, shall be the successor of such Relevant Trustee hereunder; provided such Person shall be otherwise qualified and eligible under this Article, without the execution or filing of any paper or any further act on the part of any of the parties hereto.

#### SECTION 8.13. Preferential Collection of Claims Against Sponsor or Trust

If and when the Institutional Trustee shall be or become a creditor of the Sponsor or the Trust (or any other obligor upon the Subordinated Debt Securities or the Trust Securities), the Institutional Trustee shall be subject to the provisions of the Trust Indenture Act regarding the collection of claims against the Sponsor or Trust (or any such other obligor). For purposes of Section 311(b)(4) and (6) of the Trust Indenture Act:

(a) "cash transaction" means any transaction in which full payment for goods or securities sold is made within seven days after delivery of the goods or securities in currency or in checks or other orders drawn upon banks or bankers and payable upon demand; and



(b) "self-liquidating paper" means any draft, bill of exchange, acceptance or obligation which is made, drawn, negotiated or incurred by the Sponsor or the Trust (or any such obligor) for the purpose of financing the purchase, processing, manufacturing, shipment, storage or sale of goods, wares or merchandise and which is secured by documents evidencing title to, possession of, or a lien upon, the goods, wares or merchandise or the receivables or proceeds arising from the sale of the goods, wares or merchandise previously constituting the security; provided the security is received by the Institutional Trustee simultaneously with the creation of the creditor relationship with the Sponsor or the Trust (or any such obligor) arising from the making, drawing, negotiating or incurring of the draft, bill of exchange, acceptance or obligation.

#### SECTION 8.14. Reports by Institutional Trustee

(a) Within 60 days after May 15 of each year commencing with May 15, 2004, if required by Section 313(a) of the Trust Indenture Act, the Institutional Trustee shall transmit a brief report dated as of such May 15 with respect to any of the events specified in such Section 313(a) that may have occurred since the later of the date of this Declaration or the preceding May 15.

(b) The Institutional Trustee shall transmit to Securityholders the reports required by Section 313(b) of the Trust Indenture Act at the times specified therein.

(c) Reports pursuant to this Section shall be transmitted in the manner and to the Persons required by Sections 313(c) and (d) of the Trust Indenture Act.

#### SECTION 8.15. Reports to the Institutional Trustee

The Sponsor and the Regular Trustees on behalf of the Trust shall provide to the Institutional Trustee such documents, reports and information as required by Section 314 of the Trust Indenture Act (if any) and, within 120 days after the end of each fiscal year of the Sponsor, the compliance certificate required by Section 314(a)(4) of the Trust Indenture Act in the form and in the manner required by Section 314 of the Trust Indenture Act.

Delivery of such reports, information and documents to the Institutional Trustee is for informational purposes only and the Institutional Trustee's receipt of such shall not constitute constructive notice of any information contained therein or determinable from information contained therein.

#### SECTION 8.16. Evidence of Compliance with Conditions Precedent

Each of the Sponsor and the Regular Trustees on behalf of the Trust shall provide to the Institutional Trustee such evidence of compliance with any conditions precedent, if any, provided for in this Declaration, including an Officers' Certificate and an Opinion of Counsel that relate to any of the matters set forth in Section 314(c) of the Trust Indenture Act. Any certificate or opinion required to be given pursuant to Section 314(c) of the Trust Indenture Act shall comply with Section 314(e) of the Trust Indenture Act.

SECTION 8.17. Number of Trustees

(a) The number of Trustees shall initially be four; provided that the Sponsor by written instrument may increase or decrease the number of Regular Trustees.

(b) If a Trustee ceases to hold office for any reason and the number of Regular Trustees is not reduced pursuant to Section 8.17(a), or if the number of Trustees is increased pursuant to Section 8.17(a), a vacancy shall occur. The vacancy shall be filled with a Trustee appointed in accordance with Section 8.10.

(c) Except as provided in Section 9.02, the death, resignation, retirement, removal, bankruptcy, incompetence or incapacity to perform the duties of a Trustee shall not operate to annul, dissolve or terminate the Trust. Whenever a vacancy in the number of Regular Trustees shall occur, until such vacancy is filled by the appointment of an Regular Trustee in accordance with Section 8.10, the Regular Trustees in office, regardless of their number (and notwithstanding any other provision of this Declaration), shall have all powers granted to the Regular Trustees and shall discharge the duties imposed upon the Regular Trustees by this Declaration.

SECTION 8.18. Delegation of Power

(a) Any Regular Trustee may, by power of attorney consistent with applicable law, delegate to any other natural person over the age of 21 his or her power for the purpose of executing any documents contemplated in Section 2.07(a), including any registration statement or amendment thereto filed with the Commission, or making any other governmental filing; and

(b) The Regular Trustees shall have power to delegate from time to time to such of their number the doing of such things and the execution of such instruments either in the name of the Trust or the names of the Regular Trustees or otherwise as the Regular Trustees may deem expedient, to the extent such delegation is not prohibited by applicable law or contrary to the provisions of the Trust, as set forth herein.

SECTION 8.19. Enforcement of Rights of Institutional Trustee by Securityholders

If (i) the Trust fails to pay Distributions in full on the Preferred Securities for more than five consecutive years at any one time, or (ii) an Event of Default occurs and is continuing, then the Institutional Trustee may enforce its rights against the Company as the holder of the Subordinated Debt Securities. In addition, the Holders of a majority in aggregate Liquidation Amount of the Preferred Securities will have the right to direct the time, method, and place of conducting any proceeding for any remedy available to the Institutional Trustee or to direct the exercise of any trust or power conferred upon the Institutional Trustee under this Declaration, including the right to direct the Institutional Trustee to exercise the remedies available to it as a holder of the Subordinated Debt Securities; provided that such direction shall not be in conflict with any rule of law or with this Declaration, and could not involve the Institutional Trustee in personal liability in circumstances where reasonable indemnity would not be adequate. If the Institutional Trustee fails to enforce its rights under the Subordinated Debt Securities, a Holder of Preferred Securities may, to the fullest extent permitted by applicable law, institute a legal

proceeding against the Company to enforce its rights under this Declaration without first instituting any legal proceeding against the Institutional Trustee or any other Person, including the Trust; it being understood and intended that no one or more of such Holders shall have any right in any manner whatsoever by virtue of, or by availing of, any provision of this Declaration to affect, disturb or prejudice the rights of any other of such Holders or to obtain or to seek to obtain priority or preference over any other of such Holders or to enforce any right under this Declaration, except in the manner herein provided and for the equal and ratable benefit of all such Holders. Notwithstanding the foregoing, a Holder of Preferred Securities may institute a legal proceeding directly against the Company, without first instituting a legal proceeding against or requesting or directing that action be taken by the Institutional Trustee or any other Person, for enforcement of payment to such Holder of principal of or interest on the Subordinated Debt Securities having a principal amount equal to the aggregate stated liquidation amount of the Preferred Securities of such Holder on or after the due dates therefor specified or provided for in the Subordinated Debt Securities. The Company shall be subrogated to all rights of the Holders of Preferred Securities in respect of any amounts paid to such Holders by the Company pursuant to this Section.

#### SECTION 8.20. Delaware Trustee

(a) Notwithstanding any other provision of this Declaration, the Delaware Trustee shall not be entitled to exercise any powers, nor shall the Delaware Trustee have any of the duties and responsibilities of the Regular Trustees or the Institutional Trustee described in this Declaration. The Delaware Trustee shall be a trustee for the sole and limited purpose of fulfilling the requirements of Section 3807 of the Delaware Statutory Trust Act.

(b) It is expressly understood and agreed by the parties hereto that in fulfilling its obligations as Delaware Trustee hereunder on behalf of the Trust (i) each of the representations, undertakings and agreements herein made on the part of the Trust is made and intended not as representations, warranties, covenants, undertakings and agreements by SunTrust Delaware Trust Company in its individual capacity but is made and intended for the purpose of binding only the Trust, and (ii) under no circumstances shall SunTrust Delaware Trust Company in its individual capacity be personally liable for the payment of any indebtedness or expenses of the Trust or be liable for the breach or failure of any obligation, representation, warranty or covenant made or undertaken by the Trust under this Declaration, except if such breach or failure is due to any gross negligence or willful misconduct of the Delaware Trustee.

### ARTICLE IX

#### DISSOLUTION AND LIQUIDATION

##### SECTION 9.01. Dissolution Upon Expiration Date

The Trust shall automatically dissolve on December 31, 2034 (the "Expiration Date") or earlier pursuant to Section 9.02.

SECTION 9.02. Early Termination

Upon the first to occur of any of the following events (such first occurrence, an "Early Termination Event"), the Trust shall be dissolved in accordance with the terms hereof:

- (i) the occurrence of a Bankruptcy Event in respect of the Sponsor, dissolution or liquidation of the Sponsor, or the dissolution of the Trust pursuant to judicial decree;
- (ii) the delivery of written direction to the Institutional Trustee by the Sponsor at any time (which direction is optional and wholly within the discretion of the Sponsor) to dissolve the Trust and distribute the Subordinated Debt Securities to Securityholders as provided in Section 9.04; and
- (iii) the payment at maturity or redemption of all of the Junior Subordinated Debt Securities, and the consequent redemption of all of the Preferred Securities.

SECTION 9.03. Termination

The respective obligations and responsibilities of the Trust and the Trustees created hereby shall terminate upon the latest to occur of the following: (a) the distribution by the Institutional Trustee to Securityholders upon the liquidation of the Trust pursuant to Section 9.04 or 9.05, or upon the redemption of all of the Trust Securities pursuant to Section 4.04, of all amounts or instruments required to be distributed hereunder upon the final payment of the Trust Securities; (b) the payment of any expenses owed by the Trust; and (c) the discharge of all administrative duties of the Regular Trustees, including the performance of any tax reporting obligations with respect to the Trust or the Securityholders.

SECTION 9.04. Liquidation

(a) If any Early Termination Event specified in clause (ii) of Section 9.02 occurs, the Trust shall be liquidated and the Institutional Trustee shall distribute the Subordinated Debt Securities to the Securityholders as provided in this Section 9.04.

(b) In connection with a distribution of the Subordinated Debt Securities, each Holder of Trust Securities shall be entitled to receive, after the satisfaction of liabilities to creditors of the Trust (as evidenced by a certificate of the Regular Trustees), a Like Amount of Subordinated Debt Securities. Notice of liquidation shall be given by the Institutional Trustee by first-class mail, postage prepaid, mailed not later than 30 nor more than 60 days prior to the Liquidation Date to each Holder of Trust Securities at such Holder's address appearing in the Securities Register. All notices of liquidation shall:

- (i) state the Liquidation Date;
- (ii) state that from and after the Liquidation Date, the Trust Securities will no longer be deemed to be Outstanding and any Trust Securities Certificates

not surrendered for exchange will be deemed to represent a Like Amount of Subordinated Debt Securities; and

(iii) provide such information with respect to the mechanics by which Holders may exchange Trust Securities Certificates for Subordinated Debt Securities as the Regular Trustees or the Institutional Trustee shall deem appropriate.

(c) In order to effect the liquidation of the Trust and distribution of the Subordinated Debt Securities to Securityholders, the Institutional Trustee shall establish a record date for such distribution (which shall be not more than 45 days prior to the Liquidation Date) and, either itself acting as exchange agent or through the appointment of a separate exchange agent, shall establish such procedures as it shall deem appropriate to effect the distribution of Subordinated Debt Securities in exchange for the Outstanding Trust Securities Certificates.

(d) After the Liquidation Date, (i) the Trust Securities will no longer be deemed to be Outstanding, (ii) certificates representing a Like Amount of Subordinated Debt Securities will be issued to Holders of Trust Securities Certificates, upon surrender of such certificates to the Regular Trustees or their agent for exchange, (iii) any Trust Securities Certificates not so surrendered for exchange will be deemed to represent a Like Amount of Subordinated Debt Securities, accruing interest at the rate provided for in the Subordinated Debt Securities from the last Distribution Payment Date on which a Distribution was made on such Trust Certificates until such certificates are so surrendered (and until such certificates are so surrendered, no payments of interest or principal will be made to Holders of Trust Securities Certificates with respect to such Subordinated Debt Securities) and (iv) all rights of Securityholders holding Trust Securities will cease, except the right of such Securityholders to receive Subordinated Debt Securities upon surrender of Trust Securities Certificates.

(e) The Sponsor will use its best efforts to have the Subordinated Debt Securities that are distributed in exchange for the Preferred Securities to be listed on such securities exchange as the Preferred Securities are then listed. The Sponsor may elect to have the Subordinated Debt Securities issued in book-entry form to the Clearing Agency or its nominee pursuant to a Certificate Depository Agreement.

#### SECTION 9.05. Bankruptcy

If an Early Termination Event specified in clause (i) of Section 9.02 has occurred, the Trust shall be liquidated. The Institutional Trustee shall distribute the Subordinated Debt Securities to the Securityholders as provided in Section 9.04, unless such distribution is determined by the Regular Trustees not to be practical, in which event the Holders will be entitled to receive out of the assets of the Trust available for distribution to Securityholders, after satisfaction of liabilities to creditors, an amount equal to the Liquidation Amount per Trust Security plus accrued and unpaid Distributions thereon to the date of payment (such amount being the "Liquidation Distribution"). If such Liquidation Distribution can be paid only in part because the Trust has insufficient assets available to pay in full the aggregate Liquidation Distribution, then, subject to the next succeeding sentence, the amounts payable by the Trust on the Trust Securities shall be paid on a pro rata basis (based upon Liquidation Amounts). The

Holder of the Common Securities will be entitled to receive Liquidation Distributions upon any such dissolution, winding-up or termination pro rata (determined as aforesaid) with Holders of Preferred Securities, except that, if an Indenture Event of Default has occurred and is continuing, the Preferred Securities shall have a priority over the Common Securities.

#### SECTION 9.06. Certificate of Cancellation

A Certificate of Cancellation ("Certificate") to terminate the Trust (as permitted hereby) may be signed by any Regular Trustee, individually, in such capacity so long as such Certificate fully complies with all legal requirements.

### ARTICLE X

#### REMARKETING PROCEDURES

##### SECTION 10.01. Election to Remarket

If the Company, and the Regular Trustees acting at the direction of the Company, elect to conduct a Remarketing, the Trust, not less than 20 nor more than 35 Business Days prior to the related Election Date, is required pursuant to Section 4.02(b) to give the written notice of proposed Remarketing of the Preferred Securities to the Clearing Agency, the Institutional Trustee, the Indenture Trustee, the Remarketing Agent and the Calculation Agent. If the Preferred Securities are not issued in global, fully registered form to the Clearing Agency, such notice shall be delivered to the Holders instead of the Clearing Agency. As required by Section 4.02(b), such notice will describe the Remarketing and will indicate the length of the proposed new Fixed Rate Period, the proposed Remarketing Date and any redemption provisions that will apply during such new Fixed Rate Period. At any time prior to the Election Date, the Company and the Regular Trustees may elect to terminate a Remarketing by giving the Clearing Agency (or the Holders, as applicable), the Remarketing Agent, the Institutional Trustee, the Indenture Trustee and the Calculation Agent written notice of such termination.

##### SECTION 10.02. Notice of Election

(a) Not later than 4:00 P.M., New York City time, on an Election Date, each Holder of Preferred Securities may give, through the facilities of the Clearing Agency in the case of Book-Entry Preferred Securities Certificates, a written notice to the Institutional Trustee of its election ("Notice of Election") (i) to retain and not to have all or any portion of the Preferred Securities owned by it remarketed in the Remarketing or (ii) to tender all or any portion of such Preferred Securities for purchase in the Remarketing (such portion, in either case, is to be in the Liquidation Amount of \$1,000 or any integral multiple thereof). Any Notice of Election given to the Institutional Trustee will be irrevocable and may not be conditioned upon the level at which the Fixed Rate is established in the Remarketing. Promptly after 4:30 P.M., New York City time, on such Election Date, the Institutional Trustee, based on the Notices of Election received by it through the Clearing Agency (or from the Holders, if Definitive Preferred Securities Certificates have been issued) prior to such time, will notify the Regular Trustees, the Company and the Remarketing Agent of the number of Preferred Securities to be retained by holders of

Preferred Securities and the number of Preferred Securities tendered for purchase in the Remarketing.

(b) If any Holder of Preferred Securities gives a Notice of Election to tender Preferred Securities as described in 10.02(a), the Preferred Securities so subject to such Notice of Election will be deemed tendered for purchase in the Remarketing, notwithstanding any failure by such Holder to deliver or properly deliver such Preferred Securities to the Remarketing Agent for purchase. If any Holder of Preferred Securities fails timely to deliver a Notice of Election, as described above, such Preferred Securities will be deemed tendered for purchase in such Remarketing, notwithstanding such failure or the failure by such Holder to deliver or properly deliver such Preferred Securities to the Remarketing Agent for purchase.

(c) The right of each Holder of Preferred Securities to have Preferred Securities tendered for purchase in the Remarketing shall be limited to the extent that (i) the Remarketing Agent conducts a Remarketing pursuant to the terms of the Remarketing Agreement, (ii) Preferred Securities tendered have not been called for redemption, (iii) the Remarketing Agent is able to find a purchaser or purchasers for tendered Preferred Securities at a Fixed Rate and (iv) such purchaser or purchasers deliver the purchase price therefor to the Remarketing Agent.

(d) Any Holder of Preferred Securities that desires to continue to retain a number of Preferred Securities, but only if the Fixed Rate is not less than a specified rate per annum, shall submit a Notice of Election to tender such Preferred Securities pursuant to this Section 10.02 and separately notify the Remarketing Agent of its interest at the telephone number set forth in the notice of Remarketing delivered pursuant to Section 10.01. If such Holder so notifies the Remarketing Agent, the Remarketing Agent will give priority to such Holder's purchase of such number of Preferred Securities in the Remarketing providing that the Fixed Rate is not less than such specified rate.

#### SECTION 10.03. Determination of Distribution Rate

(a) If Holders submit Notices of Election to retain all of the Preferred Securities then outstanding, the Fixed Rate will be the rate determined by the Remarketing Agent, in its sole discretion, as the rate that would have been established had a Remarketing been held on the related Remarketing Date.

(b) On any Remarketing Date on which the Remarketing is to be conducted, the Remarketing Agent will use commercially reasonable efforts to remarket, at a price equal to 100% of the Liquidation Amount thereof, Preferred Securities tendered or deemed tendered for purchase. Except as provided in Section 10.03(a), if, as a result of such efforts, on any Remarketing Date, the Remarketing Agent has determined that it will be able to remarket all Preferred Securities tendered or deemed tendered for purchase in the Remarketing at a Fixed Rate and at a price of \$1,000 per Preferred Security, prior to 4:00 P.M., New York City time, on such Remarketing Date, the Remarketing Agent will determine the Fixed Rate, which will be the rate per annum (rounded to the nearest one-thousandth (0.001) of one percent per annum) which the Remarketing Agent determines, in its sole judgment, to be the lowest Fixed Rate per annum that will enable it to remarket all Preferred Securities tendered or deemed tendered for

Remarketing at a price of \$1,000 per Preferred Security. By approximately 4:30 P.M., New York City time, on a Remarketing Date, the Remarketing Agent shall advise, by telephone, (i) the Clearing Agency, the Institutional Trustee, the Indenture Trustee, the Trust, the Company and the Calculation Agent of any new Fixed Rate established pursuant to the Remarketing and the number of remarketed Preferred Securities sold in the Remarketing; (ii) each purchaser of a remarketed Preferred Security (or the Clearing Agency Participant thereof) of such new Fixed Rate and the number of remarketed Preferred Securities such purchaser is to purchase; and (iii) each purchaser to give instructions to its Clearing Agency Participant to pay the purchase price on the Remarketing Settlement Date in same day funds against delivery of the remarketed Preferred Securities purchased through the facilities of the Clearing Agency.

(c) If the Remarketing Agent is unable to remarket by 4:00 P.M., New York City time on the third Business Day prior to the Remarketing Settlement Date, all Preferred Securities tendered or deemed tendered for a purchase at a price of \$1,000 per Preferred Security, the Distribution Rate for the next Distribution Period shall be the Floating Rate and the new Distribution Period shall be a Floating Rate Period. In such case, no Preferred Securities will be sold in the Remarketing and each Holder will continue to hold its Preferred Securities at such Floating Rate during such Floating Rate Period.

(d) All Preferred Securities tendered or deemed tendered in the Remarketing will be automatically delivered to the account of the Remarketing Agent through the facilities of the Clearing Agency against payment of the purchase price therefor on the Remarketing Settlement Date. The Remarketing Agent will make payment to the Clearing Agency Participant of each tendering holder of Preferred Securities in the Remarketing through the facilities of the Clearing Agency by the close of business on the Remarketing Settlement Date.

In accordance with the Clearing Agency's normal procedures, on the Remarketing Settlement Date, the transaction described above with respect to each Preferred Security tendered for purchase and sold in the Remarketing will be executed through the Clearing Agency Participants, will be debited and credited and such Preferred Securities delivered by book entry as necessary to effect purchases and sales of such Preferred Securities. The Clearing Agency is expected to make payment in accordance with its normal procedures.

This Section 10.03(d) shall not apply if Definitive Preferred Securities Certificates have been issued.

(e) If any Holder selling Preferred Securities in the Remarketing fails to deliver such Preferred Securities, the Clearing Agency Participant of such selling Holder and of any other person that was to have purchased Preferred Securities in the Remarketing may deliver to any such other person a number of Preferred Securities that is less than the number of Preferred Securities that otherwise was to be purchased by such person. In such event, the number of Preferred Securities to be so delivered will be determined by such Clearing Agency Participant and delivery of such lesser number of Preferred Securities will constitute good delivery. This paragraph shall not apply if Definitive Preferred Securities Certificates have been issued.



(f) The Remarketing Agent is not obligated to purchase any Preferred Securities that would otherwise remain unsold in a Remarketing. Neither the Trust, any Trustee, the Company nor the Remarketing Agent shall be obligated in any case to provide funds to make payment upon tender of Preferred Securities for Remarketing.

## ARTICLE XI

### MISCELLANEOUS PROVISIONS

#### SECTION 11.01. Guarantee by the Sponsor

Subject to the terms and conditions hereof, the Sponsor, as obligor of the Subordinated Debt Securities, irrevocably and unconditionally guarantees to each Person to whom the Trust is now or hereafter becomes indebted or liable (the "Beneficiaries") the full payment, when and as due, of any and all Obligations (as hereinafter defined) to such Beneficiaries. As used herein, "Obligations" means any indebtedness, expenses or liabilities of the Trust, other than obligations of the Trust to pay to Holders of any Preferred Securities, Common Securities or other similar interests in the Trust the amounts due such Holders pursuant to the terms of the Preferred Securities, Common Securities or such other similar interests, as the case may be. This guarantee is intended to be for the benefit of, and to be enforceable by, all such Beneficiaries, whether or not such Beneficiaries have received notice hereof.

#### SECTION 11.02. Limitation of Rights of Securityholders

The death or incapacity of any Person having an interest, beneficial or otherwise, in a Trust Security shall not operate to terminate this Declaration, nor entitle the legal representatives or heirs of such Person or any Securityholder for such Person, to claim an accounting, take any action or bring any proceeding in and for a partition or winding up of the arrangements contemplated hereby, nor otherwise affect the rights, obligations and liabilities of the parties hereto or any of them.

#### SECTION 11.03. Amendment

(a) This Declaration may be amended from time to time by the Institutional Trustee and the Holders of a Majority in Liquidation Amount of the Common Securities, without the consent of any Holder of the Preferred Securities (i) to cure any ambiguity, correct or supplement any provision herein that may be defective or inconsistent with any other provision herein, or to make other changes to the provisions with respect to matters or questions arising under this Declaration; provided, however, that such amendment shall not adversely affect in any material respect the interests of any Holder of Trust Securities; (ii) to facilitate the tendering, remarketing and settlement of the Preferred Securities, as herein contemplated; (iii) to modify, eliminate or add to any provisions of this Declaration to such extent as shall be necessary to ensure that the Trust will not be taxable other than as a grantor trust for United States federal income tax purposes at any time that any Trust Securities are Outstanding or to ensure that the Trust will not be required to register as an investment company under the Investment Company Act; or (iv) in accordance with the requirements of Section 8.11. Without limiting the generality of the foregoing, if the Trust Indenture Act as in effect at the date of the execution and delivery

of this Declaration or at any time thereafter shall be amended and (x) if any such amendment shall require one or more changes to any provisions hereof or the inclusion herein of any additional provisions, or shall by operation of law be deemed to effect such changes or incorporate such provisions by reference or otherwise, this Declaration shall be deemed to have been amended so as to conform to such amendment to the Trust Indenture Act, and the Company and the Trustees may, without the consent of any Holders, amend this Declaration to evidence such amendment hereof; or (y) if any such amendment shall permit one or more changes to, or the elimination of, any provisions hereof which, at the date of the execution and delivery hereof or at any time thereafter, are required by the Trust Indenture Act to be contained herein or are contained herein to reflect any provisions of the Trust Indenture Act as in effect at such date, this Declaration shall be deemed to have been amended to effect such changes or elimination, and the Company and the Trustees may, without the consent of any Holders, amend this Declaration to evidence such amendment.

(b) Except as provided in Section 11.03(c) hereof, any provision of this Declaration may be amended by the Institutional Trustee and the Holders of a Majority in Liquidation Amount of the Common Securities with (i) the consent of Holders of at least a Majority in Liquidation Amount of the Preferred Securities, and (ii) receipt by the Trustees of an Opinion of Counsel to the effect that such amendment or the exercise of any power granted to the Trustees in accordance with such amendment will not affect the Trust's being taxable as a grantor trust for United States federal income tax purposes or the Trust's exemption from status of an "investment company" under the Investment Company Act.

(c) In addition to and notwithstanding any other provision in this Declaration, without the consent of each affected Securityholder, this Declaration may not be amended to (i) change the amount or timing of any Distribution on the Trust Securities or otherwise adversely affect the amount of any Distribution required to be made in respect of the Trust Securities as of a specified date; (ii) restrict the right of a Securityholder to institute suit for the enforcement of any such payment on or after such date; or (iii) change the consent required pursuant to this Section 11.03.

(d) Notwithstanding any other provisions of this Declaration, the Trustees shall not enter into or consent to any amendment to this Declaration which would cause the Trust to fail or cease to qualify for the exemption from status of an "investment company" under the Investment Company Act of 1940, as amended, afforded by Rule 3a-5 thereunder.

(e) Without the consent of the Sponsor, the Calculation Agent or the Remarketing Agent, this Declaration may not be amended in a manner which imposes any additional obligation on the Sponsor, the Calculation Agent or the Remarketing Agent, as the case may be. Notwithstanding any other provisions of this Declaration, the consent of the Delaware Trustee shall be required to amend any provision of, or add any provision to, this Declaration which affects the Delaware Trustee's rights, duties, immunities, liabilities or otherwise. In executing any amendment permitted by this Declaration, the Trustees shall be entitled to receive, and (subject to Section 8.01) shall be fully protected in relying upon an Officer's Certificate and an Opinion of Counsel stating that the execution of such amendment is authorized or permitted by this Declaration. Any Trustee may, but shall not be obligated to,

enter into any such amendment which affects such Trustee's own rights, duties, immunities or liabilities under this Declaration or otherwise.

(f) In the event that any amendment to this Declaration is made, the Regular Trustees shall promptly provide to the Sponsor a copy of such amendment.

#### SECTION 11.04. Separability

In case any provision in this Declaration or in the Trust Securities Certificates shall be invalid, illegal or unenforceable, the validity, legality and enforceability of the remaining provisions shall not in any way be affected or impaired thereby.

#### SECTION 11.05. Governing Law

THIS DECLARATION AND THE RIGHTS AND OBLIGATIONS OF EACH OF THE SECURITYHOLDERS, THE TRUST AND THE TRUSTEES WITH RESPECT TO THIS DECLARATION AND THE TRUST SECURITIES SHALL BE CONSTRUED IN ACCORDANCE WITH AND GOVERNED BY THE INTERNAL LAWS OF THE STATE OF DELAWARE.

#### SECTION 11.06. Successors

This Declaration shall be binding upon and shall inure to the benefit of any successor to both the Trust and the Trustees, including any successor by operation of law.

#### SECTION 11.07. Headings

The Article and Section headings are for convenience only and shall not affect the construction of this Declaration.

#### SECTION 11.08. Notice and Demand

Any notice, demand or other communication which by any provision of this Declaration is required or permitted to be given or served to or upon any Securityholder or the Sponsor may be given or served in writing by deposit thereof, first-class postage prepaid, in the United States mail, hand delivery or facsimile transmission, in each case, addressed, (i) in the case of a Holders of Preferred Securities, to such Holders of Preferred Securities as such Securityholder's name and address appear on the Securities Register and, (ii) in the case of the Holders of Common Securities or the Sponsor, to Avista Corporation, 1411 East Mission Avenue, Spokane, Washington 99202, Attention: Treasurer, Facsimile No. (509) 495-4361, or to such other address as the Holders of Common Securities or the Sponsor may give notice of to the Institutional Trustee and the Delaware Trustee. Such notice, demand or other communication to or upon a Securityholder shall be deemed to have been sufficiently given or made, for all purposes, upon hand delivery, mailing or transmission.

Any notice, demand or other communication which by any provision of this Declaration is required or permitted to be given or served to or upon the Trust or the Trustees shall be given in writing addressed as follows: (i) with respect to the Institutional Trustee and the Delaware

Trustee, Union Bank of California, N.A., 475 Sansome Street, 12th Floor, San Francisco, California 94111, Attention: Corporate Trust Services, Facsimile No. (415) 296-6754; SunTrust Delaware Trust Company, 1011 Centre Road, Suite 108, Wilmington, Delaware 19805, Attention: Corporate Trust Department, Facsimile No. (302) 892-9943 (with a copy to SunTrust Bank, 225 East Robinson Street, Suite 250, Orlando, Florida 32801, Attention: Corporate Trust Department), as the case may be, or to such other address as the Institutional Trustee or the Delaware Trustee may give notice of to the Sponsor; and (ii) with respect to the Regular Trustees, to them at the address above for notices to the Sponsor, marked Attention: Regular Trustees of AVA Capital Trust III, c/o Treasurer. Such notice, demand or other communication to or upon the Trust or the Trustees shall be deemed to have been sufficiently given or made only upon actual receipt of the writing by the applicable Trustee.

Any notice, demand or other communication which by any provision of this Declaration is required or permitted to be served upon the Calculation Agent or the Remarketing Agreement shall be given in accordance with the Calculation Agent Agreement or the Remarketing Agreement, respectively.

#### SECTION 11.09. Agreement Not to Petition

Each of the Trustees and the Sponsor agrees for the benefit of the Securityholders that, until at least one year and one day after the Trust has been terminated in accordance with Article IX, it shall not file, or join in the filing of, a petition against the Trust under any bankruptcy, reorganization, arrangement, insolvency, liquidation or other similar law (including, without limitation, the United States Bankruptcy Code) (collectively, "Bankruptcy Laws") or otherwise join in the commencement of any proceeding against the Trust under any Bankruptcy Law. In the event the Sponsor takes action in violation of this Section 11.09, the Institutional Trustee agrees, for the benefit of Securityholders, that it shall file an answer with the bankruptcy court or otherwise properly contest the filing of such petition by the Sponsor against the Trust or the commencement of such action and raise the defense that the Sponsor has agreed in writing not to take such action and should be stopped and precluded therefrom and such other defenses, if any, as counsel for the Trustees or the Trust may assert. The provisions of this Section 11.09 shall survive the termination of this Declaration.

#### SECTION 11.10. Conflict with Trust Indenture Act

(a) This Declaration is subject to the provisions of the Trust Indenture Act that are required to be part of this Declaration and shall, to the extent applicable, be governed by such provisions.

(b) The Institutional Trustee shall be the only Trustee which is a Trustee for the purposes of the Trust Indenture Act.

(c) If any provision hereof limits, qualifies or conflicts with another provision hereof which is required to be included in this Declaration by any of the provisions of the Trust Indenture Act, such required provision shall control.

(d) The application of the Trust Indenture Act to this Declaration shall not affect the nature of the Trust Securities as equity securities representing undivided beneficial interests in the assets of the Trust.

THE RECEIPT AND ACCEPTANCE OF A TRUST SECURITY OR ANY INTEREST THEREIN BY OR ON BEHALF OF A SECURITYHOLDER OR ANY BENEFICIAL OWNER, WITHOUT ANY SIGNATURE OR FURTHER MANIFESTATION OF ASSENT, SHALL CONSTITUTE THE UNCONDITIONAL ACCEPTANCE BY THE SECURITYHOLDER AND ALL OTHERS HAVING A BENEFICIAL INTEREST IN SUCH TRUST SECURITY OF ALL THE TERMS AND PROVISIONS OF THIS DECLARATION AND AGREEMENT TO THE SUBORDINATION PROVISIONS AND OTHER TERMS OF THE GUARANTEE AND THE SUBORDINATED INDENTURE AND THE AGREEMENT OF THE TRUST, SUCH SECURITYHOLDER AND SUCH OTHERS THAT THOSE TERMS AND PROVISIONS SHALL BE BINDING, OPERATIVE AND EFFECTIVE AS BETWEEN THE TRUST AND SUCH SECURITYHOLDER AND SUCH OTHERS.

IN WITNESS WHEREOF, the parties hereto have executed this Declaration or have caused this Declaration to be executed on their behalf, all as of the day and year first above written.

AVISTA CORPORATION,  
as Sponsor

By: /s/ Diane C. Thoren  
-----

Name: Diane C. Thoren  
Title: Assistant Treasurer

UNION BANK OF CALIFORNIA, N.A.,  
as Institutional Trustee

By: /s/ Sonia N. Flores  
-----

Name: Sonia N. Flores  
Title: Vice President

SUNTRUST DELAWARE TRUST COMPANY,  
as Delaware Trustee

By: /s/ Susan D. Tinsley  
-----

Name: Susan D. Tinsley  
Title: Trust Officer

/s/ Malyn K. Malquist  
-----

Malyn K. Malquist  
as Regular Trustee

/s/ Diane C. Thoren  
-----

Diane C. Thoren  
as Regular Trustee

EXHIBIT A

This Security is a Global Certificate within the meaning of the Declaration hereinafter referred to and is registered in the name of the Depository Trust Company ("DTC") or a nominee of DTC. This Security is exchangeable for Securities registered in the name of a person other than DTC or its nominee only in the limited circumstances described in the Declaration and no transfer of this Security (other than a transfer of this Security as a whole by DTC to a nominee of DTC or by a nominee of DTC to DTC or another nominee of DTC) may be registered except in limited circumstances.

Unless this certificate is presented by an authorized representative of DTC, to AVA Capital Trust III or its agent for registration of transfer, exchange or payment, and any certificate issued is registered in the name of Cede & Co. or in such other name as is requested by an authorized representative of DTC (and any payment made to Cede & Co. or to such other entity as is requested by an authorized representative of DTC), any transfer, pledge or other use hereof for value or otherwise by or to any person is wrongful inasmuch as the registered owner thereof, Cede & Co., has an interest herein.\*

Certificate Number \_\_\_\_\_ Number of Preferred Securities \_\_\_\_\_

P-\_\_ CUSIP NO. \_\_\_\_\_

Certificate Evidencing Preferred Securities  
of  
AVA Capital Trust III

Flexible Trust Preferred Securities  
(Five Year Initial Fixed Rate Period)  
(Liquidation Amount \$1,000 per Preferred Security)

AVA Capital Trust III, a statutory trust created under the laws of the State of Delaware (the "Trust"), hereby certifies that Cede & Co.\* (the "Holder") is the registered owner of \_\_\_\_\_ (\_\_\_\_\_) preferred securities of the Trust representing undivided beneficial interests in the assets of the Trust and designated the AVA Capital Trust III Flexible Trust Preferred Securities (Five Year Initial Fixed Rate Period) (Liquidation Amount \$1,000 per Preferred Security) (the "Preferred Securities"). The Preferred Securities are transferable on the books and records of the Trust, in person or by a duly authorized attorney, upon surrender of this certificate duly endorsed and in proper form for transfer as provided in Section 5.04 of the Declaration (as defined below). The designations, rights, privileges, restrictions, preferences and other terms and provisions of the Preferred Securities are set forth in, and this certificate and the Preferred Securities represented hereby are issued and shall in all respects be subject to the terms and provisions of, the Amended and Restated Declaration of Trust of the Trust, dated as of April 5, 2004, as the same may be amended from time to time (the "Declaration"), including the designation of the terms of Preferred Securities as set forth therein. The holder of this certificate

is entitled to the benefits of a guarantee by Avista Corporation, a Washington corporation (the "Company"), pursuant to a Guarantee Agreement between the Company and Union Bank of California, N.A., as guarantee trustee, dated as of April 5, 2004, as the same may be amended from time to time (the "Guarantee"), to the extent provided therein. The Trust will furnish a copy of the Declaration and the Guarantee to the holder of this certificate without charge upon written request to the Trust at its principal place of business or registered office.

Upon receipt of this certificate, the holder of this certificate is bound by the Declaration and is entitled to the benefits thereunder.

\*Insert in Book-Entry Preferred Securities Certificates only

IN WITNESS WHEREOF, the Trust has executed this certificate this \_\_\_\_ day of \_\_\_\_\_, 2004.

AVA CAPITAL TRUST III

By: \_\_\_\_\_

\_\_\_\_\_  
As Regular Trustee

CERTIFICATE OF AUTHENTICATION

This is one of the Preferred Securities referred to in the within-mentioned Declaration.

\_\_\_\_\_  
as Institutional Trustee



ASSIGNMENT

FOR VALUE RECEIVED, the undersigned assigns and transfers this Preferred Security to:

- .....  
- .....  
- .....  
- .....

(Insert assignee's social security or tax identification number)

- .....  
- .....  
- .....

(Insert address and zip code of assignee)  
and irrevocably appoints

- .....  
- .....  
- .....

agent to transfer this Preferred Securities Certificate on the books of the Trust. The agent may substitute another to act for him or her.

Date: .....

Signature: .....

(Sign exactly as your name appears on the other side of this Preferred Securities Certificate)

EXHIBIT B

AGREEMENT AS TO EXPENSES AND LIABILITIES

THIS AGREEMENT AS TO EXPENSES AND LIABILITIES (this "Agreement") is made as of April 5, 2004, between Avista Corporation, a Washington corporation (the "Company"), and AVA Capital Trust III, a Delaware statutory trust (the "Trust").

WHEREAS, the Trust intends to issue its Common Securities (the "Common Securities and its AVA Capital Trust III Flexible Trust Preferred Securities (the "Preferred Securities"), with such powers, preferences and special rights and restrictions as are set forth in the Amended and Restated Declaration of Trust of the Trust dated as of April 5, 2004 as the same may be amended from time to time (the "Declaration"), and with the proceeds thereof to purchase from the Company its Subordinated Debt Securities, Series due 2034 (the "Subordinated Debt Securities"); and

NOW, THEREFORE, in consideration of the purchase by each holder of the Preferred Securities, which purchase the Company hereby agrees shall benefit the Company and which purchase the Company acknowledges will be made in reliance upon the execution and delivery of this Agreement, the Company and the Trust hereby agree as follows:

ARTICLE I

Section 1.01. Agreement of the Company. Subject to the terms and conditions hereof, the Company hereby irrevocably and unconditionally agrees with the Trust, and with each person or entity to whom the Trust is now or hereafter becomes indebted or liable (the "Beneficiaries"), that the Company shall make full payment, when and as due, of any and all Expenses (as hereinafter defined) to such Beneficiaries and shall reimburse the Trust for any Expenses paid by it. As used herein, "Expenses" means any expenses, indebtedness or liabilities of the Trust, including, without limitation, any and all taxes, duties, assessments or other governmental charges of whatever nature (other than United States federal withholding taxes) imposed by the United States or any other taxing authority; it being understood (a) that "Expenses" shall not be deemed to include amounts to be distributed to the holders of the Common Securities and the Preferred Securities pursuant to the terms thereof and (b) that the intention of this covenant is that the net amounts received and retained by the Trust after paying all Expenses will be equal to the amounts the Trust would have received and retained had no such Expenses been incurred by or imposed on the Trust. This Agreement is intended to be for the benefit of, and to be enforceable by, the Trust and by all such Beneficiaries, whether or not such Beneficiaries have received notice hereof.

Section 1.02. Term of Agreement. This Agreement shall terminate and be of no further force and effect upon the date on which there are no Beneficiaries remaining; provided, however, that this Agreement shall continue to be effective or shall be reinstated, as the case may be, if at any time any holder of Preferred Securities or any Beneficiary must restore payment of any sums paid under the Preferred Securities, any Expense, any sums paid under the Guarantee Agreement dated

the date hereof by the Company and Union Bank of California, N.A., as guarantee trustee, or under this Agreement for any reason whatsoever. This Agreement is continuing, irrevocable, unconditional and absolute.

Section 1.03. Waiver of Notice. The Company hereby waives notice of acceptance of this Agreement and of any payment of Expenses to which it applies or may apply, and the Company hereby waives presentment, demand for payment, protest, notice of nonpayment, notice of dishonor, notice of redemption and all other notices and demands.

Section 1.04. No Impairment. The obligations, covenants, agreements and duties of the Company under this Agreement shall in no way be affected or impaired by reason of the happening from time to time of any of the following:

(a) the extension of time for the payment by the Trust of all or any portion of the Expenses or for the performance of any other obligation under, arising out of, or in connection with, the Expenses;

(b) any failure, omission, delay or lack of diligence on the part of the Beneficiaries to enforce, assert or exercise any right, privilege, power or remedy conferred on the Beneficiaries with respect to the Expenses or any action on the part of the Trust granting indulgence or extension of any kind; or

(c) the voluntary or involuntary liquidation, dissolution, sale of any collateral, receivership, insolvency, bankruptcy, assignment for the benefit of creditors, reorganization, arrangement, composition or readjustment of debt of, or other similar proceedings affecting, the Trust or any of the assets of the Trust.

There shall be no obligation of the Beneficiaries to give notice to, or obtain the consent of, the Company with respect to the happening of any of the foregoing.

Section 1.05. Enforcement. A Beneficiary may enforce this Agreement directly against the Company and the Company waives any right or remedy to require that any action be brought against the Trust or any other person or entity before proceeding against the Company.

## ARTICLE II

Section 2.01. Binding Effect. All guarantees and agreements contained in this Agreement shall bind the successors, assigns, receivers, trustees and representatives of the Company and shall inure to the benefit of the Beneficiaries.

Section 2.02. Amendment. So long as there remains any Beneficiary or any Preferred Securities of any series are outstanding, this Agreement shall not be modified or amended in any manner adverse to such Beneficiary or to the holders of the Preferred Securities.

Section 2.03. Notices. Any notice, request or other communication required or permitted to be given hereunder shall be given in writing by delivering the same against receipt therefor by

facsimile transmission (confirmed by mail), telex or by registered or certified mail, addressed as follows (and if so given, shall be deemed given when mailed or upon receipt of an answer-back, if sent by telex), to-wit:

AVA Capital Trust III  
c/o Union Bank of California, N.A.  
475 Sansome Street, 12th Floor  
San Francisco, California 94111  
Facsimile No.: (415) 296-6757  
Attention: Corporate Trust Services

Avista Corporation  
1411 East Mission Avenue  
Spokane, Washington 99202  
Facsimile No.: (509) 482-4879  
Attention: Treasurer

Section 2.04. THIS AGREEMENT SHALL BE GOVERNED BY AND CONSTRUED AND INTERPRETED IN ACCORDANCE WITH THE LAWS OF THE STATE OF NEW YORK.

THIS AGREEMENT is executed as of the date and year first above written.

AVISTA CORPORATION

By: \_\_\_\_\_  
Name:  
Title:

AVA CAPITAL TRUST III

By: \_\_\_\_\_  
as Regular Trustee

B-3

EXHIBIT C

THIS CERTIFICATE IS NOT TRANSFERABLE EXCEPT AS PROVIDED IN THE  
DECLARATION OF TRUST REFERRED TO HEREIN

Certificate Number C-1

Number of Common Securities

\_\_\_\_\_

Certificate Evidencing Common Securities  
of  
AVA Capital Trust III  
Common Securities  
(Liquidation Amount \$1,000 per Common Security)

AVA Capital Trust III, a statutory trust created under the laws of the State of Delaware (the "Trust"), hereby certifies that Avista Corporation (the "Holder") is the registered owner of \_\_\_\_\_ (\_\_\_\_\_) common securities of the Trust representing undivided beneficial interests in the assets of the Trust and designated the AVA Capital Trust III Common Securities (Liquidation Amount \$1,000 per Common Security) (the "Common Securities"). In accordance with Section 5.10 of the Declaration (as defined below), the Common Securities are not transferable, except as permitted by the Declaration referred to herein, and, to the fullest extent permitted by law, any attempted transfer hereof shall be void. The designations, rights, privileges, restrictions, preferences and other terms and provisions of the Common Securities are set forth in, and this certificate and the Common Securities represented hereby are issued and shall in all respects be subject to the terms and provisions of, the Amended and Restated Declaration of Trust of the Trust dated as of April 5, 2004, as the same may be amended from time to time (the "Declaration"), including the designation of the terms of the Common Securities as set forth therein. The holder of this certificate is entitled to the benefits of a guarantee by Avista Corporation, a Delaware corporation (the "Company"), pursuant to a Guarantee Agreement between the Company and Union Bank of California, N.A., as guarantee trustee, dated as of April 5, 2004, as the same may be amended from time to time (the "Guarantee"), to the extent provided therein. The Trust will furnish a copy of the Declaration and the Guarantee to the Holder without charge upon written request to the Trust at its principal place of business or registered office.

Upon receipt of this certificate, the Holder is bound by the Declaration and is entitled to the benefits thereunder.

IN WITNESS WHEREOF, the Trust has executed this certificate this \_\_\_\_  
day of \_\_\_\_\_, 2004.

AVA Capital Trust III

By: \_\_\_\_\_

\_\_\_\_\_,  
as Regular Trustee

CERTIFICATE OF AUTHENTICATION

This is one of the Common Securities referred to in the within-mentioned  
Declaration.

\_\_\_\_\_  
as Institutional Trustee

C-1

## AVISTA CORPORATION

Computation of Ratio of Earnings to Fixed Charges and Preferred Dividend  
Requirements Consolidated  
(Thousands of Dollars)

	12 months ended March 31, 2004	Years Ended December 31			
		2003	2002	2001	2000
Fixed charges, as defined:					
Interest expense	\$ 85,099	\$ 85,013	\$ 96,005	\$100,180	\$ 64,765
Amortization of debt expense and premium - net	8,006	7,972	8,861	5,639	3,409
Interest portion of rentals	4,409	4,452	6,140	5,140	4,324
Total fixed charges	\$ 97,514	\$ 97,437	\$111,006	\$110,959	\$ 72,498
Earnings, as defined:					
Income from continuing operations	\$ 44,885	\$ 50,643	\$ 42,174	\$ 68,241	\$109,065
Add (deduct):					
Income tax expense	31,005	35,340	34,849	40,585	81,143
Total fixed charges above	97,514	97,437	111,006	110,959	72,498
Total earnings	\$173,404	\$183,420	\$188,029	\$219,785	\$262,706
Ratio of earnings to fixed charges	1.78	1.88	1.69	1.98	3.62
Fixed charges and preferred dividend requirements:					
Fixed charges above	\$ 97,514	\$ 97,437	\$111,006	\$110,959	\$ 72,498
Preferred dividend requirements (1)	925	1,910	4,387	3,878	41,394
Total	\$ 98,439	\$ 99,347	\$115,393	\$114,837	\$113,892
Ratio of earnings to fixed charges and preferred dividend requirements	1.76	1.85	1.63	1.91	2.31

(1) Preferred dividend requirements have been grossed up to their pre-tax level.

## CERTIFICATION

I, Gary G. Ely, certify that:

1. I have reviewed this report on Form 10-Q of Avista 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)) for the registrant and have:
  - a. Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
  - b. Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
  - c. Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and
5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):
  - a. All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
  - b. Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: May 7, 2004

/s/ Gary G. Ely

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 Gary G. Ely  
 Chairman of the Board, President and  
 Chief Executive Officer  
 (Principal Executive Officer)



## CERTIFICATION

I, Malyn K. Malquist, certify that:

1. I have reviewed this report on Form 10-Q of Avista 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)) for the registrant and have:
  - a. Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
  - b. Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
  - c. Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and
5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):
  - a. All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
  - b. Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: May 7, 2004

/s/ Malyn K. Malquist

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 Malyn K. Malquist  
 Senior Vice President, Chief  
 Financial Officer and Treasurer  
 (Principal Financial Officer)

AVISTA CORPORATION

CERTIFICATION OF CORPORATE OFFICERS

(Furnished Pursuant to 18 U.S.C. Section 1350, as Adopted Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002)

Each of the undersigned, Gary G. Ely, Chairman of the Board, President and Chief Executive Officer of Avista Corporation (the "Company"), and Malyn K. Malquist, Senior Vice President, Chief Financial Officer and Treasurer of the Company, hereby certifies, pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, that the Company's Quarterly Report on Form 10-Q for the quarter ended March 31, 2004 fully complies with the requirements of Section 13(a) of the Securities Exchange Act of 1934, as amended, and that the information contained therein fairly presents, in all material respects, the financial condition and results of operations of the Company.

May 7, 2004

/s/ Gary G. Ely

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Gary G. Ely  
Chairman of the Board, President and  
Chief Executive Officer

/s/ Malyn K. Malquist

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Malyn K. Malquist  
Senior Vice President, Chief  
Financial Officer and Treasurer